

Options on  
the  
Dow Jones  
Industrial  
Average<sup>SM</sup>

**DJX and DIA**



**Act on the  
Market You  
Know Best.**

**A glossary of options definitions appears on page 21.**

**The Chicago Board Options Exchange (CBOE) was founded in 1973, creating the world's first standardized, listed equity options. Today, CBOE continues to be a dominant force in the financial industry. This success has been accomplished by CBOE's leadership and innovation, and its commitment to individual and institutional investors worldwide.**

Do you ever have  
**strong opinions**  
on the market's direction?

Are you looking to  
**participate in the market**  
without holding a large stock portfolio?

Are you looking for  
**new investment tools**  
that allow you to trade  
the market like a stock?

Are you interested in  
**short-term protection**  
of your portfolio in a sometimes  
volatile stock market?

**CBOE offers you  
Options on the Dow Jones  
Industrial Average<sup>SM</sup>**

**DJX**  
Cash-settled options on the DJIA<sup>SM</sup>.

**DIA**  
Share-settled options on DIAMONDS<sup>®</sup>  
Exchange-traded Fund.

# Options on the Dow Jones



# Industrial Average

**Now, you have options**

**to trade on one of the most recognized and followed market indicators in the world — the Dow Jones Industrial Average (DJIA).**

With cash-settled options on the DJIA (trading symbol DJX) and options on DIAMONDS (trading symbol DIA), you have tools for participating in the performance of 30 blue-chip stocks. Armed with widely available research and investment advice, you can act on your market opinion with just one trade.

## **With DJX & DIA options:**

- **Risks of purchases are known.**
- **Trading is easy.**
- **Capital outlays can be limited.**

### **Products with unlimited possibilities.**

With DJX and DIA options, you can choose a strategy to participate in a bull, bear or neutral market. Purchasing calls may enable you to commit less capital than you would need to buy the stocks outright — with the added advantage of knowing your risks ahead of time. Purchasing puts gives you the opportunity to participate even in bearish markets. With options based on The Dow<sup>SM</sup> and DIAMONDS, the possibilities are endless.

### **It's simple.**

Whether you choose to trade DJX or DIA options, it's simple. DJX options are cash-settled options on the DJIA stock index. DIA options are options on DIAMONDS, an exchange-traded fund (ETF) of DJIA stocks. With DJX and DIA options, you can trade on the overall direction of the DJIA market, whether it rises, or falls, or stays flat.

*For the sake of simplicity, taxes and commissions have been omitted from the discussions and strategies that follow. The tax-treatment you receive may depend on your choice of DJX or DIA options. DJX options are considered section 1256 contracts and, therefore, may receive 60/40 long-term/short-term tax treatment. The tax treatment of DIA options is less certain. Please see *Taxes and Investing: A Guide for the Individual Investor*, at [www.cboe.com/LearnCenter/RCCGeneral.aspx](http://www.cboe.com/LearnCenter/RCCGeneral.aspx).*



A DJX or DIA call option gives the buyer the ability to profit if the index rises *above* a predetermined level — the break-even point (call strike price *plus* premium paid) — during the life of the option. When you purchase a call option, your profit potential is unlimited in a rising market. Should the market fall, your loss is limited to the amount paid for the call option.

A DJX or DIA put option, on the other hand, provides its owner the potential to profit if the DJIA falls *below* the break-even point (put strike price *less* premium paid) during the life of the option. The holder of a put option has substantial profit potential in a down market — the more the index falls below the option's strike price, the higher your profit potential. Again, if the market does not react the way you have anticipated, your loss is limited to the amount paid for the option.

As an investor, you have a choice of options with short-term and long-term expirations, as well as many strike prices. No matter what your market outlook, there is an options strategy for you.

DJX options are **cash-settled**; meaning no actual stocks are ever bought or sold on behalf of the option buyer. They have a **European-style exercise** — they can be exercised for cash only at expiration. That is, while DJX options positions can be opened or closed before expiration, they can only receive a cash-settlement at expiration.

DIA options are **physically settled**; meaning that DIAMONDS shares are bought or sold when the option is exercised. They have **American-style exercise** and therefore may be exercised for DIAMONDS on any business day prior to expiration.

### **Your risk is limited.**

The buyer of a call or put option pays the seller of the option a price known as the *premium*. The options premium for DJX and DIA options is stated in decimals. The prices are multiplied by \$100 to determine total cost. For example, if the option price is quoted at 4.5, the premium paid is \$450. The risk for the buyer of an option is limited to the amount of the premium. So the risk to a buyer is both known and limited.

