

ASSET PRICING IN THE INDIAN CAPITAL MARKET: A STUDY OF POSITIVE AND NEGATIVE RETURN PERIODS

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Abstract

Capital Asset Pricing Model (CAPM) predicts that expected returns on securities are a positive linear function of their market betas and market beta alone is adequate to describe the cross section of expected returns. However there is a controversy regarding the empirical validity of CAPM. The present research paper is an empirical assessment of this financial model in the Indian capital market. It shows that for the overall period of study, there do not exist any positive relationship between the stocks' beta and their expected returns. It also shows that the stocks' expected return is more closely related to their betas in the negative return periods than in the positive return periods. Lastly, it observes that the Indian capital market investors are not adequate diversifiers and expects risk premium for bearing un-systematic risk.

Keywords: Asset pricing, CAPM, Empirical testing, Indian capital market, Beta.
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