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Volatility and Derivatives

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JMDinvestments

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Volatility and Derivatives

There are six primary inputs used to determine the price of a stock option: underlying stock price, exercise price, time to expiration, volatility of the underlying stock's price, market interest rate, and dividend yield on the underlying stock. Each has a particular relation to option value. For example, as stock price increases, the value of a call would increase, while the value of a put would decrease. For volatility, an increase in volatility has a positive impact on the value of both puts and calls, since payoffs are asymmetric. That is, no matter how low the stock's price goes, all an investor can lose is the premium. Last year market volatility was low. This led to a good year for equities, but the derivative market lagged as a result of the lower volatility. [See article here, The Trade News.](#)

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