Many US investors allocate to international stocks, but there is no clear consensus on whether it is better to allocate to developed markets vs emerging markets or in what proportions. Below is some data and some thoughts on this question. The term "international" often refers to the developed market stocks, while "emerging" refers to stocks from emerging markets. Our analysis will focus on the MSCI EAFE Index (since it is the most popular, even though there are other indices with arguably better coverage) for developed markets and the MSCI Emerging Markets Index for emerging markets. Since inception, emerging markets have outperformed developed markets by a wide margin. The annualized performance of 8.78% is nearly double developed markets' annualized performance of 4.87%. However, the past 35 years is a story in two acts. For the first 20 years, returns for both developed and emerging stocks were elevated with emerging markets returning 15.04% annually versus developed markets 7.19% annually. Both developed and emerging markets were hammered from 2007 to 2009 and both have exhibited low annualized returns since. Developed markets have returned an annualized 1.8% since the end of 2007, while the emerging markets have only returned an annualized .83% since. So developed has actually outperformed emerging markets in the second act. In my (and many others') analysis, most of the volatility (for US investors) in international stocks comes from the currency risk. As the above chart shows, the volatility and drawdowns in emerging markets are not that much more than in developed markets. When looking at the global market cap, developed markets typically account for 25-30% and emerging markets often range from 10-15%. The percentages fluctuate due to the relative performance of the regions. Each of these indices also is primarily composed or large-caps, so we are comparing apples to apples. It is clear that investing in emerging markets stocks would have been more beneficial over the long-term. Recent performance complicates that decision a bit. Just as stock market returns are "lumpy" and factor returns are lumpy, the outperformance and underperformance of international stocks is lumpy and time dependent. Of course, it is anyone's guess about what the future holds. My personal opinion is that since emerging markets have had periods of massive outperformance without much additional volatility, I personally overweight emerging market exposure and underweight developed market exposure. As the charts show, emerging markets have outperformed by a wide margin since inception. This was primarily driven by emerging market outperformance in the first 20 years, even though developed markets have slightly outperformed recently. Emerging markets have had higher returns historically, relative to developed markets outside the US. However, this may or may not continue in the future. Emerging markets had higher returns than developed international markets from 1987 through 2007, but they have had lower returns since then. Emerging market stocks tend to be more volatile due to less liquidity and more extreme currency fluctuations, among other factors. There is an additional factors that emerging markets are more vulnerable to various geopolitical and economic shocks and a lower degree of rule of law. This is why diversification is very important when investing in emerging markets. The five largest emerging markets by market cap are: China Taiwan India South Korea Brazil Some emerging markets benefit from inflation, while others do not. It depends on what is inflating and whether that market is a producer or consumer of that good or service. For instance, if oil prices rise, it may be good for Saudi Arabia (an oil producer) and bad for India (an oil importer). Emerging markets offer rapid growth potential and investment opportunities, while developed markets provide stability and established infrastructure.Emerging markets and developed markets offer unique investment opportunities. While developed markets have established economies with strong growth and stable investment potential, emerging markets offer greater opportunities for sudden growth. Read on for the pros and cons of emerging markets versus developed markets to understand the investment opportunities in each. What is an Emerging Market?An emerging market in investing refers to a country whose economy is transitioning into a developed market economy. Emerging markets are in the process of transitioning from a low-income, even preindustrial economy, to a modern economy with a higher standard of living. As the emerging market grows, the nation becomes more engaged with global markets. Other characteristics of emerging markets include rapid gross domestic product (GDP) growth, increasing income per capita, increased commodity prices and increased debt and equity market liquidity. To become an emerging market, countries generally need an established financial system infrastructure, regulatory institutions and a unified currency. The most famous emerging markets of the last two decades are the BRICS countries: Brazil, Russia, India, China and South Africa. The GDP of these countries has grown significantly in the last two decades, suggesting that they could become major players or even leaders in the global economy and global market share in the decades to come.As an investor, you might seek out emerging markets for the possibility of high returns. These markets typically experience faster economic growth as measured by GDP. But with higher returns come higher risk as well.What is a Developed Market?Investors consider developed markets as economies with the greatest development in financial infrastructure and regulation and the largest capital markets. Generally, a developed country has a high GDP, high income per capita compared to global averages, greater market liquidity and higher debt. Other characteristics of a developed market include openness to foreign ownership and investment, ease of capital movement and efficiency of market institutions. Developed markets include the United States and Canada, most of Europe, Israel, the U.K., Australia, New Zealand, Singapore, Japan and Hong Kong. Comparing Emerging Markets vs. Developed MarketsShould