



OPTIONSMART  
3-D OPTION TRADING STRATEGIES

# 3-D Research Note on HPQ



Chart courtesy of StockCharts.com

| # | Date   | Most Recent News  | Stock's Reaction |
|---|--------|---|------------------|
| 1 | 22-Sep | HPQ announced buybacks plans (The buyback would equal about 166 million shares, or 6.8 percent of the stock outstanding)  | negative         |
| 2 | 10-Oct | HPQ to expand PC manufacturing in China   | negative         |
| 3 | 14-Oct | HPQ and DELL remain the world's top producers of desktops and notebooks despite the global economic downturn (In Q3 2008, HPQ shipped nearly 14.8 mln PCs, DELL 15.1 mln) | negative         |
| 4 | 20-Oct | HPQ launched Eco-Friendly Consumer PCs with energy-efficient AMD processors, ship in 100% recyclable packaging, and use 45% less energy compared with other HP desktops   | positive         |
| 5 | 21-Oct | HPQ and VOD to launch two new smartphones in Europe   | -                |

**OUR RECOMMENDATION: STRONG BUY**

**RECOMMENDED TRADING VEHICLE:**

Bullish Debit Call Spread

Buy to Open HPQAG HPQ Jan9 35 Call IV 55.0 Delta .769

Sell to Open HPQAU HPQ Jan9 37.5 Call IV 51.8 Delta .689

Debit 2.00

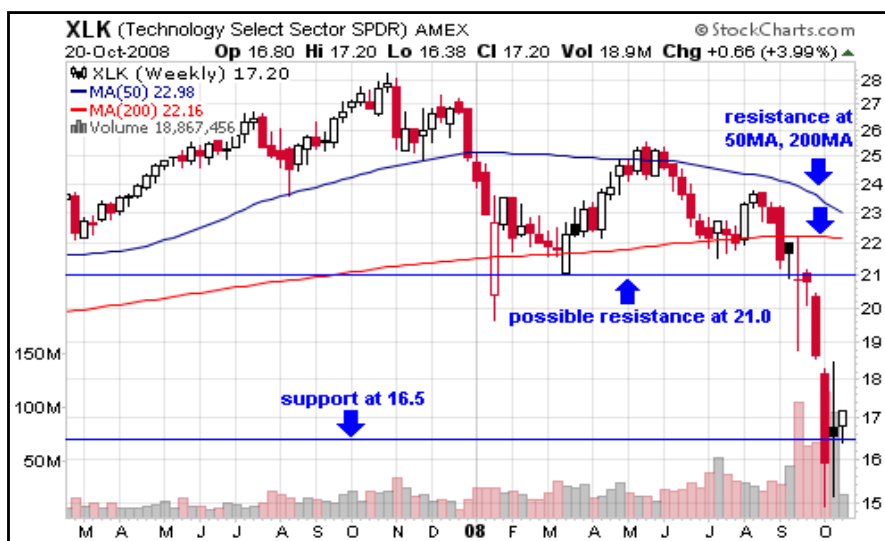
Position Net Delta .080

Max Gain .50

Max Risk 2.00

Target Credit 2.30

## WEEKLY CHART



| Key sector components             | Fundamentals  |
|-----------------------------------|---|
| APPLE INC. ( <b>AAPL</b> )        | Trailing P/E (19); Forward P/E (17); PEG Ratio (0.85); EPS Trends- mixed        |
| AT&T INC. ( <b>T</b> )            | Trailing P/E (11.6); Forward P/E (8.32); PEG Ratio (1.18); EPS Trends- bearish  |
| CISCO SYS INC ( <b>CSCO</b> )     | Trailing P/E (14); Forward P/E (9.80); PEG Ratio (0.75); EPS Trends- bearish    |
| MICROSOFT CP ( <b>MSFT</b> )      | Trailing P/E (12); Forward P/E (10.0); PEG Ratio (1.0); EPS Trends- bearish     |
| INTL BUSINESS MACH ( <b>IBM</b> ) | Trailing P/E (11.37); Forward P/E (9.98); PEG Ratio (0.93); EPS Trends- bearish |

