

How to Double Your Money From a 5% Move in the S&P 500

by Bob McHugh

Main Line Investors, Inc.

www.technicalindicatorindex.com

mainrdmch@aol.com

June 4th, 2024

At Main Line Investors, we are hunters for option trade opportunities that gather exceptional profits. Our **Platinum membership** program's goal is to identify such opportunities and provide subscribers with real-time detailed trades that we believe could produce strong returns. This may be a way to generate additional income to deal with the present hyperinflation economy. We identify trade opportunities for the major stock indices, precious metals, Treasuries, the volatility index, and oil. Platinum subscriptions are available at the **Subscribe Today** button at the left of the home page at www.technicalindicatorindex.com . If interested, email us at mainrdmch@aol.com with questions, for a disclosure form, or for information on our latest discounted special subscription deals.

Let's start this article by defining an actual scenario to examine how a 5% move in the S&P 500 could lead to a "doubling of our money"

investment trade, using options on the SPY, the ETF that tracks the S&P 500's moves closely.

The SPY is priced at about one-tenth of the S&P 500. So, as we show below, the S&P 500's price was 5,291 on June 4th. The SPY was priced at 528.39. Movements between the S&P 500 and SPY correlate extremely well, so if we play an options trade on SPY, we will be trading a tight relationship to the S&P 500.

The SPY has strong liquidity, high volume, as do options on the SPY, so we can expect narrow bid/ask spreads when we enter a position, and exit. The point is, trading options on SPY will be a good way to play a 5% move in the stock market, specifically the S&P 500.

Let's begin.

The SPY was trading in the cash market at 528.39 on June 4th, 2024. So, for the SPY, as a representation of the S&P 500 stock market we are playing, a 5% move would see this price change by 26.42 points. So, let's round the 5% target change in price to 25 points.

So how much money can we make if the SPY moves 25 points?

It starts with our market forecast. Let's say we have studied the charts, the indicators, the patterns, the economy, and have come to the conclusion the S&P 500 is about to drop 5%.

In this case, to make money on a decline, we want to purchase Put Options on the SPY. Puts play declines; Calls play rallies.

Let's take a look at the following chart.

SPY SPDR S&P 500 ETF Trust

\$528.39

Strike	Action	Last	Change	Bid	Ask	Volume	Open Int	Imp Vol	Delta
PUTS		Aug 16 '24 (73 days)							
495	▼	2.71	-0.08	2.72	2.75	31116,724	15.68 %	-0.1444	
496	▼	2.89	-0.39	2.81	2.84	296957	15.55 %	-0.1493	
497	▼	2.94	-0.32	2.90	2.94	8023,782	15.43 %	-0.1545	
498	▼	3.25	+0.15	3.00	3.04	1251,834	15.29 %	-0.1596	
499	▼	3.18	-0.28	3.10	3.14	2491,575	15.17 %	-0.1652	
500	▼	3.24	-0.07	3.21	3.25	2,63146,352	15.05 %	-0.171	
505	▼	3.90	-0.12	3.84	3.87	1,10316,945	14.43 %	-0.2034	
510	▼	4.69	-0.01	4.61	4.65	2,10826,282	13.83 %	-0.2427	
515	▼	5.60	-0.38	5.57	5.61	44212,987	13.25 %	-0.2903	
520	▼	6.81	-0.11	6.78	6.82	1,20313,023	12.69 %	-0.3477	
525	▼	8.38	-0.03	8.27	8.32	1,1369,049	12.14 %	-0.4158	
530	▼	10.17	-0.19	10.15	10.21	2,33618,359	11.63 %	-0.4955	
535	▼	12.95	+0.15	12.47	12.55	6244,273	11.13 %	-0.586	
540	▼	15.04	-3.48	15.17	15.60	18208	10.69 %	-0.6799	
545	▼	19.67	-1.14	18.58	19.08	4159	10.28 %	-0.7743	
550	▼	23.16	-2.09	22.52	23.06	240	9.90 %	-0.8573	
555	▼	30.60	0.00	26.88	27.38	01	9.17 %	-0.9205	
560	▼	33.75	0.00	31.54	32.12	04	--	-0.9612	
565	▼	33.82	0.00	36.38	36.97	01	--	-0.9836	
570	▼	41.26	0.00	41.30	41.90	01	--	-0.9938	

So, we have decisions to make.

