

# MSCI China A-Share Inclusion: A Long Term Catalyst For The Mainland Chinese Equity Market

Overview of the KraneShares MSCI  
China A Share UCITS ETF (ticker: KBA)



# Introduction to KraneShares

## About KraneShares

Krane Funds Advisors, LLC is the investment manager for KraneShares ETFs. The firm is focused on providing investors with strategies to capture China's importance as an essential element of a well-designed investment portfolio. KraneShares ETFs represent innovative, first to market strategies that have been developed based on the firm and its partners' deep knowledge of investing. These strategies allow investors to stay current on global market trends and provide meaningful diversification.

In 2019, KraneShares established a London headquarters to better deliver its renowned China-focused ETFs to European investors. In addition to launching Europe-specific versions of its most popular US-listed funds, KraneShares also develops strategies tailored to meet the specific needs of its European clients.





**KraneShares MSCI  
China A Share UCITS  
ETF**

### Investment Strategy:

KBA is benchmarked to the MSCI China A Index which captures large and mid-cap representation across China securities listed on the Shanghai and Shenzhen exchanges (A-shares). Over the coming years, MSCI will complete the incremental inclusion of China A-shares into their Global Standard Indexes, including the MSCI Emerging Markets Index, which may potentially benefit the securities KBA holds today. The MSCI China A Index is designed for global investors accessing the A-share market using the Stock Connect framework and is calculated using China A Stock Connect listings based on the offshore RMB exchange rate (CNH).

### MSCI China A-Share Inclusion Overview:

- China A-Shares are vastly underrepresented in global indexes. While the United States has a weight of 58.25% in the MSCI All Country World Index, China only has a weight of 5.20%<sup>1</sup>.
- MSCI is incrementally realigning China's overall weight in their Global Standard Indexes through the inclusion process, and by the end of 2019, MSCI's definition of China included 264 large-cap and 172 mid-cap A-Share securities, including 30 securities from the ChiNext board<sup>2</sup>.
- Upon completion, China A-Shares are predicted to account for about 20% of the MSCI Emerging Market (EM) Index<sup>3</sup>.

### MSCI China A Index Overview:

- The Index captures large and mid-cap equities listed on the Shanghai and Shenzhen stock exchanges and reflects the full 2019 inclusion of China A-Shares in the MSCI Emerging Markets Index.
- On March 11, 2019, the Hong Kong Stock Exchange announced a license agreement with MSCI to introduce futures contracts on the MSCI China A Index<sup>4</sup>.
- There are a total of 475 constituents<sup>1</sup> giving investors diverse exposure to A-Shares.

1. Data from MSCI as of 30/Sep/2020.

2. MSCI, "MSCI Will Increase the Weight of China A Shares in MSCI Indexes", 28/Feb/2019.

3. Data from MSCI as of 30/Sep/2020

4. HKEx, MSCI China A Index Futures, 11/Mar/2019.

# The Evolution of China's Capital Markets and KraneShares



**Oct 2016**  
China's currency, the RMB, designated a reserve currency by the International Monetary Fund



1990

Shanghai and Shenzhen Stock Exchanges launch

2011

- RQFII is established**
- Allowing international access to A-share market with daily liquidity
  - First international funds with Interbank Bond Market exposure approved

Mar 2014

**KraneShares Boserá MSCI China A-Share ETF (Ticker: KBA) launches**  
KraneShares partners with Boserá Asset Management to list KBA, the first MSCI-linked China A-Share ETF in the U.S.

MSCI puts China A-Shares up for inclusion within their Global Standard Indexes

Nov 2014

**Shanghai Hong Kong Stock Connect launches**  
Eligible Shanghai listed stocks now freely tradable through international brokerage accounts

Jun 2017

MSCI announces inclusion of A-Shares in Global Standard Indexes starting June 1<sup>st</sup>, 2018

Oct 2017

CICC (China International Capital Corporation) acquires a 50.1% majority stake in Krane Funds Advisors, LLC

March 2019

HKEX launches futures contracts for the MSCI China A Index

1990

2002

**QFII is established**  
allowing the first international access to A-share market

2013

**KraneShares launches its first U.S. listed China ETF**



Dec 2014

**KraneShares E Fund China Commercial Paper ETF (Ticker: KCONY) Launches**  
KraneShares partners with E Fund Asset Management to list KCONY, giving investors exposure to China's Interbank Bond Market

Aug 2016

**Shenzhen Hong Kong Stock Connect launches**  
Eligible Shenzhen listed stocks now freely tradable through international brokerage accounts

Mar 2018

Bloomberg announces it will add China's Interbank Bond Market to the Bloomberg Barclays Global Aggregate Indices starting April 2019

