

Greetings from the Pirate!

Hey everybody, I hope this edition of Traders Edge Insider finds you well. Wow, what a ride that 1st quarter proved to be, closing out with two of the major U.S. indices having set new record highs.

Just goes to prove that you can't over-think or get in the way of the market – it's going where it's going no matter what the fundamentals seem to be or what the smart guys in suits are telling us. Whether the move is up, down or sideways, we have one job – trade effectively and bag profits...period!

That said, now that we clipped the old numbers you can bet that Tom, Dick and Harry are gonna be on the box daily calling for a sharp selloff...too far too fast, lack of catalyst, uneven recovery, fear the Fed is gonna close down the gravy train...yadayadayada. Man, they just don't seem to be able to learn - or they don't have the audience's best interest at heart...but that's another discussion altogether!

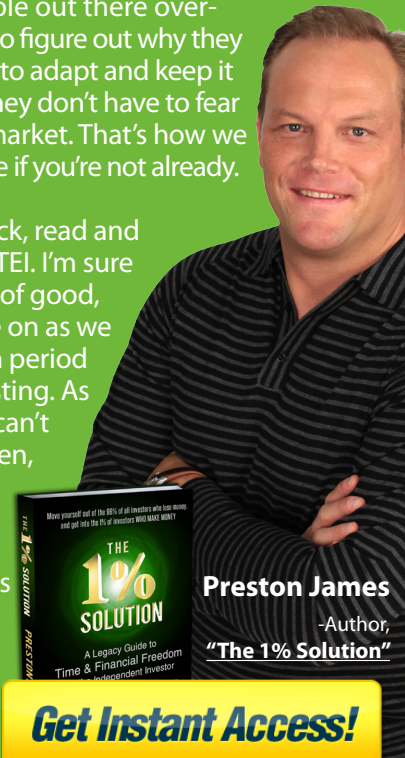
Fact is no matter how much this game has changed, and it's changed big time in the years I've been knee-deep in the action taking my piece, one thing has remained consistently the same – simply stated, those who check their egos at the door, come to the party with a solid plan and are always set to adapt, adjust and effectively trade whatever the market is offering tend to come out on top!

Trust me, I know that to many this might sound simplistic, but the truth is the KISS approach is the one that works and has done so consistently for years. The game has never been about being a genius and being right...it's always been about percentages - getting it right more often than not, regardless of where the market might be, how it's acting or where it's heading.

Truth is the vast majority of people out there over-complicate things and can't seem to figure out why they continue to lose. Those who learn to adapt and keep it simple find liberation in the fact they don't have to fear every move and gyration in the market. That's how we do it and I suggest you do the same if you're not already.

Well, for now I invite you to sit back, read and reflect on this month's edition of TEI. I'm sure you'll find it's packed with plenty of good, actionable info you can capitalize on as we begin the 2nd quarter of 2013 – a period that promises to be pretty interesting. As usual, I'm the first to admit that I can't predict or tell you what will happen, but I am certain there will be plenty of opportunity for profit!

— Preston James



Preston James
-Author,
"The 1% Solution"

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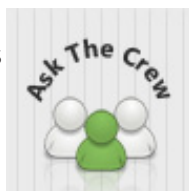


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MONSTER

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Ask The Crew

Crew members tackle questions submitted by readers each month...



[Read more » page 18](#)

Traders Talk

In this month's Traders Talk, the Pirate once again invites us into his lair to talk shop and pass on some wisdom...



[Read more » pages 2-8](#)

Monster's Perspective

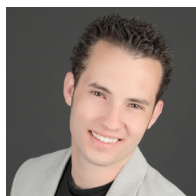
Our friend and colleague at optionMONSTER, Chris McKhann, just recently asked the rhetorical question, "Is now the right time to buy calls"...



[Read more » pages 9-10](#)

Karson's Insight

If you are at all in touch with the macroeconomic picture, you have undoubtedly heard about the insane things happening in Cyprus...



[Read more » page 11](#)

Musings from the Editor

Good friend of mine recently turned me on to a blog run by an author/blogger/music company vet who prolifically cranks out some good stuff near daily...

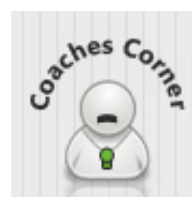


[Read more » pages 12-15](#)

Coaches Corner

For this month's article in the coaching corner, I'd like to address a basic understanding of implied volatility...

[Read more » pages 16-17](#)



Traders Talk:

TEI's Louis Horkan Interviews Preston "Pirate" James



In this month's Traders Talk, the Pirate once again invites us into his lair to talk shop and pass on some wisdom. Unlike the first interview, where Preston shared insight and hard-learned lessons (who can forget the indelible visual from Wrong in the Thong...yikes) gained during his many years in the market - as student, trader and teacher - the focus this month is squarely on what he considers to be the most exciting opportunity to ever emerge for the independent trader. In his view, there's a new paradigm in trading that's not before existed - one that traders must take heed of and learn to capitalize on.

This time around, Pirate spells out his game-changing approach tailored to individuals - a strategy that the big boys envy, yet are precluded from utilizing. Indeed, a unique opportunity that finally levels the playing field and provides you, me and the rest toiling the markets with a real advantage. I highly encourage you to take your time reading through the interview...and to reach out to Preston and his Crew thereafter to learn more...it may well prove to be the most important financial step you ever undertake.

TEI: Everybody and their brother is offering guesses on what happens with the market up here around record-territory. What are your thoughts on people spending their time trying to decide whether the market is going to take off or not?

PJ: Yeah, it's in our face more now than ever - the different opinions. It just seems noisier than ever in that respect. I try to mellow people out rather than try to predict where the market is going next. Trade the market that you have at hand and realize that when we talk about market cycle, it takes three out of four stocks with it. If the market is like what we've seen lately - a strong market cycle with stocks less punished when they have bad news and a tide that is now rising - one of the aggressive things you can do is go even more on margin. No matter what you hear the market is going higher - it's just taken out all time highs. Then it'll inevitably turn and correct - go down the other way. But it's not going to do that in one day. It just seems like the market wants to fool the most amount of participants. So you never know how high it can go

and you never know how low it can go. The point is you want to trade the market at hand.

TEI: Looking at the market cycle as it now stands, how is your trading influenced?

PJ: Well, there's always little hiccup-type things or it wouldn't be a market. As we're recording the Cyprus thing came in and scared it, but it looks like it's rebounded because that vote didn't go through. Until we see some breakdown I adjust everything that I'm doing with a more bullish bent to it. That means utilizing margin, but also portfolio margin...which a lot of people still don't know about. You basically don't want to be looking at the short-side of the market too much right now. I'm a little forgiving on what a stop loss or protections might be. Those are a little more aggressive, meaning they're a little further away. If the market cycle were to turn, I'm going to be a lot more selective...it's going to be smaller size and there's going to be protections that are a lot closer.

