National Inflation Association
Preparing Americans for Hyperinflation

EDUCATIONAL REPORT ON OPTIONS TRADING

The National Inflation Association believes the best way for Americans to preserve purchasing power during the upcoming hyperinflationary crisis is by accumulating physical **gold.** Gold is real money, its value always stays the same. When gold prices rise and fall, it is only showing just how unstable the U.S. dollar is. In our opinion, 1 ounce of gold will buy the same amount of clothing, food, and energy, today as it will one, five, or ten years from now.

For Americans who wish to increase their purchasing power, NIA believes that accumulating physical **silver** is the best way to do it. In NIA's top 10 predictions for 2010 re-leased in December of 2009, we predicted a sharp decline in the **gold/silver ratio,** which was 64 at the time. During the year 2010 it declined by 28% down to 46. In NIA's top 10 predictions for 2011, we once again predicted another large decline in the gold/silver ratio, and it has already declined by another 7% down to 43. The ratio is down 33% during the past 17 months.

Historically, going back to when the U.S. dollar was convertible into gold and silver, the gold/silver ratio was pegged at 16 where it remained for many decades and has averaged for centuries. NIA believes at a very minimum, the gold/silver ratio will fall back to 16, which means those who own silver will see a **2.68 times increase** in **purchasing power** compared to those who own gold.

NIA believes the best way to become **wealthy** during the upcoming hyperinflationary crisis will be by investing into **gold/silver mining stocks.** In our opinion, those who pick the right gold/silver mining stocks could see their wealth increase **100-fold** this decade. However, gold/silver mining stocks are high risk and if you pick the wrong stocks, you could lose all of your money.

Once you become a successful, experienced, stock market investor, NIA believes the next type of investment all NIA members need to become educated about in order to master is **stock options trading.**

While gold/silver mining stocks provide huge leverage over rising physical gold/silver prices, stock options provide even greater leverage over stocks. Those who learn how to successfully utilize options, can literally see gains in their portfolio of thousands of percent within months or even weeks!

In February of 2010, **JP Morgan** manipulated the price of silver down to below $15 per ounce. Back then, over a year ago, very few people were aware of JP Morgan's naked short position in silver and how they were artificially manipulating the markets. NIA was able to successfully recognize the manipulation for what it was, and we knew as soon as the manipulation was over, we would see a massive rise in silver prices. We were so confident that silver prices would soar from their lows in February that we decided to suggest call options as a way to speculative on rising silver prices.

On February 5th, 2010, silver hit its 52-week low of $14.926 per ounce. That weekend, NIA suggested to you January 2011 SLV call options at a price of $0.93 per contract. These options were out of the money by over $5 per contract, yet NIA was extremely confident that silver prices would rise dramatically over the next 11 months. NIA was right, SLV reached a high in the last week of December 2010 of $30.25.

While SLV gained 103%, the SLV call option NIA suggested gained 1,002%.

The option contract we suggested at $0.93, rose to a high of $10.25 **for a gain of 1,002%** in **less than 11 months.**

An **investment of just $100,000 would have yielded a $1 million profit**!

A single stock **options contract** gives the owner the **right to buy or sell 100 shares of a stock** at a certain price on or before a certain date. A **call option** gives the holder the right to buy 100 shares of a stock. A **put option** gives the holder the right to sell 100 shares of a stock. The price the option holder has the right to buy or sell 100 shares of a stock at is called the **strike price.**

All options expire on a certain date, called the **expiration date.** Each month has its own option and options always expire on the **third Friday of the month.** Therefore, if you buy June calls, you need to either exercise or sell your calls before the end of the third Friday of June, or else they will **expire worthless.**

The price that you pay for an option is called the **option premium.** The option premium is based mainly on how much an option is **"in the money"** and as well as how much time there is until expiration, along with other factors including the **volatility** of a stock.

Meaning, if stock XYZ is currently $25 per share and we are currently in the first day of June the premium for a June call option in XYZ with a strike price of $20 will at least be $5 per options contract. This is because the $20 call option for XYZ would be $5 in the money.

However, the actual premium/price for the option will most likely be higher than $5 per contract because not only is it $5 in the money, but you have three weeks before expiration. Therefore, the cost for this particular option might actually be $5.25 per contract.

