On The Mark

CAPSTAR FINANCIAL

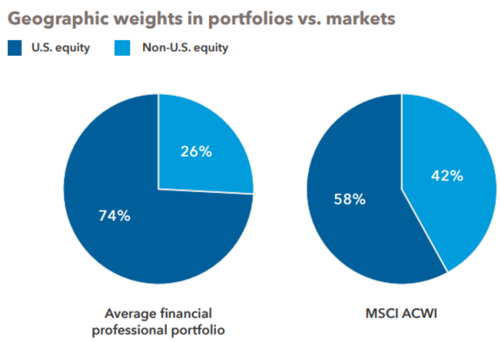
Is your portfolio ready for what's next?

Key Takeaways

- Despite the economic upheaval brought on by COVID in 2020, 2021 remains a year of hope.
- The start of the new year is a great time for investors to evaluate how their portfolios have likely drifted after a wild ride like 2020 and prepare for the next opportunities and risks.

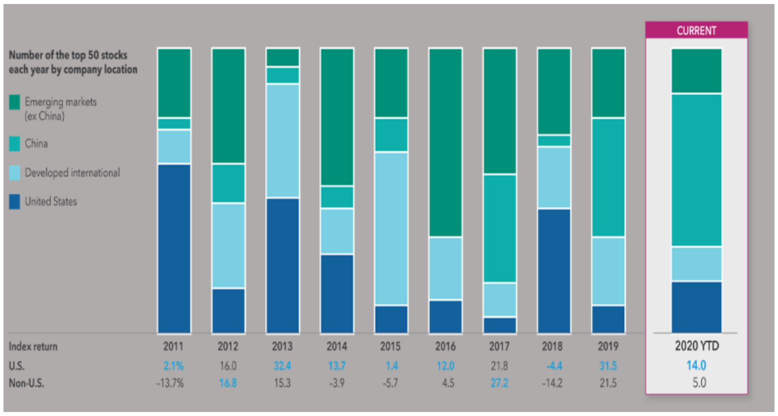
Many of us are happy to see 2020 come to an end. While the economy is not completely out of the woods, vaccine distribution and support from global central banks offers hope and light at the end of the tunnel. In 2021, amid a healing global economy, markets offer a wide range of opportunities and risks. To prepare for these opportunities and risks, investors should begin by evaluating your portfolios. It is likely that many portfolios have drifted substantially from the planned mix of investments.

When it comes to investing in the stock market, investors tend to hold a large allocation to their country of residence. This is known as home-country bias. Capital Group's Portfolio and Analytics team analyzed more than 4,000 advisor portfolios last year and found the average financial professional portfolios had almost three times as much domestic equity as international. In comparison, the global equity index (MSCI All Country World Index) has an allocation of 58% in US equities in comparison to 42% in international equities[1]. By having a US-centric focus, investors are essentially ignoring nearly half of the opportunity set in equity investing.



Source: Capital Group. As of 9/30/20

Home-country bias has only grown stronger over the past decade as US equities have outperformed international equities. However, a look at individual companies instead of index returns, shows that the companies with the best returns are overwhelmingly located outside the US. Nearly 75% of the top stocks since 2011 have been based outside of the US[2].

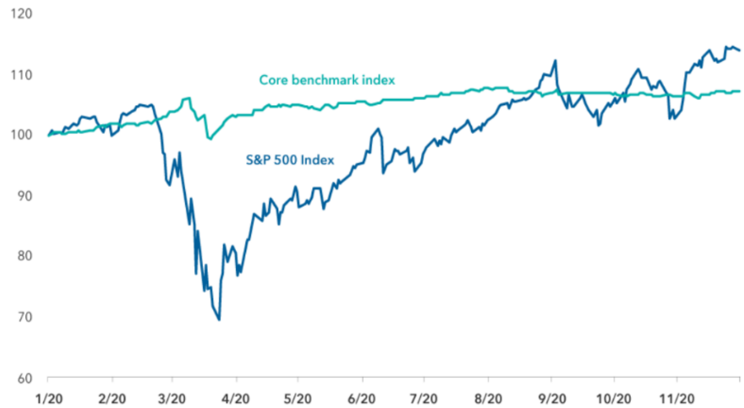


Source: Capital Group. As of 11/30/20

With US equities at all-time highs, failing to look across borders at shares of non-US companies means you are likely overlooking opportunities.

When it comes to investing in bonds, investors have been shifting towards riskier bonds in search of higher yield. Since 2018, the average allocation to riskier bond categories has increased from roughly 12% to nearly 20%[3]. Riskier bonds carry similar risk to equities and thus diminish the benefits of diversification. Instead, even as interest rates are likley to remain low, an allocation to high-quality core bonds that includes Treasuries will remain crucial to buffer volatility. This was never more evident than the humbling experience shown in 2020, as equity markets took the fastest tumble and recovery in history while core bonds held steady. Looking forward, with low interest rates, investors should temper their return expectations for core bonds in the coming years, but the need for diversification and capital preservation remains.

The core bond benchmark held steady as stocks sank



Source: Capital Group. Bloomberg Index Services Ltd., Morningstar. Core benchmark shown is the Bloomberg Barclays U.S. Aggregate Index. As of 11/30/20. Returns indexed to 100 as of 1/12020

Despite the economic upheaval bought on by COVID in 2020, 2021 remains a year of hope. The start of the new year is a great time for investors to think about what the next opportunity could be, and at the same time keep an eye on the ball for managing near-term risks.

1 https://www.capitalgroup.com/advisor/pdf/shareholder/MFCPBR-080-646301.pdf
2 https://www.capitalgroup.com/advisor/insights/articles/5-keys-investing.html
3 https://www.capitalgroup.com/advisor/insights/articles/5-keys-investing.html

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IMPORTANT INFORMATION

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