| BULLISH | LONG-TERM FACTORS  | BEARISH |
|---------|--|---------|
|         | Fed cut key lending rate by 50 BPs to 1.5%. In coordinated effort, ECB and Bank of England each dropped their key rates by 0.5%, to 3.75% and 4.5% respectively.   | ✓       |
|         | Same-store sales figures: 71% of stores missed analyst expectations, while overall retail sales growth fell to just 0.8% - the worst since at least 2000.  | ✓       |
|         | Home prices down 16.3% from previous year in 20 major metro areas, according to S&P/Case Shiller   | ✓       |
|         | Manufacturing plunges. The ISM's index of factory activity fell to 43.5 in September, compared with 49.9 in August and 50.0 in July, well below consensus forecasts of 49.5. A reading below 50 indicates contracting economic activity. | ✓       |
| ✓       | FDIC's new liquidity guarantee program: The government insurer will cover \$1.4T in senior unsecured debt and \$400-500B in transaction deposit accounts, which businesses use to meet payrolls and pay vendors.                         |         |
| ✓       | Initial jobless claims declined to 478,000 from last week's revised figure of 498,000 better than economists's 480K consensus.   |         |
|         | RBC Consumer Attitudes and Spending by Households [CASH] Index dropped 32 points in October - the largest-single month drop since the index began in 2002. The current level stands at 37, vs. 69.2 in September.                        | ✓       |

## 3D CHECK LIST

| BULLISH | FACTORS   | BEARISH |
|---------|---|---------|
|         | <b>Technicals</b>   |         |
|         | Bearish daily and weekly MACD   | ✓       |
|         | Bearish weekly Stochastic Oscillator                                    | ✓       |
| ✓       | The stock forming a bottom  |         |
| ✓       | Support at 38.0   |         |
|         | Resistance at 42.0, 50MA, 200MA   | ✓       |
| ✓       | Similar stocks or key components are trying to form a bottom            |         |
|         | <b>Fundamentals</b>   |         |
| ✓       | Forward P/E (10.0) < Trailing P/E (12.7)                                |         |
| ✓       | PEG (0.89)  |         |
| ✓       | P/S (0.89)  |         |
|         | Operating Margin (9.18%), ROE (22.22%), ROA (7.17%)                     | ✓       |
|         | Bearish EPS revisions trend   | ✓       |
|         | <b>Market Play</b>  |         |
| ✓       | Program trading buy orders at 37.2 after Oct 16                         |         |
| ✓       | Implied volatility (52.19%) < Historical volatility (61.46%)            |         |
|         | Inadequate reaction on the latest positive news (see the chart above)   | ✓       |
| ✓       | Unusually high option trading volumes for Jan9 37.5-50.0 Calls and Puts |         |

## BULLISH PLAY

## BUY STOCK

| Stock Symbol | Last Stock Price | Recommended Entry Stock Price | Break-even | Sum Invested (per share) | Projected Stop Price | Max Loss (per share) | Max Profit (per share) | Exit Price (Target Price) | Target Profit (per share) | Target Return |
|--------------|------------------|-------------------------------|------------|--------------------------|----------------------|----------------------|------------------------|---------------------------|---------------------------|---------------|
| HPQ          | 41.01            | 40.00                         | 40.00      | 40.00                    | 38.00                | 2.00                 | Unlimited              | 42.40                     | 2.40                      | 6.0%          |

## BUY CALL

| Stock Symbol | Last Stock Price | Expiration Month | Strike Price | Option Symbol | Recommended Entry Stock Price | Entry Call Option Price | Break-even | Max Profit (per one contract) | Sum Invested (per one contract) | Exit Price (Target Price) | Target Profit (per one contract) | Target Return |
|--------------|------------------|------------------|--------------|---------------|-------------------------------|-------------------------|------------|-------------------------------|---------------------------------|---------------------------|----------------------------------|---------------|
| HPQ          | 41.01            | Jan-09           | 37.50        | .HPQAU        | 40.00                         | 5.35                    | 42.85      | Unlimited                     | 5.35                            | 6.16                      | 0.80                             | 15.0%         |

