



SECURITIES AND
FUTURES COMMISSION
證券及期貨事務監察委員會

Warrant Investor Survey

Hong Kong
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1. Executive Summary

In January and February 2006, the Securities and Futures Commission (SFC) engaged the Centre for Corporate Governance and Financial Policy of the Hong Kong Baptist University to conduct the Warrant Investor Survey. The survey aims to understand retail investors' objective of trading warrants, their level of understanding and whether they made profits or suffered losses out of trading warrants.

In the study, warrant investors are defined as those Hong Kong adults aged 18 or above who had traded warrants in Hong Kong in the last two years. 250 warrant investors were successfully interviewed, 130 of them were among the 246 warrant investors identified in the SFC's Retail Investor Survey 2005¹. The remaining 120 warrant investors were newly identified through making calls to 12,702 randomly selected residential phone numbers.

Retail participation and demographic profile of warrant investors

- As per the SFC's Retail Investor Survey 2005, 4.7% of Hong Kong adults aged 18 or above or 12.9% of retail investors² had traded warrants during the last two years.
- Of the 250 warrant investors interviewed, 61.2% were male; 79.1% were aged between 30 and 59; and 35.2% were degree holders or above and 30.8% were upper secondary school graduates.

Trading objectives

- 76.0% of warrant investors said that they had some knowledge about warrants and hoped to make short-term gains. 8.4% used warrants for risk management (e.g. hedging) or long-term investment purposes. 10.8% stated they knew nothing about warrants and simply bet on their luck.
- 36.8% of warrant investors started trading warrants out of their own initiative. 31.6% said they were influenced by their friends or family members who had traded warrants. 20% were prompted to trade warrants by market commentators' views in the mass media.

¹ Conducted in September to November 2005, the Retail Investor Survey 2005 focuses on estimating retail participation in different investment products, ascertaining the level of financial understanding of retail investors in some areas, their choices of intermediaries, types of accounts used and their views on the SFC's investor education work.

² Retail investors are defined as those Hong Kong adults aged 18 or above who had invested in one or more kinds of investment products (e.g. stocks, managed funds (excluding MPF investments), bonds, derivatives, structured products, leveraged foreign exchange contracts) in the last two years.

Risk perception

- The majority of warrant investors perceived derivative warrants as risky. 66% and 26.4% perceived the risks of derivative warrants were “very high” and “high” respectively. 4.8% considered the risk level as “medium”. Only 2.4% viewed that derivative warrants were of low risk.

Level of understanding

- 76% of warrant investors understood that the underlying asset’s price is not the only factor that affects the price of a warrant. Among these investors, 64.2% could at least cite one additional factor that could influence the price of a warrant.
- 47.6% of warrant investors understood that a higher implied volatility indicates that a derivative warrant is more expensive.

Trading history

- The majority (73.2%) of warrant investors had been trading warrants for more than 12 months.

Portion of portfolio

- Around half (51.6%) said warrants accounted for less than 10% of their investment portfolios. On the other hand, 16.8% of them had over 50% of their portfolios invested in derivative warrants.

Trading decisions

- Warrant investors chose warrants as an investment tool mainly because of higher volatility (52.0%) and better liquidity (23.6%) of warrants.
- In selecting a specific derivative warrant to trade, 76.8% of warrant investors said they did their own analysis. 19.6% were influenced by market commentators’ views in the mass media. 8.4% and 8% considered recommendations of issuers and brokers respectively.
- 83.6% of warrant investors usually compared similar derivative warrants before deciding to trade a particular one.

Trading results

- 30.8% of warrant investors had made a net gain from trading derivative warrants during the past 12 months. 47.2% suffered a net loss while 12% broke even. 10% responded that they didn’t know.

- Among those who made profits from trading warrants, their gains ranged from around HK\$1,000 to around HK\$300,000 with the median being HK\$20,000. In percentage terms, their gains represented approximately 2% to 300% of their capital used in trading derivative warrants. The median was 25%.
- Among those who lost money in trading warrants, their losses ranged from approximately HK\$1,000 to HK\$400,000 with the median being HK\$20,000. In percentage terms, their losses represented approximately 0.5% to 100% of their capital used in trading warrants. The median was 40%.
- 47.5% of loss-making warrant investors said that they would continue to trade. Their main reasons were that: 53.6% understood the risk of investing and were prepared to take the risk; 41.1% had learnt more about warrants and hoped to do better in future; 37.5% hoped to recover their losses from further trading. 10.7% stated that they were addicted to trading derivative warrants.

