

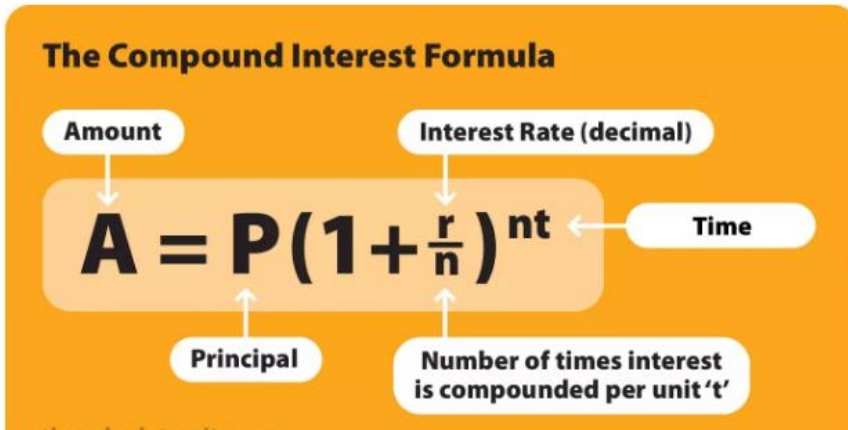
# BASICS OF PERSONAL FINANCIAL MANAGEMENT

## CHAPTER1—TIME VALUE OF MONEY

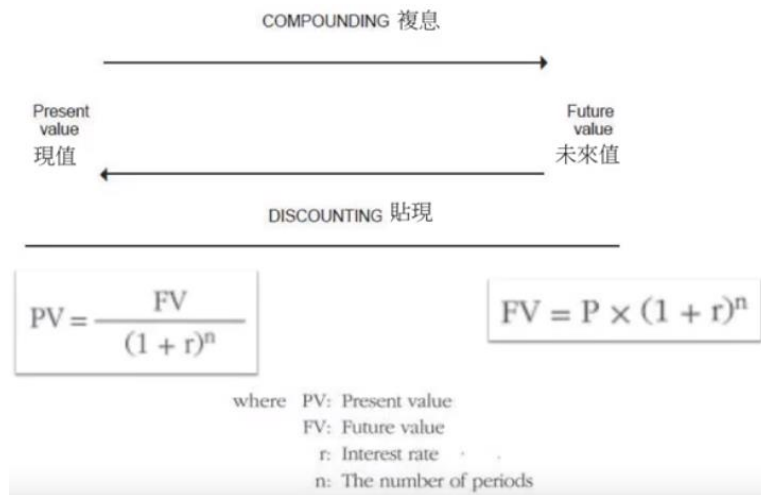
O Time Value of Money—a dollar received today is worth more than a dollar received in future.  
 (investment/deposits ↻ \$ grows over time ↻ □ interest)

### A. Basic Concepts

**1.Compounding**--accumulating value over time [=process of finding PV]



↻ compound interest: interest earned ↻ reinvest ↻ part of subsequent deposit ↻ make more profit



### Calculating the time value of money

- Future value (FV)  $FV = PV \times (1+r)^n$
- Present value (PV)  $PV = \frac{FV}{(1+r)^n}$
- Net present value (NPV)  $NPV = \frac{FV_1}{(1+r)^1} + \frac{FV_2}{(1+r)^2} \dots - I$  if  $NPV \geq 0 \rightarrow$  invest
- Effective (actual) rate of return(ERR)  $ERR(\%) = (1 + \frac{r}{k})^k - 1 \rightarrow$  invest in higher ERR  
 → more frequently interest is compounded, the larger the sum received at the end

