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# THE OUTLOOK FOR CHINA

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China's financial reforms could lead to the increasing prominence of China in emerging market indexes as well as global investor portfolios. But does your benchmark provide a broad coverage of Chinese equities? We recently worked with S&P to license the [S&P China 500 Index](#), which provides exposure to all flavors of Chinese equities. Our Director of Research, Jeremy Schwartz, sat down with Michael Orzano, S&P's senior director of global equity indexes, to take a closer look at the S&P China 500 Index. Here is a quick excerpt from their conversation, with the full video below.

**Q: What is the macro outlook of some of the key factors driving the Chinese economy, and then, with those factors, what's your outlook given the current dynamics?**

**Jeremy Schwartz:** China is really the epicenter of global growth, both long run and short run. You saw a lot of optimism in 2017—emerging markets performing well. A lot of it's on the back of Chinese investment in infrastructure ahead of their 19th Party Congress that they just had in October. Now, China is generally trying to transition long run from an investment-led economy to a consumer-led economy.

You can see the investment buildup, massive construction over the years, big buildings everywhere. You could see an example just through high-speed rail. They have more high-speed railways than the rest of the world combined. But they really do want to emphasize a sort of new China and a consumer-driven China. And you can see remarkable progress.

You already see China is the largest auto market in the world. About 20 million cars every year. They're the largest purchaser of luxury goods. They have the most cellphone users, the most internet users. China really is a big player on global growth. And when you say, "What's happening in the global economy?," "What's happening in China?" is the most important question.

In the long run, when investors think about their portfolios, one of the big questions is whether they have enough representation of exposure to China. It's been hard to access before. But they're opening up to foreigners. And that hopefully should give people more of a reason to look at China as part of their global portfolio.

**Q: What are some of the unique challenges that people trying to access Chinese markets need to confront? And how does the S&P China 500 Index help alleviate some of those challenges?**

**Michael Orzano:** Given its legacy of capital controls in China, what I call a segmented-equity market developed where companies, a lot of companies, decided to list their shares offshore in order to have access to global capital markets. And then there are also companies listed onshore known as A-shares that are accessible to mainland Chinese investors.

Now, over the years, that's changed a bit. There's been a relaxation of those foreign investment restrictions. So, sitting there today, it's more sensible to look at China from a total China framework. Now, a lot of existing indexes that are widely used continue to look specifically at either offshore listings or onshore listings.

With the S&P China 500, the main goal was to create an index that would be representative of the complete Chinese equity market. First of all, from a completeness standpoint, that's important. But possibly even more important is that

there are material differences in the types of companies that are listed in different locations.

For example, onshore markets are heavily concentrated in banks and financial institutions. And then offshore, particularly in New York, most of the large technology companies are listed. So, it's really important to have that total comprehensive look at China.

**Q: How do you view market participants who want to access China? Where does China fit within global allocation strategies, in your view?**

**Jeremy Schwartz:** What Michael talked about there, getting the representative portfolio, you have new China and old China, and you want to get all China. I think making sure you get part of that new China as part of the portfolio is important. When we think about where the global market cap is today, a global market portfolio is roughly 50% U.S., 40% developed world and 10% emerging markets.

That's partly because of the float restrictions, and China is only about 3% of that total global pie. When you think about China's total size if you included all the state ownership, if they opened access to foreign investors, you could see a global portfolio that was really 15% China and had twice as much weight as in Japan, which is right now one of the biggest countries outside of the U.S.

You probably should have more China than 3% in terms of a global market portfolio. Getting that total representative China exposure with new China in addition to old China is really an important part of how to get access to that part of the market.

***See the full video here.***

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