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Euronext
Introduction to Options Trading

Michael Barclay
Senior Product & Sales Manager
Euronext

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Disclosure:

Introduction to Options

Anticipating price movements through options trading

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September 2024

What is an Option?

Investors can acquire the option to buy or sell an underlying asset

An option is a derivative contract: **its value changes according to changes in the price of an underlying asset.**
For example, the value of an option on the CAC 40 Index changes with movements in the price of the CAC 40.

An option is a right.
There exist two types of 'rights': **calls** (right to **buy** an underlying) and **puts** (right to **sell** an underlying).

What is an Option?

All contract conditions are established in advance

Investors can choose the price at which they wish to buy or sell the underlying asset (such as an index or a share). This pre-determined price is called the **strike price**.

The investor can choose the duration of the contract. These range from daily, weekly, monthly and yearly periods. This is known as the **maturity** date of the contract.

To acquire the right to buy or sell an underlying, the option holder must pay a **premium**.

What is an Option?

Options markets are where rights to buy and sell an underlying are traded.
The buyer has the right, however the **seller** has an **obligation**, as they must deliver the contract if the option is exercised by the buyer.

Buyer

Pay a premium

Holds the option right

Risk limited to the price of the premium paid

Seller

Receive a premium

Has an obligation

Potentially unlimited risk

Where to trade Options?

Trade options via international exchanges, supported by a central counterparty clearing house that guarantee the terms of trades.

Why Trade Options?

Options can be used to hedge portfolio risk.

Holding an option allows investors to either benefit from increasing prices, or to hedge versus falling prices

Options can be used to boost the performance of portfolios

Benefit from positive effects of leverage

Paying an option premium often requires far less capital outlay than buying the underlying, whilst still allowing holders to generate benefits from underlying price movements

Risks to be Aware of When Trading Options

Options can be complex! Sufficient knowledge is required to trade options

Options trading bears risk and certain option strategies can have potentially unlimited losses

Liquidity varies between different contracts and different maturities

Six Key Components of an Option Premium

	Call Price	Put Price
Underlying Price	▲	▼
Interest Rates	▲	▼
Maturity	▲	▲
Underlying Volatility	▲	▲
Exercise Price	▼	▲
Dividends	▼	▲

The Power of Leverage

Leverage allows investors to increase their exposure to an asset with low capital outlay.
This can amplify potential gains, but also losses.

Context: An investor anticipates a rise in the price of the CAC 40 index in 2024.

CHOICE 1: Buy a CAC 40 ETF

- Purchase Price: €40
- Investment: 100 × 40 = €4,000

CHOICE 2: Buy a CAC 40 Call Option

- Strike Price: €8,200
- Maturity: December 2024
- Premium: €400
- Investment: 1 contract × 10 × 400 = €4,000

At the end of December 2024, the CAC 40 price has risen by 10% to 9,020 points

Profit at maturity:

(ETF CAC 40 Price – Purchase Price) × Quantity

(44 – 40) × 100 = €400

$$\textbf{Profit} = \frac{400}{4\,000} = \textbf{10\%}$$

Profit at maturity:

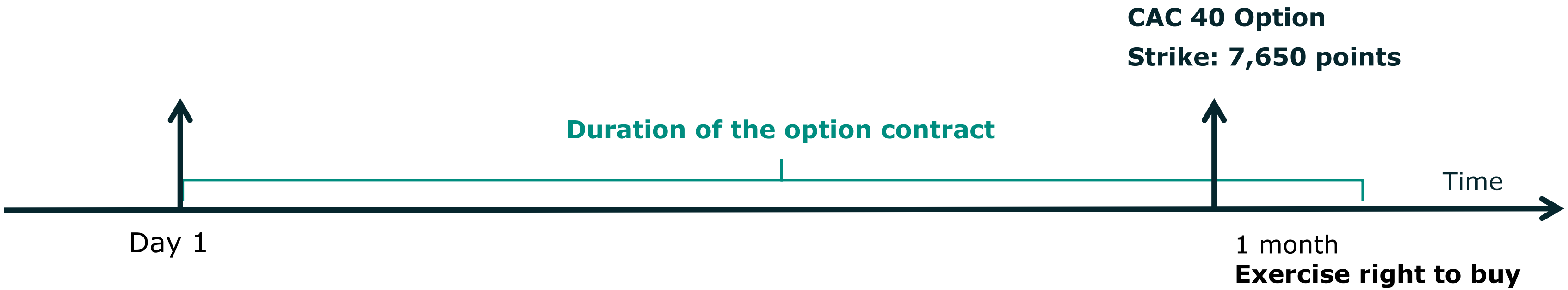
(CAC 40 Price – Strike Price – Premium Paid) × Quantity × Contract Multiplier

