MY TOP 5 EARNINGS TACTICS FOR OPTIONS TRADERS... INCLUDING MY #1 STRATEGY FOR EARNINGS SEASON

Why trade around earnings? Any option buyer knows that the ultimate options purchase is one that moves sharply in the least amount of time possible in order to minimize time erosion in the option. Earnings provide opportunities for sharp price gaps, usually overnight.

In this report, I will detail the times where I like to trade options in front of, as well as after, the earnings event. You want to make sure to give yourself the best opportunities for big moves while remaining aware of what the market expects. You have to be careful when buying options if the market already expects a big move and in this report, you will learn how to take advantage of these expectations.

Overview of My Top 5 Tactics

There are many potential strategies for earnings season and here are my top 5 favorite techniques to consider. I will overview each of these strategies in this report, and then share with you my #1 favorite earnings strategy to consistently profit from earnings reports over time.

1. Buy straddles or strangles to play a big move in either direction

2. Know the stock's history of gaps and find relatively cheap options to trade the average gap

3. Consider an options spread, where you sell relatively high implied volatility in short-term options right before earnings and then you bet the move will be less than the market’s high expectations

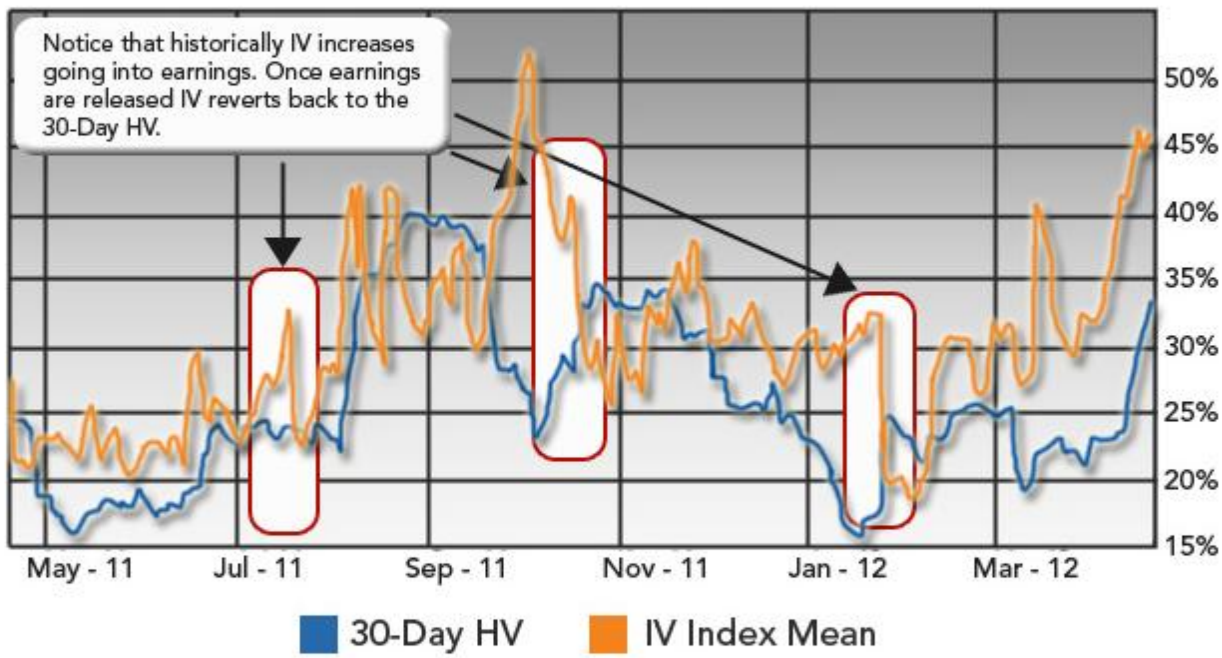
4. Buy after earnings and follow the trend

5. Identify high momentum ahead of earnings and purchase straight calls and puts in anticipation of a continuation in the existing trend direction (my #1 strategy!)

First, a Quick Primer on Volatility

While "volatility" is often thrown around as a broader term relative to market risk, it actually is a specific measurement of movement in the options markets. Historical Volatility (HV) is the actual movement that the stock has had over the “lookback” period.

