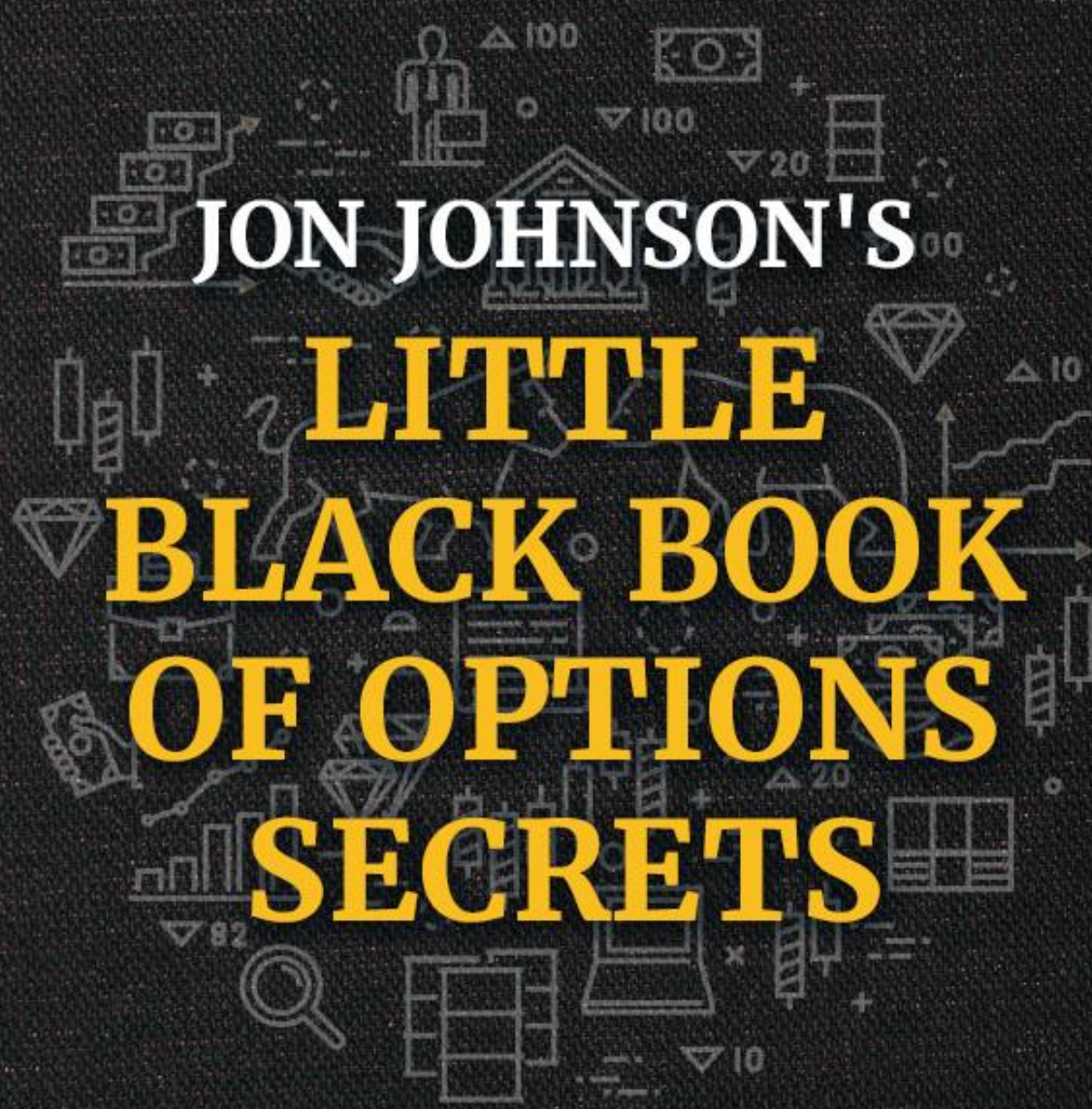




INVESTMENT
HOUSE
SPECIAL REPORT



JON JOHNSON'S
LITTLE
BLACK BOOK
OF OPTIONS
SECRETS

IMPORTANT NOTE: This special report is for information and educational purposes only, based on data as of 2023. Do not buy or sell any investments until you have read a current *Investment House Daily* alert or email update. Therefore, do not buy or sell any investments until you have read the current hotline of *Investment House Daily*, or an email update from Jon Johnson.

