Choosing the Long for Poor Man's Covered Calls

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Poor Man's Covered Calls

- A *covered call* means selling a short OTM call while holding 100 shares of the underlying.
- This strategy generates additional revenue compared to holding the shares under any situation other than a sudden spike in the underlying, where it still isn't exposed to loss.
- 100 shares can be quite capital intensive however. A *poor man's covered call* (PMCC) recreates similar P/L dynamics by using an ITM long call in place of shares.
- But how do we decide what long call to use when forming a PMCC?

The study:

- Using 15 years of data in SPY options we investigated a variety of poor man’s covered calls.
- All short options sold were 45 DTE, 30Δ calls.
- For the long calls, we explored:
    - 60Δ, 70Δ, 80Δ, and 90Δ strikes with
    - the same expiration (really just a long call vertical), 60 DTE, 120 DTE, or 1 year to expiration.
    - All positions were closed when the short option expired.
- We also included “rich man’s” covered calls, the results from using 100 shares of SPY in place of the long call over the same time frame.

Choosing the Longs for PMCCs

45 DTE Long Calls	60Δ Long Calls	70Δ Long Calls	80Δ Long Calls	90Δ Long Calls	Rich Man's
Win%	65%	66%	66%	68%	71%
Avg P/L	$27	$27	$26	$26	$29
Avg. Capital Requirement	$488	$739	$1,115	$1,819	$18,052

Choosing the Longs for PMCCs

60 DTE Long Calls	60Δ Long Calls	70Δ Long Calls	80Δ Long Calls	90Δ Long Calls	Rich Man's
Win%	66%	69%	69%	69%	70%
Avg P/L	$29	$29	$27	$27	$29
Avg. Capital Requirement	$559	$845	$1,290	$2,079	$18,052

Choosing the Longs for PMCCs

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6 Month Long Calls	60Δ Long Calls	70Δ Long Calls	80Δ Long Calls	90Δ Long Calls	Rich Man's
Win%	67%	69%	69%	70%	70%
Avg P/L	$28	$28	$27	$26	$29
Avg. Capital Requirement	$1061	$1641	$2,475	$4,034	$18,052

Choosing the Longs for PMCCs

MARKET MEASURES
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1 Year Long Calls	60Δ Long Calls	70Δ Long Calls	80Δ Long Calls	90Δ Long Calls	Rich Man's
Win%	69%	69%	70%	70%	70%
Avg P/L	$27	$27	$26	$26	$29
Avg. Capital Requirement	$1,855	$2,503	$3,782	$6,180	$18,052

Choosing the Longs for PMCCs

Takeaways:

- Writing covered calls in SPY has been a generally successful strategy over the past decades.
- PMCCs were able to recreate almost all of this success while requiring vastly less capital.
- When choosing a long call to form your PMCC, it was hard to go wrong, but 70Δ and 60 DTE provided a nice balance of capital efficiency without giving up profits or reliability compared to a rich man's.
- Due to the length of the study, expect current SPY costs to be higher, but the relative differences between strikes and expirations should remain.