The field of Finance has traditionally made assumptions of human rationality in decision making in order to facilitate modeling. It has been a great success that has developed powerful Nobel prize-winning theories that are quite consistent with observation – contributions such as portfolio theory, option-pricing, valuation, agency and signaling among others. These contributions have gone on to revolutionize the practice of both investment and corporate finance. However, there remain many anomalies that these traditional models struggle to explain; such as, various anomalies in the price of assets (e.g., why low P/E firms outperform the high ones), the wide swings in stock prices – say relative to the more stable dividends shareholders receive, and why managers attempt to keep earnings stable through Earnings Per Share (EPS) manipulation. The field of Behavioral Finance has put forth explanations for these anomalies and others by relaxing the assumption of the perfectly rational human. In this course, I define the traditional finance’s decision-maker as having three traits: (1) he is only interested in maximizing his own welfare; (2) his models for determining his utility as a function of his actions follow perfect mathematical logic; and (3) the cool, calm and collected decision-maker takes actions without emotional bias. We will find that there are substantial violations of each of these. Thus, humans being aware of them can help themselves in their everyday life as well as in finance, and that they might shed light on some of the anomalies that Traditional Finance have had a hard time explaining.

This course has the following learning goals:

1. To gain an enhanced understanding of how individuals actually make financial decisions with a view to more informed, prescriptive decision making within investment, organizations and on a personal basis.

2. To critically discuss existing behavioral economics research as well as to present their own research ideas, with a view to empirical application.

3. To apply important behavioral biases of beliefs and preferences in financial settings, e.g., overconfidence, loss aversion, skewness preference, reference-dependence, narrow framing, myopia, or time-inconsistency

Students are expected to attend class regularly and arrive on time. Students must complete all assigned readings before the class meeting and be prepared to participate actively in discussions of the readings and current events. Students are required to turn in all written assignments on the dates scheduled. Late work will be penalized.

Students will be evaluated on the following basis:

1. Weekly Homework Exercises (10%)
2. Midterm Examination (30%)
3. Final Paper, including Proposal (20%)
4. Final Examination (40%)

Failure to submit or fulfill any one of the required course component results in failure of the class.

**Assessment Expectations**

**Grade A:** Full attendance, thoughtful participation, assignments turned in on time and meet assigned grading criteria

**Grade B:** Full attendance, thoughtful participation, assignments turned in on time but partially meet assigned grading criteria

**Grade C:** Partial attendance, little participation, assignments turned in late and/or partially meet assigned grading criteria

**Grade D:** Partial attendance, no participation, assignments turned in late and/or do not meet assigned grading criteria

**Grade F:** Poor attendance, no participation, assignments turned in late and/or do not meet assigned grading criteria

**Grade conversion**

A=94-100
A-=90-93
B+=87-89
B=84-86
B-=80-83
C+=77-79
C=74-76
C-=70-73
D+=67-69
D=65-66
F=below 65

**Grading Policy**

No-shows for in-class presentations and assignments submitted after the deadline without requesting an extension will receive zero grades.

If a student believes an inadvertent error was made in the grading of an individual assignment or in assessing an overall course grade, a request to have the grade re-evaluated may be submitted. To appeal an assigned final grade, the student should first email the course instructor requesting clarification about how the grade was determined. If the student is not satisfied with the outcome of the discussion and wishes to appeal the grade further, a formal written appeal should be submitted to the site director. **This appeal must be submitted within 30 days after the grade has been posted; appeals that are submitted after this deadline will not be considered.**
Study abroad at Global Academic Centers is an academically intensive and immersive experience, in which students from a wide range of backgrounds exchange ideas in discussion-based seminars. Learning in such an environment depends on the active participation of all students. And since classes typically meet once or twice a week, even a single absence can cause a student to miss a significant portion of a course. To ensure the integrity of this academic experience, class attendance at the centers is mandatory, and unexcused absences will be penalized with a two percent deduction from the student’s final course grade. Students are responsible for making up any work missed due to absence. Repeated absences in a course may result in failure.