you invest in emerging markets or developed markets? Here are key comparisons:RiskRisk factors vary between markets. Generally, emerging markets are considered higher risk than developed markets. However, any investing activity can come with significant risk. Investors need to know about the risk associated with changes in currency exchange devaluations, government policies or a destabilized economy resulting from changes in tax structures, internal conflict, liquidity issues or a lack of capital that can present additional risk in emerging markets. Developed markets aren't without risk. Investors still need to be alert for bear markets or market adjustments, increasing inflation and the performance of individual stocks or funds to balance risk within their portfolios. Signs of ProgressSigns of progress vary for emerging markets versus developed markets. For emerging markets, look for physical financial infrastructure, including banks, a stock exchange and a unified currency. Watch for reforms and the development of institutions like those of modern developed countries aimed at promoting economic growth. Governments of emerging markets may pursue industrial and trade strategies that encourage economic growth and industrialization.In developed markets and emerging markets, look for signs of stability like low unemployment, steady inflation growth, increasing GDP, increased new home construction and a high score on the consumer confidence index as signs of growth. Market Economies ClassificationsAs definitions of emerging markets vary among investors, there is currently no agreed-upon definition and classification of emerging markets. Generally, factors weighed include income levels, employment levels, GDP growth rates and the quality of the financial system. Other factors may include financial infrastructure, government stability and openness to foreign investment.The International Monetary Fund (IMF) classifies 20 countries as emerging markets, while Morgan Stanley Capital International (MSCI) classifies 24 countries as emerging markets. Countries can move to developed market status or regress to frontier markets. In recent years, several institutions have downgraded Greece to an emerging market, joining the Czech Republic, Hungary, Poland and Turkey as the only non-developed EU markets. Around the same time, Argentina and Qatar were upgraded to emerging markets from frontier markets. Future OutlookEmerging markets are just that, a place of potential future development and strong growth. But it's up to these countries to stabilize their governments and economic systems to build future economic growth. For that reason, the future outlook varies. Developed markets are generally considered more stable and expected to make more modest, consistent progress. Even developed economies and stock markets can experience destabilizing influences, changes in government or policies that can have ripple effects on the economy. While emerging markets carry more risk, any investment carries risk and uncertainty. How to Invest in Emerging and Developed MarketsInvesting in emerging markets offers unique opportunities for growth potential, as these economies often exhibit faster growth rates compared to their developed counterparts. Investors may find appealing returns as these countries continue to develop their infrastructures, bolster their financial markets and expand their consumer bases. However, with the potential for high returns exists, there are also inherent risks involved in investing in these regions. Political instability, currency volatility and less mature regulatory environments can create challenges that investors must navigate carefully. In contrast, developed markets are often associated with stability and lower risk profiles. These economies typically have established financial systems, predictable regulatory environments and mature markets, leading to steadier returns over time. Investors looking for reliable income streams can find opportunities in dividend-paying stocks, bonds and real estate within developed markets. While the growth potential may be slower in these regions, they provide a cushion against the volatility often seen in emerging markets. Investors can invest in both markets by buying shares in managed funds. This can help mitigate the risk of emerging markets while offering greater investment growth potential. Learn more about emerging market ETFs and how to invest in emerging markets. Invest in Emerging and Developed Markets with Benzinga's Best BrokersHere, you can find some of Benzinga's best brokers for both emerging and developed markets. These professionals can help you create a customized, risk-managed investment strategy. Final Tips on Investing in Emerging vs. Developed MarketsInvesting in any market requires in-depth research and understanding. Look at historical performance, fund or company management, liquidity and total debt. Remember to diversify across asset classes, investment types and markets. With strong investment knowledge and a risk-balanced strategy, investors can take advantage of growth opportunities in emerging markets and profit from stable, long-term returns offered by developed markets. Frequently Asked Questions Yes, you can invest in emerging markets through funds, ETFs or other investment vehicles. Emerging markets present excellent investment opportunities. Generally, emerging markets are considered riskier than developed markets. The best emerging market stocks vary based on who you ask. Some popular options include India-based MakeMyTrip and ICICI Bank or iShares Core MSCI Markets ETF (IEMG), which touches many global regions for portfolio diversification. Or, you can consider the MSCI Emerging Market index or find the best emerging markets ETFs right now. When you're looking through global investments, it can be difficult to choose between an international stock mutual fund or an emerging market fund. It helps to understand what each one is and their differences so that you can decide whether to use them in your portfolio. Emerging markets are countries with quickly growing economies, such as Brazil, China, India, and Mexico.International stock funds choose the best-performing stocks from a range of developed economies, though