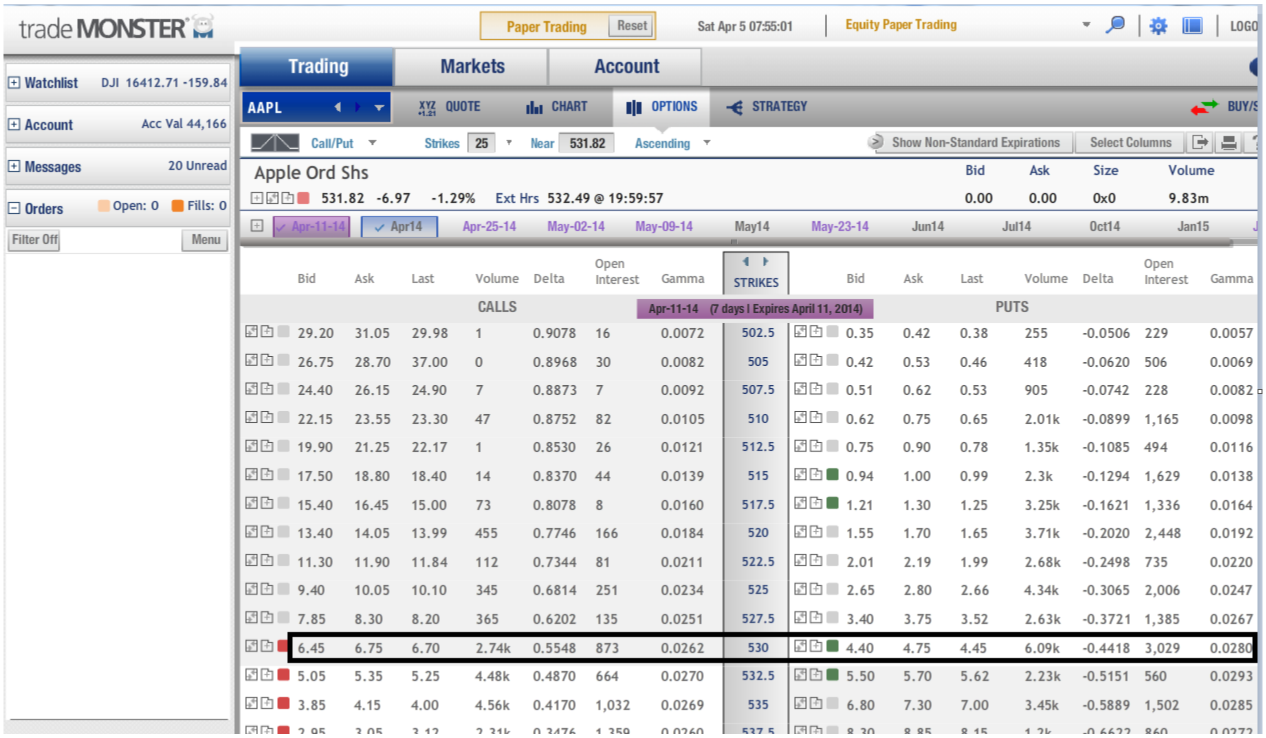
Implied Volatility (IV) is how much the market expects the stock to move going forward. The tendency is for the IV to rise ahead of an event before reverting back down after the event has passed. Here’s an example:



We want to make sure that if we are buying an option ahead of earnings, that we don't buy too much IV that's well ahead of HV. There are times when IV has not spiked much and the coming volatility from the earnings news is actually greater (sometimes much greater) than the market expects. Therein lies the opportunity.

Straddle Pricing Ahead of Earnings

I like to look at the total cost of the shortest-term options (those closest to expiration) to see how the options are priced. The straddle is if you bought BOTH a call and a put near the current price of the stock, known as the "at-the-money" or "near-the-money" straddle. Look at the chart below as an example:



Bid	Ask	Last	Volume	Delta	Open Interest	Gamma	STRIKES	Bid	Ask	Last	Volume	Delta	Open Interest	Gamma
29.20	31.05	29.98	1	0.9078	16	0.0072	502.5	0.35	0.42	0.38	255	-0.0506	229	0.0057
26.75	28.70	37.00	0	0.8968	30	0.0082	505	0.42	0.53	0.46	418	-0.0620	506	0.0069
24.40	26.15	24.90	7	0.8873	7	0.0092	507.5	0.51	0.62	0.53	905	-0.0742	228	0.0082
22.15	23.55	23.30	47	0.8752	82	0.0105	510	0.62	0.75	0.65	2.01k	-0.0899	1,165	0.0098
19.90	21.25	22.17	1	0.8530	26	0.0121	512.5	0.75	0.90	0.78	1.35k	-0.1085	494	0.0116
17.50	18.80	18.40	14	0.8370	44	0.0139	515	0.94	1.00	0.99	2.3k	-0.1294	1,629	0.0138
15.40	16.45	15.00	73	0.8078	8	0.0160	517.5	1.21	1.30	1.25	3.25k	-0.1621	1,336	0.0164
13.40	14.05	13.99	455	0.7746	166	0.0184	520	1.55	1.70	1.65	3.71k	-0.2020	2,448	0.0192
11.30	11.90	11.84	112	0.7344	81	0.0211	522.5	2.01	2.19	1.99	2.68k	-0.2498	735	0.0220
9.40	10.05	10.10	345	0.6814	251	0.0234	525	2.65	2.80	2.66	4.34k	-0.3065	2,006	0.0247
7.85	8.30	8.20	365	0.6202	135	0.0251	527.5	3.40	3.75	3.52	2.63k	-0.3721	1,385	0.0267
6.45	6.75	6.70	2.74k	0.5548	873	0.0262	530	4.40	4.75	4.45	6.09k	-0.4418	3,029	0.0280
5.05	5.35	5.25	4.48k	0.4870	664	0.0270	532.5	5.50	5.70	5.62	2.23k	-0.5151	560	0.0293
3.85	4.15	4.00	4.56k	0.4170	1,032	0.0269	535	6.80	7.30	7.00	3.45k	-0.5889	1,502	0.0285

If you were buying the Apple (AAPL) April 11th (weekly options) 530 call AND also buying the 530 put, that near-the-money 530 straddle would cost a total of 11.50 to purchase immediately (6.75 asked for the call plus 4.75 asked for the put).

