



The 1987 Crash... Being There

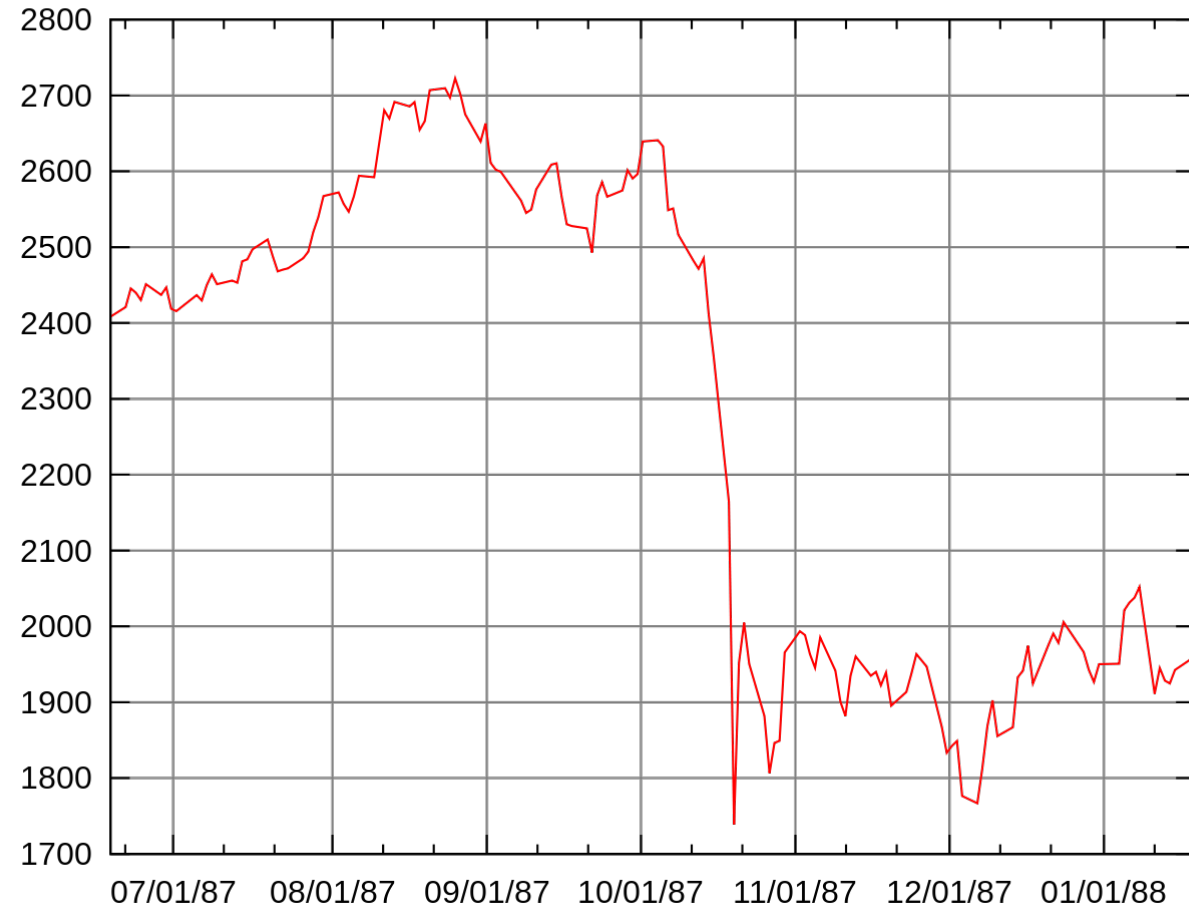
The importance of relative pricing and option spread relationships.

By Tony Saliba

Crash Anniversary

Black Monday: October 19th, 1987

Dow Jones (1987-06-19 through 1988-01-19)



