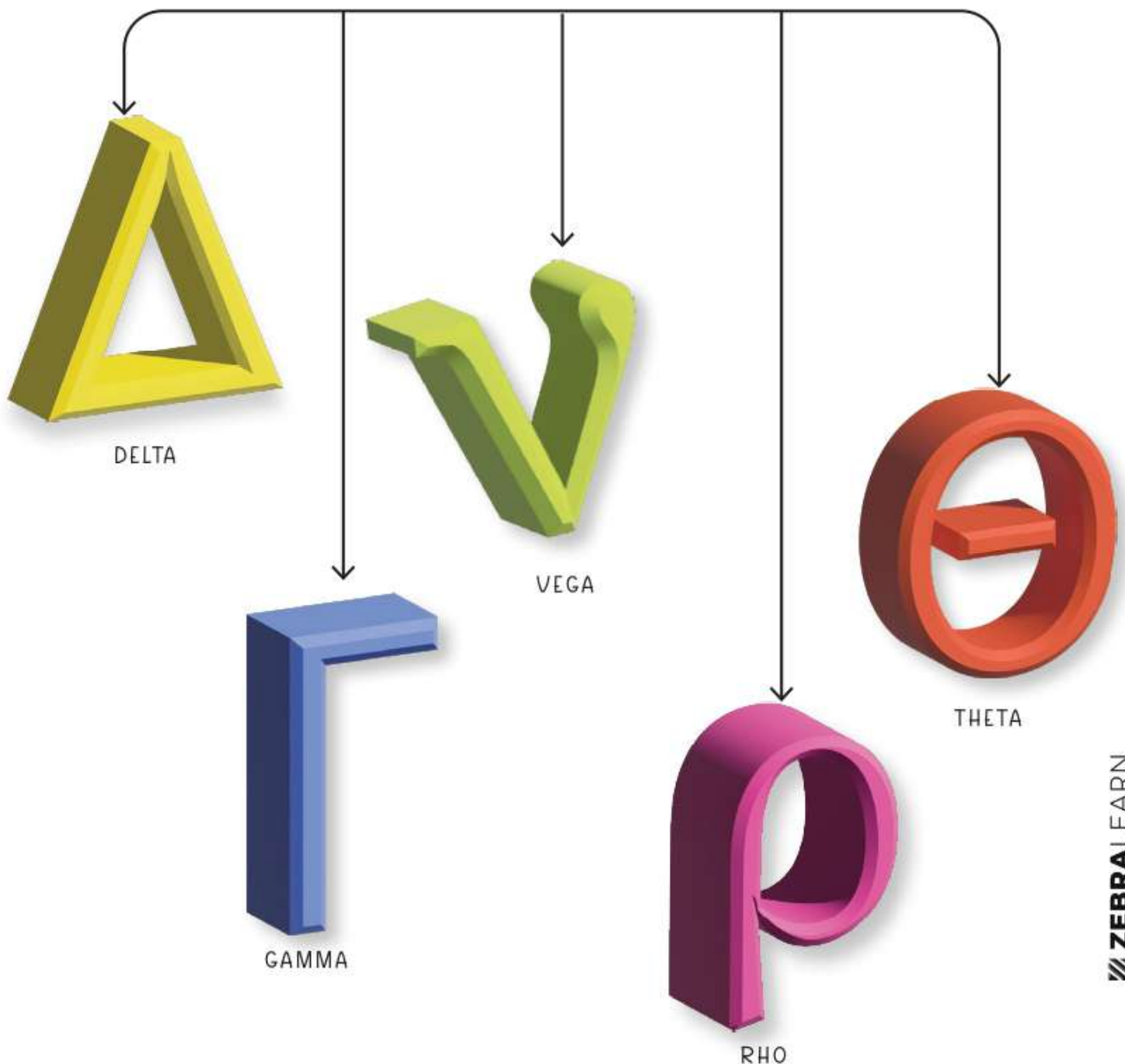


9.6 WHAT ARE OPTION GREEKS?



Explainer Video

Option Greeks refer to different financial measures that help us understand the sensitivity of an option contract in relation to the factors that affect the option pricing. For instance, it shows how sensitive is option's price to time to expiry, how sensitive is option's price to volatility in the market and so on. Different Greeks are used - Delta, Vega, Gamma, Rho and Theta. Do not stress about using them from day 1. Make sure you understand these well. But only with time in the market will you get comfortable with trading based on Option Greeks. Lets understand each one that we have mentioned.



DELTA



Delta talks about how much the price of the options changes with a change in the price of the underlying asset.

For example, if the price of the underlying changes by 1%, and the option price changes by 20% then we can say that the delta for this option contract is 20.

$$\text{DELTA} = \frac{\% \text{ CHANGE IN OPTION}}{\% \text{ CHANGE IN PRICE OF UNDERLYING ASSET}}$$

Gamma is simply the change in Delta with respect to the change in underlying asset price. Here we intend to understand, how quickly option's sensitivity to underlying price changes.

$$\text{GAMMA} = \frac{\% \text{ CHANGE IN DELTA}}{\% \text{ CHANGE IN PRICE OF UNDERLYING ASSET}}$$

GAMMA



VEGA



Vega tells us about how much the option price changes with a change in the volatility of the underlying asset.

$$\text{VEGA} = \frac{\% \text{ CHANGE IN OPTION}}{\% \text{ CHANGE IN VOLATILITY}}$$

Rho tells us about how much the option price changes with a change in the risk-free rate of return.

$$\text{RHO} = \frac{\% \text{ CHANGE IN OPTION}}{\% \text{ CHANGE IN RISK FREE RATE OF RETURN}}$$

RHO



THETA



Theta tells us about how much the option price changes with a change in the time to expiry of the contract.

Option Greeks are commonly used tools by traders who trade in Options. It tells them how sensitive is an option to different factors that affect the option's price. Again, do not stress about using them from day 1. Just spend time and get comfortable with them first.

Understanding option pricing and how different factors affect this pricing is fundamentally important to understand before we move ahead with option strategies. Try spending as much time as possible on different option chains on the NSE website. Calculate Option Greeks for different options. Look for reasons behind difference in prices of different option contracts.

With this, we conclude our discussion on option pricing and the different factors that affect the price of any given option contract. Remember, practice is the key. More time you spend on the Option chain, more comfortable will you get with these factors. Now, in the next chapter, we move ahead with different option strategies. Lets get started with them.

