

Financial Planning





About the Investor and Financial Education Council

Established in 2012 and supported by four financial regulators and the Education Bureau, the Investor and Financial Education Council (IFEC) is a public organisation dedicated to leading financial literacy in Hong Kong. The IFEC promotes and delivers free and impartial financial education resources and programmes through its consumer education platform, The Chin Family, and leads the Financial Literacy Strategy to create a conducive environment for stakeholders to deliver more quality financial education to various segments of the Hong Kong population.

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What Is Financial Planning?

Managing your present and future finances



Financial planning is the process of setting, planning, achieving and reviewing your life goals through the proper management of your finances.

A holistic financial plan not only involves investing money and building your wealth; but also your credit and tax obligations, everyday spending, planning for a family, setting up your home, saving for your children's education fund, and saving for retirement - as well as protecting yourself and your family with suitable insurance policies and arranging your estate. All these facets of your financial plan are interconnected.

Financial planning is an important life skill to help you plan for your future and take better control of your financial goals by helping you to set realistic plans, evaluate alternatives and take effective measures.

Sounds difficult? It does not have to be! With the steps outlined in this simple guide, you can start putting together a basic financial plan all by yourself.

Common misconceptions about financial planning

Misunderstanding

1

One only needs to start financial planning when approaching retirement.

Financial planning is a life-long process. The earlier you start, the sooner you can enjoy the benefits – and the more time you have to grow your savings.

Misunderstanding

2

Financial planning is just another name for investing.

Financial planning is more than just investment. Rather, it is about the big picture: bringing together all aspects of personal finance to achieve your financial goals.

Misunderstanding

3

Once you finish your financial plan, you do not have to think about it again.

Financial planning is not a one-time deal! You should revisit and review your financial plan regularly to make sure you are on the right track towards achieving your goals.

Misunderstanding

4

You need a lot of money to do financial planning.

Everyone can benefit from financial planning, not just multi-millionaires! No matter how much income or savings you have, you can always benefit from having a clear plan for your finances.

Why do you need a financial plan?

Financial planning is important because it gives you a plan to achieve your financial goals in different life stages. A prudent plan can help you:

Satisfy today's financial needs by monitoring your savings and expenses.

Save for emergencies by providing a financial cushion to deal with unexpected crises.

**A
Prudent
Plan...**



Meet future financial goals by helping you to plot your course such as buying a house and getting married.

Plan for your retirement by amassing enough wealth to meet your future expenses.

Provide protection for you and your family by having the right insurance in place if something goes wrong.

The Financial Planning Process

Key steps to draw up a basic financial plan



STEP 1

Assess your financial situation



A good first step when developing your financial plan is to assess your financial situation. With a clear understanding of your current financial situation, you can decide where you should start from, and what you need to achieve your financial goals.

Knowing your net worth is important to assessing your financial situation. Start by making a list of all your assets as well as your liabilities.

Net worth is broadly calculated as your assets minus your liabilities. Assets are what you own, including savings, property, investments; and liabilities are what you owe, such as mortgage loans, tax bills and outstanding debts.



STEP 2

Create a budget

Track the ins and outs of your money to understand your money habits and take control of your spending and savings.

Prioritise your needs and wants and look for any unnecessary expenses you can cut to save money. Also refrain from overspending especially impulse buying by credit card. Before you decide to borrow money, make sure you can afford new debt repayments on top of your current expenses or commitments.



Budget Planner

The Budget Planner can help you record all of your incomings and outgoings, and give you a breakdown of where your spending goes each week, month or year across the following broad categories: household, transport, food and drinks, leisure, shopping, health and beauty, education and profession, family and friends, taxation, financial commitments, etc.

You can save your budget planner results on your computer, print it out for later reference or work offline by downloading the budgeting spreadsheet onto your computer.

You can access the Budget Planner at:

www.ifec.org.hk ➔ **Tools**



What's your budget?