many of these are also available domestically.Short-term returns are often higher from emerging markets. International funds can be more stable in the long term.Investing globally provides diversification. Still, conservative investors may want to limit international investments to 20% of their portfolios. Emerging markets are countries with rapidly growing economies that are generally "less developed" than larger or more established nations, such as the United States and Western European countries. Some of the largest countries that are considered emerging markets (by western standards) are China, India, Russia, Brazil, and Mexico. In general, the market risk is higher for emerging markets than that of more developed countries. This risk is usually due to political instabilities, civil unrest, questionable accounting standards, or unstable currencies. However, the higher relative risk generally provides higher potential returns. International stock funds purchase several shares of stocks across developed countries. These funds place the stocks into a collection of funds. Many international funds follow indexes created from the best-performing stocks in broad geographic areas. For example, the MSCI EAFE Index tracks 874 stocks from many countries. Developed countries have more robust and mature economies. Therefore, there is less risk when investing in international stocks, compared to emerging market stocks. Investors may find that many international stock funds invest in the same companies that domestic funds invest in. Some of the top holdings for MSCI EAFE are from Nestle, Novartis, Toyota, Unilever, and Sony. Investors who access foreign investments through international funds reduce foreign investing risks through diversity, indexing, and familiarity. Most investors who are deciding between buying emerging market funds or some other international stock funds are looking for higher returns. Due to the higher relative risk, it's easy to believe that emerging market funds have better returns than international stock funds. This is generally true in the short term, but investors can also see low returns. In the long run, stock funds that don't concentrate on emerging markets tend to generate better returns based on economic stabilizing factors such as monetary policies from central banks and legislation enacted by the government to help consumers and businesses. International stocks can have emerging market stocks mixed within them. The opposite is also true. It helps to study each fund's holdings to understand what you're buying. It's important to remember that the returns of international stock funds and emerging market funds also depend on how they are managed. Fund managers of both types generally try to match an index. One type might perform better than the other over different periods, but the risks will generally remain the same. For instance, the Vanguard FTSE Emerging Markets Index Fund ETF Shares (VWO) price is higher than the Vanguard Total International Stock Index Fund Admiral Shares (VTIAX). Holdings at the top of both types of funds include Tencent, Alibaba, and Taiwan Semiconductor Manufacturing. The international fund has fewer holdings in any of the companies than the emerging market, making it more diversified. Diversification, along with lower prices and steady growth, makes the global fund less risky and higher-returning in the long run. Still, your returns are slightly better with the emerging market fund in the short run. You might get better returns in fewer years with the emerging market funds, but you spend more and take on more risk. Neither investment is "better" than the other. Which is better for your portfolio depends on your risk tolerance, investment strategy, and how much capital you have to dedicate to investing. Whether it is emerging markets or foreign stock, any international or emerging stock fund can be an intelligent part of a diversified portfolio of funds. Relatively more conservative investors may wish to limit their international exposure to 20% of total stock holdings (with 75% and 25% to developed and emerging markets, respectively). However, investors with a higher tolerance for risk may look to expand their international exposure toward the global footprint of 45% international and 55% U.S. Keep in mind that many foreign stocks invest in emerging market countries. Therefore, one good foreign stock fund may already have sufficient exposure to emerging markets. Your strategy and comfort level dictate how you organize your global investments. It is possible to invest in one, both, or neither, depending on your preferences and portfolio. Thanks for your feedback! November 14, 2022 Many investors recently are looking to the markets outside of the US to chase higher returns. Typically, international markets are more volatile than in the US generally because of the sheer size of the US markets. Just a few companies that investors are familiar with but may not know are international are companies such as Nestle, Volkswagen or Sony. Like investing is any company's stock, they have the standard risk, however, there's also an added layers of risk; currency exchange and import/export laws affect these companies but would not affect domestic companies. This added level of risk may come with higher potential for returns. International companies are any company outside of the US; however, the implication of International Funds is that they are invested in developed countries such as Japan, Germany, and England. Typically, these countries have set trade relations with the US and have been established in the world market for a number of years and therefore may be less sensitive to changes in policy. These companies are often considered lower risk than undeveloped markets. Emerging markets are made up of developing countries that do not have the same footing; Some examples are Brazil, India and China. These countries have less stable economies and are more susceptible to changes in the world market. Russia, for example, used to be on this list of developing countries however the war in Ukraine it may no longer be considered a prudent investment at this time. The funds that invest in these companies may have huge potential for growth but also pose huge potential for loss. They are considered one of the riskiest places to invest. Almost all investment vehicles may have a place in a portfolio, including the international markets; however you should review and reassess your portfolios often to make sure they are in line with your goals and objectives.   If you find yourself curious about the balance you have, let's start a conversation, today. Financial Advisor E-Mail: jslish@brightonsecurities.com Direct: 585.340.2209
