EXAM FM QUESTIONS OF THE WEEK

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Week of May 7/07

You are given the following European option premiums at various strike prices. The options all expire in one year and the underlying stock pays no dividends.

Strike Price	Call Price	Put Price
20	16.62	0.66
30	9.94	3.50
40	5.71	8.79
50	3.24	15.85

What is the premium now on a long forward contract on the stock for delivery in one year at a delivery price of $30?

A) – 6.44 B) – 3.08 C) 0 D) 3.08 E) 6.44

The solution can be found below.

Week of May 7/07 - Solution

A long forward can be created synthetically with a long call and a short put whose strike prices are the forward delivery price. The value of the long forward with delivery price 30 is $C_{30} - P_{30} = 9.94 - 3.50 = 6.44$. Answer: E