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12 Invest Wisely: The SFC's Investor Education Programme

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Today I'd like to discuss an issue which to date has not been closely examined in Hong Kong - namely the need for investor education.

Why Investor Education?

"Why do we need investor education in Hong Kong?" you may ask. That need, as I see it, is based on three factors.

Well-informed Investors

First, efficient financial markets require well-informed investors who understand the risks and potential rewards of different types of investments as well as their rights as clients. Informed investors look beyond the packaging of a financial product to see what's inside. Informed investors know their financial priorities and ask the right questions when choosing their broker or adviser or their investments. In doing so, these investors make demands upon intermediaries resulting in more business going to those who can meet their needs and less going to those who can't.

Those of you in the brokerage industry know the positive long-term effect that educated investors have on the market. In a recent speech to US retail investors, SEC Chairman Arthur Levitt enumerated the benefits: "A greater number of first-time investors, starting at a younger age. A more stable market, with sophisticated investors riding out down markets. And as investors learn to avoid frauds and uneconomic deals, more money will flow to legitimate businesses that create jobs and wealth and strengthen the economy."

SFC Investor Survey Results

The second factor behind the SFC's investor education effort are the results of a recent SFC survey of retail investors in Hong Kong. That survey, copies of which I've brought along today, revealed that few adults in Hong Kong are aware of the array of investment opportunities available or of the risks and potential awards of those products.

Almost one in three Hong Kong adults was unable to nominate spontaneously - without prompting - a personal investment other than property. Even among those who could identify specific financial products, many confessed to knowing "very little" about that product or class of investment. The survey also revealed that people had insufficient knowledge of their rights as investors and little if any understanding of the regulatory system itself.

As you might expect, this low level of awareness is reflected in low levels of participation in any investment form. Six in ten Hong Kong adults had never invested in any financial products other than Hong Kong dollar deposit accounts in the last three years, and seven in ten had not been active in the past 12 months. Even among current investors, 26% do not intend to invest in the next 1-2 years.

You may also be interested to know that the most popular investments cited were - in order of priority - foreign currency savings accounts, stocks and investment-linked insurance products.

Lack of Knowledge/Confidence

The third factor behind the need for investor education stems from the second. Successive surveys have shown retail participation in the Hong Kong stock market at 7% to 9% of the adult population and now hovering at between 30-35% of market turnover. The main reason given for this low level of participation has been two-fold: the public's lack of knowledge about financial products and their lack of confidence in intermediaries.

Together, these factors led the SFC to conclude that a program of investor education was not just a good idea, but a necessity. Regulators in a number of developed markets including the US and Australia have made the same conclusion, recognizing the importance of encouraging informed investment in their markets.

As an organisation charged with investor protection as well as the encouragement of greater participation of investors in our markets, the SFC feels that it is our task to keep investors well informed and at the same time facilitate public education work by market bodies such as the exchanges and industry organisations.

What's crucial is that there be a partnership between regulators, exchanges and the industry in this process because it's in our collective interest to do so.

Our Key Messages to the Investing Public in Four Steps

In light of this background, the SFC has formulated the following key messages to the investing public, which based on the results of our retail investor survey, we believe is best conveyed in four steps. Most of you here are no doubt very familiar with the dos and don'ts of investment, but let me go through the main points of our message with you, so that if you think we can improve upon our message, you might let me know.

Step 1: How to Make Your First Moves Towards Investing

The first step is "How to Make Your First Moves Towards Investing." We advise investors to start by *setting priorities*, such as determining their goals (for example, saving for retirement versus preserving capital for a near-term commitment), their time horizon, and the level of risk they are willing to take, which will depend on such factors as job stability, age, and investment experience.

If you do not clearly identify your priorities, you could end up with a financial product or portfolio which is not suited to your needs - for example, a 10-year investment plan with penalties for early withdrawal will not be suitable if you think you might need to draw out money in the shorter term.

We also advise investors to *balance the risks against the returns* by diversifying their investments through a balanced portfolio approach rather than putting all their eggs in one basket. In addition, we ask investors to *'know' their investments*. This means *doing your homework* by evaluating the potential profitability of your investment and understanding the nature of the investment offered to you by reading the offer document (if there is one). Otherwise, always get the facts before trading. When you trade derivative warrants, for instance (which are very popular in Hong Kong but not recommended for novice investors), know who the issuer is and its financial standing.