~:text=Short%20term%20returns%20are%20often,to%2020%25%20of%20their%20portfolios. (Graph 9/24/2022) June 22, 2020 Read Time 4 MIN Which offers more compelling opportunities for investors now: emerging markets or developed markets? As investors consider reallocating their portfolios heading into the second half of 2020, we share our views on this subject to help them navigate across asset classes and make informed investment decisions for the remainder of the year and beyond. Firstly, we expect growth to be the main driver of emerging markets equity returns in the next five years. We believe quality growth companies with strong fundamentals and solid growth estimates will be at the front and center of a new decade of economic transformation. We are optimistic that continued fiscal and monetary support in emerging markets countries should help counter the economic impact of the unfortunate pandemic. Secondly, developed markets have been overcrowded and overvalued, whereas emerging markets have evolved and become much more exciting to follow and invest in today—for example, healthcare in China and digitization in India. Emerging markets companies are currently trading at a discount and are rather attractive from an investor's total portfolio diversification perspective. Emerging Markets Growth Is Leading the Future of Global Economies Despite the uncertainty surrounding COVID-19, we believe emerging markets growth prospects are increasingly relevant to the global economy. As illustrated in the graph below, the emerging markets growth trend should pick up and outpace developed markets growth. According to the International Monetary Fund estimates dated April 2020, for the Emerging Markets and Developing Economies group, growth (as measured by real GDP) is expected to decrease to -1.0% in 2020 and increase to +6.6% in 2021. Advanced Economies growth is projected to plummet to -6.1% levels in 2020 and bounce back to +4.5% in 2021. To summarize, Global Economic growth is estimated to be negative -3.0% in 2020, primarily driven by Advanced Economies' underperformance; and increase to +5.8% in 2021, as a result of Emerging Markets & Developing Economies driving that global growth effort forward. The estimated emerging markets growth trajectory, coupled with low inflation targets1 set by countries' independent central banks, make emerging markets a compelling investment opportunity for global investors. World Economic Outlook: Growth Projections Source: IMF Staff Calculations. As of April 2020. Herd Alert: Developed Markets Are Overcrowded and Overvalued Over the last 10 years, global investors have been chasing the same assets: the safest government bonds, investment-grade corporate bonds, technology stocks and dollar-denominated assets.2 This trend in allocations has led developed markets, like the U.S., to become overcrowded and overvalued. A thoughtful allocation to emerging markets may help protect against such massive herding risk. S&P 500 Index has been overvalued and overcrowded, with relative DM Value trending negatively over the last 10 years Source: Bloomberg. As of 5/31/2020. Attractive Emerging Markets Valuations vs. Developed Markets Currently, emerging markets stocks are trading at a discount vs. developed markets, as outlined in the graph below. We are optimistic that our emerging markets portfolio company valuations will increase over time, as emerging markets are catching up with the developed world. Companies on the VanEck Emerging Markets Equity Strategy's Focus List, for example, are reporting solid numbers and are relatively cheap versus historical estimates or current DM valuations for our estimated operating profitability growth. Their balance sheets are in good shape, generating strong cash flows over a three- to five-year time horizon. Emerging Markets Are Trading at a Discount Source: Bloomberg. As of 5/31/2020. In terms of the price-to-book value, stocks in the MSCI Emerging Markets Equity Index have been trading at a major discount in comparison to those of developed markets, as highlighted in the graph below. Emerging Markets Are Trading at Compelling Valuations vs. Developed Markets Source: Bloomberg. As of 5/31/2020. Emerging Markets Equity: Growth vs. Value Investing Within emerging markets, we believe that growth will continue to outpace value. This is partly driven by most value companies being represented by companies with highly cyclical (and economically dependent) earnings streams, combined with larger state ownership. We call this "value-for-a-reason." In addition, as many value strategies are predicated on some form of mean regression in their valuation methodologies, the accelerating disruption that we see across industries can make value investing quite challenging. Avoid Herding: Take the Emerging Markets Equity Route With the emphasis on growth as the driver of future emerging markets and global economies, coupled with attractive valuations and a compelling case for investors' total portfolio diversification, the VanEck Emerging Markets Equity Strategy is well positioned to identify and invest in exceptional, structural growth companies that are front and center, and the potential future, of emerging markets and global economies! 1 Based on the Economist article "Away from the Crowd" published on October 26, 2019, most of the 25 emerging market economies listed on the indicators page of the publication have inflation below 4%. 