

How I made 124% on Fannie Mae

(while the stock fell 8.4%)

By Dr. Terry F. Allen

It will take you about 10 minutes to read about my very extraordinary gains on a very ordinary financial instrument. (Maybe a bit longer if you decide to read the free links to my tips).

By the end of your 10-minute investment, you'll discover how you can profit, too, with a little help from me to get you started.

When you finish, you will know about a stock options strategy that has taken me 20 years to create and polish. This strategy has generated truly extraordinary investment gains for me. And it can for you as well. Do your investment portfolio (and your loved ones) a big favor, and read through to the very end. Even better, print it out and keep it as reference.

You Can Bet Your Fanny on Fannie Mae

Fannie Mae was just about my favorite stock for many years. Peter Lynch raved about it in the early 90's when it had gone up 700% in seven years. I have owned it for many years, and have earned exceptional returns on this staid old stock, using my [10K Strategy To Double Your Money Every Year](#).

Fannie Mae is one of only five companies in the S & P 500 to record double-digit growth in operating income for each of the past 14 years. [Note: In late 2004, the company admitted that they had over-stated earnings by as much as \$9 billion, the president resigned under fire, the dividend was cut, and even higher earnings adjustments were hinted at. The stock subsequently crashed, and short-term options are no longer available for trading. At this time, Fannie Mae is no longer a valid stock to use for my [10K Strategy](#).

However, the strategy itself remains valid. In 2003, I earned 196% with this strategy using QQQQ as the underlying stock, although the trades were far more numerous and complicated. In 2005, I used the same strategy in 8 different portfolios, and the average annualized gain of all 8 was 103%. The following Fannie Mae example will give you a clearer understanding on how the strategy works, even though it is less current than other examples I could use.]

In 2001, Fannie Mae did not enjoy a great year in the stock market, even though it chalked up another year of 15% earnings growth (at least that's what they reported at the time). The stock started out the year at \$86.75, and ended at \$79.50, for a loss of 8.4%. Owners of the stock would have received a 2.5% dividend to partly offset this loss.

During 2001, I employed my [10K Strategy To Double Your Money Every Year](#) on Fannie Mae, and earned over 124% on my investment for the year. I did this without using margin. It did

require adherence to the **10 Trading Rules** I set forth for the 10K Strategy (which is spelled out for Terry's Tips Insiders, in detail, in my White Paper, including exactly what trades need to be made each month depending on what the stock has done).

Too Good To Be True?

I know this may sound too good to be true. But please read on. The strategy may seem confusing at first, but once you get the hang of it, you will find that it is really simple. You may even find it to be boring. But making 124% in a year when your stock falls 8.4% is anything but boring. (By the way, I would have earned a lot more if the stock had gone up.)

Following is a list of the actual trades I made in one of my accounts for 2001 (on a pro-bono basis, I manage a small endowment for a school in Vermont, and these trades were made in their account).

Are You Familiar With Stock Options?

Before you start reading, you may want to read two short reports as background. They're free at Terry's Tips - <http://www.terrystips.com/tip1.shtml>. Tip #1 includes a short primer on stock options, and Tip #2 tells all about LEAPS (long-term equity options). Print out both of these and keep them for reference as you read the following story of how I traded Fannie Mae options.

Getting Rich With Stock Options Isn't Brain Surgery

It's true – I graduated from Harvard Business School and earned my Doctorate in Business from the University of Virginia before I got involved with stock options. And I started out trading right on the floor of the CBOE (Chicago Board Options Exchange). Before they let you trade on the floor as a market maker, you must take courses and pass lots of tests concerning stock options. Over the years, I have read every book I could get my hands on involving stock options – over 100 in all.

Admittedly, I had some advantages that many option traders do not enjoy. But I didn't need them to make it big with stock options. What I'm telling you about here is really simple. You will only need a basic understanding of stock options to make riches on your own using one of my 4 trading strategies.

But First, The Summary

Before I get on with the exact trades that I made each month, you might like to see the summary of results first. In fact, you might prefer not even to read the month-by-month details, as they can be a little tedious. But here is what happened:

- 1) During 2001, Fannie Mae (FNM) fell from \$86.75 to \$79.50, a drop of 8.4%.