2. Retail Participation and Demographic Profile of Warrant Investors

As per the SFC's Retail Investor Survey 2005, 4.7% of Hong Kong adults aged 18 or above or 12.9% of retail investors had traded warrants during the last two years.

Of the 250 warrant investors interviewed, 61.2% were male; around one quarter lied in the age ranges 30-39 (25.3%), 40-49 (27.3%) and 50-59 (26.5%) respectively; and 35.2% were degree holders or above and 30.8% were upper secondary school graduates (Table 1).

Table 1: Demographic Profile of Warrant Investors

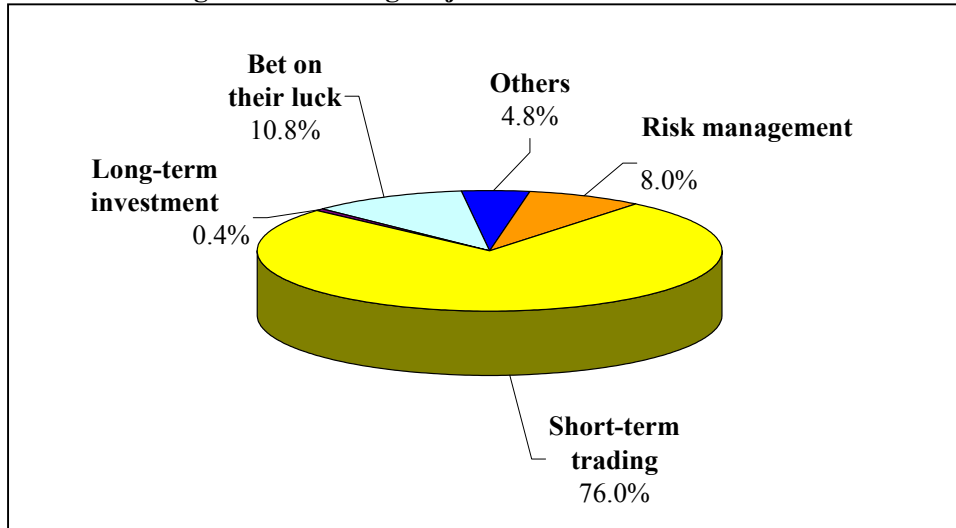
	<u>Warrant investors (%)</u>
<u>Gender</u>	
Male	61.2
Female	38.8
<u>Age group</u>	
18-29	14.9
30-39	25.3
40-49	27.3
50-59	26.5
60 or above	6.0
<i>Median</i>	<i>45</i>
<u>Education</u>	
No schooling/kindergarten	0.4
Primary	7.2
Lower secondary	12.8
Upper secondary	30.8
Matriculation	7.6
Tertiary: Non-degree	6.0
Tertiary: Degree or above	35.2

(Base: all answers excluding refusal cases)

3. Trading Objectives

8.4% of warrant investors traded warrants for risk management (e.g. hedging) or long-term investment purposes. Most (76.0%) of them said that they had some knowledge about warrants and hoped to make short-term gains. 10.8% stated that they knew nothing about warrants and simply bet on their luck (Figure 1).