The longer until an option expires, the higher the premium will be. So if XYZ is $25 per share and the June XYZ $20 call option costs $5.25 per contract, the July XYZ $20 call option might cost $5.50 and the August XYZ $20 call option might cost $5.75. Basically speaking, the more days until expiration, the more you will pay above the "in the money" value.

When you buy 1 option contract for $5.25, that 1 options contract represents 100 shares and therefore has a total cost of $525. The cost to buy 100 call options at a premium/price of $5.25 would be $52,500. You always calculate the cost of an options transaction by: the number of contracts you are buying X 100 X the option premium price.

Therefore, if an option has a premium of $10 and you have $10,000 to invest, simply divide $10,000 by 100 and then divide again by $10 and you will be able to afford 10 contracts.

Most options never get exercised. NIA co-founders have never once exercised an options contract. We always buy call or put options with the hope that their premium will increase in value before the expiration date and if it does, we sell our options contract and collect the difference.

Options provide a lot of **leverage** and allow you to make much **larger profits,** if you are right about the direction a stock is going. However, if you are wrong, there is a good chance your option will expire worthless and you will lose your entire investment. Therefore, there is also much **greater risk** when you buy call or put options.

If it is the month of June and there is a $50 stock with the symbol MMM that you believe will fall to $25 by December, the only way to bet against that stock without using options would be by shorting it. If you short 1,000 shares of that stock at $50, you will be betting $50,000 that the stock will decline if value. If you are right and that stock falls to $25, you can cover your 1,000 shares short for a cost of $25,000, generating a $25,000 profit.

However, options provide an opportunity to make much larger gains. If MMM is $50 in June and you believe will fall to $25 in December, you can buy out of the money put options in MMM. The premium for **out of the money** options is based mainly on the **time until expiration** and the volatility of the stock.

You might want to consider the December $30 put options for MMM. Because the odds of MMM falling from $50 to below $30 in just six months are very low, the premium/price for the MMM December $30 put option might be only be $1. If you are right about MMM and the stock falls from $50 to $25, by the third Friday of December when your $30 put option expires, your put option will most likely rise to $5, because the option will be $5 "in the money" at the time.

Therefore, if you had $50,000 to invest, you could buy 500 MMM December $30 put options at $1. If MMM falls down to $25 per share and these options reach $5, you can sell your 500 contracts for $5 before they expire for total proceeds of $250,000, earning a profit of $200,000.

With your option rising from $1 to $5, your total percentage gain will be 400% vs. if you shorted the stock at $50 and it fell to $25 you would only earn a 50% profit. A 400% gain vs. a 50% gain means you would be earning a profit that was 8 times larger with the option.

Keep in mind, if come the expiration date on the third Friday of December, if MMM was trading $30 or higher, your option will be "out of the money" and be worthless. Most likely, you won't be able to sell it at all and you will just let it expire worthless.

If you want to take less of a risk with MMM, you could consider buying the December $40 put options. Because

the stock will only need to drop greater than $10 to be "in the money" vs. the stock needing to drop greater than $20 to be "in the money", the premium/price to buy the MMM December $40 put options will likely be substantially higher than the premium/price for the MMM December $30 put options.

If the MMM December $30 put options cost $1, the MMM December $40 put options might cost $3.50. If you invested $50,000 into the MMM December $40 put option at a premium/price of $3.50 per contract, you will be able to buy around 143 contracts (the actual cost for 143 contracts at $3.50 would be $50,050).

If you are right and MMM declines to $25 per share, the MMM December $40 put option will likely be $15 on the third Friday of December, its expiration date, because it will be $15 "in the money". You will be able to sell your 143 contracts for $15 per contract (times 100 of course, because each contract represents 100 shares), and you will generate proceeds of $214,500 or a profit of $164,500, which would equal a percentage gain of around 329%.

Your percentage gain on the MMM December $40 put options of 329% wouldn't be as high as your percentage gain on the MMM December $30 put options of 400%, but the MMM December $40 put options are far less risky.

If MMM was trading for $50 in June and you bought the MMM December $40 put options at a cost of $3.50 per contract, you will need MMM to decline by 27% to $36.50 per share by the third Friday of December, just to break even.

