

## Twitter Thread by Nikita Poojary



**Nikita Poojary**

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**Few weeks ago @Ronak\_Unadkat Sir conducted an exclusive session for me & @adityatodmal to explain how he trades.**

**He was kind enough to share all his trade strategies and was patient enough to answer our doubts.**

**Thought of making a ■ for the benefit of the larger audience here.**

@Ronak\_Unadkat Sir's Option Selling Logic ■:

- Reversals in Intraday Option selling
- Strike Selection & SL
- Hedging for any Black Swan Event
- Positional Option selling
- Ratio Spreads
- How to manage the positions
- Capital mgmt

In collaboration with @AdityaTodmal



# Ronak Unadkat's

## Option Selling Theory

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Nov 13, 2021

### How to play reversals

- Always look at the chart as a starting point
- Spot the Swing low
- Sell Strikes 300-400 points below that swing low
- Buy a proper hedge

## How to play reversals in Intraday

- The starting point is always the chart & mark the Support/Resistance
- From the point where the market turns around, keep that swing low as SL
- Sell strikes 300-400 points below that swing low
- Instead of selling close by strikes, prefer to sell a bit far away options in double qty and buy far OTMs options to get the benefit of margin (for this don't go beyond 1000 point from the sell strike)

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- Example on how to play reversals on Intraday
- Instead of the selling the support strike sell a bit far

## Example: How to play reversals in Intraday

- Assuming Bank Nifty (BNF) is trading at 39500, support is at 39200
- Instead of selling 39200 PEs, better to opt for 38800 PE
- One can sell double the qty of 38800 PE than the planned no. of lots of 39200 PE
- Double the qty of 38800PE can be sold only with the help of margin, so the hedges will also be in double quantity

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- As the strike is far from the support you get enough cushion
- As soon as the SL is hit, you can exit the positions
- without your strike coming into ITM

## Example: How to play reversals in Intraday contd.

- Stop loss will be the same i.e. once 39200 level is taken out
- The benefit here is since you are bit away from the Support/ Resistance you have additional cushion
- If you sell the support strike or just 1 strike down the support i.e. 39200 or 39100, your SL would still be 39200
- And in case the market reverses (turns against your position) & you wait for your SL levels, then your put will be ITM, and usually people freeze when the sold OTM options come into ITM

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- Greatest fear of any option seller is the Black Swan event
- Especially if that risk plays out overnight

## The fear of Black Swan event

- “Option sellers eat like chicken and shit like an elephant”
- The greatest fear of any Option seller is that of an Black swan event
- Such events can turn out to be catastrophic and could even wipe out the capital and put a dent on both trading account & confidence
- Usually events like war, tensions emerging from Indo China border or Indo Pak border or coupe situations, natural calamities etc can lead to big gap down, worst case scenario is even a lower circuit

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- Importance of hedge over buying a margin
- Hedge is to protect your capital from any overnight adverse news/event - Black Swan

## Importance of hedging

- Black swan events can neither be predicted nor avoided, but one can properly plan to mitigate the effects
- This is where the importance of hedging in real sense comes into picture
- Focus is on hedging instead of getting a mere margin without any protection on the downside
- One can always do some adjustments etc while any news comes during market hours
- The challenge is the overnight risk which is present in positional trades

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- How selling Rs. 45 option and buying a Rs. 15 option is a superior strategy
- than selling Rs. 30 option and buying a 5 Rs. Option or
- just selling a naked Rs. 30 option

## How to play Positional option selling while defining your risk

- On Wednesdays, prefer to sell usually Rs. 45 options and buy a hedge of Rs 15. Usually the difference in such strike prices is just 500 points away
- Compare this with another option seller who just sells Rs. 30 options on Wednesday as positional
- The benefit of the former strategy over the latter is that an option seller not only pockets in Rs. 30 but also caps his/her risk to a max of 10-12% of his/her capital

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- Hedging is an insurance premium paid to get a good nights sleep ■
- And also to protect your capital from any extreme events ■

## How to play positional Option selling

- Buying Rs. 2-3 options vs. Rs. 12-15 option, the higher premium options gives more protection for 400-500 point
- Opting for lower premiums so as to ensure the lower cost doesn't make sense to him, as he could easily recover the cost incurred in the options the next day
- Also he treats the higher premium as an insurance premium as it caps his max loss at a pre defined 10-12% and lets him sleep peacefully

