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Course Package “Behavioural Finance”

Work Package	WP3: Development of Course Materials for the Reformed MA Programmes, Deliverable 3.1
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1. General information about the course

Explanation: Please fill in the table below.

Title of the course (as specified in the reformed curriculum)	Behavioural Finance
Name of the teacher	Ani Galstyan
Novelty of the course (please select as appropriate)	This course is an updated and revised version of a course which already existed in the curriculum OR <u>This course is a newly developed course (new in the curriculum)</u>
Year of the course in the curriculum	2
Semester of the course in the curriculum	3
Language of instruction of the course	Russian
Number of ECTS credits	2

2. Learning outcomes of the course

Explanation: Please specify the learning outcomes of the course.

LO Level	After competing this course students should be able to
Remembering	<ul style="list-style-type: none">• Recognize the patterns of irrational behaviour of economic agents
Understanding	<ul style="list-style-type: none">• Explain findings in human behaviour when making decisions
Applying	<ul style="list-style-type: none">• Apply research findings in behavioural economics when solving practical problems• Demonstrate analytical skills for financial decision making
Analysing	<ul style="list-style-type: none">• Analyse the decision making of economic agents.• Compare the patterns of human behaviour in various economic situations.• Identify the consequences of behavioural effects.• Identify the behavioural bias and psychological characteristics of investors
Evaluating	<ul style="list-style-type: none">• Classify the patterns of human behaviour in various economic situations.

	<ul style="list-style-type: none"> Suggest investment problems and search for solutions.
Creating	<ul style="list-style-type: none"> Design solutions for investment problems taking into account the behavioural bias.

3. Syllabus of the course

Explanation: Please provide a detailed syllabus of the course (broken down in weeks) – maximum 2 pages

The course "Behavioural finance" consists of 12 topics.

Topic	Academic hours	Description	Week
1. Economic agent - rational or irrational	1	During this class the following topics will be covered: the rationality in neoclassical economics, the irrationality of humans, why economists assume that humans are rational, rational economic agent vs irrational economic agent, how people make decisions, irrational decision making, development of behavioural economics.	1
2. The reasons for the irrational behaviour of "reasonable man"	1	During this class the following topics will be covered: mental accounting, sunk costs effect, the reasons of irrational behaviour.	1
3. Prospect theory	2	During this class the following topics will be covered: rational decision making under risk vs real decision making under risk, certainty effect, the isolation effect, framing effect, the characteristics of prospect theory, representativeness, availability, anchoring, risk aversion.	2
4. Behavioural effects in marketing, work and the public sector	1	During this class the following topics will be covered: the IKEA effect, the effect of "last chance", endowment effect, the power of free, default effect, social norms vs market norms.	3
5. Designing economic processes taking into account behavioural effects. Nudge concept.	1	During this class the following topics will be covered: behavioural "positive" projects, the problem of "consumption-saving" in the neoclassical macroeconomics vs reality, behavioural approach, save more tomorrow, the Nudge concept.	3
6. Capital markets: an analysis of the prerequisites of an efficient market hypothesis.	1	During this class we will cover what theories of asset pricing in the capital market do we use today, the disadvantages of those models and theories, the reason of existing issues, solutions for them.	4
7. Capital markets: anomalies	2	During this class the following topics will be covered: empirical verification of Capital Assets Pricing Model, market anomalies, overreaction effect, reluctance to realize losses, regret theory, disposition effect, post-earnings announcement drift, size effect, behavioural investment funds, equity premium puzzle.	4,5
8. Capital markets:	3	During this class the following topics will be covered:	5,6

