AIE Private Wealth Lite Strategy

Information Sheet

Introducing the "Private Wealth Lite" Strategy from AIE

This strategy is designed to be an “All Weather” strategy in that it trades multiple non correlated Exchange Traded Funds on Equities, Gold and Bonds utilising XSP, GLD and TLT.

Trading XSP (S&P 500 Index ETF), TLT (iShares 20+ Year Treasury Bond ETF), and GLD (SPDR Gold Shares ETF) as a portfolio can offer several benefits due to their diverse characteristics and the correlation between these assets. Here's an explanation of the benefits:

1. Diversification

Diversification is the primary benefit of including XSP, TLT, and GLD in a portfolio. By holding a mix of these ETFs, investors can reduce the overall risk of their portfolio.

- **XSP (Equities)**: XSP represents the S&P 500 index, giving exposure to U.S. large-cap equities. Equities generally offer higher returns but come with higher risk and volatility.
- **TLT (Treasury Bonds)**: TLT provides exposure to long-term U.S. Treasury bonds. These bonds are considered low-risk and tend to have an inverse relationship with equities, especially during market downturns.
- **GLD (Gold)**: GLD tracks the price of gold, a traditional safe-haven asset. Gold often performs well during periods of economic uncertainty or inflation.

2. Negative Correlation and Hedging

The correlations among these assets often provide a natural hedge.

- **XSP vs. TLT**: Historically, stocks and long-term bonds tend to be negatively correlated. When stock prices fall (e.g., during a recession), bond prices often rise as investors seek safer investments. This negative correlation helps mitigate losses in a portfolio.
- **XSP vs. GLD**: Gold is also generally negatively correlated with equities. In times of economic distress, gold prices often increase as investors look for a store of value. This provides another layer of protection for the portfolio.
- **TLT vs. GLD**: While TLT and GLD may not always have a strong negative correlation, they serve different purposes. TLT provides income and stability, while GLD offers protection against inflation and currency devaluation.

3. Risk Management

Including assets with different risk profiles helps in managing the overall risk of the portfolio.

- **XSP**: Higher risk, higher potential return.
- **TLT**: Lower risk, provides steady income and acts as a stabilizer during market downturns.
- **GLD**: Acts as a hedge against economic uncertainty and inflation, providing protection during times when both equities and bonds might underperform.

4. Improved Risk-Adjusted Returns

By combining XSP, TLT, and GLD, investors can potentially achieve better risk-adjusted returns. This means achieving a favourable balance between the return and the risk taken to achieve those returns.

5. Reduced Volatility

A portfolio composed of XSP, TLT, and GLD tends to have lower volatility compared to a portfolio consisting solely of equities. This is due to the negative or low correlations between these asset classes, which smooths out the performance of the portfolio over time.

6. Flexibility in Economic Cycles

This portfolio can perform relatively well across different economic cycles:

- **Economic Growth**: XSP is likely to perform well as corporate earnings grow.
- **Economic Downturn**: TLT and GLD provide safety and can perform well when equities are declining.
- **Inflation**: GLD acts as a hedge against inflation, maintaining value when purchasing power declines.

Example of Correlations (Hypothetical Data):

- **XSP and TLT**: -0.3 (negative correlation)
- **XSP and GLD**: -0.2 (negative correlation)
- **TLT and GLD**: 0.1 (low correlation)

In summary, trading XSP, TLT, and GLD ETFs as a portfolio offers the benefits of diversification, reduced risk through negative correlations, improved risk-adjusted returns, lower volatility, and flexibility to perform across various economic conditions. This balanced approach helps investors achieve more stable returns and manage risk more effectively.

The Private Wealth Lite Strategy for XSP, GLD, and TLT

With the Private Wealth Lite Strategy, you can sell options on the S&P 500 Mini Cash Index (XSP), SPDR Gold Shares ETF (GLD), and the iShares 20+ Year Treasury Bond ETF (TLT) to receive a weekly premium of around 1% or more on the face value of each position. This guide will walk you through the concept of options selling and show you how to consistently receive a weekly premium throughout the year.

Understanding XSP

The S&P 500 Mini Cash Index (XSP) is an options contract that represents a fraction of the standard S&P 500 Index options (SPX). Specifically, XSP options are based on 1/10th the value of the S&P 500 Index, making them more accessible for individual investors and smaller portfolio managers. These options are European-style, meaning they can only be exercised at expiration, and they are cash-settled, meaning there is no delivery of the underlying asset upon expiration. Instead, the difference between the strike price and the final index value is settled in cash.