(9,020 – 8,200 – 400) × 1 × 10 = €4,200

$$\textbf{Profit} = \frac{4\,200}{4\,000} = \textbf{105\%}$$

Option to Buy (Call)

Underlying: CAC 40 Index
Price: 7,500 points, worth €10 per point
Prediction: Bullish



- Buy an option to buy (call) on the CAC 40 / 1 month expiry / 7,650 strike price
- Pay a **premium of €25**

Case study:

- The CAC 40 rises past 7,800 points
- The option holder exercises the right to buy in 1 month
- The profit is calculated by subtracting the current underlying price by the exercise price and the premium paid

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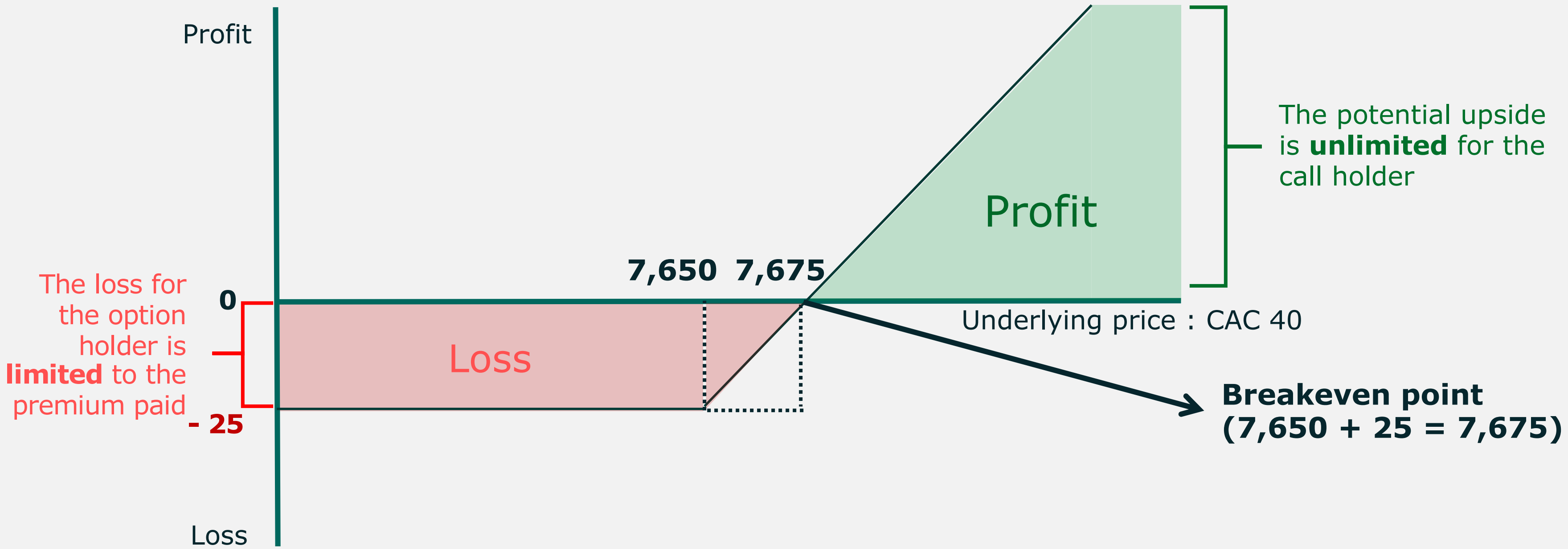
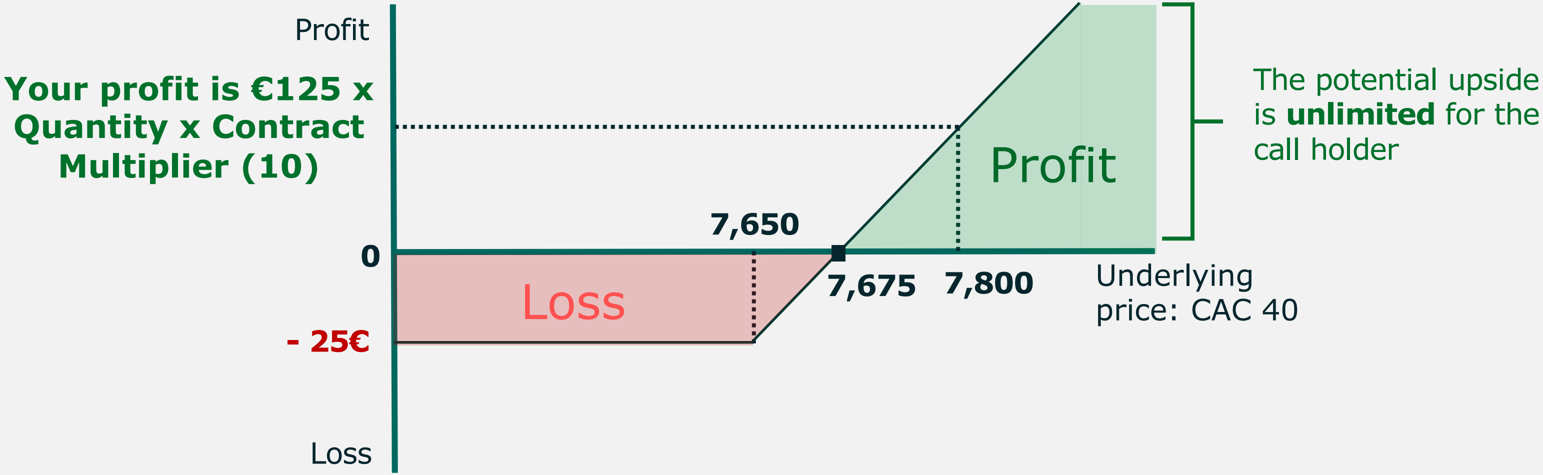
Long Call Position

- CAC 40 Index: current price of 7,500 points
- Prediction: Bullish ▲
- Long Call position on the CAC 40 / 7,650 strike price / premium: €25



Long Call Position

Your prediction comes to fruition: the CAC 40 reaches **7,800 points**



Gains:	**+ €7,800 (Underling price at maturity)**
	– €7,650 (Strike Price)
	– €25 (Call Price)
	= €125/contract

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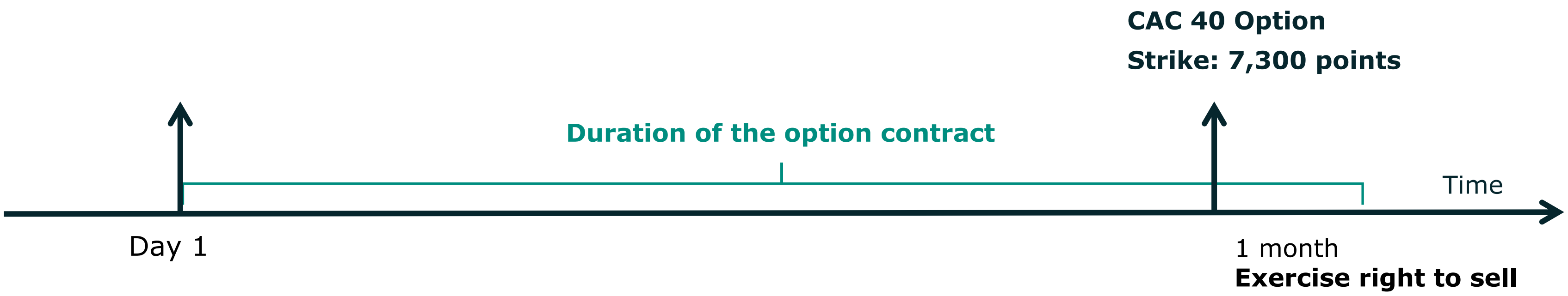
Option to Sell (Put)