That means that the buyer of this straddle has to expect the stock will move up or down by more than 11.50 points above or below 530. Why? Because if the stock doesn't move and finishes at the April 11th expiration right at the strike price of 530, then the worst case happens where both the call and the put expire worthless.

The best case is a monster move in either direction. The effective breakeven on this straddle at the expiration is 11.50 points above 530, or 541.50 (call is worth 11.50 and put is worth 0), or 11.50 points below 530 at 518.50 (put is then worth 11.50 and the call is worth 0).

We break this down in percentage terms for every example we look at, so 11.50 points divided by the strike price of 530 is a 2.17% move in either direction. So if you actually see a 4.3% move, you're looking at doubling your investment on the straddle. Note in this case that AAPL did not have earnings anticipated later in April but this straddle pricing approach can be used to estimate the expected implied volatility for a stock based on the option's market pricing.

As a side note, how does the options market reach this expectation of how much the stock will move? Based on market participants' interest in buying or selling those premiums. If the market-maker initially set the straddle pricing at 4% implied volatility and other players thought the actual move would be 2%, traders would sell the straddle and the pricing of the options would adjust downward.

So over time, you are looking at the consensus expectations for the entire market on how the stock should move based on the options pricing.

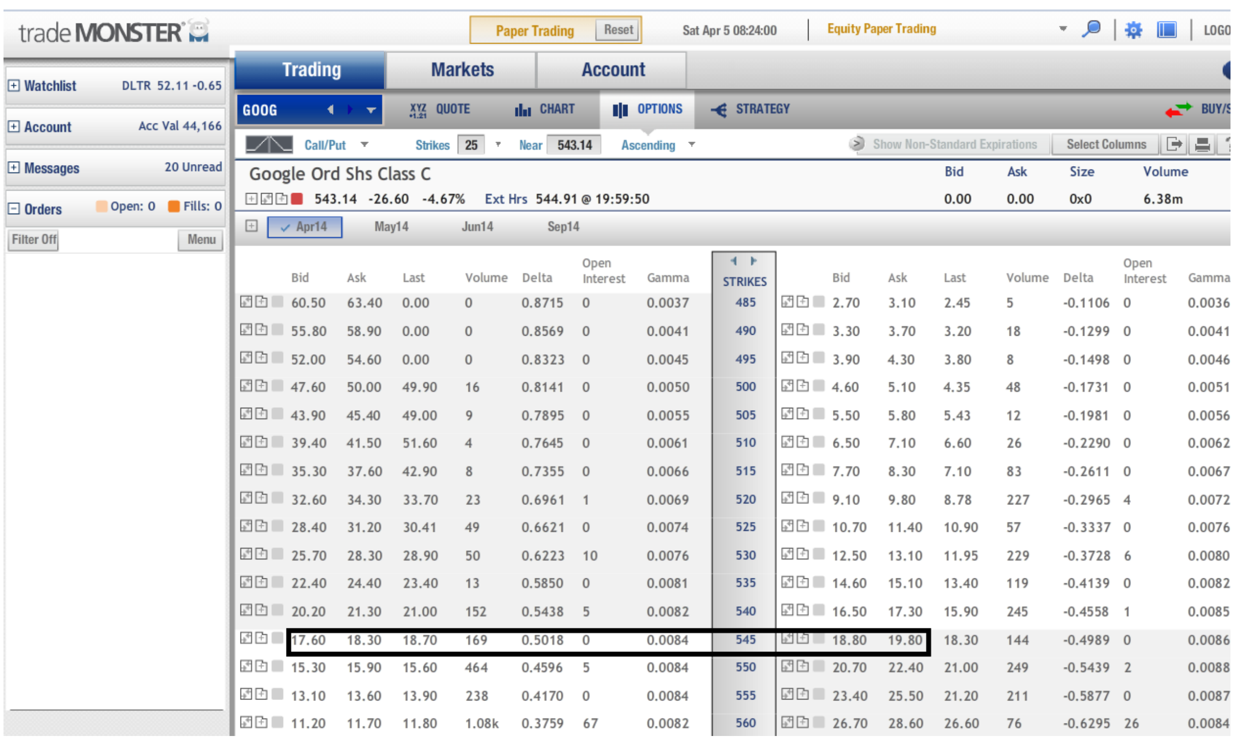
Gap History

You're thinking about buying an option on Google (GOOG) ahead of its next earnings. A first step is to look back at least 6 quarters and see how much the stock has gapped in the past:

<u>Gap from Prior Day's Close to Next Day's Open</u>

- October 2013 +9.88%
- July 2013 -3.70%
- April 2013 +0.50%
- January 2013 +4.71%
- October 2012 N/A (company accidentally released real-time 1 day before!)
- July 2012 +2.65%
- **AVERAGE +2.81%**

So if you see the upcoming earnings quarter's options priced like what's listed below, what would you do?



