

Home Bias and Global Diversification

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By pursuing a globally diversified approach to investing, one doesn't have to attempt to pick winners to achieve a rewarding investment experience.

Every day we enjoy the benefits of an interconnected world. We might start our day with a cup of coffee that originated in South America, check our email on a smartphone designed in California and manufactured in Taiwan, then shower and change into clothes woven from Egyptian fabrics before driving a German-made car or riding in a French-built train to work.

As consumers, we rarely think twice about the benefits of access to the cornucopia of goods the global market has to offer. Yet, as investors, we will often concentrate our portfolios in favor of our home market at the expense of global diversification. For example, while US stock markets represent just over 50% of the value of global equity markets, many US investors tend to allocate around 70% of their equity assets to domestic stocks.¹ This phenomenon, which can be observed across countries around the world, is known in the investment community as “home-country bias.”

Given that certain frictions may be associated with investing abroad, a home-country bias may make sense for an investor in certain cases. For example, for tax-deferred investors in the US, foreign dividend tax withholdings may present a disadvantageous tax drag on international investments. In general, however, neglecting the benefits that global diversification has to offer may increase risks and decrease the investment opportunity set.

As **Exhibit 1** illustrates, 13 different developed countries (out of 21) had the best-performing equity market in a given calendar year for the 20 years ended in December 2016, and no country had the best-performing market for more than two consecutive years.

1. Willis Towers Watson, Global Pension Assets Study 2017.

Exhibit 1: Equity Returns of Developed Markets Annual Return (%)