Sep 2018

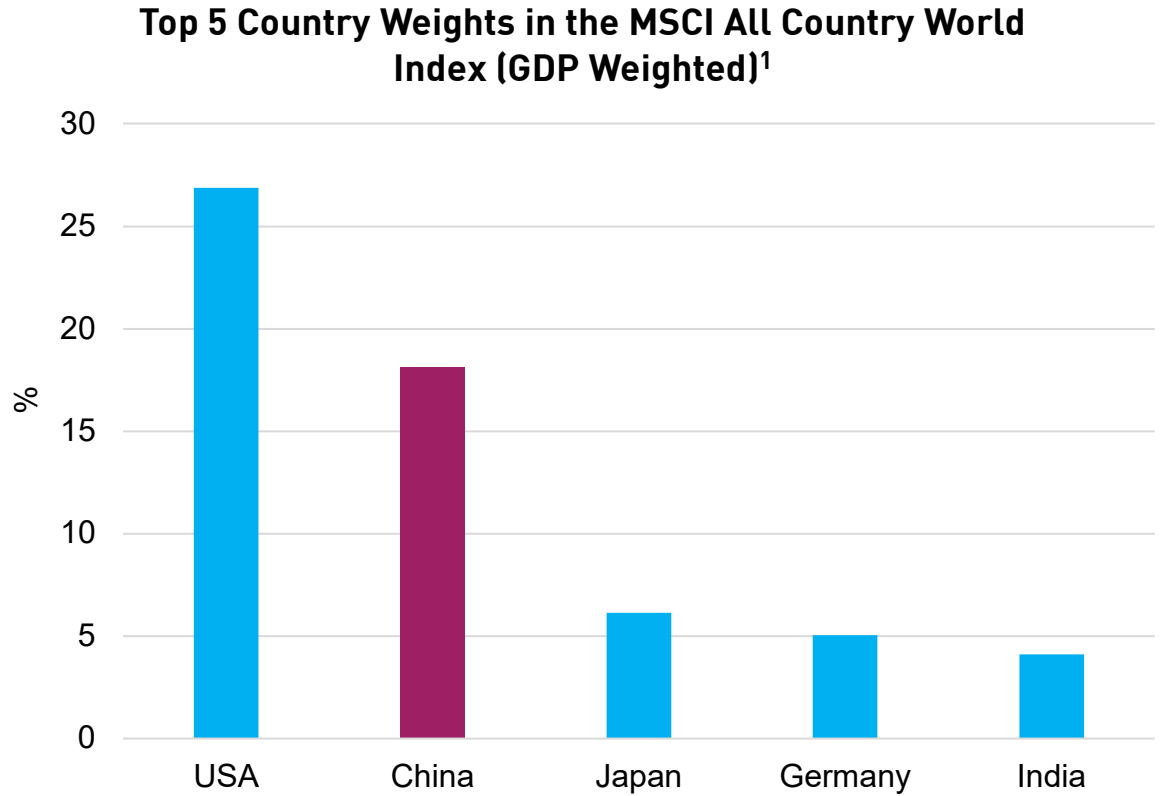
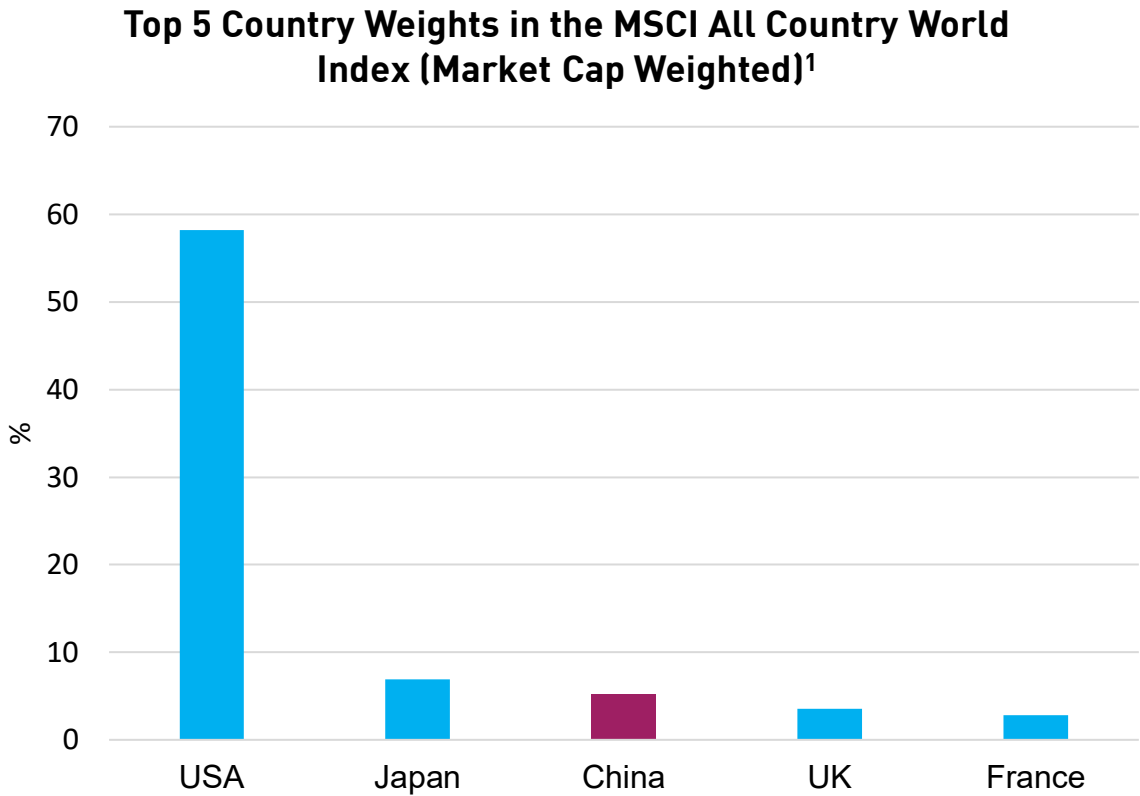
First phase of China A-Share Inclusion completed

Second phase of China A-Share Inclusion scheduled for completion

Nov 2019

# The China A-Share market is too big to ignore.

Even though China is the world’s second largest economy and stock market, China A-Shares are still underrepresented in global capital markets.

