RIVERVIEW QUARTERLY INSIGHTS

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INVESTING IN CHINA: SCALING THE GREAT WALL

Since the death of Mao (and with him, the death of a brutally repressive regime), China's economic growth has been incredible. As the world's second-largest economy (and set to overtake America as the largest, possibly in the next 20 – 30 years), it seems that investing in China should be a priority in anyone's portfolio. However, the nature of the Chinese government controls and the resulting lack of transparency make at least some direct investing in China unpredictable and therefore (from a fiduciary perspective, at least) potentially irresponsible.

Further complicating matters, the Trump administration is engaging in a "trade war" with China through the imposition of tariffs. While both sides are negotiating, China also is retaliating with tariffs of its own. The most recent imposition of tariffs in mid-May caused a significant drop in both the Dow and the S&P 500. This uncertainty makes investing in China even more tenuous.

Even with such concerns, however, China's growing place in the financial world will probably be the most important economic story of the 21st Century. Several articles published in The Economist in the February 23rd through March 16th editions provide helpful insights into the problems of investing in China. This article draws from them to provide an overview of the challenges.

Government-Sponsored Companies Create Confusion.

As post-Mao China sought to invigorate its economy and catch up with the rest of the world, a major shift from state-owned to private investment took place. As the employment in state-owned enterprises (or "SOEs") dropped significantly in the 1990's, employment in the private sector took off, to the point that the private sector accounts for

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50% of tax revenues, 60% of GDP, 70% of innovation, 80% of jobs and 90% of its companies. The transition from public to private enterprise has been dramatic.

Yet SOEs still occupy a large (and largely distracting) place in the Chinese economy. The 150,000 or so SOEs hold 70% of corporate debt in the country, owing to preferential (and government sponsored) lending practices. This disproportionate lending environment has only gotten worse since Xi Jingping took control. Further, SOEs still have a controlling position in certain key industries, like finance and shipping. As a result, private firms have to do a clumsy, accommodative dance with the SOEs, leading to inefficient business practices.

In fact, some in China worry that, having accomplished their goal of modernizing the Chinese economy, private firms will be squeezed out in favor of politically influenced, inefficient SOEs. The government has started to insist that private companies (and even foreign multinationals) have communist party cells. The government also has vowed to strengthen SOEs.

The Chinese Economy is Built on Three Questionable Pillars.

China has achieved amazing results over the past 30 years: in the 1990 it accounted for 4% of global economy; now it accounts for almost 18%. This growth was achieved through three factors. First, land in China is all publicly-owned, allowing the government to offer cheap rents in order to attract business investment. It provides a significant source of revenue to local governments as long as growth is strong.

The second pillar is cronyism: business people with local connections are given advantages that those in a market economy don't have access to, a competitive advantage that allows the Chinese businessperson to outperform. Corruption can actually promote incentives (at least for those who benefit from it), which can lead to economic growth when the beneficiary of the corruption is a local government.

The third pillar is debt: China over the past 30 years has gone on a government-funded building spree. Until now, Chinese debt levels were below those of most developed countries, so the increase has not proved too heavy a drag on the economy.

The problem, of course, is that all three of these factors are of limited benefit. The use of cheap land only goes so far, both because it's a finite resource and because it can only be used while the economic growth supports it. Corruption tends to morph from a source of incentive to a source of corrosion. And debt levels have finally become high enough that they are switching from an engine of growth to a source of concern.

In light of this, the Chinese government has to deal with these now-outmoded factors and at the same time come up with a new model, all while maintaining increasing levels of centralized control.

China has an Income Inequality Problem.

Investment in China is at twice the level of developed countries, while consumption is at half. However, this is changing. Over the past 30 years, consumer spending grew eight times per capita, after adjusting for inflation. China is now the world's largest market for cars, smartphones and luxury goods. The labor force is shrinking (due to an aging population) while wages are rising. This means that consumer spending is destined to increase further.