Use this worksheet to work out your own budget:

Income		Savings and investments	
Salary	HKD _____	Savings/Investments	HKD _____
Spouse's salary	HKD _____	Retirement schemes	HKD _____
Other income	HKD _____		
Subtotal:	HKD _____	Subtotal:	HKD _____
Expenses			
Household		Lifestyle/Leisure	
Rent/Mortgage	HKD _____	Movies	HKD _____
Management fee	HKD _____	Music	HKD _____
Utilities (water, electricity, gas)	HKD _____	Interest class/Hobbies	HKD _____
Internet/Telephone/ Mobile phone service	HKD _____	Others _____	HKD _____
Pay TV	HKD _____	Shopping	HKD _____
Others _____	HKD _____	Health and beauty	
Transport	HKD _____	Medical/Dental care	HKD _____
Food and drinks	HKD _____	Health supplements	HKD _____
Grocery shopping	HKD _____	Fitness and beauty	HKD _____
Eating out	HKD _____	Cosmetics and skincare	HKD _____
Others _____	HKD _____	Others _____	HKD _____
Family and friends	HKD _____	Education and profession	HKD _____
Support for parents and relatives	HKD _____	Planning for ageing	HKD _____
Children	HKD _____	Financial and legal advice	HKD _____
Others _____	HKD _____	Miscellaneous	HKD _____
Financial commitments		Others _____	HKD _____
Insurance	HKD _____	Others _____	HKD _____
Loan repayment	HKD _____	Others _____	HKD _____
Charity donations	HKD _____	Taxation*	HKD _____
Others _____	HKD _____	Subtotal:	HKD _____
Income - Savings - Expenses		HKD _____	

* You can save up for your annual tax bill by estimating your taxes for the year, then divide that figure by 12 to calculate how much to set aside every month.

Life events and you

Starting work

Starting your first job can be one of life's most exciting times. While you are enjoying the freedom of financial independence, it is crucial to develop good money management skills to keep you on solid financial footing.

Financial priorities

If you have unpaid student loans or other debts, make it a first priority to clear the debts the soonest possible. Next on the list should be building up your savings into an emergency fund which serves as a safety net against life's many uncertainties.

Watch your spending and use your income to start building your savings. Be sure to maintain a good credit rating, review your insurance needs and get started with long-term financial planning.

Keys to managing personal finances

- Create a budget to track your finances.
- Make it a habit to save part of your income every month. The earlier you start saving, the better chance you have to realise your financial goals.
- Set aside money for paying tax.
- Maintain a good credit rating by making your loan and debt payments on time.
- Review insurance coverage to ensure it meets your needs – medical and life insurance are good choices to start with.
- Set some long-term goals for different stages in life. And it is never too early to start planning for your retirement!



STEP 3

Set your financial goals



Based on a sound understanding of your financial situation, you may be able to identify your short-, medium- and long-term financial goals. This will help you review your budget, determine your investment time frame and work out a strategy for deciding on the appropriate investments. With measurable and clearly defined goals, it will be easier to monitor the progress.



Savings Goal Calculator

Saving up for something special? Getting married? Buying a home? Furthering your education? The Savings Goal Calculator can help you work out how you can achieve your savings goals. It will help you calculate how much you will need to save regularly to reach your goal in time; how much you will have if you put aside a fixed amount of money regularly; and how long it will take to achieve your savings target.

You can access the Savings Goal Calculator at:

www.ifec.org.hk ➔ **Tools**

When setting your financial goals, you have to consider:

It is important to know what you are planning for. Make a list of all your needs and goals. Remember, managing your day-to-day expenses should come first.

The key thing is to set realistic goals and prioritise. For example, if you have borrowed money at a high interest rate (eg credit card advances or other personal loans), make paying off that debt your first priority before taking on other goals. You also need to map out the cost of each goal and how much time you have to save or invest before you need to pay for it (eg investment time horizon).

When setting your financial goals, it is important to be realistic. As you regularly review and refine your financial plan and assess your risk tolerance level, you may find it worthwhile to adjust your goals accordingly.



What are your financial goals?

In the next few years, I want to...



Set aside emergency funds



Buy a car



Further my education



Buy a home



Get married

In the long run, I want to...



Set up an education fund for my children



Start my own business



Pay off my mortgage



Build a nest egg for retirement



Provide enough funds for my family after my death

Saving - the earlier the better!