All medical-based absence requests MUST be presented to the Manager of Student Life and Housing (MSLH). In the case of illness, contact the MSLH within seven (7) days of the absence or as soon as practicable and provide medical documentation. Non-medical requests should be made to the Assistant Director for Academics (AD/Academics) and in advance of the intended absence. Your instructors will be informed of any excused absence; they are not authorized to approve your absence, and they are required to report any absences to the AD/Academics.

**NYU Policy on Religious Holidays**

1. Students who anticipate being absent because of any religious observance should, whenever possible, notify faculty and the AD/Academics in advance of such anticipated absence.

2. Whenever feasible, examinations and assignment deadlines should not be scheduled on religious holidays. Any student absent from class because of his/her religious beliefs shall not be penalized for any class, examination, or assignment deadline missed on that day or days. In the event that examinations or assignment deadlines are scheduled on a religious holiday, any student who is unable to attend class shall be permitted the opportunity to make up any examination or to extend any assignment deadline missed on that day or days.

3. That no adverse or prejudicial effects shall result to any student who avails him/ herself of the provisions of the resolution.

4. A violation of these policies and principles shall permit any aggrieved student to bring forward a grievance, provided under the University Grievance Procedure.

**Late Submission of Work**

All works must be submitted on time, unless you have received an explicit extension. Any late submission may result in grade deduction at the sole discretion of the instructor.

**Academic Accommodations for Students with Disabilities**

Academic accommodations are available for students with documented disabilities. Please contact the Moses Center for Students with Disabilities at 212-998-4980 or see their website (http://www.nyu.edu/life/safety-health-andwellness/students-with-disabilities.html) for further information.

**Plagiarism Policy**

Plagiarism is the presentation of another person’s words, ideas, judgment, images or data as though they were your own, whether intentionally or unintentionally. Plagiarism constitutes an academic offence for which you can be disciplined. Punishment may include a failing grade, suspension or expulsion. In all confirmed cases, a report will be sent to the student’s Dean at NYU or, in the case of a non-NYU student, to the home institution.

**Required Text(s)**

Daniel Kahneman, Thinking Fast and Slow, Farrar, Straus and Giroux.


Internet Research Guidelines

It is hard to overestimate the importance of the internet to the build up of contemporary knowledge of the world around us. But it needs to be used wisely. This means that one must be selective and careful when relating to internet-based sources, identifying and distinguishing opinions from facts, and journalism from academics. One should make clear reference to internet sources, allowing the reader the opportunity to consult these resources as and if required. As with all sources of information, use the internet critically.

Please also note that the ‘world-wide web’ exists in many languages. Many sources about Israel in English, for instance, will be aimed at tourists or readers living primarily in English-speaking regions of the world. Sources might differ when reading them in other languages.

NYUTA’s Writing Center

Established in coordination with NYU’s Expository Writing Center, NYUTA’s Writing Center is available to help you with all genres of writing, from senior theses to smaller response papers; from personal statements to cover letters; from PowerPoint presentations to creative assignments. The Center can help you at any stage of the writing process, from figuring out the demands of an assignment, to working with or researching sources, to brainstorming a thesis and outline, to finalizing a project or reviewing a draft. However, please note that writing sessions are held as a joint session, an active exercise between the student and writing advisor – this is not a proofreading service!

Please view the Writing Center as an opportunity, not a punishment. It is meant equally for student-writers who are not confident in their skills as well as students who are quite talented and strong, but recognize the value of a second look. Moreover, rest assured that your instructors will value and appreciate your initiative to visit the writing center.

For more information or to schedule an appointment, please contact NYUTA’s AD/Academics, Edan Raviv (room 201; edanr@nyu.edu).

Additional Equipment

Students should have a graphing calculator.

