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# OPTIONS

and the

# OPTIONS INVESTOR

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This brochure discusses exchange-traded options issued by The Options Clearing Corporation. No statement in this brochure is to be construed as a recommendation to purchase or sell a security, or to provide investment advice. Options involve risk and are not suitable for all investors. Prior to buying or selling an option, a person must receive a copy of *Characteristics and Risks of Standardized Options*. Copies of this document may be obtained from your broker, from any exchange on which options are traded or by contacting The Options Clearing Corporation, One North Wacker Dr., Suite 500 Chicago, IL 60606 (1-800-678-4667).

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[www.OptionsEducation.org](http://www.OptionsEducation.org)

**OIC** The Options  
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In 2009 options trading in the U.S. set a new record for the seventh year in a row. Institutions, advisors and investors traded more than 3.6 billion contracts. As the numbers show, the appeal of options as a risk management tool or a way to generate portfolio income is appreciated by a wide swath of the market.

For financial advisors this is great news for several reasons. First, options investors make attractive clients and prospects. Second, options require a level of expertise that even self-directed investors often lack. And third, the growing acceptance of options makes it more likely that a client or prospect will be open to this investment choice and select advisors that can offer this alternative when appropriate.

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Every five years, since 1995, The Options Industry Council (OIC), an educational organization sponsored by the U.S. options exchanges and The Options Clearing Corporation, has commissioned a national survey.

The survey is designed to create a profile of the current options investor, better understand how and why they use options and compare options investors to non-options investors.

Since the first survey the financial world has changed dramatically. The markets have collapsed twice, new investment products have come on the scene, and the Internet – not even mentioned in the first survey – is now a primary source of information and trading activity. Yet despite this transformation, each successive survey has shown options investors are more affluent, better educated and more open to investment ideas than their counterparts.

For the 2010 survey Harris Interactive conducted online interviews from December 1, 2009 through January 26, 2010 with 1,330 investors.<sup>1</sup> Five discount brokerage firms made their clients available for the study, but all of the participants reported multiple brokerage relationships. Again, researchers found that investors who trade options are a highly desirable group with many of the characteristics advisors seek in their clients.

# OPTIONS

INVESTORS *are*

# AFFLUENT



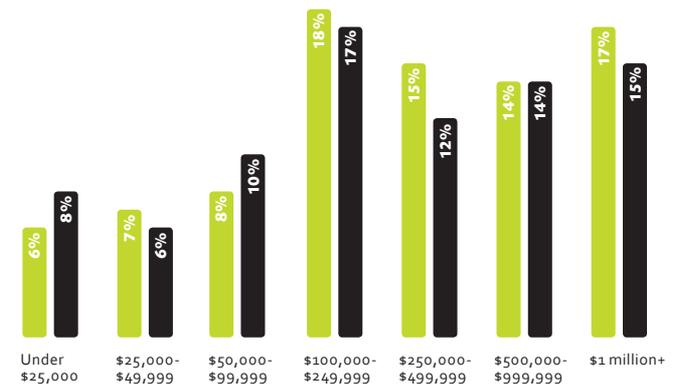
Options investors have significantly higher annual household incomes.

Thirteen percent of options investors had incomes in the \$250,000 to \$1 million+ range, compared to only eight percent of investors who do not trade options. Options investors also have greater reserves. On average, options investors had \$643,000 in liquid assets versus \$580,000 for non-options investors.

## ANNUAL HOUSEHOLD INCOME



## VALUE OF LIQUID ASSETS



Options users Non-options users

# OPTIONS

INVESTORS *are*

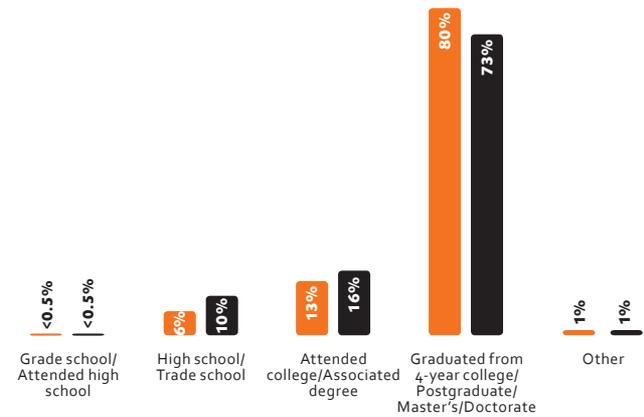
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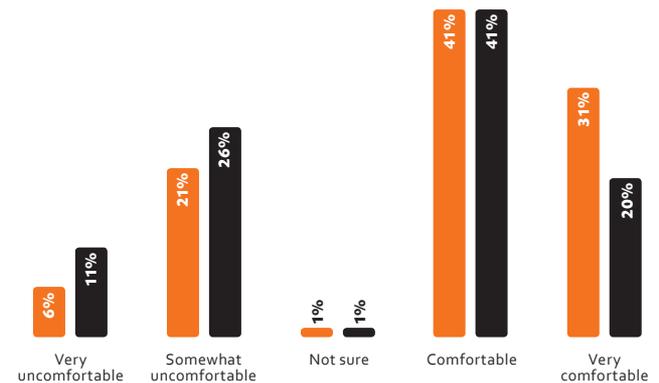
Options investors are more educated than non-options investors.