Little Black Book of Options Secrets

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The Little Black Book of Options Secrets

First, let me congratulate you on your desire to learn more about one of the most powerful investment vehicles in the markets. Second, I would like to welcome you to the wonderful world of options trading.

Ever hear of the formula RISK=REWARD? Well, that comes into play when you think of options. Options offer a way to earn large profits, but they also come with increased risk, compared to traditional stock investing.

Indeed, the buying and selling of options can be used to turbo-charge your portfolio by earning tremendous profits.

How Do Options Work?

By definition, options are a contract giving the buyer the right, but not the obligation, to buy or sell an underlying asset (such as a stock) at a specific price on or before a certain date. An option, just like a stock or bond, is a security. It is also a binding contract with strictly defined terms and properties.

Buying an options contract gives you control of a “block” of 100 shares of a particular stock. An option also grants you the right, but not the obligation, to purchase the related shares in that stock at a pre-determined price within a certain period of time. This period of time concludes with an expiration date. I typically like to buy call options that have a life cycle of at least several months in order to allow enough time for the call options to rise in value sufficiently to sell at a nice profit before they expire.

What is the benefit to buying an option instead of just buying the stock outright? Well, for one, options tend to be far cheaper than their related stocks. As a result, you can buy options with comparatively little investment capital to leverage your money in search of heightened profits. And, your investment risk is fully disclosed up front. You can never lose more than you spend on an options contract. However, the profit potential with options is virtually limitless. Even a tiny move in the underlying stock can yield a tremendous jump in the value of an option.

Generally speaking, there are two types of options – calls and puts. You buy a call option when you think the price of a stock is destined to go up. And, you buy a put option if you think the price of a stock will go down.

Both are equally powerful and profitable, given the right set of circumstances. But since my services almost exclusively use calls, and not puts, I'll focus this special report on them.

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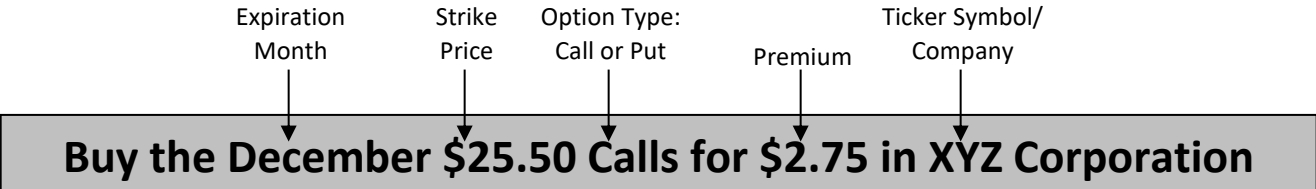
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What Does an Option Recommendation Look Like?

An option is defined by five main components:

- 1. The ticker symbol
- 2. The expiration month
- 3. The strike price
- 4. Whether it's a call or a put
- 5. The premium paid to buy the option



So, an option recommendation might look something like this: **Buy the December \$25.50 Calls for \$2.75 in XYZ Corporation.**

This is a completely theoretical recommendation. But let's examine what each component means and how it would impact your investment if this was an actual recommendation.

A **ticker symbol** is quite simply a short-hand description, featuring a unique combination of letters, to help investors identify a specific publicly traded company.

The **expiration month** is just what you would expect. It indicates the month in which an option expires. If the month when the option becomes invalid (or expires) is reported without including a particular year, you can assume that the option expires in the current year. All stock options end their useful life on the Saturday after the third Friday of their expiration month. I'll provide further explanation about expiration dates elsewhere in this report.

The **strike price** of an option is the price that signifies the investment is “in the money” and able to help you turn a profit. I watch for the stock price of a related option to rise to and especially above its strike price. When a given stock rises well beyond the strike price in a call option, the investor can sell the option at a handsome profit. I will alert you to such opportunities through my trading services.

