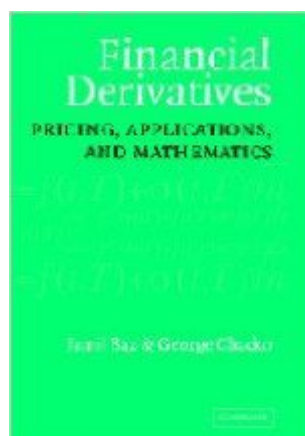


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# Financial Derivatives: Pricing, Applications, And Mathematics



## Synopsis

Combining their corporate and academic experiences, Jamil Baz and George Chacko offer financial analysts a complete, succinct account of the principles of financial derivatives pricing. Readers with a basic knowledge of finance, calculus, probability and statistics will learn about the most powerful tools in applied finance: equity derivatives, interest rate markets, and the mathematics of pricing. Baz and Chacko apply concepts such as volatility and time, and generic pricing to the valuation of conventional and more specialized cases. Other topics include:

- \*Interest rate markets, government and corporate bonds, swaps, caps, and swaptions
- \*Factor models and term structure consistent models
- \*Mathematical allocation decisions such as mean-reverting processes and jump processes
- \*Stochastic calculus and related tools such as Kilmogorov equations, martingales techniques, stochastic control and partial differential equations

Meant for financial analysts and graduate students in finance and economics, *Financial Derivatives* begins with basic economic principles of risk and builds up various pricing and hedging techniques from those principles. Baz and Chacko simplify the mathematical presentation, and balance theory and real analysis, making it a more accessible and practical manual. Jamil Baz holds an M.S. in Management from MIT and a Ph.D. in Business Economics from Harvard University. He is a Managing Director at Deutsche Bank in London. George Chacko has a B.S. from MIT in electrical engineering and a Ph.D. in Business Economics from Harvard University. He is an Associate Professor of Business Administration at Harvard Business School. Both authors have worked extensively for financial services firms in the private sector. They have published in leading academic journals including the *Review of Financial Studies* and the *Journal of Financial Economics* as well as practitioner journals such as the *Journal of Fixed Income* and the *Journal of Applied Corporate Finance*.

## Book Information

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## Customer Reviews

One of the author, Baz, gave me a copy of this book when it came out and it went to sleep in my library as I was not in a finance mood. I forgot about it until this week as I was stuck on a problem related to risk-neutral pricing and the Girsanov theorem concerning changes in probability measure. I looked at every passage on the the subject until I hit on it. Then I realized that I should have read it before: it is a condensed, but extremely deep , and complete exposition of the subject of theoretical finance.No financial book has the clarity of this text.Other quant books do not have such notions as "pricing kernel" and economic theoretical matters. I would recommend it as a necessary piece of the "quant" toolkit. Every quant should have it as a background tool as the usual quant literature is standalone and devoid of these concepts.

This book draws on the PhD course that Prof. Chacko teaches at Harvard Business School and the substantial real-world experience with derivatives of both authors to offer a solid package that is useful for both theory and practice. There are other books with clear and rigorous mathematics (e.g. Wilmott), variety of methodologies for pricing (e.g. Neftci) and guides to practical hedging (e.g. Taleb), but this one presents all three components and is therefore a must-have for any serious derivatives shop. Highly recommended.

Financial derivatives are the products traded by the financial industry, banks and trading companies; a contract whose payoff depends on the behavior of a benchmark; financial instruments whose value is derived from a number of underlying variables. Examples: futures, options, and swaps ; or other tradable assets, e.g., stocks or commodities; or such non-tradable items such as the temperature (weather derivatives), the unemployment rate, or any kind of (economic) index. Since the industry has undergone a recent explosive growth, so have the number of variety of books covering the subject.The book by Baz & Chacko is useful for readers wanting a mathematical introduction.Covered are mathematical tools, financial valuation, financial models, asset pricing, Black-Scholes.On the math side: Ito's lemma, and a systematic presentation of stochastic differential equations; and dynamical programming.There are other similar books are out there, roughly the same level, and roughly the same emphasis; for example by Willmott-Howison-Dewynne, and by Capinski-Zastawniak.I believe they all serve a very useful

purpose. Review by Palle Jorgensen, July 2011.

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