

WisdomTree MINDS ON THE MARKETS



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India Is Starting to Rival China in Emerging Indexes

Week of April 23, 2024

Don't look now, but there could be a new sheriff in town in some of the major indexes. It was not long ago—just before the 2020s arrived—that most emerging markets indexes allocated a single-digit proportion to India. It was a sharp contrast to China's dominant proportion, which would often exceed the weight of all the other countries combined.

Times changed. Over the last five years, the MSCI India Index has returned an annualized 9.8%, while its neighbor has gone the other way: MSCI China's total return has declined at a 7% annual clip.

Suddenly, we have a situation where the MSCI Emerging Markets Index's China weight has fallen to 25% while India's proportion has risen to 17%. In the FTSE Emerging Markets Index, the gap is narrower: China comprises 27% of that index, and India 22%.

Though India has been one of the better-performing countries in recent years, the country still flies under the radar of many American investors. For example, consider CNBC's website. Click on the Asian stock market section, and quotes for five country indexes will flash before you: the ASX 200 (Australia), Nikkei 225 (Japan), KOSPI (Korea), Hang Seng (Hong Kong) and Shanghai Composite (China). India is snubbed.

Because of the sheer overwhelming force of the U.S. in the market-cap league table, India remains an afterthought in global allocations, comprising just 1.8% of the MSCI All Country World Index. It is an intriguing situation because many forecasters see India leapfrogging Japan and Germany to become the world's third-largest economy by 2030. If Goldman has it right, India will jump into the first slot come 2075.

There are catalysts for equity index inclusion, too, notably in the form of the index houses getting around to adding India on the fixed income side of the business. JP Morgan is a huge player in bond indexing. This summer will witness India being added to its much-followed JPM GBI-EM Global Diversified Index, with the full phase-in finished by March 2025. However, we should note that another major index house, FTSE Russell, has decided to hold off on boosting India in fixed income for now.

Nevertheless, game this out for a day in the life inside the four walls of some active money management firm.

The fixed income team suddenly finds itself under pressure to buy up Indian sovereign and corporate bonds because the benchmark evolved on them. On the other side of the office sits the equity team, which may or may not have bought too much China in COVID-19's early days. Because India used to be "just another country" in their emerging markets benchmark, the extent of their India research is possibly on the light side.

Now these two analysts, one fixed income, one equity, are both in something of a scramble.

Before, maybe the fixed income guru was doing zero India research. After all, the country wasn't in the benchmark, so why bother? But now comes the deep dive. Meanwhile, the equity research person had just a small handful of India longs "before" because the country was not yet such a heavy allocation in the benchmark.

But now the indexes are changing on them both; pencils are being sharpened, and notes are being compared. In money management, you will have to look hard to find forces more powerful than portfolio drift and benchmark index inclusion when it comes to hunkering down your research process. Inside emerging markets, India has both.

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Glossary

ASX 200 Index: An index that tracks the performance of the 200 largest companies listed on the Australian Securities Exchange.

Corporate bond: A debt security issued by a corporation.

Emerging market (EM): Characterized by greater market access and less potential for operational risks when compared to frontier markets, which leads to a larger base of potentially eligible investors.

FTSE Emerging Markets Index: Provides investors with a comprehensive means of measuring the performance of the most liquid large- and mid-cap companies in the emerging markets.

Hang Seng: A market capitalization-weighted index that tracks the daily changes of the 50 largest and most liquid companies on the Hong Kong Stock Exchange.

JPM GBI-EM Global Diversified Index: A market capitalization-weighted index that tracks the traded market for local emerging market government bonds.

Korean Composite Stock Price Index (KOSPI): A market-weighted index that tracks the South Korean stock exchange.

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.

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

MSCI Emerging Markets Index: A free float-weighted equity index that captures large- and mid-cap representation across emerging markets (EM) countries.

MSCI India Index: A market capitalization-weighted index designed to measure the performance of the large- and mid-cap segments of the Indian equity market.

Nikkei 225 Stock Average Index: A price-weighted average of 225 top-rated Japanese companies listed in the First Section of the Tokyo Stock Exchange.

Shanghai Composite Index: A stock market index of all A shares and B shares that are traded on the Shanghai Stock Exchange.

Sovereign bond: A debt security issued by a government to raise money for its operations, pay down debt and pay interest on current debt.

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