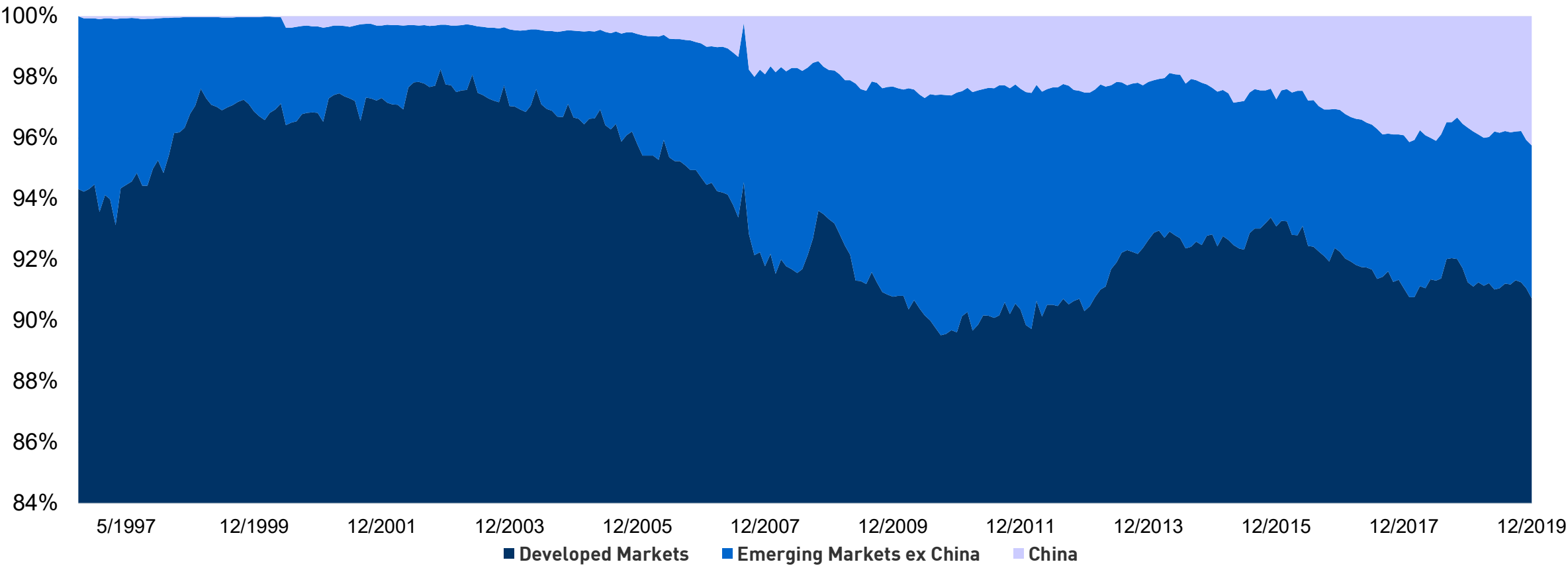


1. Data from MSCI as of 30/Sep/2020, retrieved 30/Sep/2020. See page 17 for index definitions

# Emerging Market Evolution

- China’s weighting in the MSCI ACWI Index has grown since 1997 but remains a small percentage overall.
- We believe China will occupy a larger portion of both the MSCI All Country World Index and investors’ portfolios in general as its markets continue to open up.

Historical Developed and Emerging Market Allocations within the MSCI ACWI Index



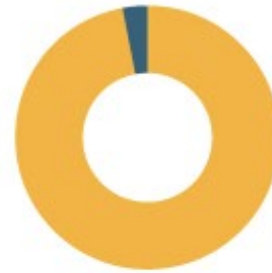
Data from Morningstar as of 31/Dec/2019. See page 16 for index definitions.

## The Index Matters

MSCI is a trusted index provider for the largest global investment managers.



**>\$14.8 trillion**  
in equity assets are  
estimated to be  
benchmarked to  
MSCI indexes<sup>1</sup>



**99 of top 100**  
global investment  
managers are  
MSCI clients<sup>2</sup>



**1040+**  
ETFs are based on  
MSCI indexes, more than  
any other index provider<sup>3</sup>



**94%**  
of US pension fund  
assets invested in  
global equities are  
benchmarked to MSCI<sup>4</sup>

<sup>1</sup> As of June 30, 2018, as reported on September 30, 2018 by eVestment, Morningstar and Bloomberg, retrieved 30/Jun/2020.

<sup>2</sup> Based on latest P&I AUM data and MSCI clients as of March 2018, retrieved 30/Jun/2020.

<sup>3</sup> As of September 2018, retrieved 31/Mar/2020; defined as each share class of an exchange traded fund, as identified by a separate Bloomberg ticker. Only primary listings, and not cross-listings, are counted.

<sup>4</sup> As of Dec 2016, according to Intersec LLC, retrieved 30/Jun/2020.

# **MSCI's current Global Standard definition of China only represents a small portion of China's total market.**

The MSCI China Index was historically limited to Chinese companies listed on the Hong Kong Stock Exchange. Recently, MSCI expanded this definition to include US-listed Chinese companies and China A-shares. This definition represents only a small percentage of Chinese stocks.

