

## Time to Rethink Your Portfolio's International Mix?

### *Tips to develop a structured approach to international allocation decisions*

After years of U.S. market dominance, international investments are receiving renewed attention from strategic investors. Significant valuation disparities, evolving trade policies, and shifting global economic dynamics create both challenges and opportunities for portfolio allocations beyond U.S. borders. As the global investment landscape undergoes transformation, a thoughtful reassessment of international exposure has become essential for well-diversified portfolios.

#### The Case for International Rebalancing

Several compelling factors suggest that international allocations warrant careful reconsideration:

**Valuation Differentials:** U.S. equity markets continue to trade at premium valuations relative to international developed and emerging markets. By historical standards, these valuation gaps remain wide, creating potential opportunities for relative outperformance as valuations normalize over time.

**Economic Growth Differentials:** While the U.S. economy has demonstrated remarkable resilience, economic growth in certain international regions may accelerate as inflationary pressures ease and monetary policies become less restrictive.

**Currency Considerations:** After a period of dollar strength, potential shifts in monetary policy differentials and trade dynamics could create a more favorable environment for international currencies,

potentially enhancing returns for U.S.-based investors in foreign markets.

**Sector Composition Variations:** International markets offer exposure to sectors and industries that may be underrepresented in U.S. indexes, potentially enhancing diversification benefits beyond what is reflected in headline correlations.

**Policy Environment Evolution:** The return of the Trump administration signals potential shifts in trade policy, international relations, and global economic governance that could significantly impact relative performance across regions and sectors.

#### Regional Considerations and Opportunities

A nuanced approach to international allocation requires consideration of distinct regional dynamics:

**European Markets:** Despite persistent economic challenges, European markets offer compelling valuations and exposure to global industrial and luxury goods companies with strong competitive positions. Recent economic data suggests potential for improved growth as the region addresses energy transition challenges and benefits from moderating inflation.

### **Key considerations include:**

- Selective opportunities in export-oriented industrial firms benefiting from global infrastructure spending
- Financial institutions potentially benefiting from a normalized interest rate environment
- Luxury goods companies with strong brand equity in growing Asian markets

**Asia Pacific (Developed):** Japan's corporate governance reforms continue to create potential for improved capital allocation and shareholder returns. Australia provides commodity exposure with developed market stability, while Singapore offers a strategic hub for Southeast Asian economic growth.

Notable developments include:

- Japanese companies' increasing focus on return on equity and shareholder value
- Significant cash reserves on Japanese corporate balance sheets with potential for increased dividends and buybacks
- Australia's strategic position as a commodity provider with proximity to growing Asian economies

**Emerging Markets:** This diverse category requires particularly careful assessment, with significant differentiation in economic fundamentals, policy approaches, and geopolitical positioning. Selectivity is essential, with attention to:

- Countries with improving governance and economic reform momentum
- Regions benefiting from supply chain diversification trends
- Markets with favorable demographic profiles and growing domestic consumption
- Consideration of geopolitical alignments and their implications for trade and investment flows

## **Implementation Strategies for International Rebalancing**

Effective international rebalancing requires a thoughtful implementation approach:

**Strategic vs. Tactical Allocation:** Distinguish between long-term strategic international allocations based on portfolio diversification needs and shorter-term tactical positions responding to specific opportunities or risks.

**Currency Hedging Decisions:** Rather than applying a uniform hedging approach, consider a currency-by-currency assessment based on:

- Interest rate differentials affecting hedging costs
- Currency valuation metrics suggesting potential appreciation or depreciation
- The role of currency exposure as a portfolio diversifier during market stress periods

**Active vs. Passive Implementation:** While passive approaches offer cost-effective broad exposure, international markets often exhibit greater inefficiencies than the U.S. market, potentially creating opportunities for skilled active managers to add value through security selection and country allocation.

**Sector-Based Approaches:** Rather than allocating strictly by region, consider sector-based international exposure that focuses on:

- Global leaders regardless of domicile
- Industries where certain regions maintain competitive advantages
- Sectors benefiting from specific economic or policy developments

**Geopolitical Risk Management:** Incorporate geopolitical risk assessment into allocation decisions, including:

- Exposure to regions with heightened conflict risk
- Vulnerability to potential trade policy changes
- Regulatory and policy stability considerations
- Energy security and resource accessibility

### Monitoring and Adjustment Framework

International allocations require ongoing assessment and potential adjustment based on evolving conditions. Establish a monitoring framework that includes:

**Valuation Metrics:** Regularly review relative valuation metrics across regions, including price-to-earnings ratios, price-to-book values, and dividend yields.

**Economic Indicators:** Track key economic data points indicating potential shifts in growth trajectories across regions.

**Policy Developments:** Monitor monetary, fiscal, and trade policy changes that may impact relative performance.

**Corporate Fundamentals:** Assess trends in earnings growth, return on equity, and margin development across regions.

### A More Nuanced Global Portfolio

By developing a structured approach to international allocation decisions, investors can move beyond simplistic domestic/international splits toward a more nuanced global portfolio that appropriately balances risk, return potential, and diversification benefits in today's complex investment environment.