

fd_gauss_vasicek1d_zbo

Input parameters:

- Space StepNumber N_r
- Time StepNumber M

Output parameters:

- Price

The stochastic differential equation representing the short rate is given by

$$dr_t = k(\theta - r_t)dt + \sigma dW(t)$$

The price of the zero-coupon bond with maturity $S > T$ is solution of the following PDE

$$u_t + \frac{1}{2}\sigma^2 u_{rr} + [k(\theta - r)]u_r - ru = 0, u(r, S, S) = 1$$

that we solve using explicit scheme of Hull-White[1]. The price of the option is obtained solving the same PDE with boundary condition at the maturity of the option T , the price of the Zero Coupon Bond. We apply Dirichlet boundary conditions at $r = r_{min}$ and $r = r_{max}$.

References

- [1] J.Hull and A.WHITE. Valuing derivative securities using the explicit finite difference method. *Journal of Financial and Quantitative Analysis*, 25:87–100, 1990. [1](#)