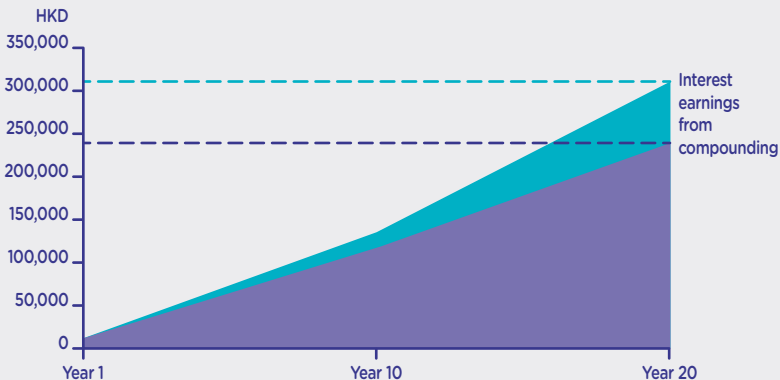
The earlier you start saving, the sooner you will allow yourself to benefit from the effect of compounding, a powerful mechanism that puts time to work on your savings.

When you save or invest in something that pays interest, you earn interest on your principal (the original investment amount). If you continue to save and earn interest, you will receive interest on the principal plus the interest you earned last time, ie earning interest on your interest. This is called compound interest, and it can significantly boost your savings over time.

Case study

How compounding works over time

Stephen has started his first job. He decided to keep a separate savings account from his regular transaction account to make it easier to save. He deposits HKD1,000 into the savings account every month at an annual interest rate of 2.5%, compounded monthly. After working for 20 years, Stephen has accumulated HKD310,975 with some HKD70,000 being the interest earnings. Most of his wealth gains in later years are due to the powerful effect of compounding.





Do you need a financial adviser?

Choosing whether or not to use a professional financial planner depends on your particular circumstances. If you have the time and interest to conduct your own research – and a reasonable understanding of financial markets and products – you may choose to manage your finances on your own.

If you have complicated financial affairs, or you have a significant financial decision or plan to make, you may choose to work with a financial adviser.

What to look for

Make sure to check the following when you consider a financial adviser or planner:

- They must know your personal circumstances including your investment objectives, investment horizon, knowledge and experience (including any knowledge of derivatives), financial situation and risk tolerance (including risk of loss of capital), and carefully evaluate your risk profile before making any strategies or financial product recommendations to you.
- They should give you proper explanations of why recommended products are suitable for you and the nature and extent of risks the investment products bear. They should also document and provide you with a copy of the rationale underlying the investment recommendations made to you.
- In providing services involving derivative products, they must assure that you understand the nature and risks of recommended products and that you have sufficient net worth to be able to assume the risks and bear the potential losses of trading in the products.

10 questions to ask your financial adviser

When selecting a financial adviser or planner, there are 10 basic questions you should ask to assess his/her suitability for helping you to plan your finances:

Q1 What experience does the planner have?

Q2 What are the planner's qualifications?

Q3 What services does the planner offer?

Q4 What is the planner's approach to financial planning?

Q5 Will the planner be the only person working with you?

Q6 In what way will the planner be remunerated?

Q7 How much does the planner typically charge?

Q8 Could the planner's recommendation unduly benefit any third parties?

Q9 Has the planner ever been publicly disciplined for any unlawful or unethical actions in his/her professional career?

Q10 Is the agreement put in writing?

Life events and you

Getting married

Planning your wedding and the start of a new life with your partner is a thrilling time. One of the keys to a successful marriage is preparing your and your partner's financial life together, and keeping money issues from putting a strain on the relationship.

Financial priorities

With financial problems a contributing factor to divorces, it is important to first understand each other's financial histories and goals (including unsettled debt), then discuss and plan finances together.

There is no best approach so make sure you talk through the differences and work out a common approach that both of you accept.