But, as with everywhere else, such growth leads to growing inequality. However, for structural reasons, the gap will be worse in China. The government controls heavily where people can live, and therefore where they can work and where their kids can go to school. Urbanites grow more affluent, while those in the country are stuck with limited opportunities.

Chinese Financial Data is Manipulated.

A key principle of modern investing is that of "market efficiency," which posits that investors make rational decisions based on all available market data. This principle, if true, requires transparency of data. On this score, at least, China fails. A recent study published by the Brookings Institution suggests that, despite the volumes of data the Chinese government collects, industrial output and investment have been "embellished," with the result that China has overstated its real GDP growth by an average of 2% from 2008 to 2016. Interestingly, the study's authors argue that this overstatement is not the result of a malign government manipulating data to reach desired outcomes, but rather the central government's lack of ability to control local officials. For example, when provincial GDP totals are tallied, they exceed national GDP. This lack of data transparency should worry potential investors in Chinese markets.

The Chinese Economy Faces Uncertainty.

The Chinese Prime Minister's annual work report, typically a routine affair, struck a different tone this year. China would aim for growth of 6 – 6.5%, the lowest in 30 years. Bureaucrats were ordered to make spending cuts, and the government would focus on keeping the unemployment rate below 5.5%, to counteract the layoffs in manufacturing and tech. Given that the Chinese government always seems to meet its projections, this lowering of expectations seems troubling.

The Prime Minister warned that a growth in lending in January could create more risk, and has disavowed the kind of "flood-style stimulus" in which the government has engaged in the past. In fact, he mentioned "risk" in this speech more than at any other time in a decade. In other words, investors should not count on extensive government spending to bail the economy out.

Recent Changes May Help.

Chinese citizens are starting to travel. A lot. Last year, they averaged five times as many trips as they did in the first decade of the century. This is just one factor behind China's current account surplus (that is, the amount by which its exports exceed its imports) disappearing. In 2007, that surplus was 10% of GDP; it has dropped to .4%. This drop in surplus will be further exacerbated by a drop in the savings rate and an aging population.

If handled the right way, the switch from a current account surplus to a deficit may not be a bad thing. Market economies, that often run such deficits, offset them by luring in foreign investment. China traditionally has limited foreign investment, and preferred institutional investors like pension funds. In other words, one result of switching from an account surplus to a deficit may be for China to further open itself to foreign investment. On the other hand, it might clamp down in order to maintain its surplus, which could potentially have a negative impact on foreign investment. Time will tell.

So What Do U.S. Investors Do Now?

Chinese investments are increasingly becoming part of the mainstream, especially since China has continued to open mainland Chinese stock markets ("A-shares") a bit more to foreign investment (buying "A shares" is the way an investor invests directly in Chinese companies; the indirect alternatives to invest in China have primarily been through Chinese stocks that trade in Hong Kong ("H-shares"), or New York ("N-shares")). Emerging market index funds governed by MSCI will quadruple their weight of mainland China stocks to 3.3%. Next month Chinese bonds will be added to the Bloomberg Barclays bond index, which could bring $100 billion of Chinese bond inflows over two years. So direct investment in China will become more available. It does seem strange, though, to invest in China (the second largest economy in the world) through an emerging market index fund, particularly when only three cents of your investment dollar will be held in mainland Chinese stocks.

Another option is to buy individual Chinese stocks, or invest in an actively-managed fund whose manager does so. But investors should take note of the uncertainties and complexities outlined above.
A third choice is to invest in funds that benefit from the Chinese economy, rather than investing in the shares themselves. For example, investing in Australian companies that do significant business in China gives you indirect access to the ups and downs of the Chinese markets without the added uncertainty of identifying Chinese companies that might suffer from a change in government policies.

The final option is to avoid investing in China until things settle down. I have no idea how an investor would know when that happens.

None of these choices is ideal. At the moment, we are pursuing a combination of the second and third options through an actively-managed emerging market fund, but that could change as we monitor changing conditions.
The main point is that China can be neither ignored nor blindly pursued. It is now and will continue to be one of the most important financial stories of the next twenty to fifty years. Get ready for an interesting ride.