How far out in time do we want our Put Option purchase to expire?

Two to three months is often an optimal choice, as it gives the expected move that we are playing the time to occur fully; minimizes

Theta risk of options value decay for the first several weeks; and yet is short enough that we can reap nice returns.

Here, we are choosing an August 2024 expiration.

Next, we pull up an options chain from our online Options broker for SPY, which gives us a string of possible strike price choices for our option. We can choose any strike we want. We show that chain above.

The further below the current cash market SPY price we choose, the cheaper the Put Option price. These would be “out of the money” choices. Our strategy is that if we purchase an out of the money strike price, 25 points below the current SPY cash price, a 5% decline in the SPY will result in a repricing (increase in value) of our option to a value close to that seen 25 points above where we purchase it.

So, in looking at the chart below, if we purchase an August expiration Put Option with a strike price of 505 (about 25 points below current SPY price of 528.39), then a 5% drop in the value of SPY down to 502 will result in a substantial profit for us. As we will see in a moment, **the price gain could double our money.**

The ask price to purchase the August strike 505 Put Option is \$3.87 per options share. A contract has 100 shares, so the price of one options contract will be \$387. This is our initial investment before the S&P 500 drops 5%.

Again, looking at the options chain chart for Puts, if we add 25 points to our strike 505, we can estimate the expected future value of our investment after a 25-point decline. So, to do this, we simply look at the price for a strike 530 option ($505 + 25 = 530$). The bid price for a

strike 530 is \$10.15 per options share, which is \$1,015 for our options contract.

In other words, **a 5% decline from where and when we purchased our Put option, has theoretically increased the value of our option from \$387 to \$1,015!**

Now, for the reasons we list below, our gain will likely be less than this, because this estimate of future gains assumes the 5% decline will occur fast, over a couple of days. If it takes longer, say several weeks, the time decay on options as they approach expiration will eat away at a portion of expected profits. So, instead of tripling our profit, we might only get a doubling of our profit.

However, on the plus side, as we discuss below, **when we play the market to decline, we get a boost in price appreciation of our option.** When sharp declines occur, the VIX rises (the volatility component of options prices), which increases the value of our Put Option. This is one key reason why playing declines can be a more profitable options play than playing a rally in the stock market (because the VIX declines on rallies).

Now let's look at a scenario where we believe the S&P 500 is about to rally 5%.

In this case, we have the same starting point. The SPY is trading at 528.39. So, if we are playing an expected 5% rally in the S&P 500 (and SPY ETF), we are expecting the SPY to rally about 25 points above

528.39, to 550. So, let's look at the next chart of an options chain for August 2024 SPY Call Options:

