Generate Over $1,000 in Instant Income Without Immediately Selling Any Shares in These 2 Popular Companies

Description

Covered calls are a brilliant way for long-term investors to take some money off the table without selling shares. This can be particularly useful when there has been a recent run up in share prices. Investors may want to take cash off the table, without giving up all potential upside. The current environment is potentially such an environment where investors may be contemplating such a move. Here are two examples that demonstrate the power of covered calls.

Two examples

Shopify (TSX:SHOP)(NYSE:SHOP) has had a magnificent run this year, more than doubling off its March low. Many investors may be questioning whether now is the time to take the money and run. However, those lingering thoughts about missing out on further gains may keep investors from selling. Those who want to take some cash off the table, while preserving some upside potential, should look to covered calls.

Shopify's Canadian January 2021 $1,150 calls, at the time of writing, are trading at approximately $145 ($1,450 per contract). This means that investors get paid $1,450 (minus fees) to agree to sell 100 Shopify shares for $1,150 in January 2021. This still represents an 11% upside to Wednesday's closing price. Should the options get exercised, the investor is ultimately getting paid $1,295 to sell their 100 of their shares in Shopify. This represents a total of 25% upside to Wednesday's closing price, and aggregate sale proceeds of $115,000 (in addition to the $1,450 from the covered call sale).

The best part is that you may get to keep the money without ever having to sell your shares. If Shopify isn't trading above $1,150 in January 2021, the options expire and will not be exercised. You still get to keep the money from the covered calls though!

Unfortunately, options can only be purchased in lots of 100. Understandably, not every investor was fortunate enough to purchase Shopify when 100 shares was affordable. However, selling covered calls also works with lower priced shares.

Air Canada (TSX:AC) has also bounced just under 100% from its March low at the time of writing. This also makes it a prime candidate for covered calls, as those sitting on almost 100% profits over the course of two months might be getting a bit nervous.

Investors can sell the January 2021 $30 calls for approximately $1.45 ($145 per contract). This allows investor to enjoy a gain of over 80% if the stock crosses the $30 by January 2021. This is, of course, on top of the $145 immediate income, per 100 shares, that the investor generates. This gives a third party the right to buy 100 shares of Air Canada from the investor for $3,000 in January 2021, and pays the investor $145 for that right. Investors with 1,000 shares of Air Canada would enjoy $1,450 in immediate income if they sold 10 of the covered January 2021 $30 calls on their entire Air Canada position.

Given that Air Canada's success is highly dependent on the return of travel demand, it may be prudent to consider taking money off the table now. It is impossible to predict whether a second or third wave of COVID-19 could hamper Air Canada's demand through the rest of 2020.

Takeaway

Markets have recovered sharply off their March lows. Investors may be looking to take some profits but fear leaving potential upside on the table. Covered calls are an ideal way to alleviate some short-term fear without completely compromising near-term upside.

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