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Highest Return	Switz 44.25	Finland 121.64	Finland 152.60	Switz 5.66	NZ 3.42	NZ 24.24	Sweden 64.53	Austria 71.52	Canada 23.31	Spain 49.38	Finland 46.65	Japan 39.21	Norway 67.27	Sweden 33.75	Ireland 13.71	Belgium 46.04	Finland 46.04	US 12.69	Denmark 23.43	Canada 24.69
	Italy 35.45	Belgium 67.74	Singapore 69.40	Canada 5.34	Australia 1.68	Australia 16.85	Germany 63.83	Norway 53.27	Japan 25.92	Ireland 46.81	UK 41.20	Switz 30.49	Australia 76.43	Denmark 30.75	NZ 5.54	Denmark 31.27	Finland 41.15	UK 7.34	Ireland 16.45	NZ 18.37
	Denmark 34.52	Italy 79.74	Sweden 34.44	Denmark 3.44	Ireland -1.34	Australia -1.34	Spain 58.46	Belgium 43.53	Austria 24.64	Canada 45.71	Germany 35.21	US -37.57	Singapore 73.96	HK 23.23	US 1.36	Singapore 30.96	Finland 31.79	Denmark 6.18	Belgium 12.10	Norway 13.31
	US 33.38	Spain 49.90	Japan 61.83	Norway -5.65	Austria -7.26	Norway -7.26	Austria 56.96	Ireland 43.07	Denmark 24.90	Norway 45.12	Norway 31.43	Spain -40.60	Sweden 64.16	NZ 22.14	UK -2.55	Germany 30.90	Germany 31.37	HK 5.07	Japan 9.67	Australia 11.45
	Spain 25.41	France 41.54	HK 59.92	-1.33	-10.89	-7.33	55.43	Sweden 36.28	Norway 24.26	Sweden 43.39	Canada 29.57	France -43.27	HK 60.15	20.45	-5.77	23.28	Spain 31.32	UK 4.12	Austria 3.46	Austria 11.26
	Germany 24.57	Ireland 35.33	Canada 53.74	-4.09	-11.36	-10.28	54.60	NZ 35.17	Finland 16.69	Denmark 38.77	Singapore 28.35	Canada -45.51	Belgium 57.49	15.44	-10.01	HK 26.27	Finland 31.30	Singapore 3.03	Italy 2.30	US 10.89
	Nether 23.77	US 30.14	Norway 31.70	-4.31	-12.22	-10.31	Australia 49.46	Switz 32.49	Australia 16.33	Belgium 36.66	Australia 23.34	Germany -45.87	Canada 56.18	14.77	-10.62	Belgium 25.90	Belgium 27.61	Austria 2.29	Finland 2.02	Austria 4.88
	UK 23.82	Germany 23.43	France 23.43	US -12.39	-12.39	-12.39	Denmark 49.25	Denmark 30.32	Denmark 16.02	Australia 35.84	Denmark 25.59	Singapore -17.35	NZ 50.40	14.82	-10.95	Australia 22.07	Australia 27.16	Nether 1.30	Nether 1.34	Nether 4.82
	Finland 17.23	Switz 23.53	US 21.92	-11.33	-14.05	-13.19	Norway 48.11	Australia 30.34	Singapore 14.37	Spain 35.99	Denmark -47.58	Spain 43.48	Switz 11.79	-12.12	-12.12	Sweden 21.97	Switz 26.61	Switz -0.09	US 0.69	Germany 2.76
	Ireland 15.84	Nether 23.23	Germany 20.04	-11.96	-14.81	-14.97	Ireland 43.83	Spain 28.93	Nether 13.68	France 34.48	Nether 20.59	-48.22	UK 43.30	Norway 10.95	-12.28	France 21.27	France 25.33	Finland -0.71	Finland 0.44	Japan 2.38
	Belgium 13.55	UK 17.92	Australia 17.92	HK -13.61	-12.33	-12.33	France 40.22	UK 24.98	Switz 10.31	Italy 35.49	France 10.34	UK -43.34	Austria 43.20	10.23	-12.71	Canada 20.59	Denmark 25.25	Australia -3.41	France -0.11	Nether 2.27
	Sweden 12.92	Sweden 13.96	UK 12.90	-12.84	-20.43	-19.29	38.10	Denmark 22.27	Switz 9.92	31.38	8.90	-49.96	42.25	9.88	-14.33	Japan 20.35	Switz 24.50	-3.46	-0.54	Sweden 1.42
	Canada 12.80	Denmark 9.99	Denmark 12.45	-14.21	-21.38	-16.03	37.83	Canada 9.98	Australia 30.86	8.36	Italy -49.98	Denmark 36.57	UK 8.76	-15.98	18.55	UK 20.67	UK -1.62	Japan -1.89	Germany 0.62	
	UK 11.84	Australia 12.26	Denmark 12.26	HK -17.19	-17.19	-17.19	Singapore 15.97	UK 9.05	Belgium 30.81	UK 11.36	Australia -20.07	France 31.83	Germany 3.44	-10.92	13.71	US 20.43	US 20.43	Switz -4.67	Switz -4.67	UK -5.10
	Norway 6.24	Japan 6.05	Nether 6.88	-15.59	-22.36	-20.33	35.91	France 18.48	HK 30.35	5.44	UK -51.21	26.57	NZ 8.32	-16.02	UK 16.28	UK 13.42	UK -6.39	-6.26	Spain -1.02	
	Austria 1.57	Austria 0.35	Spain 4.83	Spain -15.36	Germany -22.39	-21.15	Belgium 35.33	Germany 16.17	UK 7.35	Finland 29.94	Switz 5.29	NZ -63.79	US 26.25	1.74	-16.87	France 11.27	NZ 11.27	Sweden -7.85	UK -7.86	Finland -4.70
	Australia -10.44	HK -15.92	Italy -15.92	Belgium -20.42	US -20.42	-20.42	Switz -20.59	Switz 34.08	Japan 15.96	Switz 27.40	Austria 27.40	Finland -43.34	Switz 26.81	Belgium -0.42	-0.42	Canada 20.59	Denmark 25.25	Australia -3.41	France -0.11	Nether 2.27
	NZ -14.15	Canada -6.14	-7.02	-21.29	-26.59	-26.24	32.06	UK 14.96	4.41	17.80	0.62	-64.24	25.15	-4.11	-18.08	9.09	Canada 9.40	-9.92	-14.99	Norway -7.07
	HK -23.29	Singapore -12.58	Austria -9.11	-27.72	-27.18	-30.31	21.41	US 12.24	1.90	16.56	-2.73	Belgium -66.43	Ireland 12.23	-15.01	-23.19	1.19	Canada 5.63	Germany -10.36	Spain -16.64	Belgium -7.57
	Japan -23.61	NZ -23.62	Ireland -23.62	Switz -33.40	Japan -33.40	-33.40	Nether 28.89	US 10.14	1.74	14.67	Finland -43.34	Finland 11.14	Finland -15.12	-33.50	Finland 8.18	Australia 5.74	Australia -22.04	Norway -19.93	Italy -14.15	
Lowest Return	Singapore -30.09	Norway -30.06	Belgium -33.55	NZ -38.18	Germany -38.18	Finland -38.18	Finland 19.40	Finland 6.14	-2.29	Japan 6.24	Ireland -2.09	Ireland -71.52	Japan 6.25	-21.95	-36.43	Spain 3.00	Singapore 1.70	-29.77	-24.16	Denmark -15.77

In US dollars.

