Spread Bet & CFD Options

Reference Sheet

What are options?

There are two types of options: calls and puts.

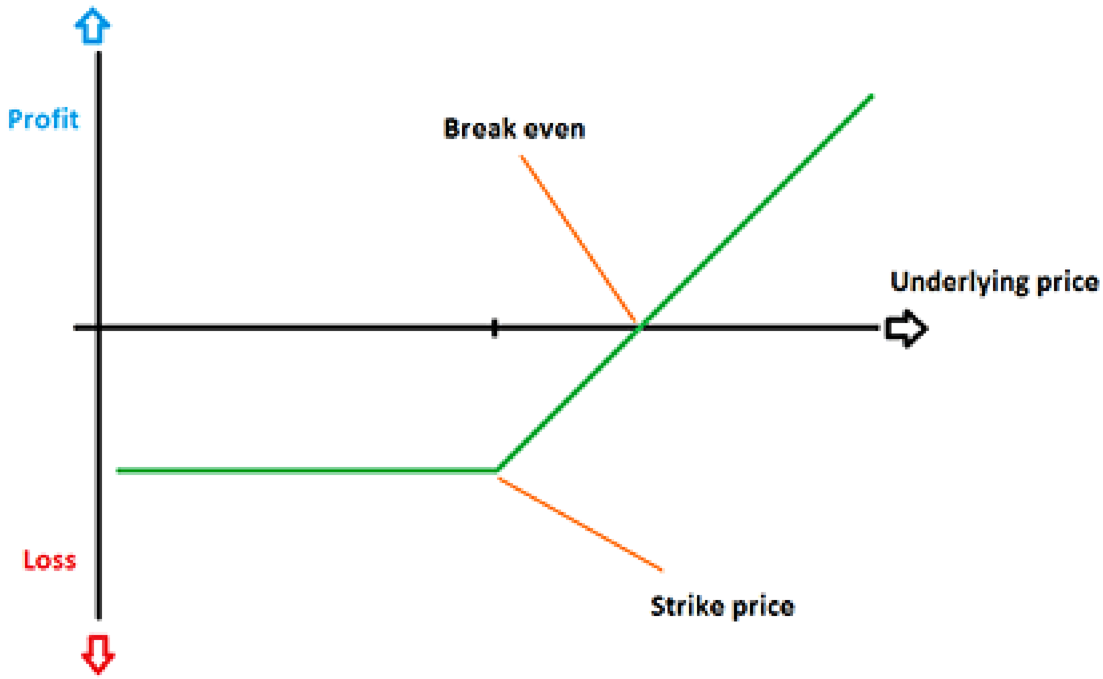
Call option:

The buyer of the call option has the right (but not the obligation) to buy an agreed quantity of an underlying instrument from the seller of the option on or before a certain time (the expiration date) and at a specific price (the strike price). The seller is obligated to sell the instrument should the buyer decide to do so.

You can go long or short on a call option, determining whether you are the buyer of the option or the seller of the option.

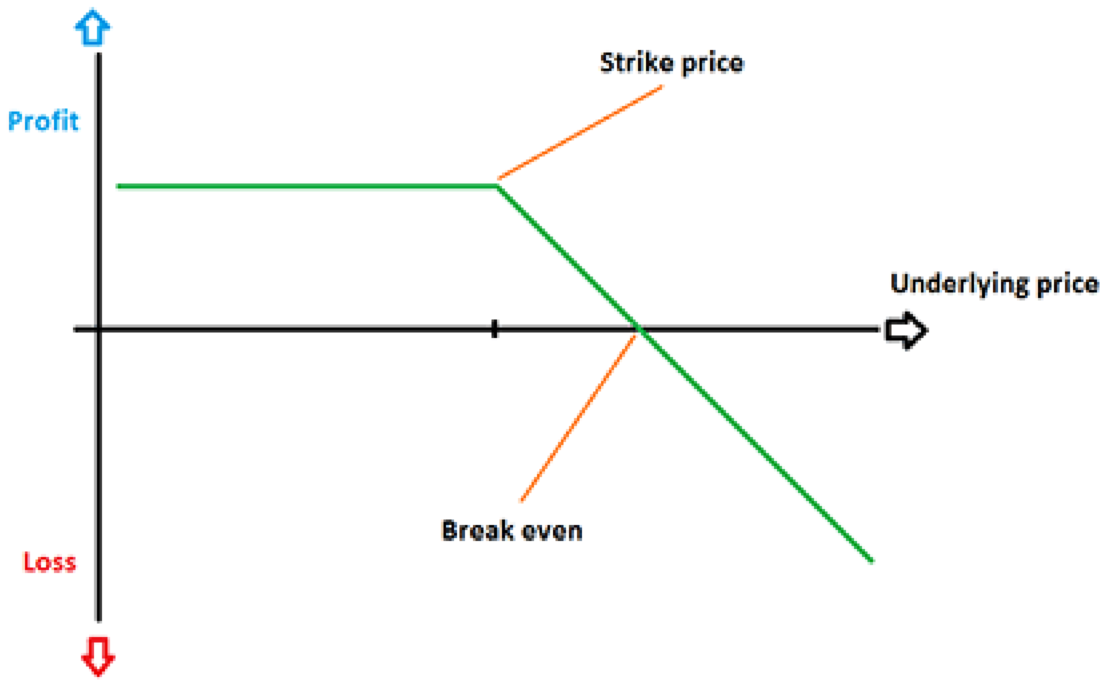
Long Call (buyer):

