

# CONTENTS

Acknowledgments	xi
<b>Introduction</b>	<b>xiii</b>
<b>Part I: Options for the Intelligent Investor</b>	<b>1</b>
Chapter 1: Option Fundamentals	3
Characteristics and History	4
Directionality	9
Flexibility	20
Chapter 2: The Black-Scholes-Merton Model	29
The BSM's Main Job is to Predict Stock Prices	30
The BSM is Lousy at Its Main Job	39
Chapter 3: The Intelligent Investor's Guide to Option Pricing	49
How Option Prices are Determined	50
Time Value versus Intrinsic Value	56
How Changing Market Conditions Affect Option Prices	59
<b>Part II: A Sound Intellectual Framework for Assessing Value</b>	<b>75</b>
Chapter 4: The Golden Rule of Valuation	77
The Value of an Asset	78
Cash Flows Generated on Behalf of Owners	80
The Company's Economic Life	82
Time Value of Money: Summing Up Cash Flows Over Time	87
Chapter 5: The Four Drivers of Value	91
Bird's Eye View of the Valuation Process	91
A Detailed Look at the Drivers of Value	97

Chapter 6: Understanding and Overcoming Investing Pitfalls	113
Behavioral Biases	114
Structural Impediments	131
<b>Part III: Intelligent Option Investing</b>	<b>141</b>
Chapter 7: Finding Mispriced Options	143
Making Sense of Option Quotes	144
Delta: The Most Useful of the Greeks	151
Comparing an Intelligent Valuation Range with a BSM Range	155
Chapter 8: Understanding and Managing Leverage	163
Investment Leverage	164
Simple Ways of Measuring Option Investment Leverage	169
Understanding Leverage's Effects on a Portfolio	174
Managing Leverage	183
Chapter 9: Gaining Exposure	187
Long Call	189
Long Put	201
Strangle	205
Straddle	208
Chapter 10: Accepting Exposure	211
Short Put	212
Short Call (Call Spread)	220
Short Straddle/Short Strangle	230
Chapter 11: Mixing Exposure	233
Long Diagonal	235
Short Diagonal	238
Covered Call	240
Protective Puts	248
Collar	258
Chapter 12: Risk and the Intelligent Option Investor	263
Market Risk	263
Valuation Risk	265
Intelligent Option Investing	267

Appendix A: Choose Your Battles Wisely	269
Where the BSM Works Best	269
Where the BSM Works Worst	273
Appendix B: The Many Faces of Leverage	282
Operational Leverage	282
Financial Leverage	285
Appendix C: Put-Call Parity	287
Dividend Arbitrage and Put-Call Parity	288
<i>Notes</i>	<b>295</b>
<i>Index</i>	<b>305</b>