SPOTLIGHT ON PLANNING

UNDERSTANDING MEDICARE

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Medicare is a federal program that provides health insurance to retired individuals, regardless of their medical condition, and certain younger people with disabilities or end-stage renal disease. Here are some basic facts about Medicare that you should know.

What does Medicare cover?

Medicare coverage consists of two main parts: Medicare Part A (hospital insurance) and Medicare Part B (medical insurance). These parts together are known as Original Medicare. A third part, Medicare Part C (Medicare Advantage), covers all Part A and Part B services, and may provide additional services. A fourth part, Medicare Part D, offers prescription drug coverage that can help you handle the rising costs of prescriptions.

Medicare Part A (hospital insurance)

Generally known as hospital insurance, Part A covers services associated with inpatient hospital care. These are the costs associated with an overnight stay in a hospital, skilled nursing facility, or psychiatric hospital, including charges for the hospital room, meals, and nursing services. Part A also covers hospice care and home health care.

Medicare Part B (medical insurance)

Generally known as medical insurance, Part B covers other medical care. Physician care — whether you received it as an inpatient at a hospital, as an outpatient at a hospital or other health-care facility, or at a doctor's office — is covered under Part B. Laboratory tests, physical therapy or rehabilitation services, and ambulance service are also covered. Medicare Part B also covers 100% of the cost of many preventative services and an annual wellness visit.

Medicare Part C (Medicare Advantage)

A Medicare Advantage plan is a private health-care plan that contracts with Medicare to provide Part A and Part B benefits. A Medicare Advantage plan covers all of the services that Original Medicare covers except hospice care. Some plans offer extra coverage for expenses not covered by Original Medicare such as vision, hearing, dental, and other health expenses. Most also offer prescription drug (Part D) coverage. Several types of Medicare Advantage plans may be available, including health maintenance organization (HMO) plans, preferred provider organization (PPO) plans, private fee-for-service (PFFS) plans, and special needs plans (SNPs). You can choose to enroll in either Original Medicare or a Medicare Advantage plan. If you enroll in a Medicare Advantage plan, you'll generally pay a monthly premium for it, in addition to your Part B premium.

Medicare Part D (prescription drug coverage)

All Medicare beneficiaries are eligible to join a Medicare prescription drug plan offered by private companies or insurers that have been approved by Medicare. Although these plans vary in price and benefits, they all cover a broad number of brand name and generic drugs available at local pharmacies or through the mail. Medicare prescription drug coverage is voluntary, but if you decide to join a plan, keep in mind that some plans cover more drugs or offer a wider selection of pharmacies (for a higher premium) than others. You can get information and help with comparing plans on the Medicare website, medicare.gov, or by calling a Medicare counselor at 1-800-Medicare.

What is not covered by Medicare Parts A and B?

Some medical expenses are not covered by either Part A or B. These expenses include:

- Your Part B premium
- Deductibles, coinsurance, or co-payments that apply
- Most prescription drugs
- Dental care
- Hearing aids
- Eye care
- Custodial care at home or in a nursing home

Medicare Part C may cover some of these expenses, or if you're enrolled in Original Medicare you can purchase a supplemental Medigap insurance policy that will help cover what Medicare does not.

Are you eligible for Medicare?

Most people age 65 or older who are citizens or permanent residents of the United States are eligible for Medicare Part A (hospital insurance) without paying a monthly premium. You are eligible at age 65 if:

- You receive or are eligible to receive Social Security or Railroad Retirement Board benefits based on your own work record or on someone else's work record (as a spouse, divorced spouse, widow, widower, divorced widow, divorced widower, or parent), or

- You or your spouse worked long enough in a government job where Medicare taxes were paid

In addition, if you are under age 65, you can get Part A without paying a monthly premium if you have received Social Security or Railroad Retirement Board disability benefits for 24 months, or if you are on kidney dialysis or are a kidney transplant patient.