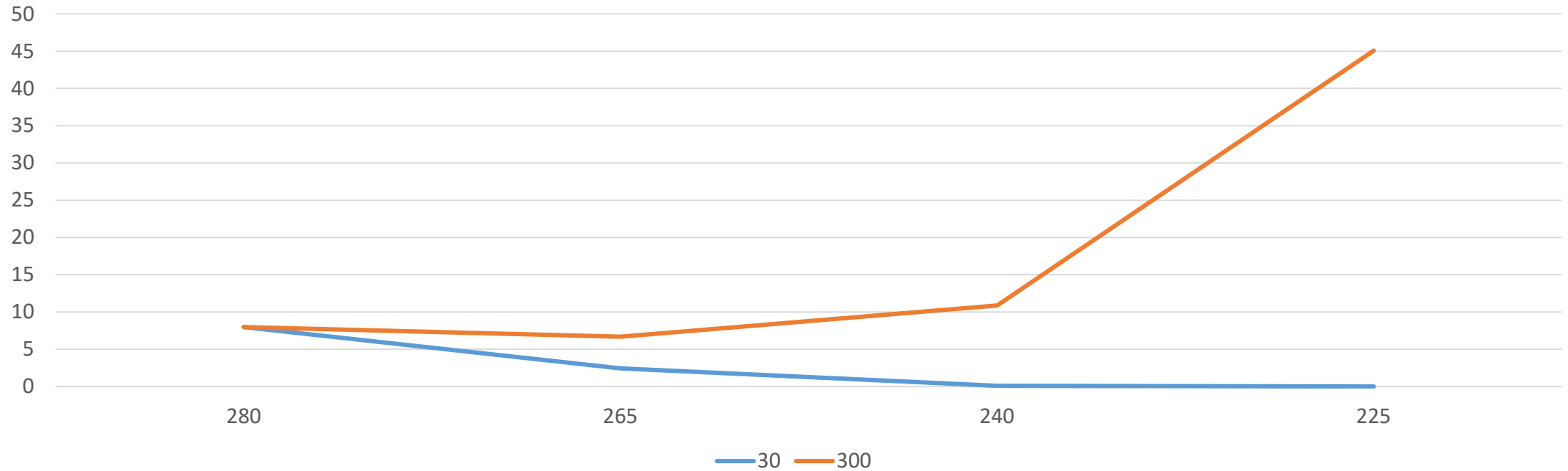
Graph Source: Wikipedia

What Happened?

- Dow Jones Industrial Average:
 - down 22.61%, falling 508 points to 1738.74, equals around 5800 points today
- S&P 500:
 - dropped 20.4%, falling 57.64 points to 225.06, equals around 600 points today.
- Volatility: over 300
 - What would you do?
 - How much is the option in the money on Tuesday morning?
- What did I trade:
 - Customers were buying the box
 - I ended up with a lot of puts