**2.Discounting**-process of finding PV[reverse of compounding]

☞ know how much \$ needed to grow into certain amount in future

### Calculating the Future Value of an Investment


$$FV_1 = PV(1 + I)^n$$

The future value at the end of one year

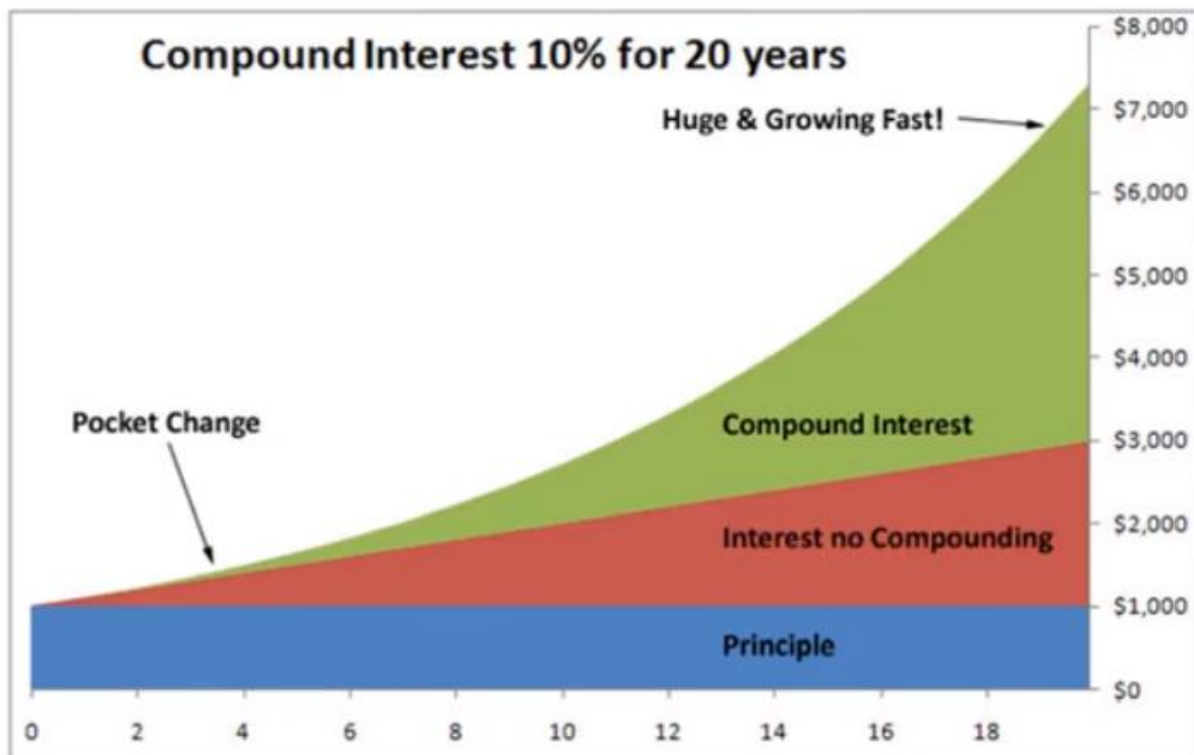
Present value

Interest rate

Number of compounding periods



the balance



**B. Calculations**

1.Future Value (FV) & Present Value (PV)

(a).FV--value at end of time period from a sum of money today= $PV \times (1+I)^n$


(b).PV--current value of a future sum of money[=time weighted cost] =  $FV/(1+i)^n$


☞ i=interest rate, n=no. of time periods

☞ find n: minimum no. Of years can't exceed required amount

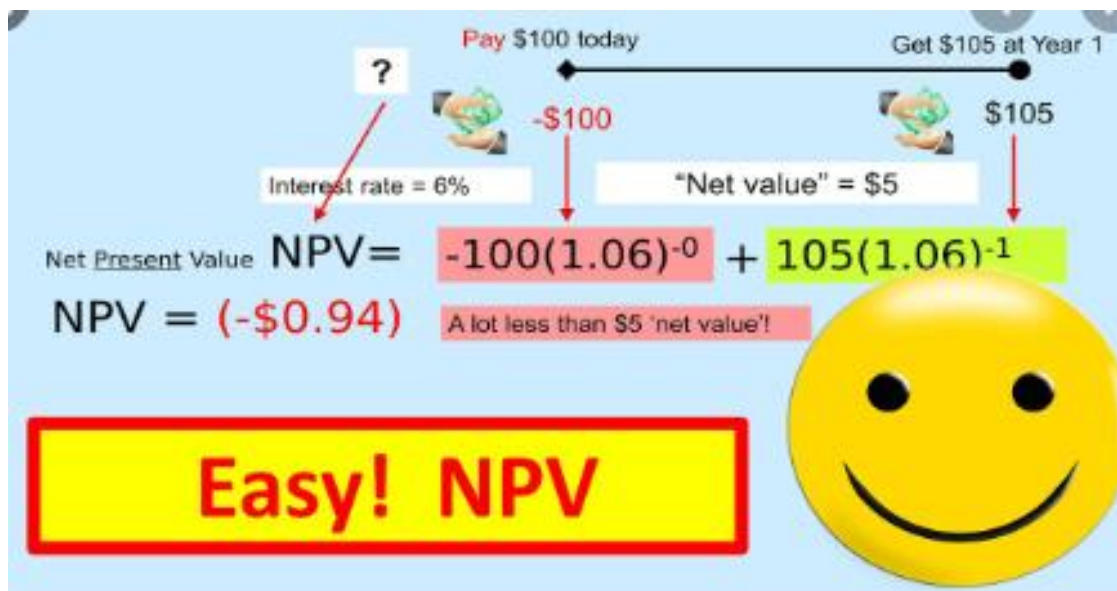
☞ cost of capital—rate of returned that can be earned next best alternative

## Time Value of Money Formula

**Future Value of Money** =  $PV \times \left(1 + \frac{i}{n}\right)^{(n \times t)}$  

**Present Value of Money** =  $\frac{FV}{\left(1 + \frac{i}{n}\right)^{(n \times t)}}$  

2. Net Present Value (NPV) =




Pay \$100 today      Get \$105 at Year 1

Interest rate = 6%

Net Present Value  $NPV = -100(1.06)^0 + 105(1.06)^{-1}$

$NPV = (-\$0.94)$       "Net value" = \$5

A lot less than \$5 'net value'!

**Easy! NPV** 

Total PV of future annual net cash inflows + PV of machine's market value at end of investment –initial cost [/outlay]

☞ ≥0: invest (financial benefits outweigh/equal costs)

☞ <0 :x invest(loss)

☞ PV ▲ /FV ▲ /interest rate ▼ /initial cost ▼ :NPV ▲

# Net Present Value Formula



$$NPV = \sum \frac{CF_n}{(1 + i)^n} - \text{Initial Investment}$$



### 3. Rate of Return

- (a) **Nominal**—interest rate stated on financial instruments  
may not reflect the actual return on an investment because the return of investment depends on how the effect of compounding per year. (how frequently the interest is compounded)
- (b) **Effective**—reflects effect of compounding frequency on actual investment return  
[=Effective Annual Rate/ Effective Interest Rate/ Annual Percentage Rate]

### Effective Rate of Interest Formula

- Solving the last equation for  $R$  we obtain the formula for computing the effective rate of interest:

$$r_{eff} = \left(1 + \frac{r}{m}\right)^m - 1$$

where

- $r_{eff}$  = Effective rate of interest
- $r$  = Nominal interest rate per year
- $m$  = Number of conversion periods per year