Even if you're not eligible for free Part A coverage, you may still be able to purchase it by paying a premium. Call the Social Security Administration (SSA) at (800) 772-1213 for more information.

Although Medicare Part B (medical insurance) is optional, most people sign up for it. If you want to join a Medicare managed care plan or a Medicare private fee-for-service plan, you'll need to enroll in both Parts A and B. And Medicare Part B is never free — you'll pay a monthly premium for it, even if you are eligible for premium-free Medicare Part A.

How much does Medicare cost?

Medicare deductible amounts and premiums change annually. Here's what you'll pay in 2019 if you're enrolled in Original Medicare:

	Premium	Deductible	Coinsurance
Part A (hospital)	None for most people, but noneligible individuals pay up to $437 per month (if they have 39 or fewer quarters of Medicare-covered employment)	$1,364 per benefit period	$341 a day for the 61st to 90th day each benefit period; $682 a day for the 91st to 150th day for each lifetime reserve day (total of 60 lifetime reserve days); $170.50 a day for the 21st to 100th day each benefit period for skilled nursing facility care
Part B (medical)	The standard Part B premium amount is $135.50 (subject to an income-based adjustment). However, some people who get Social Security benefits will pay less than this amount. See below for more information.	$185 per year	After satisfying a deductible if one applies, you normally pay 20% of the approved amount for medical expenses (20 to 40% for outpatient mental health services, 20% for hospital charges for outpatient hospital services, nothing for laboratory services)

If you have your premiums deducted from your Social Security benefits, and the increase in your benefits for 2019 will not be enough to cover the Medicare Part B increase, then you may pay less than the standard Part B premium. Otherwise, you may pay the standard Part B premium of $135.50. You'll also pay the standard Part B premium of $135.50 (or higher) if:

- You enroll in Part B for the first time in 2019.
- You don't get Social Security benefits.
- You're directly billed for your Part B premiums.
- You have Medicare and Medicaid, and Medicaid pays your premiums.
- Your modified adjusted gross income as reported on your federal income tax return from two years ago is above a certain amount.*

The table below shows what you'll pay if you're in this group.

If you file an individual income tax return with income that is:	If you file a joint income tax return with income that is:	If you file an income tax return as married filing separately with income that is:	Monthly premium in 2019:
$85,000 or less	$170,000 or less	$85,000 or less	$135.50
Above $85,000 up to $107,000	Above $170,000 up to $214,000	N/A	$189.60
Above $107,000 up to $133,500	Above $214,000 up to $267,000	N/A	$270.90
Above $133,500 up to $160,000	Above $267,000 up to $320,000	N/A	$352.20
Above $160,000 and less than $500,000	Above $320,000 and less than $750,000	Above $85,000 and less than $415,000	$433.40
$500,000 and above	$750,000 and above	$415,000 and above	$460.50

**Beneficiaries with higher incomes have paid higher Medicare Part B premiums since 2007. To determine if you're subject to income-related premiums, the SSA uses the most recent federal tax return provided by the IRS. Generally, the tax return you filed in 2018 (based on 2017 income) will be used to determine if you will pay an income-related premium in 2019. You can contact the SSA at (800) 772-1213 if you have new information to report that might change the determination and lower your premium.*

Since Original Medicare doesn't cover every type of medical care, and you'll have to pay deductibles and coinsurance, you may want to buy a Medicare supplemental insurance (Medigap) policy.

If you're enrolled in a Medicare Advantage plan, you'll generally pay one monthly premium for that plan in addition to your Medicare Part B premium. Each Medicare Advantage plan has different premiums and costs for services, and coverage varies, so what you'll pay depends on the plan you have.

Who administers the Medicare program?

The Centers for Medicare & Medicaid Services (CMS) has overall responsibility for administering the Medicare program and sets standards and policies. The CMS also manages the official government website for Medicare, medicare.gov. But it's the SSA that processes Medicare applications and answers Medicare eligibility questions.