DJX and DIA options are regulated securities, in the same class of investments as stocks or bonds. Like trading in stocks, options trading generally takes place only on registered securities exchanges and is regulated by the Securities and Exchange Commission. DJX and DIA options trade at the Chicago Board Options Exchange (CBOE).

**The 30 stocks in the Dow Jones  
Industrial Average<sup>SM</sup> are\*:**

**3M Co.**  
**Alcoa Inc.**  
**Altria Group Inc.**  
**American Express Co.**  
**American International Group Inc.**  
**Boeing Co.**  
**Caterpillar Inc.**  
**Citigroup Inc.**  
**Coca-Cola Co.**  
**E.I. DuPont de Nemours & Co.**  
**Exxon Mobil Corp.**  
**General Electric Co.**  
**General Motors Corp.**  
**Hewlett-Packard Co.**  
**Home Depot Inc.**  
**Honeywell International Inc.**  
**Intel Corp.**  
**International Business Machines Corp.**  
**Johnson & Johnson**  
**JPMorgan Chase & Co.**  
**McDonald's Corp.**  
**Merck & Co. Inc.**  
**Microsoft Corp.**  
**Pfizer Inc.**  
**Procter & Gamble Co.**  
**SBC Communications Inc.**  
**United Technologies Corp.**  
**Verizon Communications Inc.**  
**Wal-Mart Stores Inc.**  
**Walt Disney Co.**

*\*As of October 31, 2004.*

If you see the  
market rising,  
you can explore  
DJX or DIA  
call options.

**Challenge:**

**You believe that the stock market will rise in the near-term and would like to participate, but you wish to limit the capital outlay required to buy the stocks outright.**

**Solution: Buy a call option.**

Purchasing a call option is the simplest of bullish options strategies. There is unlimited profit potential with this tactic. Profit increases as the DJX or DIA rises above the break-even point — the point at which the DJX or DIA equals the call strike price *plus* the premium paid. Investors are aware of the risks in advance; losses are solely limited to the premium paid, no matter how far the DJX or DIA moves below the break-even point.

## Buying DJX Calls

*This strategy is based on a hypothetical situation and should only be considered as an example of a potential trading approach. Taxes, commissions and margin requirements are not included but must be taken into account when calculating the actual net returns for any option transaction.*

Suppose the DJIA is at 9,300. DJX is based on 1/100th of the DJIA, so the options index value would be at 93. As shown in the table, you could purchase five 6-month call options with a strike price of 93. Each premium point is multiplied by \$100 to determine total cost. Therefore, if you paid a premium of 5.00, you have paid \$2,500 for five contracts ( $5.00 \times 5 \times \$100 = \$2,500$ ). To make a profit, the DJX must rise above a break-even point of 98 ( $93 + 5.00 = 98$ ).

If the Dow reaches 9,950 at expiration (DJX = 99.50), the five 93 calls would be worth \$3,250 [ $(99.50 - 93) \times 5 \times \$100 = \$3,250$ ]. You would then reduce this amount by the premium paid (\$2,500) to arrive at a profit of \$750.

If the Dow fell to a level of 9,150 (DJX = 91.50), your calls would have no value and your loss would be limited to the total premium paid of \$2,500.

**Possible outcomes of purchasing five DJX 93 calls at a premium of 5.00:**

<b>LEVEL OF DJX AT EXPIRATION:</b>	<b>100.05</b>	<b>102.85</b>	<b>107.50</b>
<b>Move in the DJIA</b>	<b>+ 7%</b>	<b>+ 10%</b>	<b>+ 15%</b>
<b>Expiration value of five 93 strike calls</b>	<b>\$3,525</b>	<b>\$4,925</b>	<b>\$7,250</b>
<b>Less: premium paid (five calls @ 5.5)</b>	<b>-\$2,500</b>	<b>-\$2,500</b>	<b>-\$2,500</b>
<b>Net gain/loss*</b>	<b>\$1,025</b>	<b>\$2,425</b>	<b>\$4,750</b>
<hr/>			
<b>LEVEL OF DJX AT EXPIRATION:</b>	<b>86.95</b>	<b>84.15</b>	<b>79.50</b>
<b>Move in the DJIA</b>	<b>- 7%</b>	<b>- 10%</b>	<b>- 15%</b>
<b>Expiration value of five 93 strike calls</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Less: premium paid (five calls @ 5.5)</b>	<b>-\$2,500</b>	<b>-\$2,500</b>	<b>-\$2,500</b>
<b>Net gain/loss*</b>	<b>-\$2,500</b>	<b>-\$2,500</b>	<b>-\$2,500</b>

\*Exclusive of commissions, taxes, and other transaction costs.

