A REGRESSION CASE STUDY

THE CAPM MODEL

THE CAPM MODEL

HIGH RISK, HIGH RETURN

THIS IS A MAXIM THAT'S
HEARD QUITE OFTEN IN
THE BUSINESS WORLD

CAPM IS A FINANCIAL
MODEL THAT QUANTIFIES
THIS MAXIM

THE CAPM MODEL

THE CAPITAL ASSET PRICING MODEL IS USED FOR PRICING RISKY SECURITIES

$$R_i = R_f + \beta_i (R_m - R_f)$$

THE CAPITAL ASSET PRICING MODEL

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THE RETURN ON A SECURITY

THE CAPITAL ASSET PRICING MODEL

$$R_i = R_f + \beta_i (R_m - R_f)$$

THE RISK FREE RATE OF RETURN

+

A PREMIUM

THE CAPITAL ASSET PRICING MODEL

$$R_i = R_f + \beta_j (R_m - R_f)$$

THE RISK OF THE SECURITY AS COMPARED TO THE MARKET

A MEASURE OF RISK

THE CAPITAL ASSET PRICING MODEL

$$R_i = R_f + \beta_i (R_m - R_f)$$

EXPECTED RETURN
OF THE MARKET
OVER AND ABOVE
THE RISK FREE RATE

THE CAPITAL ASSET PRICING MODEL

$$R_i = R_f + \beta_j (R_m - R_f)$$

USING CAPM AND
LINEAR REGRESSION

WE CAN FIND THE
VALUE OF BETA

THE CAPITAL ASSET PRICING MODEL

$$R_i = R_f + \beta_i (R_m - R_f)$$

BETA OF A SECURITY IS AN IMPORTANT MEASURE

IT CAN TELL YOU HOW MUCH RISK THE SECURITY ADDS TO A PORTFOLIO