

Multi-Act Technical Desk

Options for **yield enhancement**

The core objective of a fundamentally strong long-term portfolio is to generate potential long-term alpha. However, in our quest for long-term gains, we sometimes overlook intermittent opportunities for enhancing overall returns. In that regard, select option strategies can be used to enhance the income from stocks that are already in the portfolio.

Two such strategies are:

Covered Calls

Cash Covered Puts

Covered Calls

This is a popular option writing strategy that is used to generate income in the form of options premium by using calls.

Strategy

Write (sell) out-of-the-money call options on stocks that are already a part of the investment portfolio.

Prerequisite

Investors should be holding the stock in the portfolio.

Expectation

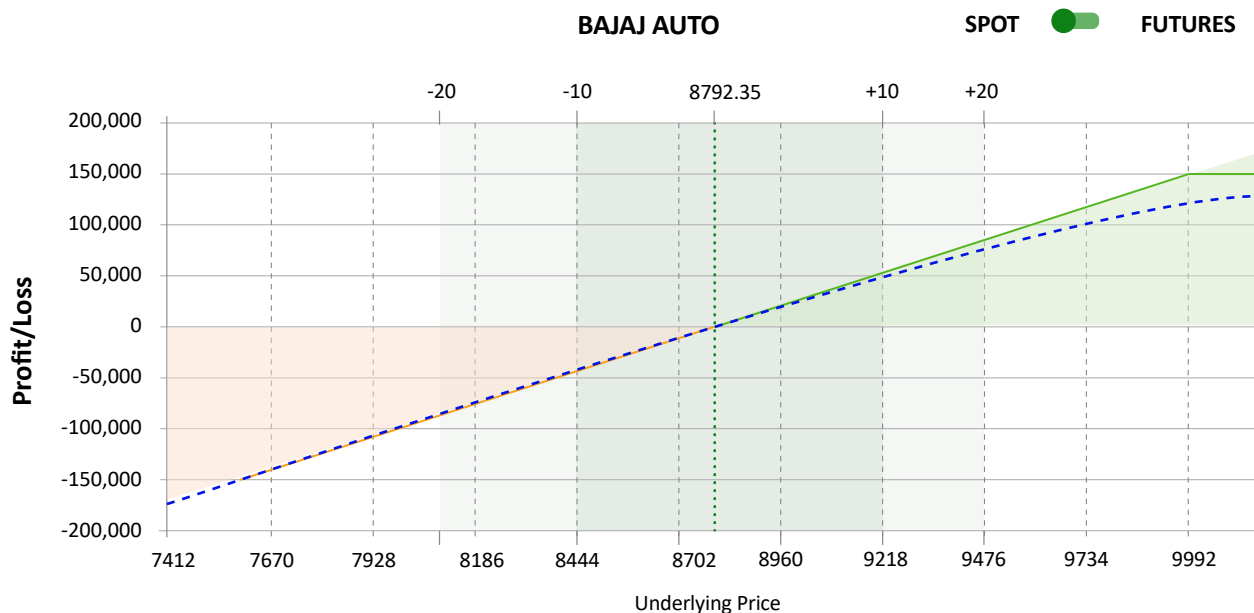
This strategy is ideal for an investor who believes that the underlying price will not move much over the near-term but wants to convert that belief into regular income by writing out of the money options.

How does it work?

When you write an out-of-the-money call option you earn the premium amount and profit as long as the price of the underlying does not rise above the strike price of the call option.

Take the example of Bajaj Auto Ltd. Call written at strike price of 10,000 (premium INR 26 per share, lot size 125).

Exhibit: Bajaj Auto Strategy Pay-off



The payoff diagram shows the profit and loss breakeven. If the stock crosses 10,026 (10,000+26) then the profits are constant since the gain in the stock is offset by the loss in the call option position. If the stock stays below 10,000 then the investor would earn the full premium amount of INR 26 per share.

This strategy can consistently generate good income on the stocks already in the portfolio.

Exhibit: Call writing on Varun Beverages (Recommended to clients between January 2025 to May 2025)

Reco date	Expiry date	Call / Put	Strike Price	Stock Price (₹)	Strike Price Away from CMP [^]	Premium per share	Initial Yield (monthly)	Stock Price (₹)	Strike Price Away from CMP [^]	Realised yield on margin
30 JAN 2025	27 FEB 2025	Call	690	540.6	27.64%	1.5	0.97%	448.3	-17.07%	0.97%
27 FEB 2025	27 MAR 2025	Call	540	448.3	20.46%	1.95	1.60%	536.3	19.63%	1.60%
27 MAR 2025	24 APR 2025	Call	620	536.3	15.61%	2.8	2.01%	532.3	-0.74%	2.01%
24 APR 2025	28 MAY 2025	Call	640	532.3	20.22%	3.55	2.47%	483.9	-9.10%	2.47%
28 MAY 2025	26 JUN 2025	Call	570	483.9	17.79%	1.4	1.09%	458.4	-5.27%	1.09%

Note: Margin assumed 22.5% of contract value. | [^]CMP - Current Market Price

Cash Covered Puts

This is a popular option writing strategy that is used to generate income in the form of options premium by using puts.

