

Pre-class survey 3: Investment decisions simulation

This survey is based on the experiment discussed in Zhang, Ting, Pinar O. Fletcher, Francesca Gino and Max H. Bazerman (2015). Reducing bounded ethicality: How to help individuals notice and avoid unethical behaviour. *Organizational Dynamics*, vol. 44, No. 4, pp. 310-317.

Role Description

Your role in this simulation is to be an investment advisor. As an investment adviser, your job entails managing funds and making investment recommendations for your clients. You currently manage a portfolio of \$10,000,000.

Imagine that a new client has come to you for your advice on an investment decision. Your client is a professional that has a solid income and has recently received a \$75,000 bonus, which he intends to put in a portfolio of investments for the next two years, when the returns will be cashed. Your client does not have any investments currently.

The client has sent you the following note: "I have recently received \$75,000, and would ideally like to invest in one of the four funds that I am considering. I am particularly interested in Fortitude Investments which has been performing very well and consistently above market. Which fund would you recommend?"

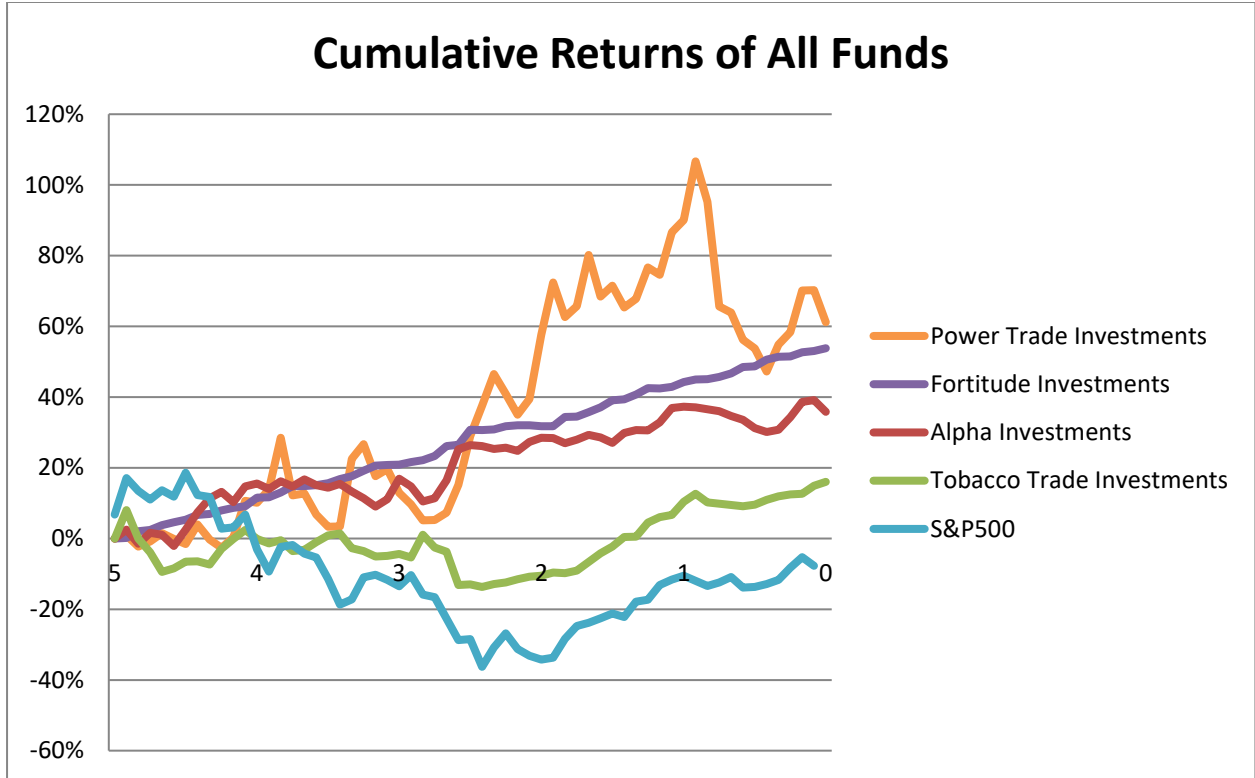
Fund Information

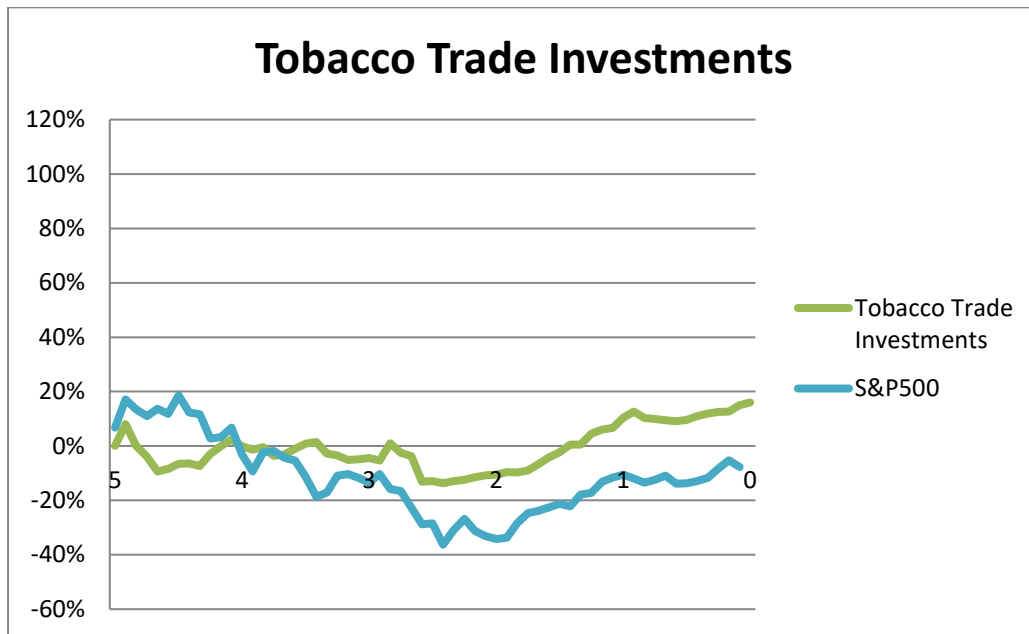
The four funds you are considering for your client are shown in the following graphs, with the first graph showing their cumulative returns. The data provided are real, although the provided fund names and dates are fictitious. The graphs are followed by a questionnaire you should complete before class.

Definition of Terms

- **S&P 500:** The Standard & Poor's 500 refers to an American stock market index based on the market capitalizations of 500 large companies.
- **Annual Return:** The percentage change in price of the fund over the course of the year. For example, if you invest \$10 in a company and that investment is worth \$15 a year from now your annual return would be 50% (i.e. $(15-10)/10$).
- **Volatility:** This is a measure of how much and how quickly the price of an investment changes within a given period of time, often used as a measure of risk.
- **Risk-Adjusted Return:** This is a measure that explains how much you would get beyond investing in the S&P 500 for the amount of risk that is associated with the fund. The greater a portfolio's risk-adjusted return, the better the fund in terms of the amount of returns you receive, factoring in the amount of risk that you are taking to get those excess returns.

$$\text{Risk adjusted return} = \frac{\text{Returns beyond S\&P 500}}{\text{Volatility}}$$





Risk-adjusted return*: 0.42

Five-year cumulative returns: 16.02%

Average monthly returns: 0.40%

Volatility: 2.99%

S&P 500 five-year cumulative returns: -7.69%

S&P 500 average monthly returns: -0.25%

S&P 500 volatility: 4.68%

*With S&P 500 as benchmark

Office location:

Our offices are located at:

Ten Corporate Street

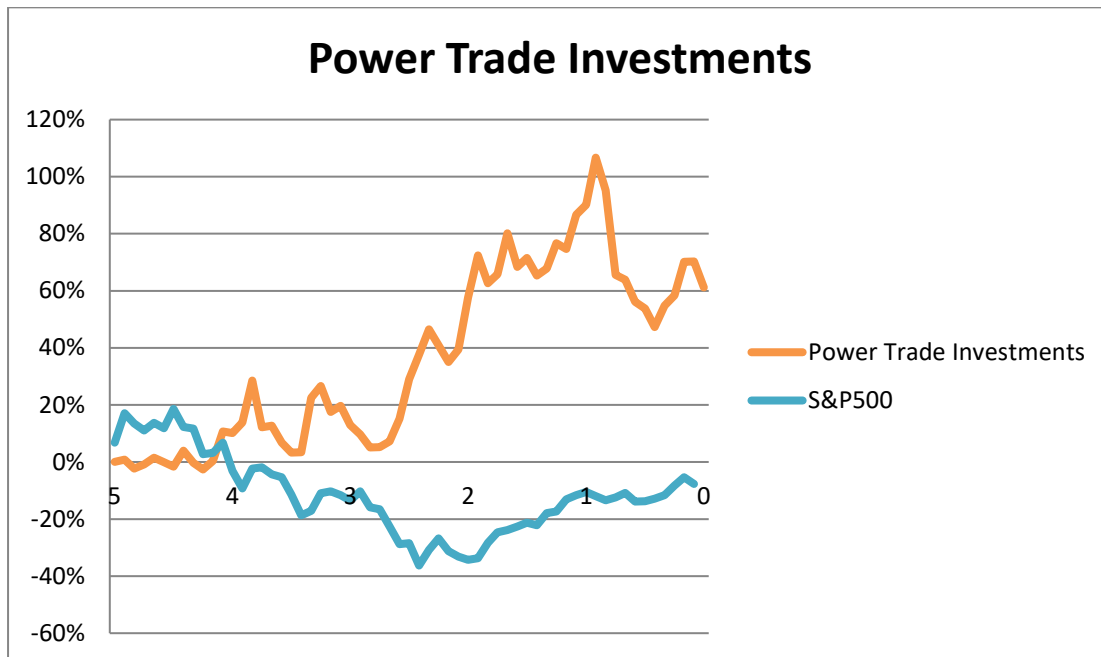
Rye, NY 10580

Mission statement: To earn a superior risk-adjusted return for our investors over the long-term by providing value-added products. By earning returns for our investors, we will be earning returns for all our stakeholders.

Investment strategy: We have initiated positions in companies which operate in fairly good sectors but have been sold down over the past year and are now trading at attractive valuations. The main sector is in the tobacco industry. As long as their cash-flow is positive, balance sheet is strong and dividends are paid, we are happy to be investors in such companies.

How do investors get into fund: Our investors typically contact hedge fund brokers.

Information on how Tobacco Investments is audited: Tobacco Trade Fund uses the services of DP Associates LLP. DP Associates is a well-respected auditing firm that has been auditing clients for the last 51 years—it has 48 clients across the U.S.



Risk-adjusted return: 0.46

Five-year cumulative returns: 61.20%

Average monthly returns: 0.93%

Volatility: 6.22%

S&P 500 five-year cumulative returns: -7.69%

S&P 500 average monthly returns: -0.25%

S&P 500 volatility: 4.68%

Office location:

1 New York Plaza, 54th Floor

New York, NY 10004

Mission statement: Our mission is to compete in every market in the world, combining insight and technology to profit and make the markets more efficient; to recruit the most capable people and train them to the highest standard; and to foster openness, communication and idea sharing.