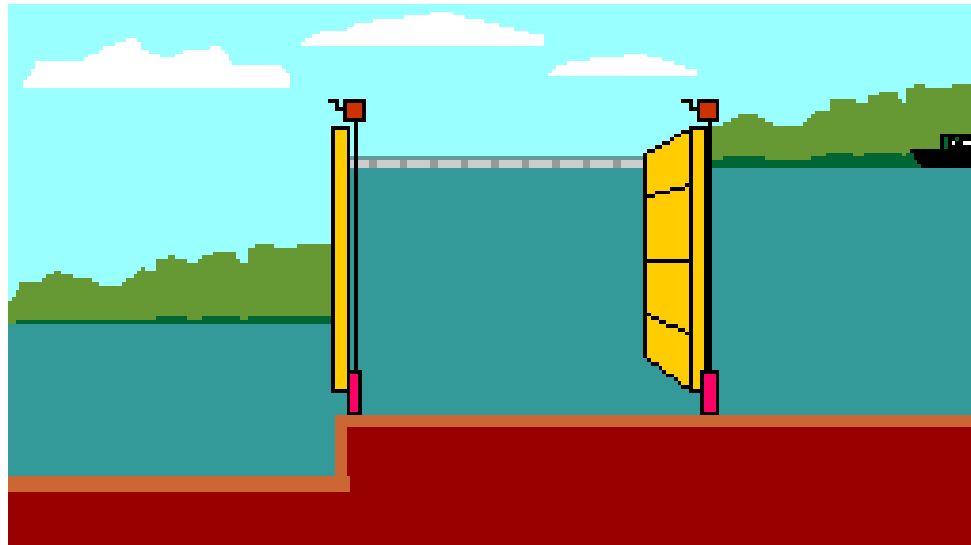
30 vol vs 300 vol

280 Calls



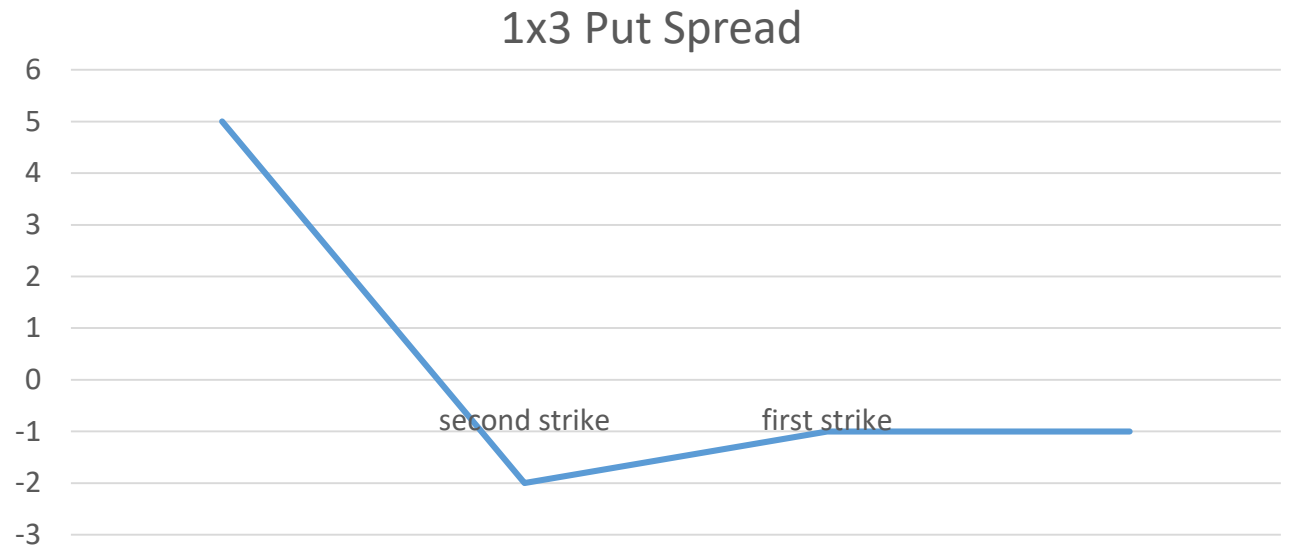
Relative Pricing

- “The Lock Choice”: Upstream/Downstream Lock
 - Tied on the boat vs tied on the wall
 - linked with volatility vs linked with spread relations
 - Theoretical Value vs Relative Pricing



