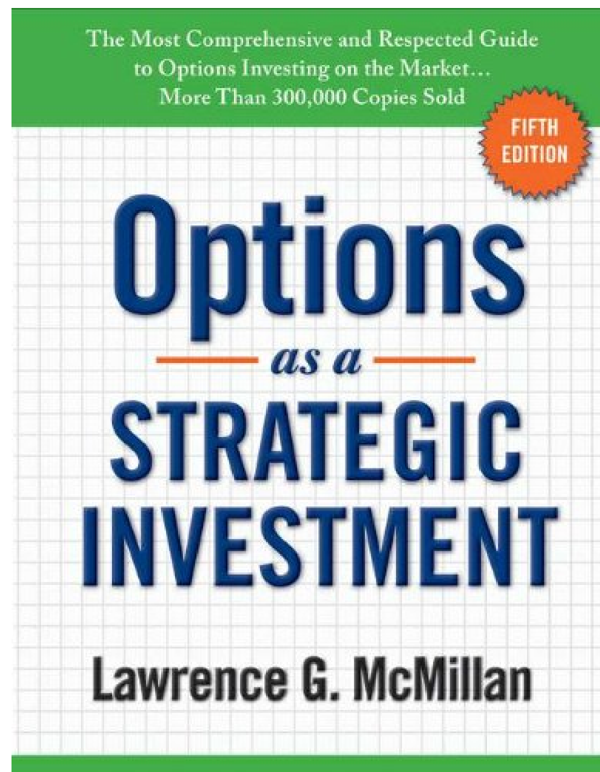
OPTIONS AS A STRATEGIC INVESTMENT BY LAWRENCE G. MCMILLAN



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The market in listed options and non-equity option products provides investors and traders with a wealth of new, strategic opportunities for managing their investments. This updated and revised Fifth Edition of the bestselling Options as a Strategic Investment gives you the latest market-tested tools for improving the earnings potential of your portfolio while reducing downside risk—no matter how the market is performing.

Inside this revised edition are scores of proven techniques and business-tested tactics for investing in many of the innovative new options products available. You will find:

•Buy and sell strategies for Long Term Equity Anticipation Securities (LEAPS)
•A thorough analysis of neutral trading, how it works, and various ways it can improve readers' overall profit picture
•Detailed guidance for investing in Preferred Equity Redemption Cumulative Stocks (PERCS) and how to hedge them with common and regular options
•An extensive overview of futures and futures options

Written especially for investors who have some familiarity with the option market, this comprehensive reference also shows you the concepts and applications of various option strategies -- how they work, in which situations, and why; techniques for using index options and futures to protect one's portfolio and improve one's return; and the implications of the tax laws for option writers, including allowable long-term gains and losses. Detailed examples, exhibits, and checklists show you the power of each strategy under carefully described market conditions.

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- Binding: Hardcover
- 1072 pages

Most helpful customer reviews

143 of 147 people found the following review helpful.
This is THE book.
By The Honest Conn Man
Try as I might, I cannot understand the negative reviews here. This is THE book on options. McMillan writes clearly and well. There is nothing glib here -- no promises of great wealth, no hype, no pandering to fools. What is here is solid information presented well and thoroughly.
A criticism that came up more than once (copy cat reviews?) is that the book doesn't show practical stuff.

What! It provides all the information that any reasonably intelligent person needs to UNDERSTAND exactly what the strategies are and when to apply them. To ask for more is to ask for easy and oversimplified answers that will part you from your money.
The book is thick. True. You don't need all that is in it. True. The book is frightening or dull or not as useful as (gimme a break!) Wade Cook!!!
Hey! It's a text book, not a novel. Wake up! You can use it to find what YOU want to know.
There is more useful information in this book than in any hustler's high-priced and hype-filled seminar. It's all you need and it's currently selling for less $. Don't get scared off by the negative reviews or you'll miss out on the most respected and best of all the many books written on options.
If you're not willing to spend $ and a little effort to learn about options, you're not likely to profit from them. Buy the book. Then, sit down and read in it to find the definitive answers to your option questions. It simply doesn't get any more accurate, any clearer, or any better.
(Oh yes, one or two reviewers suggested that the book is out of date.

75 of 76 people found the following review helpful.
The Best Reference Book on Options
By A Customer
I won't say I've read every book on Options out there, but I've looked at a range, from the very complex, full of calculus equations and whatnot, to the very simple, and to my mind, this is the best. First of all, it is very thorough and well organized. It goes step by step through virtually every option strategy, analyzing the various payoffs, follow-up actions if the market goes against you, etc. It is written clearly and concisely, with lots of examples. One reviewer says it's too complicated. If you think this book is too complicated, then you simply should not be trading options. Period. Another critic says there are too many examples. Yes, there are a lot of examples, and if you find you understand the concepts the author describes just fine without the example, then you'll probably just skip them. However, if there is something you don't quite get, the examples are a real help. I think some reviewers were hoping for a book that would tell them how to get rich in a few months trading options. Well, good luck, and let me know when you find it. But for a terrific reference that every serious amateur will go back to time and again, then this book should be the first on your Options bookshelf.

170 of 180 people found the following review helpful.
A four-star book but a three-star update.
By Chris G. Pflum
Several years ago my broker recommended the 4th (2002) edition of this book. I liked it so much that I bought two of McMillan's subsequent publications: McMillan on Options, Second Edition (Wiley Trading) (cited as McMillan, 2004) and Options for Volatile Markets: Managing Volatility and Protecting Against Catastrophic Risk (Bloomberg Financial) (cited as McMillan, 2011). I've learned much from McMillan's books and have given them four-star reviews; however, I am a bit disappointed in the updates to this 5th edition.