Step 2: Choosing the Right Expert to Help You

After deciding what type of investment you wish to make, you need to choose a good broker or financial advisor. First, you must *make sure the person and the company you deal with are both properly licensed with the SFC.* The SFC's licensing regime imposes entry and ongoing requirements on registrants. An SFC licence, nevertheless, is not a guarantee either of honesty or future performance on the part of a person or company. An investor may still suffer loss due to the inefficiency, carelessness or negligence of an intermediary.

Before I go any further, let me be absolutely clear that the vast majority of people selling financial products are honest. There are many financially secure individuals who can thank their brokers for putting them on the right track long ago, helping them to plan for a comfortable retirement, their children's education, or other important investments.

Nevertheless, there are some people in the industry who do not always have their clients' interests at heart, or worse, and they can do enormous damage. That's why the best advice we can offer investors, is to ask the right questions of their broker or adviser. For example, they should ask up front about:

- the category of licence held by the intermediary;
- fees and charges;
- the grievance channels available if they are dissatisfied with the service they are receiving or if there is a dispute; and
- how their assets are held.

Prudent investors should also "get it in writing" by making proper, contractual agreements before trading. Furthermore, always ask for a clear explanation of the agreement's contents, in language you fully comprehend, and make sure you understand and agree with it before signing.

Step 3: The Importance of Monitoring Your Investments

Once you have invested, it is important for you to monitor your investments and this goes for the novice as well as the seasoned investor. How many of us have invested in what we thought was a safe long-term investment, only to lose track of its performance or the way it is being managed?

Monitoring your investments means being vigilant. Give clear instructions, check your transaction advice, contract notes, statement of accounts and last but not least, be alert to signals that things are not going the way they should; for example, the person with whom you are dealing suddenly becomes inaccessible, trade confirmations have been hand-amended or, instead of receiving a cheque for settlement of sale, you get excuses.

Step 4: When to Pursue a Complaint

Under such circumstances, you may wish to pursue a complaint. Investors can play a key role in enforcement and regulatory action by alerting the SFC to malpractices they encounter. The SFC has successfully exposed many abuses within the industry and punished the individuals concerned; many of these successes have stemmed from complaints from the public.

Certainly, investors can air their grievances through other channels, for instance to the senior management of the company concerned, or if they are dealing with a member of either the Stock or Futures Exchanges, they can contact these self-regulatory bodies.

The SFC maintains a Hotline which investors can call if they have a complaint about a registered person. All reports are treated as strictly confidential. We then carefully assess each case and act accordingly. Our Hotline number is 2840-9333.

Despite the SFC's willingness to deal with such complaints, part of our investor education role is to explain to investors what we can't do to help them and what they must do to protect themselves.

For instance, the SFC does not have the legal right or obligation to arbitrate or intercede in civil disputes between investors and intermediaries, and so can do little to assist in the recovery of lost investments. Nor can we make an order for compensation or damages.

An enforcement action by the SFC will not usually result in any monetary award to a private party, and is not a substitute for civil action for damages, which you may need to resort to if you have been given fraudulent advice.

How Do We Get the Message Across?

The four steps which I've outlined above are the subject of a series of easy-to-read booklets we've created for investors which will soon be available to the public at the SFC Counter and at all 16 Consumer Council offices. Trade bodies and intermediaries are welcome to display these booklets at their premises for their clients if they like. (I assure you that no disciplinary action will be taken if they choose not to). These booklets will soon be available on the SFC's new Internet Home Page as well. Next time you're "surfing the net", I encourage you to visit our Home Page the address of which, for those interested and with a pen ready to write this down, is http://www.cuhk.edu.hk/sfc*.

We are also considering delivering these messages through other media, including an investor education column in cooperation with a local newspaper. You'll be hearing more about these activities in the months to come.

Conclusion

For those of you concerned that the SFC's Investor Education campaign may overemphasize the risks than the rewards of investing, I assure you that is not the case. While our message to investors does point out danger signals, it does so only to encourage them to ask questions, to be vigilant, to get the best deal for their investment dollar, and - at the end of the day - to *invest wisely*.

I hope that the industry will support us in this educational effort by encouraging their clients to examine their investment options carefully. That's not just good for business; it should also go a long way towards helping the retail investor market in Hong Kong achieve its true potential.

* Presently, the website address is http://www.hksfc.org.hk
For Investor Education Centre, the address is http://www.eirc.org