## **MSCI's Current Global Standard Definition of China**

### **MSCI China Index**

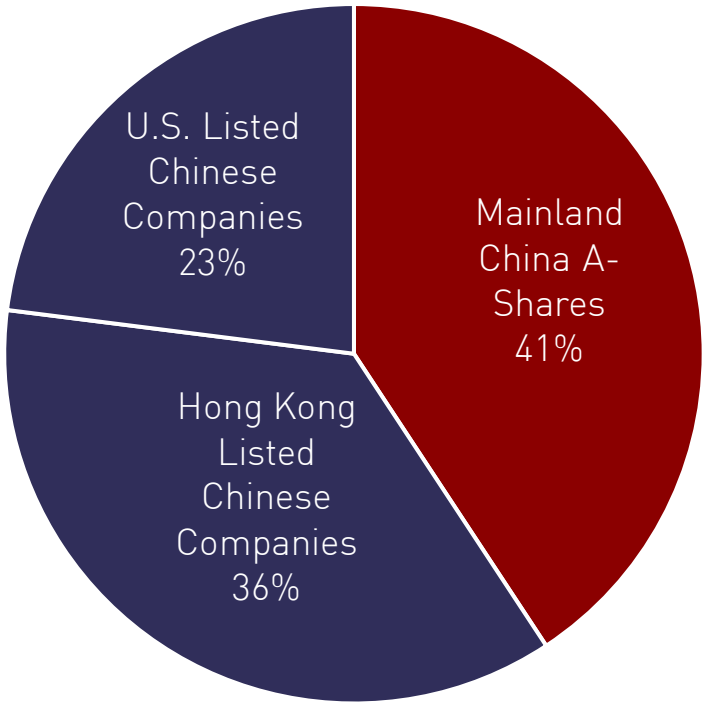
Hong Kong and US = 88.24%  
 China A-Shares = 11.76%  
 714 Stocks

## **MSCI's Definition of Entire Mainland A-Share Market**

### **MSCI China A Onshore IMI Index**

Shanghai and Shenzhen only  
 2,865 Stocks

## **SHARE CLASS BREAKDOWN OF THE MSCI CHINA ALL SHARES INDEX**

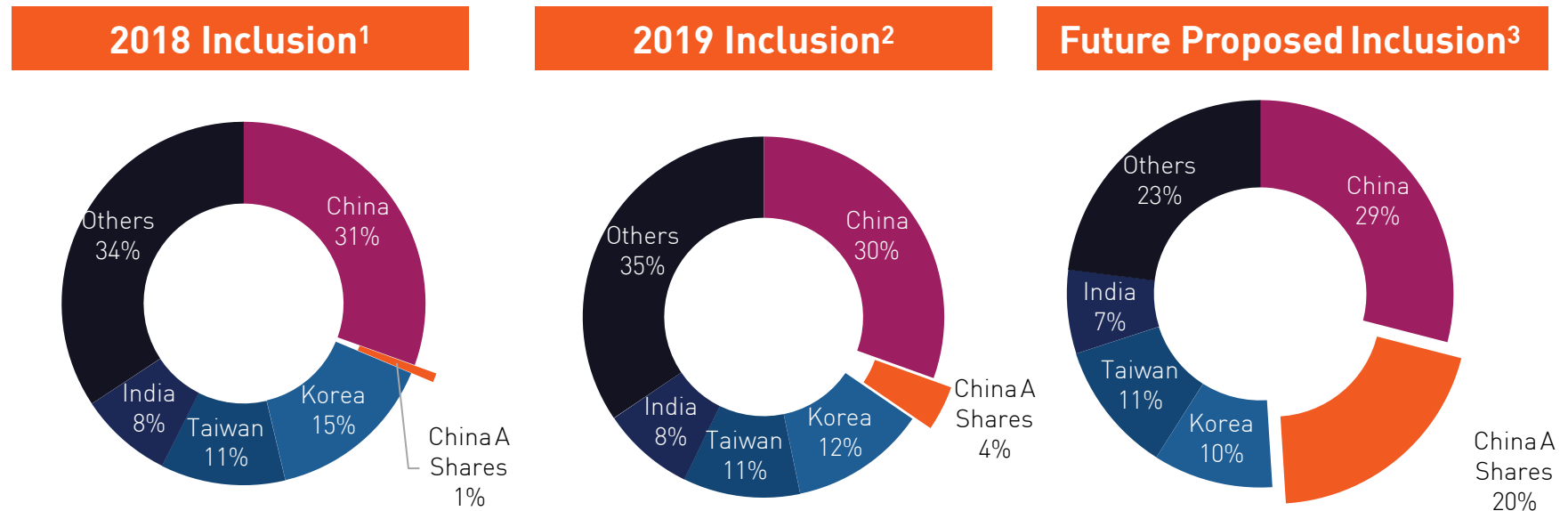


**On February 28, 2019, MSCI made a larger than expected China A-Shares inclusion announcement. MSCI increased the inclusion factor of China A-Shares in their Global Standard Indexes from 5% to 20% in 2019.**

Currently, **\$1.5 trillion** track the MSCI EM Index. **Up to \$360B** are expected to be reallocated to China A-Shares after full inclusion.

- On September 3, 2018 MSCI completed the first 5% of the inclusion process for China A-Shares within the MSCI Emerging Markets Index.
- At the end of 2019, MSCI's inclusion process for China A-Shares was 20% complete.
- The full proposed inclusion weight is projected to reach 20% of the Emerging Markets Index.
- We believe multiple inclusions could provide a sustained catalyst for the outperformance of the Mainland market.

### China A-Share Inclusion in MSCI EM



1. MSCI.com/China, retrieved 9/30/2020

2. "MSCI Will Increase The Weight Of China A Shares In MSCI Indexes" MSCI, Feb. 2019, retrieved 9/30/2020

3. Data from MSCI as of 6/30/2020, retrieved 9/30/2020

Source: MSCI as of 12/31/2019. See page 17 for index definitions. Country weights are rounded to the nearest percentage point. Please note that the inclusion factor percentage represents the percentage of the inclusion process that has been completed and not the resulting weight of China A-Shares in the MSCI EM Index.