Bid	Ask	Last	Volume	Delta	Open Interest	Gamma	STRIKES	Bid	Ask	Last	Volume	Delta	Open Interest	Gamma
60.50	63.40	0.00	0	0.8715	0	0.0037	485	2.70	3.10	2.45	5	-0.1106	0	0.0036
55.80	58.90	0.00	0	0.8569	0	0.0041	490	3.30	3.70	3.20	18	-0.1299	0	0.0041
52.00	54.60	0.00	0	0.8323	0	0.0045	495	3.90	4.30	3.80	8	-0.1498	0	0.0046
47.60	50.00	49.90	16	0.8141	0	0.0050	500	4.60	5.10	4.35	48	-0.1731	0	0.0051
43.90	45.40	49.00	9	0.7895	0	0.0055	505	5.50	5.80	5.43	12	-0.1981	0	0.0056
39.40	41.50	51.60	4	0.7645	0	0.0061	510	6.50	7.10	6.60	26	-0.2290	0	0.0062
35.30	37.60	42.90	8	0.7355	0	0.0066	515	7.70	8.30	7.10	83	-0.2611	0	0.0067
32.60	34.30	33.70	23	0.6961	1	0.0069	520	9.10	9.80	8.78	227	-0.2965	4	0.0072
28.40	31.20	30.41	49	0.6621	0	0.0074	525	10.70	11.40	10.90	57	-0.3337	0	0.0076
25.70	28.30	28.90	50	0.6223	10	0.0076	530	12.50	13.10	11.95	229	-0.3728	6	0.0080
22.40	24.40	23.40	13	0.5850	0	0.0081	535	14.60	15.10	13.40	119	-0.4139	0	0.0082
20.20	21.30	21.00	152	0.5438	5	0.0082	540	16.50	17.30	15.90	245	-0.4558	1	0.0085
17.60	18.30	18.70	169	0.5018	0	0.0084	545	18.80	19.80	18.30	144	-0.4989	0	0.0086
15.30	15.90	15.60	464	0.4596	5	0.0084	550	20.70	22.40	21.00	249	-0.5439	2	0.0088
13.10	13.60	13.90	238	0.4170	0	0.0084	555	23.40	25.50	21.20	211	-0.5877	0	0.0087
11.20	11.70	11.80	1.08k	0.3759	67	0.0082	560	26.70	28.60	26.60	76	-0.6295	26	0.0084

Given that the April 545 straddle is priced at a total of 38.10 points, or 7.01%, I'd say the market has potentially overreacted to the big move last quarter and with volatility expectations more than double the average of +2.81%, it's certainly not a straddle I'd want to buy.

So should you sell it? Over time, net sellers should benefit, but individual situations can still have big gaps (against you if you did a selling strategy), so I don't tend to sell these options in front of events, unless I want to create a time spread.

The end result was a move more than double expected, as the straddle gained around +150% on the 10% gap up. So clearly the market tends to remember (and perhaps overly adjust to) what happened in the prior quarter.

What <u>Spread</u> Strategy Makes The Most Sense In Front of Earnings?

I'm a fan of the Iron Condor options strategy right in front of earnings, which involves selling options for a net credit on both sides of the market.

Here's how it works:

Let's say you're not expecting much from Nike (NKE) into its earnings and the options market is expecting the stock to move 2.25 points in either direction from the current level at 54.50.

You could sell the shortest-term weekly options which expire at the end of the current week, about 2.50 points or more on either side of the stock's closing price right before the earnings are announced. In this case you would consider selling the 57 call and then buying the call right above it, in this case at 57.50 (usually we will give at least the market's expected move, and sometimes some extra breathing room on top of that as well).

At the same time, you are also selling the 52 put and buying the strike price right below that at 51.50, which is meant to protect your maximum risk in case of a bigger than expected gap in either direction.

What scenarios could occur? A big gap up, a milder than expected move up, a flat market, a slight edging down or a bigger down move. Remember that selling the 57 call and protecting it by buying the 57.50 call is like saying, "I think the stock will not go over 57.00 at the expiration at the end of this week."

