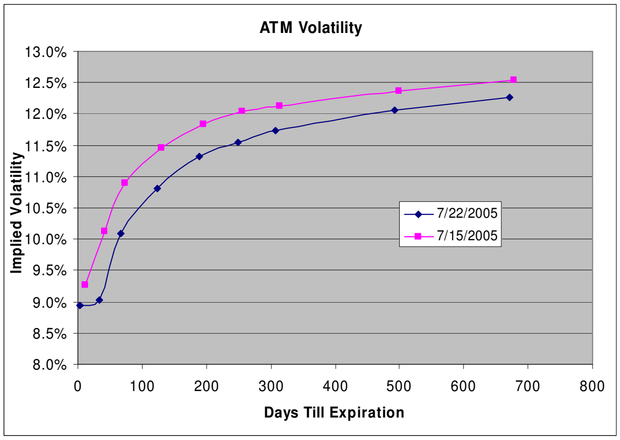
Ari Pine
Derivatives Research & Trading

24 July 2005

Gold Options Weekly Review



Past Week Review

Overall, last week was very quiet. Implieds moved down on Monday with only a little follow through for the rest of the week. The December ATM straddle traded 21.5 on Monday and 20.9 on Friday (different strikes). Paper selling the Oct 425 straddle at 15 (10%) on Monday led the way down. The August 425 straddle traded as low as 2.2 on legs with still two full trading days left.

Next Week

Now that Greenspan has made clear his concerns on home prices, real estate statistics have become more important. This week existing home sales is released Monday and new home sales on Wednesday. GDP is out Friday. August options expire Tuesday after the close.

Market Observations and Trade Ideas

There is no need to break out the volatility cone again. Everything is solidly in the cheaper than one standard deviation zone, even September implied volatility.

Ignore model inputs, i.e., implied volatility, to look at the dollar price of the September ATM straddle. It is priced at about $9.5. There are 33 calendar days remaining and about 24 trading days remaining. This actually falls into the category of a “move that can be made in one day.”

Consider that examining rolling 24 trading day periods shows that futures move from the prior day close (prior to the period examined) more than $9.5 over 82% of the time. On average, gold futures move just over $17 from the closing price of the start of the period to the ultimate maximum distance.

Table 1 highlights the results. The data uses December 2005 futures from 8 January 2001 and examines rolling 24 trading day periods. The numbers reflect the maximum distance from the prior day closing price to any of the period’s closing prices. For example, the prior day closing price is $400 and during the 24 trading days, the minimum closing price is $393 and the maximum closing price is $403. The maximum distance is $7.

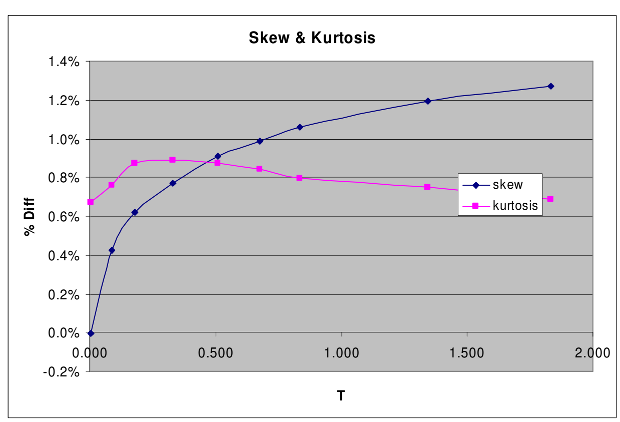
Table 1:

	2001 Onward	2005
%’age of times distance > 9.5	82.3%	94.2%
Avg Max Distance	17.1	17.3
Median Max Dist	16.2	16.4
Max Max Dist	44.5	37.8
Min Max Dist	3.6	7.3
Std Dev Max Dist	7.8	6.4

To make sure that the results were not biased toward prior years’ volatility levels, the experiment was run again on data from the start of 2005. The results are shown in the second data column of Table 1.

One can see from Table 1 is that it is a horrible risk to sell a 24 trading day straddle at $9.5. It is a losing trade over 82% of the time and, in 2005, over 94% of the time. On average, futures move over $17 from its starting point. The minimum movement has been $3.6 representing a risk of $5.9 to the trade (paying $9.5); for 2005 the minimum has been $7.3 or a risk of $2.2. On the other hand, the profit can be in excess of $25 when the futures move $35 or more from its starting point. One can see the upward skew in the distribution by noting that the maximum distance is greater than $9.5 82% of the time, but that the standard deviation of 7.8 indicates that only 67% of the time would the movement be over $9.3 (17.1 – 7.8).

The clear conclusion is that the September 425 straddle is very cheap at $9.5 or under.



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Contact Info:

Ari Pine
(516) 690-1904
aripine@optonline.net

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