For example, if company XYZ traded at \$20 a share, but I think there’s a good chance the stock price will reach *at least* \$25.50 per share by the Saturday after the third Friday in October when the related option expires, I might recommend that you buy call options in the stock that have a strike price of \$25.50. Of course, I’ll want the stock price to soar above the strike price to enhance the value of the call options. As the related stock price jumps, so does the value of the options.

As I previously stated, I almost always recommend call options, rather than put options. Call options are bullish investments that are aimed at achieving heightened gains if the price of the underlying stock increases (which is why I recommend the stock in the first place).

Finally, I want you to understand that the **premium** is the price that you pay to buy an option. The price of an option typically is written in as a “per-share” value. In the case of our example, featuring the hypothetical company XYZ, each contract that you buy applies to 100 shares. So, if the price of the option is listed as \$2.75 then your total premium – or the price you pay for the right but not the obligation to exercise the option – would be \$275 per contract. You always pay the premium on an option regardless of whether the underlying stock rises or falls.

So, let’s recap the basic terms that we’ve just covered.

Let’s say company XYZ Company has been trading steadily around the \$20 mark. But my research and indicators lead me to project that XYZ Company was about to sign a huge deal or launch a breakthrough new product before December. Based on this information I am ready to recommend the stock and the coordinate December call options with a strike price that I feel the company is likely to reach. With this information in hand, I might issue a recommendation to buy XYZ Company December \$25.50 Calls for \$2.75.

At this point, you would need to tell your broker the information that you would receive in your alert to place your order. You would tell your broker in plain English that you want to purchase the XYZ Company December \$25.50 Calls for \$2.75 and indicate how many contracts that you would like to purchase. Then you would follow the stock's price and the options to wait for the rise.

Understanding How Options Work

As I already mentioned, each options contract grants you control of 100 shares of a particular stock. And the price you pay for an option is called the **premium**. The **premium** is determined by a combination of two factors: an option's **intrinsic** and **extrinsic value**.

The **intrinsic value** is based directly upon the price of the underlying stock. An option can be **in the money**, **out of the money** or **at the money**.

I typically recommend low-priced call options that are **out of the money** to maximize your potential return. The reason for this is that you want the stock price to be below the **strike price** when you buy into the call option and then you want it to rise above the **strike price** so that it is **in the money** and you can collect your profits.

The further **out of the money** your call option is, the cheaper the premium will be that you pay to buy it. But a key goal is to buy an option inexpensively, while it's **out of the money**, and have it move into the money within our forecasted time frame before expiration. As I explained in my introduction, this approach is the one that I use.

When the stock price matches the **strike price**, the option is considered at the money. If the **strike price** is below the current share price, the option is **in the money** and an investor will need to pay a heightened premium to buy it. However, when you are looking to buy any particular option play, you would want to purchase an **out of the money** option.

Ultimately, the goal is for the stock price to rise well above a **strike price** so that the related call options will climb in value. So after you have purchased the options, you want them to rise to become **in the money**, so that you can make money on the investment.

The **extrinsic value** is a much bigger variable in an option's premium. A complex formula is used to determine the **extrinsic value** of an option. That formula includes the expiration date and the perceived volatility of the option. Volatility generates value in an option.

Consider the hypothetical XYZ Company, once again. In our example, I predicted that the stock price would go from \$20 a share to top \$25.50 by December of this year. Assuming that we bought the option in October, only two months exist for those shares to exceed \$25.50 – an increase of more than 27.5%. Since the chances of a move in that direction might seem unlikely in such a short period of time, the price of the premium that would be required to pay for the options most likely would be low.

If I predicted that the share price wouldn't top \$25.50 until the following December, an additional 12 months away, the likelihood of the stock reaching the strike price would be much greater.

Therefore, the premium required to buy it almost certainly would be higher.

Of course, volatility is another factor that affects the price of an option. Let's say the share price of XYZ was \$10 in August, \$15 in September and \$20 in October. It seems far more likely to hit \$25.50 in the next two months... raising the premium of the option.

Supply and demand also are factors. As the share price gets closer to our strike price, more people will want to buy that option – driving up its price even further.

How Do We Make Money with Options?

Now that you have a general understanding of what options are and how they work, I want to explain how you can trade them in pursuit of tremendous profits. That is why you're reading this report, right?