How do you sign up for Medicare?

You'll generally be automatically enrolled in Medicare when you turn 65 if you're already been receiving Social Security or Railroad Retirement Board benefits for at least four months before you turn 65. The SSA will notify you that you're being enrolled. If you're not automatically enrolled and are eligible for Medicare at age 65, you have a 7-month initial enrollment period to sign up for Part A and/or Part B.

Although there's no cost to enroll in Medicare Part A, you'll pay a premium to enroll in Medicare Part B. If you've been automatically enrolled in Part B, you'll be notified that you have a certain amount of time after your enrollment date to decline coverage. Even if you decide not to enroll in Medicare Part B during the initial enrollment period, you can enroll later during the annual general enrollment period that runs from January 1 to March 31 each year. However, you may pay a slightly higher premium as a result, depending on the circumstances

If you decide to postpone applying for Social Security past your 65th birthday, you can still enroll in Medicare when you turn 65. The SSA suggests that you call (800) 772-1213 three months before you turn 65 to discuss your options. The easiest way to apply for Medicare is online at socialsecurity.gov.

* * * * *

MARKET SNAPSHOT

MARKET SUMMARY – SHORT- AND LONG-TERM INDEX RETURNS

	US Stock Market	International Developed Stocks	Emerging Markets Stocks	Global Real Estate	US Bond Market	Global Bond Market ex US
Q1 2019	**STOCKS**				**BONDS**	
	14.04%	10.45%	9.92%	14.07%	2.94%	2.96%
1 Year						
	8.77%	-3.14%	-7.41%	13.93%	4.48%	5.23%
5 Years						
	10.36%	2.20%	3.68%	6.63%	2.74%	4.27%
10 Years						
	16.00%	8.82%	8.94%	14.84%	3.77%	4.29%

