CASE STUDY (AN):
How to Time Your Trade Repair Adjustments

*The following case study is based on a successfully repaired put selling trade on **AN** during the spring and summer of 2018 . . .*

Today, I want to share some of the details of a put selling trade on AN we did inside the Leveraged Investing Club because it's a nice illustration of the two factors we consider when deciding when to roll or adjust a trade in repair mode.

(As I've said in other of these case studies, I'm a firm believer that every trade has something to teach us, or something to reinforce in us, and this is another great example – it doesn't matter how old a trade is when the lessons and principles are timeless.)

TIMING OUR ROLLS AND ADJUSTMENTS

I've actually put together a visual resource I call the **Timing Adjustment Cheat Sheet** and include in **Module 6 of the Sleep at Night Course** inside the **Leveraged Investing Club**.

It's basically a flowchart that takes all the guesswork and stress out of knowing when to make a repair move on an in the money short option (and which repair move to make).

But I'll explain the process here and demonstrate it with a real world trade.

>> By default, when it comes to timing our adjustments, we manage a trade primarily in terms of remaining time value.

When we can lock in the majority of our gains in a fraction of the time (because the underlying stock has moved higher) then we'll often close a successful trade early.

And on the flip side, if a position trades in the money on us, we'll generally leave it alone until all, or nearly all, time value has been depleted.

The rationale for waiting until time value is gone or mostly gone before rolling/adjusting an in the money short option position is that rolls are essentially "spreads" between what it costs to close out the old/expiring leg and what we receive when setting up or selling the new leg.

We want that spread to be as wide as possible, so the more time value we have to buy back on our roll, the more that crimps the spread.

>> But there can be an exception - such as if the technicals intervene and tell us that we're likely better off making an adjustment at present rather than waiting for the remaining time value to dissipate.

Let's look at this intraday chart on **AN** ion June 13, 2018 to illustrate:

Now, I didn't annotate this, but you can clearly see the issue - the stock had been doing really well but **hit a brick wall at the $50 level (and 200-day moving average)** and had pulled back substantially during that day's trading session.

And the **MACD Histogram** (the bars behind the MACD) looked like they may have topped out and could perhaps be reversing.

So those were a couple of big red flags warning us that the stock was at higher risk of trading lower in the near term.

At the time, my position consisted of **(2) AN JUNE 15 2018 $48 SHORT PUTS** – these were expiring at the end of the week and were still out of the money, but not by much.

Obviously, there was still time value remaining on them, so per our default trade management, I should've simply left them alone.

(Again, the rationale for waiting until virtually all time value is gone before rolling is that it maximizes the "spread" between what you pay to close an expiring position and what you receive for selling or setting up the new position).

But I felt the technicals were definitely intervening here - in fact, based on the chart, I believed that $48 level was quite vulnerable.

So the next step was to look around and consider my choices:

>> I could simply buy back the two $48 short puts and be out of the trade (for some perspective, I originally began with a single contract earlier in the year at the $52.50 strike) - both this leg of the trade along with the overall trade would be moderately profitable, and I could claim victory and move on

>> I could roll the existing $48 short puts straight out one month to July for a very nice net credit

>> I could make a Stage 1 move and roll the (2) $48 JUNE SHORT PUTS down and out to the JULY $47 STRIKE and still walk away with a decent net credit on the roll (meaning I would collect more from selling the July $47 puts than what it cost me to buy back the June $48 puts)

>> Or I could roll the (2) $48 short puts straight out to July at the same strike - and in the process reduce the number of contracts from two back down to one - and still get a very solid net credit

Of all the choices, I liked the last two the most because they reduced the risk on the trade the most.

And of the final two, I liked the last one the best because it reduced risk the most.