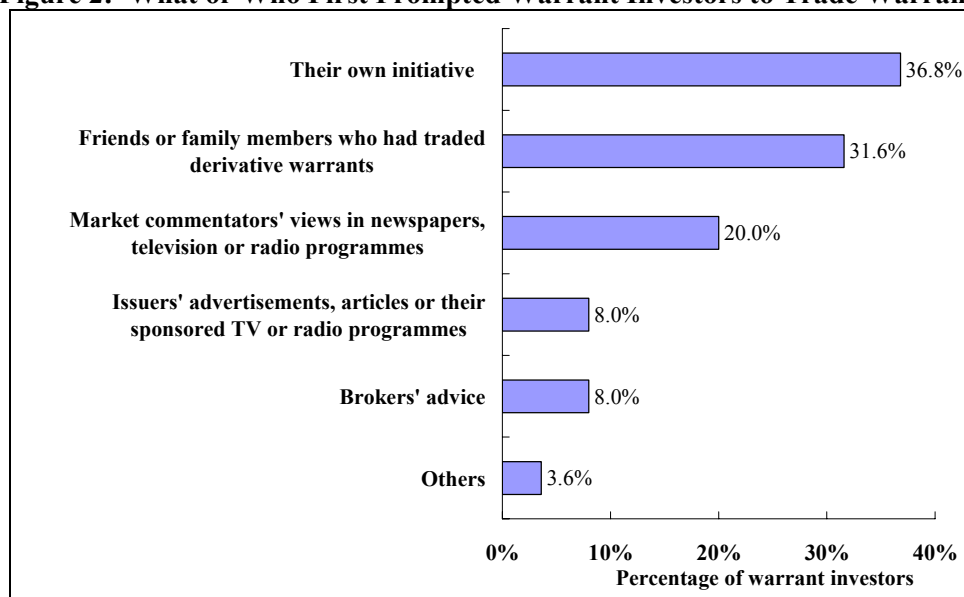
Figure 1: Trading Objectives of Warrant Investors



(Base: all warrant investors)

When asked what or who first prompted them to trade warrants, 36.8% of warrant investors responded that they traded warrants just out of their own initiative. 31.6% were influenced by their friends or family members who had traded warrants. 20% were driven by market commentators' views in newspapers, television or radio programmes to trade warrants. Less than 10% traded warrants because of brokers' advice (8%) or issuers' advertisements, articles or their sponsored television or radio programmes (8%). (Figure 2)

Figure 2: What or Who First Prompted Warrant Investors to Trade Warrants



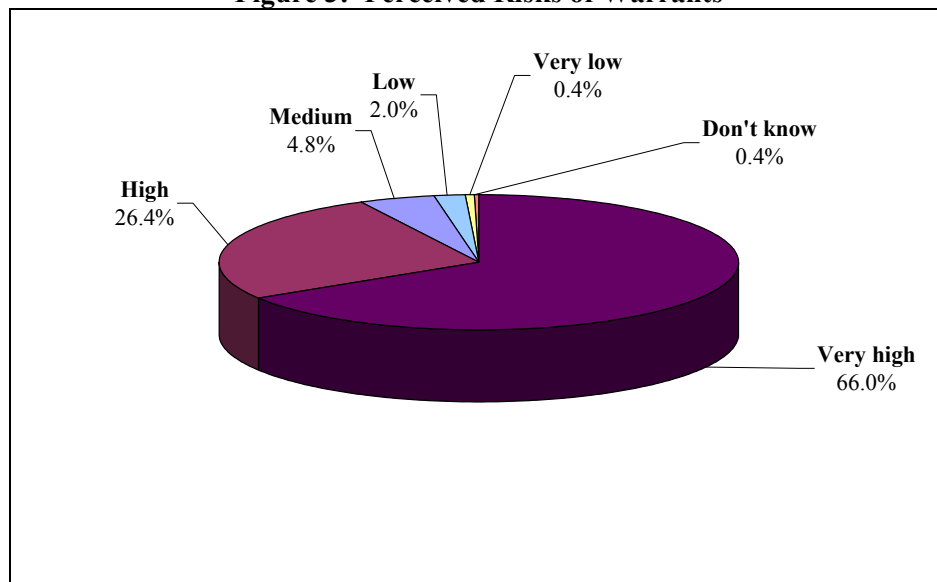
(Note: multiple answers allowed except for the answer "Their own initiative")

(Base: all warrant investors)

4. Risk Perception and Level of Understanding of Warrants

66% and 26.4% of warrant investors perceived the risks of warrants were “very high” and “high” respectively. 4.8% considered the risk level as “medium”. 2.4% viewed that the risks were “low” or “very low”. 0.4% said that they did not know (Figure 3).

