Basic Diagonal Spread Rules

This strategy is typically applied once you have determined there is a long term Bullish Trade.

The Main Driver

1. Find a long term bullish opportunity
2. Assess the chart and determine how much time you feel the trade will need to develop over the long term.
3. Be liberal on the amount of time you purchase but try not to go out to far beyond 6 months.
4. Buy an .80 delta call or whatever option is closest to the .80 delta as the basis of your trade. “This should increase in value as the stock moves up.”

The Hedge

1. Assess the chart again for a shorter time frame. “Typically 30 days” use some technical analysis to determine a reasonable potential move for that shorter time frame.
2. Once you have assessed the chart for a shorter movement go to the Option Chain and see what’s available there. We usually won’t be interested in a Call Option that pays us less than .20 cents per share.
3. This is The Call Option we sell; this should bring in Premium and help offset the remaining time decay on the Option we purchased.
4. When you put these two positons together realize that the Hedge is limiting the Driver, at this point we want to make sure that if the Stock goes beyond our hedge in the 30 day time frame we are able to at least make a 25% return on our investment in case we decide to exit the trade at this point.