Last	Change	Bid	Ask	Volume	Open Int	Imp Vol	Delta	Action	Strike
CALLS		Aug 16 '24 (73 days)							
37.88	0.00	40.15	40.69	0672	15.78 %	0.8623	▼	495	
33.50	0.00	39.25	39.79	0374	15.65 %	0.8577	▼	496	
39.02	-1.30	38.35	38.89	1352	15.52 %	0.8529	▼	497	
30.70	0.00	37.46	37.99	0200	15.39 %	0.8481	▼	498	
34.13	0.00	36.57	37.10	02,637	15.26 %	0.8429	▼	499	
36.22	+2.63	35.69	36.21	1073,334	15.14 %	0.8375	▼	500	
30.89	+0.86	31.35	31.85	107,689	14.51 %	0.8077	▼	505	
27.51	+0.30	27.15	27.63	554,495	13.97 %	0.772	▼	510	
23.20	+0.95	23.23	23.45	1225,446	13.36 %	0.7295	▼	515	
19.45	+1.55	19.49	19.55	4509,401	12.82 %	0.6784	▼	520	
15.82	+0.19	15.91	15.96	85511,297	12.28 %	0.6206	▼	525	
12.70	+0.34	12.64	12.69	5,34514,716	11.77 %	0.555	▼	530	
9.71	+0.33	9.74	9.79	65413,565	11.32 %	0.4828	▼	535	
7.04	-0.02	7.27	7.31	85012,736	10.91 %	0.4067	▼	540	
5.27	+0.22	5.23	5.27	2,00020,184	10.56 %	0.33	▼	545	
3.66	+0.20	3.63	3.67	1,16020,355	10.27 %	0.2575	▼	550	
2.46	+0.23	2.44	2.47	9357,114	10.06 %	0.1931	▼	555	
1.62	+0.11	1.59	1.63	60319,787	9.90 %	0.1395	▼	560	
1.01	+0.12	1.02	1.04	2467,685	9.80 %	0.0974	▼	565	
0.65	+0.11	0.65	0.66	2043,030	9.78 %	0.0669	▼	570	

So, we select a strike price of 550, which is about 25 points “out of the money” (from the SPY cash price). The price for that Call option is \$3.67 per options share, which is \$367 for one SPY August 2024 Call Option.

Our projection, our ballpark estimate of future value, is that should the SPY rally 25 points, 5%, from here, the value of our Call Option will rise to the current price for a 525 Call Option. The bid on that strike 525 option right now is \$15.91 per option share, or \$1,591 per option contract.

In other words, the expectation for this option trade is a rise in value from \$367 to \$1,591 if the S&P 500 (and SPY) rises 5%, **an increase of 4 times our investment!**

Now this is not likely to be the true increase in the value of our trade investment, because it will likely take several weeks for the 5% rise to complete, and options value decays over time. Also working against this trade is that as the S&P 500 rises, it is likely the VIX (a measure of volatility risk for options writers) will decline (volatility risk premiums are a component of options pricing valuation).

That said, what would be a reasonable expectation would be a doubling of our money for this Call option trade on a 5% rally. The faster the rally, the greater the profit return for this trade.

The two charts at the end of this article, show where the S&P 500 was trading at the time of this theoretical trade set up, on June 4th, 2024, as well as where the VIX was trading at.

As a note, the VIX was trading at 13.16 on June 4th. That level could be described as moderately low, with potential to decline toward the 11.00 level if a 5% rise occurred in the S&P 500, and with the potential to rise toward 18.00 on a 5% decline.

Risks and a Recap

Now, while the above charts can be used to give us a ballpark estimate of an expected profit return on the option position as the S&P 500 (SPY ETF) price moves, **there are variables that affect the performance of option trades that will result in a different profit than our ballpark estimate:**

****1)** First of all, we have to have the **direction of the trade** right. If the S&P 500 (SPY ETF) is about to start a 5% rally, we better be in a Call option position, and not a Put. Calls play markets to rally, and Puts play markets to decline. And if the S&P 500 is about to start a 5% decline, we do not want to be in a Call option position, but would want to be in a Put option.

****2)** If the stock market goes into **an extended sideways move**, and we do not get a 5% vertical move, the options investment will likely decay rapidly and we could lose money on the trade. So, it is important that we only enter when we have evidence that a vertical move is about to start in the S&P 500 (SPY).

****3)** The **speed of the 5% move** impacts our profit potential. The faster the move, the greater the profit. This is because part of the price of an option is the time premium component. We are buying time when we buy an option. The longer the move takes, the more time premium decay occurs, reducing the value of the option (Theta risk).

****4)** The closer our chosen strike price to the value of the SPY when we enter, the greater the value change (delta) of the option. The further away from our chosen strike price to the value of the SPY when we enter, the less profit gain occurs as the stock market moves.