Yes, I could've worked my (2) short put contracts down to the $47 strike price, but by reducing my (2) contracts down to (1), that left me the ability to add a contract in the future in the event that the stock really sold off - and in that event, my two short puts would be at a much lower strike than $47

In fact, that's exactly what I ended up doing:

>> Date of Roll/Adjustment: June 13, 2015

>> I bought back my (2) AN JUNE 15 2018 $48 SHORT PUTS for $0.35/contract

>> I sold to open a single AN JULY 20 2018 $48 SHORT PUT for $1.46/contract

>> That resulted in total, post-commissions net premium of $66.75 projected over the following 37 days for a very respectable 13.72% annualized over this leg of the trade

At this point, I was really, really happy with how this trade had worked out

I had been totally wrong on the original set up (selling a put at the $52.50 strike), and yet at this point, the position (which I'd worked down to the $48 strike) was out of the money/near the money, it had generated net premium at a more than 15% annualized rate over a nice, extended 5-month period, and I was back down to a single contract.

And at this point, the cost basis/breakeven on the trade was all the way down to just $43.45/share (i.e. calculating assignment at the $48 strike less all the accumulated net premium collected throughout the entire campaign).

(Stay with me – I'm including a Trade Performance Table below that includes all the final numbers on this one.)

FAST FORWARD ONE MONTH

So about a month later, on July 19, 2018, one day ahead of expiration, **AN** was trading @ $49.41/share, and I was able to **buy back my expiring AN $48 short put for just $0.05/contract.**

That locked in a 13.04% annualized ROI over the previous 36 days.

And, of course, I was very happy with the final returns of the entire campaign @ 15.23% annualized over 149 days - especially since I started at the $52.50 strike:

AN- Trade Leg	Days Open	Cap Required	Closed/ Rolled	Net Credit/ Premium Booked
1 AN MAR 16 2018 $52.50 SHORT PUT	24	$5,250	2018-03-16	$157.28
1 AN APR 20 2018 $52.50 SHORT PUT	17	$5,250	2018-04-02	$85.50
2 AN MAY 18 2018 $48 SHORT PUTS	44	$9,600	2018-05-18	$23.77
2 AN JUN 15 2018 $48 SHORT PUTS	28	$9,600	2018-06-13	$121.97
1 AN JUL 20 2018 $48 SHORT PUT	36	$4,800	2018-07-19	$61.73
Net Premium				**$450.25**
Breakeven (Cost Basis)				**$43.50/sh**
Total Return (Based on Daily Avg-Weighted Capital)				**6.22%**
Annualized ROI		$7243.29 (daily avg-weighted capital)	149 Days	**15.23%**

When I first entered the trade back on 2018-02-20, **AN** was trading @ $52.67. 149 days later, when I was finally able to exit the position, the stock was trading @ $49.41/share.

On an annualized basis, the shares LOST value at a rate of 15.16% while my position GAINED value at an annualized rate of 15.23%.

(One of the many reasons I love selling options.)

TECHNICALS – WEATHERVANE VS. CRYSTAL BALL

To wrap up, let's look at how the stock traded after I made that June roll/adjustment – back when I said the chart was flashing warning signs and pulling back from the $50 share price level.

Check out the chart below:

Feel free to zoom in to see better, but after I rolled out (and reduced the contracts from two to one), AN actually traded higher.

Shares briefly traded above $51/share and even traded around $52/share on an intraday basis over the next week or two before pulling back.

As you can also see, a few trading sessions before I would exit the trade, **AN** was actually trading below $48/share.

Had I done nothing back in June, my $48 short puts would've expired worthless then and there, and I would've been out of the trade with no need to extend the repair campaign another month.

Does that mean the technicals – or my interpretation of them – were wrong?

This is a key point about technicals that I frequently make – **technical analysis is a weathervane, not a crystal ball**. Technical analysis doesn't tell you what will or will not happen with precision and confidence. **It simply tells you what's more likely to happen, and what's less likely to happen, in the near term.**

Despite **AN** trading above that $50/share price level – at least briefly – I maintain that heeding the technical warning signs and rolling/adjusting when I did was the smart move. And I would make the same move under similar circumstances.