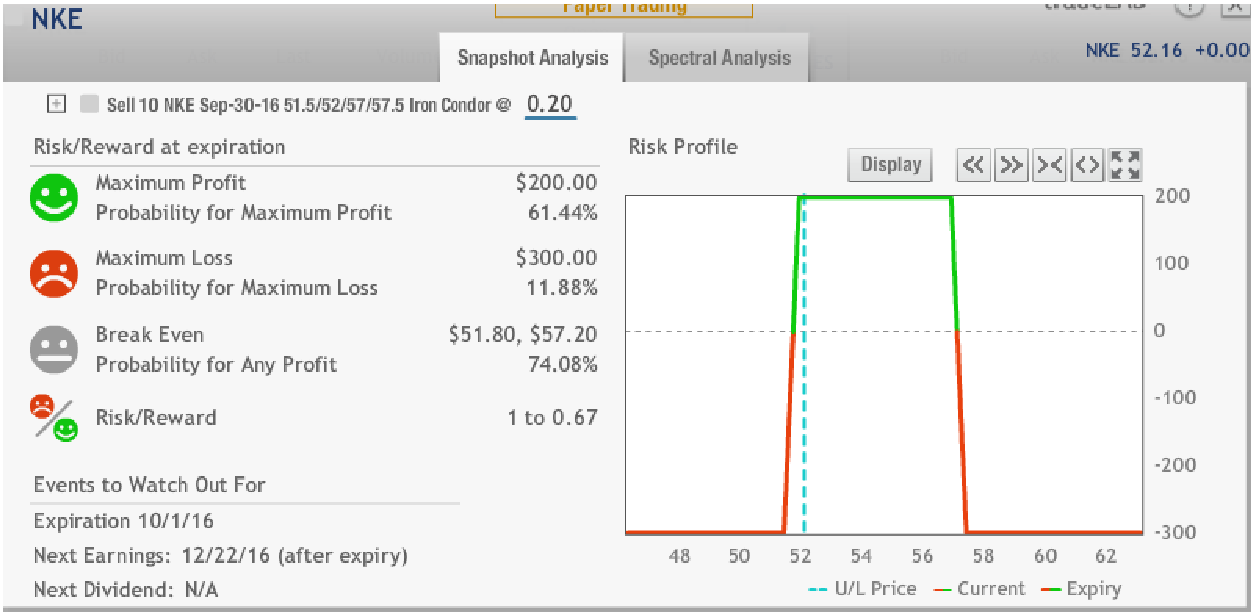
So obviously a big move above that is not desired in this strategy. However, if the stock does test the upper or lower boundary in our iron condor, remember that the other side is winning to at least mitigate your risk. Ideally, however, you want the options to go out with no value with a stock finish between 52.00 and 57.00 at the expiration.

That allows you to pocket the initial premium you collected, in this case $20 per iron condor contract minus your opening commissions. So a 10-lot would be $200 collected against a net risk of $300 (since the maximum risk would be $500 on 10 contracts but you collected $200 up front).

Your broker would then require you to hold the net risk of $300 as margin if the worst case scenario unfolds (where NKE shares finish above 57.50 or below 51.50 at expiration). You can't lose any more than that if NKE shares crash to 45 or if they skyrocket to 60.

In actuality, NKE gapped down less than 1 point and then edged down a bit above 52.00 to stay in the expected range.

Nike (NKE) Profit and Loss Graph on Expiration Morning:

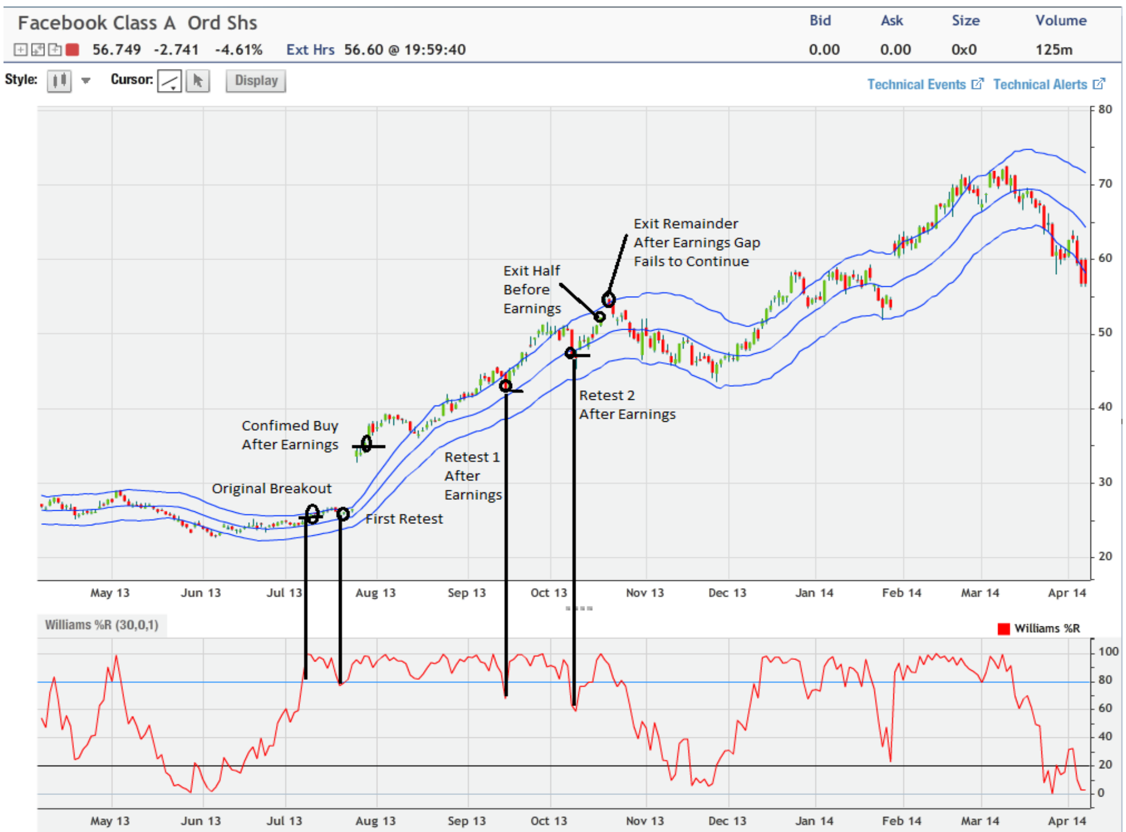


When the trade stays in the expected range, you keep the full credit received and you wait for the next opportunity!

