



## Trader Profile

BY DANIEL P. COLLINS

# Caine: Managing premium, managing risk

**A**nthony Caine, a successful businessman and entrepreneur, wasn't looking for a new line of work when he befriended a group of traders on his daily commute to downtown Chicago in the early 1980s, but his natural curiosity about derivatives trading started him down a path that led to his successful commodity trading advisor (CTA), Barrington, Ill.-based LJ&M Partners.

LJ&M earned 53.83% in 2004 following a 68.10% performance in 2003 in its market-neutral S&P option premium writing program. The discretionary program, which has a compound annual return of 29.98% since its inception in 1999, is the result of years of trial and error in Caine's personal trading.

Caine's inquisitive nature led him to pepper fellow commuters with questions about their trading. Finally, one of his friends, a specialist at the Chicago Board Options Exchange, handed him a pile of books and said, "Here, kid, read these before you ask any [more] questions."

He did and he began trading while continually working his day job in the computer and software industry — which included the founding of arguably the first commercial Web browser company, Spyglass, that he would eventually take public.

Caine had worked for and invested in Apple Computer and Hewlett-Packard and saw how he could get more bang for his buck with options. "Instead of spending \$5,000 on 100 shares of stock, I could spend 10% of that to control the same amount," Caine says.

He learned the hard way about option pricing when a positive move in the underlying did not translate to his options position.

"The stock had a nice jump, [but] the option barely moved and that is when I scratched my head," Caine says.

The disappointment of being right but not profitable led Caine to learn more about strike dates and prices and explore strategies involving selling options. He parlayed his expanding options expertise and his knowledge of the tech sector into a decent side income, riding the volatility in tech stock options.

When he received the windfall from the Spyglass IPO in 1995, he thought it was a good time to devote more time to his family. He coached his kids athletic teams, traded occasionally and allocated money to an option broker to manage.

"Candidly, they thrashed the account. Commission rates were excessive and in 60 days the account was down 40%," he

says. "I arrested that trading and I started trading S&P futures options using my strategies and got the accounts whole."

Chicago-based Fox Investments bought the brokerage firm where Caine maintained his account and owner Jeff Fox, after observing Caine's trading, asked him if he wanted to become a CTA. Caine was interested. He abandoned trading equity options, focused on the S&P 500 and began managing a couple accounts of friends and family, which led to LJ&M.

"Getting off of the premium of the technology sector is like getting off heroin. Once you are on a big premium, it is hard to leave," Caine says. But S&P options had lower volatility and were a product better suited for managing client funds.

Caine uses a mostly market-neutral option strategy entering positions on strangles.

"Writing strangles to take advantage of time decay is so common. Where I develop my expertise is the adjustments when the market moves strongly toward one end of your strangle," Caine says. Where many option writers look at monthly cycles, Caine takes a longer view. He initiates with strangles four to seven weeks out, adding positions closer in and further out to manage risk.

LJ&M earned 60.52% in 1999, its first full year, but Caine wasn't done learning lessons. Though the program had a market-neutral element, Caine would allow the program to make directional bets. When the S&Ps were tanking in the summer of 2002, Caine figured the market was oversold and allowed the program to move to a long bias. The stock index kept trading lower, however, and the program had its worst drawdown of 46%.

"When the market started tanking, I stopped writing calls against it. I was afraid of a whipsaw," Caine

says. He moved his short put positions down to 800 and below, thinking there was no way the market would get near it. "I theorized the market was going to bounce, which it did, but I was completely wrong on the timing," Caine says.

The program now maintains a completely market neutral position and uses less leverage than in 2002.

"Any single option position I have on may not have merit, but within the construct of the open option portfolio, there is a reason for it," Caine says. "I don't trade off of specific options positions. I manage premium [and] I manage risk. The relative premium will dictate the relative risk."



ANTHONY CAINE

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