What is the better rate of return, 7% compounded quarterly or 7.2 % compounded semianually?

$$i_{eff} = \left(1 + \frac{r}{k}\right)^k - 1$$

- ☞ I investment decisions (more frequent = higher actual return)
- ☞  $ERR = (1 + i/m)^n - 1$ .
- ☞  $m$  = no. of times compounded per year,  $n = m \times \text{total years}$

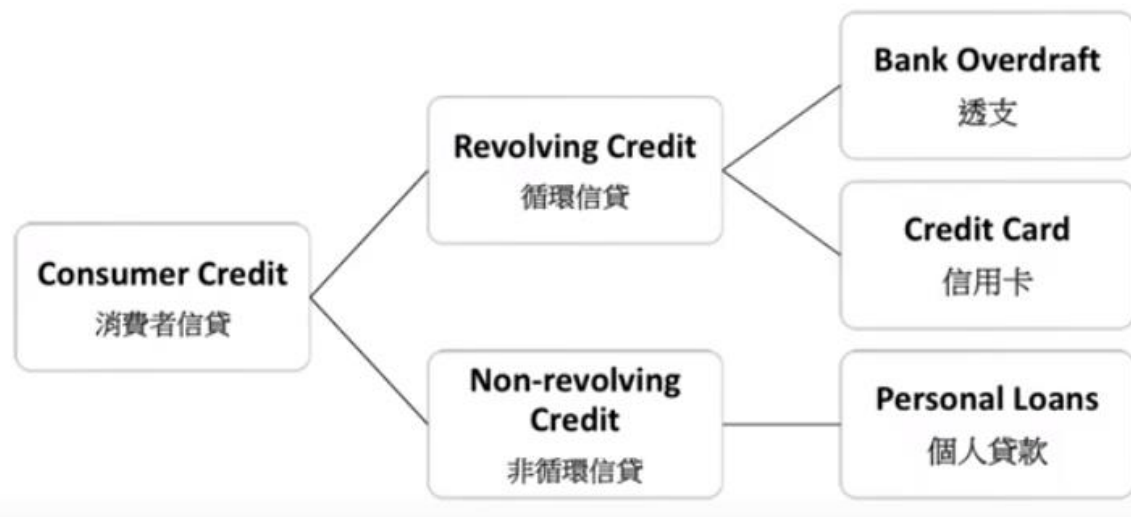
## Chapter 2 – Consumer Credit

- **Consumer Credit**
- non-mortgage personal loans for purchasing consumer goods and services, usually unsecured.  
→ Credit-any arrangement for obtaining money , good or services now but paying for them later



### Consumer Credit 消費者信貸

- **Loans** obtained by consumers for the consumption of goods and services



**A. Types**

	Credit Cards	Overdrafts	Personal Loans	
			Line of Credit	Instalment loans
<b>Definition</b>	Cardholders purchase goods or services on credit	Bank customers withdraw more than deposited	Borrow & repay pre-approved amount anytime	Repay by fixed no. of payment
<b>Repayment</b>	Pre-approved limit			Principal & interest
<b>Others</b>	Monthly statements (transaction list)	/	(=revolving loans) Credit limit restored after repayment	(=instalment credit)
<b>General Adv.</b>	Safe & convenient: buy expensive item + no need carry much cash + risk or loss/theft ↓			
<b>Interest Rate</b>	Higher (Disadv.) Unpaid balance	daily	Lower (Adv.)	
<b>Repayment Flexibility</b>	<input type="checkbox"/> (Adv.) <ul style="list-style-type: none"> <li>Only monthly minimum</li> <li>Full repayment: no fixed deadline/ no. of payment</li> </ul>		<input type="checkbox"/> (Disadv.) Fixed no. of payments → Trouble / bankruptcy	

<b>Convenience</b>	<input type="checkbox"/> (Adv.) <b>Sign sales voucher</b> ->No need automatic teller machine/ delay purchase	<input type="checkbox"/> Adv. Prevent dishonored cheque		/
	<input type="checkbox"/> (Adv) Worldwide->ignore currencies	Anytime & no need re-apply once approved		
	<input type="checkbox"/> (Adv) Rejected by some shops (small/ low-value goods)			
<b>Debt Trap (abuse)</b>	<input type="checkbox"/> (Disadv)			<input type="checkbox"/> (Adv)
	Lack self-discipline → Trouble/ bankruptcy	/		Must plan
<b>Liquidity</b>	/	<input type="checkbox"/> (Adv): Short-term		/





Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Convenient and safe</li> <li>• Worldwide acceptance</li> <li>• Repayment flexibility</li> </ul>	<ul style="list-style-type: none"> <li>• High interest cost</li> <li>• Risk of credit card abuse</li> <li>• Credit rating damaged</li> </ul>