I want to back up for one second to reiterate something [important] about the market cycle. It's often detached from what the economy is doing. If you listen to the evening national news and heard the first five stories about the economy, that is completely not the market cycle. The other little corollary of that is that some people just can't do it - they cannot trust the market cycle. They cannot see what is right in front of them. They're too tainted and clouded, either by the person that just got laid off next to them or a neighbor that just had to move. I don't blame them. We're not always wired to see what is plain in front of us. We're constantly trying to interject and think about things in the world. Some people just can't ever do it - it's the most frustrating thing for them. They revert back to old habits - this stock has to go up because of this-and-that reason. They keep interjecting what they think should happen or what shouldn't happen - and it's a recipe for disaster.

TEI: One of your primary offerings is the Weekly Options Windfall or WOW service, focused on trading weekly



options. Although we talked about them some last month, please share your thoughts on the opportunity they provide traders in today's environment?

PJ: I think it's real important to drill into a couple of key things when we're talking about the weekly options - this animal that was created in the spring of 2010. There's probably five things I want to hit as to why someone really needs to stop what they're doing right now and pay attention to why they might want to sell some income on weeklies this coming Thursday, or whenever the next Thursday is.

Securities now get created every Thursday morning and they expire the following Friday. Now when you look at the major component out there that has produced more volatility across the board - near-zero interest rates - it has money flying around. Not only from one stock to another, but out of the market entirely and back into the market entirely. Money is not idly sitting around - it's actively moving around. The latest Barron's Round Table said we're going to have these [low rates] for the next five years at least and some are saying it's going to be here at least 10 years. So we've got these near-zero interest rates that create volatility. Volatility is great when you turn it around and become a seller of options, because options are higher-priced in general. So we have that major underlying factor. Then there's the fact that about 80 percent of the trading volume that you and I see every day is being pushed around by these big institutions. It's not you and me and our friend over our backyard fence who are participants in the market - we're a small minority. So you have all this major money sloshing around because of low interest rates.

Now all of the sudden you have this instrument - the weekly option... There are two big hot-zones of time decay in the life of an option - whether it's a 6-month option, a 3-month option or 1-year option - when it actually declines the most...loses most of its time value. Why do we even care? Because when you turn around to become a seller of these options you become very interested in where the time decay spots are. The two biggest spots are over the weekend before the final week of their existence and between the last Thursday and Friday - that Friday meaning the last day of its existence. So every weekly option created has these

two biggest time decay spots built in - that fact can't be understated! Not to mention that when you add up the Thursday to the following Friday's premium, and you compare that to the former 1-month premium, four of those 1-week expiring options equals roughly double what a 1-month premium used to bring in if you were selling a 1-month option.

Now there's reason for that. I was in Austin, Texas last weekend for the South by Southwest Music Festival. There are lots of parties and revelers there, with 2,200 bands over four days. Well, you'd constantly be seeing people dropped off in taxicabs two or three blocks away from 6th Street. Inevitably they were going into the first bar they could find - they weren't walking down eight blocks to find a bar. The majority ducked into the first little thing that looked like fun. That's just like weekly options. Why some of this big premium exists is because it's the closest thing that's happening. For some reason in an option market that just seems to attract most of the volume and interest. This is my theory on why they're pumped up. Why does that exist? Why do 4-weekly options equal double a 1-month premium? Well, I just think it's the closest bar. It's the closest action people can go to. These factors I'm laying out are impossible to ignore in terms of what they can do for you when you become a seller - doing spreads and money presses. That's the backbone and the root of why it's so damn compelling. They never used to exist.

TEI: You mentioned last month you don't see this opportunity going away any time soon.

PJ: Oh no. In fact, last Thursday there were eight new stocks carrying weekly options for the very first time. Now that's a big jump for one week - there are plenty of weeks that go by and we haven't added any. They've actually taken some off from time to time. I was just listening to a seminar that I did in the summer of 2010; there were 18 stocks that had weeklies - I think it's over 160 now. Now, maybe some have heard these things for the very first time. Sometimes those things are just kind of tucked away, so as we were getting ready to talk, I thought, "I've got to dig up the backbone of what is so compelling about these things." I had sleepless nights when they were first out - just contemplating what this means. For example, right now with these

low interest rates, you could purchase stock at a 1 percent margin rate. For someone who is buying a boatload of stocks that pay a 4.5 percent dividend yield, that also happens to have weeklies - just right there you're making a spread on your money. Of course a stock is going to fluctuate, but when you go out and purchase a 5 or 6-month out protective put option a few dollars underneath the stock, and then turn around every Thursday and become a seller of weekly call premiums... What I'm saying is you put together these low interest rates that we have, [combined with] these volatile options that we have (for the most part - they do go off the behavior of the stock, but overall, you have more volatility today), and you start socking away these weekly premiums. You can see the math. I'm getting a dividend of 4.5 percent and the low cost of my margin. If you wanted to take that \$1 million and go \$7 million worth of stocks, you can as soon as you buy these put options. It releases this margin and then you're selling more and more of these weekly calls. You can get ahead pretty quick and really not have a way to lose money after a while. And you've got four more months left of premium writing, which means 16 periods of weekly writing or selling. And if you decide not to trade - let's say an earnings announcement is coming up and you just don't feel comfortable selling premium that week. Well, you could take that week off. Before you only had a 1-month choice. You're waiting for four or five weeks not doing anything so you can get earnings out of the way. Now you can sell three weekly premiums, which by the way carry more of a premium because earnings are getting nearer. On some stocks it's just insane - like a Chipotle Mexican Grill or an Apple. What are they gonna announce? These premiums just start going through the roof. You can be selling those in the weeks leading up to earnings and then choose not to participate over the earnings announcement.

Getting back to market cycle, if we have a general cycle behind us that is bullish, that helps me adjust what strike price I sell. Sometimes I don't sell options over the full position that I can. Maybe I will sell half. Say it looks like market cycle is going well, you have stock in a nice trend and [during] the last two earnings announcements the stock really started rising into that announcement; maybe you don't want to sell 100 percent of what you can. Maybe you sell

half to bring in some premium and you're looking for a capital gain on the other half.

TEI: Are you using any kind of different indicators, aside from IBD, to gauge market cycle when you're trading the weeklies, especially since they are so short term?

PJ: I try to keep it as simple as possible because it's a never-ending abyss with indicators and all kinds of crazy stuff. If you just look at the names out there with candlestick charting - dojis and hanging man and all this stuff. There's six and seven-word descriptions. The hanging man doji upside down, a throat slit day... It's an abyss that you don't want to stare into.

There's also knowing that it's imperfect - there's a little bit of artwork coming into this. That's why I think engineers have the hardest time with this; they're trying to measure every last little thing and the idea is just to determine where the broad stuff is going. Don't forget if you're trading these weekly strategies, your universe shrinks down by a big factor. If there's 150 weekly stock options, that's probably 1 percent of stocks. That sure shortens your window.

