



**TESTING THE RELIABILITY CAPITAL ASSET PRICING MODEL
(CAPM):
EMPIRICAL STUDY ON THREE SECTORS IN BURSA MALAYSIA
SECOND BOARD**

**DAHLIANA BINTI JAMIAN
2005374693**

**Submitted In Partial Fulfillment of The Requirement For The Bachelor
Of Business Administration
(Hons) Finance**

**BACHELOR OF BUSINESS ADMINISTRATION
(HONS) FINANCE
FACULTY OF BUSINESS MANAGEMENT
UNIVERSITI TEKNOLOGI MARA
JOHOR**

NOVEMBER 2007

ACKNOWLEDGEMENT

Alhamdulillah, praise to Allah S.W.T the Al Mighty and Merciful, because of the blessing that made possible for this project to be completed in time.

This thesis is prepared to fulfill the graduation requirement of Bachelor of Business and Administration (Hons) Finance. One semester of completing this thesis together with the classes to be attended as the requirement on the completion of BBA (Hons) Finance has given me opportunity to gain knowledge and being exposed to the current economic condition before continuing with the future endeavor challenges.

Foremost, I would like to take this opportunity to express my sincerely gratitude to all those efforts facilitated in the completion of this thesis. Without helped and support from various people, the completion of this study would not be made possible.

Firstly, I would like to express my deepest gratitude and thanks to my most respected thesis advisor, En Kamal Fahrulrazy b Rahim, from whom I sought and received valuable guidance, comments, views, advices as well as encouragement based upon his own extensive experience. I am also grateful for her tolerance towards my weaknesses and ignorance in completing this thesis. I wish to express my special word of thanks and indebted to En.Muhamad Sukor bin Jaafar, who also responsible for the preparation of the contents and the flow of the thesis.

Special thanks are due to all staff of Uitm Johore library and Bursa Malaysia library for their helped, guidelines and information regarding this study. Last but not least, special word of thanks and sincere gratitude to my beloved family, for the prayer and constant support for the beginning until the end of this study. Thanks a million.

DAHLIANA BTE JAMIAN

TABLE OF CONTENT

PAGE

Declaration of Original Works	iii
Letter of Submission	iv
Acknowledgement	v
Table of contents	vi
List of table	viii
Abstract	ix

CHAPTERS

CHAPTER 1: INTRODUCTION

1.0	Background of Study	1
1.1	History of Capital Asset Pricing Model	2
1.2	Problem Statement	4
1.3	Objectives of the Study	4
1.4	Significance of Study	5
1.5	Hypothesis	5
1.6	Limitation of the Study	7
1.7	Definition of terms/ concept	9

CHAPTER 2: LITERATURE REVIEW

2.0	Literature review	11
-----	-------------------	----

CHAPTER 3: METHODOLOGY

3.0	Methodology	
3.1	Capital Asset Pricing Model Methodology	16
3.2	Data Collection	20
3.3	Population and Sample	
	3.3.1 Population	21
	3.3.2 Sample	22

CHAPTER 4: DATA ANALYSIS AND FINDING

4.0	Data Analysis	
4.1	Results and Findings	23
4.2	Discussion on Results	28

ABSTRACT

This study examine the Capital Asset Pricing Model for the Malaysia stock market using monthly stock return from the three sectors in Bursa Malaysia second board for the period 1998 to 2005. The purpose of the study is to examine thoroughly if the CAPM holds true in the capital market of Malaysia and to test the reliability CAPM by checking on different sectors. In particular, a risk that can be diversified away when held along with other investments in a portfolio is, in a very real way, not a risk at all. The CAPM gives us insights about what kind of risk is related to return. Then CAPM can serve as a benchmark for understanding the capital market phenomena that cause asset prices and investor behavior to deviate from the prescriptions of the model. Then, I also will review the history of empirical work on the model and what it says about shortcomings of the CAPM that pose challenges to be explained by more complicated.

The Secondary data being used for this study are monthly stock price, 90-days T-Bills Rate and KLCI Index. This study concentrated on the 60 companies listed in Second Board of Bursa Malaysia and 10 companies were selected from each three different sector.

This study is conducted by using SPSS in order to find the beta value of the security through regression. Based on the analysis, the findings of this study are not supportive of the theory's basic statement that higher risk (beta) is associated with higher levels of return. However, the results obtained lend support to the linear structure of the CAPM equation being a good explanation of security returns.

CHAPTER ONE

INTRODUCTION

1.0 BACKGROUND OF THE STUDY

Since its introduction in early 1960s, CAPM has been one of the most challenging topics in financial economics. Almost any manager who wants to undertake a project must justify his decision partly based on CAPM. The reason is that the model provides the means for a firm to calculate the return that its investors demand. The model is the first model that successful attempt to show how to assess the risk of the cash flows of a potential investment project, to estimate the project cost of capital and the expected rate of return that investor will demand if they are to invest in the project.

The model was developed to explain the differences in the risk premium across assets. According to the theory these differences are due to differences in the riskiness of the returns on the assets. The model states that the correct measure of the riskiness of an asset is its beta and that the risk premium per unit of riskiness is the same across all assets. Given the risk free rate and the beta of an asset, the CAPM predicts the expected risk premium for an asset.

This study examines the Capital Asset Pricing Model for the Malaysia stock market using monthly stock return from the three sectors in the Second Board of