**信用卡利息比較** 資料來源：消委會

發卡機構	未還付最低還款/ 拖欠還款實際年利率	現金透支 實際年利率	被盜 實際年利率
富 邦	47.09%	33.26% 起	13.80% 起
美國運通	42.58%	34.00%	31.89%
花旗	42.58%	33.61%	32.00%
中信銀行國際	42.58%*	32.95% 起*	29.84% 起*
中國建設(亞洲)	38.48至42.58%*	31.89%*	30.61%*
永 亨	42.58%	21.83%	20.51%
星 展	37.27至42.16%	32.74至47.49%	31.37至36.07%
豐 明	40.95%	28.09至36.09%	16.39至33.19%
大 新	40.95%	28.09至36.09%	9.89至33.19%
東 亞	39.83%*	36.35%*	34.00%
上海商業	37.6%*	31.97% 起*	26.82% 起*
恒 生	35.25% 起	34.2% 起	30.29% 起
大 眾	34.50%	36.79%	34.50%
創 興	21.7至34.49%	22.98至36.79%	21.70至34.49%
永 隆	34.11%	35.51%	34.11%
中國工商(亞洲)	16.08至31.89%*	21.16至36.76%*	16.08至31.89%*
滙 豐	31.86%	33.07%	31.86%
交 通	26.82%	最高36.76%	最高26.82%
安信信貸	8.41% 起	20.62% 起	8.41% 起
渣 打	按現行財務費及透支 現金利率，附加每日 0.014%至0.0165%	34.70%	31.70%
中銀香港	按個別客戶而定	34.11%	32.40%

\*未計算手續費及罰息；|紅色|為該項目最高息率

銀行手續審批容易  
 80後卡奴清債需10年



76,267

**80後**

收入	平均收入
支出	還卡數 交租(若有) 高消費項目 固定開支(強積金、 其他開支(如家用、

民簽卡習慣

【有借有還】  
 魏先生：「最近銀行貸款利率太高，還唔起，所以...」

【唔會買樓】  
 區小姐：「信用卡還款...」

【卡數月月清】  
 王小姐：「習慣有幾多...」

**80後**

Jackey (C)

- 擁有第一張信用卡
- 高峯期信用卡數量
- 初期卡數欠款
- 6年間被凍或透支總額
- 6年間還款總額
- 6年間利息佔還款總額
- 最後仍未清還卡數總額
- 高峯期每月最低還款

Source: <http://hk.apple.nextmedia>

**B. Factors to Consider for Choice of Consumer Credit**

- a) **Purchase price:** repayment period, amount & ability  
 → Credit card (cheaper items) vs instalment loan (more expensive items)
- b) **Total costs of different plans:** different calculations & presentation of interest rates-> compare
- c) **Terms of loans:** late charges, restrictions on early payments, other penalties



## Bank Overdraft 透支

- Withdraw more funds than the amount in the bank account within agreed credit limit
- E.g. a cheque written from the current with insufficient fund
- The following fees may be charged:



- overdraft handling fees
  - daily overdraft interest
- Purposes
    - Prevent cheque being dishonoured (拒付)
    - Provide a short-term liquidity

## Bank Overdraft 透支

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Prevent a cheque from being dishonored</li> <li>• Provide short-term liquidity</li> <li>• Repayment flexibility</li> </ul>	<ul style="list-style-type: none"> <li>• High interest rate</li> <li>• Can be a trap for creating used improperly</li> </ul>

## Personal Loans 個人貸款

- Instalment loan:  
a fixed payment schedule of both principal and interest

- Examples

- Personal loan
- Car loan
- Tax loan
- Mortgage loan



## Personal Loans 個人貸款

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Fixed repayment schedule</li> <li>• Lower periodic repayment</li> <li>• Easy and fast to obtain</li> </ul>	<ul style="list-style-type: none"> <li>• Fixed terms of instalment loan</li> <li>• Fixed loan interest rate may be higher than market interest rate</li> </ul>

## Personal Credit Record 個人信貸紀錄

- Credit report is a record of credit history that lenders use to determine a borrower's **creditworthiness** (信譽).

**A credit report may include**



**Personal information**

Name, ID number, date of birth, addresses and telephone numbers



**Credit activities**

Credit usage and repayment history



**Public records**

Litigation relating to recovery of debt, bankruptcy and insolvency petitions



**Enquiry records**

Members' reviews within the last two years



**Credit score**

A numerical snapshot of your credit report



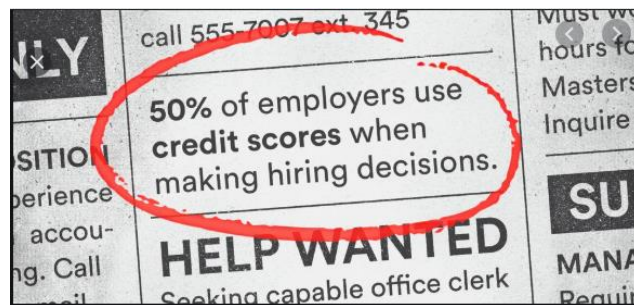
## C. Personal Credit Record-detailed report of individual's credit history

→ Credit Score-numerical value representing individual's creditworthiness

- **Lender: loan-approval decisions**
- **Individuals: ensure accuracy & avoid identity theft/ fraud**

A credit record (credit report) provides information on an individual's credit and repayment history, and bankruptcy → assess one's creditworthiness (*likeliness of repaying a loan*)

- *Credit applicants* with good credit records can find it easier to borrow money from lenders, and even at lower interest rates
- 



### I) Factors Affecting Record

- Repayment history:** pattern of on-time payments
- Credit history:** pattern of successful applications & usage
- Outstanding balance:** amount of debt
- Past delinquency:** amount & frequency of overdue loan
- Bankruptcy record**

#### Factors affecting credit worthiness



**Types of consumer credit**

**1. Revolving loans (Line of credit)**

- allows consumers to borrow and repay money anytime up to a pre-approved amount(limit)

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>- Convenient: do not need to apply for a new loan every time.</li> <li>- Greater flexibility in repaying loan</li> </ul>	<ul style="list-style-type: none"> <li>- a trap for creating debt slowly if used improperly.</li> </ul>