TEI: How do you determine which ones you prefer to play, given the universe of weekly options has greatly expanded from a couple years ago?

PJ: My head is in the paper and kind of looking around every day. A good example is Transocean Offshore - they were in the doghouse stock wise, with a lot of uncertainty regarding the Gulf oil spill. You kind of tuck that away - you've read an article here or there and you know the fundamentals. They're one of the winners in the world and have all these untouchable things... and they're not going to go out of business. All of the sudden you see news that a settlement has happened and all this uncertainty gets removed. There's an opportunity there. It's got weekly options. When you hunt down when they're going to announce earnings next and you see that it's two and one-half months off, and they've just got this - not an 800 pound gorilla, but a 3,000 pound car off their shoulders - that's kind of an event or news-type of opportunity. Not to day trade it in my world, but to say, "Wow, look at all the uncertainty that's been removed." It's likely they're going to have some fresh new forecasts they can finally

talk about - maybe that happens on the earnings podium. But whatever is going to happen, right now I can go buy some protective puts out past that earnings date. I can be in business being a weekly put seller, not even touching the stock...just see if we can make some money off of something that's not a situation you or I created. We did not create the explosion that happened and we could have never foreseen all these events, but all of a sudden they're kind of lined up. That's an example that comes to mind. There are companies like Priceline and Apple and Google. What's nice about those is they're not up-and-coming companies that have to prove themselves. You've got Apple that has \$54 billion in revenues every 3 months. I mean, they won...they're a winner. There's not anyone else like them. Consequently, their stock price has got out of control for a lot of small investors. You're talking about a \$400 or \$500 stock - it got up to \$700. Well, one thing I love about structuring these weekly trades is that all stocks like that are in play. You're not shying away from a Google. You're not shying away from a Priceline that's \$700 or \$800 a share. There's still an intense amount of interest about what Apple may or may not report. Coincidentally, it just so happens that as we're talking right now it's about four to five weeks away from their next earnings announcement. And Apple is starting to trade higher on days where the whole market is selling off. It's having some really curious action right now. There are rumors that they might increase the dividends, rumors of a share buyback and rumors of new products. Well, we don't have to know what the earnings are gonna be. We can structure trades with these weeklies right now heading into the earnings announcement and be picking off this weekly income - these weekly premiums.

TEI: So you're always on alert for anything going on with the companies that offer weekly options?

PJ: Absolutely. I'm to the point now where it's easy to know what weeklies are on - Netflix, Amazon, Priceline, Apple or whatever. When I see LinkedIn breaking out, I've looked at the weekly list enough to know, "Hot damn that has weeklies." I'm all over that more than the 99 percent of other companies that don't. They might have something that's worth a look, but if LinkedIn is doing a big break out, that's got my attention for the entire day. Everything else gets blinded off.

TEI: You used to do the pinning strategies a lot with the weeklies. What has happened with those?

PJ: Pinning has had its own evolution in a way that doesn't favor us. When weeklies were newer I cancelled all my plans every Friday because Friday was the pinning day. It was just an absolute treat. I don't know if it is a function of all this volatility, but it's been knocked off its perch. It's not the opportunity it was when they were newer, so I've migrated away.

TEI: So what is your favorite type of strategy with the weeklies now?

PJ: What I'm doing with weeklies now is a strategy I've termed the "money press." Basically it's taking advantage of being a weekly seller of option premiums, but rather than buying a 1-week premium underneath, which would decay as fast as the one on top, you're simply going out and buying an option 2, 3, 4-months out - it just depends on the particular situation. I like to think of it like Baskin Robbins selling a single or double ice cream cone. Say the big 5-gallon tub has a wholesale cost of \$10.00. Well, they dig in and get one little scoop out of there and there's still all this ice cream left, but they're selling that scoop for \$2.00. I think of that ice cream tub as option time - you're buying time in bulk... Take any stock across the spectrum and look out at a 4-month option and then divide it by 16. And then go check what the quote is on a 1-week option. It's drastically different. You never want to buy week-to-week protection, you want to buy that bulk and then you want to become a seller. Just like Baskin Robbins, you want to buy your ice cream in bulk and then you want to sell the singles. That's really what the concept is.

From there it gets to why this stock and why now? There is some set up and you want to be aware of the market cycle in general...there's some artwork there too. Some people just like to shortcut that and say, "Just show me what you're doing," which is what I do on the Weekly Options Windfall membership [program]... If you just take a look at like a dozen stocks and follow their little lives - they're the bigger name stocks. I have money press [trades] going on Netflix, LinkedIn and Apple right now. Your universe of choice really shrinks down. Gone are the days of rifling through 250 new highs for the day. I deal with a very small universe of stocks.

TEI: You just mentioned the change that occurred that negated the opportunity built into the pinning strategy. Do you see or anticipate more of this in the weekly market?

PJ: The amount of people who know about this stuff is so miniscule. I know when portfolio margin got passed by the SEC - it happened in the fall of 2007 - it was nine months until the first brokerage firm actually was able to offer that to clients. They didn't even know what to do with it at first. So I think we're really in the infancy of weekly options. It'll be interesting to see, but I don't think that human nature will change. I know from talking to the Najarian brothers that the volume on these weekly options is outdoing the 1-month options. That just means institutions are in there shoving money around and repositioning options and laying it on, perhaps for the earnings announcements. It just really zoomed into popularity right away, according to the action that they see.

TEI: The good news is they are staying under the radar and the opportunity hasn't been taken away in them.

PJ: Right. Even still, options have been around for close to 40 years in some shape or form. And it's always been the case that the 1-month option had the most activity. If you took that 1-month premium and multiplied it by six months, those premiums added up were way bigger than that 6-month option [premium]. So all we've done is scrunch the time down. When you do the 1-week option and you add up what that 1-week premium is compared to a 3-month out option, where you take 12 of those 1-week premiums, it's actually even more skewed in favor of being the seller of those 1-week options.

TEI: What's your research like? How do you go about doing your research on a daily basis?

PJ: I start early because I have a son that has early morning band - that's 5:30 in the morning. I pick up the paper about an hour before the market opens. I subscribe to Investor's Business Daily. I give that a read through and I check the market cycle in it. I'll look at the new highs list and I look for articles and stories that came over later in the day yesterday, especially if I closed the computer lid early and didn't

see the [market] close. I also love Briefing.com. To be honest, I used to spend a lot longer time doing research because anything and everything was open for opportunity - there could have been opportunity anywhere. Coming back to the scrunched universe of stocks that have weekly options, especially the tippy-top most "Bad A" beasts that roam the jungle, there's only a handful of them. Physically and generally that's what I'm doing in the morning. I open the laptop lid and that's the only screen that I have up. I look at charts from Yahoo Finance...it is not too overbearing. And I never ever have CNBC on during the day.