However, being further away from the SPY value upon entry, the cheaper the option price is to purchase at time of entry.

****5)** If a Call option is purchased to play a 5% rally in the S&P 500, when there is a high VIX level (which occurs after a previous sharp decline), our profit potential may be weaker than if the VIX was at a low level, because the Volatility component of an options price will work against profit potential in this instance. This is because as a 5% rally occurs, the VIX declines, so the volatility component of the option declines. Another way of saying this is, options are more expensive after a decline in the S&P 500 and a rise in the VIX.

****6)** On the other hand, if a Put option is purchased to play a 5% decline in the S&P 500 (SPY ETF), the profit potential increases as stocks decline, because the VIX will likely rise, so the **Volatility component of the option price** increases in value, providing a tailwind behind our trade.

****7)** If we are correct in our positioning, and we experience a rising value in our options position *before* the market has moved 5%, **we run into a dilemma: do we take an early profit**, or do we hang onto the option and hope for a full 5% move to occur? It is hard to leave a profit on the table, because **surprises can happen**, and the direction of the S&P 500 (SPY ETF) move could reverse before a full 5% move occurs, and **we could lose our profit**. Thus, we may be tempted to take a lesser profit than a “double our money” goal that might not happen. Maybe the move is destined to only be 1%, or 3%. This is where a careful study of technical analysis indicators and patterns can

provide useful guidance. This is where risk appetite, financial strength, and trading experience play a role.

****8) Caution: Options can lose value fast if the move we are playing does not develop as expected, so **we should never invest (trade) more than we can afford to lose**, or more than allows us to sleep well at night. A safer strategy might be to do small \$ trades, and more frequent trades, and only within a designated speculative allocation from within our total investment portfolio of funds, perhaps a maximum allocation to speculative options trading of only 5% or 10% of our total funds, with limits on the amount we invest per trade of perhaps up to 1% or so. **You should consult your financial adviser for guidance on these risks before trading options**. If new to options trading, it may be wise to do paper trades, not actual money investing, to learn the ropes and get a feel for how options can perform.**

Disclaimer: McHugh's Market Forecasting and Trading Report and this Executive Summary from that report is an educational service providing a body of technical analysis that measures the possibility and probability of future changes in mass psychology (swings from pessimism to optimism and back) which identifies possible new trends in major markets within various time frames, from very short term (daily) through very long term (years and decades). The tools we use are based upon price patterns, indicators and other proprietary measures that we have identified as correlative to future market

trends. While an investor or trader could come up with ideas and strategies from the information published in our reports, at no time should a reader or viewer be justified in inferring that any such advice is intended by this publication or our other services. We are not offering investing advice, but are only offering some (but not all) of the information that can be used in the investment decision making process with your own personal financial adviser. Investing carries risk of losses. Information provided by Robert D. McHugh's Market Forecasting and Trading Report is expressed in good faith, but it is not guaranteed. The market service that never makes mistakes does not exist. Long-term success trading or investing in the markets demands recognition of the fact that error and uncertainty are part of any effort to assess future probabilities. Please ask your broker or your adviser to explain all risks to you before making any trading and investing decisions. Information contained herein is believed to be reliable, but the publisher cannot be held liable for errors or omissions. No specific advice can be construed from this article. The reader is solely responsible for all actions taken. Copyright c 2024 Robert McHugh

\$SPX S&P 500 Large Cap Index INDX

© StockCharts.com

4-Jun-2024

Close 5291.34 Volume 2.1B Chg +7.94 (+0.15%) ▲



\$VIX Volatility Index - New Methodology INDX

© StockCharts.com

4 Jun 2024

Op 13.51 **Hi** 14.08 **Lo** 13.11 **Cl** 13.16 **Chg** +0.05 (+0.38%) ▲

▲ RSI(14) 47.88



— Full STO %K(14,3) %D(3) 45.93, 60.29