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- If hedging is too expensive for you, then here's a hack

## How to play positional Option selling contd.

- If one is not convinced to pay such high premiums as it dents one's RoI, then;
- One can just buy such high premium hedges before the market close and just square them off the following day at the opening and switch to lower premiums during market hours
- Historically people overreact out of fear, so to he follows this hedge mechanisms for his positional PE sell
- On the CE front, he prefers ratio spread. Ratio works well on Wednesdays & Thursdays

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- Ratio spread strategy when moderately bullish & expecting a gap up

## Ratio Spread for scenario 1: Slight gap up

- When he is mildly bullish, and expecting a slight gap up the following day he would do a ratio spread
- Since he is mildly bullish he would buy 1 ATM CE & sell 2 OTM CEs
- Eg: Buy 1 lot of ATM CE usually ranging at Rs. 300 & sell 2 lots of OTM CEs in the range of Rs. 120, thereby going for a net debit of Rs. 60

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- Ratio spread strategy when strongly bullish & expecting a huge gap up

## Ratio Spread for scenario 2: Huge Gap Up

- When he is strongly bullish, and expects a huge gap up the following day he would do a ratio spread of 1:1
- Since he is strongly bullish, he would buy 1 ATM CE & sell 1 OTM CE
- Eg: Buy 1 lot of ATM CE usually ranging at Rs. 300 & sell 1 lot of OTM CE in the range of Rs. 120, thereby going for a net debit of Rs. 180

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- Ratio spread strategy when neutral to slightly negative & expecting a flat to slight -ve opening

## Ratio Spread for scenario 3: Flat to slight gap down

- When he is neutral about the market to mildly negative, and expects a flat to slight negative opening the following day he would do a ratio spread of 1:3
- Since he is neutral to mildly negative, he would buy 1 ATM CE & sell 3 OTM CE
- Eg: Buy 1 lot of ATM CE usually ranging at Rs. 300 & sell 3 lots of OTM CE in the range of Rs. 120, thereby going for a net credit of Rs. 60
- *Vice Versa for PE side in all three scenarios*

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- Always important to book the buy legs first as theta works against in option buying

## How to manage the positions the following day when in profit Scenario 1: Gap up

- The following day, if there is a gap up and the buy leg is in profit
- He will book the buy leg as it would be ITM by then and buy a far OTM as time decay can come in the sell and in the worst case he can even convert it to a straddle and manage them
- He acknowledges that in option buying one needs to act fast to lock the profits

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- Prefer to sell straddles in monthly over weekly as you have a huge range plus theta decay will work in your favour
- In weekly you will be caught adjusting due to gap up and gap down scenarios



## Few key Points

- Never sell straddles in weekly options, prefer monthly straddles
- Weekly straddles are affected most in gaps and you only make if it opens flat
- However in monthly you get enough time for it to decay before you start to adjust them
- The probability of the highest spike is in ATM options, so buy them and sell OTM options

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- In case of gap down no need to worry on the spreads as they are in net credit or most likely at 0 cost

## How to manage the positions the following day when in profit Scenario 2: Slight gap down

- If there's a gap down we have to only worry about the sold PEs
- No need to worry on the ratio spread, especially when we have done 1:3 ratio spread where we are in net credit or at no cost
- If there's a gap up or gap down, always square off the ATM options which was bought the previous day and buy far OTM CEs if you think the market will reverse (this is for the hedge)

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- Capital management is the key
- Keeping a buffer of 15-20% for any adjustments
- Always be aware of the total risk of your open positions

- Prefer a good nights sleep ■ over watching SGX Nifty & Dow in the night ■■■
- Never jeopardize your capital & mental peace■

## Capital Management

- He usually keeps 15-20% of his capital free for any unforeseen adjustments
- Follow the same process every day. Don't choose to do it only on some days and avoid on other days; otherwise chances are, usually the day you avoid, the risk will play out
- RULE IS TO NEVER LOSE MORE THAN 10% IN AN OVERNIGHT GAP UNDER ANY CIRCUMSTANCE
- Hence always prefer a proper hedge instead of a mere margin at the risk of capital erosion

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This was a ■on @Ronak\_Unadkat Sir's option selling strategies curated & presented by

@AdityaTodmal

&

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Happy learning ■ to everyone!