Written Re-exam at the Department of Economics winter 2019-20

Behavioural Finance

Final Exam

07-02-2020

(2-hour closed book exam)

This exam question consists of 3 pages in total

Falling ill during the exam

If you fall ill during an examination at Peter Bangs Vej, you must:

- contact an invigilator who will show you how to register and submit a blank exam paper.
- leave the examination.
- contact your GP and submit a medical report to the Faculty of Social Sciences no later than five (5) days from the date of the exam.

Be careful not to cheat at exams!

You cheat at an exam, if during the exam, you:

- Make use of exam aids that are not allowed
- Communicate with or otherwise receive help from other people
- Copy other people's texts without making use of quotation marks and source referencing, so that it may appear to be your own text
- Use the ideas or thoughts of others without making use of source referencing, so it may appear to be your own idea or your thoughts
- Or if you otherwise violate the rules that apply to the exam

<u>Please answer all questions as concise and short as possible!</u>

<u>Good Luck!</u>

Question 1 – Anchoring

a) Please define the anchoring heuristic and how selective accessibility explains it.

b) Please briefly explain how anchoring might affect prices on the real estate market.

Question 2 – Decision under risk and uncertainty

In our financial decisions, we are often faced with risks and uncertainties.

a) Please explain the Ellsberg Paradox and how it relates to ambiguity aversion. Note, in your answer you should explain how Ambiguity Aversion is defined.

b) What is a possible psychological explanation for ambiguity aversion and how can the MaxMin preferences by Gilboa & Schmeidler (1989) explain ambiguity aversion.

Question 3 – The equity premium puzzle

a) What is myopic loss aversion and how can it explain the equity premium puzzle. Note, in your answer you should also define what the equity premium puzzle is.

b) In their paper entitled "Myopic Loss Aversion and the Equity Premium Puzzle" Bernatzi and Thaler (1995) analyze the equity premium puzzle with the help of myopic loss aversion. Also in the paper "Gneezy, Kapteyn and Potters (2003), Evaluation Periods and Asset Prices in a Market Experiment, Journal of Finance, 58(2), 821-837" myopic loss aversion is analyzed. Please explain and compare the analyses performed in these two papers. Furthermore, explain the results shown in the following graph (Note: the graph is taken from the paper Gneezy, Kapteyn and Potters (2003), Evaluation Periods and Asset Prices in a Market Experiment)

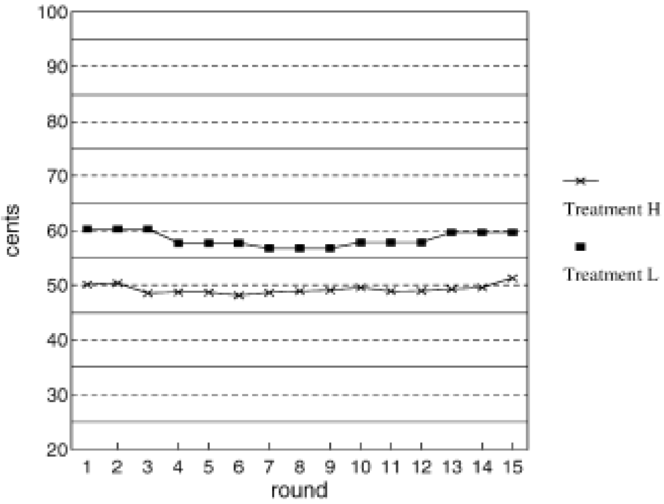

Figure 3. Average prices per round. For each round, asset prices are averaged first over the transactions in a session, then over the five sessions of each treatment.