**Example: Credit card and Bank overdraft**

**Credit card**

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>- Convenience: no need carry large sums of cash around, online payment</li> <li>- Safety: no need carry large amount of cash → reduce the risk of robbery</li> <li>- Worldwide acceptance: no need to carry different currencies when travel overseas</li> <li>- Repayment flexibility: no need repay the balance in full as long as he settles the monthly minimum payments on time.</li> </ul>	<ul style="list-style-type: none"> <li>- High interest rate: If did not repay full before due, high interest charges.</li> <li>- Risk of credit card abuse: over-borrowing</li> <li>- Rejected by certain shops</li> </ul>

**Overdraft : withdraw more money than deposit in their bank accounts**

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>- Prevent a cheque from being dishonoured</li> <li>- Provide short-term liquidity</li> <li>- No fixed deadline or number of payments to repay the loan in full</li> </ul>	<ul style="list-style-type: none"> <li>- Interest charges are relatively high</li> <li>- a trap for over-borrowing</li> </ul>

**2. Instalment loans (Instalment credit)**

- loans with a periodic repayment for both the loan principal and the interest (no need repay in a lump sum), non-revolving

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>- Fixed repayment schedule</li> <li>- Lower periodic repayment amount</li> <li>- Easy and fast to obtain</li> </ul>	<ul style="list-style-type: none"> <li>- Fixed rate</li> <li>- Fixed terms</li> </ul>

**How to choose among different types of consumer credit**

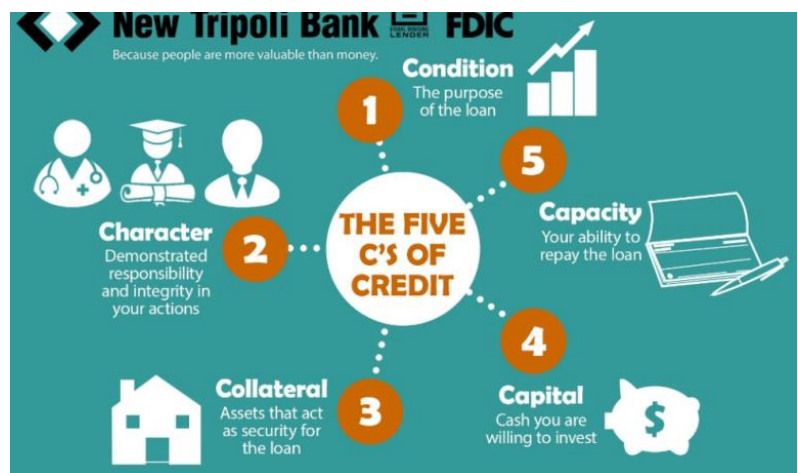
- The price of the item: small purchases → credit card; Expensive items → instalment loan
- The total costs of different plans: lower total interest payments
- The terms of the loans: restrictions on early repayment, charges and penalties r



## II) Maintaining Good Record

→ Risk of default ↓ --> obtain credit more easily with lower interest rates

- a) Consumption plan: affordability--> guidelines
- b) Regular review on spending habits: monthly spending--> don't overspend unnecessarily
- c) Discipline for convenience-->Not for unaffordable consumption
- d) Avoid sudden increase in credit card applications: lenders may suspect financial trouble
- e) Consider repayment ability when applying: not for gifts
- f) On-time payment of bills: no matter what reason (e.g. busy, loss of bill, careless)



### Major factors affecting individual's credit record:

- repayment history, credit history, outstanding debt, past delinquency and record of bankruptcy

### Maintain a good credit record, an individual should:

- (d) Plan for consumption: Understand how much they can afford to consume
- (e) Review spending habits regularly: distinguish between necessities and wants
- (f) Use consumer credit with discipline: only buy affordable items
- (g) Avoid a sudden increase in credit card applications.
- (h) Consider repayment ability when applying for loans
- (i) Repay on time.

## Chapter 3 – Financial Planning & investments

### A. Risk & Returns

- Return – ration of money gained or lost on investment relative to money invested
  - Positive return (gain) : selling price > purchase price
- Risk – uncertainty of an outcome (mostly: perception & feeling)
  - Risk averse – choose the one with lowest risk among investments with similar expected returns
  - Types : firm-specific (☒diversified & eliminated) vs market (overall economic / political changes)

#### I. Risk – return Trade-off-investor has to bear greater risks for higher returns

- High risk, high returns: compensates for risk --> attractive
- High risk, huge losses: not necessary to have return
- No risk, no return: must take calculated & acceptable risks



#### II. Risk Tolerance Level – indicator of level of investment risk an investor is willing to assume

- Ability to face uncertain outcome --> subjective & unique --> may change in different life stages
- Guaranteed return: for highly risk averse investor --> still have little risk

#### III. Common Financial Products

- Bank deposits: amount won't ↓ (if no bankruptcy)
  - Lowest risk-return trade-off
    - a) Saving deposit: withdraw anytime --> very low interest
    - b) Term deposit (time/fixed): can't withdraw until saving term --> higher interest
- Bonds-interest-bearing long-term debts issued by government and companies
  - Fixed % of return --> received principal on maturity date --> guaranteed (if no bankruptcy)
  - Medium risk-return trade-off (corporate bonds > government bonds)
- Stock (share) - holders have part of ownership of limited companies
  - Dividends – usually distributed when limited company earns profit (not a must)
  - Capital gains – difference between purchase price and selling price of investment
  - Highest risk-return trade-off : stock price ↑ / ↓ --> uncertain (common stock > preferred stocks)

## IV. Risk Diversification- strategy of reducing risk by investing in uncorrelated financial products

→ e.g. Different countries/ industries → prices won't move at same time → overall risk ↓

### Risk-return relationships of common financial products

Asset class/ investment vehicle	Product	Risk
<b>Bank deposit</b> (earn interest)	Term Deposit Saving Deposit	The lowest
<b>Bonds</b> interest-bearing long-term debts (earn coupon and premium from price appreciation)	Government bonds	Very low
	Corporate bonds	Low
<b>Stocks/ shares</b> (earn dividend and premium from price appreciation)	Preferred stocks/ Preference shares	High
	Common stocks/ ordinary shares	Higher

### **Risk tolerance**

- It refers to an individual's ability to face an uncertain outcome.
- Risk tolerance level decreases as the financial burden increases/ income decreases.