## We believe that the MSCI China A Index has distinct advantages over the CSI 300 Index.

- The CSI 300 Index, originally built for domestic Chinese investors, consists of the 300 largest China A-Share stocks ranked by market capitalization.
- In comparison, the MSCI China A Index currently tracks 475 securities deemed most suitable for international investors by MSCI.<sup>1</sup>
- Over 80% of the CSI 300 constituents are included in the MSCI China A Index, which contains a larger set of securities<sup>2</sup>.
- We believe gaining exposure to China A-Shares through an MSCI index provides international investors with several distinct advantages.

MSCI China A Index and CSI 300 Index Comparison <sup>2</sup>			
	MSCI China A Index	CSI 300 Index	MSCI Advantage
<b>Index Construction Methodology</b>	Based on MSCI's Global Investable Market Index (GIMI) methodology	Largest 300 China A-share companies ranked by full market capitalization	Consistent with MSCI EM and MSCI ACWI which enables building and monitoring portfolios in a cohesive manner
<b>Eligible Universe</b>	Only A-shares that can be traded through Stock Connect	Any A-share listed in Shanghai and Shenzhen Stock Exchanges	No QFII or RQFII quota restraints
<b>Foreign Ownership</b>	Takes into account Chinese regulator's foreign ownership limits of 30%	Does not consider foreign ownership limits, creating potential for tracking error	Tailored for foreign investors
<b>Size Segmentation</b>	Large Cap Size Segment targets 70%, Standard Size Segment targets 85%, and IMI Size Segment targets 99% of the coverage universe	Uses a fixed number of constituents methodology	Designed to dynamically reflect the growing China capital markets
<b>Index Review</b>	Semi-Annual and Quarterly Index Reviews	Semi-Annual Reviews	More timely reflection of the market

1. Data from Bloomberg and CSI as of 30/Sep/2020, calculated by KraneShares.

2. Data from Bloomberg as of 30/Jun/2020. See page 17 for index definitions.

## The MSCI China A Index stocks are the largest and most liquid stocks in the A-Share market.

- There are currently 4,363 A-Shares listed in Mainland China.
- A-Shares contain predominantly mega cap and large cap securities in the top decile of the Mainland market in terms of market capitalization and 30-day average trading volume.

## China Mainland Market Capitalization and 30-day Average Trading Volume Decile Breakdown as of 31/Dec/2019

		Average Market Cap	30 Day Average Daily Volume
<b>93%</b> KBA Net Assets	<b>1</b>	<b>15.0 B</b>	<b>34.0 M</b>
<b>7%</b> KBA Net Assets	<b>2</b>	<b>2.6 B</b>	<b>20.7 M</b>
<b>0%</b> KBA Net Assets	<b>3</b>	<b>1.5 B</b>	<b>16.2 M</b>
	<b>4</b>	<b>1.0 B</b>	<b>14.0 M</b>
	<b>5</b>	<b>738.8 M</b>	<b>10.7 M</b>
	<b>6</b>	<b>571.0 M</b>	<b>9.0 M</b>
	<b>7</b>	<b>444.2 M</b>	<b>7.7 M</b>
	<b>8</b>	<b>334.7 M</b>	<b>5.7 M</b>
	<b>9</b>	<b>230.4 M</b>	<b>4.8 M</b>

## Mainland China A-Share equities exhibit low correlation to other global markets.

As Emerging Markets (EM) have become more correlated with Developed Markets over the years, the diversification benefits of EM investing have largely diminished.

- Frontier Markets, countries whose stocks are less mature than those in EM, still have relatively low correlations with the rest of the world.
- Remarkably, China A-Shares exhibit an even lower correlation to the MSCI All Country World Index than Frontier Markets.

### MSCI Indexes Correlation to MSCI China A Index

	ACWI	EAFE	EM	USA	China	Frontier	China A
ACWI	1	0.942	0.837	0.955	0.692	0.539	0.349
EAFE	0.942	1	0.807	0.817	0.664	0.551	0.317
EM	0.837	0.807	1	0.707	0.867	0.522	0.421
USA	0.955	0.817	0.707	1	0.573	0.475	0.31
China	0.692	0.664	0.867	0.573	1	0.423	0.583
Frontier	0.539	0.551	0.522	0.475	0.423	1	0.28
<b>China A</b>	0.349	0.317	0.421	0.31	0.583	0.28	1