Source: MSCI developed markets country indices (net dividends). MSCI data © MSCI 2017, all rights reserved.

Indices are not available for direct investment. Index performance does not reflect expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results.

This trend was also observable in emerging markets. As Exhibit 2 illustrates, 13 different emerging market countries (out of 20) had the best-performing market in a given year, and no country had the best-performing market in consecutive years.

Exhibit 2: Equity Returns of Emerging Markets Annual Return (%)

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Highest Return	Turkey 110.05	Korea 141.15	Turkey 282.41	Czech Rep. 1.62	Russia 55.85	Czech Rep. 44.16	Thailand 144.58	Colombia 132.95	Egypt 161.59	China 82.87	Peru 94.74	Colombia 25.10	Brazil 128.62	Thailand 56.27	Indonesia 6.50	Turkey 64.67	Taiwan 9.77	Egypt 29.35	Hungary 36.31	Brazil 68.75
	Russia 110.12	Philippines 13.45	Russia 247.05	Malaysia 4.24	Korea 45.71	Indonesia 42.83	Turkey 125.83	Egypt 107.52	Indonesia 74.83	Brazil 79.59	Chile 127.53	Indonesia 35.35	Peru 127.53	Malaysia 56.27	Malaysia 6.50	Philippines 64.67	Philippines 9.77	Indonesia 29.35	Russia 36.31	Russia 68.75
	Hungary 56.21	Thailand 11.56	Malaysia 69.21	-11.37	-11.37	45.77	Malaysia 115.01	Brazil 102.83	Hungary 73.77	Russia 62.55	Turkey 74.81	S. Africa -37.89	Russia 104.91	Chile 48.81	Philippines 0.10	Egypt 47.10	Malaysia 7.65	Philippines 26.40	India -6.12	Peru 55.61
	Mexico 53.92	Czech Rep. 0.54	Indonesia 19.42	Chile 19.42	Peru 19.42	Peru 30.50	Peru 37.25	Colombia 55.00	Philippines 59.65	India 73.11	Peru -40.11	102.81	Colombia 43.41	Thailand -2.40	Poland 40.97	China 4.18	India 23.87	Hungary -6.25	Hungary 35.37	
	Colombia 41.76	Poland -6.69	Korea 92.42	-15.35	19.55	27.99	Egypt 91.34	Poland 81.52	Russia 59.93	China 66.24	Malaysia -41.21	Turkey 95.45	Malaysia 37.51	Czech Rep. 35.99	Colombia 3.95	China 3.95	Turkey 3.95	Korea -6.33	Thailand 27.91	
	HK 31.23	Hungary -6.16	Egypt 98.40	S. Africa -17.19	10.47	27.59	China 87.57	Indonesia 52.21	56.94	India 51.00	58.43	-42.75	86.73	35.49	-5.02	34.94	3.62	16.84	-7.62	26.48
	Brazil 27.34	Taiwan -20.64	India 67.35	-20.49	5.25	25.36	84.41	45.32	49.11	45.80	58.93	-42.94	84.35	34.62	-11.76	29.05	1.35	Peru 10.51	Taiwan -10.97	19.59
	Peru 20.59	India -21.24	Mexico 50.07	-21.74	4.56	15.71	78.35	44.91	Poland 41.93	Indonesia 53.83	Taiwan -45.98	80.26	Taiwan 34.91	Mexico -12.11	25.97	0.21	10.05	Taiwan -14.21	Mexico 18.41	
	India 11.27	Egypt -27.00	Brazil 67.23	-2.91	-2.91	8.82	78.23	42.03	37.57	India 41.44	Thailand 46.63	-48.27	77.61	27.61	-13.36	23.10	Philippines -2.01	China 3.26	Czech Rep. 17.52	
	Chile 5.92	S. Africa -27.56	S. Africa 57.20	-26.90	-2.83	8.37	Russia 75.94	36.47	35.00	Malaysia 37.14	Malaysia 46.07	-0.83	China 77.31	Korea -18.24	Hungary -3.83	S. Africa 5.69	Chile -16.85	Chile 16.81		
	-6.29	-20.50	62.71	-30.03	-5.49	1.59	Colombia 66.93	29.01	23.34	Czech Rep. 34.69	Philippines 41.68	-51.07	72.06	Taiwan 22.79	-19.30	21.43	-5.78	Czech Rep. -2.42	Indonesia 9.25	
	S. Africa -3.18	Malaysia -33.31	Thailand 47.16	China -30.34	Hungary -5.16	1.20	Czech Rep. 66.30	Philippines 24.96	Poland 33.70	China 32.53	Egypt -42.38	Peru 72.06	Peru 21.24	China -20.00	20.24	Malaysia -5.82	Hungary -19.23	Mexico -20.36	China 1.11	
	Poland -22.39	-31.53	39.01	-33.85	-16.99	-0.66	45.96	22.36	23.92	29.33	25.79	-54.49	67.98	20.95	-20.15	19.01	-5.10	-10.66	-23.32	0.69
	Mexico -22.69	Mexico -33.53	Poland 31.50	-43.71	-13.31	Philippines -13.31	Philippines 42.76	19.11	21.82	20.90	Russia -55.07	62.63	China 19.40	Russia -21.37	17.66	-14.34	-10.70	Korea -23.52	Egypt -1.43	
	China -27.59	Brazil 30.50	Taiwan -44.50	Hungary -19.99	China -14.05	-19.99	Taiwan 42.45	Malaysia 15.17	19.77	China 20.53	Chile -68.01	Poland 4.83	Poland 15.95	China -21.59	14.39	Brazil -15.79	China -19.93	Chile -24.91	Czech Rep. -2.45	
	Philippines -62.59	Peru -40.22	China 13.33	Philippines -45.01	-19.45	-19.45	35.94	9.83	18.30	Hungary 17.08	S. Africa 16.14	-56.20	56.63	Indonesia 12.42	-25.52	14.27	-21.14	-13.60	-25.13	-3.89
	Korea -56.67	Colombia -41.71	Hungary 11.66	Turkey -45.85	China -24.70	Taiwan -24.45	Poland 35.48	5.69	15.76	Indonesia 13.78	Hungary 16.80	-61.53	Malaysia 52.06	6.81	HK 33.65	Chile 8.34	-21.41	-13.74	Philippines -6.10	
	Malaysia -43.37	China -43.37	Czech Rep. 18.56	Korea -22.44	Poland -22.44	-22.44	Philippines 32.31	Mexico 3.16	9.16	Thailand 11.61	China 15.19	15.20	China -64.63	Poland 4.83	China 4.83	Turkey 5.22	-23.10	Indonesia -19.93	Peru -3.12	
	Thailand -73.43	-52.51	3.32	-56.27	-32.66	-30.65	32.31	1.39	7.25	Thailand 11.61	12.15	-64.63	China 35.74	-1.66	-37.17	3.48	-26.82	-27.44	-41.18	-5.58
Lowest Return	Indonesia -74.06	Russia -62.59	Colombia -41.38	China -61.90	India -41.30	-41.30	China 35.74	Thailand 26.61	Thailand -0.92	Malaysia 2.29	Taiwan -6.97	Taiwan 9.13	Russia -73.83	Czech Rep. 27.77	-6.59	China 0.34	Brazil -29.84	Peru -45.86	Colombia -41.80	Denmark -11.39

