

Som-Lalit Institute of Management Studies (SLIMS)

Subject Code: 4539222, Subject Name: Financial Derivatives, Sem III

Written by Mrs. Rani Shah, Assistant professor, SLIMS

Topic: Using butterfly option strategy, module 3

A trader named Mr Maliya expects his favourite stock TCS to trade around Rs 950 (with about 2-3% spread on the higher side). Overall market is volatile and therefore he does not want to take price risk. He is able to invest in TCS call options having strike price Rs 930, Rs 955 and Rs.975 with strike price of Rs.950. Details are as below-

Call option of strike price $X= 930$, $C = 40$

Call option of strike price $X= 955$, $C = 51$

Call option of strike price $X= 975$, $C = 65$

1. Suggest an appropriate low cost option trading strategy to Mr Mukesh
2. Draw a diagram and show the pay-off matrix under each possible scenario.