## BULLISH PUT SPREAD

| Stock Symbol | Last Stock Price | Expiration Month | Lower Strike | Option Symbol | Higher Strike | Option Symbol | Recommended Entry Stock Price | Entry Credit | Break-even | Max Profit (per one contract) | Sum Invested (per one contract) | Exit Debit (Target Debit) | Target Profit (per one contract) | Target Return |
|--------------|------------------|------------------|--------------|---------------|---------------|---------------|-------------------------------|--------------|------------|-------------------------------|---------------------------------|---------------------------|----------------------------------|---------------|
| HPQ          | 41.01            | Jan-09           | 35.00        | .HPQMG        | 37.50         | .HPQAU        | 40.00                         | 1.00         | 36.50      | 1.00                          | 1.50                            | 0.75                      | 0.25                             | 16.7%         |

## BULLISH CALL SPREAD

| Stock Symbol | Last Stock Price | Expiration Month | Lower Strike | Option Symbol | Higher Strike | Option Symbol | Recommended Entry Stock Price | Entry Debit | Break-even | Max Profit (per one contract) | Sum Invested (per one contract) | Exit Credit (Target Credit) | Target Profit (per one contract) | Target Return |
|--------------|------------------|------------------|--------------|---------------|---------------|---------------|-------------------------------|-------------|------------|-------------------------------|---------------------------------|-----------------------------|----------------------------------|---------------|
| HPQ          | 41.01            | Jan-09           | 35.00        | .HPQAG        | 37.50         | .HPQAU        | 40.00                         | 2.00        | 37.00      | 0.50                          | 2.00                            | 2.30                        | 0.30                             | 15.0%         |

## SHORT GLOSSARY

**Break-even.** Point at which gains equal losses. This is the market price that a stock must reach for an option to avoid loss if exercised. For a call, the break-even equals the strike plus the premium paid.

**Call option.** The right, but not the obligation, to buy the stock at a predetermined price (also known as the strike) at any moment before the expiration date for a paying a premium.

**Put Option** - the right, but not the obligation, to sell stock at a predetermined price (also known as a strike) at any moment before the expiration date.

**Expiration Date.** The day when an option contract becomes void (the Saturday after the third Friday of the expiration

**In-the-Money Option.** An option that has intrinsic value. A call (put) option is in-the-money if the strike is less (greater) than the current market price of the stock.

**Intrinsic Value:** The value of an option if it were to expire immediately with the underlying stock at its current price or the amount by which an option is in-the-money. For call options, this is the difference between the stock price and the striking price, if that difference is a positive number, or zero otherwise. For put options it is the difference between the striking price and the stock price, if that difference is positive, and zero otherwise.

**Spread.** A position with long and short options of the same type on the same underlying stock or index.

**Time Value.** Amount by which the current market price of an option exceeds its intrinsic value (the difference between the stock price and the strike). This additional value of an option is due to the volatility of the market and the time remaining until expiration.

### Auto-trade in 5 easy steps

| optionsXpress  | thinkorswim   |
|--|---|
| 1. Log into your brokerage account.  | 1. Log into your brokerage account.   |
| 2. Select Xecute, select OptionSmart as an Investor Publisher  | 2. Select Autotrade, click Sign Up/Newsletter Providers and choose OptionSmart as newsletter provider                           |
| 3. Select a service  | 3. Select Autotrade Management, click Allocations (per trade)   |
| 4. Determine Amount Type (Specific Dollar Amount, # of Contracts/Shares, % of Cash Available, % of Buying Power, % of Total Account Value) | 4. Determine Amount Type (Specified Dollar Amount, Srecified Quantity, % of Available Buying Power, % of Net Liquidating Value) |
| 5. Select a Trade Amount   | 5. Select a Trade Amount  |

There is risk in trading options. One's financial suitability should be considered carefully before placing any trades. Past performance is not indicative of future results.

Copyright © 1998-2008 OptionSmart.com (Stock Markets Institute). All rights reserved.

Released on 10/21/08