market modelling and bubbles		factors that impact the decision making of traders, the relationship of market returns and external factors (geomagnetic activity, sunny days, winter depression), calendar effects (Monday effect, pre-holiday rally, January effect, end of December), investment sentiments, Coherent markets hypothesis, investor expectations, house money illusion, emotions, Behavioral Models of Asset Pricing, bubbles and uncertainty	
9. Capital structure: a behavioural approach. Initial Public Offering (IPO).	2	During this class the following topics will be covered: traditional theories of capital structure (trade-off theory, pecking order theory), empirical researches, behavioural theories of capital structure (the market timing theory, the theory of informational cascades, the theory of managerial investment autonomy), behavioural approach to IPO.	7
10. Dividend Policy: A Behavioural Approach	1	During this class the following topics will be covered: The problem and theories of dividend policy in modern finance, Catering Theory of Dividends.	8
11. Mergers and Acquisitions: Behavioural Aspects	1	During this class the following topics will be covered: the reasons patterns of mergers and acquisitions, behavioural theories of corporate acquisitions (irrationality of managers and investors), winner's curse.	8
12. Managing company value in an inefficient market.	2	During this class the following topics will be covered: Neoclassic vs Inefficiency, strategies of value management, value maximisation in efficient and inefficient markets, the game of the name, information management, the role of market expectations.	9

4. Teaching methodology of the course

Explanation: Please explain the teaching methodology and pedagogical approaches of the course – maximum ½ page

This course will be taught in an interactive manner, involving classroom experiments. At the same time main topics will be presented to students by using presentation slides. The understanding of key issues will be enhanced during the classroom discussions.

It is important to enhance the ability of students to solve problems themselves, without any guidance, as nobody is going to guide them through every problem in their workplace. In order to improve this ability, the students will be given freedom to solve some problems during this course. Firstly, they will have to choose a topic to write an essay and they will not be given any requirements concerning to the structure. Secondly, they will have to present a case-study by designing and structuring the presentation as they like, creativity is appreciated.

5. Labour market relevance of the course

Explanation: Please explain the labour market relevance of the course (linked to findings of WP1) – maximum ½ page

Behavioural economics has become a mainstream in the field of economics several years ago. Nowadays investment policies succeed or fail at least in part depending on how well they reflect or account for behavioural responses. Insights from behavioural finance, which allow for realistic deviations from standard economic assumptions about behaviour, have consequences for the design and functioning of investment policies.

Moreover, the conducted labour market survey within the Erasmus+ Capacity Building in Higher Education Project - “Reforming Master Programmes in Finance in Armenia and Moldova” (REFINE), revealed that the main requirement of the labour market regarding the MA programme in finance was the practice orientation. Behavioural finance, which takes into account the irrationality of economic agents, gives knowledge that can be used when solving practical economics problems and making decisions in workplace. Another issue, that was found out by the labour market analysis, was improving the strategic planning skills of the graduates. In this respect too, the knowledge in behavioural finance will allow to further improve the abilities of students in strategic planning by allowing them to recognize and take into account the behavioural bias.

Thus, finance master's programme graduates must have knowledge in the field of behavioural finance, so that they can apply them in the companies where they work.

6. Assessment and grading

Explanation: Please explain the form of assessment of the course – maximum ½ page

The assessment of the knowledge of the students enrolled in this course consists of three parts: written tests, essay and case-study.

The written tests will form 50% of the final grade.

The submission of the essay will form 25% of the final grade.

The presentation of the case-study will form 25% of the final grade.

7. References

Explanation: Please provide the main references and recommended reading for the course – maximum 1 page

