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# SUBSIDIZING CHINA'S SUPERPOWER ASPIRATIONS

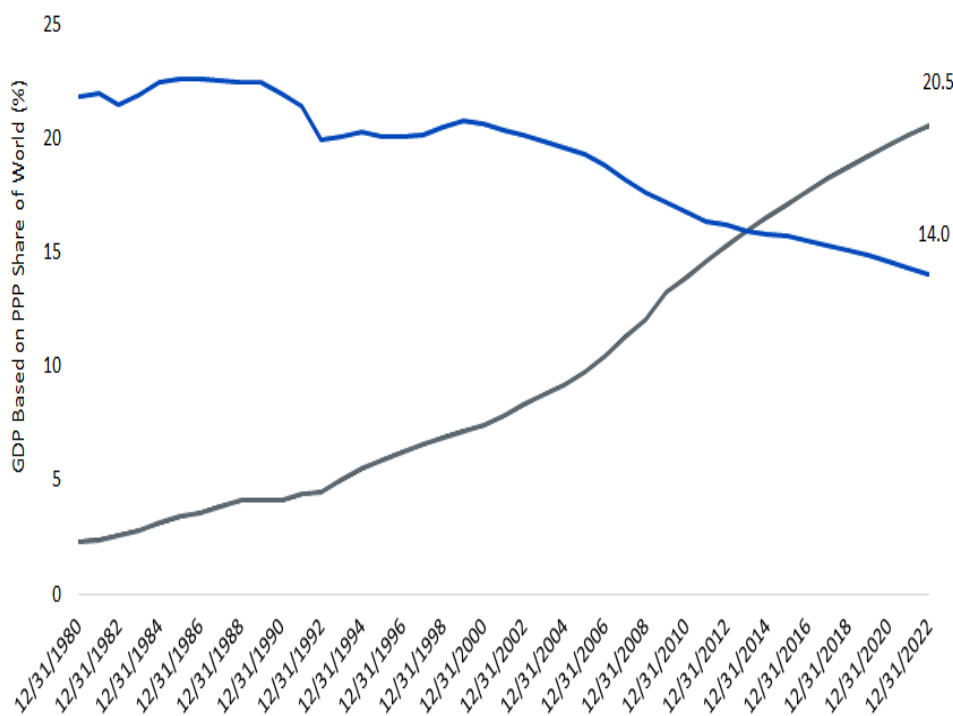
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Christine Lagarde, head of the International Monetary Fund (IMF), is warning that China's Belt and Road Initiative—the potentially multitrillion-dollar network of roads, rails, pipelines and other infrastructure across Eurasia—risks saddling unstable governments with unpayable debt. Because of the IMF's concerns, it plans to fund the China-IMF Capacity Development Center (CICDC) to train the Chinese to minimize the headaches caused by this century's Marshall Plan. If all goes according to plan, the Belt and Road project will connect land- and sea-based trading routes to cement China as the center of global commerce in a decade or two.

While China appears to be ascending into world superpower status in the coming decades, a \$100 investment in "global" equities allocates just \$3.51 to the country, if we track an index like the [MSCI All Country World \(ACWI\)](#).<sup>1</sup> That seems remarkably low for a country that is going head-to-head with the U.S. on the global stage.

It was only last year that MSCI announced it would be adding Chinese [A-shares](#), companies listed in Shanghai and Shenzhen, to its [MSCI Emerging Markets Index](#). That is late for an economy whose size surpassed the U.S. in 2014, at least on a [purchasing power parity](#) basis (see chart below).

## **China & U.S. Shares of Global Gross Domestic Product**



Source: IMF. All data in real time, with forecasts to 2022 (labels at end of time series for that year). Data compiled April 2018. Past performance is not indicative of future results.

## Covering China, Wherever the Listing

While some Chinese companies are only available in Shanghai or Shenzhen, others are listed solely in Hong Kong. Still others have [American Depositary Receipts \(ADRs\)](#) or are traded in Singapore.

The [WisdomTree ICBCCS S&P China 500 Fund \(WCHN\)](#) ETF tracks the [S&P China 500 Index](#), before fees and expenses, covering stocks in all those bourses. This index currently holds over 50% in local A-shares. MSCI, by contrast, is only starting to add A-shares securities up to a 5% inclusion factor in 2018, a small starting point. It's high time China has its own [S&P 500](#), especially if President Xi Jinping has anything to say about it.

## Going Out

Deng Xiaoping, ruler of China from 1978 to 1989, famously advised his country to “hide your strength, bide your time.” China’s great goal of the last four decades—development, development, development—was to happen quietly, with fingers crossed that the U.S., Japan and Western Europe wouldn’t get too frightened.