2) Using my 10K Strategy to Double Your Money Every Year, I earned a profit of over 124% on my average invested capital for the year. (If you read this report to the very end, you will discover that my return was much greater than this, but if I told you that now, you would probably think I was smoking some illegal substance.)

3) This system involved making between 1 and 4 option trades on (or near) the third Friday of every month. (Insiders are emailed specific trading instructions just before expiration day each month).

4) This system does not involve the use of margin. It CAN be used in your IRA - a secret that very few people know about (most brokerage firms choose not to allow option spreads in IRA accounts). I will give you the name of two brokerage firms that welcome option spreads in IRA accounts. Even better, their commission rates on option trades are some of the lowest around. And these firms can get you great prices – they have years of option trading experience.

5) My initial investment made in January (\$38,570) was completely paid back to me, in cash, by October.

6) At the end of the year, I had all my original investment back (plus over \$10,000), and still owned LEAPS which could potentially generate a profit above \$6000 every month for another 12 months.

7) The 124% return rate actually understates what I earned for the year. If I had re-invested the cash inflow each month into another similar investment, I could have dramatically increased my net profit for the year. (I actually did this, but that is a whole new story.)

Note: While I started out with an investment of nearly \$40,000, the 10K Strategy can be executed with \$5,000 or less using slight modifications of the basic Trading Rules.

If you are ready to invest in yourself, and learn all about the great potential of the 10K Strategy (including Trading Rules) now, before reading all the details of how it performed with Fannie Mae, go directly to our order page - <http://www.terrystips.com/order.php>.

Getting Started with Fannie Mae

The year 2001 started out with Fannie Mae (FNM) trading at \$86.75. My 10K Strategy to Make 100% Every Year involves owning a LEAP rather than actually buying the stock. (See a full discussion of LEAPS at Terry's Tips - <http://www.terrystips.com/tip2.shtml>.)

To start the year off, I purchased 30 Fannie Mae January 2003 call LEAPS with a strike price of \$80 (symbol VFNAP). The LEAP cost me \$16.50 (\$1650 each), for a total cost of \$49,560, including commissions at my discount broker's rates. (From this point forward, all option purchases and sales figures will include the commissions I paid, rounded off to the highest dollar amount ending in zero.) By the way, I now trade at a different brokerage firm where commissions are a lot lower than I paid in this Fannie Mae example.

While I really didn't own the stock, I had all the rights of ownership (except voting and collecting dividends) for 3000 shares of Fannie Mae. Someone who purchased this number of shares rather than the LEAPS would have shelled out over \$260,000, or almost 7 times my starting investment.

I immediately sold someone else the right to buy 2000 of my "shares" at a price of \$85 (the strike price) for the three-week period ending on the third Friday of January 2001 (the option expiration date). I received \$4.50 per share (\$450 for each of 20 option contracts) for these options, or \$8960.

What I did is called writing a call option. If you are not familiar with how this works, click here - <http://www.terrystips.com/tip1.shtml> to read "All About Stock Options".

I also sold someone the right to buy 1000 of my Fannie Mae "shares" at a price of \$90 until the January, 2001 expiration, receiving \$206 each for 10 options, or \$2030 after commissions. (I put the word "shares" in quotations because I really didn't own shares. Instead, I owned the right to buy these shares at \$80 for a little over two years, and this gave me the right to sell someone else a right to buy these "shares" as long as the strike price is not less than \$80 nor is the expiration date further out in the future than January 18, 2003.)

So, if you're not terribly confused, I'll calculate that my starting investment in Fannie Mae at the beginning of 2001 was \$38,570 (\$49,560 for the cost of the LEAPS, less the \$8960 and \$2030 I received from selling call options to someone else).

January Expiration Was a Bummer

On the third Friday in January, I suddenly felt poor. FNM had dropped from \$86.75 all the way to \$76.81, a plunge of 11.5% in less than one month. But if you think I felt bad, how do you think those guys felt who paid me \$11,000 for options to buy FNM at \$85 or \$90? They lost 100% of what they invested.

