



Behavioral Finance Course Syllabus

Fall 2021

Sarah Khalaf

FIN 435 – Behavioral Finance

Lecture Time and Location

Section 01A : M/W at 2:00 PM – 3:15 PM. Location in Area C1 – Room 1021

Contact Information

Location : Department of Finance & Financial Institutions – Area B – 4th Floor
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Office Hours : M/W 12:30 – 1:30 or by appointment
Social Media : N/A

Course Description

The course will examine the key psychological obstacles to value maximizing behavior, along with the steps that managers can take to mitigate the effects of these obstacles. The principles of psychology are used to analyze valuation, capital budgeting, perceptions of risk and return and other issues.

The course go over relevant financial topics as taught through traditional financial theory, then highlight empirical violations to the theory, and finally introduce psychological concepts that help explain the disconnect between theory and practice.

Course Learning Outcomes

The learning outcomes for this course, listed below, relate to the learning goals of the College of Business Administration Undergraduate Program, which can be found at the end of the this syllabus. The numbers in parenthesis indicate to which specific learning goal the outcome relates.

Upon successful completion of the course, students will be able to:

1. Recognize the various heuristics and biases that predictably influence our financial decision-making abilities (LG1, LG5)
2. Use mean-variance optimization and value-at-risk analysis to examine risk and return of a portfolio in both the traditional and behavioral methods. (LG1, LG5)
3. Start recognizing behavioral patterns that may lead to profitable trading strategies. (LG1, LG5)
4. Present and discuss new strategies or behavioral experiments and any associated analyses performed to a wider audience. (LG2)
5. Distinguish between unfavorable emergent behavioral phenomenon and conscious fraudulent decisions in the financial domain. (LG4)



CLO Mapping to CBA Skill Based Competency Goals¹

CLO	Competency Goal			
	Analytical	Communication	Information Technology	Business Ethics
1	I			
2	R			
3	I			
4		A		
5				I

Type of Emphases:

- **(I)ntroduce:** Students will be introduced to the skill and their grasp of it assessed in the course.
- **(A)pply:** The course will not cover the skill. Students should have a high-level grasp of the skill and are required to apply it in the course.
- **(R)einforce:** Students should have an introductory-level grasp of the skill and the course will improve their mastery to a higher level.

Suggested Prerequisites

Principles of Financial Management (FIN220), Principles of Investment (FIN320), Intermediate Financial Management (FIN327)

Textbooks and Reference Material

Textbook: Ackert, Lucy, and Richard Deaves. *Behavioral finance: Psychology, decision-making, and markets*. Cengage Learning, 2009.

Selected chapters from books and published academic papers will be distributed to students, along with a Course Handbook. The required readings for each course topic are provided in detail in the Course Outline below.

Reference Books:

1. Chancellor, Edward. *Devil take the hindmost: A history of financial speculation*. Penguin Books, New York, 1999.
2. Gigerenzer, Gerd, and Peter M. Todd. *Simple heuristics that make us smart*. Oxford University Press, USA, 1999.
3. Kindleberger, Charles P., and Robert Z. Aliber. *Manias, panics and crashes: a history of financial crises*. Palgrave Macmillan, 2011.
4. Shefrin, Hersh. *Beyond fear and greed. Understanding Behavioral Finance and the Psychology of Investing*. HBS, Boston, 2000.
5. Surowiecki, James. *The Wisdom of Crowds*. Doubleday, New York. 2004

¹ CBA Competency Goals can be found at the end of this document



E-Learning System: Moodle and MS Teams

Course Website: N/A

Course Requirements and Policies

Individual Assignments: There will be **three** assignments, cases or problem sets, to solve. They will count towards 15% of your grade (5% each). All work must be done individually. You will have at least 1 week to complete each assignment from the date that it is posted on Moodle. You may come to office hours with any questions and for help solving the problems. The assignments will include the analysis of a behavioral bias, a trading strategy that takes advantage of a bias, and the analysis of a historical price bubble.

Presentation: Each student will be required to professionally present to the class. You will be basing your presentation on one of your assignments. You are free to choose which assignment to present. You will have 3 opportunities to present during the semester. If you do not volunteer for a date to present, I will assign presentation dates to each student. This presentation will count towards 5% of your final grade. Presentations for earlier assignments will be graded more leniently than those for later assignments.

Online Games: We will have 2 games during class that will be played online. Instructions for registration and signing up to the appropriate website will be provided before the games. After the end of each game, you are required to complete a worksheet on Moodle. This will count towards your attendance and participation grade.

Exams:

Midterm Exams

There will be 2 midterms during the semester, which may both be conducted outside regular class hours. Each exam will account for 15% of the course grade. The exams will not be cumulative and the professors will attempt to cover the material in accordance with the assignment and course coverage sheet. However, students should be aware that the field of finance is in its nature cumulative.