The hiding and biding is over. Xi’s 2017 Davos speech, replete with all the platitudes about smiling outreach, set the template for an acceleration of “Going Out,” Beijing’s euphemistically named colonialism in central Asia, Africa and client states as far as Latin America.

Recall that the big issue for about two minutes in 2015 was Britain’s fence-sitting on joining the Asian Infrastructure Investment Bank (AIIB), China’s answer to the IMF, World Bank and other such supranational bodies. The U.K. held strong for a bit, until fear of missing out caused it to relent and join the infrastructure bank. Development banks have metastasized through the years, and the AIIB is the new kid on the block, so the IMF will try to keep up.

And while U.S. politics splinters into ever-more-hostile factions, Europe is distracted by its own fragile fabric. Britain?

Tied up with Brexit. Meanwhile, the Asian hegemon flexes muscle. Look at the three votes against Syrian air strikes: China, Russia and Bolivia, the latter being one of several South American puppet governments. China is going to do what China wants to do.

Spreading its influence across the world's largest land mass—and beyond—is the new goal for China, and the IMF is going to help the cause, adding resources for the Belt and Road, as if China needs money. This is the new Marshall Plan, and with the U.S. "donation" to the IMF three times larger than China's,<sup>2</sup> the West is paying for its own relative decline.

Beijing is sitting on a \$3.1 trillion [foreign exchange](#) reserve fortress, is the global leader in mobile payments, is home of Amazon-esque Alibaba and Tencent, is number two in international patent applications, and on and on.<sup>3</sup> And the U.S., Japan, France—all of the usual suspects—are funding the IMF, thus training the Chinese in their industrialization efforts.

Allocate accordingly.

Xi, ruler for life, intends to plant a figurative flag as the global leader of the 21st century. Again, China's current weight in MSCI ACWI is 3.5%, the same amount as France.<sup>4</sup> If the future China looks anything like the U.S. in the 20th century or Britain in the 19th, 3.5% of the pie is off the mark.

Learn more about WCHN.

<sup>1</sup>Source: MSCI ACWI, as of 12/31/17.

<sup>2</sup>Source: IMF Members' Quotas and Voting Power, and IMF Board of Governors, 4/15/18. China's quota is 6.4% of the total, while the U.S. has the largest quota, at 17.5% of the total.

<sup>3</sup>Source: Statista, for 2017. Click [here](#) for current holdings of WCHN. [links to fund page]

<sup>4</sup>Source: MSCI, as of 12/31/17.

#### Important Risks Related to this Article

There are risks associated with investing, including possible loss of principal. Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. The Fund focuses its investments in China, including A-shares, which include risk of the RQFII regime and Stock Connect program, thereby increasing the impact of events and developments associated with the region, which can adversely affect performance. Investments in emerging or offshore 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. The Fund's exposure to certain sectors may increase its vulnerability to any single economic or regulatory development related to such sector. As this Fund can have a high concentration in some issuers, the Fund can be adversely impacted by changes affecting those issuers. The Fund will be required to include cash as part of its redemption proceeds which introduces additional risks, particularly due to the potential volatility in the Chinese market and market closures. The Fund invests in the securities included in, or representative of, its index regardless of their investment merit and the Fund does not attempt to outperform its index or take defensive positions in declining markets. Due to the investment strategy of this Fund, it may make higher capital gain distributions than other ETFs. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

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.

For more investing insights, check out our [Economic & Market Outlook](#)

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## **DEFINITIONS**

**MSCI All Country World Index** : a broad global equity benchmark that represents large and mid-cap equity performance across 23 developed and emerging market countries.

**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 Emerging Markets Index** : a broad market cap-weighted Index showing performance of equities across 23 emerging market countries defined as “emerging markets” by MSCI.

**Purchasing power parity** : Academic concept stating that exchange rates should adjust so that equivalent goods and services cost the same across countries, after accounting for exchange-rate differences.

**ADRs** : American Depositary Receipts, shares of a firm incorporated outside the U.S. but issued by a global bank and traded in the U.S., denominated in U.S. dollars.

**S&P China 500 Index** : Comprises 500 of the largest, most liquid Chinese companies while approximating the sector composition of the broader Chinese equity market. All Chinese share classes including A-shares and offshore listings are eligible for inclusion.

**S&P 500 Index** : Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor’s Index Committee designed to represent the performance of the leading industries in the United States economy.

**Foreign Exchange (FOREX, FX)** : The exchange of one currency for another, or the conversion of one currency into another currency.