And, you'll be happy to know there are several ways we can use options to make money... a lot of money. The "traditional" way to make money in the stock market is to simply buy a stock at a low price and sell at a higher one.

Let's look at company XYZ one more time. If you bought 100 shares, at \$20 per share, in October and the stock reached \$30 per share in December, you might opt to lock in the gain by selling. The simple math shows that you notched a 50%

profit. In other words, 100 shares would have cost you \$2,000, without factoring in the commission for the trade. When the stock jumped to \$30, your 1000 shares are now worth \$3,000 – a \$1,000 profit, before subtracting the commission for the trade. Not bad for two months’ “work.”

However, let me now explain a way that we can make a lot more money by investing in options. I have used this method successfully to help my readers land profits of 333%, 330%, and 304% with comparatively small movements in the underlying stock price.

You see, an option grants you the right but not the obligation to buy the underlying stock. Selling the option contract itself can be highly profitable!

For example, let’s say on May 20, I recommended that traders buy LLY (Eli Lilly and Company) October \$62.50 calls for \$1.50, or \$150 per contract.

At the time, Eli Lilly’s stock was trading for \$58.64 per share, but I felt confident that it would top \$62.50 on or before October of that year.

If you’d simply bought the stock at \$58.64, and sold it about five months later on October 14 for \$63, you’d have made an **7.4% profit** (calculated by dividing the gain of $\$63 - \$58.64 = \$4.36$ over the initial investment of $\$58.64$ -- $\$4.36/\$58.64 = 7.4\%$). And that is a decent return. But I helped my readers earn far higher profits with my recommendation of the call options. Indeed, the readers who followed my advice saw the value of their options contracts soar. On September 9, the stock price had risen to \$64 and I advised that my subscribers sell half of their contracts for \$2.78 to net an impressive **85% profit**, (gain is $\$278 - \$150 = \$128$; $\$128/\$150 = 85\%$ gain).

But wait. Just 13 days after that, on September 22, when the stock price was only \$63 (an **8%** increase), I suggested that they sell the other half for \$3.53. Readers who followed my advice to the letter stood to make a 135% profit with that trade. That equates to 110% average gains on the options trade with only an 8% increase in the stock price. Now that’s leverage for you!



Let's look at another real-life example.

On November 2, let's say I recommended buying RAI (Reynolds American Inc.) February \$55 calls for \$.30, or \$30 per contract. The stock was trading for \$48.39 then. But I projected that it would be on a steady rise and I felt confident that we might see the price top \$55 by February... So I recommended those options.

In a little more than one month, the price jumped and our options leapt from \$.30 to \$1.25. So we'd sell half of the options for a whopping 317% gain. Meanwhile, the underlying stock went up just 7% to \$51.95, but that was enough to push our options way up by 317%.

Still, that was only half of our options play. We'd go on to sell another quarter on December 14, for 433% and the final quarter for 150% on January 11, the following year. We were able to average **300% profits** on this play in less than three months' time (calculated by $[317\%+433\%+150\%]/3=300\%$).

A Tip About Options Trading:

Please remember that options trading is not for everyone. If you are a beginner investor, you should not be trading options.

Only experienced investors should trade options. Please consult your broker for more information on how to trade options and any requirements they may have to



See how powerful investing with options can be?

Even if I was wrong, the most anyone could have lost from buying the RAI call options was \$30 per contract – or their original investment.

But it gets better still.

And best of all, you can buy options as easily as you can buy stocks. You don't need a special account or broker. Just a few clicks of the mouse to trade in an online account or a five-minute call to your broker is all it takes to make an options trade. Of course, your brokerage may require you to fill out a consent form to ensure you understand that options will put your money at risk.

Then all you have to do is sit back, relax, wait for my sell recommendation and rake in staggering profits! Keep in mind that a small number of big winners can compensate for a larger number of modest losers. My time-tested success formula involves buying options cheaply enough to ensure that the big winners that I recommend more than offset any losing positions.

I'll be right by your side, walking you through them, telling you exactly what to do for each trade.

An Alternative to Consider – Exercising Your Options

An alternative way to try to make money with an option is to “exercise” it. My preferred method is to sell the option at a profit before it expires but I will explain what happens when you exercise an option, in case you ever decide to do so.