TEI: You talked last month about trading effectively. What are the one or two things that a trader needs to be doing right now in the market to find success?

PJ: The market cycle is one of those main, effective things. You could have five screens open, the lowest commission rates, the best IQ and health and happiness. But if you're trying to buy stocks in a down market cycle, that's super inefficient...no matter how efficient and happy you are, you're constantly fighting that because of what you think. Well, that's freaking ineffective. A main thing that I'm always looking at in a stock move is its price action and volume. When you boil everything down at the end of the day, that's very effective as well. If LinkedIn has a breakout in the first 30 minutes of the day and it's at an all time high, and volume during that first 30 minutes already surpasses what it trades in a normal day, that's very important to know. You have to stand up and pay attention to things like that.

TEI: Those things can't be faked - they're real.

PJ: Right, there's some far smarter and more numerous people close to the situation of the company than we'll ever be. What does it matter living out here by the Rocky Mountains that you think that LinkedIn is overvalued? You've got to be kidding me. You've got thousands of people with billions of dollars who are keyed into all the little nuances that you'll never ever know. That's probably always been like that.

TEI: Touching on your rules. What's the maximum percentage of your overall bank you'll risk in a trade?

PJ: Take the money press trade. As you buy protection three or four months out and you're selling premium on top of that, you've already defined your risk in a way that's more unconventional than just buying 1,000 shares of an IPO that just came out...no options, there's no margins - you're just buying it and you'd have some stop losses on that stock and you'd have to determine what that is. Another thing it depends on is market cycle and the setup of the stock, where you can go more aggressive in your size - it's not going to be the same exact thing across the board. When I start a trade, it seems like I've got a 5 percent risk for a money-press position as it relates to my entire account. That could be added to if it starts behaving.

TEI: How many positions do you typically have on and how many do you suggest for the average person?

PJ: I'll typically have seven to eight of them on. They're not all dot com type stocks...there will be an oil driller or a yoga apparel maker in there. You end up getting a little diversification, if you want to call it that, from different industries. To me that just seems like a happy medium where it's not brain frying - where you're in 25 different positions. What I suggest to the person starting is don't limit yourself to one - maybe two or three if they can. The best way to learn it is to jump in and do it. Again, you've already carved out what you're risking right from the get go.

TEI: What do you have to say to somebody out there contemplating the Traders Edge trading and training programs in terms of why they should do it and what they should expect?

PJ: People come in with so many different backgrounds and talents and expectations. Maybe they come to the conclusion on their own or because they've heard from a financial planner or a stupid retirement calculator... that you'll need \$1.6 million now to have X amount of money peel off from a bank CD. The paradigm now is that person can have a \$200,000 brokerage account. Just doing some pretty rudimentary stuff on some no-name companies like Intel - you know, real charlatan companies like that or a tobacco producer - doing small things like that, with a dividend spread against margin interest, and then writing weekly premium. This is a paradigm shift where you could have a tenth

of what you thought you needed, according to a financial planner, in order to make the same amount of money as with a big pot of \$1 million to \$2 million. That gets back to the goal for that person. We don't want people to come in the door and have unrealistic expectations. "Hey, I need to be doubling my money every four months. What strategy's best for that?" We want to change people's paradigm, but we also don't want to work with unrealistic expectations. It really depends on the person contemplating this. They really have to sit down and re-evaluate what they've been told their entire life. That can determine where we want to point them and what we want to get them started doing. Maybe they want to adjust and change their dreams and goals upwards because of some things we can do for them. This is still new, to be brutally frank and honest. This way of trading didn't exist just three years ago. We think we've done a good job getting up to speed with it, but we're talking about another type of ballgame compared to what people were doing that had a Schwab account for the last 25 years. Hey, hats off to anyone that has been disciplined and set money aside - we're not talking about that. I have to think we are the only company out there offering this type of game-changing know-how. We're not teaching someone how to be a better traditional trader. I don't even like the term trading anymore. We came up with Master Income Trader and Weekly Options Windfall. We're in a whole different paradigm here. I know that sounds kind of creepy - that's what everybody says... that's the language - it's going to be different this time... You should see the face of someone when they kind of get it a little bit. They walk away going, "Holy crap, I hadn't thought about this, that and the other."

TEI: So it boils down to what's available out there for that individual - the small guy out there. There are opportunities that are created because of the way trading has evolved, because of institutional trading, high-frequency trading, new trading vehicles, the ability to leverage an account with portfolio margin and myriad other factors. In that sense, the training offered is important to individuals in order to understand what the opportunities are and how best to leverage them, correct?

PJ: Absolutely. Look, this is stuff we teach an individual independent investor to do. You'd think that if this is

so good, why aren't all the hedge funds doing it? They can't because they're the ones actually creating all this opportunity now. They have to go put gobs of money and takes positions here and there. Najarian was telling me once that even if a \$3 billion hedge fund had an idea that, "Hey, this stock's moving," they can't buy enough options to go do that. Even if they buy a 1,000 contracts and make a couple bucks on it, that doesn't even pay the light bill. These guys have to put billions of dollars in the market constantly. They're always going to trade a very different way than we can trade as individual people. It's funny, but it's the scenario of the world right now that's created a lot of the opportunity that we get to take advantage of. They're never going to be able to do it - they can't trade like we can.

TEI: Anything else you'd like to offer before we wrap up?

PJ: This will likely require a little courage to look at something and realize, "Hey, this is where the opportunity really is and I've got to change how I've always thought and felt...what I thought was important about making money."

Also, one of the most awesome things for us, because we're all sitting behind computer screens, is hugging our folks as soon as we meet someone for the first time. Part of breaking habits and embracing something that's new like this is getting out from behind that computer. We don't do seminars all the time, but we love for people to just show up at our doorstep and want to chat. If Chef Paula is about making something,

then we'll sit down and break some bread. We just love, love meeting people. It just seems to forge something that's an intangible you can't replace. It helps you break habits - it helps you do things right...I can't say enough about it! It's probably the biggest thrill ever to finally put a face with an email address. To know that someone's out there getting up every morning and doing this is Austin, Texas or New York City or Australia. It's really heartwarming! That's my parting thing - let's meet each other!

Preston James

Preston James is a self-professed "stock market linebacker" who is proud of the notion that the only reason he graduated college was due to his football scholarship. His interest in trading began at a young age, actively trading his own accounts since 1996.

Specializing in cutting-edge strategies, volatile markets and small trading accounts, Preston's passion for trading has attracted a following of like-minded income traders seeking his help in taking their trading to the next level.

Preston is a noted author and speaker in the field of trading and investing, having published "The 1% Solution" and his controversial "Online Trading Manifesto." In spite of high praise from legendary floor trader Jon "Dr. J" Najarian and Tobin Smith of Fox News "Bulls and Bears" fame, Preston insists he is "no one special"... crediting only his passion and pig-headed determination as the reason for his trading success.



