ABSTRACT

The Capital Asset Pricing Model (CAPM) and Arbitrage PortfolioTheories (APT) are the most commonly used techniques for calculating the required return of a risky asset in the global investing community.

This paper compares the two models APT and CAPM and helps in explaining the return on stocks in order to make better investment decisions. A simplistic approach has been adopted wherein Monthly data for a set of macroeconomic variables, market return as well as six indices were taken for the period ranging from 1999-2010.

It was observed that the Index returns are mainly explained by market returns, however not much could be explained by the macroeconomic variables.

According to the findings of the tests an inference was drawn that Arbitrage Price Theory could explain the index returns more efficiently as compared to the Capital Asset Pricing model.

Key Words: Capital asset pricing model, Arbitrage price Index , Market returns, Macroeconomic variable ,Risk free rate of Interest.