Figure 3: Perceived Risks of Warrants



(Base: all warrant investors)

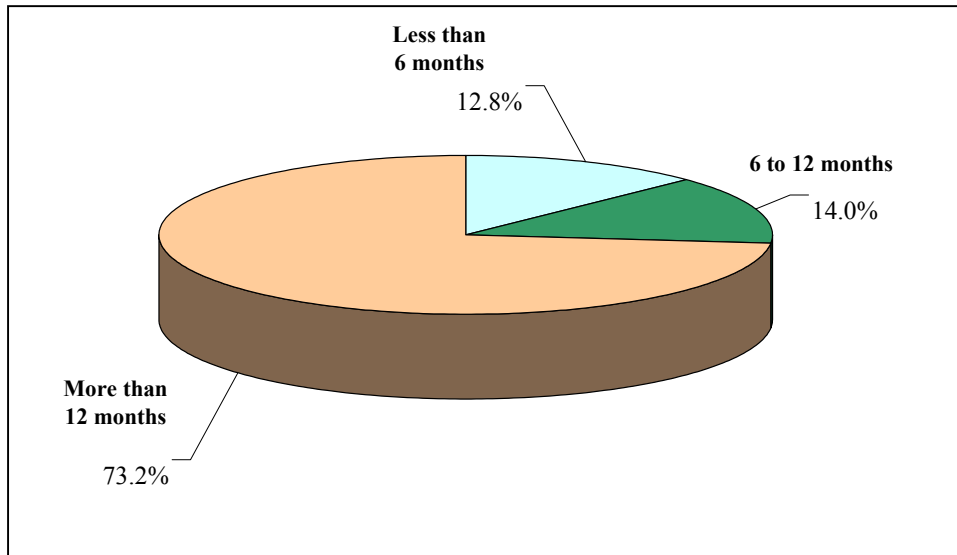
76% of warrant investors understood that the underlying asset’s price is not the only factor that affects the price of a warrant. Among those who could pinpoint the above, 64.2% could at least cite one additional factor that could influence the price of a warrant. The three most commonly quoted factors were “time to maturity”, “volatility of the price of the underlying” and “supply and demand of the warrant”.

47.6% of warrant investors understood that a higher implied volatility indicates that a derivative warrant is more expensive.

5. Trading History and Portion of Portfolio

The majority (73.2%) of warrant investors had been trading warrants for more than 12 months. 14% had 6 to 12 months experience. 12.8% had been dealing for less than 6 months (Figure 4)

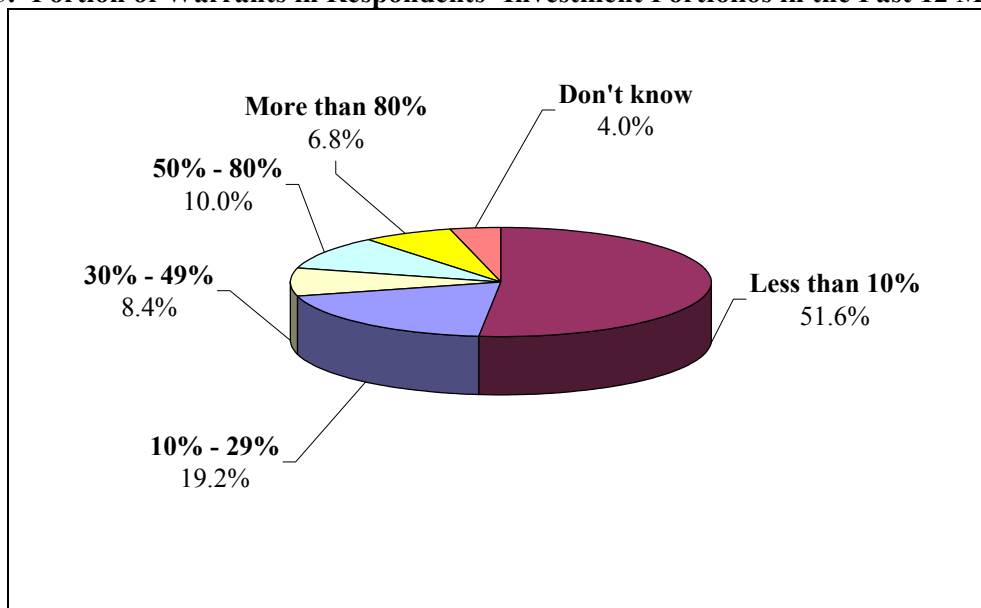
Figure 4: Trading History of Warrant Investors



