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Put buying is the opposite of buying a call.

Here’s how it works…

Buying a put is an option to sell a particular stock at a certain price for a limited period of time.  It’s a bearish position.  A put option increases in value as the price of the underlying stock goes down.

There are three primary benefits to a put buying strategy.

First, risk is limited to the premium paid.  No matter what happens to the underlying stock price, you can never lose more money than the initial cost to open the position.

Second, reward is unlimited.  The lower a stock price falls, the higher the value of a put option climbs.

Third, buying a put option provides a great deal of leverage.  That means a small decrease in the underlying stock price results in a large increase in the option value.

Here’s an example of buying put [options](http://www.optionstradingresearch.com/options/) on **Exxon Mobil** (XOM)…

Let’s say XOM is trading for $80 per share.  Let’s assume a put option on XOM with a $75 strike price and an expiration date 6-months in the future sells for $3.00 per contract.

Remember, each option contract controls 100 shares of stock.  So, buying one contract will cost $300.  An investment of $300 gives the investor the right to sell 100 shares of XOM for $75 anytime in the next six months.

In a nutshell, if XOM’s price goes down, the value of the put option goes up.

Let’s take a look at three possible outcomes at [options expiration](http://www.optionstradingresearch.com/options-expiration/).  Don’t forget, you have the right to sell the option at any time.  There’s no need to wait until expiration to sell.  But talking about the value at expiration is an easy way to illustrate the potential outcomes when buying put options.

First, let’s look at breakeven.  In this scenario, you get your $300 investment back.  The breakeven on our XOM put option is $72 ($75 strike price – $3 option premium).  In other words, if XOM’s price falls by 12.5% to $72 during the next six months, the put buyer will breakeven at expiration.

Second, let’s look at a 100% loss.  If XOM is trading for more than the $75 strike price, the option will expire worthless.  The good news is you can only lose the $300 premium.  Even if XOM stock’s worth $500 per share, the most you lose is the premium you paid to buy the option.

Our third scenario is the most exciting, and the reason many investors buy put options… profits!

If XOM is worth less than $72 at expiration, you’ll make a profit.  Let’s say XOM falls 25% to $60.  The option would be worth $15 ($75 strike price – $60).  That means our $3 put option increased an eye-popping 400%!

In other words, a 25% decrease in the underlying stock caused the option to increase by 400%.  That’s the type of leverage that gets option traders’ juices flowing.

*[[http://traffic.shareaholic.com/e?a=7&r=2&p=39943952-9e1b-4279-8691-1956cbc871e8&u=http%3A%2F%2Fwww.optionstradingresearch.com%2Fcall-options-or-put-options-on-best-buy-bby%2F](http://www.optionstradingresearch.com/call-options-or-put-options-on-best-buy-bby/)](http://www.optionstradingresearch.com/call-options-or-put-options-on-best-buy-bby/)*

[Call Options Or Put Options On Best Buy (BBY)?](http://www.optionstradingresearch.com/call-options-or-put-options-on-best-buy-bby/)

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[BBY, HPQ, XLF Options -- Unusual Trading Activity -- May 25, 2012](http://www.optionstradingresearch.com/bby-hpq-xlf-options/)

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[MGM, WFC, T Options -- Unusual Trading Activity -- July 27, 2012](http://www.optionstradingresearch.com/mgm-wfc-t-options/)