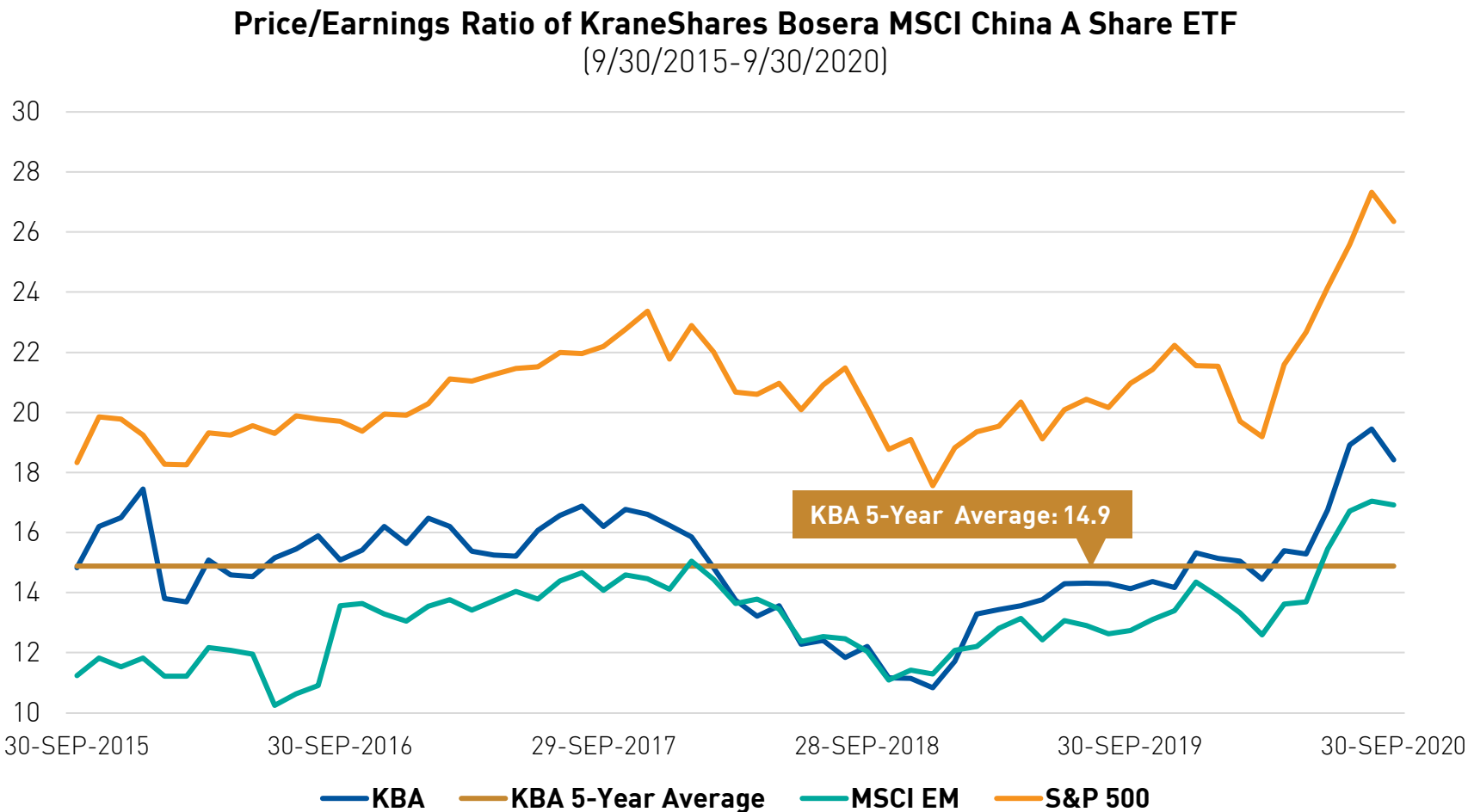
- MSCI ACWI Index (ACWI) - All Country World Index
- MSCI EAFE Index (EAFE) - Europe, Australasia and Far East
- MSCI Emerging Markets Index (EM) - Emerging Markets
- The MSCI USA Index (USA) - United States of America
- MSCI China Index (China) - Chinese companies listed in Hong Kong & USA
- MSCI Frontier Markets Index (Frontier) - Frontier Markets
- MSCI China A Index (China A) - Chinese companies listed on Shanghai and Shenzhen Stock Exchanges

Source: Table from Bloomberg, weekly correlation from 31 March 2010 to 31 March 2020

Index returns are for illustrative purposes only. Index performance returns do not reflect any management fees, transaction costs or expenses. Indexes are unmanaged and one cannot invest directly in an index. See page 16 for index definitions.  
Past performance is no guarantee of future results.

Current Valuations in the Mainland Chinese equity market are lower than those in the US equity market.

KBA is currently close to its long run Price-Earnings (P/E)<sup>1</sup> average.



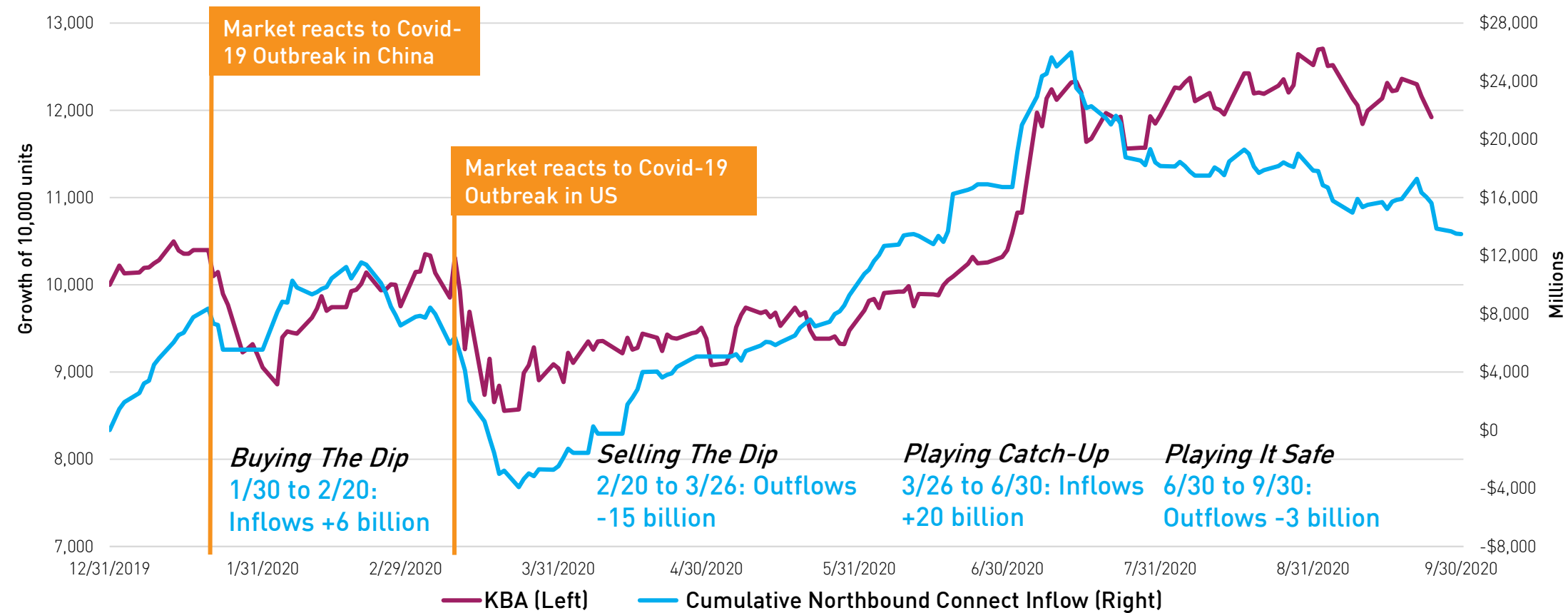
Data from FactSet as of 30/Sep/2020. See page 17 for index definitions.