Final Exam

The final exam counts for 40% of the grade. It will be cumulative and comprehensive. The final exam will continue to follow the same pattern established in the midterms except that the problems and the exam will be more extensive. Students will be notified of the exam date at the beginning of the semester; however, the instructor retains the right to change the dates.

Attendance and Participation: Every student in this course must abide by the Kuwait University Policy on Attendance (published in the Student Guide, Chapter 3, Section 13). Late comers will be counted as absent. Showing up to class is not sufficient to receive the full 10% of your grade. Students must be prepared for the day's lecture by reading the required material as class discussions will require participation. A copy of the student guide can be accessed online on:

http://www.kuniv.edu/cs/groups/ku/documents/ku_content/kuw055940.pdf



Cheating and Plagiarism: Every student in this course must abide by the Kuwait University Policy on Cheating and Plagiarism (published in the Student Guide, Chapter 3, Section 2). A copy of the student guide can be accessed online on:

http://www.kuniv.edu/cs/groups/ku/documents/ku_content/kuw055940.pdf

Please carefully note all sources and assistance when you turn in your work. Under no circumstances should you take credit for work that is not yours. You should neither receive nor give any unauthorized assistance on any deliverable. If you have any questions about what constitutes “unauthorized assistance” please email me before the deliverable is submitted.

Writing Style: Students must refer to APA writing style for their assignments and report writing. Refer to the English Language Center for help.

Grading:

The scores in this course will be the weighted average of the following items:

Weight	Description
10%	Attendance and Participation
15%	Assignments (x3)
5%	Presentation
30%	Midterm (x2)
40%	Final
100%	TOTAL

Grade Distribution:

Grade	Range	Grade	Range
A	≥ 95	C+	≥ 77 and < 80
A-	≥ 90 and < 95	C	≥ 73 and < 77
B+	≥ 87 and < 90	C-	≥ 70 and < 73
B	≥ 83 and < 87	D+	≥ 65 and < 70
B-	≥ 80 and < 83	D	≥ 60 and < 65
		F	< 60

Course Outline:

Title	Topics
Foundations of Finance	Rational Agents • Modern Portfolio Theory • Risk and Return • Diversification • Mean-Variance Optimization • Capital Asset Pricing Model <u>Required Readings</u> 1. Sections 2.1 and 2.2 of “Chapter 2: Foundations of Finance II: Asset Pricing, Market Efficiency, and Agency Relationships.” Pages 19 – 28. Ackert and Deaves (2009).
Efficient Market Hypothesis	Law of One Price • Arbitrage • Intrinsic Value • Present Value and Discounting Cash Flows • Efficient Market Hypothesis • Information



	<p>Theory • Wisdom of the Crowds • In-class experiments • Joint Hypothesis Problem</p> <p><u>Required Readings:</u></p> <ol style="list-style-type: none"> Section 2.3 of “Chapter 2: Foundations of Finance II: Asset Pricing, Market Efficiency, and Agency Relationships.” Pages 28 – 31. Ackert and Deaves (2009). “Chapter 1: Part II: The Wisdom of Crowds.” Pages 7 – 11. Surowiecki (2004)
Limits to Arbitrage	<p>Perfect Substitutes • Cost of Information Acquisition • Processing Information, Investor Attention and Sophistication • Risk Aversion • Agency Problems in Money Management and Investment</p> <p><u>Required Readings:</u></p> <ol style="list-style-type: none"> Section 2.4 of “Chapter 2: Foundations of Finance II: Asset Pricing, Market Efficiency, and Agency Relationships.” Pages 31 – 33. Ackert and Deaves (2009). “Chapter 4: Challenges to Market Efficiency.” Pages 72 – 75. Ackert and Deaves (2009). “Chapter 11: Part I: Markets: Beauty Contests, Bowling Alleys, and Stock Prices.” Pages 224 – 228. Surowiecki (2004) <p><u>Recommended Readings:</u></p> <ol style="list-style-type: none"> Shleifer, Andrei, and Robert W. Vishny. "The limits of arbitrage." <i>The Journal of finance</i> 52.1 (1997): 35-55.
Theory of Investor Sentiment	<p>Expected Cash Flow Errors and Discount Rate Changes • Systematic Behavioral Biases • Heuristics and Rules of Thumb • Macro Factors: Culture, Language, and Location, etc.</p> <p><u>Required Readings:</u></p> <ol style="list-style-type: none"> “Chapter 5: Heuristics and Biases.” Pages 83 – 101. Ackert and Deaves (2009). “Chapter 6: Overconfidence.” Pages 106 – 115. Ackert and Deaves (2009). “Chapter 8: Implications of Heuristics and Biases for Financial Decision-Making.” Pages 137 – 147. Ackert and Deaves (2009). <p><u>Recommended Readings:</u></p> <ol style="list-style-type: none"> “Chapter 1: Introduction.” Pages 3 – 12. Shefrin (2011).
Semi-Strong Efficient Markets	<p>Combining Limits to Arbitrage and Investor Sentiment • Implications of Semi-Strong Efficient Markets • Long-Short Trading Portfolios • Market Anomalies • Multiple Risk Factor Models (Fama-French 3-Factor, etc) • Market Puzzles</p> <p><u>Required Readings:</u></p> <ol style="list-style-type: none"> “Chapter 13: Behavioral Explanations for Anomalies.” Pages 219 – 222. Ackert and Deaves (2009). “Chapter 14: Do Behavioral Factors Explain Stock Market Puzzles?” Pages 237 – 243. Ackert and Deaves (2009). “Chapter 17: IPOs: Initial Underpricing, Long-term Underperformance, and “Hot-Issue” Markets.” Pages 239 – 255. Shefrin (2011).
Bubbles, Crashes, and Manias	<p>Minsky Model • Tulip Mania, Soug AlManakh • Violations to the Wisdom of the Crowds</p> <p><u>Required Readings:</u></p>