At least I still had my LEAPS, although the price had fallen all the way to \$11.50. I had experienced a loss (on paper, not in real money) of about \$15,000 which was partly offset by the almost \$11,000 I took in from the options I sold. Still, I was down over \$4,000 in less than a month.

From this point on in my story, I will only comment on the cash transactions each month. The paper value of my LEAPS will rise and fall with changes in the stock price, but the only really significant event is what I sell them for at the end of their life (or earlier, if I choose). Fortunately, owning the LEAPS meant that I still had 23 months left during which I could sell options to someone else every month.

I have created **10 Option Trading Rules** to be used with the 10K Strategy to Make 100% Every Year – the strategy I used with FNM in 2001. These Rules dictate exactly which options should

be sold each month. They also spell out exactly how you place orders with your discount broker (i.e., where in the bid-asked range, and on which day orders should be placed).

Different Trading Rules may apply each month, based on special circumstances which may have occurred in the past month, such as unusual moves in the stock price, the exact price where the stock ends up at expiration, or announcement of a stock split. **Rules #5 and #6** apply every month, and deal with exactly how and when to place option orders. Terry's Tips Insiders receive the 10 Trading Rules before they make their first investment decision.

At the January expiration, **Rule #3** was applicable, so I sold 30 February 80 calls for \$2, netting \$5940. Now I had almost \$6000 free cash in my pocket after a losing month. I calculated that my initial cash investment of \$38,570 had been reduced to \$32,630 (\$38,570 - \$5940).

Rule #4 tells you what you should do with this cash to considerably increase your profits (and reduce your risk at the same time). I did not use this rule in this example because it would have impossibly confused most readers. Instead, I put the money that came in (I gained cash every month except one for the year) to work on a similar position in another stock I liked at the time.

February Expiration – a Turn-Around

By February expiration, FNM had jumped all the way back to \$82.45. I bought back the February 80 calls for \$2.50. (While these calls were theoretically worth only \$2.45 when they expired - the difference between the stock price and the strike price - when you buy back calls on expiration day, you generally pay a little more than the intrinsic value at the close.) It cost me \$7560 to buy these calls back.

I then employed **Rules #1 and #2**, and sold 15 March 80 calls for \$4.70 and 15 March 85 calls for \$1.75, netting me \$9690. My original investment declined a little further, to \$30,500 (\$32,630 + \$7560 - \$9690).

March Expiration – Down Once Again

By the third Friday in March, FNM had slipped again, closing at \$75.64. The two options I had sold expired worthless, and I got to keep the \$9690 I had received them for. I then employed **Rule #1**, and sold 30 April 80 calls for \$1.80, collecting \$5340, and reducing my original investment to \$25,160. (The \$1.80 premium may seem a little high for anyone who is following these prices closely, but the April expiration day was 5 weeks away rather than the customary 4 weeks.)

April Expiration – A Real Winner.

Expiration day in April showed FNM moving up a bit, to \$78.25. Once again, I was able to keep all the proceeds from the options I had sold a month earlier. This was one of the months where I made money both on the options I had sold, and the LEAPS, which had increased in value along

with the increase in the price of FNM. But I agreed not to mention the gains or losses on the LEAPS, so I won't get into those details.

In April, I used **Rule #1**, and sold 30 May 80 calls for \$2.25, collecting \$6690, and reducing my original investment to \$18,470.

May Expiration – Stock Down, But More Cash For Me

By May expiration, FNM had dropped once again, to \$75.56. The options I had sold in April expired worthless once again. I then employed **Rule #1** again, and sold 30 June 80 calls for \$1.30, netting \$3840, and reducing my original investment to \$14,630.

June Expiration – My Investment Gets Cut In Half

By June expiration, FNM had gone up to \$80.66. I had to buy the 30 June 80 call options back at \$.75, paying \$2310. I then used **Rules #1 and #2**, and sold 15 July 80 calls for \$3.50, and 15 July 85 calls for \$2.10, netting \$8340, and reducing my original investment to \$8600 (\$14,630 + \$2310 - \$8340).

