

The Disciplined Investor Podcast – Guest Interview Summary

Guest: Larry McMillan

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Quick recap

Larry McMillan shared his journey from programming to options trading, discussing his early experiences, career transitions, and the development of his influential book. He explained his daily trading routine, strategies for various market conditions, and insights on indicators like the VIX index and put-call ratio. Larry also discussed high-dividend ETFs that use options strategies, providing examples and highlighting their potential benefits as alternative investment vehicles.

Summary

Larry's Journey Into Options Trading

Andrew and Larry discussed Larry's journey into options trading, which began with a book on convertible arbitrage during his graduate studies at the University of Colorado. Larry mentioned his early exposure to derivatives and his subsequent work at Bell Labs as a programmer, where he used the Bell Labs computer for advanced modeling. He later transitioned to Wall Street, working as an option strategist at Thompson McKinnon, where he had to manually calculate and type in pricing data from the Wall Street Journal due to limited options liquidity at the time.

Larry's Trading and Options Journey

Larry discussed his career transition from programming to trading, highlighting his early experiences with options trading and his development of option strategies. He explained how his book "Options as a Strategic Investment" came about after being approached by the New York Institute of Finance, which led to a successful and enduring publication. Larry reflected on his career trajectory, noting that while programming was theoretically valuable, trading offered more practical opportunities at the time, eventually leading to lucrative work on Wall Street.

Trading Strategies and Market Analysis

Larry explained his daily trading routine, which involves analyzing theoretical values, straddle buying opportunities, and put call ratios. He emphasized the importance of indicators that other traders are watching, as these can become self-fulfilling prophecies. Larry also discussed his approach to options on futures, noting the challenges of timing differences between futures and options markets. Andrew expressed concerns about the anxiety of trading overnight and the potential for sleep disturbances.

VIX Trading Strategy Discussion

Andrew and Larry discussed the VIX index, noting its seasonal low in July and the current low level of 17. Larry advised that while low VIX levels are not a signal to sell, traders should watch for an increase above the 200-day moving average as a potential sell signal. They explored trading strategies, with Larry recommending staying short-term and going 33% out of the money for VIX options. Andrew and Larry agreed that while current implied volatility across sectors is relatively low, they would monitor for any unusual patterns.

Put-Call Ratio Trading Insights

Larry explained the put-call ratio as an indicator, invented by Marty Zweig in the 1950s, which measures the volume and price of put and call options to gauge market sentiment. He emphasized the importance of using dollar-weighted calculations for more accurate readings and highlighted how extreme put-call ratios can signal buying opportunities in stocks like Apple. Larry also shared his approach to trading earnings using historical data from Options Slam.com and noted that current market indicators, including low put-call ratios and new highs versus lows, suggest potential upside.

High-Dividend ETF Option Strategies

Larry explained the mechanics and benefits of high-dividend ETFs that use options, such as covered calls and credit spreads, to provide income while limiting downside risk. He highlighted examples like the MicroStrategy and Nvidia ETFs, noting that some, like MicroStrategy, have paid their entire price as dividends in 16 months. Andrew expressed interest in these products as an alternative to direct option strategies, emphasizing the importance of believing in the underlying assets. Larry also mentioned a Morgan Stanley ETF, JEP, which he found underperforming, and Andrew shared his experience with a VIX option trade.