On the Risk-Return Tradeoff in the Stock Exchange of Thailand: New Evidence

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Abstract

This paper provides new evidence on the positive risk-return tradeoff in the Thai stock market using monthly data. An AR(p)-GARCH-in-mean model is applied to the data from January 1981 to December 2009. Since stock prices and dividend series are not cointegrated, the excess returns are separately calculated as capital gain and dividend excess returns. By incorporating the dummy variables that capture the impact of the 1987 global stock market crash and the Asian 1997 financial crisis in the conditional variance equations, the results show that the persistence of excess return volatility is reduced. It is also found that there exists a positive risk-return tradeoff in the stock market in both capital gain and dividend excess returns. The size of the risk-return tradeoff is higher and more highly significant when the market dividend yield is used to obtain the excess return. Therefore, dividend is more important than capital gain. In addition, the impact of volatility on excess returns is not asymmetric implying that the AR(p)-GARCH-in-mean model is sufficient to detect the positive risk-return tradeoff.

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