Main references

- Gigerenzer, G. (2001) "Decision making: Nonrational theories," In N. J. Smelser & P. B. Baltes (Eds.), *International Encyclopedia of the Social and Behavioral Sciences*. Vol. 5 (pp. 3304-3309). Oxford, UK: Elsevier.
- Kahneman, D., and A. Tversky (1974), "Judgment Under Uncertainty: Heuristics and Biases," *Science* 185, 1124-31.
- Kahneman D. and A. Tversky (1979), "Prospect Theory: An Analysis of Decision Under Risk," *Econometrica*, 47, pp. 263—91.
- Shleifer, Andrei and Vishny, Robert W., 1997, *The Limits of Arbitrage*, *Journal of Finance*, 52, 35-55.
- Simon, H. (2000), "Barriers and bounds to rationality," *Structural Change and Economic Dynamics*, 11, 243–253.
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- Kahneman, Daniel. *Thinking, Fast And Slow*. New York : Farrar, Straus And Giroux, 2011.
- Thaler, R. H. (2015). *Misbehaving: The making of behavioral economics*.
- Ackert, L. F., & Deaves, R. (2010). *Behavioral finance: Psychology, decision-making, and markets*. Mason, OH: South-Western Cengage Learning.
- Edward Cartwright (2014). *Behavioral Economics*. Routledge, Taylor and Francis Group.
- Peter Diamond, Hannu Vartiainen, *Behavioral Economics and Its Applications*, Princeton University Press, 2012.
- H. Kent Baker, John R. Nofsinger, *Behavioral Finance: Investors, Corporations, and Markets*, John Wiley & Sons. 2010.
- Edwin Burton, Sunit Shah, *Behavioral Finance: Understanding the Social, Cognitive, and Economic Debates*, John Wiley & Sons. 2013.
- Michael M. Pompian, *Behavioral Finance and Investor Types: Managing Behavior to Make Better Investment Decisions*, 2012.
- A gradient of childhood self-control predicts health, wealth, and public safety. Edited by James J. Heckman, University of Chicago, Chicago, IL, and approved December 21, 2010 (received for review July 13, 2010).

- Ralph Adolphs, Daniel Tranel, and Antonio R. Damasio: Dissociable neural systems for recognizing emotions. Department of Neurology, Division of Cognitive Neuroscience, University of Iowa College of Medicine, Iowa City, IA 52242, USA Accepted 26 September 2002.

- Dan Ariely and Michael I. Norton. From thinking too little to thinking too much: a continuum of decision making. Volume 2, January/February 2011, John Wiley & Sons, Ltd.

Recommended reading

- Ariely, Dan. The Upside of Irrationality: The Unexpected Benefits of Defying Logic at Work and at Home. Harper, 2010.

- Baker, Malcolm and Wurgler, Jeffrey, 2002, Market Timing and Capital Structure, Journal of Finance, 57, 1-32.

- Burnham, Terry, 2003, Caveman Economics: Proximate and Ultimate Causes for Non-Materially Maximizing Behavior, Manuscript.

- Copeland, J., Dolgoff, A. and A. Moel (2004). "The role of expectations in explaining the cross-section of returns," Review of Accounting Studies, Vol. 9.

- Damasio, A.R., 1994, Descartes' Error: emotion, reason and the human brain. Avon Books, New York.

- Fama, Eugene, 1998. Market efficiency, long-term returns, and behavioral finance. Journal of Financial Economics, 49, 282-306.

- Loewenstein, George, 2002. When Genius Failed: The Rise and Fall of Long-Term Capital Management.

- Shleifer, A. Inefficient Markets: An Introduction to Behavioral Finance. New York: Oxford University Press, 2000.

8. Course assignments

Explanation: Please provide two assignments for the course (e.g. group work, project, essay, case study, homework).

8.1 Assignment 1

Submission of an essay on a suggested topic, which is confirmed by the lecturer.

During these assignment students will have the challenge to select a topic in the field of behavioural finance, which is interesting for them and write an essay about it. The only requirements are the following: minimum 5 pages, no plagiarism, it has to be their opinion.

8.2 Assignment 2

Presentation of a case study project on the topic of the student's master's thesis.

During these assignment students will make a minimum of 30 minutes' presentation of a case study project on the topic of their master's thesis, which they will have the opportunity to use in their research. Students will have the freedom to design their presentation as they like by demonstrating creativity.

Annex: Presentation slides

Explanation: Please provide presentation slides for your course (this can be done in a separate document, e.g. Power Point (Minimum: 25 slides))