

- You think that Big 'n' Oily Malted Balls candy (symbol BOMB) is going to be the next big thing. The stock is currently selling for \$29. You purchase a call options contract to buy 100 shares at \$30. The price of the option was \$2. Answer the following questions: *market price = 29 strike price = 30 \$1 out-of-the-money*

 - Is your option: a) "in-the-money" b) "at-the-money" c) "out-of-the-money"
 - What is the break-even point for your option? *option price \$2 + strike price \$30 = \$32 break-even point*
 - Ignoring commissions, if the stock price rose to \$36, what would be your profit?
*\$36 stock price - \$32 break-even point = \$4 profit * 100 shares = \$400 profit for one contract*
- You are sure that the price of Opie's Obedient Pet Service (symbol OOPS) is far too high. You think investors have bid up the price to an outrageous amount. About a month ago, you purchased a put options contract to sell 100 shares at \$90. The price of the option was \$3. The stock is currently selling for \$88. Answer the following questions: *\$90 strike price \$88 market price*

 - Is your option: a) "in-the-money" b) "at-the-money" c) "out-of-the-money" *\$2 in-the-money*
 - What is the break-even point for your option? *Strike price \$90 - option price \$3 = \$87 break-even price*
 - Ignoring commissions, if the stock price fell to \$82, what would be your profit?
*\$87 break-even price - \$82 stock price = \$5 profit * 100 shares = \$500 profit for one contract*
- Your broker calls you and says, "Ya' know, straddles are a great way for you to generate commissions, uh, I mean make money. This stock, Young's Underwater Crab Hatchery (symbol YUCH), is extremely volatile. It's currently selling for \$33. I suggest you purchase a call option to buy at \$35 and a put option to sell at \$35. The price of the call option is \$2 and the price of the put option is \$5." Even though you're not quite sure whether or not this is a good idea, you go ahead with the offer from your broker. Answer the following questions: *\$2 call + \$5 put = total price \$7 * 100 shares = \$700*

 - What's the total price of your options (excluding commissions)? *call + put = total price \$7 * 100 shares = \$700*
 - How far does the stock price have to swing from \$35 in either direction before your straddle is "in-the-money?" (i.e. What's the break-even point?)
must swing \$7 in either direction above \$42 or below \$28
- You purchased 100 shares of Pretzel's Unlimited (symbol PU) some time ago when the price was \$10. The current price is around \$72. You are thinking of selling but you aren't sure. Instead, you sell (write) a single call options contract at the strike price of \$75. The option price was \$1. Answer the following questions: *\$1 * 100 = \$100 option premium*

 - How much money did you receive when you sold (wrote) the call options contract? *strike price = \$75*
 - If the option is exercised, what price will you receive for your 100 shares of PU stock?
 - What is the total amount you will receive? What are the disadvantages of this strategy?
*\$75 strike price + \$1 option price = \$76 per share * 100 shares for one contract = \$7600 received*
If the price were to rise very high, you would lose the opportunity to sell the stock at the very high price
- Fire Abatement Technology (symbol FAT) is currently selling for \$15. You are thinking of purchasing 100 shares but you're not quite sure. Instead, you sell (write) a single put options contract with a strike price of \$15. The put option sells for \$2. Answer the following questions: *\$2 option price * 100 shares for one contract = \$200 received*

 - How much money did you receive when you sold (wrote) the put options contract? *strike price \$15*
 - If the option is exercised, what price will you pay for the 100 shares of PU stock? *\$15 - 2 = \$13 effective price*
 - What's the effective price per share that you paid for PU (assuming the option is exercised)?
 - Is this an effective strategy? What are the advantages and disadvantages?
It may be an effective strategy -- as long as you have the cash (covered put option)
advantage - cheaper price than what you would have paid
disadvantages - price could fall very low and you still have to buy the stock at \$15 - might not get the stock if price goes up