

NAG Library Function Document

nag_asian_geom_price (s30sac)

1 Purpose

nag_asian_geom_price (s30sac) computes the Asian geometric continuous average-rate option price.

2 Specification

```
#include <nag.h>
#include <nags.h>

void nag_asian_geom_price (Nag_OrderType order, Nag_CallPut option,
    Integer m, Integer n, const double x[], double s, const double t[],
    double sigma, double r, double b, double p[], NagError *fail)
```

3 Description

nag_asian_geom_price (s30sac) computes the price of an Asian geometric continuous average-rate option for constant volatility, σ , risk-free rate, r , and cost of carry, b (see Kemna and Vorst (1990)). For a given strike price, X , the price of a call option with underlying price, S , and time to expiry, T , is

$$P_{\text{call}} = Se^{(\bar{b}-r)T}\Phi(\bar{d}_1) - Xe^{-rT}\Phi(\bar{d}_2),$$

and the corresponding put option price is

$$P_{\text{put}} = Xe^{-rT}\Phi(-\bar{d}_2) - Se^{(\bar{b}-r)T}\Phi(-\bar{d}_1),$$

where

$$\bar{d}_1 = \frac{\ln(S/X) + (\bar{b} + \bar{\sigma}^2/2)T}{\bar{\sigma}\sqrt{T}}$$

and

$$\bar{d}_2 = \bar{d}_1 - \bar{\sigma}\sqrt{T},$$

with

$$\bar{\sigma} = \frac{\sigma}{\sqrt{3}}, \quad \bar{b} = \frac{1}{2}\left(r - \frac{\sigma^2}{6}\right).$$

Φ is the cumulative Normal distribution function,

$$\Phi(x) = \frac{1}{\sqrt{2\pi}} \int_{-\infty}^x \exp(-y^2/2) dy.$$

The option price $P_{ij} = P(X = X_i, T = T_j)$ is computed for each strike price in a set X_i , $i = 1, 2, \dots, m$, and for each expiry time in a set T_j , $j = 1, 2, \dots, n$.

4 References

Kemna A and Vorst A (1990) A pricing method for options based on average asset values *Journal of Banking and Finance* **14** 113–129

5 Arguments

- 1: **order** – Nag_OrderType *Input*
On entry: the **order** argument specifies the two-dimensional storage scheme being used, i.e., row-major ordering or column-major ordering. C language defined storage is specified by **order** = Nag_RowMajor. See Section 3.2.1.3 in the Essential Introduction for a more detailed explanation of the use of this argument.
Constraint: **order** = Nag_RowMajor or Nag_ColMajor.
- 2: **option** – Nag_CallPut *Input*
On entry: determines whether the option is a call or a put.
option = Nag_Call
 A call; the holder has a right to buy.
option = Nag_Put
 A put; the holder has a right to sell.
Constraint: **option** = Nag_Call or Nag_Put.
- 3: **m** – Integer *Input*
On entry: the number of strike prices to be used.
Constraint: **m** \geq 1.
- 4: **n** – Integer *Input*
On entry: the number of times to expiry to be used.
Constraint: **n** \geq 1.
- 5: **x[m]** – const double *Input*
On entry: **x**[$i - 1$] must contain X_i , the i th strike price, for $i = 1, 2, \dots, \mathbf{m}$.
Constraint: **x**[$i - 1$] $\geq z$ and **x**[$i - 1$] $\leq 1/z$, where $z = \text{nag_real_safe_small_number}$, the safe range parameter, for $i = 1, 2, \dots, \mathbf{m}$.
- 6: **s** – double *Input*
On entry: S , the price of the underlying asset.
Constraint: **s** $\geq z$ and **s** $\leq 1.0/z$, where $z = \text{nag_real_safe_small_number}$, the safe range parameter.
- 7: **t[n]** – const double *Input*
On entry: **t**[$i - 1$] must contain T_i , the i th time, in years, to expiry, for $i = 1, 2, \dots, \mathbf{n}$.
Constraint: **t**[$i - 1$] $\geq z$, where $z = \text{nag_real_safe_small_number}$, the safe range parameter, for $i = 1, 2, \dots, \mathbf{n}$.
- 8: **sigma** – double *Input*
On entry: σ , the volatility of the underlying asset. Note that a rate of 15% should be entered as 0.15.
Constraint: **sigma** $>$ 0.0.
- 9: **r** – double *Input*
On entry: r , the annual risk-free interest rate, continuously compounded. Note that a rate of 5% should be entered as 0.05.
Constraint: **r** \geq 0.0.