	<ol style="list-style-type: none"> 1. “Chapter 1: This Bubble World: The Origins of Financial Speculation” Pages 14 – 29. Chancellor (1999). 2. Craig, Ben. “The Souk al-Manakh Crash.” <i>Federal Reserve Bank of Cleveland Economic Commentary</i> (2019). 3. “Chapter 6: Euphoria and Paper Wealth.” Pages 132 – 142. Aliber and Kindleberger (2011). 4. “Chapter 11: Part IV: Markets: Beauty Contests, Bowling Alleys, and Stock Prices.” Pages 241 – 258. Surowiecki (2004)
Complex Systems and Emergent Behavior in Financial Markets	System 1 and System 2 • Nudging • Biases or Heuristics for Survival? • Complex Systems • Emergent Behavior • Ecological Rationality • Bounded Rationality • Satisficing • Recognition Heuristic

Course Schedule

Day	Month	Lecture	Due	Slides #
25	Oct	Introduction and Syllabus		
27	Oct	Foundations of Finance		1
1	Nov	Foundations of Finance		1
3	Nov	Foundations of Finance		1
8	Nov	Market Efficiency		2
10	Nov	Market Efficiency		2
15	Nov	MIDTERM		
17	Nov	Limits to Arbitrage		3
22	Nov	Ultimatum Game - Online	Worksheet	
24	Nov	Investing Game - Online	Worksheet	
29	Nov	Limits to Arbitrage		3
1	Dec	Theory of Investor Sentiment		4
6	Dec	Theory of Investor Sentiment	Homework #1	4
8	Dec	Theory of Investor Sentiment		4
13	Dec	Theory of Investor Sentiment Presentations	HM 1 Due	4
15	Dec	MIDTERM		
20	Dec	Semi-strong Efficient Markets		5
22	Dec	Semi-strong Efficient Markets	Homework #2	5
27	Dec	Semi-strong Efficient Markets		5
29	Dec	Semi-strong Efficient Markets Presentations	HM 2 Due	5
3	Jan	Bubbles, Crashes, and Manias		6
5	Jan	Bubbles, Crashes, and Manias	Homework #3	6
10	Jan	Bubbles, Crashes, and Manias		6
12	Jan	Bubbles, Crashes, and Manias Presentations	HM 3 Due	6
17	Jan	Complex Systems		7
19	Jan	Complex Systems		7
31	Jan	FINAL EXAM 5:00 PM - 7:00 PM		



CBA Competency Goals

1. **Analytical Competency:** A CBA graduate will be able to use analytical skills to solve business problems and make a well-supported business decision.

Student Learning Objectives:

- 1.1. Use appropriate analytical techniques to solve a given business problem.
- 1.2. Critically evaluate multiple solutions to a business problem.
- 1.3. Make well-supported business decisions.

2. **Communication Competency:** A CBA graduate will be able to communicate effectively in a wide variety of business settings.

Student Learning Objectives:

- 2.1. Deliver clear, concise, and audience-centered presentations.
- 2.2. Write clear, concise, and audience-centered business documents.

3. **Information Technology Competency:** A CBA graduate will be able to utilize Information Technology for the completion of business tasks.

Student Learning Objectives:

- 3.1. Use data-processing tools to analyze or solve business problems.

4. **Ethical Competency:** A CBA graduate will be able to recognize ethical issues present in business environment, analyze the tradeoffs between different ethical perspectives, and make a well-supported ethical decision.

Student Learning Objectives:

- 4.1. Identify the ethical dimensions of a business decision.
- 4.2. Recognize and analyze the tradeoffs created by application of competing ethical perspectives.
- 4.3. Formulate and defend a well-supported recommendation for the resolution of an ethical issue.

5. **General Business Knowledge:** A CBA graduate will be able to demonstrate a basic understanding of the main business disciplines' concepts and theories.

Student Learning Objectives:

- 5.1. Acquire a fundamental understanding of knowledge from the main business disciplines (e.g. finance, accounting, marketing, and management information systems, among others).