THE WISDOMTREE EX-STATE-OWNED CHINA INDEX REBALANCE: WHAT'S CHANGED AND WHAT REMAINS?

Liqian Ren — Director of Modern Alpha
10/24/2022

We recently released the annual rebalance of the WisdomTree ex-State-Owned Enterprises China Index (CHXSOE) and WisdomTree Emerging Markets ex-State-Owned Enterprises Index (EMXSOE). China is about one-third of EMXSOE.

Here are some more details of the CHXSOE rebalance:

1. Tencent, Baidu and Weibo removed from the Index

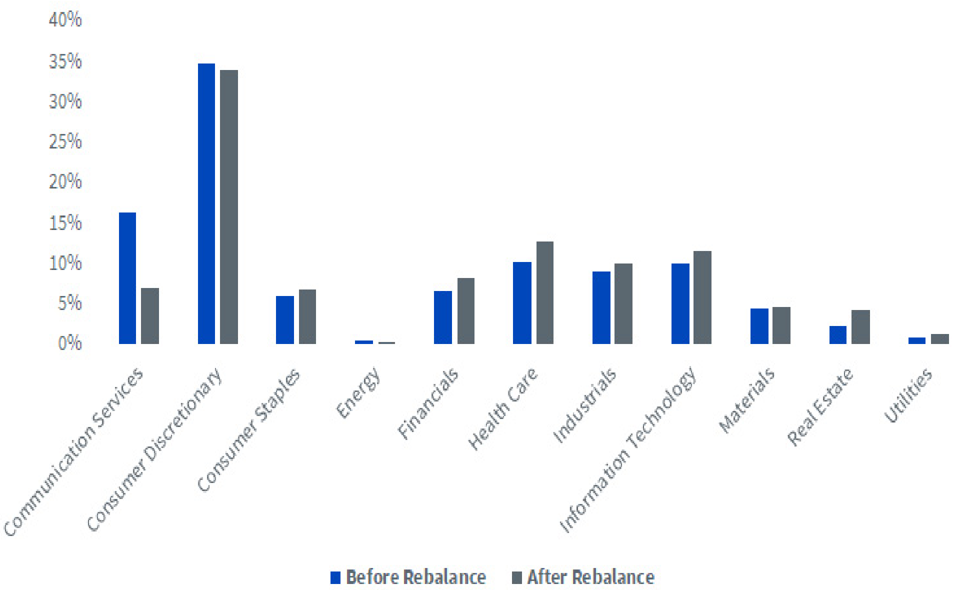
CHXSOE uses ESG data from Sustainalytics, a Morningstar company, to assess companies' compliance with the United Nations (UN) Global Compact Principles.

Due to their involvement in severe violations of freedom of expression in China, these companies were downgraded from being on a watchlist to being non-compliant with UN principles.

Dropping them from our Index results in 28% turnover.

WisdomTree's ex-stated-owned approach attempts to reduce government influence over corporate bottom lines. Sector exposures also change, resulting in smaller allocations to communication services.

WisdomTree ex-State-Owned Enterprises China Index Sector Weight



Sources: FactSet, WisdomTree, as of 9/30/22.

2. We continue moving into Hong Kong-listed shares and away from U.S. shares, with about a 94% weight in Hong Kong and China-mainland shares

Recently China's SEC equivalent—CSRC—signed a confidential agreement, allowing the U.S. super auditor PCAOB to inspect the intermediate audit files of Chinese companies listed in the U.S.

The U.S. press release mentioning this agreement is nuanced. It touts unfettered access, while a Chinese press release emphasized pre-screening of audit papers. By December, there will be clarity on whether the process meets the U.S. standards of having unfettered access to Chinese auditors' files.

We continue to prefer trading the Hong Kong-listed shares of companies when they reach sufficient liquidity, rather than the U.S.-listed shares. Under this guideline, we now have close to 94% weight of the Index in Hong Kong and mainland shares, protecting against a worst-case scenario. The Index still has 13 companies listed in the U.S., but they are a small weight as we evaluate how the U.S. and China work out the delisting issue.

3. We continue to maintain a 33% allocation to China A shares, higher than MSCI China index but lower than S&P China 500 index.

We've written before on a typical broad China equity index's exposure to A shares. Just taking the largest 500 Chinese public companies, China A shares would account for about 50%. We assess the listing location landscape of Chinese companies annually to decide the weight of A shares. The final portfolio reflects broad China equity exposure.

