SYLLABUS

Program: Mestrado Profissional em Controladoria e Finanças

Course: Behavioral Finance

Course load: 45 hours **Credits**: 3

Instructor: Prof. Dra. Luciana Maia Campos Machado

2th semester 2020

General goals: Modern Finance Theory assumes that investors have rational beliefs, optimize their expected utility and there are no limits on arbitrage. In these models, the influence of psychological and emotional effects on individuals are disregarded. This course aims to discuss the literature and empirical findings that question this central premise of classical finance theory.

Topics: Efficient Markets. Prospect Theory. Framing and mental accounting. Non-expected utility preferences and decision-making. Beliefs, biases and heuristics. Limits to arbitrage. Anomalies.

Course overview: The field of behavioral finance relies on psychology in order to explain some inefficiencies and mis-pricings observed in financial markets, the so-called "anomalies". The classical economic models of rational behavior assume that investors always make decisions that result in the optimal level of benefit or utility for an individual. Market anomalies are not consistent with these models and their assumptions.
On the other hand, in behavioral models, we assume that individuals and markets can behave irrationally for a short or long period of time, subjected to bias and heuristics, and that, also, there may be limits on arbitrage, preventing the markets from reflecting pricing information immediately.

Course structure: The first part of class will consist of a teacher's presentation. Students are expected to have previously read the basic biography indicated for discussion. Also, each session will cover four or five papers and all students must read them before class. Students will form groups of their own choosing, depending on the number of students enrolled for the course. Two or three articles will be designated for each group, to prepare a 60 minute critical presentation, that will be followed by an in-class discussion.

Grading:

Paper proposal: 40%
Participation in class discussions: 30%
Presentations: 30%

1. Quality of the presentations: the discussions to be held by the students will be evaluated in terms of the depth of the content approach and the capacity of the debaters to convey the main concepts, theoretical foundations and reflections on each theme. The grade will be individual. This evaluation item will correspond to 30% of the final concept of the discipline.

2. Participation in class discussions: participation (measured by the quality and frequency of interventions) and depth of critical handouts will account for 30% of the final concept.

3. Paper proposal: each group will prepare a paper proposal to be submitted at the end of the course, accounting for 40% of the final grade. This paper must be conceptually based on one of the themes discussed in class, applying the concepts to the resolution of a practical problem that may arise from the professional

performance of one or more members of the group or from a selected case study. The proposal structure must contain:

Resume
Introduction
Theoretical Reference
Diagnosis of the problem situation (in light of the theoretical framework and discussions held in the classroom)*
*Methodology (*for the solution of the exposed problem situation)*
Final considerations
References

Course schedule and readings:

Session	Date	Topic	Readings/ Presentations
1		Efficient Markets	Shleifer, Andrei (2000) – Chapter 1: "Are Financial Markets Efficient?"
2		From Efficient Markets to Behavioral Finance	De Bondt, W. F., & Thaler, R. (1985). Does the stock market overreact?. *The Journal of finance*, *40*(3), 793-805. Carrion, A. (2013). Very fast money: High-frequency trading on the NASDAQ. *Journal of Financial Markets*, *16*(4), 680-711. Chung, D., & Hrazdil, K. (2010). Liquidity and market efficiency: A large sample study. *Journal of Banking & Finance*, *34*(10), 2346-2357. Fama, E. F. (1998). Market efficiency, long-term returns, and behavioral finance. *Journal of financial economics*, *49*(3), 283-306.
3		Introduction to expected utility	de Castro, P. A. L., Teodoro, A. R. B., de Castro, L. I., & Parsons, S. (2016). Expected utility or prospect theory: Which better fits agent-based modeling of markets?. *Journal of Computational Science*, *17*, 97-102. Friedman, M., & Savage, L. J. (1952). The expected-utility hypothesis and the measurability of utility. *Journal of Political Economy*, *60*(6), 463-474. Livanas, J. (2011). Are investors rational and does it matter? Determining the expected utility function for a group of investors. *Journal of Behavioral Finance*, *12*(2), 53-67. Moscati, I. (2016). Retrospectives: how economists came to accept expected utility theory: the case of samuelson and savage. *Journal of economic perspectives*, *30*(2), 219-36.
4		Non-Expected Utility Preferences	Barberis, N., & Thaler, R. (2003). A survey of behavioral finance. *Handbook of the Economics of Finance*, *1*, 1053-1128. Fryer Jr, R. G., Levitt, S. D., List, J., & Sadoff, S. (2012). *Enhancing the efficacy of teacher incentives through loss aversion: A field experiment* (No. w18237). National Bureau of Economic Research.

