Quick Take: Diversification Matters (Finally)

ACADIAN

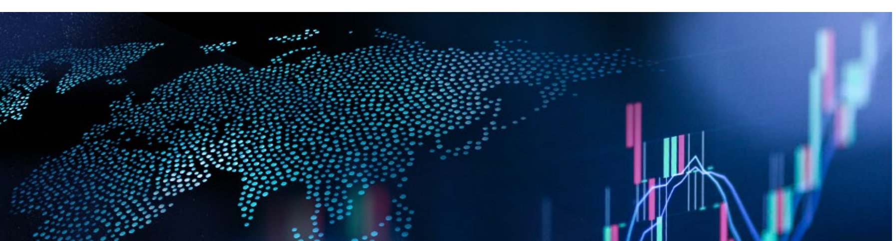
May 2025

Shaky U.S. equities: A wake-up call for asset owners

- Relative to the U.S., non-U.S. equities had their best start to the year in three decades (top chart). MSCI's All-Country World (ACW) ex-U.S. Index outperformed by 14.3% through April (+9.3% vs. -5.0%).
- The drivers were roughly equally split between 1) relative strength of non-U.S. stocks in local currency terms and 2) the U.S. dollar's weakest four-month start to the year since 1986.
- Nevertheless, U.S. equities still have a historically large weight in ACWI—64% at end-April, not far from the all-time high of 67% reached in 2024 and above levels reached in other periods of U.S. market strength (bottom chart).

Are investors overexposed to U.S. equities and the dollar?

- The U.S. weight in the global market portfolio may look high to investors concerned about the uncertainty that has rattled U.S. equities and the dollar.
- To illustrate, an investor who expects that U.S. equity returns will be flat relative to both EAFE and EM (in USD terms), might—based on conventional assumptions from portfolio theory—allocate only about 40% to the U.S. in maximizing expected risk-adjusted returns across the three regions (bottom right chart).*
- But the recent relative strength of non-U.S. equities serves as a caution against reflexively expecting post-GFC-like U.S. equity market and dollar dominance to continue. In a highly uncertain world, balancing allocations towards international equities may instead look more prudent.



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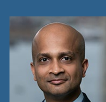

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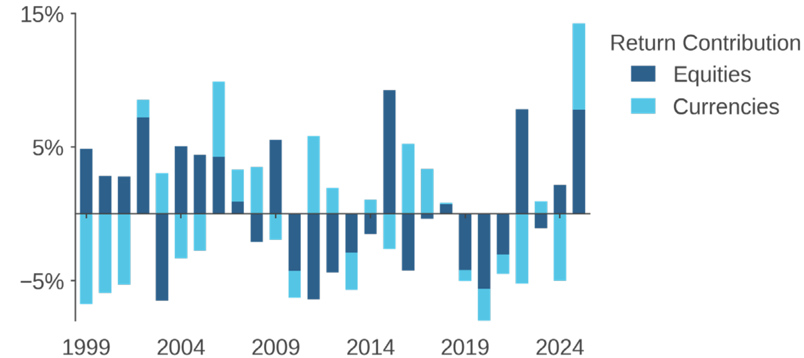
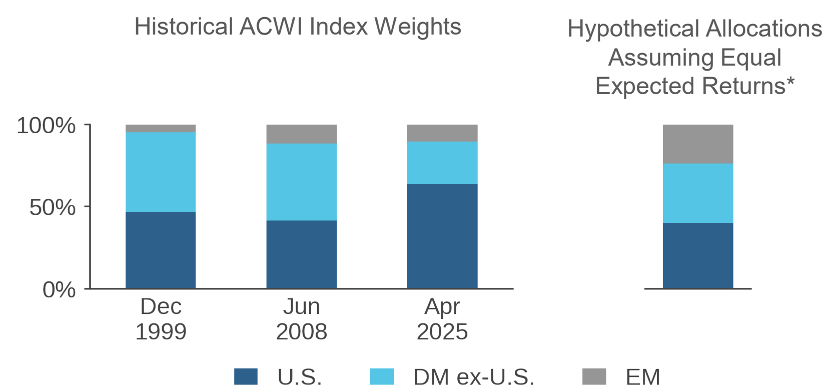
Non-U.S. equities: historically strong start vs. U.S.

Jan-Apr relative USD returns: MSCI ACW ex-U.S. minus MSCI U.S. Index



Regional weightings



* Results of mean-variance optimization assuming 1) equal expected excess USD returns for U.S., DM ex-U.S., and EM and 2) covariance matrix estimated from 10-year trailing historical returns. Hypothetical results do not reflect trading, borrow costs, and other implementation frictions, and they are not indicative of actual future results. Every investment program has the opportunity for loss as well as profit. It is not possible to invest directly in an index. Every investment program has the opportunity for losses as well as profits.

Sources for Top and Bottom charts: Acadian based on index data from MSCI. For illustrative purposes only.

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