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Behavioral Aspects of Covered Call Writing: An Empirical Investigation

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Abstract

Various covered call strategies have been explored in the literature, focusing on risk aversion, hedonic bias, and the role of cash flow. That is, studies have shown that over a short period, identical covered call strategies can have pronounced effects on cash flow, especially for a relatively short period. Covered call writing is required.

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Notes

1. The term covered call generally refers to overwrites, i.e. to short a call option on a stock that one already owns, as well as buy-writes, that is, to first buy a stock and then to short a call option on this stock (Figlewski, Silber and Subrahmanyam [[1990](#)]).

2. For more information about these products, see www.cboe.com or www.euronext.com.

3. The BMX is a hypothetical buy-write strategy that entails the simultaneous purchase of the S&P 500 and the shorting of an at-the-money S&P 500 Index call option (www.cboe.com).

4. While the Sorti is a measure of return variability, the Sorti is used as a measure of return variability.

5. The U is a measure of inside risk given mini

6. We th e value function ([2](#)]) may also drive inv oncur, but an inves

7. DRCs ular bonds with a short put option on stocks (Breuer and Perst [[2007](#)]).

8. We thank an anonymous reviewer for noting that in case probabilities are small, not 50–50 as in Shefrin and Statman [1993] and here, investors may exhibit risk seeking in the domain of gains, even with concave utility.
9. We thank an anonymous reviewer for noting that our graphical display of the binominal case used by Shefrin and Statman [1993] may mask the true payoff pattern of covered calls (e.g., [Figure 2](#)). Future research should employ more realistic examples that also include intermediate payoffs.

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