Keys to planning your finances together

- Talk about your experiences with money, savings and credit; and ask your partner about the expectations on marital finances and financial planning.
- Draw up a budget jointly to understand money management habits and discuss how to improve your family finances.
- Review and update your financial documents including insurance coverage so that your loved ones will have better protection if something unexpected happens.
- Wedding costs can be significant, so talk with your partner about the kind of wedding you want and how you are going to pay for it. Make a budget and agree on which parts of the wedding are the most important.



STEP 4

Know your risk tolerance

An important part of your financial planning is to evaluate your tolerance for risks.

Risk is the potential threat that may impact the expected outcome of your investments. Investments that deliver potentially higher returns are usually accompanied by higher risks. Are you willing to accept potential losses in exchange for greater potential gains?

Risk tolerance can be classified into five categories. Which one best describes you?

Conservative Not willing to take up risk and see loss in investment and may rather forgo potential gains.

Moderately cautious May be willing to accept a limited amount of risks to improve their long-term investment returns, but still try to avoid large short-term fluctuations.

Balanced Weighting the risks and returns, balanced investors recognise that taking on a measured amount of risks will improve the probability of achieving their long-term financial goals.

Moderately aggressive By taking on greater investment risks, moderately aggressive investors expect to see their investment portfolio outperform the market; and do not mind accepting a bit more risk or loss than the market bears.

Aggressive Ready to take on higher levels of risks in order to substantially outperform the markets.



Understand investment risks

<input type="checkbox"/> Market risk	Market risk, also known as systematic risk, usually refers to that type of risk associated to a specific market. It stems from the economic, geographical, political, social or other factors of that market.
<input type="checkbox"/> Interest rate risk	Shifts in interest rates affect a wide range of investments – including bank deposits, stocks, bonds and property.
<input type="checkbox"/> Business risk	A company in which you invest may suffer a severe decline in profits or even go bankrupt.
<input type="checkbox"/> Corporate misgovernance	A company you invest in may conduct a corporate transaction that you deem detrimental to shareholders' interests.
<input type="checkbox"/> Currency risk	Overseas investments can be badly hit if currencies suddenly turn against you.
<input type="checkbox"/> Inflation risk	Increases in the price level can eat away the value of your capital and reduce your purchasing power.
<input type="checkbox"/> Liquidity risk	Tying up investments in products which are hard to liquidate, or carry heavy costs for liquidation, can prove a burden.
<input type="checkbox"/> Policy risk	Changes in government policies and regulations could have profound impact on your investments.
<input type="checkbox"/> Scams risk	The best way to keep away from investment scams is by using common sense and taking precautions. Avoid get-rich-quick schemes.
<input type="checkbox"/> Broker failure	If your broker defaults or goes bankrupt, you may find your investments at risk. It is best to deal with authorised and licensed brokers.

Managing risks

You cannot totally avoid risks. But you can control your exposure to risks to an acceptable level. Make sure you understand exactly what you are investing in and recognise the potential risks.

Take the trouble to learn about the products you wish to invest in. Read prospectuses, offer documents, annual reports and announcements carefully. Pay attention to the “risk factor” sections or “risk warning” messages. If in doubt, seek professional advice.

Case study

Risk profiles at different stages of life

Michael has just graduated from university and is starting his first job. As he lives with his parents, his expenses are relatively low and his food and board are covered. At this stage of his life, Michael can afford to take on more risks as he has a long investment horizon ahead.

Eight years later, Michael is married and has a family of his own. With a mortgage to pay and increasing financial responsibility for his parents, Michael is more conservative in his risk profile these days. While he still has time on his side, he is taking a more prudent approach.

Now retired, Michael’s risk profile has changed again. As he no longer receives a monthly salary, Michael now focuses on preserving and protecting the wealth he has built up during his career – while enjoying the fruits of his labour in his golden years.



STEP 5

Work out and implement a basic financial plan





Future consumption

Future consumption includes life events such as furthering education, getting married, purchasing property, having children, supporting parents, changing careers, starting business or retirement. These expenses may deplete your assets and can be long-term financial commitments.



Insurance

Unexpected incidents or emergencies in life such as accidents, illness and death can deplete your savings and erode your assets. Having adequate insurance coverage for these eventualities should be a key component of your financial planning. As a minimum, consider critical illness and accident/disability insurance. You should also consider setting up an emergency fund to cover about three to six months of living expenses.