Buying After Earnings to Ride a Trend

While perhaps not as thrilling to buy after a potential gap, it's often lower risk with plenty of reward potential remaining. Check out this example of Facebook (FB) which offered numerous opportunities.

Facebook (FB) After Earnings Call Study



As you can see above, the initial breakout on FB shares (using my proprietary indicators like Williams' Percent R (The BigTrends Way)) took place in early July 2013 and confirmed that move about 2 weeks before the earnings hit. The stock was at around 25.50 and it even gave a first retest just 1 week after the first buy. The retest shows a spot where the stock's trend should hold. This was 3 days before the earnings. Upon the earnings, the stock gapped up from 26 to 33, giving those willing to play the bull trend a profit of over 150% on the August 26 calls.

But for those who missed the gap, there were more opportunities. The confirmed breakout above the gap day high now around 35 gave the chance to ride the September 35 calls up to the mid-40s, again offering more than 100% returns on average on the whole position.

And if you missed this first "after earnings" opportunity, you still had not one but two retests to hop back on the uptrend. Retest #1 went from 43 in mid-September to 50 two weeks later, while

Retest #2 in early October gave a chance to position ahead of the next earnings two weeks after that. That move went from 48 to 55. Generally, if I'm in well advance of the earnings date, I like to sell off half my position at a double if I can to get my risk capital back before the event. The rest of the trade is essentially a free trade at that point, which can lead to even bigger potential profits while not stressing the account if the gap goes the wrong way.

And this leads us to my #1 favorite options strategy for earnings season which forms the basis for the ***BigTrends Earnings Extravaganza*** advisory service and that is…

Trading Options Immediately BEFORE the Earnings Are Released, When the Directional Momentum is Already High

The primary considerations to merit making a quick pre-earnings trade are these:

1) **Only Trade in the Direction of the Current Momentum –** We use the Commodity Channel Index (CCI) and Williams Percent Range (The BigTrends Way) to identify high momentum in a particular direction and we only take trades in the direction of this existing momentum. Both Williams Percent R and CCI must be confirmed bullish (or bearish) before we buy calls (or puts) before earnings.

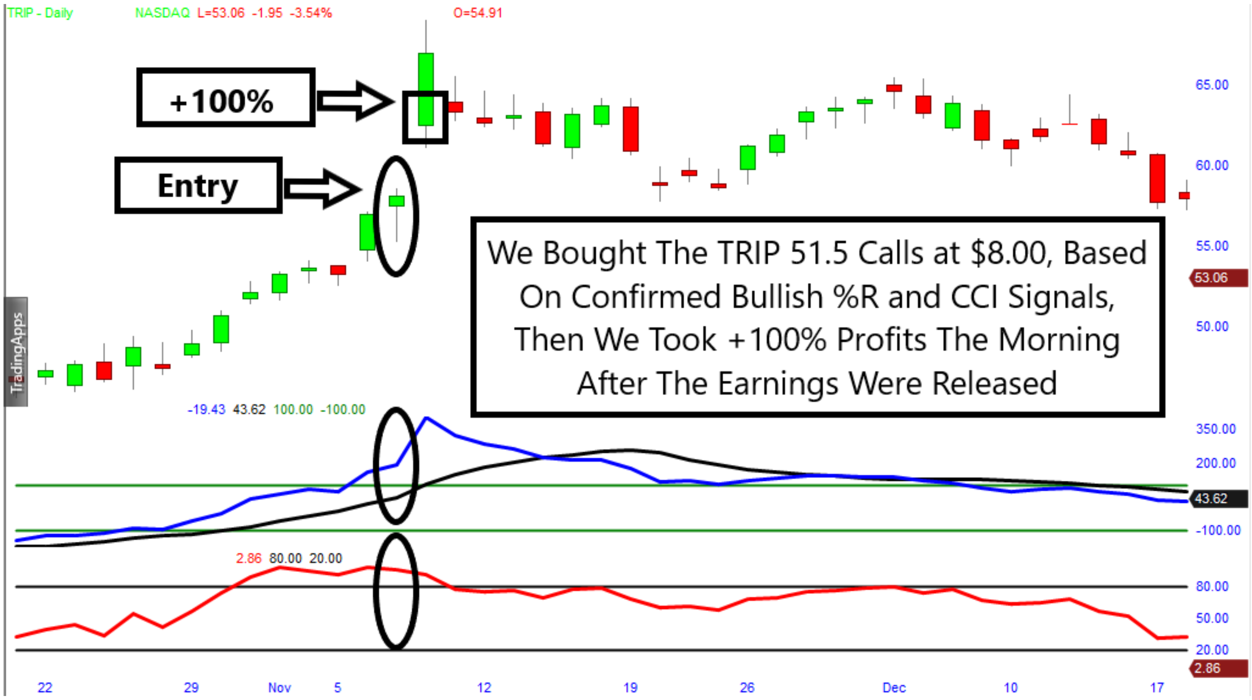
2) **Buy Options that Are Deep In the Money –** To avoid getting blasted by the volatility crush that follows an earnings release, we make sure that our options are deep enough in the money to withstand TWICE the expected move before our stop is triggered. This leads to a more stable trade while maintaining large upside potential if the stock moves greatly in our favor. Our potential loss is limited to the premium paid for the options while our potential upside is unlimited! This service truly takes advantage of asymmetric risk-reward ratios.

