**NSS Exploring Economics (3rd Edition)**

**National Security Education Pack for Senior Secondary Economics**

**CONTENTS**

**Worksheet 1** Introduction: What does national security mean?

**Worksheet 2** Factors affecting national economic security

**Worksheet 3** How the Hong Kong government maintains Hong Kong’s banking and financial stability **SAMPLE**

⬩ *Topics of economic curriculum: H Money and Banking*

⬩ *Strands of national security education: Strand 7*

⬩ *Learning elements: Explore the relationship between monetary stability and national security*

⬩ *Related book and chapters: Ch 8, 9 and 11 of BK 6*

**Worksheet 4** Effects of Sino-US trade conflicts on national economic security

⬩ *Topics of economic curriculum: J International Trade and Finance*

⬩ *Strands of national security education: Strands 1 and 7*

⬩ *Learning elements: Explore topics related to economic security (e.g., trade disputes) and recognise the importance of safeguarding economic security*

⬩ *Related book and chapters: Ch 13 and 14 of BK 6*

**Worksheet 5** How can Hong Kong citizens fight against national security threats

**Worksheet 3: How the Hong Kong government maintains Hong Kong’s banking and financial stability SAMPLE**

|  |  |  |
| --- | --- | --- |
| **Book** | **Chapter** | **Related concepts** |
| 6 Money and Trade | 8 | Functions of the HKMA |
| 9 | Money contraction |
| 11 | Effects of money contraction on aggregate output |

**Source A:** An example of how a financial crisis may occur

Negative rumours about banking system are spread

Large groups of depositors withdraw money from banks at the same time

Money contraction and bank failures

Liquidity shortage for businesses (e.g., hard to get loans and higher interest rates paid)

Investment decreases, stock market declines and unemployment increases

**Financial crisis forms and economic depression results**

**Source B:** The functions of the Hong Kong Monetary Authority (HKMA)

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| The HKMA is responsible for the authorisation, regulation and supervision of banking business and the business of taking deposits in Hong Kong. The HKMA adopts a risk-based approach in evaluating banks’ safety and soundness, risk-management systems and internal controls. To ensure the safety of customer deposits, the HKMA requires banks to conduct their business prudently, maintain adequate capital, and manage their credit, liquidity, technology, money-laundering and other risks properly. |

*Source: Hong Kong Monetary Authority*

**Source C:** Hong Kong’s Deposit Protection Scheme

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| Under the Deposit Protection Scheme (DPS), all deposits denominated in Hong Kong dollars, Renminbi or any other currency deposits held with all licensed banks (Scheme members) are protected. The maximum protection is up to HK$500,000 per depositor per Scheme member, including both principal and interest. |

*Source: Hong Kong Deposit Protection Board*

**Source D:** How the Exchange Fund protected Hong Kong’s banking stability against global financial crises

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| --- |
| The global financial crisis broke out following the collapse of Lehman Brothers (雷曼兄弟) in mid-September 2008. In October 2008, the Hong Kong government announced the use of the Exchange Fund to provide a 100% guarantee for all Hong Kong dollar and foreign-currency bank deposits in Hong Kong to maintain banking and financial stability in Hong Kong.  During the Asian financial crisis in 1997-98, the Exchange Fund supported the value of the Hong Kong dollar, making it the only Asian currency to weather the Asian financial crisis. In August 1998, the Hong Kong government spent HK$118 billion (18% of the Exchange Fund at the time) to buy 33 constituent stocks of the Hang Seng Index, successfully supporting the stock market in a fight against currency speculators. |

*Source: Hong Kong Monetary Authority and summary of news report*

**Discussion**

**1.** With reference to Source A and your own knowledge of Economics, explain how a decline in depositors’ confidence might lead to an economic depression.

**2.** With reference to Source B and your own knowledge of Economics, determine whether the following is/are functions of the HKMA related to Hong Kong’s economic security. Put a ‘🗸’ in the appropriate box(s).

**a.** To ensure the safety of bank customers’ deposits 🞏

**b.** To evaluate banks’ safety and soundness 🞏

**c.** To keep the required reserves of deposit-taking institutions 🞏

**d.** To regulate banks to maintain adequate capital 🞏

**e.** To receive deposits from the public and offer reasonable interest rates 🞏

**f.** To act as the lender of last resort 🞏

**3.** Refer to Source C. How could the Deposit Protection Scheme (DPS) help prevent the economic security threat mentioned in (1)?

**4.** With reference to Source D and your own knowledge of Economics, state TWO important functions of the Exchange Fund.

**5.** Based on your answer in (1), what serious consequences might occur if the Exchange Fund did NOT hold sufficient assets?

**Answers:**

**1.** When there is a decline in depositors’ confidence, large groups of depositors withdraw their money from banks at the same time. As the banking system only keeps a fraction of its deposits as reserves, some banks might fail to meet the demand for withdrawals. Bank failures might occur and the economy might suffer from a liquidity shortage. As a result, investment would decrease and the stock market would decline. Aggregate demand would decrease and so would aggregate output, causing an economic depression.

**2.** a, b, d, f

**3.** With DPS, deposits of less than HK$500,000 will be fully protected. This can strengthen depositors’ confidence in the safety of their deposits. Thus, bank runs and their resulting consequences can be prevented.

**4.** To stabilise the value of the Hong Kong dollar (or maintain the stability of Hong Kong dollar exchange rate); to support and stabilise the financial markets

**5.** Free answer: Investors and the public would lose confidence in Hong Kong’s monetary and financial systems. Hong Kong’s monetary, banking and financial systems would become unstable. The government would lack the resources to fight against speculators and maintain public confidence in the value of the Hong Kong dollar.