(Base: all warrant investors)

Around half (51.6%) of warrant investors said that on average, their investments in derivative warrants in the past 12 months accounted for less than 10% of their investment portfolio. 19.2% said it accounted for 10%-29% of their portfolio. 8.4% told that it accounted for 30%-49%. 16.8% had invested over 50% of their portfolios in warrants (Figure 5).

Figure 5: Portion of Warrants in Respondents' Investment Portfolios in the Past 12 Months

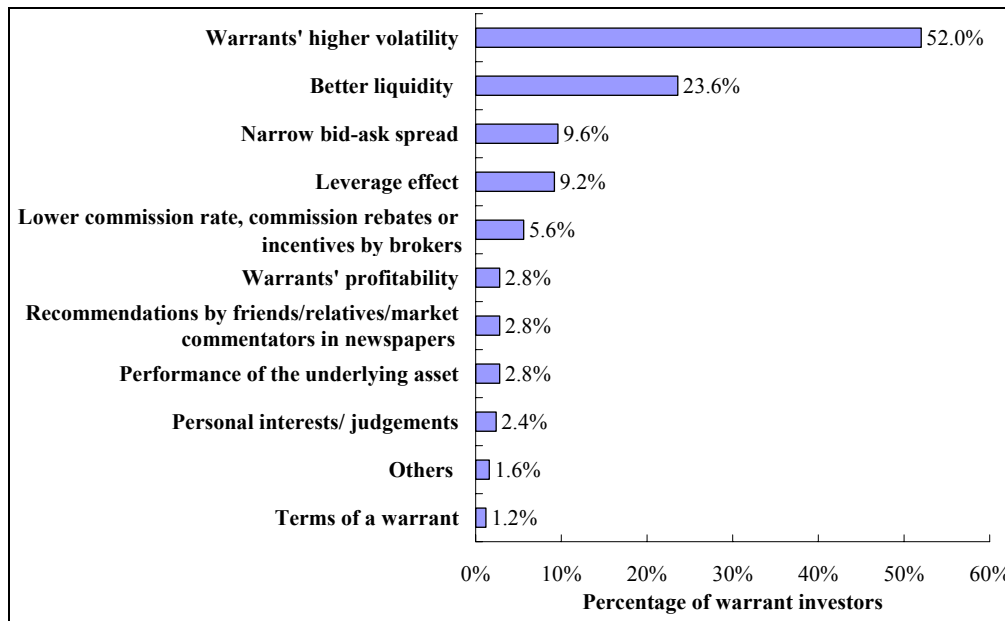


(Base: all warrant investors)

6. Trading Decisions

When asked why they picked warrants as an investment tool, 52.0% of warrant investors were attracted by the higher volatility of warrants. 23.6% cited better liquidity of warrants as a reason. Nearly 10% chose warrants because of the narrow bid-ask spread (9.6%) and the leverage effect of warrants (9.2%). 5.6% were attracted to trade by the lower commission, commission rebates or other incentives offered by their brokers (Figure 6).