If MMM was trading for $50 in June and you bought the MMM December $30 put options at a cost of $1 per contract, you will need MMM to decline by 42% to $29 per share by the third Friday of December, just to break even.

If you were wrong about MMM declining to $25 per share and MMM on the third Friday of December was trading for $35 per share, the MMM December $40 put option will be trading for $5 per contract, while the MMM December $30 put option will be worthless. Therefore, if you bought the MMM December $40 put option you would be up around 43% if MMM only declined to $35, compared to losing 100% of your investment if you bought the MMM December $30 put option.

Another way to take on less risk, besides buying an option with a higher strike price, is to buy an option with a later expiration date. To take on even less risk than the MMM December $40 put option, you might want to consider a MMM March 2012 $40 put option. If the MMM December $40 put option had a cost of $3.50 per contract, the MMM March 2012 $40 put option might have a cost of $4 per contract. That is because you have an extra three whole months for MMM to make its decline.

If MMM was $50 in June and declined to only $45 in December, but then declined to $30 in March, your MMM December $40 put option would have expired worthless in December because it would have been $5 "out of the money". However, the MMM March 2012 $40 put option would have a value of $10 on its expiration date because it would be $10 "in the money. If you bought 125 contracts in June at $4, those 125 contracts at $10 would now be worth $125,000 and you would be up $75,000 or 150% on a $50,000 investment.

Although making a profit of $75,000 on MMM March 2012 $40 put options with the stock declining from $50 to $30 over a period of 9 months would be a lot less than making a profit of $200,000 on MMM December $30 put options with the stock declining from $50 to $25 over a period of 6 months, it is sometimes worth taking on less risk by buying higher strike price put options with later expiration dates, because you have more time for the stock to fall and the stock wouldn't have to fall as much to make a profit.

NIA almost always uses options to speculate and increase leverage when we are confidence that the price of a stock or ETF is heading in a certain direction. However, options can also be used as a **hedge against risk,** kind of like an insurance policy if you want to **protect** yourself against a stock that you own going down, or a stock that you are short going up.

Let us say you are invested heavily into the stock Silver Wheaton (SLW), which at the time of this report is approximately $34 per share. Imagine owning 5,000 shares of SLW that are currently worth $170,000 and you paid only $15 for your shares or $75,000. You are currently making a $95,000 profit and you don't want to risk losing your profits, if for some reason the price of silver declines in the short-term and the share price of SLW falls.

SILVER WHEATON
the pure silver company

What you could do is purchase 50 put option contracts in SLW, which give you the right to sell your 5,000 SLW shares at a certain strike price up until the expiration date of that option. It is currently May and let's say you are concerned about SLW declining within the next 7 months. You might want to buy 50 December put options in SLW, which expire the third Friday of December or on December 16th, 2011.

You can buy 50 put options in SLW at almost any strike price you want, but because the price of SLW is currently

$34 and you want to protect yourself from SLW declining below $34, you decide to buy SLW December $34 put options. The SLW December $34 put options are currently priced at $5.10 per contract. The cost to buy 50 of them would be $25,500.

If you buy 50 SLW December $34 put options at a cost of $25,500 and SLW crashes during the next 7 months down to $20 per share, you will still be able to sell your SLW up until December 16th at a price of $34. Therefore, if in December SLW is $20, you would likely exercise your option and sell your 5,000 SLW shares at $34, earning a profit on the stock of $95,000, however, after the cost of the option your actual profit would now be $69,500.

A profit of $69,500 would by far be better than sell- ing your SLW at $20 and earning a profit of only $25,000. Therefore, in this situation, buying put options in SLW as a hedge against a decline would have far been worth it and saved 73% of your profits. Whereas, if you didn't buy the options you would have lost 74% of your profits.

If, however, SLW rises during the next 7 months up to $45 per share, you will have no reason to exercise your option and it will just expire worthless. If SLW is $45 in the month of December you will now be up $150,000 on the stock. But, once you subtract the money you spent on the option that expired worthless, you will only be up $124,500 on the stock.

Only 83% of the profits you would have had after it gained during those next 7 months, will you will have after the option cost. In other words, the $25,500 you spend for the option will go to waste if the price of SLW goes up, but will save you a great deal of money if the price of SLW falls dramatically.

