⇒ Call options

In a call option, the option buyer has the right (But not the obligation) to buy the commodity at the predetermined price.

For ex:— Jerry House paid a premium of ₹ 4 per share for one 6-months call option contract (total of ₹ 400 for 100 shares) of the Mahony Corporation. At the time of the purchase, Mahony stock was selling for ₹ 56 per share and exercise price of call option was ₹ 55.

① Determine jerry's profit or loss if the price of Mahony's stock is ₹ 54 when option is exercised?

② What is jerry's profit or loss if the price of Mahony's stock is ₹ 62 when option is exercised? Ignore taxes and transactions cost.

Sol:– ① Cost of Call ⇒ ~~[illegible]~~.

$\Rightarrow (₹\,4 \text{ premium}) \times 100 \Rightarrow 400$

ending Value $= (-400 \text{ cost}) + (0 \text{ gain})$

$= 400$ loss.

The option was worthless because the stocks price is less than the exercise price at maturity.

② Cost of Call $=$ ₹ 400.

Ending Value $= -400 + (62 - 55) \times 100$

$= -400 + 700$

$= 300$ gain.