

In my mentoring experience, intrinsic value and extrinsic value are two of the most consistently misunderstood terms in options trading. Every option premium you see is made up of exactly two components. Getting these straight changes how you think about every trade you place.

### Intrinsic Value

Intrinsic value is the difference between the underlying's current price and the strike price of the option. For a call, it is the underlying price minus the strike price. For a put, it is the strike price minus the underlying price.

$$\text{Intrinsic Value (Call)} = \text{Underlying Price} - \text{Strike Price}$$

$$\text{Intrinsic Value (Put)} = \text{Strike Price} - \text{Underlying Price}$$

By definition, only in-the-money options carry intrinsic value. A call is in the money when the strike price is below the current underlying price. A put is in the money when the strike price is above the current underlying price. Any option that is at the money or out of the money has zero intrinsic value.

$$\text{In-the-Money (Call)} = \text{Strike Price} < \text{Underlying Price}$$

$$\text{In-the-Money (Put)} = \text{Strike Price} > \text{Underlying Price}$$

### Time Value (Extrinsic Value)

Any premium above the option's intrinsic value is time value. The more time remaining before expiration, the greater the time value, because more time gives the underlying a greater opportunity to make a favorable move. Investors pay a higher premium for more time when comparing options at the same strike. Time value erodes continuously and reaches zero at expiration. This is theta decay, and for premium sellers it is the edge working in your favor every single day.

$$\text{Time Value} = \text{Premium} - \text{Intrinsic Value}$$

$$\text{Option Premium} = \text{Intrinsic Value} + \text{Time Value}$$

CALL OPTION EXAMPLE	
Stock Price	<b>\$57.00</b>
Strike Price	<b>\$50.00</b>
In the Money by	<b>\$7.00</b>
Intrinsic Value	<b>\$7.00</b>
Time Value	<b>\$2.00</b>
Option Premium	<b>\$9.00</b>

PUT OPTION EXAMPLE	
Strike Price	<b>\$57.00</b>
Stock Price	<b>\$50.00</b>
In the Money by	<b>\$7.00</b>
Intrinsic Value	<b>\$7.00</b>
Time Value	<b>\$2.00</b>
Option Premium	<b>\$9.00</b>

**For premium sellers:** When you sell an option, time value is what decays in your favor every day the position is open. That daily erosion is theta working for you. It is one of the structural advantages of being on the selling side.

**Good Luck and Great Trading,**

Past performance is not indicative of future results. Trading involves risk. This material is for educational purposes only and is not investment advice.

The table below shows how intrinsic and extrinsic value change as you move across strikes. ITM options carry intrinsic value. OTM options are made up entirely of extrinsic (time) value. As a premium seller, the extrinsic value column is what you are collecting — and what theta erodes in your favor every day.

Call — In the Money  
  Put — In the Money  
  Current Underlying Price  
  Out of the Money — extrinsic value only

CALLS				Strike	PUTS			
Delta	Option Price	Intrinsic Value	Extrinsic Value		Option Price	Intrinsic Value	Extrinsic Value	Delta
0.74	25.10	17.75	7.35	230	5.40	—	5.40	-0.25
0.69	21.30	12.75	8.55	235	6.67	—	6.67	-0.29
0.64	17.65	7.75	9.90	240	8.15	—	8.15	-0.35
0.59	14.40	2.75	11.65	245	9.77	—	9.77	-0.41
Current Underlying Price				\$247.75	Current Underlying Price			
0.52	11.40	—	11.40	250	11.77	2.25	9.52	-0.48
0.45	8.67	—	8.67	255	14.12	7.25	6.87	-0.56
0.38	6.57	—	6.57	260	16.90	12.25	4.65	-0.64
0.31	4.67	—	4.67	265	20.60	17.25	3.35	-0.71
0.25	3.30	—	3.30	270	24.37	22.25	2.12	-0.79

Option prices are mid-market. Intrinsic value (call) = Underlying - Strike | Intrinsic value (put) = Strike - Underlying. Extrinsic value = Option Price - Intrinsic Value. Update from Google Sheet as needed.