2 As cited in the Economist article "Away from the Crowd," published on October 26, 2019. The information presented does not involve the rendering of personalized investment, financial, legal, or tax advice. Certain statements contained herein may constitute projections, forecasts and other forward looking statements, which do not reflect actual results, are valid as of the date of this communication and subject to change without notice. Information provided by third party sources are believed to be reliable and have not been independently verified for accuracy or completeness and cannot be guaranteed. The information herein represents the opinion of the author(s), but not necessarily those of VanEck. Emerging Market securities are subject to greater risks than U.S. domestic investments. These additional risks may include exchange rate fluctuations and exchange controls; less publicly available information; more volatile or less liquid securities markets; and the possibility of arbitrary action by foreign governments, or political, economic or social instability. The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets countries. The MSCI Emerging Markets Investable Market Index (IMI) is a free float adjusted market capitalization index that is designed to capture large-, mid- and small-cap representation across emerging markets countries. The MSCI All Country World Index (ACWI) is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets (DM) and emerging markets. The Standard & Poor's 500, often abbreviated as the S&P 500, is an American stock market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. The S&P 500 index components and their weightings are determined by S&P Dow Jones Indices. The S&P 500 Pure Growth Index includes only those components of the parent index that exhibit strong growth characteristics, and weights them by growth score. The S&P 500 Pure Value Index is a style-concentrated index designed to track the performance of stocks that exhibit the strongest value characteristics by using a style-attractiveness-weighting scheme. The Russell 2000 Index is an index which measures the performance of the smallest 2,000 companies within the Russell 3000 Index. The Russell 2000 Pure Growth Index includes only those components of the parent index that exhibit strong growth characteristics, and weights them by growth score. The Russell 2000 Pure Value Index is a style-concentrated index designed to track the performance of stocks that exhibit the strongest value characteristics by using a style-attractiveness-weighting scheme. All investing is subject to risk, including the possible loss of the money you invest. As with any investment strategy, there is no guarantee that investment objectives will be met and investors may lose money. Diversification does not ensure a profit or protect against a loss in a declining market. Past performance is no guarantee of future results. Emerging Markets Fund - Class A Targets companies with structural growth at a reasonable price across sectors, and market capitalization VanEck Emerging Markets Equity SMA Access local companies across sectors positioned to be leaders in India's digital future VanEck India Growth Leaders ETF Access fundamentally sound Indian companies with attractive growth potential at a reasonable price Portfolio of the largest 100 names on the ChiNext Market (A-Shares) Companies must be incorporated in, or derive at least 50% of total revenues from Vietnam Broad sector exposure to Israel's vibrant economy, including information technology, health care, and financials VanEck Indonesia Index ETF Companies incorporated in or that derive at least 50% of total revenues from Indonesia Companies incorporated in or that derive at least 50% of total revenues from Africa VanEck Brazil Small-Cap ETF Small-Cap companies must be incorporated in, or derive at least 50% of total revenues from Brazil DISCLOSURES 1 Based on the Economist article "Away from the Crowd" published on October 26, 2019, most of the 25 emerging market economies listed on the indicators page of the publication have inflation below 4%. 2 As cited in the Economist article "Away from the Crowd," published on October 26, 2019. The information presented does not involve the rendering of personalized investment, financial, legal, or tax advice. Certain statements contained herein may constitute projections, forecasts and other forward looking statements, which do not reflect actual results, are valid as of the date of this communication and subject to change without notice. Information provided by third party sources are believed to be reliable and have not been independently verified for accuracy or completeness and cannot be guaranteed. The information herein represents the opinion of the author(s), but not necessarily those of VanEck. Emerging Market securities are subject to greater risks than U.S. domestic investments. These additional risks may include exchange rate fluctuations and exchange controls; less publicly available information; more volatile or less liquid securities markets; and the possibility of arbitrary action by foreign governments, or political, economic or social instability. 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In the long run, stock funds that don't concentrate on emerging markets tend to generate better returns based on economic stabilizing factors such as monetary policies from central banks and legislation enacted by the government to help consumers and businesses. International stocks can have emerging market stocks mixed within them. The opposite is also true. It helps to study each fund's holdings to understand what you're buying. It's important to remember that the returns of international stock funds and emerging market funds also depend on how they are managed. Fund managers of both types generally try to match an index. One type might perform better than the other over different periods, but the risks will generally remain the same. For instance, the Vanguard FTSE Emerging Markets Index Fund ETF Shares (VWO) price is higher than the Vanguard Total International Stock Index Fund Admiral Shares (VTIAX). 