Investor's risk tolerance level		Action
Low ↓ High	Highly risk averse (Conservative investor)	Only invests in financial products with a very low level of risk, such as those with a guaranteed return
	Does not mind taking an acceptable level of risk (Moderate investor)	May consider buying low-risk financial products
	Willing to accept a high level of risk (Aggressive investor, risk-taker)	May invest in high-risk financial products

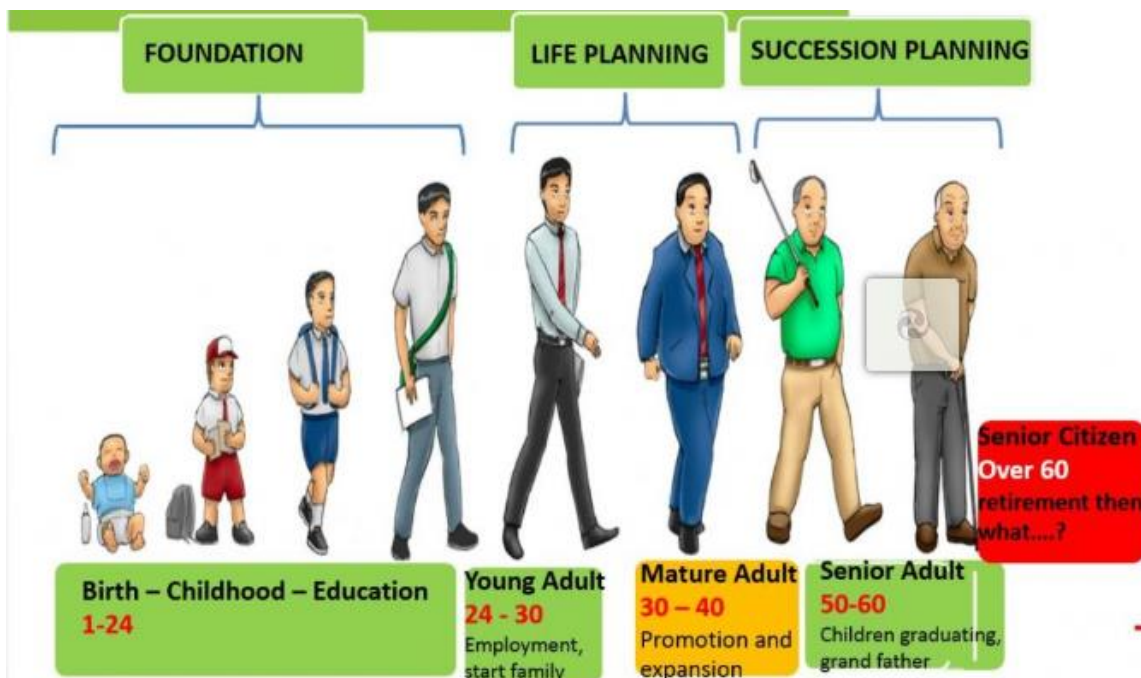
**B. Life Cycle** → how individuals manage their finance and wealth

**I. Personal Financial Planning** - evaluating individual’s financial needs in all aspects to achieve Financial goals

- Consumption, taxation, insurance, investment, retirement, estate (arrangement of assets after death)
- Importance
  - (a) Achieve financial goals : workable plan
  - (b) Avoid financial mistakes (e.g. overspending / misusing consumer credit )
  - (c) Maintain living standard : prevent decline in life quality under low income levels
- Steps : needs > goals > data > analyse > plan > implement > monitor & adjust

**Financial needs at different life stages in a life cycle**

Life stage	Financial needs	
Young single	<ul style="list-style-type: none"> <li>• Objective: Create and accumulate wealth</li> <li>• Saving for marriage, further education</li> <li>• Paying credit card debt, salaries tax</li> </ul>	<ul style="list-style-type: none"> <li>• Insurance</li> <li>• Repaying Student loan</li> </ul>
Couple	<ul style="list-style-type: none"> <li>• Preparing family (home purchase, raising child)</li> </ul>	<ul style="list-style-type: none"> <li>• Insurance</li> </ul>
Early family (newborn baby)	<ul style="list-style-type: none"> <li>• Family expense</li> <li>• Save for major purchases and retirement</li> </ul>	<ul style="list-style-type: none"> <li>• Children’s expense (education)</li> </ul>
Late family (kids=teenager)	<ul style="list-style-type: none"> <li>• Save for their children’s university education</li> </ul>	<ul style="list-style-type: none"> <li>• Save for medical expenses and retirement</li> </ul>
Pre-retirement	<ul style="list-style-type: none"> <li>• Save for retirement and</li> </ul>	<ul style="list-style-type: none"> <li>• medical expenses</li> </ul>
Retirement	<ul style="list-style-type: none"> <li>• Estate planning (expenses on funeral arrangement)</li> <li>• Meeting contingencies (urgent medical expense)</li> </ul>	<ul style="list-style-type: none"> <li>• Paying daily expenses to maintain desired lifestyle (food, transport, leisure, entertainment, vacation)</li> </ul>