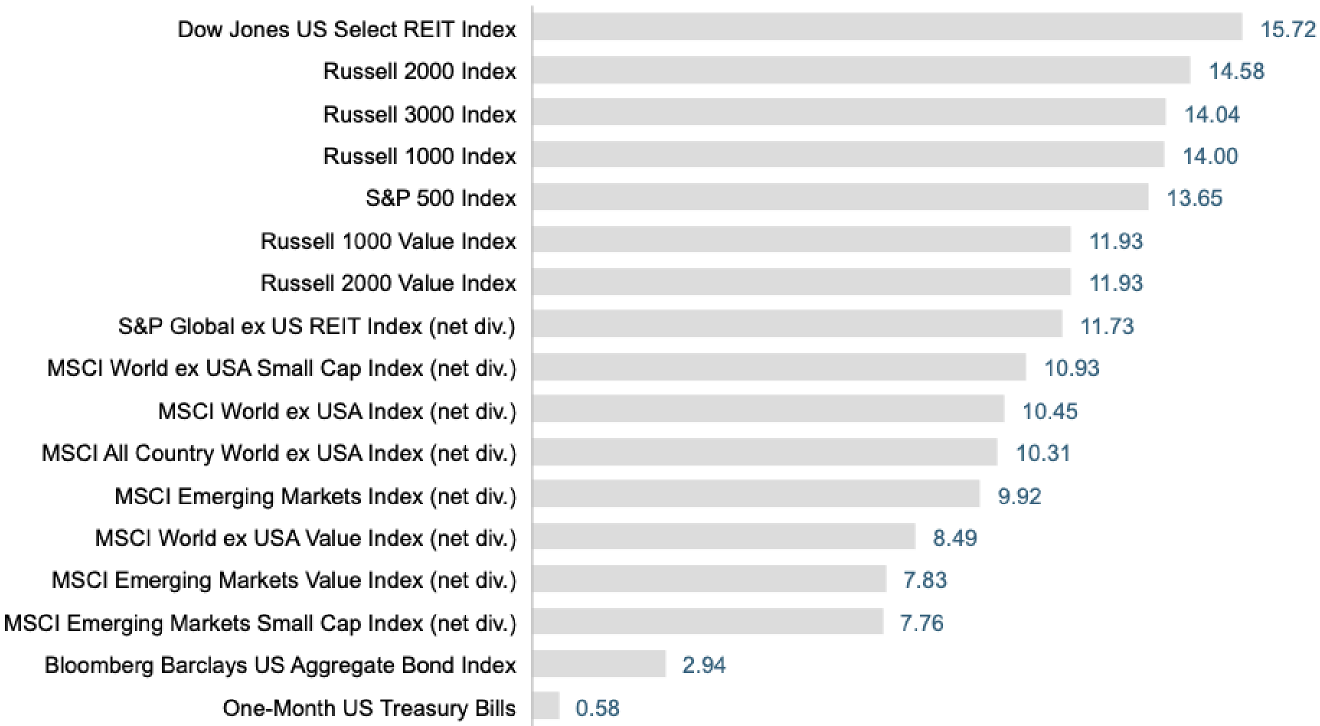
See important disclosure information

GLOBAL MARKETS – FIRST QUARTER 2019 INDEX RETURNS (%)

Equity markets posted positive returns around the globe in the first quarter. Looking at broad market indices, US equities outperformed non-US developed and emerging markets.

Small caps outperformed large caps in the US and non-US developed markets but underperformed in emerging markets. Value stocks generally underperformed growth stocks in all regions.

REIT indices outperformed equity market indices in both the US and non-US developed markets.



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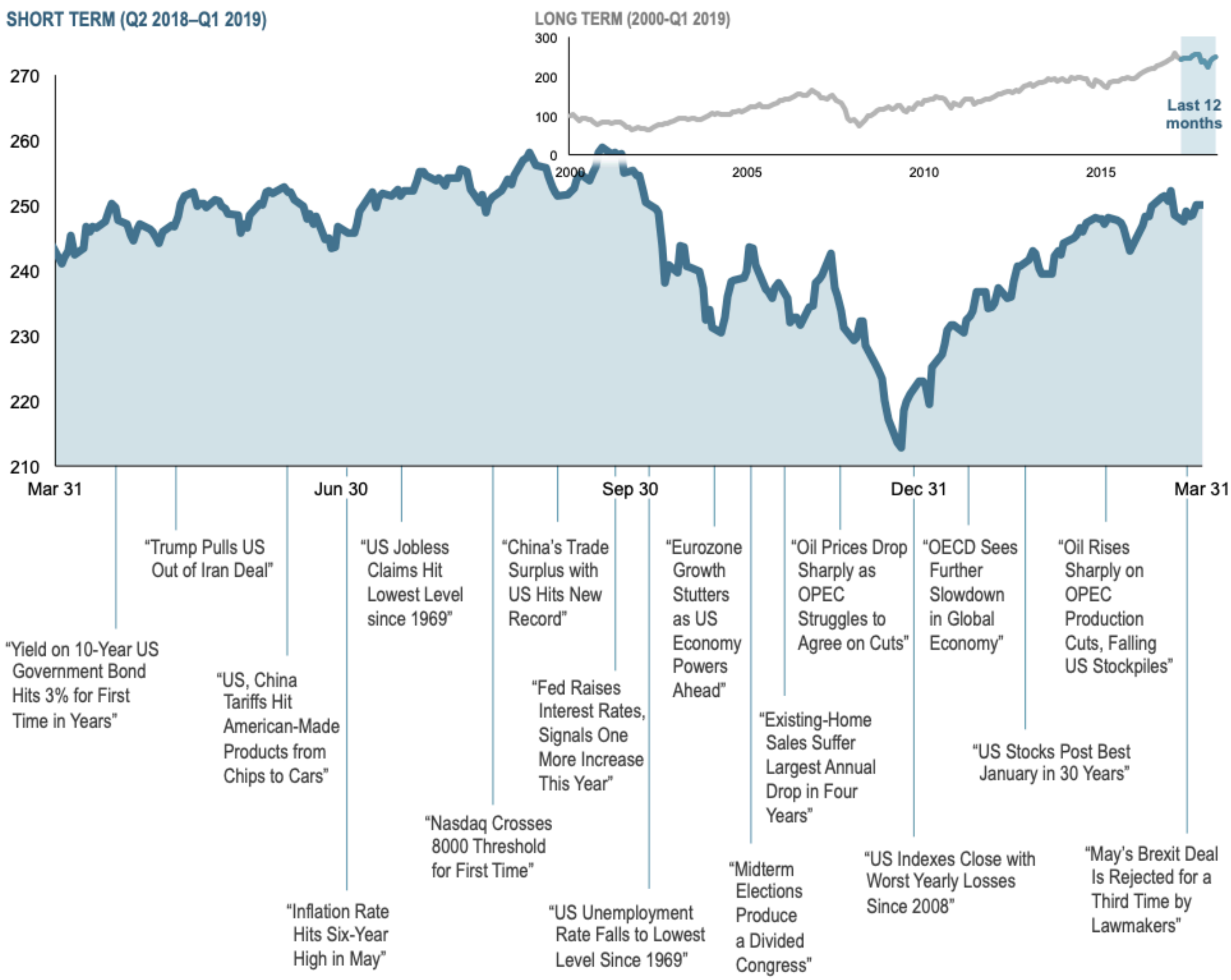
WORLD STOCK MARKET PERFORMANCE

