

## EXPECTED RETURNS = sum of (probabilities & possible returns)

<u>Prob.</u>	<u>Possible Return (over next year)</u>
0.5	50%
0.3	10%
0.2	-20%

Exp. Return =  $0.5 * 50\% + 0.3 * 10\% + 0.2 * -20\% = 24\%$

Standard deviation = 28%, link to Normal Distribution

# Risks

Introduction to Investments

Prof S G Badrinath

Measuring Expected Returns, Discussing Risk

- Business Risk
- Financial Risk
- Exchange rate/Country risks
- Systematic and unsystematic risks
  - Beta Risk



- ✓ Systematic risk – risk inherent to the entire market.
  - also known as “undiversifiable risk”, “volatility” or “market risk.”
- ✓ Unsystematic risk – risk specific to a particular stock or industry.

# Beta Risk

- ✓ Statistical measure of systematic risk of an enterprise.
  - ✓ Systematic risk is the only risk that matters – since unsystematic risk cancels out when you diversify your portfolio.
- ✓ Beta risk is not diversifiable.

**© All Rights Reserved.**

This document has been authored by Prof S G Badrinath and is permitted for use only within the course “Introduction to Investments” delivered in the online course format by IIM Bangalore. No part of this document, including any logo, data, illustrations, pictures, scripts, may be reproduced, or stored in a retrieval system or transmitted in any form or by any means – electronic, mechanical, photocopying, recording or otherwise – without the prior permission of the author.