Understanding GLD

SPDR Gold Shares ETF (GLD) is one of the most popular ETFs designed to track the price of gold. GLD provides investors with a cost-effective and convenient way to access the gold market, offering exposure to the price of gold without the need to physically own and store the metal. Here are some key characteristics of GLD options:

- **Physical Gold Backing**: GLD holds physical gold bullion, stored in secure vaults, which backs the shares of the ETF. This means that the price of GLD closely follows the price of gold.
- **American-Style Options**: GLD options are American-style, meaning they can be exercised at any time before expiration. This provides more flexibility compared to European-style options, which can only be exercised at expiration.
- **Deliverable**: Unlike cash-settled options, if a GLD option is exercised, it results in the delivery of GLD shares rather than a cash settlement. This allows investors to take possession of the ETF shares.

Understanding TLT

The iShares 20+ Year Treasury Bond ETF (TLT) is an ETF that aims to track the investment results of an index composed of U.S. Treasury bonds with remaining maturities greater than 20 years. TLT offers exposure to long-term U.S. Treasury bonds, providing a way to invest in government debt and benefit from interest rate movements. Here are some key characteristics of TLT options:

- **Long-Term Bond Exposure**: TLT invests in U.S. Treasury bonds with maturities of 20 years or more, making it sensitive to changes in interest rates. This can offer both income and potential for capital appreciation if interest rates fall.
- **American-Style Options**: TLT options are American-style, allowing them to be exercised at any time before expiration. This flexibility can be advantageous for strategic option trades.
- **Deliverable**: Similar to GLD, TLT options result in the delivery of TLT shares upon exercise, rather than a cash settlement. This means investors can take possession of the ETF shares if the options are exercised.

How Does the Private Wealth Lite Strategy Work?

The strategy involves the following steps:

1. **Selling Delta 0.5 Puts on XSP:**
    - Start by selling put options with a delta of approximately 0.5, typically with 2-4 days to expiry.
    - Delta measures the sensitivity of the option's price to the underlying asset's price movements. A delta of 0.5 indicates that the option has a roughly 50% chance of finishing in the money (ITM).
2. **Selling Delta 0.5 Puts on GLD and TLT:**
    - Similarly, sell put options with a delta of approximately 0.5 for GLD and TLT.
    - If these options are assigned (i.e., the puts are exercised and you acquire the underlying assets), you then sell call options with a delta of approximately 0.3 against the positions until the calls are exercised.
3. **Managing ITM Options:**
    - If these options expire out of the money (OTM), you keep the premium and start the process again.
    - If these options finish in the money (ITM), for XSP they are cash-settled and you would then sell delta 0.7 puts for the next expiry until they finish OTM. For GLD and TLT, you will receive the underlying assets and then proceed to sell delta 0.3 calls against the positions.
4. **Returning to Selling Delta 0.5 Puts:**
    - Continue selling delta 0.7 put options on XSP until they expire worthless, then resume selling delta 0.5 puts on XSP.
    - Continue selling delta 0.3 calls on GLD and TLT until they are exercised.
    - Once the calls are exercised, resume selling delta 0.5 puts on GLD and TLT.

Benefits of the Private Wealth Lite Strategy

- **Weekly Premiums:**
    - Consistently receive premiums that can amount to 1% or more of the underlying value on a weekly basis.
- **No Assignment Risk for XSP:**
    - Since XSP options are European-style and cash-settled, there is no risk of being assigned and having to manage the underlying asset. This simplifies the strategy and focuses on cash management.
- **Downside Protection:**
    - Selling puts can provide some downside protection compared to outright ownership of the underlying asset. The extrinsic value, or time value, captured from selling options can help cushion against losses.

Example Scenario: Bullish Market

1. **Initial Put Sale:**
    - Sell delta 0.5 puts on XSP with a strike price close to the current market price. For example, if XSP is trading at $550, sell a put option with a strike price of $550.
    - Collect a premium of ~$4.25 per share.
2. **Cash Settlement:**

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  - If XSP stays above $550, the option expires worthless, and you keep the premium.
  - If XSP drops below $550, the option is cash-settled. For example, if XSP settles at $544.25, you pay $5.75 per share (the difference between the strike price and the settlement price) but still keep the initial premium of ~$4.25.
3. **Selling Delta 0.5 Puts on GLD and TLT:**
  - Sell delta 0.5 puts on GLD and TLT with strike prices close to their current market prices.
  - If assigned, you acquire the underlying assets.
4. **Selling Delta 0.3 Calls on Assigned GLD and TLT:**
  - After acquiring GLD or TLT through assignment, start selling delta 0.3 calls against the positions.
  - Continue this until the calls are exercised, at which point you return to selling delta 0.5 puts.