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Relatively more conservative investors may wish to limit their international exposure to 20% of total stock holdings (with 75% and 25% to developed and emerging markets, respectively). However, investors with a higher tolerance for risk may look to expand their international exposure toward the global footprint of 45% international and 55% U.S. Keep in mind that many foreign stocks invest in emerging market countries. Therefore, one good foreign stock fund may already have sufficient exposure to emerging markets. Your strategy and comfort level dictate how you organize your global investments. It is possible to invest in one, both, or neither, depending on your preferences and portfolio. Thanks for your feedback! Give your money a passport to the overseas markets. Understanding investment types You may not be as familiar with the names of companies outside the United States, which might make you feel like the stocks and bonds they issue are risky. But if you invest in an international mutual fund or ETF (exchange-traded fund), you're increasing your portfolio's diversification by getting access to hundreds—sometimes thousands—of foreign securities. Markets outside the United States don't always rise and fall at the same time as the domestic market, so owning pieces of both international and domestic securities can level out some of the volatility in your portfolio. This can spread out your portfolio's risk more than if you owned just domestic securities. In general, Vanguard recommends that at least 20% of your overall portfolio should be invested in international stocks and bonds. However, to get the full diversification benefits, consider investing about 40% of your stock allocation in international stocks and about 30% of your bond allocation in international bonds. For most people, investing internationally through mutual funds or ETFs is the easiest option. Not only do you get the benefits of diversification, but investing through funds is also generally cheaper and easier since you don't have to worry about the costs and timing considerations involved in trading on international exchanges or through American Depositary Receipts. Investments in international markets are exposed to an additional source of volatility: currency fluctuations. This is especially true for international bonds. To dampen that volatility, consider international investments hedged in U.S. dollars. International markets are generally divided into 2 categories: Developed markets are located in countries that have established industries, widespread infrastructure, secure economies, and a relatively high standard of living. Examples of developed markets include the United Kingdom, Japan, Australia, Canada, and France. Emerging markets are located in countries that have developing capital markets and less-stable economies. However, they're considered to be in the process of transitioning into developed markets, and they may be experiencing rapid growth. Currently, emerging markets make up about 15% to 20% of international markets in total. Examples of emerging markets include India, China, Egypt, South Africa, Mexico, and Russia. Not surprisingly, developed markets are similar to the United States when it comes to volatility levels and the range of potential returns. Emerging markets are more volatile than developed markets and have a wider range of potential outcomes. For that reason, we recommend that you don't overweight your allocation to emerging markets. Many international funds invest across multiple markets within a specific area of the globe, like: Asia-Pacific (Australia, Japan, Hong Kong, Singapore). Europe (United Kingdom, France, Spain, Germany). Latin America (Brazil, Mexico, Argentina, Peru). There are a few ways you can invest in foreign markets: International funds invest only in foreign markets, excluding the United States. Global or world funds provide exposure to both foreign and U.S. markets. Regional funds invest primarily in a specific part of the world, like Europe or the Pacific region. Developed markets funds focus on foreign countries with proven economies, like Japan, France, or the United Kingdom. Emerging markets funds combine investments in countries that are considered to have "developing" economies, like India, Brazil, or China. Get a list of: Vanguard international stock funds Vanguard international bond funds Vanguard international stock ETFs Vanguard international bond ETFs You can use just a few funds to invest overseas. Each of these funds gives you access to a wide variety of international securities in a single, diversified fund or ETF. Vanguard founder Jack Bogle famously argued that international stocks didn't merit inclusion in investors' portfolios. He argued that U.S. companies, especially U.S. large caps, derive plenty of their revenue from selling goods and services overseas. So, if non-U.S. economies thrive, investors in U.S. companies should, too.The past few decades have borne out Bogle's aversion to non-U.S. equities, as U.S. stocks have handily outperformed non-U.S. stocks. Even investors who buy into the argument that non-U.S. stocks should confer diversification and therefore improve their portfolios' risk-adjusted performance may be having difficulty keeping the faith.Portfolio Basics: How to Build an Investment PortfolioIn our recently published 2023 Diversification Landscape report, we examined the case for international diversification, assessing short- and long-term trends in correlations, returns, and risk. While the correlation between non-U.S. and U.S. stocks has increased over the past several decades, non-U.S. stocks held up slightly better than those in the U.S. in 2022. Moreover, non-U.S. stocks have made a strong case for themselves in certain environments, such as when the dollar has declined relative to other major foreign currencies. As the U.S. market has grown increasingly top-heavy with large technology stocks, non-U.S. indexes' higher exposure to value sectors should help diversify that bias.Recent Performance TrendsEven though diversifying into non-U.S. stocks makes intuitive sense and modestly reduced the standard deviation of a U.S.