



ASX

AUSTRALIAN SECURITIES EXCHANGE

# ASX Index Options

## Fact Sheet

### What are Index Options?

Index options over the S&P/ASX 200 Index (commonly referred to as XJO Index Options) provide wide coverage of the share market.

Regarded as a leading benchmark by professional investors for broad movements in the stockmarket, the S&P/ASX200 Index reflects the prices of the largest 200 stocks currently listed on ASX, and represents almost 80% of the market as a whole.

There are put and call index options with different exercise prices and a tick value of \$10 per point of the S&P/ASX 200 Index.

Using index options, it only takes one simple transaction to hold a view across the broad market. The same principles that apply to buying and selling stock options apply to index options. They offer you the investment and risk management tools used by fund managers.

XJO Index Options cash settle against the value of the S&P/ASX 200 Index and are European style options. Unlike futures-styled index options where the underlying is a futures contract, the XJO is a premium-upfront option.

For all share investors, large or small, this means you can:

- participate in many of Australia's leading companies in one trade as a cost-effective alternative to stock ownership
- protect the value of your share portfolio e.g. by the purchase of an index put option
- earn extra returns e.g. by selling an index call option
- diversify your portfolio
- profit on the performance of the benchmark stocks used by professional investors
- tailor your exposure to take advantage of limited risk strategies.

### Why invest in index options?

#### 1. One Easy Transaction

Buying an XJO call option gives you exposure to a share portfolio of 200 of the largest stocks on the market. This may be an effective way to gain market exposure if you have limited funds.

#### 2. More Trading Opportunities

With the ease of trading and low transaction costs, you can gain short-term exposure to market moves and profit from small changes due to leverage. You can take advantage of trading opportunities whilst leaving your share portfolio intact. Advanced investors can also write options, which allows them to earn income.

#### 3. Protect the Value of Your Share Portfolio

Buying an XJO put option helps protect your share portfolio from stock market downturns without changing the actual holding. It enables you to reduce the overall market risk of holding shares in falling markets.

#### 4. Minimise the Cost of Trading

XJO Index Options can be used as margin offsets if you are trading other options and cost considerably less than buying every security in the index.

### How do they work?

#### Index options – A trading example:

Let's say that in July 2009 the S&P/ASX 200 Index is at 3800 points and you think the market is going to increase over the next three months. As an alternative to buying a portfolio of shares directly, you decide to buy a September 3800 S&P/ASX 200 call option for 90 points or \$900.

In September the S&P/ASX 200 Index has risen to 4200 points and the September 3800 call is now trading at 430 points (most of the time value has decayed away by now and there is mainly intrinsic value left). You decide to "close out" your position by selling the September 3800 call option and make the following profit:

	MARKET PREMIUM	PREMIUM VALUE
July: Buy 3800 call	90 points	\$900
September: Sell 3800 call	430 points	\$4,300
Profit*	340 points	\$3,400

\* excluding transaction charges, taxes and commissions.

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## Expiry of index options and serial options

Traditionally, ASX has listed index options over the calendar-end quarterly months of March, June, September and December out to a period of 18 months.

The ASX has introduced serial options which are options in near months that will expand the range of available options to cover the immediate three months at any point in time.

Serial Options have been otherwise referred to by ASX in previous Derivatives Notices for equity options as "rolling 1/2/3 expiries".

The expiry date is the third Thursday of the month, unless otherwise specified by ASX.

## Daily settlement price

The Daily Settlement Price (DSP) is determined in the same way for index options as it is for stock options.

While the XJO is an option over the index, market makers hedge their books using ASX SPI 200™\* futures (traded on SYCOM® system). In order to more accurately track the pricing in the market, the Australian Clearing House (ACH) uses XJO futures prices for day-to-day settlement rather than use the value of the index. The XJO futures is in turn priced using the ASX SPI 200® Futures market data where it is available.

At expiry, the futures price and the index pricing converge, so the procedure does not affect the expiry cash settlement based on the Opening Price Index Calculation (OPIC).

\* For this contract the market is operated by Sydney Futures Exchange Limited ACN 000 943 377

## How are margins determined?

The clearing house margin system called TIMS (Theoretical Intermarket Margining System) applies to index options as it does to stock options.

## How do they settle?

XJO Index Options cash settle against the value of the S&P/ASX 200 Index. The settlement price used will be the ASX Opening Price Index Calculation (OPIC). The OPIC is based on the first traded price of each constituent stock in the index on the expiry day. If a constituent stock does not trade on the expiry day, the last traded price from the previous trading day will be used.

## Liquidity risks

The obligations to provide quotes are not unqualified and your ability to trade out of a strategy may depend on if you are able to obtain a quote from a Market Maker. The scope of the obligation of Market Makers is described on page 31 of 'Understanding Options Trading' [www.asx.com.au/resources/publications/booklets.htm](http://www.asx.com.au/resources/publications/booklets.htm)

## Additional information

Consult your advisor, visit the ASX website [www.asx.com.au](http://www.asx.com.au) or contact ASX customer service on 131 279 for further information.

Why not take advantage of an ASX options free online course [www.asx.com.au/resources/myasx/index.htm](http://www.asx.com.au/resources/myasx/index.htm)

Or download a copy of ASX 'Understanding Options Trading' booklet from [www.asx.com.au/resources/publications/booklets.htm](http://www.asx.com.au/resources/publications/booklets.htm)

Like any investment, index options have risks that you need to understand before investing. Specific risks include market risk. You should obtain independent advice from a professional advisor prior to making any final decision.

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