

**BETA STABILITY AND PREDICTABILITY OF
MALAYSIAN STOCK**



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ABSTRACT

Investors in general will make investment decisions based on information available in the market. In regards to this, beta coefficients are used by some investors as a forecasting tool to evaluate the investment risk. However, whether or not beta values are a good estimator of risk for a particular stock depends on its stability and predictability over time. Previous studies however reveal inconclusive results in terms of stability and predictability of beta values. This study examines the stability and predictability of beta values of one hundred stocks listed in Bursa Malaysia from the year 1998 to 2007. Beta values are computed based on Single Index Model proposed by Sharpe (1964). Stability of beta is examined based on paired observation test and risk-class membership, while predictability of betas is investigated based on correlation analysis. The study reveals that beta values are not stable during the observation period for Malaysian stocks. However, it can be predicted with confidence from those in an earlier period. The results suggest that the investors need to be careful when examine the stability of beta values for the stocks as there may be changing economic conditions which can contribute to the changing of the company profile over time. Nevertheless, investors and fund managers may still use beta as one of their risk forecasting tools as beta can be predicted with certain degree of accuracy from those in an earlier period. The results of this study will facilitate investors and fund managers in investment decision making process.

CHAPTER 1

INTRODUCTION

1.0 INTRODUCTION

In making investment decision in the stock market, investors need to consider many factors that would have impact on their investment. Whether or not they would make wise investment decisions depends on the amount of information they have on the security they wish to invest. One of the aspects that raise attention of the investors is risk and return trade-off on the investment. Risk and return trade-off are essential for investors in making investment decisions and constructing a portfolio which stipulated that in order to get higher return, investors must be willing to bear more risk. However, owing to the information asymmetry problem, not all the investors have access to the information they need for their investment making processes. Therefore, to assess the risk of an investment, investors in general can use beta value as a simple measure to assess the risk and return level in their investment. Beta value is often used as an indicator for required returns on investment for the investors.

Beta is a measure of stock price volatility which is used to evaluate the sensitivity of each stock's price to changes in the market (Levy, 1974). Beta of a stock is the measure of systematic risk which relates the returns of the stocks against the returns of the market. Generally, a stock with beta coefficient of more than one is regarded as volatile stock. Thus, it is considered to be more risky and therefore able to provide higher