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**TESTING THE CAPITAL ASSET PRICING MODEL TOWARDS THE
INDONESIAN STOCK EXCHANGE: THE CASE OF LQ-45**

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Abstract

Objective The main purpose of this empirical research is to test whether the Capital Asset Pricing Model valid for predicting the returns of individual stocks in Indonesia, particularly from the LQ-45 category.

Method The samples collected are from the LQ-45 companies in Indonesia. The total final samples used are 37 samples. Risk-free Rate and Market Return are collected from the SBI (Sertifikat Bank Indonesia) and IHSG (Indeks Harga Saham Gabungan) respectively. Stock returns from the LQ-45 and market returns from the IHSG are calculated using the Holding Period Return, and were regressed to find the beta of each stocks. Hence, the CAPM will be calculated, and correlated with the actual stock returns. Methods used are the linear regression analysis and corelation analysis.

Result The result of this research indicates that there are a very weak correlation between the expected return using the CAPM model and the actual return of stocks. However, the beta as the systematic risk are significant enough to represent the proxy of risk and returns relationship.

Conclusion The conclusion of this research is that CAPM is still not valid to apply in the LQ-45, but a better result might be obtained in accordance with a good economic stability of the country and a better proxy for calculating the CAPM. Otherwise, Beta is still a good proxy to represent the relationship between risk and return.

Key words

Capital Asset Pricing Model (CAPM), Stock Return, Expected Return, Beta, Market Return, Market Premium, Risk-free Rate