- 10: **b** – double *Input*
On entry: *b*, the annual cost of carry rate. Note that a rate of 8% should be entered as 0.08.
- 11: **p**[**m** × **n**] – double *Output*
Note: where **P**(*i*, *j*) appears in this document, it refers to the array element
 $\mathbf{p}[(j-1) \times \mathbf{m} + i - 1]$ when **order** = Nag_ColMajor;
 $\mathbf{p}[(i-1) \times \mathbf{n} + j - 1]$ when **order** = Nag_RowMajor.
On exit: **P**(*i*, *j*) contains P_{ij} , the option price evaluated for the strike price \mathbf{x}_i at expiry \mathbf{t}_j for $i = 1, 2, \dots, \mathbf{m}$ and $j = 1, 2, \dots, \mathbf{n}$.
- 12: **fail** – NagError * *Input/Output*
The NAG error argument (see Section 3.6 in the Essential Introduction).

6 Error Indicators and Warnings

NE_ALLOC_FAIL

Dynamic memory allocation failed.

See Section 3.2.1.2 in the Essential Introduction for further information.

NE_BAD_PARAM

On entry, argument *<value>* had an illegal value.

NE_INT

On entry, **m** = *<value>*.

Constraint: **m** ≥ 1.

On entry, **n** = *<value>*.

Constraint: **n** ≥ 1.

NE_INTERNAL_ERROR

An internal error has occurred in this function. Check the function call and any array sizes. If the call is correct then please contact NAG for assistance.

An unexpected error has been triggered by this function. Please contact NAG.

See Section 3.6.6 in the Essential Introduction for further information.

NE_NO_LICENCE

Your licence key may have expired or may not have been installed correctly.

See Section 3.6.5 in the Essential Introduction for further information.

NE_REAL

On entry, **r** = *<value>*.

Constraint: **r** ≥ 0.0.

On entry, **s** = *<value>*.

Constraint: **s** ≥ *<value>* and **s** ≤ *<value>*.

On entry, **sigma** = *<value>*.

Constraint: **sigma** > 0.0.

NE_REAL_ARRAY

On entry, **t**[*<value>*] = *<value>*.

Constraint: **t**[*i*] ≥ *<value>*.

On entry, $\mathbf{x}[\langle value \rangle] = \langle value \rangle$.
 Constraint: $\mathbf{x}[i] \geq \langle value \rangle$ and $\mathbf{x}[i] \leq \langle value \rangle$.

7 Accuracy

The accuracy of the output is dependent on the accuracy of the cumulative Normal distribution function, Φ . This is evaluated using a rational Chebyshev expansion, chosen so that the maximum relative error in the expansion is of the order of the *machine precision* (see nag_cumul_normal (s15abc) and nag_erfc (s15adc)). An accuracy close to *machine precision* can generally be expected.

8 Parallelism and Performance

nag_asian_geom_price (s30sac) is threaded by NAG for parallel execution in multithreaded implementations of the NAG Library.

Please consult the X06 Chapter Introduction for information on how to control and interrogate the OpenMP environment used within this function. Please also consult the Users' Note for your implementation for any additional implementation-specific information.

9 Further Comments

None.

10 Example

This example computes the price of an Asian geometric continuous average-rate put with a time to expiry of 3 months, a stock price of 80 and a strike price of 85. The risk-free interest rate is 5% per year, the cost of carry is 8% and the volatility is 20% per year.