Underlying: CAC 40 Index
Price: 7,500 points, worth €10 per point
Prediction: Bullish

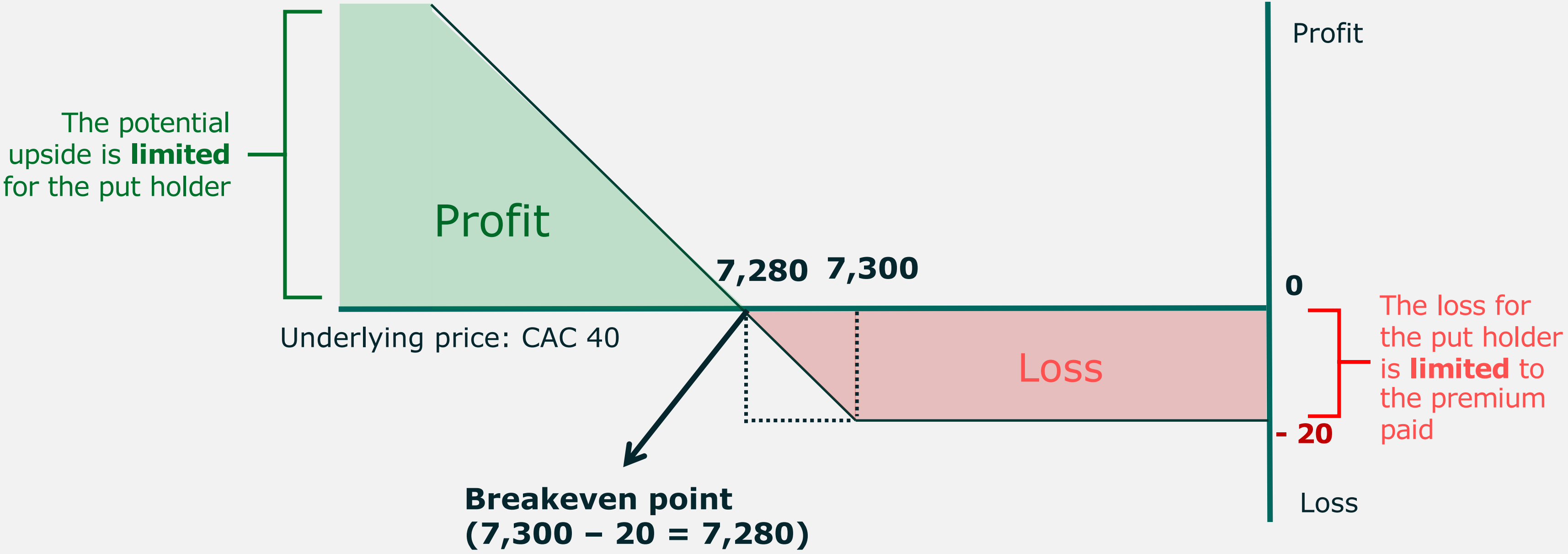


- Buy an option to sell (put) on the CAC 40 / 1 month expiry / 7,300 strike price
- Pay a **premium of €20**

Case study:
- The CAC 40 falls below 7,500 points, falling to a price of 7,100
- The option holder exercises their right to sell in 1 month
- The profit is calculated by subtracting the strike price of 7,300 by the current index price and the premium paid