3) **Buy Options with a Bit More Time than You Need –** While the average holding period for our ***BigTrends Earnings Extravaganza*** trades is roughly 1-3 trading days, we find that the liquidity in the monthly options allows us to have more favorable prices than the shortest-term weekly options. This gives up a little leverage but it is well worth it for the greater stability and tighter bid/ask prices on the monthly options, allowing us to lower our execution costs over time.

4) **Be Ruthless about Exiting on Patterns that are Not Continuing After the Gap –** We've found that for the quick trades before earnings, the proper pattern is a steady and persistent trend in our desired direction. To keep our risk tight and our reward potential large, we use a profit target of +100% on the full position and a stop of -50%. We also use a trailing stop of -50% from the peak option trade. If the trade hasn't hit its +100% target by 12:00PM EST on the day of the reaction, then the profit target shifts from +100% to +50%. This allows us to catch the big winners when they occur right away while reducing our risk if the pattern doesn't fit the typical "winning profile".

See the next page for specific examples of this strategy…

TripAdvisor (TRIP) Call Purchase Case Study

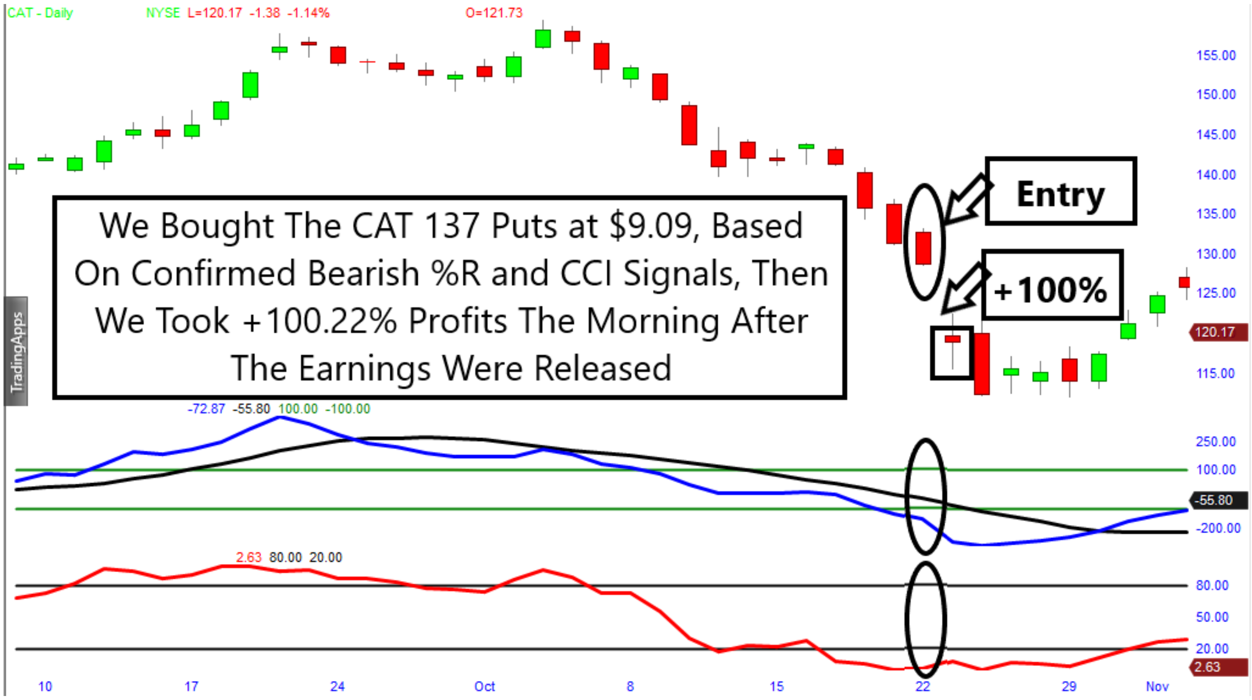


Here's a call example where TripAdvisor (TRIP) was confirmed BULLISH on %R and CCI so we bought calls right before the earnings were released. You'll notice that this particular trade hit our +100% target and we exited the full position at that level.

Note that this trade was exited on the next day's open, which is not always the case but it does happen on some of our quick profits or quick stops. Most trades last between 1 to 3 days and we have a 3-day time-stop that exits trades that haven't hit their stop or target before then.

We also have a rule to issue a maximum of 3 new trades on any given day. This will keep our overall exposure limited and allows our trading capital to be spread out more evenly over multiple days of earnings.

Caterpillar (CAT) Put Purchase Case Study



Here's a put example where Caterpillar (CAT) was confirmed BEARISH on %R and CCI so we bought puts right before the earnings were released. You'll notice that this particular trade hit our +100% target and we exited the full position at that level. Note that this trade was also exited on the next day's open.