Eighty percent of options investors had at least a four-year college degree compared with 73% of non-options investors. Options investors have a higher level of risk tolerance and understand the correlation between risk and reward. Seventy-two percent of this group agreed that they were comfortable with high levels of risk in return for significant gain versus 61% of the non-options investors.

## EDUCATION LEVEL



## COMFORT IN TAKING HIGH LEVELS OF RISK IN RETURN FOR SIGNIFICANT GAIN



Options users Non-options users

# OPTIONS

INVESTORS *are*

# STRATEGIC

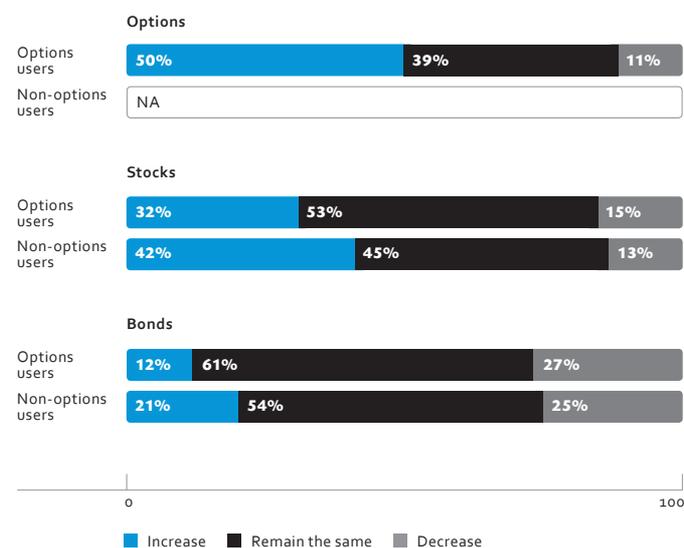


Options investors are receptive to a wider range of investment offerings.

They are more likely to have exchange-traded funds, futures, or American Depository Receipts in their portfolios than non-options investors. Mutual funds is the only investment category where those who do not trade options invest more, with 65% of non-options investors choosing mutual funds compared to 53% of options investors.

Options investors see the long-term value of options. One-half of this group reported that they plan to increase their use of options over the next 12 months, and 58% reported an increased allocation to options over the last two years.

## OPTIONS USERS ANTICIPATE INCREASED OPTIONS ACTIVITY RELATIVE TO OTHER INVESTMENT OPPORTUNITIES OVER THE NEXT 12 MONTHS



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## WHY INVESTORS

*want*

# OPTIONS

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And why advisors should offer them.

There is no question that most advisors are already over-extended, so there has to be a very compelling reason for them to add a service to their practice. In the case of options there are three; options can generate income, provide risk management and offer real portfolio customization.

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## 1

### GENERATE INCOME

In the Harris Interactive study, the primary reason given by options investors for trading options is to increase income on their current portfolio. With interest rates low there are limited ways investors can produce income. And, as the largest investing generation – baby boomers – grows older, the population needing income will only expand.

Covered call writing is far and away the most popular options strategy employed by individual investors and for good cause. A program of covered call writing cannot only guarantee an income flow; it is one of the few transactions where investors can know before they invest what their maximum gain and loss will be.

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## 2

### MANAGE RISK

Risk management has always been a major concern of high net worth investors, and many advisors believed they had addressed it through asset allocation. In the market meltdown of 2008, however, all categories lost value and many investors questioned their advisors' ability to protect their portfolios.

Options offer a variety of strategies to manage risk. A collar, for example, can be established to protect profits accrued from the underlying security and there are a wide range of option indexes that can be used to hedge a portfolio.

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## 3

### CUSTOMIZATION

While many products and services are positioned as customized, today's sophisticated clients recognize that they are simply being offered a choice of alternatives. Successful advisors realize they have to offer more.

Options strategies are built on a client's existing portfolio. As a unique plan for that investor alone, options provide the customization that many affluent customers seek. It also enhances the value of the advisors that provide options, since they have expertise in an area that their competitors do not.

