

## Chapter 4

# Basics of Personal Financial Management



### Case Questions

1. B    2. C    3. B    4. D    5. B    6. D    7. B    8. C    9. C    10. D  
11. D    12. C    13. B    14. C    15. D

1. **B**  
Frank has already worked for not less than 60 days for the company as an employee. Also, he is not a domestic employee. He fulfils the corresponding requirements, so he is required to join the MPF scheme.  
A is incorrect. It is true that employees who are required to join an MPF scheme should be at least 18 years of age. However, whether Frank pays salaries tax or not is not a reason to explain why he is required to join the MPF scheme.  
C is incorrect. Whether Frank has a close relationship with the government or not is by no means a reason to explain why he is required to join the MPF scheme.  
D is incorrect. Whether Frank is a fresh graduate or not is not a reason to explain why he is not required to join the MPF scheme.
2. **C**  
(1) is correct. Employees can change the trustees and fund choices after reviewing fund performance.  
(2) is correct. All employees have the right to make extra contribution to the MPF scheme.  
(3) is incorrect. Employees are only allowed to take out their funds in the MPF scheme when they retire at the age of 65 or in some special situations such as early retirement at the age of 60, total incapacity, permanent departure from Hong Kong and so on. Frank cannot take out his funds in the MPF scheme when he quits his job if he does not fulfil the conditions mentioned above.
3. **B**  
(1) is correct. Enrolling himself in an MPF scheme is a responsibility of a self-employed person. Note that although Frank needs to do this, he does not need to pay the mandatory contribution as he earns less than \$7,100 per month (as of 1 November 2013).  
(2) is incorrect. Although it is true that a self-employed person has the responsibility to manage his own MPF account well, he can manage it with professional managers.  
(3) is correct. Joining an MPF scheme is like making an investment choice. People need to understand the scheme details before making the choice. It is a responsibility for him to do so.
4. **D**  
(1) is incorrect. Both employees and self-employed persons can change the allocation of their contributions in the MPF scheme.  
(2) is incorrect. Starting from 1 Nov 2012, the MPF Employee Choice Arrangement allows employees to transfer their accounts to other MPF schemes once a YEAR.  
(3) is incorrect. Employees do not necessarily receive a higher return of investment than self-employed persons do.

5. **B**

(1) is incorrect. The major financial need at the stage of young single is to create and accumulate wealth to prepare for later life stages. One should not use up all the money at hand for immediate consumption.

(2) is correct. Young singles should have good financial planning for later stages.

(3) is incorrect. Setting up inheritance should be an aim of financial planning near the stage of retirement.

6. **D**

The investment period of both Plan A and B is 1 year. Thus,

The expected effective rate of return of Plan A

$$= \left( \frac{\$420,000}{\$300,000} - 1 \right) \times 100\%$$

$$= 40\%$$

The expected effective rate of return of Plan B

$$= \left( \frac{\$417,720}{\$300,000} - 1 \right) \times 100\%$$

$$= 39.24\%$$

7. **B**

By formula,  $ERR = \left( 1 + \frac{NRR}{k} \right)^k - 1$

Where ERR: effective rate of return

NRR: nominal rate of return per annum

k : the number of periods compounded in one year

As the interest is compounded half-yearly,  $k = 2$ . Thus,

$$39.24\% = \left( 1 + \frac{y\%}{2} \right)^2 - 1$$

$$y = 36$$

8. **C**

The nominal rate of return per annum of Plan A = 40%

When the interest is compounded half-yearly,

the new effective rate of return =  $\left( 1 + \frac{40\%}{2} \right)^2 - 1 = 44\%$