Upcoming Events & Special Announcements

Traders Edge Mentoring Program

In our continuing effort to provide comprehensive training for traders, TE recently expanded its mentoring program. You now have the opportunity to train side-by-side with profession traders in either Salt Lake City or St. Louis. This intensive two-day program is designed to deliver actionable instruction focused on helping you understand and apply proven strategies in a real-time trading environment - training that goes well beyond the generalized "book-based curriculums" offered by most other training services. To find out more about the Traders Edge Mentoring Program, be sure to contact us at (801)717-3993.

continued p. 11

Monster's Perspective: Is Apple really a broken stock? Hardly

By Jon "DRJ" Najarian



Our friend and colleague at optionMONSTER, Chris McKhann, just recently asked the rhetorical question, "Is now the right time to buy calls" in an article on **optionMONSTER.com** in which he highlighted the merits of **Apple (AAPL)**. Readers of my **DRJ's Blog** know I have discussed the strength of the business model metrics at Apple in the past (Jan 24).

To hear all the talking heads bemoan the state of **Apple**, you'd think the stock was heading to zero. But let's try a little experiment. Suppose we blacked out the ticker symbol and looked only at the company's metrics:

- Forward P/E minus cash of 7.
- Gross margin of 38 percent or 39 percent this year.
- Revenue growth this year of 17 percent.
- Growing revenues in China at almost 70 percent.

Wouldn't you be buying the stock with both hands? I said back in January that I think we all would. Consider this experiment against the question asked at the beginning, "Is this the right time to buy calls?"

Take a look at these more recent findings.

Call buying is probably the most recommended option strategy. That does not make it the best, and in some respects it is one of the most risky. But there are great times to buy calls, and this is one of them.

The appeal of [call buying](#) is that it is a limited-risk strategy with the potential to produce substantial gains. The leverage is huge, which is why "instant millionaire" hawkers often promote it.

For example, in Apple you could buy an April 440 call with the stock trading right around \$430, ensuring the right to buy 100 shares at \$440. The premium of that call is \$6.30 at the time of this writing, for a total cost of \$630. (Remember that one option represents 100 shares.)

An outright purchase of those 100 shares, meanwhile, would cost \$43,000. So if Apple were to rally up to last week's high around \$470, you would make \$4,000 on the stock for a 9 percent return.

But the calls - if held until expiration - would make \$2,370 (\$47,000-\$44,000-\$630) for a 376 percent return.



AAPL April 4, 2013 (Source: tradeMONSTER.com)



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The problem is that there is only a 36 percent probability that AAPL will be above \$440 at expiration and only a 7 percent probability that it will be above \$470.

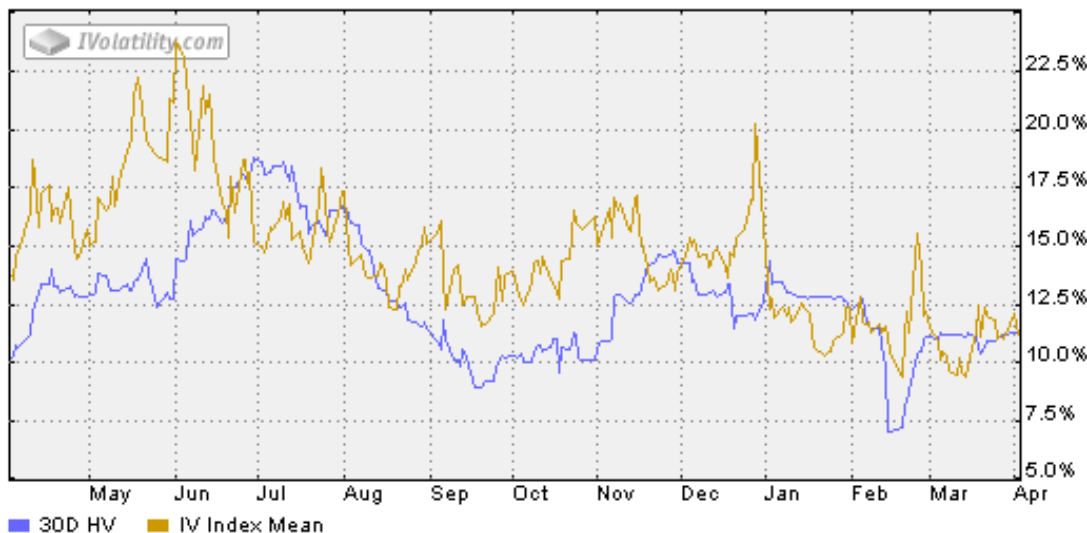
Most call buyers bet too much money on low-probability bets, and this over-leverage is what eats up capital. That is one of the biggest risks of this option strategy.

That said, there are times when buying calls make a lot of sense. The markets are near landmark highs, but volumes are light and some believe that we are poised for a correction. And [volatility](#) is low, which can be seen in a general way in the VIX.

of 9.3 percent and a 30-day historical volatility of 11.3 percent.

The key is to only replace your current exposure, not to leverage up because of the lower cost of the calls. To be clear, I would not add long calls to a long-equity portfolio here; I would replace the stock with the calls. If you had 1,000 shares of the SPY, then I would suggest buying only 10 or 20 SPY calls.

This would allow you to continue to have upside exposure while significantly lowering risk. And you want to buy options when volatility is low, as it is now.



For those of you who can't or don't want to sell your stocks, then buying [at-the-money](#) SPY puts actually gives you the same risk profile.

That [hedges risk](#) while maintaining the upside exposure. Consider it a kind of "inexpensive" insurance that is priceless if we do get a significant drop.

Regards,
Jon "DRJ" Najarian

The volatility matters because it is a key component of the option's price. The higher the expected volatility, the higher the option price, and vice versa. Often in options, that expected volatility is higher than the actual volatility turns out to be, and that is the reason many professional traders use option-selling strategies. This presents the other big risk in option buying; that you are paying more than you should, in volatility terms.

If you are bullish on the overall market, but worried about a potential pullback, then selling stocks and [replacing them](#) with long calls makes a lot of sense. You could buy SPDR S&P 500 Fund (SPY) calls to get that upside exposure, for instance.

The SPY Weekly 157 calls, with 10 days left to trade, cost \$0.52 and have an implied volatility of less than 9 percent. That compares to the current 10-day historical volatility

ask-drj@optionmonster.com

Jon 'DRJ' Najarian is co-founder of optionMONSTER® and co-lead analyst for the InsideOptions™ trade idea alert systems. He spent the first 29 years of his trading career trading in and around the pits of the Chicago exchanges.

"DRJ" is a frequent contributor to CNBC, the Wall Street Journal, as well as other prominent financial media organizations. Mr. Najarian also co-developed the patented trading algorithm the Heat Seeker®, used to detect unusual trading activity.