In US dollars.

Source: MSCI emerging markets country indices (gross dividends). MSCI data © MSCI 2017, all rights reserved.

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This data shows that it is difficult to know which markets will outperform from year to year. By holding a globally diversified portfolio, investors are instead well positioned to capture returns wherever they occur.

Due to the recent positive performance of international stocks, investors today may be less worried about a global approach to investing than they may have been in the past. Over the last several years, however, strong performance in the US equity markets has led some market participants to question the value of holding a globally diversified portfolio. In different market environments, and as sentiments about global diversification and its value ebb and flow, it is helpful to remember that history has not shown any one market around the world to be a consistent outperformer.

Clearly, attempting to pick only winning markets in any given period is a challenging proposition. By pursuing a globally diversified approach to investing, one doesn't have to attempt to pick winners to achieve a rewarding investment experience. By expanding the investment opportunity set beyond their domestic stock market, investors can help increase the reliability of outcomes. While diversifying globally implies an investor's portfolio will not be the best performing relative to any one stock market, it also means it will not be the worst performing.

Source: Dimensional Fund Advisors LP.

Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results. Diversification does not eliminate the risk of market loss.

There is no guarantee investment strategies will be successful. Investing involves risks including possible loss of principal. Investors should talk to their financial advisor prior to making any investment decision.

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