July Expiration – Cash Goes Out For the First Time

By July expiration, FNM had gone up again, to \$83.93. I had to buy back the July 80 calls I had sold, paying \$4.00, or \$6030. Then I employed **Rules #1 and #2**, and sold 15 August 85 calls for \$1.80, and 15 August 90 calls for \$.80, netting \$3840. For the first time, my original investment increased, to \$10,790 because the amount I had to pay out to buy back the expiring calls was greater than the amounts I received from selling the next month's options.

August Expiration – More Cash Comes In

By August expiration, FNM had inched up to \$84.35. The options I had sold in July expired worthless, and I employed **Rules #1 and #2**, and sold 15 September 85 calls for \$2.30 and 15 September 90 calls for \$1.00, collecting \$4890. This reduced my original investment to \$5900.

September Expiration – the Stock Plummets Again

By September expiration, FNM had really tanked, falling over 10% to \$75.44. **Rule #3** now was in effect, so I sold 30 October 80 calls for \$1.20, collecting \$3540, and reducing my original investment to \$2360.

October Expiration – Time for a Big Celebration

By October expiration, FNM had rallied to close at \$80.99. I had to buy back my 30 October 80 calls for \$1.10, paying \$3360. Then I employed **Rules #1 and #2**, and sold 15 November 80 calls for \$3.00 and 15 November 85 calls for \$1.40, collecting \$6540.

I am now a happy person. **I have received back in real cash every penny I invested at the beginning of the year**, and had \$820 in my pocket as well. This was sort of like burning the paid-off mortgage, a time for real celebration. (My original investment had been reduced to \$2360 in September, plus the \$3360 I paid out to buy back expiring calls, less the \$6540 I collected from selling November calls.) I still own my LEAPS, but now they are free and clear, and have not cost me anything.

November Expiration – More Cash Flows In

By November expiration, FNM had inched up to \$81.50. I had to buy back 15 November 80 calls for \$1.60, costing me \$2430. Then I employed **Rules #1 and #2**, and sold 15 December 80 calls for \$3.20 and sold 15 December 85 calls for \$1.55, collecting a total of \$7,060. I now have \$5450 in my pocket (\$820-\$2430+\$7060), plus the value of my LEAPS.

December Expiration – It Keeps Rolling In

By December expiration, FNM had fallen a bit, to \$80.09. I bought back the 15 December 80 calls for \$.20, paying \$330. I then employed **Rules #1 and #2** again, and sold 15 January 80 calls for \$2.05, and 15 January 85 calls for \$1.00, collecting \$4505.

I now had \$9625 (\$5450 - \$330 + \$4505) in cash. It's a nice feeling to have this much money in your pocket in spite of having bought a stock that was lower than it had been at the beginning of the year.

On December 31, 2001, FNM had fallen to \$79.50. If I wanted to close out my positions on that date, I would have to buy back my January 80 calls, then trading at \$1.40, and my January 85 calls, then selling at \$.25, costing me \$2540. Then I could sell my 30 LEAPS for \$8.30, or \$24,840. That would leave me with a total of \$31,905 in my pocket (\$9625 - \$2560 + \$24,840).

My average investment for the year was \$13,208, ranging from \$38,570 for the first month to a negative \$9,625 for the last month. My profit for the year would have been \$31,905 if I had closed out my positions on the last day of the year.

That results in a profit margin of 242% for the year. Since I knew you would never have believed that I could make that much on a stock that went down over the course of the year, I said that my earnings were “only” 124% when I first told you about how I did with Fannie Mae in a single year.

Expanding the 10K Strategy to Other Stocks: This is a system that anyone can follow. When you sign up for Insider status, I will give you a two-month real-life tutorial using the 10K Strategy with several stocks such as Google, Apple, and Sears . By following the actual trades I make, it won't be long before you are familiar with the Trading Rules. You should then be able to determine for yourself what the appropriate trades would be for each month. Then you won't need me any longer.

At the beginning of 2003, I set up an account with \$10,000 for my subscribers to watch. I agreed to use the 10K Strategy in this account, and to only trade in QQQQ, the NASDAQ 100 tracking stock. Before I made any trades, I emailed all my Insiders and told them what I intended to do (and why), so they could mirror my trades if they wished. By the end of the year, this account had grown in value to over \$29,600.

That's a profit of over 196% for the year – not bad by anyone's standards.