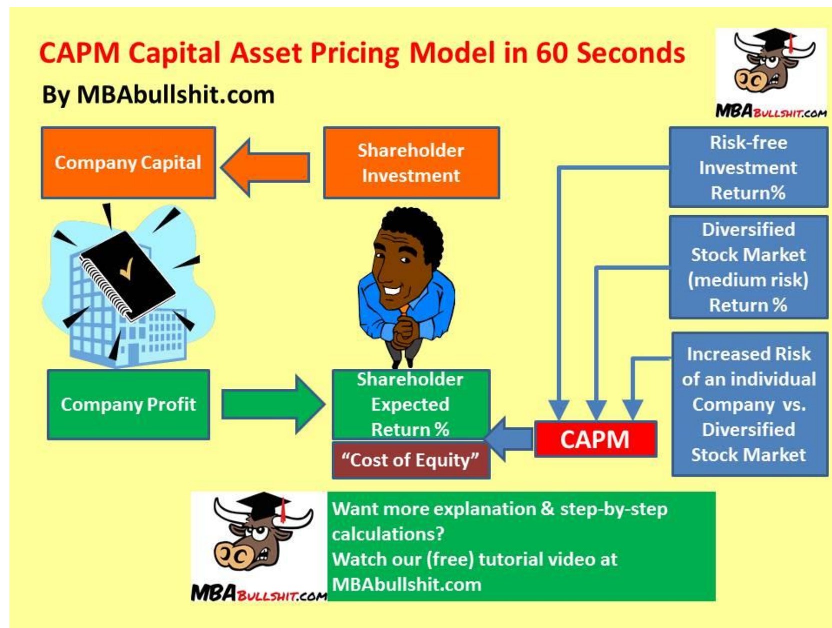
Capital Asset Pricing Model or CAPM Summary "Cheat Sheet" by MBAbullshit.com

- CAPM is just a "model" or formula used to calculate COST OF EQUITY
- Cost of Equity is how much an investor "wants" to earn for investing in a company which is more risky than a safe bank deposit (or government bond), and (usually) more risky than investing in the general stock market with a bunch of stocks. It's called a "cost" because that's how much you should "fairly" pay your investors for investing in your risky company.
- Assumes that investing in many stocks is safer than investing in just one company's stock: "don't put all your eggs in one basket" sorta thing.. this is called "diversified" risk
- Rationale: An investor would "want" (or "expect") more income ("return") for investing in a highly risky company instead of the zero-risk bank/bond, and also instead of investing in a "medium-risk" general stock market. Therefore, cost of equity = "expected return"

You calculate Cost of Equity using the CAPM or Capital Asset Pricing Model Formula:

$$K_e = R_f + B\ (R_m - R_f)$$

DON'T panic! It's MUCH EASIER than it looks! See this formula step-by-step in action, watch it for free right now at http://www.mbabullshit.com or click here.



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