
Top Five Reasons to Trade Futures Options

AS AN OPTION TRADER, do you understand all of your option trading choices? It's common for stock traders to focus on stock options. However, there is another option choice that every stock option trader should consider, and that choice is options on futures. This article will cover similarities and differences between stock options and futures options. Here are the top five reasons stock option traders should consider trading futures options:

1. Diversification

Most stock option traders have all their eggs in one basket – and that basket often leans too heavily in one market direction or the other – which can have a disproportionately adverse effect on their account if the market moves the wrong way.

Futures options provide an opportunity to invest in markets that are not correlated to the stock market and allow the trader to diversify and spread trading risk across a range of non-correlated markets like gold, crude oil, bonds, currencies, and any number of agriculture commodities.

2. Pure Market Exposure

A stock or exchange-traded fund (ETF) option trader seeking exposure to crude would have a number of challenges: first, oil refining stocks are highly diversified beyond crude oil; second, ETFs like the United States Oil Fund (USO) use futures and swaps to create a crude oil price proxy; and third, often these instruments do not directly reflect the price action of the crude oil market.

On the other hand, the crude oil futures option trader receives pure exposure to the crude oil market; each crude oil futures option controls one crude oil future made up of 1,000 barrels of West Texas Intermediate crude oil.

3. No Earnings Surprises

The stock option trader all too often has to contend with the impact of news events – like when a company reports earnings, corporate actions, and declaration of dividends – all of which will influence the underlying stock price.

None of these issues really come into play for a futures options trader. Major market index futures are diversified over many symbols so that one or even several stock symbols have a much smaller effect on the overall index price, which can help reduce short-term trading risk.

4. Trading Anytime You Want To

Have you ever seen a dramatic news story after the market close and thought, "I wish I could trade that?" Stock option traders only have trading access during regular stock market hours. Futures options traders have access to global markets virtually 24 hours per day – five days a week. Geopolitical actions and economic events can occur at any time around the globe. A futures options trader has the ability to trade and manage risk during news events in real-time.

Take for example the Brexit vote on June 24, 2016 at 12:01 a.m. Eastern Time. Figure 1 shows the SPY ETF closing on June 23. If a stock option trader was long SPY call options at the close, they were fully exposed to any and all overnight price action related to Brexit with no way to close, adjust, or hedge their position. And when they could trade again in the morning of June 24, the market had gapped down against their position. However, with good liquidity throughout this entire news event, futures traders were able to take both long and short positions as needed overnight until the open of the next day (see Figure 2).

5. Tax Benefits

Finally, futures options provide tax benefits over stock options. Under IRS rules, short-term stock option profits are taxed 100% as regular income, whereas 60% of profits on futures options are taxed as capital gains and 40% of profits are taxed as regular income.

For example, a trader with \$10,000 in stock option profits – assuming a 30% tax bracket – would owe \$3,000 in taxes. That same trader with \$10,000 in futures options profits would pay 15% capital gains tax on 60% of the gain (\$6,000 × .15 = \$900) and 30% regular income tax on 40% of the gain (\$4,000 × .30 = \$1,200), for a total tax owed of \$2,100, a savings of \$900 over stock options.

Summary

As we explored in this article, there are many similarities between stock options and futures options. The trading strategies the stock option trader is familiar with translate directly to the futures options market. Plus, there are differences that translate to added benefits, flexibility and opportunity in trading futures options, expanding trading possibilities for the stock option trader.



Figure 1 – Stock options trading unavailable during Brexit. A daily candlestick chart of the SPY ETF for June 23 and June 24, 2016 shows the market closing higher on June 23 prior to the Brexit vote, and then gapping lower on the open, after the vote, on June 24.



Figure 2 – Futures options trading opportunities during Brexit. A 60 minute chart of the CME E-Mini S&P 500® futures contract for June 23 and June 24, 2016 shows the market closing higher on June 23 prior to the Brexit vote, and then overnight price action falling into the Brexit vote at 12:01 a.m. Eastern Time.

IMPORTANT INFORMATION

No offer or solicitation to buy or sell securities, securities derivatives or futures products of any kind, or any type of trading or investment advice, recommendation or strategy, is made, given or in any manner endorsed by any TradeStation affiliate. Past performance, whether actual or indicated by historical tests of strategies, is no guarantee of future performance or success. Active trading is generally not appropriate for someone with limited resources, limited investment or trading experience, or low risk tolerance. Please visit our website www.tradestation.com or www.tradestation-international.com for relevant risk disclosures. Equities, equities options, and commodity futures products and services are offered by TradeStation Securities, Inc. (Member [NYSE](#), [FINRA](#), [CME](#) and [SIPC](#)).

Options trading is not suitable for all investors. Your account application to trade options will be considered and approved or disapproved based on all relevant factors, including your trading experience. View the document titled [Characteristics and Risks of Standardized Options](#). Before trading any asset class, customers must read the relevant risk disclosure statements on our [Important Information](#) page. System access and trade placement and execution may be delayed or fail due to market volatility and volume, quote delays, system and software errors, Internet traffic, outages and other factors.

© TradeStation. All rights reserved.