Session 1

Efficient Market Hypothesis: Implication and Limitations

Students will be introduced to Eugene Fama’s investment theory of the Efficient Market Hypothesis (EMH), its implications in terms of ‘beating the market’ and the three key hypotheses related to it. Students will critically engage with the theory via journal articles, and their own analysis and evaluation of the theory.


Session 2

Anomalies: Cross-Sectional, Arbitrage, Macro

Students will analyze the presence of regularly occurring anomalies in conventional economic theory, and how and why they directly violate modern financial and economic theories, which
assume rational and logical behavior. Students will consider the January Effect, The Winner’s Curse and the Equity Premium Puzzle in small groups.


**Session 3**

**Institutional Finance and Applications**

Students will be introduced to the options of intermediary financial institutions between savers and investors, which provide services outside of the purview of traditional commercial banking including PFIs, NBFCs and ITMFs. Students will consider the key opportunities and limitations these potential avenues present.


**Session 4**

**Prospect Theory**

Students will critically engage with the way people choose between risk inclusive probabilistic alternatives, where they are unable to engage with the probabilities through an active workshop, followed by a critical analysis of loss aversion and risk seeking behavior.


Daniel Kahneman, Thinking Fast and Slow, Farrar, Straus and Giroux. Part IV.

**Session 5**

**Probability Processing**

Students will explore topics including cognitive processing, conceptual discretizing, loss aversion and probability weighting through various theories proposed in the field.

Daniel Kahneman, Thinking Fast and Slow, Farrar, Straus and Giroux. Part II.

**Session 6**

**Overconfidence**

Students will explore the role of overconfidence within the investment industry, despite having access to the best industry reports and computational models, the impacts of this – as well as potential solutions.


Daniel Kahneman, Thinking Fast and Slow, Farrar, Straus and Giroux. Part III.

Session 7

Relativism, Home Bias, Two Systems
Students will be introduced to the equity home bias puzzle, and explore the issues of portfolio diversification in both portfolios and stocks, a key puzzle of international macroeconomics. Students will compare its presence in emerging and developed market economies, and the impact on volatility and in the longer term – economic growth and development.

Daniel Kahneman, Thinking Fast and Slow, Farrar, Straus and Giroux. Part I.

Session 8

Hyperbolic Discount and Procrastination
Students will be introduced to the discounted utility approach and the value of intertemporal choices, and their relative utility value. Students will discuss its criticisms, both qualitatively through empirical engagement, and also via the mathematical model.


Session 9

The Role of Social Capital
Students will identify the effect of social capital on financial development, and the variables that influence such results, specifically engaging in case studies within the Middle East including Israel, Palestine and Saudi Arabia.


Session 10

Culture and Religion: The Case of Israel
Students will explore the role of belief systems and cultural economics as determinants of behavioral finance, and how preferences of respective groups relate to economic outcomes such as income and productivity, with regard to the key institutions of Israel on both the micro and macro scale.


Session 11

Investor and Manager Behavior
Students will define and explore the assumption of rationality, the belief that individuals behave in a rational manner and that all existing information is embedded in the investment process, returning to the EMH, and discuss potential counters to so-called irrational behavior.


**Experimental and Neuroeconomics**

In order to explain human decision making, students will consider various research methods from within behavioral economics and cognitive-social psychology, their techniques, limitations and experimental outcomes, as well as planning their own studies in small breakout groups.


**Management in an Inefficient Market**

Given the apparent contradiction between investor rationality and perfect arbitrage and psychological and institutional evidence, students will explore and explain alternative models to generate predictions about security prices, and potential routes to implementation.


**Behavioral Finance and the 2008 Crisis**

In this final class, students will use all of the tools, methods, theories and critiques to generate a behavioral finance oriented understanding of the causes, responses and potential alternatives to the 2008 financial crisis.


Classroom Etiquette

Please raise your hand before speaking in class.

Computers are acceptable in class, but please do not abuse this privilege by using them for non-class related activities.

Place all mobile devices on silent.