			Haigh, M. S., & List, J. A. (2005). Do professional traders exhibit myopic loss aversion? An experimental analysis. *The Journal of Finance*, *60*(1), 523-534. Kahneman, D., & Tversky, A. (2013). Prospect theory: An analysis of decision under risk. In *Handbook of the fundamentals of financial decision making: Part I* (pp. 99-127).
5		Beliefs, Biases and Heuristics	Barber, B. M., & Odean, T. (2001). Boys will be boys: Gender, overconfidence, and common stock investment. *The quarterly journal of economics*, *116*(1), 261-292. Deshmukh, S., Goel, A. M., & Howe, K. M. (2013). CEO overconfidence and dividend policy. *Journal of Financial Intermediation*, *22*(3), 440-463. Ferman, B., Lersch, M. S., & Yoshinaga, C. E. (2017). Viés de familiaridade na alocação de ativos de investidores brasileiros. *Revista Brasileira de Finanças*, *15*(1), 7-24. Gokhale, J., Tremblay, C. H., & Tremblay, V. J. (2015). Misvaluation and behavioral bias in financial markets. *Journal of Behavioral Finance*, *16*(4), 344-356. Ivkovi´c, Z. and Weisbenner, S. (2005). Local does as local is: Information content of the geography of individual investors' common stock investments. The Journal of Finance, 60(1):267–306.
6		Limits to Arbitrage	Baker, M., Bradley, B., & Wurgler, J. (2011). Benchmarks as limits to arbitrage: Understanding the low-volatility anomaly. *Financial Analysts Journal*, *67*(1), 40-54. Bloomfield, R., O'hara, M., & Saar, G. (2009). How noise trading affects markets: An experimental analysis. *The Review of Financial Studies*, *22*(6), 2275-2302. Lam, F. E. C., & Wei, K. J. (2011). Limits-to-arbitrage, investment frictions, and the asset growth anomaly. *Journal of Financial Economics*, *102*(1), 127-149. Lewellen, J. (2011). Institutional investors and the limits of arbitrage. *Journal of Financial Economics*, *102*(1), 62-80. Wang, F. A. (2010). Informed arbitrage with speculative noise trading. *Journal of Banking & Finance*, *34*(2), 304-313.
7		Preferences and Anomalies in the Financial markets	Berument, H., & Kiymaz, H. (2001). The day of the week effect on stock market volatility. *Journal of economics and finance*, *25*(2), 181-193. Bomfim, A. N. (2003). Pre-announcement effects, news effects, and volatility: Monetary policy and the stock market. *Journal of Banking & Finance*, *27*(1), 133-151.

			Cao, M., & Wei, J. (2005). Stock market returns: A note on temperature anomaly. *Journal of Banking & Finance*, *29*(6), 1559-1573. Graham, J. R., & Kumar, A. (2006). Do dividend clienteles exist? Evidence on dividend preferences of retail investors. *The Journal of Finance*, *61*(3), 1305-1336. Schwert, G. W. (2003). Anomalies and market efficiency. *Handbook of the Economics of Finance*, *1*, 939-974.
8		Presentation and discussion of study proposals II	-

References

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