Syllabus: 35906 Behavioral Finance Spring 2021

Thursdays 1:30pm-4:30pm online

Instructor
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Online Instruction Details

All course meetings will occur online. Zoom will be used for class meetings and links for the Zoom session for each class will be listed on Canvas. Lectures will still happen in real time (synchronous) with class participation encouraged. Presentations will be made over Zoom.

Expectations for online class participation
- Attend class with your camera on
- Request to talk by physically raising your hand on camera, or using the zoom hand raise icon
- Keep your audio muted unless called upon
- Sharing video of the class or other course materials is not allowed and is considered a violation of the Booth honor code

Course Overview
This PhD course will examine how psychological biases and non-standard preferences interact with traditional topics in corporate finance and asset pricing. We will survey recent research on biases in individual decision-making, the predictability of security returns, and the practical limits to arbitrage. The objective of the course is (1) to familiarize students with the foundations and recent developments of research in behavioral finance, and (2) to help students develop research ideas and quantitative skills, which can be used to write a successful PhD dissertation.

Topics Covered (may change as the course progresses)
- Non-standard preferences: Prospect theory, realization utility, fairness, relative earnings concerns, etc.
- Time inconsistent preferences: hyperbolic discounting, nudge, retirement savings
- Household trading behavior: disposition effects, mental accounting, limited attention
- Sequencing errors: gambler's fallacy, hot hand, contrast effects, extrapolative beliefs
- Asset pricing anomalies: cross sectional facts, earnings, dividends, sentiment
- Limited attention
- Limits to arbitrage
- Irrational managers and/or irrational markets: CEO overconfidence, CEO market timing, firm norms and culture
- Exploitation of behavioral biases: strategic news disclosure, security design, obfuscation/shrouded attributes
- Practical guide to publishing in behavioral finance: data sources, journal submission process

Assignments

- Three 3-4 page research proposals, due in weeks 3, 6, and 8. Each research proposal should describe a different research idea. The research proposal should clearly state (1) the research question, (2) motivating facts, related literature, and contribution, (3) potential data sources for empirical papers, (4) baseline regression/empirical framework, or sketch of potential model mechanism, (5) how you plan to deal with measurement confounds, alternative explanations, and likely objections, and (6) a 150-word abstract, supposing that you are able to obtain your ideal data and results.
- Present your best idea in week 9. We will discuss expectations of this presentation in class.
- In class presentation (do 1 of 2):
  - 25 minute presentation of a paper (papers are announced as the class progresses). Your goal during this presentation is to pretend you are an author of the paper and you are presenting at a conference.
  - 15 minute discussion of a paper. Your job is place the paper in the literature, evaluate the contribution, point out problems/issues, and propose ways to improve the paper. Present as if the author is in the audience at a conference
- Two problem sets / data exercises.

Recommended reading for a broad overview of the field

Barberis, Nicholas, and Richard Thaler (2003), "A Survey of Behavioral Finance," in George Constantinides, Milton Harris, Rene Stulz (eds.), *Handbook of the Economics of Finance*,

Baker, Malcolm, Richard Ruback, and Jeffrey Wurgler (2007), "Behavioral Corporate Finance: A Survey," in Espen Eckbo (ed.), *Handbook of Corporate Finance: Empirical Corporate Finance*, Elsevier.

Hirshleifer, David (2001), "Investor Psychology and Asset Pricing," *Journal of Finance* 56, 1533-1597.

Kahneman, Daniel (2011), *Thinking, Fast and Slow*, Farrah, Straus, and Giroux.

Thaler, Richard, and Cass Sunstein (2008), *Nudge: Improving Decisions about Health, Wealth,and Happiness*, Yale University Press.

Thaler, Richard (2012), *Misbehaving: The Making of Behavioral economics*, WW Norton & Company.

Shleifer, Andrei (2000), *Inefficient Markets: An Introduction to Behavioral Finance*, Oxford University Press.

Shiller, Robert (2005), *Irrational Exuberance*, 2nd edition, Crown Publishing Group.