प्रेस प्रकाशनी PRESS RELEASE

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RBI Working Paper Series:
Asset Pricing Model for Inefficient Markets:
Empirical Evidence from Indian Market

The Reserve Bank of India today placed on its website a Working Paper for the month of April 2012 titled "Asset Pricing Model for Inefficient Markets: empirical evidence from the Indian market**".** The Working Paper has been written by Dr. Debasish Majumder.

The paper provides a direction for incorporating market sentiments in the domain of standard models of asset pricing. The market sentiment is unobservable. However, it can be defined as the stationary departure of the market return from its fair value. This part of the market return is explained by the exuberance or pessimism by investors to certain information. Any autocorrelation that is observed in the market return might be the result of possible bullish/bearish responses by investors to market information.

Often, Indian equity market returns are serially correlated for at least one lag. Unfortunately, 'mispricing' might be a common outcome of application of any familiar asset pricing models for these markets because these models ignore the qualitative aspects of human decision making. To widen the applicability of these models ranging from an efficient to an inefficient market, the author proposed a transformation through which the original market would be transformed to a hypothetical market which is relatively efficient. The empirical study for Indian markets reveals that hypothetical market returns are, in general, not serially dependent and so meet the prerequisites of applying a standard asset-pricing model. Any conventional bond or stock pricing model could, therefore, be efficiently manipulated for those returns. The model is applicable for a 'less than' efficient market and, therefore, may be a useful addition in investors' toolkits.

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