## Reaching a new Market Segment

Many advisors assume that the only way to gain new clients is by persuading them to leave their current advisor and much of the time that is the case. But according to a recent study of independent advisors, 24% of new assets they received in the last six months of 2009 came from self-directed investors.<sup>2</sup>

### What prompts do-it-yourselfers to switch?

The Spectrem Group regularly conducts research with affluent investors.<sup>3</sup> Spectrem defines this group as investors with \$500,000 or more in investable assets minus the value of their primary residence. Within this group they have identified four segments:

- **ADVISOR DEPENDENT** (21%) relies on their advisors to make most if not all investment decisions.
- **ADVISOR ASSISTED** (30%) consults their advisor but makes most decisions on their own.
- **EVENT DRIVEN** (23%) makes most decisions independently but uses an advisor for specialized needs.
- **SELF-DIRECTED** (25%) makes all decisions on their own.

Interestingly, Spectrem has found that only one-half of the self-directed investors actually enjoy handling their own finances. They suggest that those who do not like handling their own finances, plus those in the event driven segment may seek the assistance of an advisor when they have a task that requires more in-depth knowledge or they are looking for a specialist in a specific area. Options are an obvious choice for specialization.

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## TALKING *about* OPTIONS

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While the Harris Interactive study focuses on the appeal of investors that use options, most advisors work with clients who are not using options.

Advisors might be surprised to learn that some of these clients may be more familiar with options than they think. Harris Interactive's research considered options investors to be any investor who had traded an option in the last 12 months. Among the non-options investors, Harris Interactive found that one-third had actually used options in the past and three-quarters of them would consider trading options again. Even among those who had never traded options, almost half expressed interest for the future.

Nonetheless there will be clients who are not familiar, and perhaps even a little scared of options. OIC has interviewed several advisors on how they speak with clients about options. While each uses a slightly different approach, every advisor makes certain their clients understand the fundamentals of how options work as well as the opportunities and risks that accompany them.

### Some advisors like to explain the concept first:

*"In talking with clients about options strategies I sometimes compare them to an insurance policy, where the client is forgoing some upside in order to protect the downside. Not all clients are comfortable with the concept but I have found over time that more and more clients are interested in learning about them."*

*“I explain it this way. You buy a condominium because the market is down and you think the market is going to go up and you’ll make money. But instead of letting it sit empty you rent it out. That’s what we are doing, renting the stock. If it goes up we sell it and make money and we are partially protected on the downside. But if the price goes up farther than we thought we may give up some of that appreciation.”*

### Other advisors prefer to introduce the idea when a specific opportunity arises:

*“A client will come to me with a stock they have heard about from someone. Let’s say it is selling at \$10 a share. I’ll ask if they would be comfortable selling the stock at \$12.50, which is a 25% gain. They almost always say yes. So, we buy the stock and write a covered call at \$12.50 for 50 cents. The client will be out at \$13, and is covered down to \$9.50.*

*“Alternatively we may be talking about a stock they like, but don’t want to buy at the moment because they feel the stock has been climbing and the price is too high. So I ask, ‘What if the stock went to its 52-week low, would you buy it then?’ at which point they typically say yes. I then suggest, ‘Why don’t we sell a put, which would require you to buy the stock at the lower price?’”*

### Explaining the risk and confirming their clients understand it is an important part of the process.

*“I explain that options can be used to either hedge risk or enhance returns. There are potential risks – because there is leverage and time decay with options, but I explain to them that we are never naked. I make a little joke that I don’t want anyone naked in the office. At the end I give my client a little quiz. If they can’t give me the answers, they don’t understand and I explain it again.”*

<sup>1</sup> “OIC Study of Investors,” Harris Interactive, March 2010.

<sup>2</sup> “Independent Advisor Outlook Study,” Charles Schwab & Co. Inc., January 2010.

<sup>3</sup> “Winning Over the Self-Directed Investor through Specialization,” Spectrem Advisor.

## How OIC can Help

Advisors that add options to their practices have a set of tools that can help them meet a diverse range of client needs and set them apart from the competition. And they don’t have to go it alone. OIC offers a comprehensive support system.

### WEB SITE

OIC has a web site exclusively for advisors at [www.OptionsEducation.org/advisor](http://www.OptionsEducation.org/advisor). There, advisors find resources and tools including:

- Online Classes, Webcasts and Podcasts
- Covered Call and Position Simulators
- Pricing Calculator and Strategy Screener
- Client Strategies, Legislative Updates and Research
- Options News, Market Data and Quotes

### LIVE HELP

The web site offers live help from options professionals, weekdays from 8-11 AM and 1:30-4:00 PM CST.

### HELP DESK

If advisors need assistance determining a strategy or just want to confirm what they are planning they can call the desk weekdays from 7:30 AM to 5:00 PM CST at 1-888-OPTIONS to speak with an options specialist.

### EMAIL

[options@theocc.com](mailto:options@theocc.com)

### COLLATERAL

OIC has industry brochures and collateral materials that advisors can use with clients and, if they like, co-brand with their company’s name.

For a free copy of the Harris Interactive 2010 OIC Study of Investors, visit the OIC web site at [www.OptionsEducation.org](http://www.OptionsEducation.org) or call 1-888-OPTIONS.