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Risk and return in stock market investments

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Abstract

Stock market investment is an important component of modern financial planning, offering investors opportunities to generate capital appreciation and income while simultaneously exposing them to varying levels of financial risk. The fundamental relationship between risk and return suggests that investors generally expect higher returns as compensation for accepting greater levels of uncertainty. This study examines the concept of risk and return in stock market investments and analyzes the factors that influence investment performance. It focuses on different forms of investment risk, including systematic risk, unsystematic risk, market risk, liquidity risk, business risk, and financial risk. The study also considers various measures of return, such as capital gains, dividends, and total investment returns. Particular attention is given to the role of diversification in reducing unsystematic risk and improving the risk-return characteristics of an investment portfolio. Traditional financial models and concepts, including portfolio theory, the Capital Asset Pricing Model (CAPM), beta, and the risk-free rate, provide useful frameworks for evaluating the relationship between expected return and risk. Investor characteristics, market conditions, economic factors, interest rates, inflation, corporate performance, and investor psychology can also influence stock market outcomes. The study emphasizes that investment decisions should be based on an appropriate assessment of an investor's risk tolerance, investment horizon, financial objectives, and portfolio diversification. Understanding the relationship between risk and return can help investors make informed decisions and construct portfolios consistent with their financial goals. The study concludes that effective risk management and systematic investment analysis are essential for achieving sustainable returns in the stock market.

Keywords: Stock Market, Investment, Risk, Return, Portfolio Management, Diversification, CAPM, Beta, Systematic Risk, Unsystematic Risk, Investor Behaviour.