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A STUDY ON CAPITAL ASSET PRICING MODEL WITH REFERENCE TO BSE-500 INDEX

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ABSTRACT

The present study examines the Capital Asset Pricing Model (CAPM) for the Indian stock market using monthly stock returns from 250 companies of BSE 500 Index listed on the Bombay stock exchange for the period of January 2000 to December 2010. The findings of this study are not substantiating the theory's basic result that higher risk (beta) is associated with higher levels of return. The theory's prediction for the intercept is that it should equal zero and the slope should equal the excess returns on the market portfolio. The results of the study lead to negate the above hypotheses and offer evidence against the CAPM. The tests conducted to examine the nonlinearity of the relationship between return and betas bolster the hypothesis that the expected return beta relationship is linear. Additionally, this study investigates whether the CAPM adequately captures all-important determinants of returns, including the residual variance of stocks. The results exhibit that residual risk has an effect on the expected returns of portfolios.

KEYWORDS: CAPM, Portfolio Returns, Beta, Risk Free Rate, Systematic Risk