China is holding its 20th Party Congress, which is analogous to US Presidential election. China's political calendar runs every five years, and President Xi is expected to retain broad political power within foreseeable future.

Things move fast in the current unstable geopolitical environment and many political predictions about China 10 years back turned out to be quite off. We also caution clients to give healthy discounts on many current predictions of Chinese politics.

For those interested in more on this topic, please listen to this recent China of Tomorrow podcast episode.

For standardized performance and the most recent month-end performance click here NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

Related Blogs

+ Unpacking Your Portfolio's Exposure to China

+ China's Central Bank and Monetary Policy's Role in Its Economy

Related Funds

+ WisdomTree China ex-State-Owned Enterprises Fund

+ WisdomTree Emerging Markets ex-China Fund

+ WisdomTree Emerging Markets ex-State-Owned Enterprises Fund

View the online version of this article here.

IMPORTANT INFORMATION

U.S. investors only: Click here to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.

There are risks involved with investing, including possible loss of principal. Foreign investing involves currency, political and economic risk. Funds focusing on a single country, sector and/or funds that emphasize investments in smaller companies may experience greater price volatility. Investments in emerging markets, currency, fixed income and alternative investments include additional risks. Please see prospectus for discussion of risks.

Past performance is not indicative of future results. This material contains the opinions of the author, which are subject to change, and should not to be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. There is no guarantee that any strategies discussed will work under all market conditions. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This material should not be relied upon as research or investment advice regarding any security in particular. The user of this information assumes the entire risk of any use made of the information provided herein. Neither WisdomTree nor its affiliates, nor Foreside Fund Services, LLC, or its affiliates provide tax or legal advice. Investors seeking tax or legal advice should consult their tax or legal advisor. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.

The MSCI information may only be used for your internal use, may not be reproduced or re-disseminated in any form and may not be used as a basis for or component of any financial instruments or products or indexes. None of the MSCI information is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. Historical data and analysis should not be taken as an indication or guarantee of any future performance analysis, forecast or prediction. The MSCI information is provided on an "as is" basis and the user of this information assumes the entire risk of any use made of this information. MSCI, each of its affiliates and each entity involved in compiling, computing or creating any MSCI information (collectively, the "MSCI Parties") expressly disclaims all warranties. With respect to this information, in no event shall any MSCI Party have any liability for any direct, indirect, special, incidental, punitive, consequential (including loss profits) or any other damages (www.msci.com)

Jonathan Steinberg, Jeremy Schwartz, Rick Harper, Christopher Gannatti, Bradley Krom, Tripp Zimmerman, Michael Barrer, Anita Rausch, Kevin Flanagan, Brendan Loftus, Joseph Tenaglia, Jeff Weniger, Matt Wagner, Alejandro Saltiel, Ryan Krystopowicz, Kara Marciscano, Jianing Wu, Brian Manby and Scott Welch are registered representatives of Foreside Fund Services, LLC.

WisdomTree Funds are distributed by Foreside Fund Services, LLC, in the U.S. only.

You cannot invest directly in an index.

DEFINITIONS

ESG : An acronym for environmental, social and governance, ESG standards quantify the degree to which a company is socially responsible. .

United Nations Global Compact : A non-binding United Nations pact to encourage businesses and firms worldwide to adopt sustainable and socially responsible policies, and to report on their implementation.

Turnover : Tthe percentage of a portfolio that is sold in a particular month or year.

China Securities Regulatory Commission : A government ministry of the State Council of the People's Republic of China. It is the main regulator of the securities industry in China.

Public Company Accounting Oversight Board (PCAOB) : A nonprofit corporation created by the Sarbanes–Oxley Act of 2002 to oversee the audits of public companies and other issuers in order to protect the interests of investors and further the public interest in the preparation of informative, accurate and independent audit reports.

Liquidity : The degree to which an asset or security can be bought or sold in the market without affecting the asset's price. Liquidity is characterized by a high level of trading activity. Assets that can be easily bought or sold are known as liquid asset.

A-share : shares traded on the Shanghai and Shenzhen stock exchanges. This is contrast to Renminbi B shares which are owned by foreigners who cannot purchase A-shares due to Chinese government restrictions.

MSCI China Index : A free float-adjusted, market capitalization-weighted equity index designed to measure the performance of the Chinese equity market.

S&P China 500 Index : Designed to track the 500 largest and most-liquid Chinese companies while approximating the sector composition of the broader equity market.