There are many other more **advanced strategies** that options traders frequently use. If you believe the price of a stock is going to be very volatile in the short-term and make a big move to either the upside or downside, but you are not sure what direction it will be, you can use a **straddle** strategy and buy both call and put options at the same time. The idea is, one of your options will expire worthless, but the other one will gain by more than 100% and you will overall generate a profit.

Let's say for example Nike (NKE) is releasing their earnings next week and we expect it to make a big short-term move to either the upside or downside. NKE is currently around $84 per share.

Let's say we want to bet $50,000 total that NKE will make a big short-term move this month and the closest NKE option strike price to NKE's current share price is $85. The premium/price for NKE June $85 calls is currently $1.13 and the premium/price for NKE June $85 puts is currently $2.57.

If you put $25,000 each into both of them, you can buy 221 NKE June $85 call option contracts and 97 NKE June $85 put option contracts.

If NKE releases very strong earnings next week and the stock gains $10 per share to $94, the call option contracts will likely rise to $9 per contract and the put option contracts will likely expire worthless. Your 221 call option contracts will be worth $198,900 while your put options will be worth $0. Overall you will earn a $148,900 profit.

If NKE releases very weak earnings next week and the stock falls $10 per share to $74, the put option contracts will likely rise to $11 per contract and the call option contracts will likely expire worthless. Your 97 put option contracts will be worth $106,700 while your put options will be worth $0. Overall you will have a profit of $56,700.

To break even on NKE, you will need to see the stock after earnings either rise by $3.26 or decline by $4.15. If, for example, NKE stayed the same and finished June 17th at $84, your put options will be $1 per contract and have a value of $9,700 and your call options will be $0, and you will lose $40,300 or 81% of your investment.

All of the options strategies discussed above involve buying either call or put options. However, you can also place bets on options not by buying them, but by **writing** them to somebody else who is buying them.

If you are bullish on a stock, you can **write put option contracts.** When you write put opinions, you are immediately credited with and keep the premium somebody else paid for those contracts. Your hope is that the option you write finishes "out of the money" and expires worthless. That way, the person buying it will never exercise it. However, if you write options contracts, at any time you can be assigned an exercise notice and be required to buy the shares represented by those contracts at the strike price of the option.

You should only write put options if you are financial capable of and also feel comfortable owning shares in the company at the strike price of the option, because you will be obligated to buy shares of the stock at the strike price, if the option holder chooses to exercise. The premium you receive will particially offset your purchase price if the option holder exercises, but if the stock falls dramatically, you will end up buying the stock well above its market value

and could be facing a huge paper loss.

If you do not wish to buy the stock in the open market after the holder chooses to exercise, you could instead choose to buy the same option contract back in the open market and "close out" your option position. You can also "close out" your option position at any time before somebody chooses to exercise.

When you write puts, your maximum profit is limited to the premium you are credited with. Your maxmium loss is the strike price of the stock X 100 for each contract you write minus the premium you received when writing the option.

If you are slightly to moderately bullish on Newmont Mining (NEM) and the stock is $54, you can write put options based on the amount of stock you can afford to purchase at $54. Meaning, if you have over $54,000 in your account and can afford to purchase 1,000 shares of NEM, you can afford to write 10 NEM put contracts.

At the time of this report, NEM is trading for $54 and NEM's June $52.50 put option is trading for $0.96 per contract. If you write 10 of these contracts, your account will be credited with $960. If NEM is trading at $52.50 or above on its June 17th expiration date, the option will expire worthless and that $960 you were credited with will be your profit.

However, if NEM declines to $50 on June 17th, the put option you wrote will be $2.50 "in the money". The option holder will most likely decide to exercise the option and you will have a choice of either buying 1,000 shares of NEM at $52.50, a cost of $52,500, or you can "close out" the option by the end of trading on June 17th, by buying back those 10 contracts at $2.50 per contract, a cost of $2,500, and a loss of $1,540.

You can also **write naked call options** when you are bearish on a stock, but this will expose you to unlimited potential losses.

Let's say you are bearish on stock UWV, which is currently $32 per share. Let's say it is May, and you believe come January of next year, you believe the stock will be trading $30 or lower.

