

## DISCIPLINE SPECIFIC ELECTIVE -FINANCE (DSE-14)

### DSE 12: Behavioral Finance

#### Credit distribution, Eligibility and Pre-requisites of the Course

Course title & Code	Credits	Credit distribution of the course			Eligibility criteria	Pre-requisite of
		Lecture	Tutorial	Practical/ Practice		
Behavioral Finance (DSE 12)	4	3	1	0	Class XII	Basics of Finance

#### Learning Objective(s):

- Introduce the students to the role of human behavior in financial decision making.
- Develop a comprehensive view of the psychological foundations and their applications to Corporate Finance and understanding investor behavior.

#### Learning Outcomes:

- Establish a strong foundation of the basic concepts of Behavioral Finance.
- Explain the psychological biases and heuristics which affect financial decision making.
- Analyse the application of behavioral finance in Corporate Finance, Individual and Institutional Investor Trading Behavior.

#### Syllabus DSE

**Unit 1: Foundation and Key Concepts (9 Hours)** Introduction to Behavioural Finance – Overview, Evolution, Key Themes, and Applications. Traditional versus Behavioural Finance: Limits to Arbitrage – Market Efficiency, Fundamental Risk, Noise Trader Risk, Implementation Costs. Theoretical and Empirical underpinnings of Behavioral Finance – Prospect Theory, Framing Effects, Heuristics and Biases, and Affect Theory. Emotional Finance: Concept, Emotional Finance in Practice –Risk, Momentum, Bad News Anomaly.

**Unit 2: Psychological Concepts and Behavioral Biases (12 Hours)** Heuristics or Rules of Thumb, Disposition Effect, Prospect Theory and Behavioral Finance, Overconfidence, Representativeness Heuristics, Familiarity Bias, Limited Attention, Ambiguity aversion, Loss aversion, Framing, Self-deception, Mental Accounting, Self-control, Regret avoidance, Availability bias, Anchoring bias, Optimism and Wishful Thinking, Overreaction and Underreaction, Self-attribution, Endowment Effect, Herd Behavior, Hindsight bias, Winners’ Curse, Cognitive Dissonance, Status Quo bias.

**Unit 3: Behavioural Corporate Finance. (12 Hours)** Financing Decisions: Financing Decisions of an Optimistic Manager, Financing Decisions of an Overconfident Manager, Trade-off Model: Incorporating Manager-Shareholder Conflicts, Trade-off Model: Incorporating Bondholder-Shareholder Conflicts. Capital Budgeting and Other Investment Decisions:

Effects of managerial overconfidence and optimism on the capital budgeting decisions, Factors Affecting the Impact of Managerial Biases. Dividend Policy Decisions: The Dividends Puzzle, Behavioral Biases as explanations for dividends, Theories of Investor Biases, Theories of Managerial Biases.

#### Unit 4: Investor Behavior

(12 Hours)

Individual Investor Trading: Rational Explanations, Behavioral Explanations; Aspects of Individual Investor Trading – Disposition Effect, Local Bias, Learning over Time; Implications of Individual Investor Trading – Asset Prices, Cost of Time. Individual Investor Portfolios: Biases and Diversification. Cognitive Abilities and Financial Decisions: Do Older Investors Make Better Investment Decisions? Cognitive Abilities and the Three Puzzles. Role of Culture in Finance: Impact of Culture on Firm and Investor Behavior.

#### **Essential/recommended Readings (latest editions of readings to be used)**

1. Baker, H. K., & Nofsinger, J. R. (Eds.). (2010). Behavioral finance: investors, corporations, and markets (Vol. 6). John Wiley & Sons Publication.
2. Shleifer, Andrei. "Inefficient Markets-An Introduction to Behavioural Finance". Oxford University Press.

#### **Suggestive Readings (latest editions of readings to be used)**

1. Thaler, Richard & Barberis, Nicholas. (2002) A Survey of Behavioral Finance, <http://dx.doi.org/10.2139/ssrn.327880>
2. Kahneman, Daniel & Tversky, Amos. (2000). "Choices, Values and Frames". Cambridge University Press

**Note:** Examination scheme and mode shall be as prescribed by the Examination Branch, University of Delhi, from time to time