Investors' Chronicle

Investing explained

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Investing overseas

The UK is home to some of the world's leading businesses and investment opportunities. But opportunities abound overseas.

Having a diversified investment portfolio is key, which is part of the reason why most investors should choose to allocate globally. What's more, many international stock markets have a better performance record than the UK.

Most UK investors will seek overseas exposure via funds managed or listed in the UK. But advances in technology have made It much easier to buy overseas shares directly, with platforms dealing with currency exchange and different market opening hours for you.

Most platforms offer extensive international coverage, with a vast quantity of unit trusts, investment trusts and exchange traded funds (ETFs) available. This facilitates two separate approaches, says Dan Boardman-Weston, CIO at BRI Wealth Management: a "broad-brush" or "specific overseas exposure".

The broad-brush approach may focus on index funds covering the largest businesses in an economy, such as the S&P 500 (more or less the biggest 500 companies in the US). This gives investors a foothold into a market. A more focused approach may be centred on specific stocks within a market, such as a technology business in Israel, a mining firm in Australia or consumer goods manufacturer in continental Europe.

Not all investment platforms can give you direct access to international shares. But the major ones - IG, Hargreaves Lansdown, AJ Bell Youinvest and interactive investor have access to several international exchanges.

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What's in this guide?

More from this series

Guide to getting started

Guide to investing in shares

Guide to investing in funds

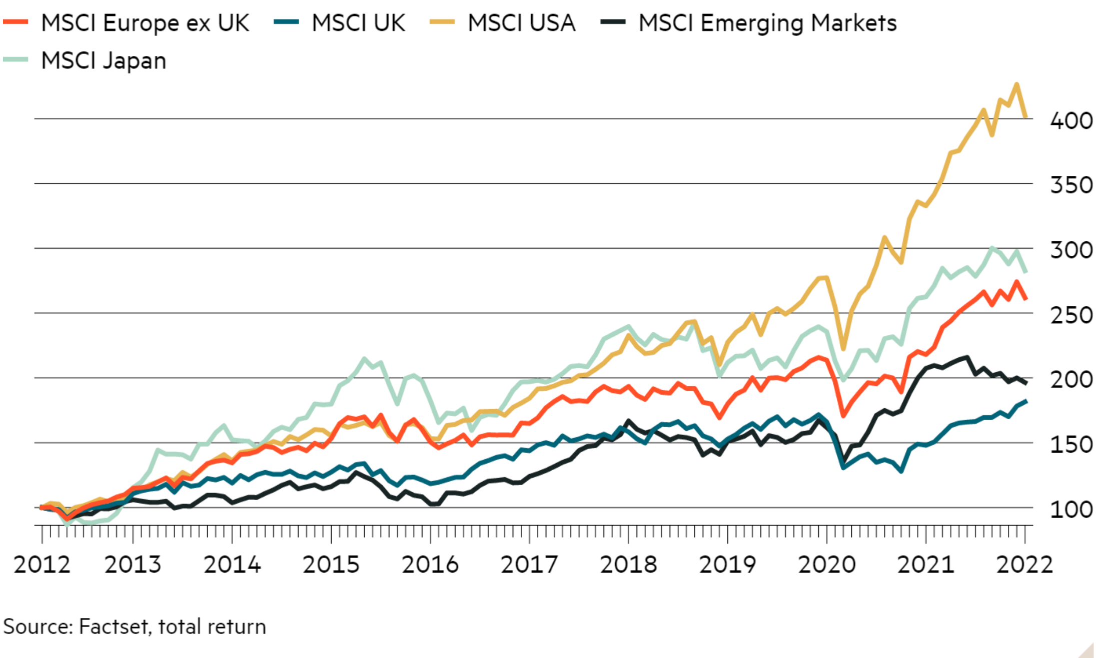
Why overseas exposure is important

The term 'diversification' is a key tenet to a successful investment strategy, and is epitomised in overseas investing, Boardman-Weston says. "There are over 40,000 companies listed on global stock markets, yet the UK only has 2,000. By solely focussing on one market such as the UK you're restricting your opportunities and missing out on some great investments."