Responsible borrowing

Responsible borrowing is an integral part of financial planning. Paying by credit card is convenient. Personal loans and mortgage for example, can help you achieve your financial goals; but over-indebtedness can jeopardise your life plan. The key thing is to make sure you are in control of credit, not the other way around. Your past credit record may also affect your cost of borrowing in the future.



Retirement planning

Retirement planning is the process of determining how you will set aside enough money so you can enjoy life after you stop working. Creating a retirement plan will help you determine how much money you will need after you retire, and help manage your finances to cover expenses in later years.



Estate planning

Preparing for the worst may be unpleasant, but it is an essential part of your long-term financial planning. In the event of serious illness, disability or death, it is important that your finances are in order so your family can be better prepared to meet life's challenges and emergencies.

Life events and you

Having children

Being a parent can be one of life's greatest joys. But as you make the transition to parenthood, you and your partner may need to adjust to a new set of long-term financial responsibilities.

Financial priorities

Review your household budget and make allowances for the essential items before and after the baby is born. You also need to prepare for the unexpected such as having twins or contingency arising from events such as medical support during childbirth as well as to plan for the children's education.

Keys to planning finances for the family

- Create a budget to calculate your new expenses and allocate your income to handle them.
- Develop a financial plan to ensure your family's long-term financial well-being. If you already have a financial plan, review it carefully to see if you need to make changes. Make sure to consider the following items:
 - Do you need a bigger home? If you rent, are you financially prepared to make the move into home ownership? Will you need to move closer to schools?
 - Do you have enough insurance coverage to protect your family against the uncertainties in life?
 - Do you need to hire a domestic helper?
 - Are you or your spouse thinking about leaving the workforce to take care of the children?
 - Do you have enough fund to support your children's education needs? Education costs can be expensive, and it is common to have a savings and investment plan in place that will help lighten the financial load when the bills start to come in.



Build and manage your investment portfolio

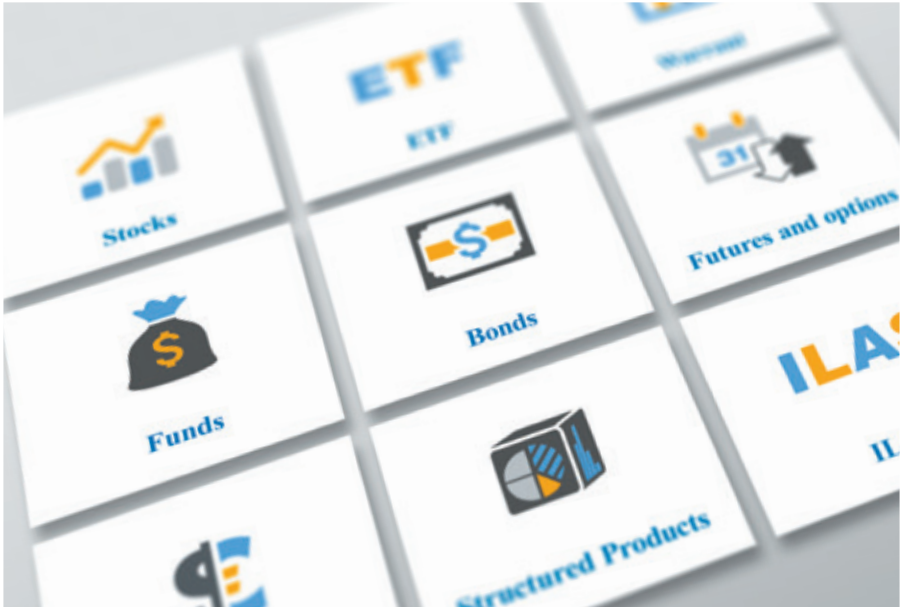


Investing plays an important role in financial planning as it may help you achieve your financial goals.

You can allocate the remaining amount for investing after you deduct necessary spending and savings from your income. A well-planned portfolio can help you ride out the ups and downs of the investment market and adjust your risk exposure.