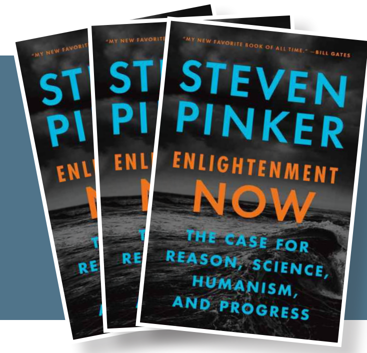
MSCI All Country World Index with selected headlines from past 12 months

These headlines are not offered to explain market returns. Instead, they serve as a reminder that investors should view daily events from a long-term perspective and avoid making investment decisions based solely on the news.



Graph Source: MSCI ACWI Index [net div.]. MSCI data © MSCI 2019, all rights reserved. It is not possible to invest directly in an index. Performance does not reflect the expenses associated with management of an actual portfolio. Past performance is not a guarantee of future results.

BOOK REVIEW



ENLIGHTENMENT NOW

By Steven Pinker

We seemed gripped by a world of fear. Fear of climate change, social upheaval, loss of traditional values, financial insecurity, terrorism, racism. The optimism of the '90s, when the Berlin Wall was gone, the Soviet Union dissolved and the Internet was changing our lives for the better, has been replaced by post-9/11, post-Financial Crisis world of uncertainty.

Not so long ago, the narrative was different. Free trade was a rising tide that would raise all boats. Democracy was inevitable. Liberalism (not the "American Liberal" kind, but the 175-year old tradition of free trade and freedom of expression) had no intellectual competition. But gradually this liberalism created winners and losers: tech billionaires and finance experts (the "Elite") versus unemployed auto workers and coal miners. Liberalism also created an environment in which cultural traditions seemed to disappear: these Elites created a world where anyone could get married, where "microaggressions" and "trigger warnings" stepped on free speech in colleges and universities. Add to this the instability and violence of the Middle East, and suddenly fear replaced optimism for millions of people around the world.

Fear is a terrible thing. It leads to people retreating from progress, stepping away from improvement brought about by new ideas. And fear creates an opening for Populism, a fear-based reaction that feeds on suspicion and worry, creating "us" and "them." Suspect the worst in those you don't know well. I only win if you lose. My party, right or wrong. America (or Europe, or China) First.