We usually trade Monthly Options with at least 3 weeks until expiration and we aim for an average contract price of less than $5.00 over time. This particular example cost us $9.09 because our method requires us to trade options that can encompass TWICE the expected move before the option hits its 50% stop level.

BigTrends Earnings Extravaganza (BEE) Key Points:

- We use a combination of Commodity Channel Index (CCI) and Williams' Percent R (The BigTrends Way) on daily charts to trigger trades
- We look for both indicators to be confirmed Bullish or Bearish before a trade is placed.
- Percent R sets up when we get a close above 80 (long) or below 20 (short). The signal is then confirmed when we get a close above the setup bar's high (long) or below the setup bar's low (short) within 5 trading days.
- CCI sets up when we get a close above +100 (long) or below -100 (short). The signal is then confirmed when we get a close above the setup bar's high (long) or below the setup bar's low (short) within 5 trading days.
- Our focus list consists of all stocks with upcoming earnings reports, this list is then filtered based on stock and option liquidity.
- Trades are entered at 3:00 PM EST on the day before the earnings are released (this means the earnings will be announced after the close of the entry day or the next morning before the release.

A New Trade Alert Looks Like This:

BE²
BIGTRENDS
EARNINGS
EXTRAVAGANZA

November 7, 2018
3:37 PM ET

New Trade:

Buy-to-Open (BTO) the TripAdvisor (TRIP) November Monthly (11/16) 51.5 Call (TRIP 181116C51.5) at 8.20 or less.

Trade Well,

Price Headley

Here's a Snapshot of Recent Performance:

BigTrends Earnings Extravaganza					
Entry Date	Exit Date	Name	Entry Price	Exit Price	% Trade Gain/Loss
10/11/18	10/15/18	JPM November 115 Put	$7.50	$7.30	-2.67%
10/11/18	10/15/18	WFC November 55 Put	$4.15	$2.34	-43.61%
10/16/18	10/17/18	IBM November 150 Put	$8.30	$16.60	100.00%
10/16/18	10/17/18	CREE November 41 Put	$4.35	$2.60	-40.23%
10/19/18	10/22/18	SLB November 62.5 Put	$4.64	$5.85	26.08%
10/22/18	10/23/18	CAT November 137 Put	$9.09	$18.20	100.22%
10/22/18	10/23/18	HOG November 42.5 Put	$4.30	$4.50	4.65%
10/22/18	10/23/18	UTX November 131 Put	$6.75	$5.55	-17.78%
10/24/18	10/25/18	LVS November 57.5 Put	$5.60	$4.64	-17.14%
10/24/18	10/25/18	CELG November 81 Put	$7.63	$5.55	-27.26%
10/24/18	10/25/18	LUV November 60 Put	$5.31	$10.60	99.62%
10/25/18	10/26/18	FSLR November 50 Put	$7.00	$10.50	50.00%
10/25/18	10/26/18	GILD November 75 Put	$6.70	$7.40	10.45%
10/25/18	10/26/18	INTC November 50 Put	$5.90	$4.30	-27.12%
10/29/18	10/30/18	CTSH November 76.5 Put	$7.90	$9.80	24.05%
10/29/18	10/30/18	TPR November 48.5 Put	$8.00	$8.00	0.00%
10/30/18	10/31/18	EBAY November 33 Put	$5.68	$3.90	-31.34%
10/30/18	10/31/18	TAP November 62.5 Put	$5.07	$1.80	-64.50%
10/31/18	11/02/18	APA November 43.5 Put	$5.75	$6.61	14.96%
11/01/18	11/02/18	ABBV November 87.5 Put	$8.05	$6.00	-25.47%
11/01/18	11/02/18	CVX November 117 Put	$7.90	$3.85	-51.27%
11/07/18	11/08/18	TRIP November 51.5 Call	$8.00	$16.00	100.00%

Past performance is no guarantee of future results. Commissions are not included, so factor your commission rates into trade examples. All trades involve risk of loss. Every trader should educate themselves on options by reading the booklet entitled "Characteristics and Risks of Standardized Options" available here: http://www.optionsclearing.com/about/publications/character-risks.jsp

You'll notice in the example above that 11 out of the 22 trades in the October 2018 earnings season were winners, for a 50% win rate.

You will also notice that the **average gain** is larger than the **average loss**, with an average gain of +48.20% and an average loss of -33.50%.

The combination of more winning trades than losing trades AND profits that are larger than losses is a recipe for success, and explains why this is our favorite buying strategy ahead of earnings!

Where do you get the earnings dates?

Start with Yahoo's earnings page for example: http://biz.yahoo.com/research/earncal/today.html It defaults to today's earnings releases and you can scroll ahead to upcoming days as well. You can search by company stock symbol as well as get an overview of the day to day list of companies with earnings due.

I'll confirm this with the company's Investor Relations department if needed on the exact timing of the earnings release (before the open or after the close on a certain day) to make sure I have the correct date and time.

For more information on the ***BigTrends Earnings Extravaganza*** alert service, call us toll-free at 1-800-BIGTRENDS (800-244-8736) or email us at clientcare@bigtrends.com.