Figure 6: Reasons for Choosing Warrants as an Investment Tool



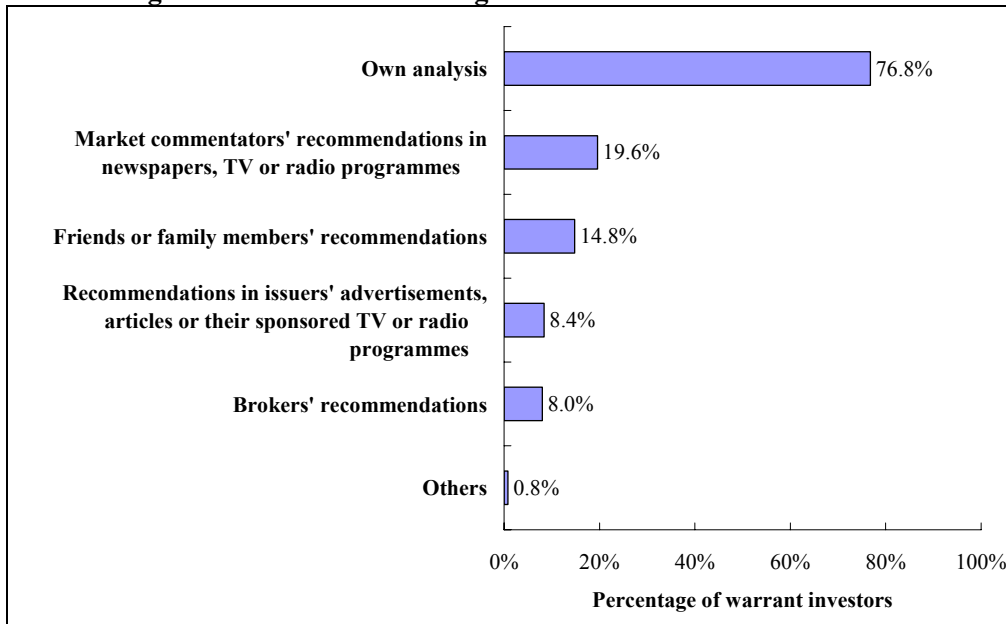
(Note: multiple answers allowed)

(Base: all warrant investors)

On the basis of selecting a particular derivative warrant, 76.8% of warrant investors said that they did their own analysis. 19.6% was influenced by market commentators' recommendations in newspapers, television or radio programmes. 14.8% considered their friends or family members' recommendations. 8.4% relied on recommendations in issuers' advertisements, articles or their sponsored television or radio programmes. 8.0% took into account their brokers' recommendations (Figure 7).

Moreover, 83.6% of warrant investors usually compared similar derivative warrants before deciding to trade a particular one.

Figure 7: Basis For Selecting a Particular Derivative Warrant



(Note: multiple answers allowed)

(Base: all warrant investors)

Of those who did their own analysis in warrant selection, 71.9% looked at the terms of the warrants. 42.7% evaluated whether the warrants were value for money or reasonably priced. 26.6% considered who the issuer was.

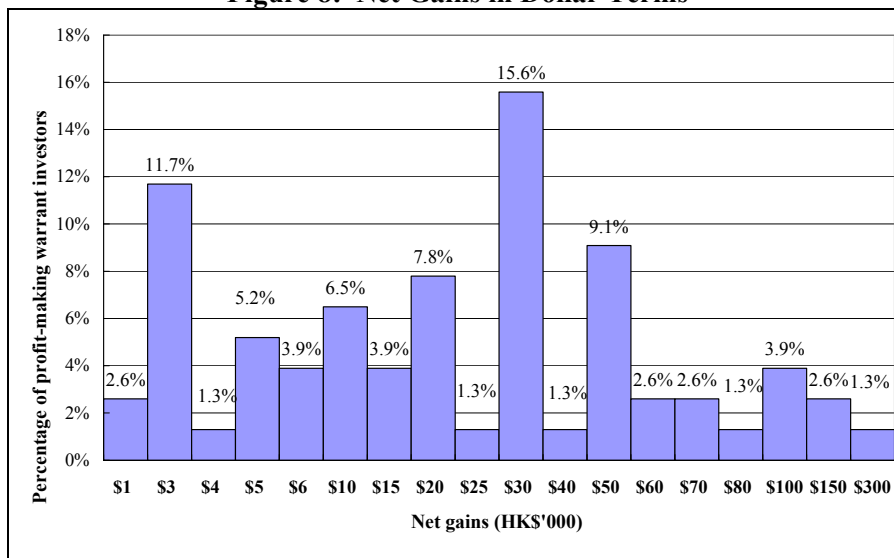
7. Trading Results

30.8% of warrant investors responded that they had made a net gain from trading derivative warrants during the past 12 months. 47.2% suffered a net loss while 12% broke even in their investments. 10% responded that they didn't know.