Limited loss capped at the price you bought the option
Unlimited potential profit


Profit
Break even
Underlying price
Loss
Strike price

Short Call (seller):

Unlimited potential loss
Limited potential profit capped at the price you sold the option

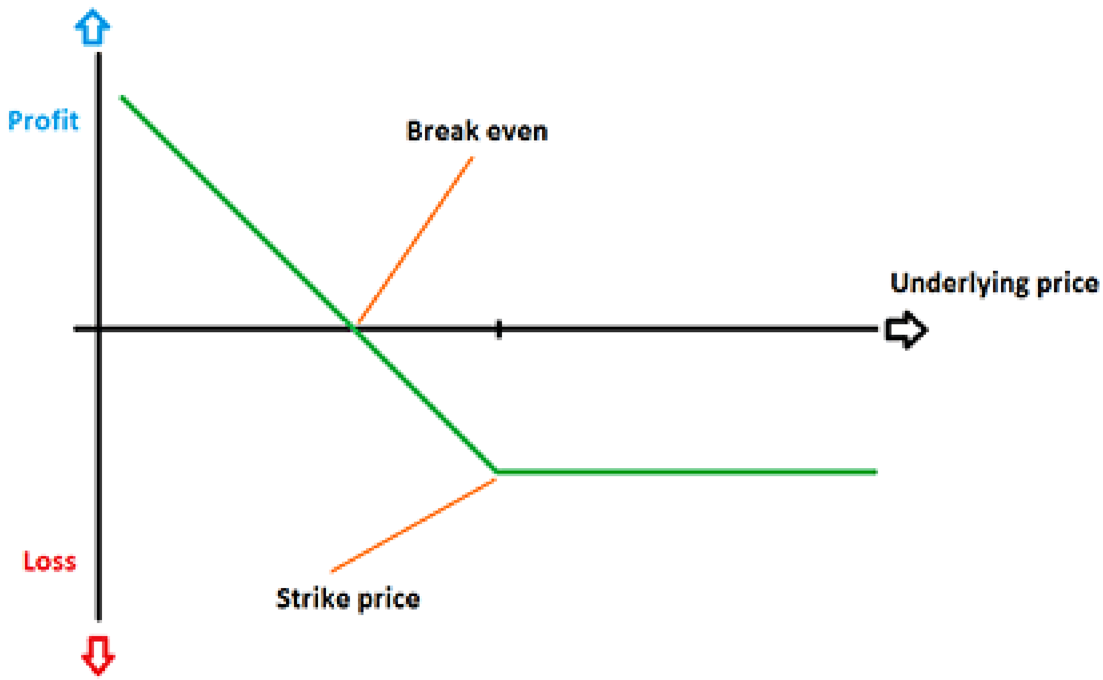


Put option:

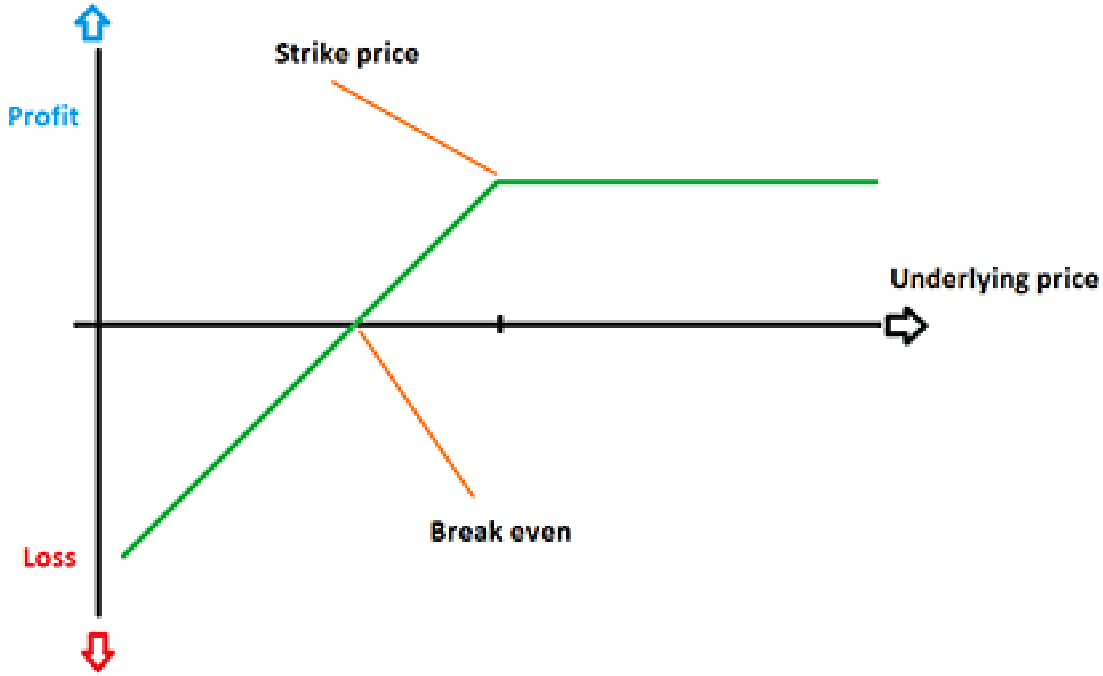
The buyer of the put option has the right (but not the obligation) to sell an agreed quantity of an instrument to the seller of the option at the strike price on or before the expiration date. The seller is obligated to buy the instrument should the buyer decide to do so.

You can go long or short on a put option, which determines whether you are the buyer of the option or the seller of the option.

Long Put (buyer):
Limited loss capped at the price you bought the option
Unlimited potential profit



Short Put (seller):
Unlimited loss
Limited potential profit capped at the price you sold the option



Trading options as a spread bet:

If you have a spread bet account then you will be placing a spread bet on an option, meaning you are spread betting on the price of the option. This works in the same way as any other spread bet: for example, if you buy GBP 10 per point of a UK100 option at 34 and you sell at 40, then you have made 6 x GBP 10 = GBP 60 (you will trade spread bet options in your base currency. In this example, base currency is GBP).

Trading options as a CFD:

If you have a CFD account then you will be trading a CFD on an option, meaning you have a contract for the difference in the price of the option. For example, if you buy 10 contracts of a UK100 option at 34 and you sell at 40, then you have made 6 x GBP 10 = GBP 60 (UK100 options are traded in GBP).

Why do traders use options?

Key features of options:

-Spread bet options are tax-free and CFD options are exempt from stamp duty[1]
-Capped risk when buying options
-Potential to profit from static markets by selling options
-High level of leverage can lead to higher returns

> *While leverage may lead to exponentially larger profits, it may also lead to exponentially larger losses.*

-Potential to profit even if you don't know which way the market will move by buying a straddle or strangle strategy
-Can profit even if the market moves against you

> *When selling an out-of-the-money option, the market can move towards your strike. At the expiry time, as long as the market hasn't moved through your strike by more than the price you sold the option for, then you will still make money.*

-Strategies for any market environment

> *Straddles, strangles, call/put spreads, ratio call/put spreads, covered call, protective put, butterfly, and more.*

Ready to Trade Options?

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[1] UK Tax laws may be subject to change, may depend on personal circumstances and can differ if you pay tax in any jurisdiction outside of the UK. It is therefore advisable to seek independent tax advice. It should be noted that conversely the losses that you may incur by the way of financial spread betting can't be offset against tax liabilities. Please note that spread betting, as contracts for differences, is legally enforceable as contract within the UK. Unlike traditional fixed odds bets, spread betting trades are not simply 'gentlemen's agreements'.