So why do people trade options?

On screen disclosure:
NOTE: The securities in this video are fictional. Everyone's situation is different, and this video is not financial advice. Do your own research.

People trade options for a variety of reasons. One reason could be that you believe a stock will go up or down. This is sometimes called “speculation.”

On screen copy:
Speculation
Traders can benefit from upward or downward movement of a stock or index

Before we explain speculation, we would like to make you aware of some key concepts:
A little background before we begin…

Buying a call is one example of a speculative bullish strategy, buying a put is one example of speculative bearish strategy. A call represents the right to buy and a put the right to sell. Each contract represents 100 shares and includes an agreed upon price known as the strike price, and a specified time frame, known as the expiration date.

On screen copy:
Long Call Purchase
Bullish & Speculative
Call
Right to buy
1 Contract
100 Shares
Strike Price
Agreed price
Expiration Date
Time Frame

Long Put Purchase
Bearish & Speculative
Put
Right to sell
1 Contract
100 Shares
Strike Price
Agreed price
Expiration Date
Time Frame

On screen disclosure:
Every example that we use is for illustrative purposes only and we do not include any commission and fees.

When you buy a stock, you may have a bullish view that the price will go up. When you buy options, you can apply the same bullish outlook, but with a few key differences.

On screen copy:
XYZ Stock
100 Shares
Your Outlook- Bullish
Purchasing Call Options can be more affordable because you're paying a small premium for the right to buy the shares rather than directly buying the shares. If you're paying less, you're also risking less capital, should the stock decline significantly.

On screen copy:
BUYING STOCK
$40.00 per share x 100 shares
$4,000.00

BUYING CALL OPTIONS
$1.00 per share (premium) x 100 shares
$100.00

To speculate upward movement with call options, you’d first pick a strike price and an expiration date.

On screen copy:
Buying a Call

[Line graph showing market price rising above strike price]

**On screen disclosure:**
For illustrative purposes only, not an actual investment. Example does not include trade commissions or other fees

If the stock goes above the price you chose you’d only net a profit if it goes higher than your chosen price PLUS the premium you paid.

On screen copy:
Buying a Call
PREMIUM $1.00
XYZ STOCK PRICE
Break Even = $46.00 ($45.00 Strike Price + $1.00 Premium)
Max Gain = Unlimited
Max Loss = Premium
BREAK EVEN
MARKET PRICE $48.00
STRIKE PRICE $45.00
TODAY

**On screen disclosure:**
For illustrative purposes only, not an actual investment. Example does not include trade commissions or other fees
You can also buy put options to speculate downward movement of a stock. If the stock price falls below your strike price plus the premium you paid, you’d reap the benefits.

[Line graph showing market price falling below the strike price]

On screen copy:
Buying a Put
PREMIUM $1.00
XYZ STOCK PRICE
Break Even = $34.00 ($35.00 Strike Price - $1.00 Premium)
Max Gain = Strike Price - Premium
Max Loss = Premium
BREAK EVEN
STRIKE PRICE $35.00
TODAY

On screen disclosure:
For illustrative purposes only, not an actual investment. Example does not include trade commissions or other fees

You can be a bull or a bear with speculative option strategies.

On screen copy:
Your Outlook- Bullish
Your Outlook- Bearish

This is why speculation is one way people trade options.

On screen copy:
Merrill® logo

[End of transcript]