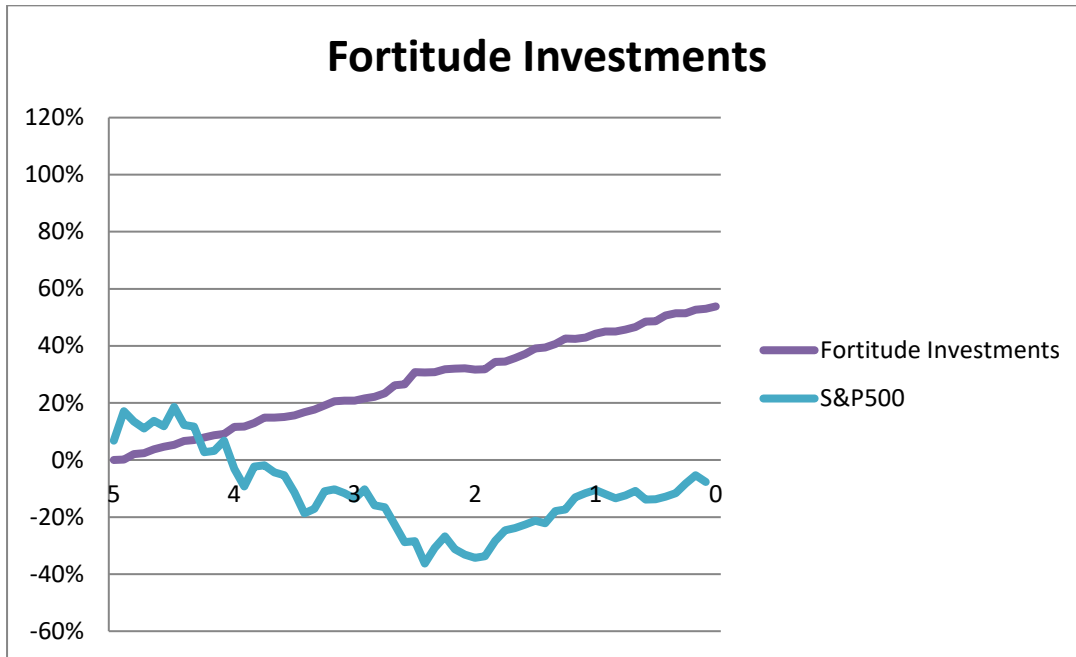
Investment strategy: Our trend-following portfolio consists of more than 200 funds in different market sectors. Markets are selected to represent a geographically balanced portfolio across different asset classes, with liquidity being the main focus. If the target exposure changes, open positions are reshuffled in order to keep trade risk constant.

How do investors get into funding:

Investors typically find us through hedge fund databases, and have their brokers contact our managers.

Information on how Power Trade Investments is audited:

Power Trade has used P&F Audit Company for auditing purposes. P&F Audit Company is a global auditing firm that has been serving 124 clients for the last 72 years and has 20 offices globally.



Risk-adjusted Return: 0.75

Five-year cumulative returns: 53.81%

Average monthly returns: 0.75%

Volatility: 0.71%

S&P 500 five-year cumulative returns: -7.69%

S&P 500 average monthly returns: -0.25%

S&P 500 volatility: 4.68%

Office location:

523 Park Avenue

New York, New York 10022

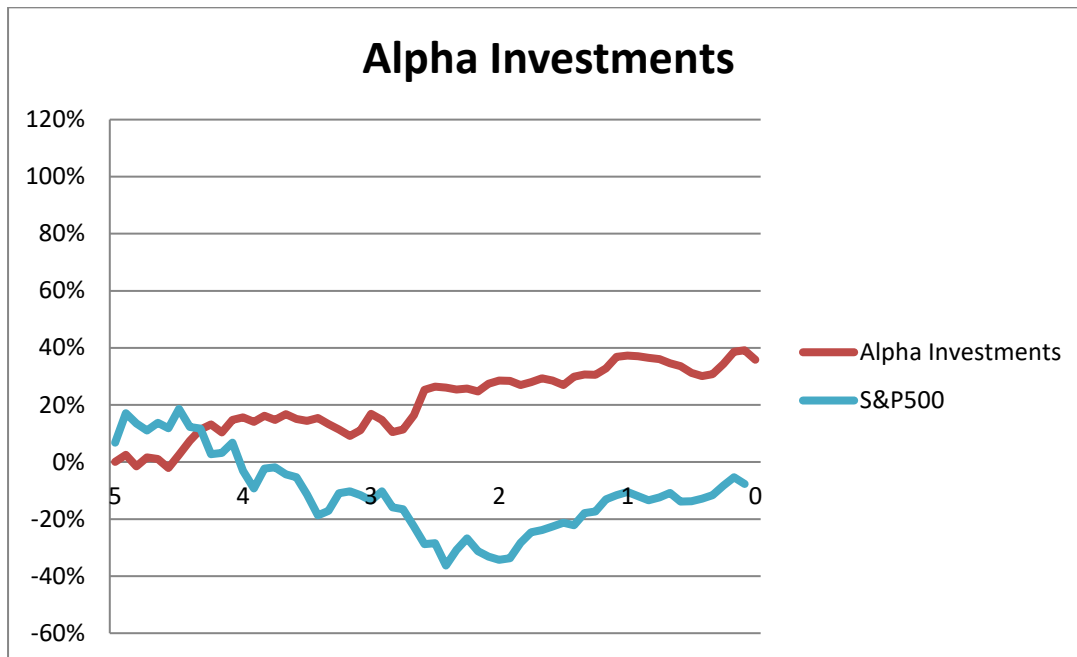
Mission statement: Our success is driven by three fundamental ideas: 1) Seek and hire the most brilliant and talented people we can find; 2) Reward those people based on merit; 3) Remain on the leading edge of innovation in investing.