### **Choices:**

If a call is not sold prior to expiration, and the DJX is above the strike price, you will receive a cash payment at expiration equal to the difference between the DJX and the strike price, multiplied by \$100.

However, suppose the market begins to turn away from your position, another method you might use to limit loss (premium paid) is to close your position. In this case, you opened your position by purchasing the 93 calls. By selling the 93 calls, you are making a closing sale, thereby creating a zero net position. Remember that you've already paid \$2,500 for the five call option contracts. If you could sell the calls at the current bid, for example, 3.50, and receive \$1,750 ( $3.50 \times 5 \times \$100 = \$1,750$ ), you could limit your net loss to \$750 ( $\$2,500 - \$1,750$ ). Therefore, using this technique could enable you to recover a portion of the call premium you have already paid and limit your net loss on the position. Don't forget that if you wish to trade out of your DJX options position, you must complete your transaction no later than the Thursday prior to the expiration date.

If you expect a  
market down-  
turn, there is a  
DJX or DIA put  
option strategy  
for you.

**Challenge:**

**You believe that the stock market will remain volatile as the global economic situation remains uncertain. You would like to protect some of the gains you made in your portfolio.**

**Solution: Buy a put option.**

Purchasing a put is the most fundamental options strategy for investors who expect a market decline. There is significant profit potential with this approach. Profit increases as the index falls below the break-even point — the point at which the DJIA equals the put strike price *less* the premium paid. The risks in buying are known in advance. Losses are limited to the premium paid, regardless of how far the index moves above the break-even point.

## Buying DIA Puts

*This strategy is based on a hypothetical situation and should be considered only as an example of a potential trading approach. Taxes, commissions and margin requirements are not included but must be taken into account when calculating the actual net returns for any option transaction.*

Suppose the DJIA is at 9,600, DIA is based on 1/100th of the DJIA, so the at-the-money options value would be at 96.00. As shown in the following table, you could purchase five 6-month put options with a strike price of 96.00. Each premium point is multiplied by \$100 to determine total cost. Therefore, if you paid a price of 4.50, you have paid \$2,250 for five contracts ( $4.50 \times 5 \times \$100 = \$2,250$ ). To make a profit, the DJIA must fall below a break-even point of 91.50 ( $96.00 - 4.50 = 91.50$ ).

If the DJIA falls to 8,640 at expiration (DIA = 86.40), the five 96.00 puts would be worth \$4,800 [ $(96 - 86.40) \times 5 \times \$100 = \$4,800$ ]. You would then reduce this amount by the premium paid (\$2,250) to arrive at a profit of \$2,550.

If the DJIA rose to a level of 10,560 at expiration (DIA = 115.60), your puts would have no value and your loss would be limited to the total premium paid of \$2,250.

**Possible outcomes of purchasing five  
DIA 96 puts at a premium of 4.5:**

<b>LEVEL OF DIA AT EXPIRATION:</b>	<b>89.30</b>	<b>86.40</b>	<b>81.60</b>
<b>Move in the DJIA</b>	<b>- 7%</b>	<b>- 10%</b>	<b>- 15%</b>
<b>Expiration value of five 96 strike puts</b>	<b>\$3,350</b>	<b>\$4,800</b>	<b>\$7,200</b>
<b>Less: premium paid (five calls @ 4.5)</b>	<b>-\$2,250</b>	<b>-\$2,250</b>	<b>-\$2,250</b>
<b>Net gain/loss*</b>	<b>\$1,100</b>	<b>\$2,550</b>	<b>\$4,950</b>
<b>LEVEL OF DIA AT EXPIRATION:</b>	<b>102.70</b>	<b>105.60</b>	<b>110.40</b>
<b>Move in the DJIA</b>	<b>+ 7%</b>	<b>+ 10%</b>	<b>+ 15%</b>
<b>Expiration value of five 96 strike calls</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Less: premium paid (five calls @ 4.5)</b>	<b>-\$2,250</b>	<b>-\$2,250</b>	<b>-\$2,250</b>
<b>Net gain/loss*</b>	<b>-\$2,250</b>	<b>-\$2,250</b>	<b>-\$2,250</b>

\*Exclusive of commissions, taxes, and other transaction costs.

**Choices:**

Since DIA has physical settlement, if the puts are not sold prior to expiration and the DIA is below the strike price, you may deliver DIAMONDS shares at the DIA strike price, multiplied by \$100.

