

Types of Options

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- Options are a type of derivative, and hence their value depends on the value of an underlying instrument. The underlying instrument can be a stock, but it can also be an index, a currency, a commodity or any other security.
- There are many different types of options that can be traded and these can be categorized in a number of ways. In a very broad sense, there are two main types: calls and puts.

- Calls give the buyer the right to buy the underlying asset, while puts give the buyer the right to sell the underlying asset. Along with this clear distinction, options are also usually classified based on whether they are American style or European style. This has nothing to do with geographical location, but rather when the contracts can be exercised.

- Options can be further categorized based on the method in which they are traded, their expiration cycle, and the underlying security they relate to. There are also other specific types and a number of exotic options that exist

- Calls
- Call options are contracts that give the owner the right to buy the underlying asset in the future at an agreed price. You would buy a call if you believed that the underlying asset was likely to increase in price over a given period of time. Calls have an expiration date and, depending on the terms of the contract, the underlying asset can be bought any time prior to the expiration date or on the expiration date

- Puts
- Put options are essentially the opposite of calls. The owner of a put has the right to sell the underlying asset in the future at a pre-determined price. Therefore, you would buy a put if you were expecting the underlying asset to fall in value. As with calls, there is an expiration date in the contract.

- American Style
- The term “American style” in relation to options has nothing to do with where contracts are bought or sold, but rather to the terms of the contracts. Options contracts come with an expiration date, at which point the owner has the right to buy the underlying security (if a call) or sell it (if a put). With American style options, the owner of the contract also has the right to exercise at any time prior to the expiration date. This additional flexibility is an obvious advantage to the owner of an American style contract

- European Style
- The owners of European style options contracts are not afforded the same flexibility as with American style contracts. If you own a European style contract then you have the right to buy or sell the underlying asset on which the contract is based only on the expiration date and not before.



- Exchange Traded Options
- Also known as listed options, this is the most common form of options. The term “Exchanged Traded” is used to describe any options contract that is listed on a public trading exchange. They can be bought and sold by anyone by using the services of a suitable broker.

- Over The Counter Options
- “Over The Counter” (OTC) options are only traded in the OTC markets, making them less accessible to the general public. They tend to be customized contracts with more complicated terms than most Exchange Traded contracts.