Long Put Position

- CAC 40 Index: current price of 7,500 points
- Prediction: Bearish ▼
- Long Put position on the CAC 40 / 7,300 strike price / premium: €20



Long Put Position

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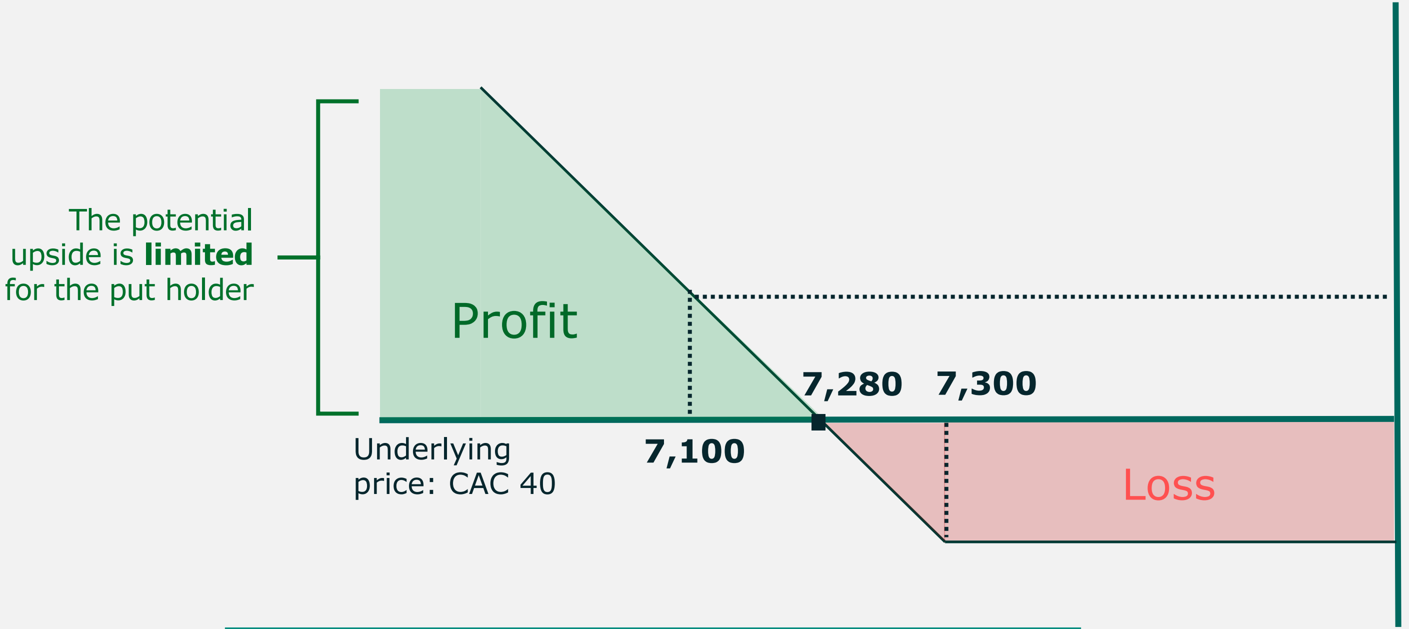
Your prediction comes to fruition: the CAC 40 reaches **7,100 points**



Your profit is €180 × Quantity × Contract Multiplier (10)

Gains: **- €7,100 (Underlying Price at Maturity)**
+ €7,300 (Strike Price)
– €20 (Premium)
= €180/contract

Thank you for listening.
For more information on options and additional financial derivatives products, please check Euronext website:

https://www.euronext.com/en/for-investors/financial-derivatives

Contacts

Charlotte Alliot
Group Head of Institutional Derivatives
calliot@euronext.com

Michael Barclay
Derivatives Business Development Manager
mbarclay@euronext.com

Emma Rosenthal
Retail Business Development Manager
erosenthal@euronext.com

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