Detailed Steps and Considerations

1. **Selling Delta 0.5 Puts:**
  - Delta 0.5 puts are chosen because they have a balanced risk-reward profile, with a 50% chance of being ITM at expiry, providing a good trade-off between premium received and probability of expiration.
2. **Managing ITM Options:**
  - For XSP, if the put expires ITM, it is cash-settled.
  - For GLD and TLT, if the put expires ITM, you acquire the underlying asset and then sell delta 0.3 calls against the position.
3. **Returning to Delta 0.5 Puts:**
  - For XSP, resume selling delta 0.5 puts after each expiry.
  - For GLD and TLT, sell delta 0.3 calls until exercised, then go back to selling delta 0.5 puts.

Risks and Considerations

- **Market Volatility:**
  - The strategy can be affected by sudden market movements and volatility.
  - Proper risk management is crucial to handle potential losses and maximize gains.
- **Cash Settlement Risk:**
  - Cash settlement at a lower price than the strike can result in temporary losses.
  - The strategy involves managing these settlements effectively.

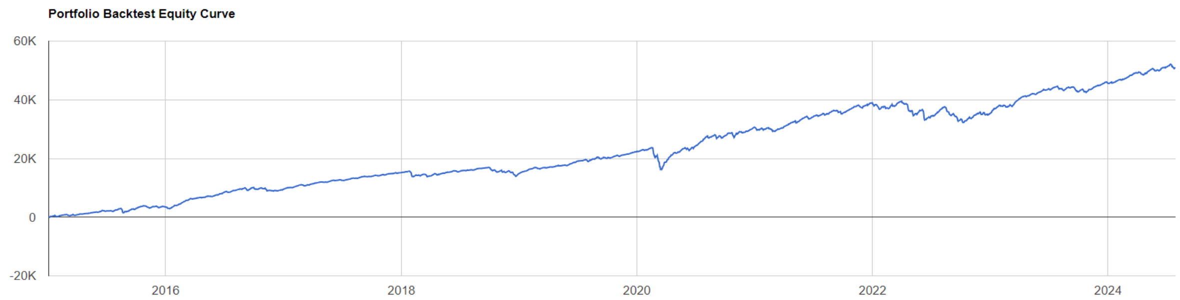
Leverage

In the context of the Private Wealth Lite Strategy, leverage can play a crucial role in enhancing returns but also increases the risk. Here's a detailed explanation of how leverage can be used in this strategy if desired:

- **Increased Premiums:**
    - Leverage allows you to control more contracts than you could with cash alone, thus increasing the total premiums you can collect.
- **Magnified Losses:**
    - While leverage can increase returns, it also magnifies losses. If the market moves against you, the losses can exceed the premiums collected.
- **Margin Calls:**
    - Sudden market movements can trigger margin calls, requiring you to deposit additional funds to maintain your positions. Failure to meet margin calls can result in the liquidation of positions at unfavourable prices.
- **Volatility Risk:**
    - Increased market volatility can lead to larger-than-expected swings in the value of the options, exacerbating the risks associated with leverage.

Return Expectations

Running a test on the combined three instruments selling one Delta 0.5 put options on a weekly basis from 2015 to August 2024 results in an equity curve that is relatively smooth in comparison to trading options on each individual market due to diversification benefits.



Holding each of the underlying assets in a portfolio results in a return of approximately 10% with an 11% std deviation over the long term. By trading options using the strategy outlined we seek to match or exceed the returns compared with holding the underlying ETFs with a lower volatility of returns compared to the underlying.

Conclusion

The Private Wealth Lite Strategy offers a systematic approach to options trading on XSP, GLD, and TLT. By following the structured process of selling delta 0.5 puts and managing positions with delta 0.3 calls or by selling in the money puts on XSP, you can generate consistent weekly income while managing risks effectively, such as the risk associated with whipsawing markets. Leverage can be utilised if desired but keep in mind leverage can enhance returns but also increases risk, requiring careful management and understanding of margin requirements and market volatility.

If you're ready to earn more from this strategy and start generating weekly income, then read the information above and start implementing the Private Wealth Lite Strategy today.

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