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## **INDIAN STOCK MARKET AND THE ASSET PRICING MODELS**

### **Abstract:**

Asset pricing models are attempts to define the relationship between returns and risks. In this study, we test and compare the performance of three asset pricing models – the Capital Asset Pricing Model, the three factor model of Fama and French (1993), and the five factor model of Fama and French (2015) – on Indian stock market (an emerging economy). The study is based on the constituent companies of CNX 500, and covers a period of fifteen years – from October 1999 to September 2014. The models are tested on portfolios formed on four firm characteristics – market capitalization, ratio of book-to-market equity, profitability, and investment. We find that the three factor model performs better than the Capital Asset Pricing Model in all the cases. For portfolios formed on investment, the five factor model performs better than the other models. However, except for cases in which portfolios are formed on investment, the four factor model (without an investment factor) is a more parsimonious model.

### **Keywords:**

Asset pricing model; market capitalization; book-to-market equity; profitability; investment; India

**JEL Classification:** G12, C52