-only portfolio over the past three-, five-, and 10-year periods, doing so has detracted from returns for U.S. equity investors, at least until very recently. In eight of the 10 calendar years from 2013 through 2022, the Morningstar Global Markets ex-US Index lagged the Morningstar US Market Index. That pattern of underperformance showed signs of reversing in 2022, as non-U.S. stocks held up better than U.S. stocks amid a bear market induced by the Federal Reserve's aggressive campaign of interest-rate hikes. But that was a modest victory in that most non-U.S. equity indexes endured sharp losses, albeit smaller than what U.S. stocks posted last year. The Morningstar Global Markets ex-US Index lost about 15% last year, compared with a 20% loss for its U.S. counterpart. Emerging-markets stocks lost more than non-U.S. stocks from developed markets last year: The Morningstar Emerging Markets Index shed 18% in 2022 versus a 15% decline for the Morningstar Developed Markets ex-US Index. Although stocks in Latin America and the Middle East performed relatively well thanks to their heavy tilts toward the rallying energy sector, the broad universe of emerging-markets equities sagged in last year's risk-off environment.From a diversification perspective, most international-stock benchmarks, especially those in developed markets, have been closely tied to the U.S. market over the past three years, as shown in the exhibit below. Not surprisingly, developed-markets European and U.K. equities have had the tightest correlation with U.S. equities. Meanwhile, emerging-markets stocks have tended to have lower correlations with U.S. stocks. Source: Morningstar Direct. Data as of Dec. 31, 2022. The small subset of European stocks from markets classified as emerging had the lowest correlation with the U.S. market over the past three years, with correlations declining significantly in 2022. (At the end of 2021, the three-year correlation of the Morningstar Emerging Markets Europe Index with the U.S. market was 0.82; by the end of 2022, it was just 0.41.) That steep drop in correlations owed largely to eastern European equities' sharp losses following Russia's invasion of Ukraine in early 2022. The Morningstar Emerging Markets Europe Index lost nearly two thirds of its value last year, a catastrophic loss by any measure and an indication that investors have grave uncertainties about Eastern European markets going forward. Such stocks are just 1.3% of the broader Morningstar Emerging Markets Index, however, and are a negligible slice of the Morningstar Global Markets ex-US Index.Longer-Term TrendsWhile non-U.S. stocks, especially those from developed markets, have exhibited a high correlation with the U.S. market in recent years, that hasn't always been the case. As shown in the next exhibit, correlations between the U.S. and international markets have been lower in some previous periods, such as from 2004 through 2008, when the U.S. dollar was generally on the decline. If the greenback goes into another longer-term slump or if the U.S. sinks into recession but other major non-U.S. markets manage to avoid one, it is conceivable that correlations between U.S. and international markets could again drift lower. Source: Morningstar Direct. Data as of Dec. 31, 2022. Longer-term correlations also demonstrate that emerging markets generally have a lower correlation with U.S. stocks than developed markets do. That's because the types of industries that are especially prominent in emerging markets, particularly energy and basic materials, have declined as a percentage of the U.S. market. Portfolio ImplicationsWhile investors who have diversified internationally haven't much benefited over the past decade, they have picked up a modest reduction in volatility relative to a U.S.-only portfolio. The 10-year standard deviation of the Morningstar US Market Index is 15.2, whereas the standard deviation of the Morningstar Global Markets Index, which includes both U.S. and non-U.S. names, is 14.4.Moreover, the U.S. market has become increasingly growth-tilted: 24% of the Morningstar US Market Index lands in the technology sector, for example, whereas just 11% of the Morningstar Global Markets ex-US Index does. The outperformance of technology stocks has redounded to the benefit of U.S.-only investors, as technology names soared for most of the past decade. But in a period in which value-type sectors lead the way, non-U.S. stocks could outperform and help diversify U.S. exposure. Indeed, non-U.S. markets' slightly higher weighting in energy and lower weighting in technology stocks contributed to smaller losses in 2022 than the U.S. market experienced.Because emerging markets have generally had a lower correlation with the U.S. equity market than developed, investors seeking diversification may want to make sure their foreign-stock allocation includes at least some exposure to less-developed markets. And while some specific regions have been better portfolio diversifiers than others, most investors will probably want to shy away from investment vehicles that focus solely on a particular geographic region.The author or authors do not own shares in any securities mentioned in this article. Find out about Morningstar's editorial policies. In casual conversation, the terms "global" and "international" tend to be used interchangeably. Hence the confusion for some investors when they learn that global and international mutual funds (and exchange-traded-funds (ETFs)) each focus their international investing differently. These funds have different investment goals and provide investors with different kinds of investing opportunities. It is up to an investor to understand the types of securities these funds contain. In investing, the terms "global" and "international" refer to different investment funds.A global fund invests in companies and securities from all over the world, including the U.S.An international fund invests in companies and securities from all over the world, except the U.S.Countries regulate their investment funds and their securities markets differently, which means the potential for less or more protections for investors.Investors should know how much exposure to domestic securities they already have in their portfolio before choosing a global or international fund. Global funds invest in securities from all parts of the world, including the country in which you reside. Think of a globe, which displays every single country. That means that you can get exposure to developed and emerging markets as well as growth opportunities in your home country. The level of exposure to each area depends on the goals of a particular fund. Global funds are chosen primarily by investors who wish to diversify their portfolios to