Having read the 4th edition and two subsequent publications, I did not find any significantly new material in this 5th edition. About 85% of the book repeats information in the 4th and possibly earlier editions. The new material includes a chapter on mathematical applications (pages 447 - 477) and an expanded discussion of volatility (pages 767 - 947). The mathematical applications give a good overview of an option's theoretical value. If you want to learn how to calculate theoretical values, however, you should also read Options, Futures, and Other Derivatives (4th Edition) (Hull, 2011).

Although new to this book, much of the information on volatility was previously published in McMillan 2004 (pages 241-568) and McMillan 2011 (pages 171 - 204). For example, Figures 41-2 (p 872) and 41-3 (p 878) in this book are identical to Figures 9.1 and 9.9 in McMillan 2011. Also, much of the volatility - related

text and several of the tables in this book are similar to those in McMillan 2004 and 2011. While one might criticize McMillan for repackaging the same material in different books, on the positive side: If you buy this book, you do not need to buy the other two.

I am disappointed that this 5th edition still uses hypothetical examples, rather than actual trades. While hypothetical examples are useful in explaining how to construct a position or to illustrate a position's sensitivity to individual variables (i.e., the Greeks: delta, gamma, vega and theta), they often do not give one a practical sense of whether the trade would be profitable or even feasible. Moreover, the hypothetical examples are mathematically rigged to give simple outcomes that do not occur in real trades.

Throughout the book McMillan advises his readers to construct option positions that are insensitive or "delta-neutral" to changes in the price of the underlying stock (e.g. Chapters 6, 11, 12 and 13). In his example of a neutral calendar spread (page 215) he buys 7 April 45 calls and sells 8 July 45 calls. The ratio of calls bought to calls sold was calculated from an unrealistic delta ratio of .7/.8. Actual delta values are expressed to at least four decimal places. A neutral position based on deltas rounded to the nearest tenth would be far from neutral.

Chapter 40 explains how to create a position that is neutral with respect to both gamma and delta and would profit at a specific rate (vega) if implied volatility increases or decreases (pages 835 - 836). Theoretically, such a position would be insensitive to changes in the stock's price but would profit with changes in implied volatility (IV). The example trade sells volatility; i.e. it would profit by $238.00 for every 1% drop in IV. To construct such a position for the hypothetical "XYZ" stock, one must buy 100 April 50 calls, sell 173 April 60 calls and short 1,759 shares of XYZ stock. In my opinion, this is an extremely large position just for the sake of making a profit when implied volatility drops.

I constructed two delta / gamma neutral spreads in a simulated account using the same math and methods that McMillan used in his example. One spread on Apple Computer (AAPL) would profit if implied volatility drops, and another spread on General Electric (GE) would profit if implied volatility rises. Unlike McMillan's example, the only way I could come close to achieving a delta / gamma neutral position was to specify a more modest return from vega e.g. -100.00 < position vega < 100.00. The position vega in McMillan's example is 278.00. Like McMillan's example, these were extraordinarily large positions; so large that the 500,000.00 cash balance in my simulated account did not provide sufficient margin to execute either trade. If anyone wants to see the specifics of these simulated trades, leave a comment or send me an email.

McMillan 2004 (page 505) includes a similar example of a huge position (555 contracts) that is delta/gamma neutral with limited vega risk. Later (page 516) McMillan concedes that this is a "theoretical example", but in this book, McMillan appears to be advising his readers to actually make these large trades. I wonder who he had in mind? Perhaps the London Whale made these types of trades until Jamie Dimon fired him.

The book exaggerates the potential profits and low cost of adding a collar to a long stock position. According to Table 17-3 (page 264), a collar made by the sale of 2 ½ year out-of-the-money (OTM) calls and the purchase of 2 ½ year at-the-money (ATM) puts allows a 30% - 70% profit with a small risk. The text states, "Thus one should consider using 2.5 year LEAPS options when he establishes a collar because the striking price of OTM calls (that are sold) can cover the costs of ATM puts." I checked the price of adding a 2 ½ year collar to NKE, IBM, JPM and AAPL and found that the sale of any OTM call would not cover the cost of an ATM put. To break even, one would have to sell at least two calls for every put purchased. Note that in "Options for Volatile Markets" (McMillan 2011) McMillan recommends a different collar strategy: buy six-month puts and sell one month calls with strike prices approximately 2% OTM (page 149).

I stumbled on a few errors that while insignificant, should not exist after six editions:

* The text states, "Figure 37-8 shows just two cases - implied volatility of 30% and implied volatility of 80%." (page 731) The two curves in Figure 37-8 are both labeled IV = 30%.

* The short "240 January 70 calls" (p 841) should have a negative delta, gamma and vega, and a positive theta.

* The text states, "Since 1986, long-term and short-term capital gains rates have been equal." (page 953). As long as I can remember, tax rates on long-term capital gains has been lower than on short-term. For tax year 2013 the maximum long-term rate is 15% and the maximum short-term rate is 35%.

This long review focuses on a very small portion of this very long book. Generally, this is a good book and it is reasonably-priced. Just keep in mind that the book is not perfect and contains information that was previously published.

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