Volatility as a judgement

> **VOLATILITY AS A JUDGEMENT**
>
> The third and most options-unique judgement: whether the underlying will move more or less than the premium's implied volatility already prices. A bought option needs the actual move to exceed the priced one; a sold option profits if it falls short. This is a judgement about the market's expectation itself - the crowd-reading discipline applied to volatility - and it is the judgement share traders have no instinct for, which is why they lose to it.

The third judgement is the one shares never required and options traders most often ignore: not which way or when, but whether the move will exceed what the market already expects. Volatility is a judgement about the crowd's expectation, and it is where directional traders lose while being right.

What the volatility judgement is

Implied volatility is the market's expectation of movement, baked into the premium (module 1) - so buying an option is buying an expected move at a price, and the option pays only if the actual move exceeds the priced one. The volatility judgement is whether it will: is the market's implied volatility too low (the move will be bigger than priced, favouring the buyer) or too high (the move will fall short, favouring the seller)? This is a judgement about the market's own expectation - a disagreement with the crowd's priced consensus on movement, held to the platform's crowd-reading discipline.

Implied versus realised, as the judgement

Buying when implied is low: if the market underprices the coming move, a bought option's premium is cheap relative to what the underlying will do - the buyer's favourable volatility judgement.Selling when implied is high: if the market overprices the coming move, a sold option collects an inflated premium against a move that falls short - the seller's favourable volatility judgement, with the tail risk of module 4 attached.The event case: implied volatility inflates before events and crushes after (module 1) - so buying into an event pays high implied volatility (a poor volatility judgement unless the move is exceptional), and selling into it collects the inflation (a favourable one, with the event's gap risk).

Why share traders lose to it

A share trader has no volatility judgement - a share has no implied volatility - so the instinct to buy an option on a directional view ignores whether the volatility is expensive, and the buyer overpays for a move the market already expected. The famous loss is buying calls before earnings: correct that the stock will move, wrong that the move will exceed the inflated implied volatility, and the position loses to the crush. The volatility judgement is the options-specific skill: reading whether the market's priced movement is too high or too low, and positioning with the reading rather than against it. It is the third judgement, the hardest for share traders, and the one that most often turns a correct direction into a loss.

Check your understanding

1. What is the volatility judgement?

a. Whether the underlying is volatile

b. Whether the underlying will move more or less than the premium's implied volatility already prices - a disagreement with the market's own expectation of movement

c. Whether to buy a call or a put

Answer: b. A bought option needs the actual move to exceed the priced one. The judgement is about the crowd's priced consensus on movement - the crowd-reading discipline, applied to volatility.

2. Why do share traders lose to the volatility judgement?

a. They trade too little

b. A share has no implied volatility, so they have no instinct for it - buying calls before earnings, correct on direction but wrong that the move exceeds the inflated implied volatility, losing to the crush

c. They pay more commission

Answer: b. The share trader's instinct ignores whether the volatility is expensive. The volatility judgement is the options-specific skill share traders most lack - and most lose to.