

# THE CAPITAL ASSET PRICING MODEL AND PERFORMANCE MEASUREMENT

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The **capital asset pricing model (CAPM)** is used to determine a theoretically appropriate required rate of return of an asset, if that asset is to be added to an already well-diversified portfolio, given that asset's non-diversifiable risk. The model takes into account the asset's sensitivity to non-diversifiable risk (also known as systematic risk or market risk), often represented by the quantity beta ( $\beta$ ) in the financial industry, as well as the expected return of the market and the expected return of a theoretical risk-free asset.

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