Thus, the new anticipated future amount of Plan A

$$= \$300,000 \times (1 + 44\%)$$

$$= \$432,000$$

9. **C**  
 Although there are exceptions, the risk on debentures is usually low while that on stocks is usually high because of the fluctuations in stock prices.  
 A and B are incorrect.  
 The nominal rate of return per annum in Plan B is 36%.  
 When the interest is compounded quarterly,  
 The new anticipated future amount of Plan B  

$$= \$300,000 \times \left(1 + \frac{36\%}{4}\right)^4$$

$$= \$423,474 \text{ (correct to the nearest dollar)}$$

$$\neq 2 \times \$417,720$$
 Thus, A is incorrect.  
 The new anticipated interest return of Plan B  

$$= \$423,474 - \$300,000$$

$$= \$123,474$$

$$\neq 2 \times \$117,720$$
 Thus, B is incorrect.  
 D is incorrect. Personal credit record is needed when you borrow money from banks or apply for credit cards, but not when you invest in debentures.
10. **D**  
 (1) is incorrect. Lodging complaints against misleading managers is a right instead of a responsibility.  
 (2) is correct. As a responsible investor, William should fully understand the terms of a contract before signing it.  
 (3) is correct. It is William's responsibility to check and monitor his investment account regularly by checking the account statements and transaction documents.
11. **D**  
 (1) is correct. Usually, borrowers with a good personal credit record can get loans rather easily from financial institutions and banks.  
 (2) is correct. When issuing a loan to a person with a poor personal credit record, financial institutions will charge a higher interest rate in order to compensate for the risk. Conversely, the financial institutions will charge a person with a good personal credit record a lower interest rate.  
 (3) is correct. Maintaining a good personal credit record can improve one's credit worthiness.
12. **C**  
 (1) is correct. When the consumer chooses to prolong the repayment period, the periodic repayment amount is lowered.  
 (2) is incorrect. Customers have to follow a fixed repayment schedule which lacks repayment flexibility.  
 (3) is correct. Non-revolving credit means credit that is extended; the loans or debts incurred through the usage of such credit are repaid via fixed repayment schedules. Paying in instalments makes instalment loans a type of non-revolving credit by definition. Consumers can only draw a particular amount on a one-off basis under non-revolving credit.

13. **B**

(1) is correct. The depreciation of Japanese yen implies the appreciation of Hong Kong dollars against yen. As a result, Japanese goods become cheaper in terms of Hong Kong dollars, attracting more Hong Kong people to travel to Japan. This increases the sales revenue of *XYZ Tours*. The share price of *XYZ Tours* goes up as well due to the better money-making ability of the company.

(2) is incorrect. The rising oil price increases the prices of airline tickets. This increases the operation costs of *XYZ Tours* and has a negative impact on the tourism industry. The share price of *XYZ Tours* goes down as a result.

(3) is correct. Investors are more willing to buy stocks of *XYZ Tours* if it is willing to distribute more dividends. Thus, the share price rises.

14. **C**

Main Board listing companies need to fulfil more financial requirements such as the profit test requirement, so we can generally believe that *XYZ Tours* is less risky to be invested in.

A is incorrect. A Main Board listed company (*XYZ Tours*) does not necessarily earn more profits than a Growth Enterprise Market (GEM) listed company (*ABC Tours*).

B is incorrect. There is insufficient information to ascertain whether the trading record period of *XYZ Tours* is longer than that of *ABC Tours*. Although *XYZ Tours* must have a trading record of not less than three financial years to be listed on the Main Board, while it is two years for GEM listed companies, they are just the minimum requirements and *ABC Tours* can actually have a longer trading period than its counterpart.

D is incorrect. It is hard to ascertain whether a company is more profitable to be invested in than others. However, investing in GEM listed companies usually gives a higher expected risk and return than investing in the Main Board listed companies.

15. **D**

The Hang Seng Index is a measurement of the performance of the Hong Kong stock market. Thus, Alex can use it to evaluate and manage his investment portfolio.

A is incorrect. The Hang Seng Index is a measurement of the performance of the Hong Kong stock market instead of the property market.

B is incorrect. The share price of a listed company, no matter it is listed on the Main Board or the GEM, is not necessarily consistent with the Hang Seng Index. The Hang Seng Index is just a value-weighted index of its constituent companies.

C is incorrect. There are only 50 constituent companies in the Hang Seng Index but there are more than 1000 companies listed on the Main Board currently.