INVESTMENT FORUM AGENDA FOR WEDNESDAY, FEBRUARY 6, 2013, 11:50AM

FORUM CAVEAT. I was reminded that the Forum caveat, about use of information shared in Forum presentations, has not been stated recently.

Information that you hear at the Investment Forum should be considered in light of your own investment goals and risk tolerance. Nothing said should be viewed as a recommendation, or form the sole basis for an investment decision. Forum members (especially your Moderator) are not Investment Advisors, and have no professional investment qualifications.

MARKET PERSPECTIVE. The market continues to levitate, with the DOW up .82%, the S&P up .68%, and the NASDAQ up .93% for the week. Both the DOW and the S&P are closing in on their all time highs of 14,165 and 1,565. This despite disappointing numbers for GDP growth in the fourth quarter, and the unemployment rate moving up a tick. Bond prices continued to edge lower, with the yield on the 10 year T moving up to 2.02%.

DOW 14,000! Continuing a tradition begun years ago, Ed Swoboda will provide a sheet cake celebrating the DOW crossing another 1,000 point milestone. We will cut the cake in mid session. Thanks Ed! Yes, we will have eating utensils. Please feel free to take another piece home at the end of the session. Who knows, perhaps we will celebrate DOW 15,000 and another sheet cake before the end of the year!

OBSERVATIONS ON FORUM MEMBER BUYS AND SELLS. Ed will comment on some of the "buys and sells" that members have posted recently.

OPTIONS, (CONTINUED.) We will have periodic, additional discussions of options and options strategies. This week, I will give another brief overview of the four options positions, and Anne Lamar will give review a covered call she has written on Deere (DE.) My comparison of the four options positions, from last week, is posted on the Forum website and attached to this agenda.

Maury Cralle will discuss an options strategy called a "strangle," which involves both a covered call and selling a put. Likely at a future session.

Tom on Bond Prices. Tom Crooker will comment on current bond prices.

BUYS AND SELLS

Buys
Jacobs Engineering Group (JEC)
Financial Select Sector SPDR (XLF)
Express Scripts (ESRX)
Ford Motor Company (F)
Crosstex Energy (XTEX)
MarkWest Energy Partners (MWE)
Novo Nordisk (NONOF)
Royal Dutch Shell (RDSA)
JP Morgan Chase (JPM)
Freeport McMoran Copper and Gold (FCX)
Apple (AAPL)
Intel (INTC)
IBM (IBM)
Cisco (CSCO)
Great Lakes Small Cap (GLS)
Pepco Holdings (POM)
I Shares MSCI Poland Investable Market Index (EPOL) - My Great Grandpappy would be pleased!

Sells
Exelon (EXC)
General Dynamics (GD)
IShares I Boxx Investment Grade Corporate Bond ETF (LQD)

Thinking About . . .
Proteus Digital Health
Sunoco Logistics Partners (SXL)

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Options Fundamentals

Four options positions:
Short (seller of the option)
Long (buyer of the option)
Call (opportunity to buy a security)
Put (opportunity to sell a security)

The four positions are short call and short put, and long call and long put.

Long Call

An investor pays a premium for the opportunity to buy a security at a specified price, until a specified time.

“Investor A pays $112 on 12/18/2012 to buy 700 shares (7 “contracts” - one contract = 100 shares) of GE at $23, on or before 3/16/2013.” GE is selling for $21 per share on 12/15/2012.

Investor A upside: Theoretically unlimited. If GE is worth $50 per share, or $1,000 per share by 3/15/2013, Investor A can purchase GE for $23 per share until 3/15/2013.

Investor A downside: $112. Investor C pays $112, which he will never recover.

What Investor A hopes for. That GE rises in value, to above $23 per share by 3/15/2013. If it does, he exercises the option, and is able to buy 700 shares of GE at $23 per share.

What Investor A does not want. GE does not rise in value to over $23, in which case he does not exercise his option, and he has no recover of the $112 he paid for the option.

Short Call

A investor and owner of stock receives a premium for the obligation to sell the stock at a specified price by a specified date, if the option is exercised.

Also knows as “covered call,” or “writing a call.” This is the counter position to a Long Call, and Investor A above.

“Investor B, who owns 700 shares of GE, receives $112 on 12/18/2012 for the obligation to sell his shares of GE at $23, by 3/16/2013, if the option is exercised by the holder of the option. The shares are worth $21 on 12/15/2012.

If the stock trades higher than $23 on 3/16/2013, Investor A, the owner of the option (long call) will exercise the option and purchase the 700 shares.   If the shares are worth less than $23 on 3/16/2013, the option will not be exercised and will expire. Investor B keeps the premium in either case.

Investor B upside: $112, which he keeps regardless.

Investor B downside. Theoretically unlimited. If GE rises in value to $50 per share or $1,000 per share by 3/16/2013, he must sell it for $23 per share.

Strategy. Selling covered calls is typically a strategy to increase the yield on a stock. The covered call seller (Investor B) continues to own the stock and collect the dividend if and until the stock is “called” away by the option holder (Investor A.) Investor B may have a substantial gain in the stock when he writes the covered call. If it is exercised (in this case at $23 per share) he will realize an additional gain.

If the option is exercised, Investor B will have a taxable gain, if the stock is held in a taxable account.

<u>Long Put</u>

An investor and owner of stock pays a premium of $112 to purchase an option to sell 7 contracts, or 700 shares, of the stock he owns at a specified price by a specified day.

“Investor C owns 700 shares of GE, which is worth $21 per share on 12/15/2012. He pays $112 for an option to sell his 700 shares of GE, at Investor C’s decision, for $19 per share, by 3/16/2013.”

Investor C’s upside: Large. If GE drops in value to below $19 per share, or to zero, Investor C is able to sell it for $19 per share. If GE does not decline, or if GE rises in value from $21 per share, Investor C does not exercise the option, but still owns GE which has risen in value.

Investor C downside: $112, which cannot be recovered.

Strategy. A Long Put is insurance, which protects Investor C from sharp declines in value of the stock he owns, but for which he pays a fee for the downside protection ($112.)

Short Put

Investor D receives a premium, which obligates him to purchase a stock from another investor, at a specified price by a specified date.

"Investor D receives $112 on 12/15/2012, which obligates him to purchase 700 shares of GE for $19 per share, until 3/15/2013. The stock is worth $21 per share on 12/15/2012."

The is the counter to the Long Put, or Investor C above.

Investor D upside: $112, which he gets to keep regardless of the price movements of GE.

Investor D downside: Large. If GE is worth less than $19 per share as of 3/16/2013 (down to zero), he will have to purchase shares at $19 per share.

Investor D hopes that GE is worth $19 per share or higher as of 3/16/2013, in which case he pockets $112 with no further obligations.

Calculation of the value of the covered call premium to the holder of the GE shares:

$112 (the premium for 3 months,) x 4 = $448.

700 shares x $21 = $14,700
$448/$14,700 = 3.05%

The dividend yield on GE is currently 3.1%. Selling covered calls quarterly, increases the yield to 6.2%.