ABSTRACT

The Capital Asset Pricing Model (CAPM) provides investors with a framework upon which they can analyze the relationship of risk and return. This study employs the CAPM framework to evaluate the relative riskiness and investment potential of property companies listed on the Stock Exchange of Singapore (SES).

The CAPM, an equilibrium pricing model, asserts that investors should only be rewarded for assuming systematic risk. Under this model, because unsystematic risk can be diversified away, there is a direct relationship between the required rate of return on a security and its systematic risk, measured by the beta value. Beta is the relevant measure of risk that cannot be diversified away in a portfolio of securities and, as such, it is the measure that investor should consider in their portfolio management decision process. Securities with high systematic risk will be compensated by high rate of return.

Three hypotheses are formulated to test the general applicability of the CAPM on the property sector. These hypotheses focus on the risk-return relationship, stability of beta coefficient and pricing of the property stocks. The results indicate that there is a linear and positive relationship between property stocks' return and systematic risk. The beta coefficients for most property companies are not stable over two non-overlapping periods, implying that the risk of a company in the past is not a good indicator of the future risk level. Also, there appear to be a consistent underpricing of the property stocks listed on the SES which could provide investors with favourable investment returns.

Keywords:

Beta Coefficients
Capital Asset Pricing Model
Investment Performance
Pricing
Return
Risk