If the market turns against you, another method you might use to limit your loss (premium paid) would be to sell your put options (close the position), leaving your net position flat. Rather than allowing your options to expire worthless, if you sell them at the current bid, for example, 3.10, you would receive \$1,550 ( $3.10 \times 5 \times \$100$ ). Since you originally paid \$2,250 when you purchased them (opened your position), selling them would limit your net loss on the position to \$700 ( $\$2,250 - \$1,550$ ).

## **LEAPS® : The long-term option.**

Long-term Equity Anticipation Securities™ (LEAPS) based on the Dow Jones Industrial Average offer investors a way to take a long-term position in the stock market with quantified risk at a fraction of the cost of purchasing shares of stock. Investors can capitalize on their long-term forecasts for the market, up to three years in the future, with one transaction.

The investment time frame of DJX and DIA LEAPS may be much longer than that of standard DJX or DIA options. While standard options provide opportunity to capture market gains due to shorter-term fluctuations in the market, LEAPS based on the DJIA allow investors to buy and hold a market position for up to three years. Investors need not predict precise timing of the market movements to profit — they need to correctly predict market trends over time. Like all options transactions, the buyer's risk is limited to the amount of the premium paid.

LEAPS offer the possibility to generate a greater percentage return and tie up less capital compared to a similar position in the stock market. Because few investors can purchase every stock they follow, LEAPS allow them to diversify with fewer dollars at risk.

# Product Specifications

## Options on The Dow<sup>SM</sup>

**Symbol:** DJX.

**Index Description:** The Dow Jones Industrial Average is a price-weighted index composed of 30 of the largest, most liquid NYSE and Nasdaq listed stocks.

**Underlying Level:** Options are based on 1/100th of the DJIA<sup>SM</sup> level.

**Multiplier:** \$100.

**Premium Quote:** Stated in decimals. One full point equals \$100. Minimum tick for options trading below 3.00 is 0.05 (\$5.00) and for all other series, 0.10 (\$10.00).

**Strike Prices:** Strike prices for options are set to bracket the index level in minimum increments of 1 point.

**Expiration Cycle:** Generally, up to three near-term months plus up to three months on the March quarterly cycle.

**Expiration Date:** Saturday following the third Friday of the expiration month.

**Last Trading Day:** Trading in DJX will ordinarily cease on the business day (usually a Thursday) preceding the day on which the exercise-settlement value is calculated.

**Exercise Style:** European.

**Settlement Value:** Calculated based on the opening prices of the component securities on the business day prior to expiration, usually a Friday. The exercise-settlement amount is equal to the difference between exercise-settlement value and the exercise price of the option, multiplied by \$100.

**Settlement Value Symbol:** DJS.

**Settlement:** Cash-settled.

**Position and Exercise Limits:** No position and exercise limits are in effect. Each member (other than a market-maker) or member organization that maintains an end of day position in excess of 1 million contracts in DJX (DJX and DJX LEAPS) for its proprietary account or for the account of a customer, shall report certain information to the Department of Market Regulation. The member must report information as to whether such position is hedged and, if so, a description of the hedge employed. A report must be filed when an account initially meets the aforementioned applicable threshold. Thereafter, a report must be filed for each incremental increase of 25,000 contracts. Reductions in an options position do not need to be reported. However, any significant change to the hedge must be reported.

**Margin:** Purchases of puts or calls with 9 months or less until expiration must be paid for in full. Writers of uncovered puts or calls must deposit / maintain 100% of the option proceeds plus 15% of the aggregate contract value (current index level x \$100) minus the amount by which the option is out-of-the-money, if any, subject to a minimum for calls of option proceeds plus 10% of the aggregate contract value and a minimum for puts of option proceeds plus 10% of the aggregate exercise price amount. (For calculating maintenance margin, use option current market value instead of option proceeds.) Additional margin may be required pursuant to Exchange Rule 12.10.

**CUSIP Number:** 12486C

**Trading Hours:** 8:30 a.m. to 3:15 p.m. Chicago time.

## Options on DIAMONDS

**Underlying:** Generally, 100 shares of DIAMONDS<sup>®</sup>, an exchange-traded fund designed to track the performance of the Dow Jones Industrial Average.

**Underlying Symbol:** DIA

**Strike Price Intervals:** Strike prices are set at a minimum of 1-point increments.

**Strike (Exercise) Prices:** In-, at- and out-of-the-money strike prices are initially listed. New series generally will be added when DIA shares trade through the highest or lowest strike price available.