Investing is a process to hold a portfolio that suits your risk appetite with a mix of investment products to keep your portfolio afloat in any economic climate.

Know your investments



When it comes to making financial decisions, it is important to adopt and apply responsible attitudes towards investing and money management. Each type of investment has its own features and downside risks. You should understand the nature and risk of any investment offered to you, and read the offering documents for details related to the investment products.

Get the facts before you invest

Find out whether fees and charges are payable by you directly, or are set against the investments. Costs are important because they lower your returns. Also, remember that past performance provides no guarantee of future price.

Check whether an investment vehicle is traded on an exchange or in the over-the-counter market. Liquidity varies between these markets, and this determines how easily you can sell your investment.

Always remember the golden rule: If an investment looks too good to be true, then it probably is!



Think before you invest

Consider both risk and return

As a general rule, the higher the return, the higher the risk. “Maximising returns by minimising risk” is an unrealistic objective. And “get-rich-quick” targets can expose you to inappropriate risks.

Understand your risk tolerance

Your risk tolerance is your ability and willingness to tolerate a decline in your investment values. Young people can usually afford to take higher risks, while older people tend to be more conservative.

Keep an eye on your liquidity

The higher your needs for ready cash, the more you should keep as liquid assets. You should also think about setting aside cash of at least three to six months of your regular expenses to meet any contingencies.

How strong are your financial resources?

If you only have a small amount to invest, then you might not be able to take too much risk. Avoid investing beyond your financial means.



Diversify portfolio risk



The easiest way for you to manage risks is to diversify your investments. Not all markets or asset classes move in tandem, and at times individual financial products within the same asset class will also perform differently. Diversification means investing in different asset classes, industries, regions and markets etc. A balanced portfolio tends to be less volatile than a single type of investment and therefore helps you reduce the risk.

To diversify your portfolio risk, first set the weight of each asset class in your portfolio, such as stocks, funds, bonds and foreign currencies etc. Then decide what investments to make within that asset class. Risk levels can vary within a single type of investment product – for example, a single country equity fund will generally be riskier than a globally diversified equity fund.



When investing, you have to limit your risks to a level acceptable to you. There is no such thing as a risk-free investment. Make sure you understand the possible downsides before committing to any investment.



Life events and you

Preparing for the golden years

Enjoying a comfortable lifestyle once we reach our golden years requires sound retirement planning and a long-term commitment.



Financial priorities

Whether you are planning for or already enjoying your retirement, capital preservation, prudent money management and adequate insurance coverage should top your priorities. Even if you plan to further build your retirement fund, you should take a cautious approach and conduct thorough risk assessment beforehand.

Keys to managing personal finances

- Determine when you want to retire and how much you will need to maintain your desired lifestyle. Then create a personal financial plan to guide you towards your financial goals and review the plan regularly as your priorities may change.
- Manage your retirement scheme well. Once you turn 65, you can withdraw your MPF benefits in a lump sum or keep investing them in the MPF system. Learn more about handling your MPF accrued benefits when you retire.
- Budgeting is an essential part of retirement living. Look for small ways to save and consider cutting back on your spending for non-essential items if necessary.
- Medical expenses can be a significant cost. Review your insurance needs early as health insurance premiums rise with age.
- When building your retirement fund, make sure you review your investment strategy to ensure it suits your needs. In particular, be cautious of making sizeable investments which may be impacted by the macro-economic environment.
- Protect your assets! Beware of financial scams targeting senior citizens – if something sounds too good to be true, it probably is.

STEP 6

Regularly review and adjust your financial plan



After formulating a financial plan, you should exercise strict discipline to follow the plan. Review your existing budget and investment portfolio from time to time to make sure they still fit your needs. In meeting your financial goals, it is considered best practice to review the performance of your portfolio regularly and rebalance your investments when necessary. This can help you avoid keeping a portfolio that may over-concentrate on certain asset classes.

Financial planning is a dynamic and continuous process. You should adjust your plan when there are significant changes in market conditions or when you enter a different life stage. You should make adjustments based on your resources, needs and situations to make sure your plan is in line with your financial goals.

+852 2700 6000 +852 2297 3300 info@ifec.org.hk



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