

## OUTSIDE THE FLAGS

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# The World Cup of Investing

When you talk about Ireland, cricket is not the first sport that springs to mind. Yet in the 2007 World Cup, the Irish defeated highly rated Pakistan, on St Patrick's Day no less. Picking the best countries to invest in can be just as unpredictable.

On paper, some countries look much stronger than others. In that immortal cricket match, the Pakistan team was full of star professionals. Ireland, by contrast, was a team of no-name amateurs that had never beaten a test-playing nation. Yet Ireland stunned the cricketing world, winning the game by three wickets.

Minnows don't just win on the sporting field. In three of the past four years, tiny New Zealand has been one of the world's top performing developed world equity markets, holding first position in 2011, fifth in 2012 and second in 2014.

Denmark, a country not much bigger than New Zealand, has been another top performer, holding second position on the developed world market tables in 2010 and 2012 and third position after the Kiwis last year.

This isn't to say that those two nations will continue to excel. Look at the example of Spain, which was the worst performing market in 2010 and 2012 as the euro zone crisis dragged on, only to vault into third position globally in 2013.

Country returns are unpredictable and don't necessarily reflect what's going on in those markets' economies at the time. In 2013, amid deflation and continuing sluggish growth, the Japanese equity market put in its best one-year performance in four decades.

In fact, if you assign a colour to each developed market and rank them from the top to bottom performers for each year over the last decade in percentage terms, the resulting haphazard pattern resembles a quilt by a sight-impaired seamstress.

**Table 1 – Developed Equity Markets 2004-2014 (% in \$AUD)**

2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Austria 64.9	Canada 37.2	Spain 38.7	Hong Kong 26.9	Japan -10.8	Norway 45.2	Sweden 17.5	New Zealand 5.5	Belgium 37.4	USA 53.3	USA 23.3
New Zealand 43.9	Japan 34.2	Singapore 36.3	Germany 21.5	Switzerland -12.5	Australia 36.9	Denmark 14.8	USA 1.4	Denmark 29.3	Germany 52.8	New Zealand 17.4
Belgium 38.0	Austria 33.3	Norway 34.8	Norway 18.2	USA -21.4	Singapore 35.0	Hong Kong 8.2	UK -2.6	Singapore 29.0	Spain 52.7	Denmark 16.1
Norway 33.0	Denmark 33.1	Sweden 33.2	Canada 16.5	Spain -25.2	Sweden 27.4	Singapore 7.3	Switzerland -6.8	Germany 28.9	Netherlands 52.7	Hong Kong 14.9
Sweden 31.0	Norway 32.9	Denmark 28.9	Singapore 15.4	France -28.6	Hong Kong 24.3	Canada 5.8	Norway -10.0	New Zealand 27.3	Belgium 48.4	Belgium 13.9
Italy 27.3	Switzerland 24.4	Belgium 26.9	Australia 15.4	Canada -31.4	Belgium 22.2	Japan 1.4	Belgium -10.6	Hong Kong 26.3	Japan 47.9	Singapore 12.7
Denmark 25.7	Australia 24.1	Austria 26.8	Denmark 12.9	Germany -31.8	Canada 21.2	USA 0.8	Australia -11.0	Austria 24.0	Switzerland 47.2	Canada 11.0
Australia 25.3	Singapore 22.3	Germany 26.3	Spain 11.4	Singapore -33.7	New Zealand 16.7	Australia 0.6	Netherlands -12.1	Australia 20.2	France 46.9	Switzerland 9.3
Spain 23.9	Netherlands 21.7	France 24.9	Netherlands 8.4	Denmark -34.0	Spain 11.4	Switzerland -1.8	Spain -12.3	Sweden 20.1	Denmark 45.7	Australia 5.6
Hong Kong 20.1	Sweden 17.9	Italy 23.0	France 1.8	Netherlands -34.8	UK 11.2	Norway -2.6	Canada -12.7	France 19.5	Sweden 44.8	Netherlands 5.6
Singapore 17.5	Germany 17.5	Netherlands 22.0	New Zealand -2.1	UK -34.9	Austria 11.1	Austria -3.5	Japan -14.3	Netherlands 18.8	UK 40.3	Japan 5.0
Canada 17.5	France 17.5	Australia 21.5	UK -2.6	Sweden -36.9	Netherlands 10.4	UK -4.5	Sweden -16.0	Switzerland 18.5	Italy 40.1	Spain 4.3
UK 14.9	Belgium 16.6	UK 21.3	Italy -4.7	Italy -37.0	Denmark 6.0	Germany -4.8	Denmark -16.0	Norway 16.9	Austria 31.9	UK 3.5
France 13.9	Hong Kong 15.9	Hong Kong 21.1	USA -5.2	Australia -37.9	France 2.3	New Zealand -4.9	Hong Kong -16.0	USA 13.6	New Zealand 29.4	Sweden 1.1
Germany 11.7	UK 14.8	Switzerland 18.3	Switzerland -5.3	Hong Kong -38.6	Italy -1.8	Netherlands -10.6	France -16.9	UK 13.5	Hong Kong 29.2	Italy -1.1
Japan 11.4	USA 12.4	Canada 9.4	Austria -8.1	New Zealand -41.8	USA -2.0	Belgium -12.5	Singapore -17.9	Italy 10.8	Norway 27.2	France -1.5
Switzerland 10.5	Spain 11.6	New Zealand 8.3	Sweden -9.5	Norway -55.0	Switzerland -2.7	France -15.8	Germany -18.1	Canada 7.4	Canada 22.8	Germany -2.0
Netherlands 7.9	Italy 9.0	USA 6.5	Belgium -12.6	Belgium -57.8	Germany -2.9	Italy -25.4	Italy -23.2	Japan 6.5	Australia 21.1	Norway -14.7
USA 5.9	New Zealand 8.8	Japan -1.3	Japan -13.9	Austria -60.2	Japan -17.5	Spain -31.5	Austria -36.4	Spain 1.5	Singapore 18.3	Austria -23.2

Source: MSCI developed markets country indices (net dividends). MSCI data copyright MSCI 2015, all rights reserved. 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.

Table 1 shows you the percentage performances of all the developed markets over the past decade, ranked from top to bottom.

This lack of a pattern in country returns is actually good news for the diversified investor. It means if you spread your equity allocation internationally, you reduce the risk of any one bad performance having an undue effect on your portfolio.

In other words, the chances are that if one part of your global portfolio is struggling, another will be doing significantly better. That's the power of diversification.

Obviously, it isn't as simple as that. There are questions about how much you want to bias your portfolio to your home country. In Australia, for instance, there are tax advantages to doing so with the system of dividend imputation.

Another question is around what you do about currencies. Some people choose to leave their international portfolio unhedged against currency moves. In this case, a depreciating home currency can soften the blow of falling international markets and magnify the windfall from rising markets, once you convert to your local currency.

On the other hand, a rising home currency can pare back your international returns if you are unhedged.

It works the opposite way for hedged investors. You are protected when your home currency is rising, but you also don't get the benefit when it falls.

The research shows no clear investment case one way or the other. So some people choose to have a dollar each way and be 50% hedged and 50% unhedged.

However, once you resolve with your advisor these questions around home bias and currency hedging, there is a strong case for international diversification.

It provides you exposure to a broader array of economic forces, companies and sectors than were you to keep all your money in your home market. It spreads your risk and it means you're not taking a more concentrated bet than you need to.

To use our cricketing analogy, being internationally diversified means you're more likely to slowly and steadily accumulate runs than trying to hit every ball for six.

Now, who do you think is going to win the 2015 World Cup?



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