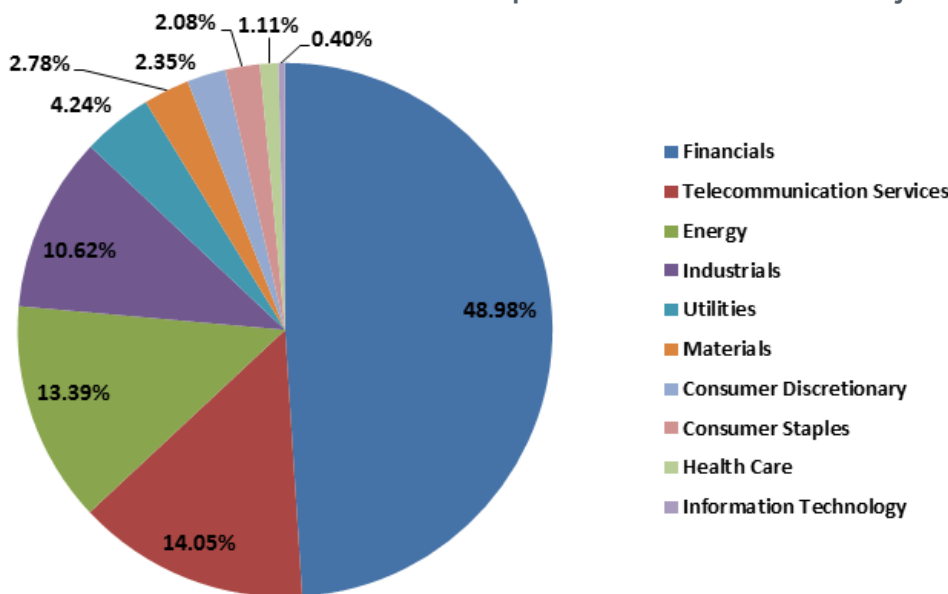


# CHINA AND STATE OWNED ENTERPRISES

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When investors allocate to emerging markets, they typically do so through broad-based [market cap- weighted](#) exposure. In doing so, investors are often making large [investments in China](#) and Chinese [state-owned enterprises \(SOE\)](#). More recently, we've seen growing interest in the [degree of exposure](#) to SOEs while avoiding the risk that may come from investing alongside emerging market governments, especially within China. State-owned enterprises are typically defined as companies that are either wholly or partially owned or operated by a government. Some investors believe that government ownership can negatively impact the operational aspects of a company because government-owned companies might be influenced by a broader set of interests, beyond generating profits for shareholders. **Characteristics of State-Owned Enterprises** State ownership levels can vary significantly among sectors and countries, depending both on a sector's significance for providing public goods or fostering economic growth and on the governmental structure. WisdomTree estimates that approximately 33% of the market cap of emerging market companies could be classified as SOEs, with governments owning more than 20% of shares. And China is the largest offender, representing more than 50% of the total SOE market cap. Within China, WisdomTree estimates that approximately 70% of the market cap could be classified as SOEs, and it is not surprising that the majority of the government ownership is within the Financials sector.<sup>1</sup>

**State-Owned Enterprises by China's Sector**



Sources: WisdomTree, Bloomberg, MSCI, as of 5/31/15. Market cap breakdown is based on constituents within the MSCI China Index. Subject to change. You cannot invest directly in an index. Index performance does not represent actual fund or portfolio performance. A fund or portfolio may differ significantly from the securities included in the index.

**Ownership Concentrated among Public Good Sectors**—Given that the Financials, Telecom, Energy and Utility sectors are among the most systemically important sectors to economic development, we are not surprised that the Chinese government tends to play a more active role in these sectors. A large percentage of the Chinese government's market cap ownership comes from the stakes it holds in the country's large financial institutions. These large state-owned banks are among the lowest-priced

areas of the entire emerging markets, with average [dividend yields](#) over 5% and [price-to-earnings \(P/E\) ratios](#) around 6x<sup>2</sup>. • **Less Ownership among Private Good Sectors**—Currently, the Chinese government is less involved in the Information Technology, Health Care and Consumer sectors (Discretionary and Staples). Companies in many consumer-focused sectors tend to be less vital to the strategic economic development and welfare of emerging market governments. These sectors also are often the focus for growth investors who see a burgeoning opportunity as [emerging market consumers](#) develop and increase their income and standard of living. **WisdomTree China ex-State-Owned Enterprises Index** Over the past year, WisdomTree created the [WisdomTree Emerging Markets ex-State-Owned Enterprises Index](#) a broad-based Index that provides exposure to emerging market stocks that are not state-owned enterprises. More recently, WisdomTree created the [WisdomTree China ex-State-Owned Enterprises Index](#) a broad-based Index that provides exposure to Chinese stocks that are not state-owned enterprises. We believe this Index will help investors monitor the performance of this important emerging market country and one of the potentially greatest risks that comes with investing within the market—the government. <sup>1</sup>Sources: WisdomTree, Bloomberg, as of 5/31/15. <sup>2</sup>Sources: WisdomTree, Bloomberg; refers to the four largest dividend-paying Chinese banks as of 5/31/15.

#### Important Risks Related to this Article

Investments in emerging, offshore or frontier markets are generally less liquid and less efficient than investments in developed markets and are subject to additional risks, such as risks of adverse governmental regulation and intervention or political developments. Investments focused in China increase the impact of events and developments associated with the region, which can adversely affect performance.

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**Market capitalization-weighting** : Market cap = share prices x number of shares outstanding. Firms with the highest values receive the highest weights in approaches designed to weight firms by market cap.

**WisdomTree China ex-State-Owned Enterprises Index** : Measures the performance of Chinese stocks that are not state-owned enterprises. State-owned enterprises are defined as government ownership of more than 20% of outstanding shares of companies.

**Dividend yield** : A financial ratio that shows how much a company pays out in dividends each year relative to its share price.