**Premium Quotation:** Stated in decimals. One full point equals \$100. Minimum tick for options trading below 3.00 is 0.05 (\$5.00) and for all other series, 0.10 (\$10.00).

**Expiration Date:** Saturday immediately following the third Friday of the expiration month.

**Expiration Months:** Three near-term months and two months from the March quarterly cycle (March, June, September and December). LEAPS may also be available.

**Last Trading Day:** Trading in DIA options will ordinarily cease at the close on the business day (usually a Friday) preceding the expiration date.

**Exercise Style:** American – DIA options generally may be exercised on any business day before the expiration date.

**Settlement of Option Exercise:** Physical Delivery. Exercise notices properly tendered on any business day will result in delivery of DIA shares on the third business day following exercise.

**Position and Exercise Limits:** 75,000 contracts on the same side of the market.

**Margin:** Uncovered writers must deposit 100% of the options proceeds plus 15% of the aggregate contract value (current DIA price multiplied by \$100) minus the amount by which the option is out-of-the-money, if any. Minimum margin is 100% of the option proceeds plus 10% of the aggregate contract value. Long puts or calls must be paid in full.

**CUSIP Number:** 252787106

**Trading Hours:** 8:30 a.m. - 3:15 p.m. Central Time (Chicago time).

# Glossary of Options Terminology

**American-Style option:** An option contract that may be exercised at any time between the date of purchase and the expiration date. **DIA** and most equity options are American-style.

**At-the-money:** An option is at-the-money if the strike price of the option is equal to the market price of the underlying security.

**Call:** A call option gives its owner the right to receive the underlying equity or exchange-traded fund at expiration, and obligates the seller to deliver the underlying.

An *index* call option gives its owner the right to receive the amount by which the settlement value of the index exceeds the strike of the call at expiration, and obligates the seller to pay such difference.

**Divisor:** A mathematical quantity used to compute an index. It may be adjusted for changes in the component stocks or for corporate activities such stock splits.

**Equity options:** Options on shares of an individual common stock. **DIA** options trade like equity options.

**European-style options:** An option contract that may be exercised only during a specified period of time just prior to its expiration. **DJX** options are European-style options.

**Exercise price:** The price at which the holder of an option can purchase (call) or sell (put) the underlying stock from or to the option writer. For listed options, the exercise price is the same as the strike price.

**Expiration cycle:** An expiration cycle relates to the dates on which options expire.

**Expiration date:** Date on which an option and the right to exercise it, cease to exist.

**Holder:** The purchaser of an option.

**In-the-money:** A call option is in-the-money if the strike price is less than the market price of the underlying security. A put option is in-the-money if the strike price is greater than the market price of the underlying security.

**Intrinsic value:** The amount by which an option is in-the-money (see above definition).

**LEAPS:** LEAPS are long-term stock or index options. LEAPS, like all options, are available in two types, calls and puts, with expiration dates up to three years in the future.

**Long position:** A position wherein an investor's interest in a particular series of options is as a net holder (i.e., the number of contracts bought exceeds the number of contracts sold).

**Margin:** The minimum equity required to support an investment position. To buy on margin refers to borrowing part of the purchase price of a security from a brokerage firm. The Federal Reserve Board sets the margin requirement—the maximum percentage of the investment that can be loaned by the firm.

**Open interest:** The number of outstanding option contracts in the exchange market or in a particular class or series.

**Out-of-the-money:** A call option is out-of-the-money if the strike price is greater than the market price of the underlying security. A put option is out-of-the-money if the strike price is less than the market price of the underlying security.

**Premium:** The price of an option contract, determined in the competitive marketplace, which the buyer of the option pays to the option writer for the rights conveyed by the option contract.

**Put:** An option contract that gives the holder the right to sell the underlying security at a specified price for a certain fixed period of time.

**Series:** All option contracts of the same class that also have the same unit of trade, expiration date and strike price.

**Short position:** A position wherein a person's interest in a particular series of options is as a net writer (i.e., the number of contracts sold exceeds the number of contracts bought).

**Time value:** The portion of the option premium that is attributable to the amount of time remaining until the expiration of the option contract. Time value is whatever value the option has in addition to its intrinsic value.

**Underlying security:** The instrument, such as a stock, exchange-traded fund or an index value, subject to being purchased or sold upon exercise of the option contract. In the case of options on the Dow Jones Industrial Average, the underlying index level, DJX or DIA, is equal to 1/100th of the DJIA.



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[www.cboe.com](http://www.cboe.com)

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