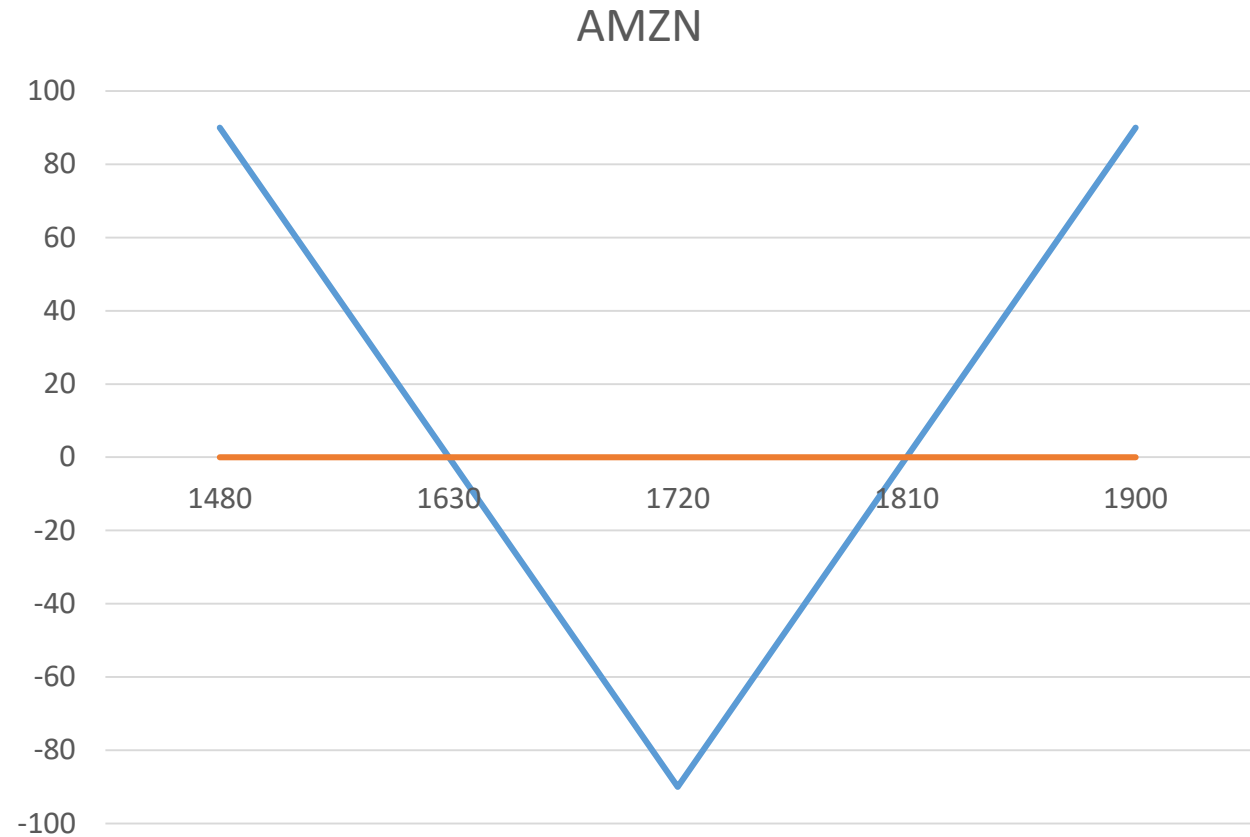
Convexity

- In our language, convexity is the “Wings”.
- How do we manufacture the Convexity?
- Buy convexity:
 - Short puts vertical on a ratio
 - Pay a little extra



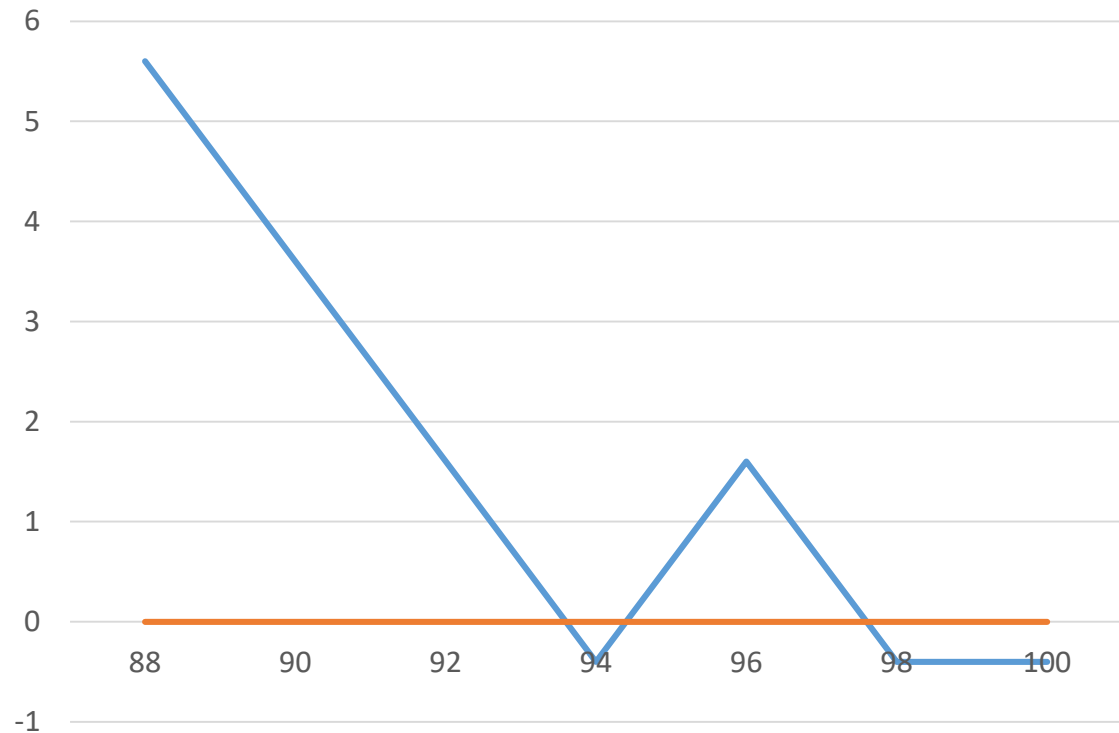
Event/Earnings trade

- Long Straddle
- Examples of Earning: Amazon
 - October 24 earnings
 - October 25 expiration
 - ATM straddle = \$90
- $\text{ATM Straddle/Spot} = \text{expected move}$



Option Strategy: the Flying AJ

- The Flying AJ Strategy:
- Butterfly with 1 extra put:
 - Long 1 put, short 2 puts, Long 2 puts
 - Example spot =100
 - +98 put X1
 - (96 put) X2
 - +94 put X2



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