REFERENCES

CFTC (2007) *Legal Text United States: Commodity Exchange Act*, 7 USC 1a.

Kloner, D. (2001) The Commodity Futures Modernization Act of 2000. *Securities Regulation Law Journal*, 29, 286.

Parkinson, P. M. (2000) Statements to the Congress. *Federal Reserve Bulletin*, 86, 644–645.

Exercise Option

M. Nihat Solakoglu
Bilkent University
Ankara, Turkey

The holder of an option contract may decide to exercise the option at the exercise or strike price if the contract is in the money. Exercising indicates that transaction of the asset takes place at the predetermined exercise price and the contract is terminated. For a European type option, holder of the contract can decide to exercise the option only at the maturity. However, for an American type option, holder of the contract has the flexibility to exercise the option before the expiration date. For a call option, which gives the owner the right, but not the obligation, to buy an asset at the exercise price, the contract will be *in the money* when exercise price is below the spot price, and owner of the contract will decide to exercise the option to take delivery of the asset. For a put option, on the other hand, owner of the contract will decide to exercise his/her rights if exercise price is above the spot price.

REFERENCES

Bodie, Z., Kane, A., and Marcus, A. J. (2003) *Essentials of Investments*. McGraw-Hill, New York, NY.

Hull, J. C. (2000) *Options, Futures, and Other Derivative*. Prentice Hall, Upper Saddle River, NJ.

Ross, S. A., Westerfield, R. W., and Jaffe, J. (2005) *Corporate Finance*. McGraw-Hill, New York, NY.

Exercise Price

M. Banu Durukan
Dokuz Eylul University
Izmir, Turkey

Exercise price, also called the strike price, of an option is the predetermined fixed per unit price at which the underlying asset is bought or sold if the option is exercised. This price once set never changes during the life of the option. The holder uses this price as a decision criterion when deciding to exercise the option (Kolb, 2000). If the exercise price provides a profitable opportunity then the holder will use the option. For example, in a call (put) option, the option will be exercised if the exercise price is less (greater) than the current market price of the underlying asset. In this case the holder of the option will have the opportunity to buy (sell) the underlying asset at a lower (higher) price than the market by using the option and have the opportunity to profit by selling (buying) the asset at a higher (lower) price at the market. In other words, the holder will exercise the option if it is in the money. Table 1 exhibits

TABLE 1

An Option in the Money, at the Money, and out of the Money

Option	Out of the Money	At the Money	In the Money
Call	$X > S_T$	$X = S_T$	$X < S_T$
Put	$X < S_T$	$X = S_T$	$X > S_T$

Note: X, exercise price; S_T, market price of the underlying asset.