Net Gains

Among those who made profits from trading warrants, their gains ranged from around HK\$1,000 to around HK\$300,000 with the median being HK\$20,000 (Figure 8).

Figure 8: Net Gains in Dollar Terms

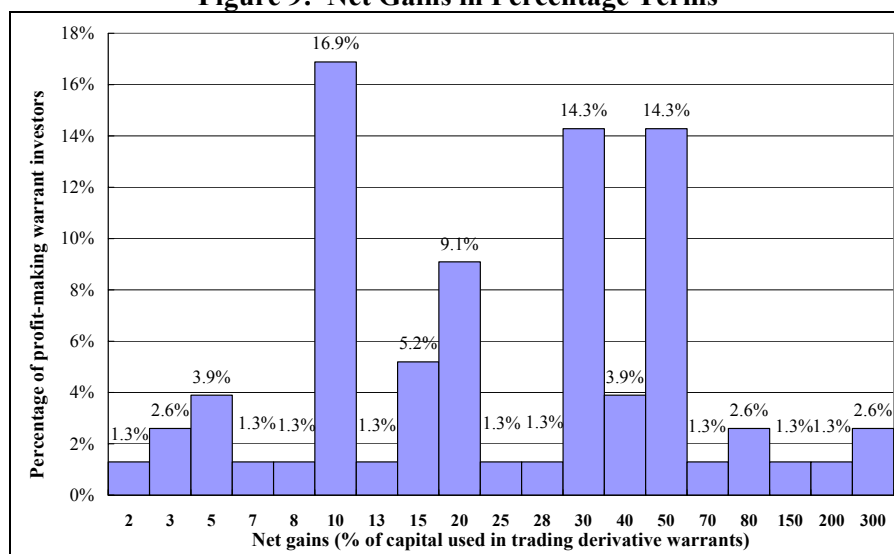


(Note: 15.6% of profit-making warrant investors could not remember.)

(Base: all profit-making warrant investors)

In percentage terms, their gains represented approximately 2% to 300% of their capital used in trading derivative warrants. The median was 25% (Figure 9).

Figure 9: Net Gains in Percentage Terms



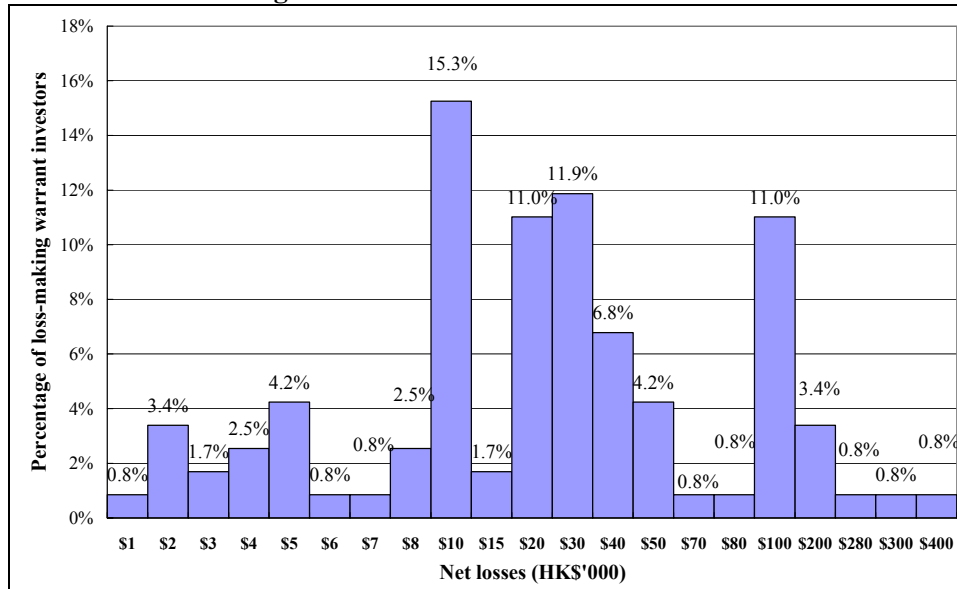
(Note: 13% of profit-making warrant investors could not remember or did not know.)