Once again, let’s consider the hypothetical XYZ Company. If you purchase one (1) contract of the XYZ December \$25.50 call option at a \$2.00 premium, you will pay \$200.00 per contract. As I explained earlier in this report, that means you have a contract that grants you the right to buy 100 XYZ shares at the price of \$25.50, any time before the Saturday following the third Friday in December.

If the price of the stock climbed to \$30.00 per share and you chose to exercise your stock option, you could buy 100 shares of XYZ Company for a total of \$2,550.00 and sell them immediately for \$3,000.00. So, that \$200.00 investment would have become \$450.00 ($\$3,000.00 - \$2,550.00$), before subtracting the \$200 price of the contract. Once the \$200 price of the contract is subtracted, the return is \$250.

That’s a gain of 125% ($(\$450 - \$200) / \$200$)! And you never had more than \$200.00 at stake.

In other words, if the Saturday after the third Friday in December had rolled around and the stock had dropped by 50% instead of being above the strike price, the options would have expired worthless and you’d be out \$275 (the call premium). However, had you bought the underlying stock for \$2,000 and it dropped by 50%, you’d be out \$1,000!

Conclusion

Options trades will be an important part of your subscription. Knowing how to trade them, and how easily they can be used to make money – big money – will soon become one of your favorite benefits of this service. I’m sure of it!

Glossary

- **At the Money** — The price of the underlying stock is equal to the strike price of the options contract.
- **Exercise** — For options, this term means you chose to buy a given stock at the price outlined in the options contract.
- **Expiration month** — The month during which your option will expire unless you exercise the contract or choose to sell it beforehand. All stock options expire on the Saturday after the third Friday of their expiration month.
- **Extrinsic value** — This is the value assigned to the premium of an options contract, based on the expiration date and the perceived volatility of the underlying stock price. It is combined with the intrinsic value to determine the total premium of an options contract.
- **In the Money** — The price of the underlying stock is above the strike price of the options contract.
- **Intrinsic value** — The value assigned to the premium of an options contract in proportion to the underlying stock price. It is combined with the extrinsic value to determine the total premium of a contract.
- **Option** — A contract that grants you the right but not the obligation to purchase 100 shares of an underlying stock at a predetermined price, within a certain time frame.
- **Out of the Money** — This occurs when the underlying stock price is below the strike price of the option. We tend to buy options that are out-of-the-money in hopes that they move in-the-money before the options contract expires.
- **Premium** — The price of each options contract. It usually is expressed in terms of a per-share dollar amount. Since each contract controls 100 shares, a premium of \$.50 would actually cost \$50.
- **Strike price** — The price at which a call option is at the money.

Biography



Jon Johnson is the editor of *Investment House Daily*, *Technical Traders Alert* and *Success Trading Group*. Jon has been a guest on CNBC-TV, Bloomberg TV, Houston's 650 Business Radio and his newsletters have been featured in various financial articles, including articles in the *Washington Post*, *Chicago Sun*, *The Wall Street Journal's Smart Money Magazine*, *Bloomberg*, *Kiplinger Personal Finance Magazine*, *Houston Chronicle*, *Business Week*, *Money Magazine* and other news magazines. He was even featured in Forbes.com's Best of The Web online edition.

Jon holds Business and Law degrees from the University of Texas at Austin and has practiced in commercial litigation and oil and gas law, arguing before the Texas Supreme Court and the US Fifth District Court of Appeals.

During his law career Jon became very interested in investing and entrepreneurship as he worked with many dynamic clients. He became an investor in several small businesses and today owns and helps operate private companies. Jon educated himself in investing and trading, reading everything he could find on markets. From that he developed his own trading and investing style. It became so successful his brokers asked if they could follow his trades themselves and with their clients. That soon morphed into him providing investing and education services to clients and then offering his insights through Investment House.

For the past 21 years, Jon has helped thousands of clients gain success in the financial markets through his newsletters and education services. His philosophy in investing and trading is to take what the market gives you regardless if that is to the upside or downside. The goal, of course, is to make money... which leads to his definition of success: doing what you want to do when you want to do it.