Asset Pricing Model: A Quality Paradigm

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Abstract : Capital asset pricing model (CAPM) draws a direct relationship between the risk and the expected rate of return. There was a criticism on the beta and the assumptions of CAPM, as they are not applicable in the real world. Fama French Three Factor Model and Fama French Five Factor Model have given different factors, which have an impact on the return of any asset like size, value, investment and profitability. This study proposes to see Capital Asset pricing Model through the lenses of the quality aspect. In the study, the six factors are studied. The Fama French Five Factor Model and addition of the quality dimension are studied. Here, Graham's seven quality and quantity criteria are measured to determine the score of the sample firms. Thus, this study tries to check the model fit. The beta coefficient of the quality dimension and the R square value is seen to determine validity of the proposed model. The sample is drawn from the firms listed on Indian Stock Exchange (BSE). For the study, only nonfinancial firms are been selected. The time period of the study is from January 1999 to December 2019. Hence, the primary objective of the study is to check how robust the model becomes after giving the quality dimension to the capital asset pricing model in addition to the size, value, profitability and investment.

Keywords : asset pricing model, CAPM, Graham's score, G-score, multifactor model, quality
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