**II. Life stage ( exclude : childhood )**

↳ variables : number / length of stages & needs / priorities / objectives at different stages



**(a) Young single**

- creation & accumulation
- financial burden of. Supporting family : insurance ( e.g. death , disability )
- saving for flat / retirement

**(b) Just Married**

- husband + wife ( employed ): more money > saving for retirement & planning for investments
- only 1 works : insurance > protect earning ability ( e.g. death , disability )

**(c) Married with Young Children**

- great financial burden : insurance
- income : reserved for educational expenses
- saving for major purchases / retirement

**(d) Married with Older Children**

- middle career stage : higher income > surplus funds  
>repaying loans , saving for university , paying for leisure activities , preparing for retirement

**(e) Pre-retirement**

- children : financially independent > need for insurance ↓
- 1<sup>st</sup> priority : saving for retirement

**(f) Retirement**

- desired lifestyle
- medical expenses : sell assets if shortage
- estate planning : effective distribution wealth with minimum taxation

C. Rights & Responsibility ( individual financial investors : protect interests & avoid unnecessary losses )

## I. Rights

- information : licence status & fees of service provides
- clarification : rational behind recommendations & alternatives
- transaction ( before signing ) : documents & statements
- clear instructions : code / name of product , purchase / selling price , quantity
- others : allowed to trade on own accounts



## II. Responsibilities

- Understanding ( before signing): feature, risk, return& contract terms
- Monitoring (investment accounts): documents& statements
- Clear instructions: code/ name of product, purchase /selling price, quality
- Others: not allowed to trade on own accounts

D. Mandatory Provident Fund System ( MPF ) — compulsory employment-based retirement protection system > since Dec 2000

## I.Features

- all employees & self-employed persons aged 18-64 : employers for > 60 continuous days
- employers must enrol employees in scheme
- gradual savings in long-term investment plans at appropriate risk level
- pooling of contributions : many employer & employees
- management : professional fund managers
- risk diversification



強制性公積金計劃管理局  
MANDATORY PROVIDENT FUND  
SCHEMES AUTHORITY

## II.Rights ( employee )

- choice of funds : under scheme chosen by employers
- own mandatory contributions & return : transfer to any “ MPF trustee and scheme ”  
→ Once per year only
- withdraw accrued benefit : lump sum at age of 65
- voluntary contributions

## III. Responsibilities(employee)

- **mandatory contributions** : 5% of monthly relevant income > maximum \$30000
- **monthly relevant income** < \$7100 : no need contribute ( employer still need )
- **choice of funds** : risk tolerance level
- **bear risks & outcomes**

Mandatory Provident Fund (MPF) System

- a compulsory **employment**-based retirement protection system.
- to help people save for retirement through long-term investment plans at an appropriate risk level

**Features of the MPF System**

- People who are required to join include:

- ◆ All employees and self-employed persons (except self-employed hawker, domestic helper, oversea worker in HK for less than 13 months)
  - ◆ aged 18 to below 65
  - ◆ monthly income ≥ HK\$7,100
  - ◆ been employed for a continuous period of not less than 60 days
- Mandatory contributions (5% of the employee’s salary) are made by both the employer and the employee to an MPF scheme.

Monthly Relevant Income	Mandatory Contributions	
	Employer Portion	Employee Portion
Less than \$7,100	Relevant income x 5%	No contributions required
\$7,100 to \$30,000	Relevant income x 5%	Relevant income x 5%
More than \$30,000	\$1,500	\$1,500

**Rights and responsibilities of employees and self-employed persons**

Rights	Responsibilities
<ol style="list-style-type: none"> <li>1. Choose MPF funds under the MPF scheme chosen by employers</li> <li>2. Transfer the employee’s portion of mandatory contributions and to any MPF trustee and scheme once every calendar year (Employee Choice Arrangement)</li> <li>3. Make voluntary contributions to the MPF scheme</li> <li>4. Withdraw the accrued benefits at age 65 (or early retirement at 60, permanent departure from HK, total incapacity, death) (small amount if no contribution for 12 months)</li> </ol>	<ol style="list-style-type: none"> <li>1. Make mandatory contribution</li> <li>2. Manage MPF accounts (Bear the investment risk and outcome)</li> <li>3. <i>(for self-employed) report income and update information</i></li> </ol>

**Rights and responsibilities of individual investors & consumers of financial services**

Rights	Responsibilities
<ol style="list-style-type: none"> <li>1. Right to be informed: timely and accurate</li> <li>2. Responsible investment management</li> <li>3. - Right to ask for rationale behind an investment recommendation made by a broker or bank</li> <li>4. Right to file a complaint (to HKMA)</li> </ol>	<ol style="list-style-type: none"> <li>1. Study information</li> <li>2. Consider the risk and return</li> <li>3. Understand the terms of a contract before signing it</li> <li>4. Monitor activities on own account by checking account statements, transaction documents</li> </ol>

**Basics of Personal Financial Management Chapter 4 – Investment of Stock Trading**

- Securities : legal documents showing either
  - a) holder’s ownership in company ( stocks )
  - b) right to buy stock at specified prices ( warrants )
  - c) loan to company / government (bonds )

A. Stocks ( /shares ) – securities that holders have part of ownership of limited companies

I.types	Common stocks ( /ordinary shares )	Preferred stocks ( /preference shares )
Voting right	✓annual general meeting g. elect board of directors for operations )	x
dividends	✓if declared	fixed & guaranteed
Priority (claims: Assets) (LIQUIDATION)	Lowers	Higher

