Enhanced Covered Call Strategies Using Credit Spreads

Introduction

In volatile markets, investors can consider strategies that generate income while still seeking capital appreciation. The basic covered call strategy is a popular way for investors to generate income on stocks that may pay little or no dividends of their own, but there are limitations. One way to enhance that strategy and address those limitations is to use credit spreads. This primer describes how credit spreads can be used to generate income but continue to provide opportunities for participating in the growth of the underlying stocks.

As described in the first primer for basic covered call strategies, that strategy works best when the investor expects the stock price to stay flat or rise slightly. If the stock price stays below the strike price of the sold call option, the investor keeps both the premium and the stock. However, if the stock rises above the strike price, the investor must sell at that price, which caps gains. Credit spreads address this issue.

A credit spread is an options strategy where you sell a call option (the short call) ***and*** buy another call option (the long call) with a higher strike price. The goal is to earn income from the premium received from the short call with the opportunity to participate in the gains of the underlying stock if its price exceeds the strike of the long call.

YieldMax™ ETFs uses this enhanced version of the covered call strategy on a diversified portfolio of stocks in one ticker.

Here's how credit spreads work within a covered call strategy, but first, a refresher on the basic covered call strategy.

Covered Call Basics

The basic **covered call** involves holding a stock and selling a call option on it. The goal is to earn income from the option premium while holding the underlying asset.

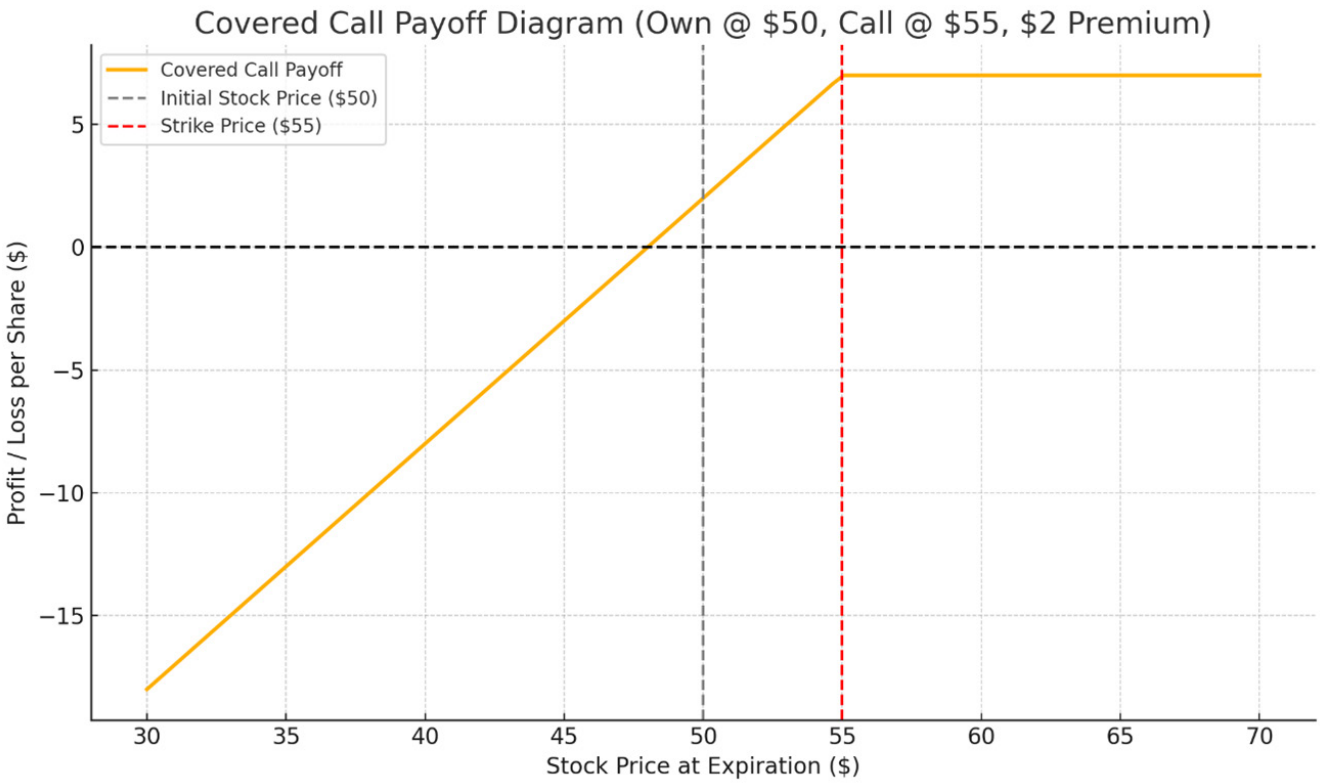
Example:

- **Own 100 shares** of stock at **$50/share**
- **Sell 1 call** with **$55 strike**, expiring in 1 month
- **Collect premium:** $2/share

Key Points:

- **Breakeven:** $48 (Stock price - premium received)
- **Potential Loss:** You are subject to losses if the stock price falls, but losses are offset by the $2 premium received
- **Max Profit:** $7 ($5 appreciation + $2 premium)

Profit rises as the stock price increases, **but is capped at $55**. If the stock falls below $48, you start losing money.)



