# Volatility Percentile Filter

Volatility Percentile is a very important part of Volatility based trading as it allows one to compare the current volatility of an underlying to past volatility levels of the same underlying.

**Percentile** - defines the position of the current value in a list of sorted historical readings, as a percent to the total number of historical readings.

For example, a Volatility in the 97$^{th}$ percentile means that 97% of Volatility readings have been lower in that particular time period.

When you are buying options, you want them to be Cheap. When you are selling them, you want them to be Expensive. It is that simple. The trick is how you determine if an option price is Cheap or Expensive.

Implied Volatility is a characteristic of option price. Can one then assume that if Implied Volatility for one stock is higher than Implied Volatility of another one, option prices for the first stock are more Expensive?

**Absolutely NOT and here is why!**

When you are buying a shirt you are not comparing its price to the price of the car and assuming that it's cheap as it cost much less than a car. You compare the current price of a shirt to its history. It's the same in option pricing!

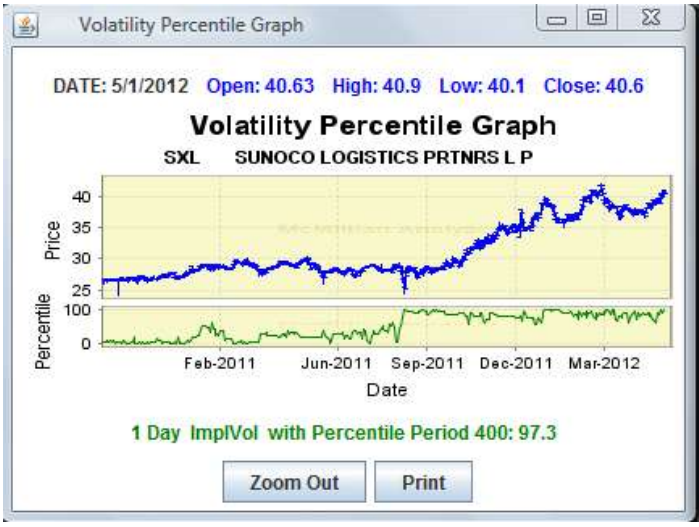
Let's compare option prices of two stocks:

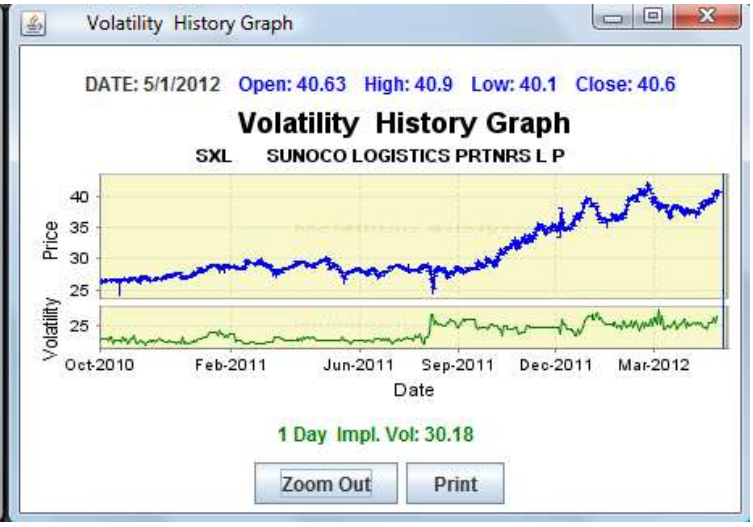
1. SXL – Sunoco Logistics Partners
2. VHC - VIRNETX HLDG CORP

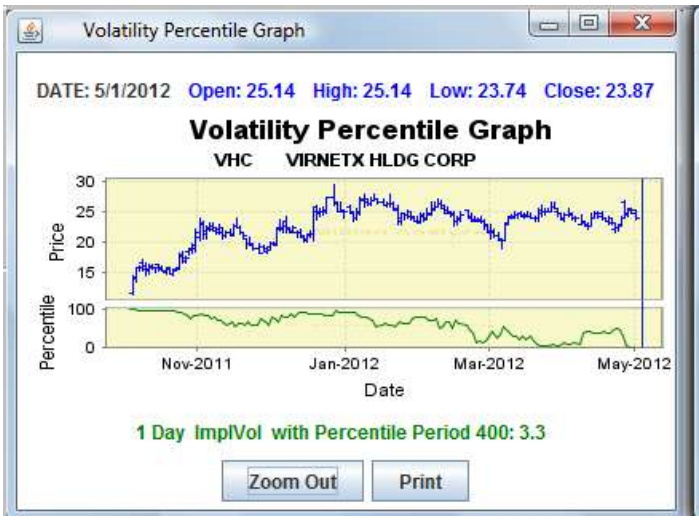
SXL has an Implied Volatility equal to 30.18% and VHC is more than two times higher at 72.48%. At the same time if you look at the charts below, SXL's Volatility is in the 97th percentile, which is almost its highest value in the last 400 days, while VHC's volatility is in the 3$^{rd}$ percentile almost the lowest in the last 400 days.

**The Absolute value of the implied volatility does not show whether today's option price for the stock is Cheap or Expensive. Only the comparison of prior volatility readings within the same stock tells us its real status.**

The Volatility Percentile and Volatility History charts that are available in **Ez Trade Builder** make it easy to determine when options are **Expensive** and when they are **Cheap**. Take a look on the charts below to understand how important Volatility Percentile value is in comparing option prices of two different underlyings.

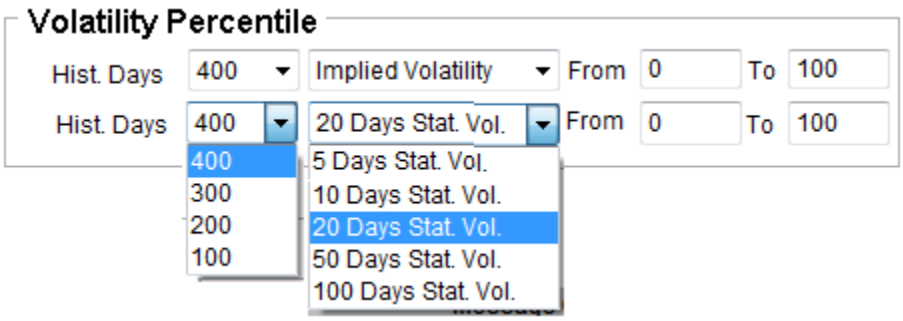




## How to set-up Volatility Percentile Range Filter.




As can be seen in the picture above **Ez Trade Builder** allows one to set the Percentile Filter for two different volatilities. It also allows you to set the historical time period, in days, one wants to analyze.

Setting Percentile Range is dependent upon the option strategy you choose. If the strategy assumes selling options (Short Put, Call/Put Credit Spreads, Iron Condors and etc.) the Percentile Range should be set to find

Expensive options. For strategies that involve buying options (Straddle, Strangle and etc.) Percentile Range should be set to find Cheap options.


Volatility Filter and Percentile Range Filter complement each other by helping to not only predict direction of a future volatility move, but also watch the investment required to execute a trade that could substantially improve Expected Return.

For more in-depth coverage please check information on our on-line Webinars or Mentoring programs.