Into this toxic atmosphere comes a refreshing breeze: "Enlightenment Now – The Case for Reason, Science, Humanism and Progress," by Steven Pinker. In short, Mr. Pinker explains how life on earth is better in almost every category because of our Enlightenment ideals. As a species, we are wealthier, better fed, healthier and better educated. We have less crime (especially murder, despite terrorist attacks) and have more equality, peace, safety and say in our political destiny than at any time in human history. Mr. Pinker wrote this book in part to answer the question, posed by one of his students, "why should I live?" His answer, in short, is that the "better angels of our nature" have driven us to make huge progress in most areas of life.

Mr. Pinker begins by briefly summarizing the forces that shape our actions: entropy, evolution and information. Life is a battle against entropy, which according to Newton's law of thermodynamics, is the tendency of things to break down in a closed system (warning: that was an English major's summary of a neuropsychiatrist's summary of physics). Any closed system (the pursuit of food or the running of a government) can break down through entropy. Mr. Pinker states that "energy channeled by knowledge is the elixir with which we stave off entropy, and advances in energy capture are advances in human destiny." This can include literal channeling of electrical energy, which raises standards of living around the world, and also the positive channeling of our physical and emotional energy toward achieving societal goals. In other words, the intelligent efforts that we make pay off in all kinds of advances in health, safety and development.

Pitted against this energy channeled by knowledge is the irrational “counter-Enlightenment” that was born in the 1800’s during the Romantic era and which has been battling Enlightenment values ever since. Contemporary iterations of these counter-Enlightenment views can be found in the glorification of the collective over that of the individual and the raising of the ecosystem as a transcendent entity. Take nuclear power, for instance: although it has serious problems, it is infinitely less harmful than burning fossil fuel, yet populist, collectivist efforts have thwarted its development. And it’s even harder to deny Mr. Pinker’s point when faced with the collectivist, religious barbarity of Islamic State.

After setting out the background, Mr. Pinker demonstrates in extensive detail all the ways in which humanity has thrived and improved under Enlightenment principles. Separate chapters on Life, Health, Sustenance, Wealth, Inequality, The Environment, Peace, Safety, Terrorism, Democracy, Equal Rights and Quality of Life all attest, through wagonloads of data, how well humanity has made advances in each area. Mr. Pinker is not oblivious to the dangers in front of us, particularly in the forms of climate change and inequality. But even there, he remains optimistic that science and humanism will find solutions if the irrational forces don’t get in the way.

Mr. Pinker’s analysis is not always perfect. He has been criticized for not pointing out the flaws in Enlightenment thinking and for not adequately describing its goals. Alison Gopnik, in reviewing the book for The Atlantic, points out a critical fact that Mr. Pinker seems to ignore, and that is crucial to the current political divide in America: “the tension between the global and the local, modernity and tradition, professional opportunity and family ties, the people who leave the place where they grew up and the people who stay.” This tension gets lost in the thicket of statistical averages, charts and graphs that Mr. Pinker uses to make his points. According to Ms. Gopnik, “[i]f the case for reason, science, humanism, and progress is really going to be convincing . . . it will have to speak to a wider spectrum of listeners, a more inclusive conception of flourishing, a broader palette of values.”

Fair enough. There is a lot of work to be done, and Enlightenment Now covers only the big picture, is only a first step. But it is an encouraging, inspiring and positive first step. And in this anger- and fear-driven period of time, we need a good first step.

IMPORTANT DISCLOSURE INFORMATION

Market segment (index representation) as follows: US Stock Market (Russell 3000 Index), International Developed Stocks (MSCI World ex USA Index [net div.]), Emerging Markets (MSCI Emerging Markets Index [net div.]), Global Real Estate (S&P Global REIT Index [net div.]), US Bond Market (Bloomberg Barclays US Aggregate Bond Index), and Global Bond ex US Market (Citi WGBI ex USA 1-30 Years [Hedged to USD]).

RIVERVIEW
trust company™

WASHINGTON
900 Washington Street, Suite 900
Vancouver, Washington 98660
360.693.7442 | riverviewtrust.com

OREGON
5400 Meadows Road, Suite 325
Lake Oswego, Oregon 97035
503.558.6454