(Base: all profit-making warrant investors)

Net Losses

Among those who lost money in trading warrants, their losses ranged from approximately HK\$1,000 to HK\$400,000 with the median being HK\$20,000 (Figure 10).

Figure 10: Net Losses in Dollar Terms

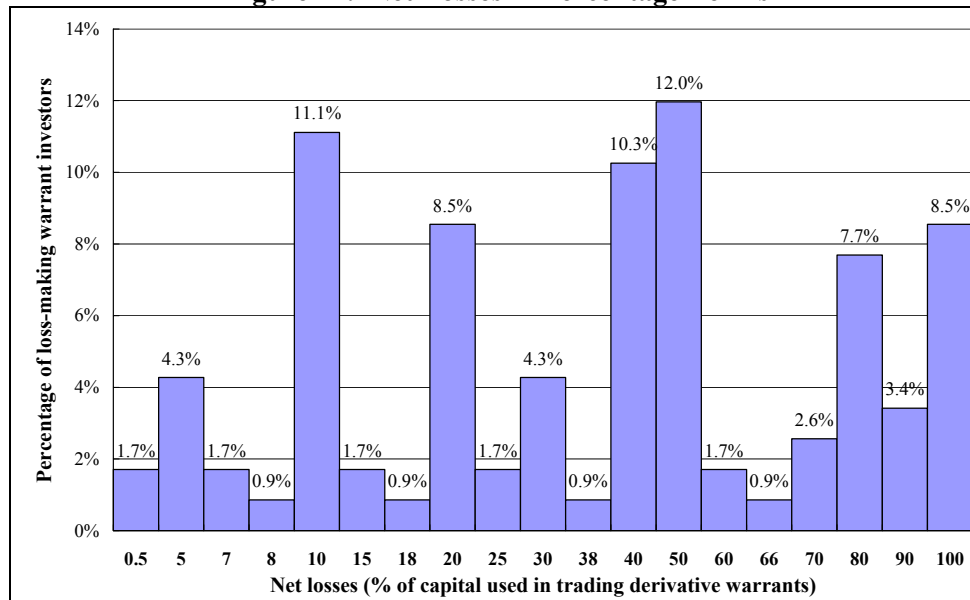


(Note: 13.6% of loss-making warrant investors could not remember.)

(Base: all loss-making warrant investors)

In percentage terms, their losses represented approximately 0.5% to 100% of their capital used in trading warrants. The median was 40% (Figure 11).

Figure 11: Net Losses in Percentage Terms



(Note: 15.4% of loss-making warrant investors could not remember or did not know.)

(Base: all loss-making warrant investors)

47.5% of loss-making investors said that they would continue to trade. 44.1% said no and 8.5% were not sure yet.

The main reasons quoted by those loss-making warrant investors who would continue to trade were that: they understood the risk of investing and were prepared to take the risk (53.6%); they had learnt more about warrants and hoped to do better in future (41.1%); they hoped to recover their losses from further trading (37.5%); they were addicted to trading derivative warrants (10.7%); and they followed the advice of their brokers (1.8%) (Figure 12).

Figure 12: Reasons for Loss-Making Warrant Investors to Continue to Trade



(Note: multiple answers allowed.)

(Base: all loss-making warrant investors who would continue to trade.)

Survey Design

Target Respondents

Definitions of the target respondents in this survey are as below:

- Respondents: Hong Kong adults aged 18 or above.
- Warrant investors: respondents who had traded warrants in the past two years.

Data Collection Method

The survey data were collected through telephone interviews from 20 January to 6 February 2006. A structured questionnaire was used to collect information from the target respondents.

Sampling Method

250 warrant investors were successfully interviewed through two different samples.

The first sample was the pool of warrant investors identified in the Retail Investor Survey 2005. In that survey, a sample of 34,999 residential telephone numbers were randomly selected, 5,210 respondents aged 18 or above were successfully contacted and interviewed, 246 of which were classified as warrant investors. All these warrant investors were invited to participate in the Warrant Investor Survey, 130 of them responded.

The second sample is a booster sample. 12,702 residential telephone numbers were randomly selected and 3,860 respondents aged 18 or above were successfully contacted and interviewed. 120 were ultimately identified as warrant investors.