II. Common Stock Terms ( HK )

- **blue chips** : largest & best-known non-foreign firms with strong financial positions  
→ Constituent stocks of Hong Kong Index ( e.g. HSBC , China Light and Power )
- **second liners** : financially weaker firms than those of blue chips
- **third liners** : financially weaker firms than those of second liners
- **H-shares** : firms listed in HK but incorporated in Mainland China ( e.g.China Telecom )
- **red chips** : firms substantially owned by Mainland firms ( >35% )  
→ Listed in HK , incorporated outside butt singly operated in Mainland China ( e.g. Lenovo )

III.Factors Affecting Stock Prices

(a) **Macro-economic ( globalisation )**

- performance↑: investment & consumption↑> profits↑> stock prices↑
- political stability↑: confidence↑> stock prices↑
- interest rates↑: costs↑> profits↓> stock prices↓

(b) **Industrial** : prospects↑> confidence↑> stock prices↑

(c) **Firm-specific** ( e.g. earning , dividends , risk , news )

- performance↑: profits & prospects↑> stock prices↑
- dividends↑: stockholders' gains↑> attractiveness↑> stock prices↑

(d) **Other** : Speculation – trading activities based on rumours

- take necessary risks if ✓potential profits ( e.g. positive rumours ) : stock prices↑
- unexpected bad news : irritation reactions > panic sales ( excessive ) > stock prices↓

**Factors affecting stock prices**

**External factors**

Economic conditions	<ul style="list-style-type: none"> <li>• If economy performs (expansion/growth/peak/bloom) well → increase in investment and consumption → higher profits → increase in stock prices</li> <li>• Poor economy: contraction/trough/recession/depression</li> </ul>
Industrial prospect	<ul style="list-style-type: none"> <li>• good industrial prospects → increase in stock prices</li> </ul>
Interest rates	<ul style="list-style-type: none"> <li>• Higher interest rate → higher cost of investment (borrowing) → decrease in amount if investment → decrease in share prices</li> </ul>
Government policy	<ul style="list-style-type: none"> <li>• Policy facilitate industry → increase in share price</li> <li>• Affect interest rate as well</li> </ul>
Speculation	<ul style="list-style-type: none"> <li>• unexpected bad news/ rumors → massive panic sales → excessive speculative activities → push down stock price</li> </ul>
Political situations	<ul style="list-style-type: none"> <li>• Politically unstable → investors lose confidence→ decrease in stock prices</li> </ul>



**Internal Factor**

Company performance	company performs well → higher profit → good prospects → increase stock price
Dividend policy	company pays more dividends → stockholders earn more → more attractive investment → increase in stock price

**B. Stock Trading Platforms : Exchanges –places where securities are listed and traded**

**The Hong Kong Exchanges and Clearing Limited (HKEx)** is the operator and frontline regulator of the securities and derivatives market in Hong Kong.

Traditional : physical place > now : electronic means

→ **Hong Kong Exchanges and Clearing Ltd.** ( HKEx ) > only exchange in HK

→ HKEx holds (a) Stock Exchange of Hong Kong Ltd ( SEHK )

(b) HK Futures Exchange Ltd

(c) HK Securities Clearing Company Ltd

(d) London Metal Exchange

**I.Process**

1. Investor : order to buy / sell stock with stockbroker System )

3. Stockbroker : charge brokerage commission (HK : stamp duty , transaction levy , Hex trending fee)

**II.Market Capitalisation – market value of all stocks listed on stick exchange (development level )**

→ = market price of a share of a listed co. X no. of shares issued

→ Largest : New York ( 6 times size of HKEx )

**III.Platform : Main Board ( MB ) vs. Growth Enterprise Market ( GEM )**

(a) Listing requirements ( MB : stricter )

• operating history ( MB > 3 years vs GEM > 2 years )

> Trading record ( management & ownership )

• financial ( GEM : no profit / revenue test )

> MB : profit attributable to stockholders , market capitalisation , revenue , cash flow

(b) Target firms ( MB : larger & more mature )

(c) Investment risk : tested > profitable > more stable stock prices ( MB : lower )

**(d) Main Board and Growth Enterprise Market (GEM)**

Listing requirements	Main Board are <b>stricter</b> than GEM's
Target companies	GEM: companies with potential growth but cannot meet the listing requirements of the Main Board.
Investment risk	Companies listed on the <b>Main Board</b> have a certain level of profitability, their <b>stock prices tend to be more stable</b> → lower risk



#### IV. Hang Seng Index ( HSI ) ( since 1969 )

V. is the most commonly used stock market index in **Hong Kong** (stock market performance)



VI. comprises the largest and most liquid stocks listed on HKEx (50 constituent companies)

- **stock market index** – indicator of overall performance of stock market
- **constituent stocks** : small group of stocks > accurately reflect general performance
- **liquid stocks** : high transaction frequency
- 50 large & liquid stocks from 4 sectors :

Finance , Utilities , Properties , Commerce & Industry

- > non -foreign , financially sound , large market capitalisation , listed >20 years
- calculated & published every 2 secs ( trading hours : 0900-1200 ,1300-1600 )
- > market capitalisation of all constituents with different weightings

- importance
  - (a) general stock prices movement : tend to follow
  - (b) HK economic performance : future prediction

#### Importance of the HSI

- Helping investors make decision: understand general movements of the Hong Kong stock market
- Reflecting the economic performance of Hong Kong in advance
  - Benefit constituent companies