Strategy

Write (sell) out-of-the-money put options on stocks that you would like to own at a future date but at a lower price.

Expectation

This strategy is ideal for an investor who wants to buy the underlying stock, but expects that he will be able to buy it at a lower price in the near future.

How does it work?

An investor who sells put options in securities they want to own will either earn income (if the put option expires worthless) or buy the stock at a desired price minus the premium earned (in case the option is exercised). In case the stock falls below the strike price, the investor intending to own the stock can convert the option position to take delivery of the shares, or if they have changed their mind about owning the stock, they can choose to exit the position (most likely at a loss).

Take the example of Kotak Bank. If the investor wants to buy Kotak Bank at 1550, the investor will write put options of strike price 1550 (premium collected 8.9). If the stock stays above 1550 then the profit per share is the premium collected. If the stock falls below 1550 then the investor buys the stock at 1550 as it was intended. The effective cost price would be 1541.1 (1550-8.9).

Exhibit: Kotak Bank Strategy Pay-off

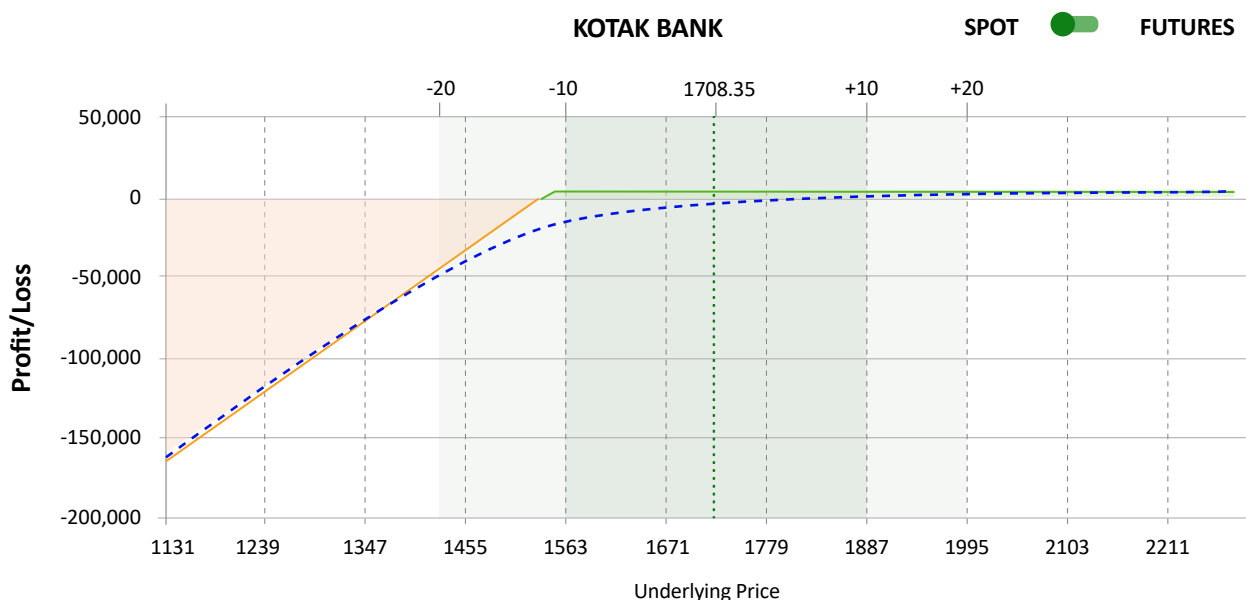


Exhibit: Put writing on Dabur Limited (Recommended to clients between November 2024 to May 2025)

Reco date	Expiry date	Call / Put	Strike Price	Stock Price (₹)	Strike Price Away from CMP [^]	Premium per share	Initial Yield (monthly)	Stock Price (₹)	Strike Price Away from CMP [^]	Realised yield on margin
28 NOV 2024	26 DEC 2024	Put	480	526	-8.75%	1.3	1.20%	505.6	-3.88%	1.20%
26 DEC 2024	30 JAN 2025	Put	480	505.6	-5.06%	1.35	1.25%	533.7	5.56%	1.25%
30 JAN 2025	27 FEB 2025	Put	460	533.7	-13.81%	1.15	1.11%	503.2	-5.71%	1.11%
27 FEB 2025	27 MAR 2025	Put	450	503.2	-10.58%	1.1	1.09%	512.8	1.91%	1.09%
27 MAR 2025	24 APR 2025	Put	460	512.8	-10.31%	1.2	1.16%	491.7	-4.12%	1.16%
24 APR 2025	29 MAY 2025	Put	420	491.7	-14.58%	1.1	1.16%	482.1	-1.95%	1.16%
29 MAY 2025	26 JUN 2025	Put	440	482.1	-8.73%	1.1	1.11%	481.5	-0.11%	1.11%