<sup>1</sup>The price-earnings ratio (P/E Ratio) is the ratio for valuing a company that measures its current share price relative to its per-share earnings.

Foreign investors largely refrained from buying the dip in Mainland equities surrounding the COVID-19 pandemic and have, for the most part, allocated to catch up with the market rebound since its bottom in mid-March.

Year to date, foreign investors have bought \$13.5 billion\* worth of A-shares through Stock Connect.

Northbound Connect Flows vs. KBA Performance



Data from Bloomberg as of 30/Sep/2020, \*year-to-date as of 30/Sep/2020. See page 17 for index definitions.

## KraneShares CSI China Internet UCITS ETF

KraneShares CSI China Internet UCITS ETF is “A sub fund of KraneShares ICAV (the “ICAV”). The ICAV is authorised as a UCITS in Ireland and regulated by the Central Bank of Ireland.

For Investors in the United Kingdom (UK). Investors should read the Key Investor Information Document and Prospectus prior to investing. The Fund seeks to track the performance of an index composed of companies from developed countries.

### Investment Strategy:

KWEB (the Fund) tracks the CSI Overseas China Internet Index (the Index) and invests in China based companies whose primary business or businesses are focused on internet and internet-related technology. These companies are publicly traded on either the Hong Kong Stock Exchange, NASDAQ Stock Market, or New York Stock Exchange.

### KWEB Performance History as of 30/Sep/2020:

	Cumulative %			Average Annualized %			
	3 Mo	6 Mo	Since Inception	1 Yr	3 Yr	5 Yr	Since Inception
Fund NAV	8.80%	49.68%	67.64%	62.82%	–	–	32.00%
Index	9.09%	49.93%	70.55%	63.86%	8.02%	19.18%	33.18%

**The performance data quoted represents past performance. Past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investors shares, when sold or redeemed, may be worth more or less than their original cost and current performance may be lower or higher than the performance quoted. For performance data current to the most recent month end, please visit.**

Index returns are for illustrative purposes only. Index performance returns do not reflect any management fees, transaction costs or expenses. Indexes are unmanaged and one cannot invest directly in an index.

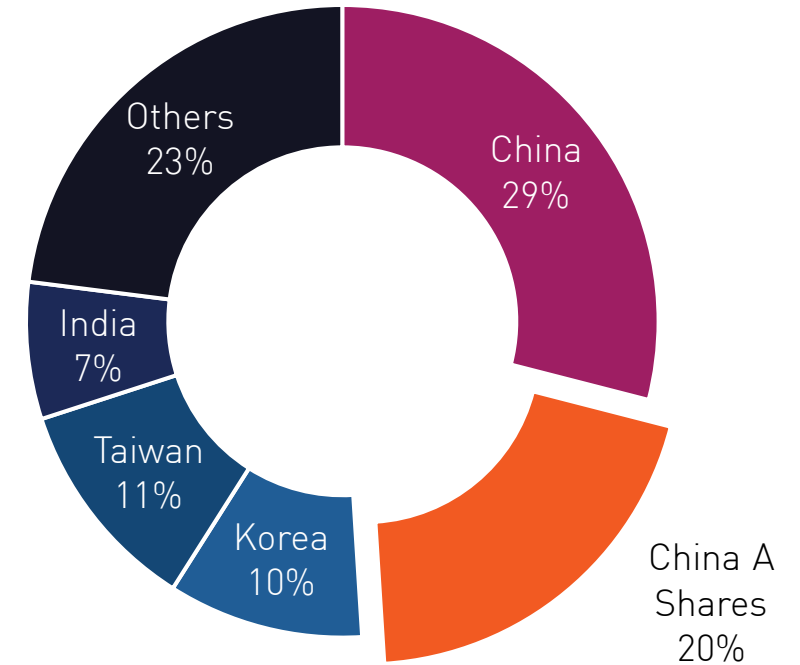
Fund Details	Data as of 30/Sep/2020
Listed Exchanges	LSE, AEX, ISE
SEDOL	BGLRQN6
ISIN	IE00BFXR7892
Total Annual Fund Operating Expense	0.75%
Inception Date	20/11/2018
Distribution Frequency	Accumulating
Index Name	CSI Overseas China Internet Index
Net Assets	\$182,313,112
Number of Holdings	34
UK Reporting Fund Status	Reporting Fund
Investment Structure	UCITS
Base Currency	USD

Top 10 Holdings as of 30/Sep/2020 Holdings are subject to change.	Ticker	%
ALIBABA GRP-ADR	BABA	10.79
TENCENT HOLDINGS LTD	700 HK	8.73
MEITUAN DIANPING-CLASS B	3690 HK	7.90
JD.COM INC-ADR	JD	7.13
PINDUODUO INC-ADR	PDD	5.26
KE HOLDINGS INC	BEKE	4.67
TRIP.COM GROUP LTD-ADR	TCOM	4.27
BAIDU INC - SPON ADR	BIDU	4.19
TAL EDUCATION GROUP- ADR	TAL	4.09
NETEASE INC-ADR	NTES	3.94

## Conclusion:

- On June 1, 2018, MSCI commenced the multi-year process of including China A-Shares into their Global Standard Indexes.
- This rebalance has triggered what may be one of the largest asset transfers in recent history, causing hundreds of billions of dollars to be reallocated to China A-Share securities KBA holds today.
- We believe full inclusion could take up to five years, potentially providing a sustained catalyst for the performance of China's Mainland market.

