

Option spreads are strategies that involve holding multiple positions in options contracts of the same type (calls or puts) on the same underlying asset, but with different strike prices, expiration dates, or both. Option spreads are used primarily to manage risk by limiting potential losses. One of the primary advantages of option spreads is that they define the maximum potential loss upfront. This allows traders to know their worst-case scenario at the outset of the trade. Option spreads typically require less capital compared to outright options trading because the premiums received from selling options can offset the premiums paid for buying options.

Examples of Option Spreads:

- 1) Bull Call Spread: Maximum Profit: Achieved when the underlying asset's price is above the higher strike price. Maximum Loss: Limited to the initial net premium paid.
- 2) Bull Put Spread: Maximum Profit: Achieved when the underlying asset's price is above the higher strike price at expiration. Maximum Loss: Limited to the difference in strike prices minus the net premium received.
- 3) Bear Put Spread: Maximum Profit: Achieved when the underlying asset's price is below the lower strike price at expiration. Maximum Loss: Limited to the initial net premium paid.
- 4) Bear Call Spread: Maximum Profit: Achieved when the underlying asset's price is below the lower strike price at expiration. Maximum Loss: Limited to the difference in strike prices minus the net premium received.