10.1 Program Text

```
/* nag_asian_geom_price (s30sac) Example Program.
 *
 * Copyright 2014 Numerical Algorithms Group.
 *
 * Mark 9, 2009.
 */
#include <stdio.h>
#include <math.h>
#include <string.h>
#include <nag.h>
#include <nag_stdlib.h>
#include <nags.h>

int main(void)
{
  /* Integer scalar and array declarations */
  Integer      exit_status = 0;
  Integer      i, j, m, n;
  NagError     fail;
  Nag_CallPut  putnum;
  /* Double scalar and array declarations */
  double       b, r, s, sigma;
  double       *p = 0, *t = 0, *x = 0;
  /* Character scalar and array declarations */
  char         put[8+1];
  Nag_OrderType order;

  INIT_FAIL(fail);

  printf("nag_asian_geom_price (s30sac) Example Program Results\n");
  printf("Asian Option: Geometric Continuous Average-Rate\n\n");
  /* Skip heading in data file */
#ifdef _WIN32
```

```

    scanf_s("%*[\n] ");
#else
    scanf("%*[\n] ");
#endif
    /* Read put */
#ifdef _WIN32
    scanf_s("%8s%*[\n] ", put, _countof(put));
#else
    scanf("%8s%*[\n] ", put);
#endif
    /*
     * nag_enum_name_to_value (x04nac).
     * Converts NAG enum member name to value
     */
    putnum = (Nag_CallPut) nag_enum_name_to_value(put);
    /* Read sigma, r */
#ifdef _WIN32
    scanf_s("%lf%lf%lf%lf%*[\n] ", &s, &sigma, &r, &b);
#else
    scanf("%lf%lf%lf%lf%*[\n] ", &s, &sigma, &r, &b);
#endif
    /* Read m, n */
#ifdef _WIN32
    scanf_s("%"NAG_IFMT%"NAG_IFMT"%*[\n] ", &m, &n);
#else
    scanf("%"NAG_IFMT%"NAG_IFMT"%*[\n] ", &m, &n);
#endif
    #ifdef NAG_COLUMN_MAJOR
    #define P(I, J) p[(J-1)*m + I-1]
    order = Nag_ColMajor;
    #else
    #define P(I, J) p[(I-1)*n + J-1]
    order = Nag_RowMajor;
    #endif
    if (!(p = NAG_ALLOC(m*n, double)) ||
        !(t = NAG_ALLOC(n, double)) ||
        !(x = NAG_ALLOC(m, double)))
    {
        printf("Allocation failure\n");
        exit_status = -1;
        goto END;
    }
    /* Read array of strike/exercise prices, X */
    for (i = 0; i < m; i++)
#ifdef _WIN32
        scanf_s("%lf ", &x[i]);
#else
        scanf("%lf ", &x[i]);
#endif
#ifdef _WIN32
    scanf_s("%*[\n] ");
#else
    scanf("%*[\n] ");
#endif
    for (i = 0; i < n; i++)
#ifdef _WIN32
        scanf_s("%lf ", &t[i]);
#else
        scanf("%lf ", &t[i]);
#endif
#ifdef _WIN32
    scanf_s("%*[\n] ");
#else
    scanf("%*[\n] ");
#endif
    /*
     * nag_asian_geom_price (s30sac)
     * Asian option: geometric continuous average rate pricing formula
     */
    nag_asian_geom_price(order, putnum, m, n, x, s, t, sigma, r, b, p,
        &fail);

```

```

if (fail.code != NE_NOERROR)
{
    printf("Error from nag_asian_geom_price (s30sac).\n%s\n",
        fail.message);
    exit_status = 1;
    goto END;
}
if (putnum == Nag_Call)
    printf("%s\n\n", "Asian Call :");
else if (putnum == Nag_Put)
    printf("%s\n\n", "Asian Put :");
printf("%s%8.4f\n", " Spot          = ", s);
printf("%s%8.4f\n", " Volatility    = ", sigma);
printf("%s%8.4f\n", " Rate          = ", r);
printf("%s%8.4f\n", " Cost of carry = ", b);
printf("\n");
printf("%s\n", " Strike      Expiry      Option Price");
for (i = 1; i <= m; i++)
    for (j = 1; j <= n; j++)
        printf("%9.4f %9.4f %11.4f\n", x[i-1], t[j-1], P(i, j));

END:
NAG_FREE(p);
NAG_FREE(t);
NAG_FREE(x);

return exit_status;
}

```

10.2 Program Data

```

nag_asian_geom_price (s30sac) Example Program Data
Nag_Put           : Nag_Call or Nag_Put
80.0 0.2 0.05 0.08 : s, sigma, r, b
1 1              : m, n
85.0             : X(I), I = 1,2,...m
0.25            : T(I), I = 1,2,...n

```

10.3 Program Results

```

nag_asian_geom_price (s30sac) Example Program Results
Asian Option: Geometric Continuous Average-Rate

```

Asian Put :

```

Spot          = 80.0000
Volatility    =  0.2000
Rate          =  0.0500
Cost of carry =  0.0800

```

```

Strike      Expiry      Option Price
85.0000    0.2500      4.6922

```