## Potential Full Inclusion of China A-Shares Within the MSCI Emerging Markets Index



Data from MSCI as of 30/Sep/2020.

## Index Definitions:

**MSCI China Index:** captures large and mid cap representation across China H shares, B shares, Red chips and P chips.

**MSCI All China Investable Market Index (IMI):** captures large, mid and small cap representation across all China securities that are listed in China and Hong Kong, the US and in Singapore. The index includes: A-Shares, H shares, B shares, Red chips and P chips as well as China securities that are listed on the NYSE Euronext (New York), NASDAQ, New York AMEX and Singapore exchanges.

**MSCI ACWI Index:** captures large and mid cap representation across 23 Developed Markets (DM) and 23 Emerging Markets (EM) countries.

**MSCI ACWI GDP Weighted Index:** is based on the flagship MSCI ACWI Index, its parent index, and includes large and mid cap stocks across 23 Developed Markets (DM) and 24 Emerging Markets (EM) countries. The index uses a different weighting scheme than its cap weighted parent index, however. The weight of each country in the index is derived from its economic size (using GDP data) rather than the size of its equity market. Over time, GDP data tends to have more stability than equity market prices.

**MSCI EAFE Index:** is an equity index which captures large and mid cap representation across Developed Markets countries around the world, excluding the US and Canada.

**S&P 500 Index:** is an American stock market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ

**MSCI Emerging Markets Index:** captures large and mid cap representation across 23 Emerging Markets (EM) countries.

**MSCI USA Index:** The MSCI USA Index is designed to measure the performance of the large and mid cap segments of the US market.

**MSCI Frontier Markets (FM) Index:** captures large and mid cap representation across 29 Frontier Markets countries.

**MSCI China A Index:** captures large and mid cap representation across China securities listed on the Shanghai and Shenzhen exchanges.

**MSCI China A International Index:** is a free-float adjusted market capitalization weighted index that is designed to track the equity market performance of large-cap and mid-cap Chinese securities listed on the Shanghai and Shenzhen Stock Exchanges. The Index is based on the concept of the integrated MSCI China equity universe with mainland Chinese securities included.

**MSCI United Arab Emirates (UAE) Index:** designed to measure the performance of the large and mid cap segments of the UAE market.

**CSI 300 Index:** consists of the 300 largest and most liquid A-share stocks. The Index aims to reflect the overall performance of China A-share market..

## Important Notes

**Carefully consider the Funds' investment objectives, risk factors, charges and expenses before investing. This and additional information can be found in the Funds' full and summary prospectus, which may be obtained by visiting [www.kraneshareseu.com](http://www.kraneshareseu.com). Read the prospectus carefully before investing.**

This information is being communicated by KraneShares, which is an appointed representative of DMS Capital Solutions UK Limited, which is authorised and regulated by the Financial Conduct Authority in the United Kingdom under the reference number 503325.

UCITs shares are not redeemable with the issuing fund other than in large Creation Unit aggregations. Instead, investors must buy or sell UCITs Shares in the secondary market with the assistance of a stockbroker. In doing so, the investor may incur brokerage commissions and may pay more than net asset value (NAV) when buying and receive less than net asset value when selling. The NAV of the Fund's shares is calculated each day the national securities exchanges are open for trading as of the close of regular trading on the London Stock Exchange ("LSE"), normally 4:30 P.M. Eastern time (the "NAV Calculation Time"). Shares are bought and sold at market price not NAV. Closing price returns are based on the midpoint of the bid/ask spread at 4:30 P.M. Eastern Time (when NAV is normally determined).

Investing involves risk, including possible loss of principal. There can be no assurance that a Fund will achieve its stated objectives. The Funds are subject to political, social or economic instability within China which may cause decline in value. Fluctuations in currency of foreign countries may have an adverse effect to domestic currency values. Emerging markets involve heightened risk related to the same factors as well as increase volatility and lower trading volume.

The ability of the KraneShares Bosera MSCI China A UCITs to achieve its investment objective is dependent on the continuous availability of A-Shares and the ability to obtain, if necessary, additional A-Shares quota. If the Fund is unable to obtain sufficient exposure due to the limited availability of A-Share quota, the Fund could seek exposure to the component securities of the Underlying Index by investing in other types of securities. The Fund may invest in derivatives, which are often more volatile than other investments and may magnify the Fund's gains or losses.

In Switzerland, the Fund has appointed as Swiss Representative Oligo Swiss Fund Services SA, Av. Villamont 17, 1005 Lausanne, Switzerland, Tel: +41 21 311 17 77, email: [info@oligofunds.ch](mailto:info@oligofunds.ch). The Fund's paying agent is Helvetische Bank AG. In respect of the Shares distributed in or from Switzerland, the place of performance and jurisdiction is Lausanne (Switzerland).

Although the information provided in this document has been obtained from sources which Krane Funds Advisors, LLC believes to be reliable, it does not guarantee accuracy of such information and such information may be incomplete or condensed. [R\_DMS]