INDEX

acceptance-rejection, 78
American options, 138
antithetic variables, 108
arbitrage opportunity, 19
arbitrageur, 59
Asian options, 136
asset, 57
asset price process, 67
Barrier option, 133
Basket Options, 152
Bayesian statistics, 177
Bernoulli density, 127
binomial lattice, 62
binomial model, 58
Black–Scholes pricing formula, 69
Black–Scholes–Merton equation, 62
boundary conditions, 63
Brownian motion, 42
call option, 57
central limit theorem, 97
CIR model, 166
conditional posterior, 181
confidence intervals, 98
congruential generator, 75
conjugate prior distribution, 179
contingent claim, 62
control variate, 120
coupon rate, 161
current price, 65
delivery date, 65
delivery price, 65
Delta, 146
delta, 102
derivative value, 62
diffusion process, 45
dividends, 71
Dow Jones Industrial Index, 187
down-and-in, 133
down-and-out, 133
drift, 45, 46
dynamic hedge, 24
eurodollars, 151
European call option, 69
European options, 57
European put option, 71
Exchange Options, 151
exchange rate, 151
exercise price, 57
exotic options, 133
expiration, 57
exponential density, 130
exponential family, 196
extrema, 152
Extreme Options, 152

face value, 161
FDM, 146
Feynman–Kac formula, 73
financial derivative, 57
financial index, 151
finite state space, 188
Fixed income securities, 161
Forward contract, 19
futures contract, 19

Gamma, 146
gamma, 104
GBM, 46
generalized error distribution (GED), 92
generalized Wiener process, 45
geometric basket option, 159
Gibbs sampling, 180

heavy-tailed distribution, 92
hedging portfolio, 58
historical volatility, 72
Ho–Lee, 175
hyperparameters, 178

identical and independent distributed (i.i.d.), 41
implied volatility, 72
importance sampling, 125
improper integral, 180
infinitesimally, 65
initial price, 58
instantaneous gain, 62
interest rate movements, 165
interest rate risk, 161
interval estimation, 98
inverse transform, 77
Itô’s lemma, 49

Japanese yen, 151
jump-diffusion model, 183

knock-out option, 64
law of large numbers, 97
least squares approach, 138
likelihood function, 178
limiting distribution, 188
lognormal distribution, 38
long position, 57
lookback options, 135
marginal density, 178
martingale, 45
maturity, 57
maximum option, 157
MCMC, 180
memoryless property, 130
Metropolis–Hastings algorithm, 188
MLE, 106
Monte Carlo, 37
Multiasset options, 151
multiperiod binomial tree, 61
multiple linear regression model, 123
multiplicative factor, 151
multivariate analysis, 156

no arbitrage assumption, 59
noninformative prior, 179

one period binomial model, 58
Option, 26
option Greeks, 145
option premium, 57
option pricing theory, 57
Ornstein–Uhlenbeck process, 53

p.d.f. (probability distribution function), 37
parameter vector, 181
Payoff, 57
percentile, 91
perpetual call, 71
portfolio, 58
posterior distribution, 178
posterior mean, 178
principle component analysis (PCA), 155
principle payment, 162
prior distribution, 178
probability measure, 59
promised payments, 161
INDEX

pseudo-random, 75
put option, 57
put-call parity, 73
quadrature, 36
quantile, 91
quantile-quantile (QQ) plot, 94
Quanto Options, 151
random walk, 41
rate, 80
Rho, 146
risk factors, 157
risk-free rate, 58
risk-neutral asset dynamics, 67
risk-neutral pricing, 20, 65
risk-neutral probability, 60
risk-neutral process, 66
risk-neutral valuation, 60
risk-neutral world, 59
sample mean, 97
sample variance, 98
Scenario analysis, 89
semiannual coupon, 162
short position, 58
short rate, 165
simulation, 35
standard Monte Carlo, 97
standard normal, 68
static hedge, 24
stratified sampling, 114
Stratonovich integral, 55
strike price, 57
tail probabilities, 129
tantamount, 60
Theta, 146
tilted density, 126, 127
time reversibility, 188
transition matrix, 190
transition probabilities, 188
Treasury bond, 161
truncated payoff, 132
value-at-risk (VaR), 91
variance, 46
Vasicek model, 166
Vega, 146
Visual Basic for Applications (VBA), 1
volatility, 45
Wiener process, 43
zero coupon bond, 161