Pacific-Basin Finance Journal
Volume 11, Issue 4, September 2003, Pages 429-437

Behavioral finance â˜†

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https://doi.org/10.1016/S0927-538X(03)00048-9

Abstract

This article provides a brief introduction to behavioral finance. Behavioral finance encompasses research that drops the traditional assumptions of expected utility maximization with rational investors in efficient markets. The two building blocks of behavioral finance are cognitive psychology (how people think) and the limits to arbitrage (when markets will be inefficient). The growth of behavioral finance research has been fueled by the inability of the traditional framework to explain many empirical patterns, including stock market bubbles in Japan, Taiwan, and the US.

Keywords

Behavioral finance; Arbitrage; Psychology; Market efficiency

JEL classification

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G14; D81

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â˜† A modified version of this paper was given as a keynote address at the July 2002 APFA/PACAP/FMA meetings in Tokyo.

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