If the January 2012 $30 call option for UWV costs $5, you can write 10 call options and your account will be credited with $5,000. If come the third Friday of January 2012 UWV is trading at $30 or lower, the option you wrote will expire worthless and you will profit the $5,000 premium you received when you wrote it.

If come the third Friday of January 2012 UWV is trading at $35, the option you wrote will be $5 "in the money" and you will be "called out". You will be required to buy 1,000 shares of UWV in the open market at $35 and sell these shares of the option holder at $30, realizing a loss on the trade of $5,000, but breaking even once you include the premium you received when writing the option.

The danger comes if UWV makes a very large move to the upside and come the third Friday of January 2012 UWV is trading at $50. In this scenario, the option you wrote will be $20 "in the money" and you will be "called out". You will be required to buy 1,000 shares of UWV in the open market at $50 and sell these shares of the option holder at $30, realizing a loss on the trade of $20,000, or a loss of $15,000 after you include the premium you received when writing the option.

Another strategy you can implement is **writing covered call options,** by buying shares in the stock at the same time you write the call option. A covered call is for somebody who is somewhat bullish on a stock, but believes it is unlikely to move much before the expiration date.

Let's use the same example as above and say UWV was $32 per share and you wrote 10 January 2012 $30 call options at a premium of $5 and were credited $5,000 in your account. But let's also say you purchased 1,000 shares of UWV in the market at $32 at the same time, for an investment of $32,000.

Come expiration if UWV is trading at $29, the option you wrote will expire worthless and you will keep the $5,000 you earned, while being down $3,000 on the stock you bought on paper. Overall, you will be making a profit of $2,000.

Come expiration if UWV is trading at $35, you will be "called out" and simply sell to the option holder the 1,000 shares you already owned at a price of $30. Being that you paid $32 for the stock that you sold for $30, you will lose $2,000 on the trade, but overall with the $5,000 premium you received, you will be making a profit of $3,000.

In the example above, by writing covered calls, you would've been able to make money with the stock both increasing and decreasing by small amounts. Covered calls are a great way to earn additional income without much risk.

NIA's favorite free web site for researching and getting

quotes on stocks and options is **Yahoo! Finance,** located at: http://finance.yahoo.com

At Yahoo! Finance, you can type in any stock symbol and get a quote on that stock. If the stock you lookup has options available, you can lookup its latest options prices by clicking on "Options" from the leftside menu that has a blue background. From there, you can choose the month of expiration near the top, and underneath it will explain the available call options followed by the available put options for that month.

The **"ask"** is the price that you can currently buy that option contract at. The **"bid"** is the price that you can currently sell that option contract at. The "vol" or **volume** is the total number of contracts that particular option traded during the past trading day. The "open int" or **open interest** is the amount of open contracts people currently own in that option. Generally, the greater the open interest, the more **investor interest** there is in that option.

NIA prefers options with greater open interest, higher volume, and smaller **spreads** between in the bid/ask, because this indicates those options contracts are very **liquid** and will be **easier to buy/sell** in the future. If you notice very large spreads between the bid/ask and see no open interest in that options contract, you might want to **avoid** that option, as it might be very **difficult** to buy and sell it.

MSN is another great site for options prices. Simply go to: http://money.msn.com/investing/ and type in the symbol of the stock and click "get quote". Afterwards, click on "options" and up will come all of its latest options prices. You can very easily toggle between the expiration months by clicking on the links near the top of the price table.

After suggesting January 2011 SLV $20 put options in February of 2010 that **gained by 1,002%** in less than 11 months, NIA has announced two more options plays.

In October of 2010, NIA announced that we liked **Moody's (MCO)** January 2011 $25 put options. They ended up **expiring worthless.** 80% of options expire worthless. No matter what, NIA is going to sometimes have some options picks that expire worthless.

In January of 2011, NIA announced that we liked **Ford (F)** June $17 put options at $1.15. This option reached a high on March 11th of $3.25 for a **gain of 183%**.

All together if we average together the **1,002%** and **183%** gains of our SLV and F options at their highs respectively together with a **100%** loss for our MCO option, which expired worthless, NIA's average options pick made a **gain of 362%**.