Abstract: A convertible bond is a security that the holder can convert into a specified number of underlying shares. In addition, very often the issuer can recall the bond, paying some compensation, or force the holder to convert it immediately. Therefore, the pricing problem has also a game-theoretic aspect. When modelling convertible (callable) bonds within the framework of a firm value model, they can be considered as an example of a standard game contingent claim as long as no dividends are distributed to the equity holders. This article reviews the classical as well as some recent literature in this field. Furthermore, we introduce a mathematically rigorous concept of no-arbitrage price processes for this kind of derivatives, which explicitly incorporates the feature that the contract can be terminated by both counterparties prematurely. We compare this dynamic conception to price derivatives with the static one by Karatzas and Kou [18].
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