Boardman-Weston points to one piece of evidence: better returns can be found abroad. "Over the last ten years, it's not been a great move to just be invested in the UK. The FTSE 100 has returned just under 100 per cent including dividends, whereas the global stock market, the MSCI All Country World Index, has returned just under 260 per cent including dividends," he says.

UK STOCK MARKET HAS LAGGED INTERNATIONAL PEERS

rebased (%)



Source: Factset, total return

Moreover, home bias, or the tendency for investors to allocate heavily towards domestic equities, can elevate risk, says Craig Melling, head of investment at Progeny Asset Management, although there are arguments to be made both ways.

Melling says that he affords clients a home bias “of around 25 per cent” seeing it as prudent to accommodate some domesticity. “Since their assets are UK-based, their salaries are from the UK and liabilities are UK-based, it is important to have exposure to your country of residence,” he says.

Investment profiles

The various stock markets of the world will often be moved by the same global factors, but each will have its idiosyncrasies. Companies of all types and sectors are found in most markets, but some will lean more heavily towards certain areas.

When constructing an international portfolio, thinking about your attitude to risk and how much exposure you are comfortable to have in equities is important, says Boardman-Weston. Once that question is answered then investors can choose their geographical asset allocation depending on several factors.

“If we look at the MSCI All Country World Index (ACWI), which is a global equity index that is constructed by market capitalisation, then this gives a steer as to how you could passively allocate to different geographies,” he says.

Under this approach, roughly 61.5 per cent would be allocated to North America, 17.5 per cent to Europe, the Middle East and Africa, 12 per cent to Emerging Markets and 9 per cent to Asia Pacific.

Boardman-Weston continues: “Depending on your level of knowledge you could then tilt those weights to markets that you consider more attractive or take a completely bottom-up approach and just focus on finding the best companies or funds, paying little attention to asset allocation.

“It has been shown that asset allocation is the major driver of investment returns and so it does need to be thought about carefully and it’s important that you have sufficient geographic diversification,” he says.

Individual shares

As mentioned, not all investment platforms allow investors to invest in individual overseas shares. On top of this, the tax implications, cost and different time zones need to be considered, according to Melling, while press coverage to inform investors is likely to be relatively low outside a company's market of origin.

Moreover, the platforms that do offer individual overseas shares involve different fees and charges that can vary significantly. Withholding tax on dividends can also make investing directly overseas less attractive, meaning that plenty of research is essential. Also make sure you check what foreign exchange fee your platform is charging you, as these can vary widely and eat into your returns.

Fractional share dealing

Most platforms will only let you buy whole shares. Some of the newer apps, however, have introduced fractional share dealing. This might be appealing given that one share In Amazon would set you back by $3,224 at the time of writing.

Fractional share dealing allows investors to own a portion of an individual share, enabling greater access for investors with lower amounts of capital, and is most commonly used when investing in large US stocks. Boardman-Weston points towards the example of Warren Buffett's Berkshire Hathaway, which at the time of writing has a price of around $480,000 (£355k) per share.

"That means that most investors can't buy that share but with fractional share dealing you can buy far smaller quantities. Not every platform offers fractional share dealing so make sure to do the appropriate research," he says.

Currency considerations

Currency movements are an important element of calculating the returns from an investment, as the headline returns quoted on indices are typically in their local currency.

For example, in 2020, the S&P 500 returned 17.75 per cent in US dollars however, in sterling the return was just 12.67 per cent, according to FE Analytics.

In the short term, the changing value of currencies can impact on returns – a 1 per cent strengthening of the pound against the dollar can immediately cancel a 1 per cent return on a US-based investment.

Being able to accurately predict the direction of currencies is incredibly difficult, yet it is less of a concern for long-term investors, as currency fluctuations will broadly iron out over time.

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