Trade Size & Allocations
About the Author

Kirk Du Plessis is a full-time options trader, real estate investor and entrepreneur.

Before launching Option Alpha more than 8 years ago, he was an Investment Banker for Deutsche Bank in NY with the Mergers & Acquisitions group, a Capital Markets Analyst for BB&T in DC covering REITs and a Senior Loan Officer in the mortgage industry.

His training courses and coaching programs have helped thousands of traders from around the world learn how to make smarter options trades. He was recently featured in Barron’s Magazine as a contributor to the Annual Broker’s Review and is the head trader here at Option Alpha.

Though a long-time resident of Virginia, he currently lives in Pennsylvania with his beautiful wife and daughter.
Why Trade Small Positions?

One of the most integral pieces to a profitable options trading system is your ability to trade hundreds of positions over the course of a year. Because we trade on probabilities we need a lot of “data points” or “individual trades” so that the targeted probability we are focusing on has a greater chance of being realized.

A simple yet powerful example of the Law of Large Numbers is explained when flipping a simple coin:
The probability of getting Heads or Tails is 50/50. But that doesn’t mean on your first 2 flips will show this result (or your first 4 or 8 flips. You may see a string of 8 Heads in a row or 8 Tails in a row right? But over time the more you flip the coin the closer the actual results will come to the expected 50/50 outcome.

*The same holds true when trading options.* . . .

For example, if you are placing 70% probability of success trades that doesn’t mean if you make 10 trades all year that 7 will be winners and 3 will be losers. It just might not happen so “perfect” in your first 10 trades.

But I almost guarantee that if you place 1,000 trades over the course of 1-3 years (notice we don’t promote success overnight) you are likely to see your percentage of winners very close to the expected 70% level. It’s just a matter of time and you can’t argue with the math behind it.

For us to be able to make so many trades we therefore need to make sure that our positions are small so that 1 or 2 trades that very bad won’t blow up our account. In this blueprint we’ll give you some guidelines on position sizing that you can use as with your own trading.

As always, you may need to scale up or down depending on your individual situation (commissions, account size, trading style etc) to fit your needs better.
The “Sliding” Scale Approach

At Option Alpha we favor a sliding scale to position sizing between 1% and 5% allocation of risk per trade.

This means that during times of high IV when option premiums are rich we actually want to be slightly more aggressive because the odds are more in our favor and move our positions sizes up towards 5%.

Conversely, during times of low IV we want to be extra conservative with position size and scale back towards 1% because our probability of success will not be as great.

Recognizing that our “edge” in trading options comes when implied volatility is highest, we should be confident and comfortable with smaller positions (or staying on the sidelines altogether) when IV is low.

The tables in the pages to follow will help you quickly narrow down the optimal positions size based on various different account sizes and allocation percentages.
### Risk Per Trade By Account Size

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***Risk per trade is based on the maximum loss on the trade or initial margin requirement to hold the position. For example, if you sell a $1 wide credit spread and take in a $30 credit your max risk is $70. If you sold a $2 wide credit spread taking in the same $30 your max risk would increase to $170. For undefined risk trades we will take the initial margin requirement. For example, if you sell a naked put below the market and take in $90 of credit but the margin requirement is $1,200 then we base the max account size off the $1,200 margin requirement needed to hold the position.***
How Many Contracts to Trade?

Using the table from above we can quickly calculate how many contracts or spreads you can trade for each position. Lucky for you, it’s a very easy 3-step formula.

**Step 1: Determine Your % Max Risk Per Trade**

This comes from the table above but let’s just say that you are using 2% of your account equity on each trade. If you have an account of $50,000 this would mean that no more than $1,000 of risk ($50,000 X 2%) is allowed per trade.

**Step 2: Determine The $ Risk Per Spread**

Let’s assume you are trading a SPY 175/170 Put Spread and take in a credit of $100. The difference in strikes is 5 points (or $500) less your credit of $100, so the max risk on this trade is $400 per spread. Undefined risk trades will use the initial margin required to hold the position.

**Step 3: Divide % Max Risk by $ Risk Per Spread**

With both of the figures from above we simply divide the max percentage allocation per trade from #1 by the risk per contract from #2. In our example above it would be $1,000 / $400 = 2.5 spreads. Based on your risk tolerance you can trade at most 2 vertical spreads (rounding down).
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We help educate and coach options traders on all levels: from people just starting out to advanced traders with multi-million dollar portfolios (and everyone in between).

Since 2007 more than 2.3 million people have trusted OptionAlpha.com to bring them the most amazing training on options trading, making us a clear leader in this market.

We believe that there is a huge lack of financial literacy and a gap that we aim to close by delivering the best possible content in multiple formats for you to consume: blog posts, video tutorials, webinars, podcasts, case studies, live events, etc.

Our goal is to pull back the curtain and give you the best online courses and training possible in all the right areas so that you can learn to make decisions for yourself. Because at the end of the day, making smarter trades isn't just our tagline - it's our mission for you.