Wolcott Wheeler wolcottwheeler@gmail.com

1 Riverside Drive, #24 (914) 826-4188

Sleepy Hollow, NY 10591

**What Is Dividend Risk? How Can Option Traders Prepare for It?: Video Script**

|  |  |
| --- | --- |
| **Voiceover** | **Visual** |
| Dividend risk is triggered by upcoming dividends, which sets in motion an option’s early assignment. What options are at risk of early assignment? ***Short, in-the-money call options***. These can be naked short calls, or short calls that are part of a spread, like a vertical spread or an iron condor. | * What options are at risk of early assignment? * Short, in-the-money call options * Naked short calls * Short calls that are part of a spread |
| Short call options can be forced into early assignment when stocks or ETFs go ex-dividend—that’s the time period between when a dividend is anno­unced and when it’s paid. If you own the call and want to be able to receive a dividend, you can exercise your right to buy the stock prior to the ex-dividend date **and** before the option’s expiration.  But as a result, you might be assigned on your short call, resulting in a short-stock or short-ETF position—that means you’re now required to pay the dividend! | * Short call options can be forced into early assignment when stocks or ETFs go ex-dividend * The time period between when a dividend is anno­unced and when it’s paid |
| How can you plan for dividend risk and prepare for it?   * Learn when the ex-dividend date will occur. * Using thinkorswim, navigate to the MarketWatch tab, and click the calendar sub-tab. * Checkmark the boxes next to Dividend and ETF Dividend. * This will filter the calendar and display the probable ex-dividend date for various underlying symbols. * Oh—and always double-check the company’s investor relations page for official information. | How can you plan for dividend risk and prepare for it?   * Learn when the ex-dividend date will occur * Using thinkorswim, navigate to the MarketWatch tab, and click the calendar sub-tab * Checkmark the boxes next to Dividend and ETF Dividend * This will filter the calendar and display the probable ex-dividend date for various underlying symbols * Always double-check the company’s investor relations page for official information |
| Now that you know when the ex-dividend date is, you can also determine the likelihood of getting assigned early.   * Start by comparing the corresponding put’s value to the dividend, or the estimated dividend amount. * The corresponding put option is the same strike as the short call option. | To determine the likelihood of getting assigned early:   * Start by comparing the corresponding put’s value to the dividend, or the estimated dividend amount * The corresponding put option is the same strike as the short call option |
| Let’s say you’re short a $95 call in ABC. By checking the bid price of the $95 put in ABC in the same series, you can gauge the likelihood of being assigned. If the corresponding put value is *less* *than* the dividend amount, there is a good chance of early assignment, and you may want to take action prior to the ex-dividend date. | * Check the bid price of the $95 put in ABC in the same series * Gauge the likelihood of being assigned |
| For example:   * ABC is trading at $100 per share. * ABC stock is going ex-dividend tomorrow. * The dividend amount is $1.20. | For example:   * ABC is trading at $100 per share * ABC stock is going ex-dividend tomorrow * The dividend amount is $1.20 |
| If the bid price of the $95 put is less than $1.20, or the amount of the dividend, then you’re at high risk of assignment. You can only guarantee no assignment by closing the short call position prior to the ex-dividend date. | The only guarantee no assignment—close the short call position prior to the ex-dividend date |
| Now let’s look at an ETF whose dividend amount hasn’t been published yet.   * Determine the front month or weekly, deep, in-the-money puts. * Then calculate the extrinsic put value to get an idea of what the marketplace is expecting as the dividend amount. | Let’s look at an ETF whose dividend amount hasn’t been published yet.   * Determine the front month or weekly, deep, in-the-money puts * Then calculate the extrinsic put value to get an idea of what the marketplace is expecting as the dividend amount |
| Imagine an ETF called XYZ is trading at $200 per share and is going ex-dividend tomorrow. The dividend amount is actually a dividend distribution, and it won‘t be known until the morning of ex-dividend, which is too late!   1. Go to the front month or weekly expiration. 2. Identify the first out-of-the money call with a zero bid. 3. Using put/call parity, the bid price of the call will indicate the amount of extrinsic value in the corresponding put option. 4. Since the CALL price is a zero bid, this indicates the put’s price is comprised 100% of intrinsic value (Put Strike – Underlying Price = Intrinsic Value). | * Go to the front month or weekly expiration * Identify the first out-of-the money call with a zero bid * Using put/call parity, the bid price of the call will indicate the amount of extrinsic value in the corresponding put option * Since the CALL price is a zero bid, this indicates the put’s price is comprised 100% of intrinsic value (Put Strike – Underlying Price = Intrinsic Value) |
| Let’s imagine the first out-of-the-money call priced at zero bid is the 208 call.   * The current market of the corresponding put is an $8.60 bid, offered at $9.60. This makes the mid-price of this put $9.10, since ($8.60 + $9.60)/2 = $9.10. * Since the intrinsic value (Put Strike – Underlying Price = Intrinsic Value) of the put being $8 and the mid-price of that pit is $9.10, the put is priced at $1.10 over its intrinsic value. * Your conclusion: the market is pricing in a $1.10 estimated dividend distribution. | Let’s imagine the first out-of-the-money call priced at zero bid is the 208 call   * The current market of the corresponding put is an $8.60 bid, offered at $9.60. This makes the mid-price of this put $9.10, since ($8.60 + $9.60)/2 = $9.10 * Since the intrinsic value (Put Strike – Underlying Price = Intrinsic Value) of the put being $8 and the mid-price of that pit is $9.10, the put is priced at $1.10 over its intrinsic value * Your conclusion: the market is pricing in a $1.10 estimated dividend distribution |
| This is because on the ex-dividend distribution date, XYZ should theoretically drop by the amount of the dividend, not taking into account tomorrow’s supply and demand. If you have short in-the-money calls, where the corresponding put is bid less than the dividend estimate, consider closing or rolling the position to a strike with an extrinsic value greater than your dividend estimate. | * If you have short in-the-money calls, where the corresponding put is bid less than the dividend estimate: * consider closing or rolling the position to a strike with an extrinsic value greater than your dividend estimate |
| Other reasons may assign you a short call option.  If you have questions, please contact the trade desk at 1-866-839-1100. | * Other reasons may assign you a short call option * If you have questions, please contact the trade desk at 1-866-839-1100 |