Investment strategy: Because our investment strategy is private, we cannot disclose any information at this time.

How do investors get into funding: We are selective in our investors and make sure that these investments are in line with their individual strategies. As a result, typical investors we do not know cannot invest with us. However, as an adviser, we will open these investments to your clients, especially those who are interested in investing their money with us long-term.

Information on how Fortitude Investments is audited:

Fortitude uses SA & Associates, CPA for their auditing purposes. SA & Associates was established 15 years ago. The chief auditor was formerly a VP at Fortitude Investments.



Risk-adjusted return: 0.54

Five-year cumulative returns: 36.81%

Average monthly returns: 0.61%

Volatility: 2.37%

S&P 500 five-year cumulative returns: -7.69%

S&P 500 average monthly returns: -0.25%

S&P 500 volatility: 4.68%

Office location:

400 W Chicago Ave. Suite 734

Chicago, IL 60654

Mission statement: We seek to deliver superior investment performance for our clients and to develop a broad array of superior investment products.

Investment Strategy: We use strategies that hedge out most market risk by taking offsetting positions, often in different securities of the same issuer. For example, we find the optimal combination of bonds and equity to create stable, low risk investments.

How do investors get into funding: Our investors contact us via their hedge fund consultants or brokers.

Information on how Alpha Investments is audited: Alpha utilizes the auditing services of RK Partners CPA Co. RK Partners is a fast-growing auditing firm that began serving international clients 7 years ago and has since developed a client base of 12 firms in Europe and 30 firms in the US.

Questions

1. Which fund would you recommend to your client? (Circle one)

- Tobacco Trade Fund
- Power Trade Investments
- Fortitude Investments
- Alpha Investments

2. Please explain why you made this selection for your client.

3. Which fund would you select for your own portfolio? (Circle one)

- Tobacco Trade Fund
- Power Trade Investments
- Fortitude Investments
- Alpha Investments

4. Please explain why you chose this fund for yourself.

5. Please rate how suspicious you think each fund is [1= not at all; 7= extremely].

Tobacco Trade Fund	1	2	3	4	5	6	7
Power Trade Investments	1	2	3	4	5	6	7
Fortitude Investments	1	2	3	4	5	6	7
Alpha Investments	1	2	3	4	5	6	7

6. Please rate how unethical you think each of these funds is: [1 = not at all; 7 = extremely].

Tobacco Trade Fund	1	2	3	4	5	6	7
Power Trade Investments	1	2	3	4	5	6	7
Fortitude Investments	1	2	3	4	5	6	7
Alpha Investments	1	2	3	4	5	6	7

a. If Tobacco Trade Investments was suspicious or seemed unethical to you, please indicate why.

b. If Power Trade Investments was suspicious or seemed unethical to you, please indicate why.

c. If Fortitude Investments was suspicious or seemed unethical to you, please indicate why.



d. If Alpha Investments was suspicious or seemed unethical to you, please indicate why.