(Portions of this article appeared in optionMONSTER's [Options Academy](#) newsletter of April 3. Chart courtesy of [iVolatility.com](#).)

Karson's Insight: Why Cyprus is a Real Wakeup Call

By Karson Keith



If you are at all in touch with the macroeconomic picture, you have undoubtedly heard about the insane things happening in Cyprus. For such a small part of the world it sure has made a big splash. It is the Euro's desperate attempt to send a message without letting chaos spread like wildfire. The goal for them is to "contain" it into just this one incident. However, this is not what I want to write about.

Though the problems throughout the world are in very high numbers, we tend to forget that we are not immune to such events like the Cyprus fiasco. I want to make it very clear that something exactly like that could easily happen in the USA.

Those of you who know me well know that I am an optimist, but the current situation is simply impossible to ignore. It is a very complicated set of problems we face, but when you look at it in its most simple terms it breaks down easily. Various companies and branches of the government go to Obama and ask for money, Obama goes to the Fed to "print money" (really just selling bonds to ourselves) and then the money gets distributed with nothing really backing it.

We have been off the gold standard for a very long time, but now it has truly become a "zero gold" standard. In other words, all of the money we are printing is simply just paper. You would think that this would flatten the dollar, but other countries have been wildly printing as well. The "weakening" dollar set aside, we have the same problem as Cyprus. If everyone went to the bank right now and demanded to withdraw their money, the bank simply couldn't do it - it doesn't have it.

The Fed goes to Obama and says we need more money. Obama says okay, let me make a phone call.... the cell phone in the pocket of the guy asking for the money starts to ring.... What happens then? I only hope that this situation never occurs.

The main reason I am writing some of this is simply to make anyone who will listen aware that we are not immune to any of the disastrous scenarios.

While I am waiting for the collapse to happen, the long butterflies have proven to be a great income-generating vehicle.

I hope this finds you well. And please note that I will be first in line to trade the collapse.

Karson Keith

Karson Keith's interest in trading started at a very young age. By age 13, he began trading and managing his father's money. Today, his passion for trading has attracted a following of like-minded income traders seeking his help in taking their trading to the next level.

Karson specializes in cutting-edge options strategies, volatile markets and small trading accounts. He not only has single-handedly grown several small accounts into large portfolio margin accounts within just a few months, but he has also helped countless people achieve the same results.



Upcoming Events & Special Announcements, *cont'd...*

Traders Edge Network Blog

Be sure to check out the Traders Edge Network blog each Thursday afternoon, as TEI Editor Louis Horkan offers a bit of tongue-n-cheek commentary on what's occurring, as well as insight on things you need to be aware of and suggestions on how best to succeed in these markets. Trust us, this isn't the same ol' staid, button-down rehashed news or analysis you're accustomed to running across most places! Join us each week on the Traders Edge website (www.tradersedgenetwork.com) and be sure to leave a comment telling us what you think...

Musings from the Editor: Then and Now...

By Louis Horkan



Good friend of mine recently turned me on to a blog run by an author/blogger/music company vet who prolifically cranks out some good stuff near daily. He weaves a good story laced with perspective, insight, history, opinion, humor, anecdotes, etc. One of my favs from amongst his offerings is his "Then and Now" postings, in which he provides a good take on the changing nature of all things in his business.

Well, our playground is the market, which is synonymous with change each day. As such, I thought I'd throw together a short list of examples of how trading and the markets have changed...both for giggles sake and to get you thinking about where things might head next in this dysfunctionally crazy business in which we participate.

Options

Then - Few knew anything about them and most who did purchased them as a hedge against their equity holdings.

Now - Those of you following Preston or Karson sell contracts to make income...now weekly income... Gone is the day you had to purchase equity shares and tie up huge sums of money and margin to participate in a stock's movement...no reason to do so with options.

Then - Lots of peeps purchased LEAPS of a year to two years on individual stocks, hoping they would go somewhere significant given enough time.

Now - Weekly options were introduced with little fanfare several years back on a small handful of stocks, ETFs and Indices. Now the list of underlying assets with weeklies attached has grown significantly (160 stocks with weeklies presently) and promises to expand much further still. Moreover, volumes are ever increasing and actually surpassing the daily

trade activity associated with many monthly options. Here at TE, one of the major approaches to trading is that of writing contracts using the weeklies to bag income.

Then - Set in stone - options were always tied to 100 shares of the underlying stock.

Now - Minis have just become available in the last couple weeks that are tied to just 10 shares of stock. At this rate, we'll soon be ordering McOptions from the value menu at McDs.

DJIA

Then - The venerable benchmark index of the masses (let's face it - those who trade with any regularity are looking at the S&P, COMPX, Russell, Euro, Dollar, Gold and others such indices to trade off of) tagged the 10K mark for the first time ever in March 1999.

Now - After plunging to a low of 6,469 in 2009 during the midst of the financial meltdown that precipitated the Great Recession, the INDU pulled a V-shaped turn that few trusted and everybody thought would eventually be retested. The bull-run embarked on at that time has now lasted four years...and in the last week culminated with an all-time closing level high for the index just above 14,660.

Futures

Then - Futures were the playground of the institutions exclusively...fund managers used them to hedge, as a trade mechanism for portfolios balancing (especially those with funds tied to key benchmarks, such as the S&P 500) and to engage in short-term directional bets.

Early on in the days of day-trading, traders would watch them closely as a “tell” on when major money-flow surges where occurring, along with major swings in the tick and other such indicators, in an attempt to time entries and exits on individual stock trades...especially those scalping.

Now - Lots of peeps shun stocks and instead trade futures on everything from the major equity indices across the globe to currencies, crude oil, gold, soybeans, treasuries and anything else you can place a financial bet on.

Scalping

Speaking of scalping...

Then - Inside-term bandied about by unscrupulous brokers in regards to their treatment of unsuspecting clients. Churning, front running and other forms of outright fraud were the norm in many firms and taking scalps to secure fat commissions was a routine practice.

Now - Scalping has always been a big part of day-trading...either by choice or because of undisciplined trade management. It's one thing when you're trading many time over for pennies and dimes (tough way to make a living, but it can be done)...quite another indeed when you're trading approach boils down to cutting your winners short and always letting your losers run (guaranteed quick trip out of the business)...

Trading

Then - Your broker called you incessantly with hot tips when you didn't want to hear from him and couldn't be reached when those hot tips turned south and you were desperate to know what to do...

Now - You cuss at your computer screen and “those” peeps out there who always seem to be lurking and whom inevitably know what you're doing, and in turn do everything in their power to head hunt you and rob you of your bank... Tell me you haven't at times felt someone was out there targeting you while you were trading... raining down on your every trade!

Then - Back in the 80s, the challenge was convincing peeps to pull their money out of the banks and CDs to invest in a stock market that most knew little about and feared. It was a big step for an individual to buy into mutual funds, let alone purchasing individual stocks.