Note: Margin assumed 22.5% of contract value. | [^]CMP - Current Market Price

Selecting the right stock

Covered call and covered put strategies are well-established in options trading, but their effectiveness depends heavily on stock selection. The key questions to consider are:

Which stocks in the portfolio appear overvalued and are therefore suitable candidates for a covered call?

Which stocks would be attractive additions at lower levels, making them ideal for a covered put?

At Multi-Act, these decisions are anchored in its proprietary fundamental analysis framework. The probability of success in an option writing strategy can be meaningfully improved by:

Assessing whether a stock is trading closer to its valuation high or low

Using times of higher volatility to write more options in a counter-cyclical fashion

Integrating technical analysis to add an additional layer of conviction

These inputs feed into a structured grid developed for Multi-Act's F&O advisory. The grid serves as a practical guide across market cycles and is designed to complement and augment overall equity portfolio outcomes.

Exhibit : F&O Strategy for stocks

	F&O Strategy for Stock	Market Volatility (Type of Trade)			Suggestive Price Range	
		High	Moderate	Low	Cyclical/Momentum	HQ Stocks
Market Valuations	Expensive/Very Expensive	Call writing on Cyclical-Momentum stocks with high premiums		Pro-active Call Writing @ premiums of 12-24% p.a.	Above EBV high end	Near 2 times Mid-band
	Moderately Expensive		Covered Call and Puts on Large Caps / Rangebound Stocks.		Call: Above EBV mid-band Put: Near EBV low-end	Call: Above EBV high end Put: Near EBV mid-band
	Cheap/Reasonable	Puts on HQ Stocks @ premiums of 12-24% p.a.		Puts on Cyclical-Momentum, high beta stocks with high premium	Put at ~50% discount to Mid-band	Near EBV low-end

EBV = Economic Business Value

The call and put writing would be taken for the stocks in portfolio and trade for a particular stock would be limited to ~1/3rd of the total holding in that stock unless the trade suggestion is for portfolio optimisation. This is to limit the impact on the overall portfolio if the client chooses to settle by a delivery settlement. However, the advisory team may suggest a higher Notional Value for certain stocks considering its weightage in portfolio, quality, and other metrics. The trades would be taken for earning premium income. In some cases, the trades could be for portfolio optimisation (adding/exiting positions).

Return Expectations – What does the yield look like?

Particulars	Amount in Rs.	% of total portfolio	Comments
Total Portfolio	10,00,000	100%	
Direct equity exposure	3,00,000	30%	
Derivative exposure to be taken	1,00,000	10%	1/3 of direct exposure
Margin money required	22,500	2.25%	22.5% of the national value
Return earned on Margin	337.50		~1.5% per month
Annual return	4,050		
Annual Return as a % on Margin money	18.00%		
Annual Return as a % on Derivative exposure	4.05%		
Annual Return as a % on Direct equity exposure	1.35%		
Annual Return as a % on Direct equity exposure	0.41%		

- In the above example, derivative exposure to be taken is 1/3rd of direct equity exposure i.e. 10% of total portfolio exposure given that direct equity exposure is 30% of total portfolio.
- For this derivative exposure, margin money required is ~ 22.5% of derivative exposure / notional value i.e. ~2.3% of total portfolio exposure which can be done in the form of cash or pledge of stock holdings/liquid bees.
- Assuming a 1.5% return per month on the margin money, an investor earns ~ 4% p.a. on derivative exposure or in other words ~ 1.4% p.a. on direct equity exposure thereby enhancing the overall equity returns.

Approach with some caution

It is well-known that risk and return are the two sides of the same investment coin. Which is why, this narrative is incomplete without a discussion on risk. Inarguably, risk is minimised due to the valuation layer added to the above two strategies. However, on an overall basis, investors must be cognisant of the risks of F&O trading, especially in day trading. In general, day trading is fraught with risk and should be avoided. Further, when it comes to options trading, investors must seek to mitigate risks that might stem from illiquid contracts, volatility, and margin calls. Thus, it is always best to establish a robust process and clear rational before trading in options – this helps to mitigate risks and potentially optimise returns.

Statutory Details: Multi-Act Trade and Investments Private Limited ("MATI") (SEBI Registered Investment Adviser – Registration No. INA000008589 and BASL Membership ID:- 1398)

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