Enhancing with a Credit Call Spread

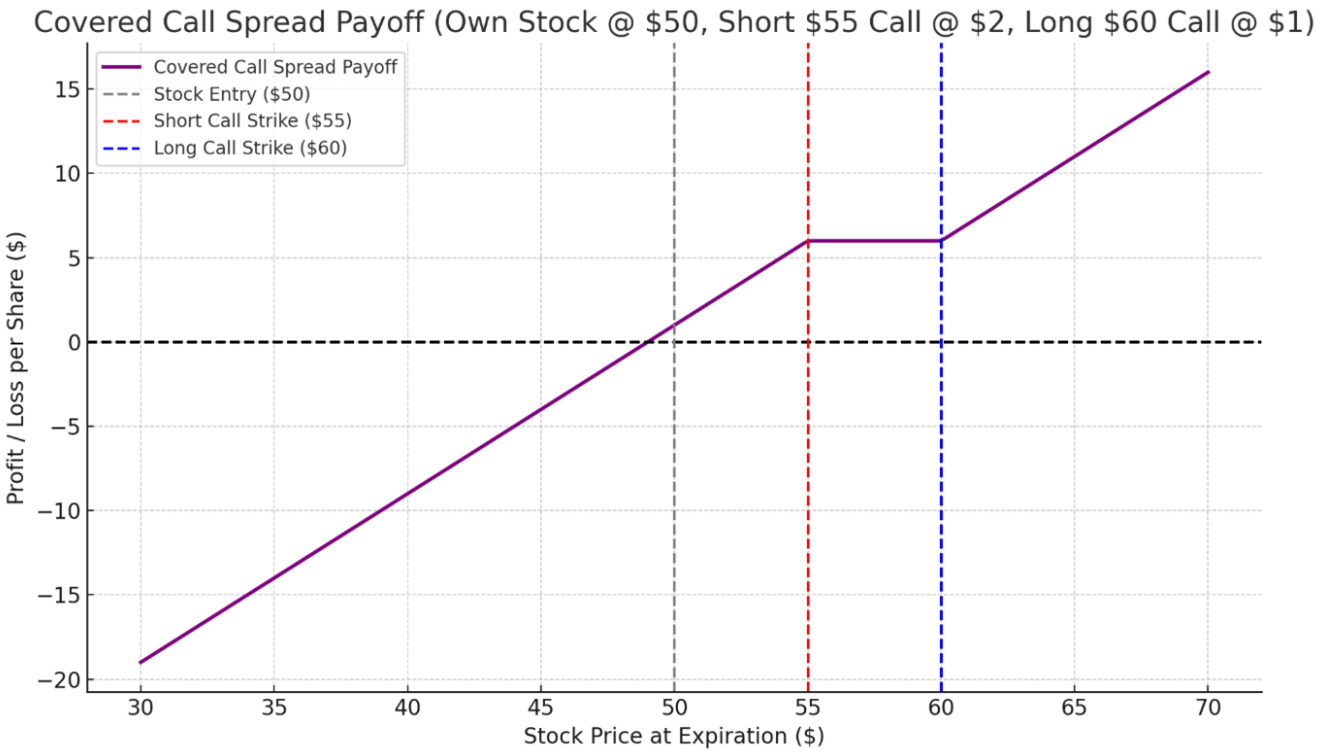
How is it different? Instead of only selling a call, you **also buy a higher strike call.** This creates a **call spread,** which lowers your premium income but **limits the risk of capped gains if the stock surges.** Here's the same example using a call spread.

Credit Call Spread Example:

- **Stock owned at:** $50
- **Sell call** with **$55 strike,** collect premium: $2
- **Buy call** with **$60 strike,** pay premium: $1
- **Net income (credit):** $1

Key Points:

- **Breakeven:** $49
- **Potential Loss:** You are subject to losses if the stock price falls, but losses are offset by the $1 premium received
- **Profit:** remains constant while the stock price stays between the strikes (between $55 and $60), but upside is not capped if the stock prices rises above the long call strike



Diversification: Portfolio of Call Spreads

Rather than applying this strategy to one stock, imagine it across **many stocks** — such as the big tech giants.

This brings:

- **Diversification across a portfolio of stocks**
- **Broader income sources**
- **Reduced single-stock risk**

YieldMax™ ETFs: One-Ticker Simplicity

YieldMax™ takes this complex strategy and **packages it into a single ETF.** You gain exposure to a portfolio of covered call positions, enhanced using credit spreads — **professionally managed, traded on exchange, and accessible to all.**

- **Expert-managed**
- **Multi-stock strategy**
- **ETF convenience**

Why Use Enhanced Covered Call Strategies?

- **Potential Steady Income:** Monetize stock price volatility with options
- **Seeks Capital Appreciation:** Retains opportunity to participate in upside exposure
- **Diversified Exposure:** Reduce reliance on one stock
- **Simplicity via ETFs:** No need to manage multiple options positions yourself

Final Takeaway

YieldMax™ ETFs: Smart option strategies, made simple.

One ticker. One strategy. Professionally managed.

Learn more at **www.YieldMaxEurope.com**