

Definitions connected to call-option

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Put-call parity is a concept that explains the relationship between the put option and the call option of stocks when the two options have the same strike price and maturity dates. Put call parity applies primarily to European options since they can only be exercised at maturity. Because American style options permit an early exercise the put-call parity does not apply, unless the options are held to maturity (Gregoriou 471).

In the money is a situation where the strike price of a call option is below the market price of the underlying stock or its put option is above the market price. An in the money situation means that the stock is worth exercising. For example, a call option on a stock with a strike price of \$ 10 and the price of the stock sitting at \$ 15 is considered to be in the money (Sincere 45).

Out of the money is a situation where the strike price of a call option is higher than the market price of the underlying stock or its put option is lower than the market price. An out of the money stock does not have an intrinsic value, but only an extrinsic value. For example, where a stock is trading at \$ 20 call options with strike prices over \$ 20 would be out of the money (Sincere 45).

At the money is a situation where the options strike price is equal to the price of the underlying security. Both the call and put options will be at the money in such a situation. For example, if stocks are trading at \$ 20 then the \$ 20 call options as well as the \$ 20 put option are at the money (Sincere 44).

Options on futures are options with futures contracts as their underlying assets. The option on futures gives the holder the right to enter into a specific futures contract when the option expires. An option on futures is formed when futures are made to trade an asset and then options are made

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to trade the future contracts at definite strike prices (Gregoriou 11).

Implied volatility is the projected volatility of a stock's price. Implied volatility shows how the markets will be volatile in the future and is also helpful in calculating probability of reaching a certain price. For instance, implied volatility decreases when the market is bullish and increases when the market is bearish (Gregoriou 231).

Works cited

Gregoriou, Greg N., ed. Encyclopedia of alternative investments. CRC Press, 2008.

Sincere, Michael. Understanding options. Michael Sincere, 2006.