Now - No one would trust putting money in a bank (ask the peeps in Cypress how they're feeling about their deposits and the banking system...while you're at it, might wanna ask their thoughts on the Germans and entire EU...or whether they still think membership in the EU has its privileges), one of the most popular ads on TV is centered around a baby talking up investing using a certain online brokerage firm, and you've got cab drivers from here to Dubai trading Forex pairs between fares.

Then - Most peeps got their stock quotes out of the paper, while those living on the cutting edge called their broker (who was unlikely to take the call unless they had something to pitch AND they weren't currently ducking calls because of their latest disastrous suggestions...) to get a delayed quote. The really smart peeps spent their mornings perusing the Wall Street Journal to stay abreast of all things business and investing.

Now - You trade, manage your portfolio and do all your research on your iPhone while simultaneously carrying on 4 or 5 text conversations and playing Words w Friends... and checking to see if your latest posting is trending on Twitter...

Goldman Sachs

Then - GS was the Big Swingin D on the street, pushin everyone around...and the envy of all.

Now - GS is the only real holdover of the “bulge bracket firms” from days of past and now a Bigger Swingin D... one that everyone hates and gets pushed around by... even the little guy... Their executives routinely retire to run (ruin...always get those two messed up) our treasury or act as special advisors to world Governments... We're certainly in good hands with such advice - just ask the Greeks how that turned out for them...

Wall Street Executive

Then - Bernie Madoff helped found and was head of NASDAQ.

Now - Bernie (often "affectionately" now referred to as another "B" word) went from being one of the largest market makers on Wall Street (in addition to his hedge fund business) to making license plates. Putting his executive experience to good use, he's now the president (amongst other positions...doh!) of the Bubba T fan club in Cell Block C.

K, I did take a little license there....there are some good peeps on Wall Street - they're not all Madoffs - they just all make-off with loads of greenbacks at the individual investor's expense... Just say'n...

Merrill Lynch and Lehman Bros

Then - Both were synonymous with Wall Street, investment banking, greed, power and all things trading and investing related.

Now - One is part of a bank and the other was bankrupted and now defunct, having been kicked out to the Street by our beloved Fed...an act many now credit as the singular event that led to the near collapse of Wall Street and the ensuing onset of a financial meltdown from which we still struggle to overcome.

Retirement Strategy

Then - When I was getting into the biz more than a couple decades past (yes, nearing fifty and old as dirt, as my sons often remind...those very same young Micks I house and feed and love unconditionally, who refer to me and all others of this age and beyond as "dults." Hmmm), and certainly ever since that time, every book, broker, advisor, financial billboard, magazine, radio commercial, infomercial, neighbor, bookie, barber, lawn boy and the 11-yr old baby-setter, has preached the same message to the baby boomer population --- start young and get to socking away as much of each paycheck as possible into

an employer-sponsored plan, as well as an IRA for you and the spouse... Good advice all, premised on the notion of creating savings for your retirement years that would gain benefit from the principle of compounding savings and interest, further enhanced by tax-deferral and reduced reportable income each year... Oh, and the jackpot of all benes - gaining access to a market sure to return a minimum of 8 percent on average, with some big-time returns handed out in the occasional year... Yes Mr. and Mrs. Boomer, there is a Santa.....

Now - Would appear Santa took a header...and with him 100s of billions in retirement savings from the dult population that now finds themselves in dire need of the dough. A sign of the times is something I heard this past weekend while spending some time up in Cape Hatteras. While driving, I happened upon a station where the host was goin off on a rant, which caught my attention. I then listened to him go on for some time, preaching to his audience a message that was quite contra to the established financial services/retirement industry party-line. He was telling his listeners to clean out their IRAs and other retirement accounts (including qualified employer sponsored plans), pay the taxes now and buy tangible assets to avoid the government stepping in and taking it all away from you later... Sounds Orwellian, till you consider what's occurring in Europe now...

Trust in Financial Institutions

Then -

Now -

Nuff said...

Microsoft vs. Apple

Then - Microsoft was the bell weather when it came to tech and the Nasdaq. They printed money at a faster clip than our government and their core product (Windows) rivaled oxygen in terms of life's necessities.

Now - Do I really need to spell out how things have changed and whose products now are considered necessities of modern life?

German Engineering

Then - Audis were built to last...and they did so

Now - Don't get me started.....

Sorry, unsure how that last one got in there... nothing to do with the 4500 pound paperweight (6 years old and less than 100k miles...) presently occupying my garage .

Louis Horkan
Editor

Louis entered the biz in the late 80s and spent over a decade working as a trader, instilling him with unique insight into trading and the markets. In 1998 he switched gears to become the group editorial director for a large network of award-winning, trading-focused newsletters. In 2002 he became the founding editor-in-chief for two financial trade magazines—each served approx. 40,000 independent financial advisers nationwide. He's appeared on business TV, in the business press and on numerous biz-focused radio programs in the past. He writes market commentary and analysis most days and trades on a daily basis.



Money Chasing You - Trading Success Stories

After trading the past several years, the most important things I have learned have been from Preston. I use the Accumulation / Distribution charts to know where we are in the market cycle and I have found that the easiest, least stressful and most successful trades are the trades that break out of bases and reach 52 week highs on convincing volume. Those setups of course are pre-announcements and 52 week highs. I have learned how to use the IBD to my advantage, finding trades and managing them.

To make a long story short, I believe I have found a system that I am going to stick with for my longer term trades and don't need to search anymore for other strategies. Preston has taught me so much that I use on a daily basis.

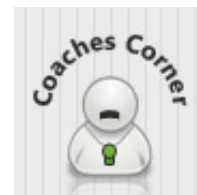
Thanks

M.E., North Carolina

continued p. 17

Coaches Corner: Understanding Implied Volatility

By Beau Keenan



For this month's article in the coaching corner, I'd like to address a basic understanding of implied volatility. Implied Volatility, often referred to as IV, is an integral part of options trading - it's at the heart and soul of many traders' trading repertoire. Implied volatility ranks as one of the most important price determinants of a stock's options, second to only the price of the stock itself.

According to one online dictionary source, volatility is defined as "tending to vary often or widely, as in price." As traders, we're technically always trying to anticipate how much a stock might or might not vary in price. Thus, implied volatility is derived as the study of "how much" or "how little" expectation is being placed upon that potential movement of a stock by current price data.

To put it in layman terms, Implied Volatility estimates a stock's possible movement potential, either up or down. The higher the Implied Volatility, the more the

stock is expected to move, driving up the extrinsic value and price of the options due to a greater possibility that it will end up moving in your favor. The inverse is also true; the lower the Implied volatility, the more stagnant the stock is expected to be, which drives down the extrinsic value and price of the options.

