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Defining Option Spreads



Toronto Stock Exchange | TSX Venture Exchange | **Montréal Exchange** | Natural Gas Exchange | Montréal Climate Exchange | Boston Options Exchange

Canadian Derivatives Clearing Corporation | TMX Datalinx | Equicom | PC Bond | Shorcan

What is an Option Spread?



- Simultaneous purchase and sale of options
- Different expiration months, strike prices or both.
- Same underlying asset.



What is an Option Spread?



- Each option position is a leg.
 - Simple spreads (vertical, horizontal, etc.)
 - 2 legs
 - Complex spreads (butterflies, condors, etc)
 - 3 or more legs



Types of Spreads



Spread	Expiration Month	Strike Price
Vertical	Same	Different
Horizontal	Different	Same
Diagonal	Different	Different



Credit vs Debit Spreads



- Credit Spread
 - Option sold $>$ option purchased
- Debit Spread
 - Options sold $<$ option purchased



Credit vs Debit Spreads



	Credit Spread	Debit Spread
Objective	Generate cash flow	Profit from a directional move
Market Condition	Neutral or directional	Directional
Risk	(Difference between the strike prices) – Net premium received	Debit (Net premium paid)
Profit Potential	Credit (Net premium received)	(Difference between the strike prices) – Net premium paid



Vertical Spreads



- Purchase and sale of either calls or puts
- Same expiration month
- Different strike prices



Vertical Spreads



Strategy	Market Outlook	Debit/Credit
Bull Call Spread	Bullish	Debit
Bear Call Spread	Bearish	Credit
Bull Put Spread	Bullish	Credit
Bear Put Spread	Bearish	Debit



Vertical Spreads



- Vertical Credit Spreads
 - **Long** call/put with **higher** strike price
 - **Short** call/put with **lower** strike price

- Vertical Debit Spreads
 - **Long** call/put with **lower** strike price
 - **Short** call/put with **higher** strike price



Horizontal Spreads



- Also referred to as 'Time spreads' or 'Calendar spreads'
- Purchase and sale of either calls or puts
- Different expiration months
- Same strike price



Horizontal Spreads



- Calendar Spreads
 - **Short near-term call/put**
 - **Long long-term call/put**

- Reverse Calendar Spreads
 - **Long near-term call/put**
 - **Selling long-term call/put**



Diagonal Spreads



- Combination of a vertical and horizontal spread.
- Purchase and sale of either calls or puts
- Different expiration months
- Different strike prices



