MONEYNESS: WHAT A PREMIUM IS MADE OF

Vajgrt Labs - Education - Lesson 37 of 72 - 6 min read - Updated Oct 21, 2026

TL;DR

- Moneyness is where the strike sits against SPY’s price. A call is in-the-money when its strike is below SPY, at-the-money at the strike nearest SPY, out-of-the-money above it. Puts read the same strikes in mirror: the 773 strike is in-the-money for the call and out-of-the-money for the put.

- Every premium splits in two: INTRINSIC value - what the contract would pay if exercised this second - and EXTRINSIC value - everything above that, the price of the remaining time and possibility. The 773 call at a mid of about 20.60 is 5.12 intrinsic + 15.48 extrinsic; the 780 call’s entire 16.06 is extrinsic.

- At expiration, extrinsic value is always zero - which is why a contract can finish in-the-money and still lose most of its premium: if SPY never moved, the 773 call would settle at exactly 5.12, and its buyer would have paid 15.48 for time that ran out.

THE TAKEAWAYS

- The labels, defined by the holder’s exercise position. For a CALL: strike below the price = in-the-money (exercising buys below market); strike above = out-of-the-money (exercising would overpay - nobody would); the strike nearest the price = at-the-money. For a PUT every label flips: strike above the price is in-the-money (exercising sells above market), strike below is out. ’The money’ always describes the contract’s relationship to the price, never the trader’s result - the 773 call is in-the-money at purchase and, at an unchanged expiry, its buyer still loses (Lessons 2’s table). Moneyness is geography, not profit.

- The split, computed on four real rows (the graphic draws them; premiums at the mid of each real quote, SPY 778.12): 773C - intrinsic 778.12 - 773 = 5.12, extrinsic 20.60 - 5.12 = 15.48. 775C - intrinsic 3.12, extrinsic 19.25 - 3.12 = 16.13. 780C - intrinsic 0 (the strike sits above SPY), extrinsic all 16.06. 785C - intrinsic 0, extrinsic all 13.14. Read the pattern, because it surprises everyone once: the extrinsic does not shrink as the strike rises away from the price in a straight line - it peaks at the strikes NEAREST the price (16.13 and 16.06 here) and thins as you walk away in either direction. Near the money is where the outcome is most undecided; undecided is what extrinsic prices.

- What extrinsic is, and its one absolute law. It is the market’s price for the contract’s remaining life: 52 days here, and the move SPY might make inside them. It is not a fee and not a markup - it is the part of the premium a buyer pays for possibility and a seller is paid for carrying the obligation through that possibility. The law: at expiration it is exactly zero, always, on every contract ever written. Which produces the stage’s most useful sentence: whatever you paid above intrinsic value is rent on time - and rent is never refunded. Stage 6 takes the extrinsic apart properly (theta collects it daily; IV inflates and deflates it); Stage 5 asks only that the split become reflexive before any premium is judged.

- The deep and the far ends of the ladder behave like different instruments, and the split tells you which you are holding. A deep in-the-money contract is mostly intrinsic - it moves nearly dollar-for-dollar with SPY (Stage 6’s delta says how nearly) and its rent is a small fraction of

its price. A far out-of-the-money contract is pure extrinsic - a priced hope with a deadline, no banked value at all, and a payoff that needs a journey, not a nudge. Beginners shop the ladder by the tag and gravitate to the pure-hope end because it looks cheap. The split is the antidote: 13.14 of pure time is not cheaper than 20.60 that is a quarter banked - it is a different bet wearing a smaller number.

RULE: Never compare two premiums until you've split them - intrinsic is banked value, extrinsic is rented time, and only one of them survives the deadline.

COMMON MISTAKES

- Calling an option 'cheap' because its premium is small. The 785C is the most expensive row on this page per unit of banked value - its intrinsic value is zero. Cheap is a statement about the split, not the tag.

- Thinking in-the-money means profitable. The 773C is in-the-money at purchase and at an unchanged expiry - and loses 15.48 of its 20.60. ITM describes the strike's geography, not the trade's result.

- Forgetting the put mirror: at the same strike, one type is in-the-money and the other is out. Read moneyness off the contract's type and the price - never off the strike alone.

- Paying for time your plan doesn't use - 52 days of extrinsic for a three-day idea (or the reverse: a deadline inside your idea's horizon). The split tells you how much of your money is time; check it is time the plan spends.

DO IT - SPLIT FOUR ROWS YOURSELF

On today's SPY chain (paper only), pick the expiry nearest 45 days out and write four call rows into your journal: the first strike below SPY, the nearest strike above it, and one strike further out on each side. For each: the strike, the mid premium, the intrinsic value, the extrinsic value. Circle the row carrying the most extrinsic - it is the row where the deadline does the most damage. This is the Stage 5 gate's second skill, rehearsed on a live shelf.

Education only - not financial advice. Contract, exercise and assignment mechanics: the OCC's (standardised terms; exercise-by-exception, Rule 805) - checked Oct 15, 2026. Call figures are arithmetic on the real SPY chain data of Oct 9, 2026 (773 call bid 20.53 / ask 20.68; SPY 778.12; Nov 30 expiry); the put lesson's premium is the lesson's labeled example number, the published chain set being the call side. SPY options are American-style and physically settled. Vajgrt Labs - Education.