Understanding the direct correlation of IV to option pricing is crucial as well. First, if you're an option seller like Preston, you need to ask yourself, "Do I want to be selling my options when IV is high or when IV is low?" It's kind of a trick question depending on the time frame you are doing your trade. For a one-time quick-sell of juiced up IV, the answer would be when IV is peaking. However, the majority of Preston's trades are swing trades that last numerous weeks, with short-term sold legs positioned against long-term protection. Thus, we would rather sell our options when IV is ramping up in the future, not falling. Selling your options while the IV is declining can be harmful on future premium expectations and the decay of your longer-term bought option premium.

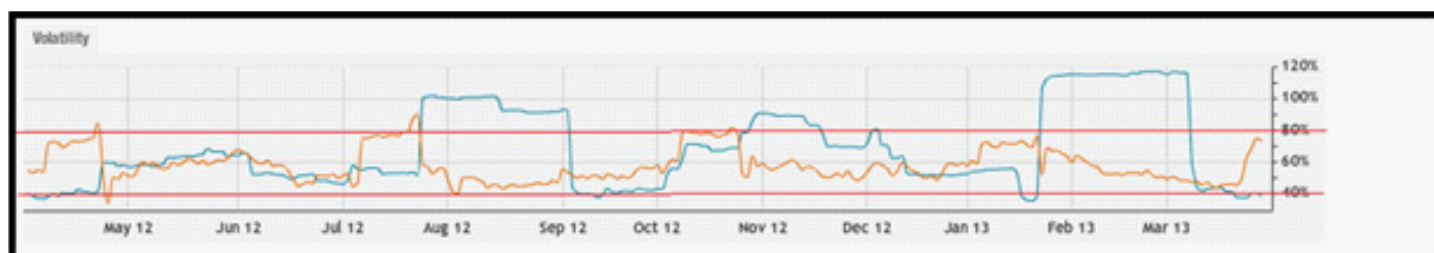
Coaching clients always want to know how they can measure the underlying asset's implied volatility to know that they're timing the rise or fall of IV appropriately. There's a study most trading platforms offer (generally found within their indicator list) demonstrating the measure of implied volatility on a graph for the underlying asset. I've included a picture of one of these graphs below from Trade Monster, conveying a 12-month volatility chart for NFLX. The orange line represents the implied volatility in this graph and the blue line represents historical volatility, which is not nearly as important in the pricing of options.

TOP 50 REASONS WHY FUTURES TRADERS LOSE MONEY

REASON NUMBER 43: Often, traders jump into a market based on a story in the morning paper; the market many times has already discounted the information.

Find Out More

ZANER



You can gather from this picture that the IV line has created some support and resistance levels (represented by the thin red horizontal lines) over the past 12 months. The support and resistance correspond with 80 percent IV and 40 percent IV, respectively - providing the stock's common IV range. Thus, we can say that if the stock's IV is near 80 percent, its implied volatility is high or peaking. Inversely, if the stock's IV is near 40 percent, its implied volatility is low or bottoming out.

Keep in mind that every stock's implied volatility is unique, so what might be low for one stock could very well be high for another. I personally like to break the graph up into thirds. When the stock's implied volatility is in the bottom third of the IV range, I know I'm not getting into a position where my options are overpriced if I happen to be buying options or setting up a money-press trade.

Hopefully you now have a better understanding of implied volatility and will find use for it in your future

trading. Further discussions of how to use implied volatility in your trading, and how it correlates to the option Greek known as Vega, can be future topics to explore in this very extensive options topic.

Beau Keenan

Beau Keenan has been an active trader for six years. He graduated from BYU's Marriott School of Business with a degree in corporate finance, but found his passion in trading. During that time he's traveled the country coaching individuals on the markets and how to trade equities, options, futures and foreign currencies. He enjoys teaching and since joining the Traders Edge Network has personally worked with hundreds of individuals. Beau is a husband and father of two young children. He enjoys the freedom he has to do lots of other activities, from traveling to building businesses.



Money Chasing You - Trading Success Stories, *cont'd...*

Karson & Jeff,

First, I can't say enough good things about the training that you are providing on Thursday mornings.

Secondly, I really liked the format that you presented the long and short butterfly trades. Mentioned was:

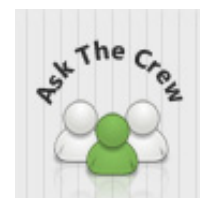
1. Why and WHEN do you want to do this trade?
2. What are your risks?
3. When do you want to do this trade?
4. What can hurt you in terms of your position?

As a new trader with a small account, I need to be careful with what I am doing. I need to avoid large losses or a bunch of little ones that pile up over time. Your training is extremely helpful in that regard.

Thanks for all that you do.

L.B., Iowa

Ask the Crew: Crew members tackle questions submitted by readers each month



Q: Which symbol do you use to trade the Emini's? \$SPX or SPY? Why do you pick the one you do?

A: ESU12 is emini. SPX and SPY are just the S&P. They all move together.

Q: I'm still a little confused on what it is you're trading on the Emini's and what to trade them on. Are you trading options on the Emini futures or just the contracts themselves? And are you just doing them on a site like TradeMonster or a different kind of company?

A: We use the actual contract. We don't trade the options. But you can do it either way. I use Tradestation for my primary account to trade the emini's.

Q: Have you ever been exercised on a Butterfly position (or a straddle or a strangle)? What's to prevent one of the legs from "getting you" that way?

A: It will usually happen when almost all of the time decay is out of the option. This typically happens when you are close to expiration.

Q: I am new to trading butterflies and found that the bid and ask spread is often 50 cents or more. So when I try to place an order to open or close a position these amounts bounce around but the "mark" is usually somewhere in the middle. Yet when I tried to close a position today on the AMZN short butterfly, I found that even though I put in to buy back the butterfly at about 1.45, the mark bounced around and even briefly below that limit price, yet it still did not fill (it did this several times)... Is this common? How close to the bid and ask price do you have to set your limit price to get filled? Why does the order not fill sometimes when the "mark" price is hit or better than your limit price?

A: I usually take the mark price and go just slightly worse. Most of the time it will take several minutes to fill. This is normal. Also keep in mind the mark price is only the middle of the three legs; it doesn't necessarily mean that is what is being traded at the time. Sometimes it gets filled instantly and I immediately start kicking myself because that means I could have gotten a better price.

Our goal is to cover ground that will benefit the entire community... so get busy sending in those questions...



Money Chasing You - Trading Success Stories

Experienced recent trading success or have a lifestyle success story as a result of your trading?

We would love to hear it!

Please email them to: alicia@tradersedgenetwork.com

Comments, Questions, Contact Us

Hey Gang, when we say we value your presence in the Traders Edge Network, we really mean it! It's not really a network, or for that matter much fun, without each of you participating... Please don't hesitate to send us your thoughts, comments, suggestions, criticisms or questions. PJ

SEND EMAIL