

CHAPTER 6

BASICS OF OPTIONS PAYOFF CHARTS

- 6.1 Introduction
- 6.2 Understanding payoff charts for call options
- 6.3 Understanding payoff charts for put options

6.1 INTRODUCTION

“

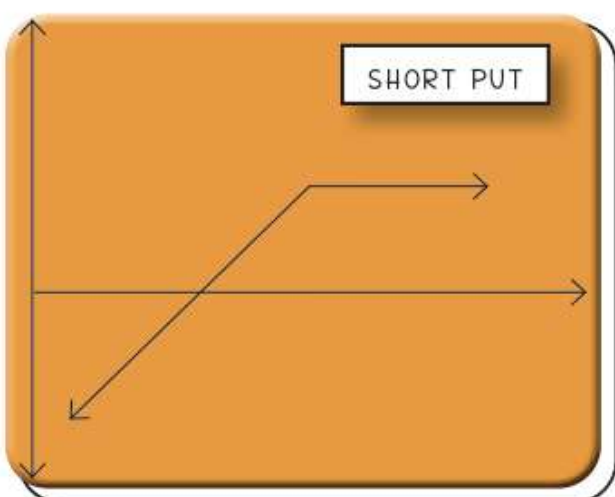
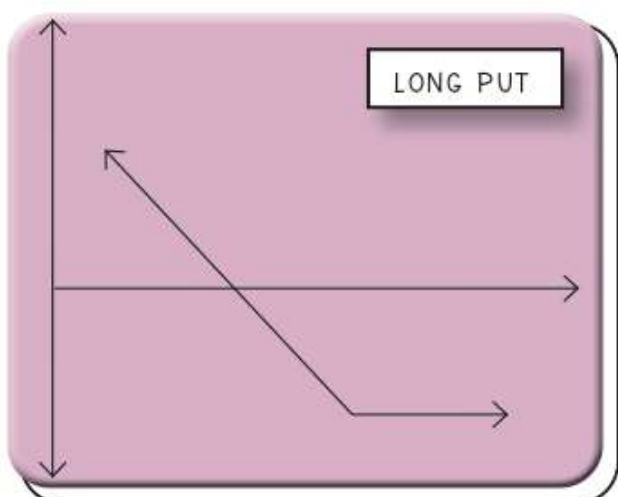
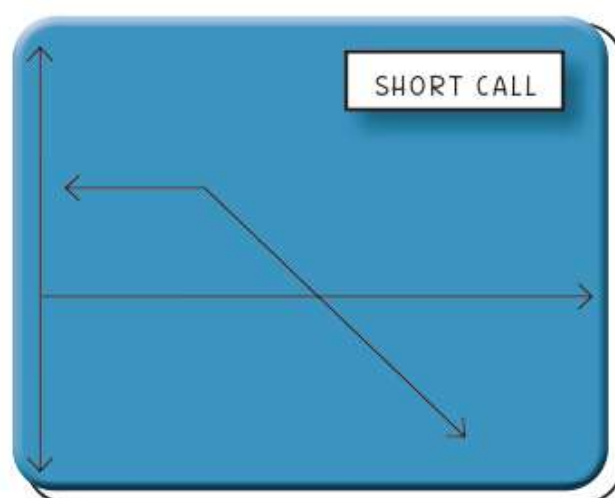
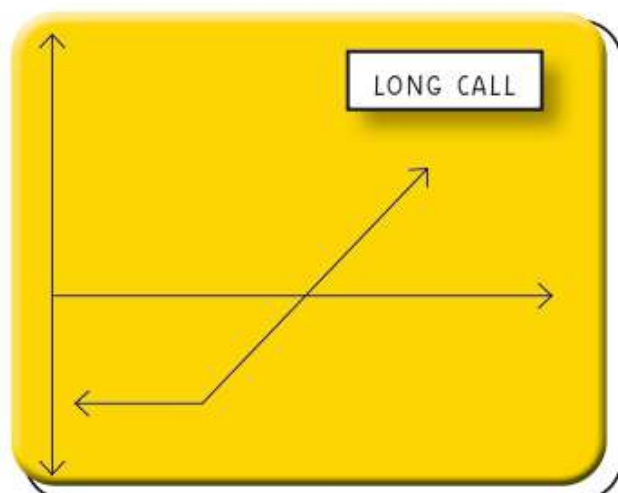
OPTION PAYOFFS MEANS THE PROFITABILITY OF AN OPTION UNDER DIFFERENT PRICE CONDITIONS.

”

It helps us to understand the Risks/Rewards profile before taking a trade. The payoff charts are visually represented using graphs and are really important when it comes to more complex strategies.



Pay off charts are graphical representation of the profit/loss at different price levels on the date of expiry. The X axis is used to denote various prices possible on the date of expiry and Y axis denotes the profit or loss incurred in the transaction. Such pay-off graphs help us visualise and understand the circumstances under which we will profit and circumstances under which we will incur losses. This helps us calculate the risk-reward ratio too.



Let us begin with simple payoff charts for simple call and put option from a buyer as well as a seller point of view. We will go into more detail or complex pay-off charts further when we will create payoff charts for different option strategies.