protect against country-specific risk, without excluding investments available in their own country. Such investors may have a lower-than-desired concentration of domestic investments or may not want to take on the high level of sovereign risk involved in making individual foreign investments. A mix of domestic and foreign investments works in your favor if the global economy is doing well. News in one country might drive its market down, but other countries may be doing well and see their markets rise. Review the fund information carefully before investing so you clearly understand which countries' securities a fund invests in. Be aware that not all countries regulate their investment funds or their securities markets in the same way. There may be significant differences in the protections that investors receive. In fact, some countries have been known to take over entire industries and have the government run them. This potentially can affect the safety and value of your foreign investments. Investors should consider international investing in general because of the growth and diversification opportunities it presents. Owning an international or global mutual fund or ETF also can reduce the volatility risk associated with a purely domestic portfolio. International funds invest in securities from all countries except the investor's home country. These funds provide exposure to developed and emerging markets worldwide that can complement the domestic exposure already inherent in an investor's portfolio. If an investor currently holds a portfolio consisting mainly of domestic investments, they may choose to add more return opportunities by purchasing an international fund. This would also allow them to diversify against country-specific risk. Alternatively, a speculator may invest in an international fund because they anticipate a rise in a particular foreign market. An international fund can invest in solid markets of developed countries, or it might invest in emerging markets, which are less mature and carry more risk. Typically, the higher the risk the greater the potential return. Just because a fund is called international, don't assume it invests in every country. Do your due diligence to learn what the focus of a particular international fund is. Many specialize in specific areas and should be categorized as country-specific or region-specific. As an individual investor, you cannot buy mutual funds that were established and registered in another country. Regulations prohibit this in every country that has mutual funds. So, to diversify in foreign securities, you have to buy a mutual fund or ETF in your own country that invests in them. This allows you to rely on the experience and expertise of a professional money manager who works for the fund. However, that's no excuse to invest blindly. Make sure you understand the risks, the type of investment, and the tax implications. Read all information about a particular global or international fund before investing. For investors who seek exposure to foreign securities all over the world, as well as investments in their own countries, it can be. However, if you already have a substantial position in domestic stocks, consider an international equity ETF or mutual fund. It does not invest in securities of the country in which it is established and registered. International investing can be valuable to investors for the exposure to additional sources of growth it offers and for the role it can play in the reduction of risk through diversification. You don't have all your eggs in one basket. If you only had domestic securities in your portfolio and that market crashed, the value of your entire portfolio would drop. By spreading your money across domestic and international investments, your portfolio is protected from drops in the value of certain investments by increases in the value of others. Global funds give investors exposure to securities in their own country as well as countries throughout the world. International funds do not offer exposure to domestic securities. Both types of fund provide opportunities for financial returns from foreign securities as well as the benefits of diversification into many different markets. However, you must be sure to determine the exposure you already have to companies in your own country before deciding on which type of fund to buy. Considers economic development sustainability; only used to determine classification of developed markets Size & liquidity requirements Determines those securities that meet the minimum investability requirements of the MSCI Global Standard Indexes Aims to reflect international institutional investing experiences in a given equity market based on five market accessibility criteria As part of the annual market classification review, MSCI communicates the list and analysis of equity markets under each category (Developed, Emerging, Frontier and Standalone), as well as the markets, if any, under review for potential market reclassification in the upcoming cycle. The MSCI's Standalone Markets are broadly classified into two groups: Newly eligible markets Newly eligible markets may either be new markets, previously not covered by MSCI or markets that were closed to a specific group(s) of investors. Markets previously classified under the Developed, Emerging or Frontier Markets categories A reclassification to a Standalone status may occur in the case of severe deterioration in market accessibility or size and liquidity. Previous Market Reclassifications *]:ms-w-full ms-row-span-1>*]:ms-w-full ms-row-span-1> Interested in learning more from MSCI?Related to market classification *]:ms-w-full ms-row-span-1>*]:ms-w-full ms-row-span-1> *]:ms-w-full ms-row-span-1>*]:ms-w-full ms-row-span-1> 1 The MSCI Standalone Market Indexes are not included in the MSCI Emerging Markets Index or MSCI Frontier Markets Index. However, these indexes use either the Emerging Markets or the Frontier Markets methodological criteria concerning size and liquidity. 2 EMEA – Europe, Middle East, and Africa 3 APAC – Asia Pacific * The West African Economic and Monetary Union (WAEMU) consists of the following countries: Benin, Burkina Faso, Guinea-Bissau, Ivory Coast, Mali, Niger, Senegal, and Togo. When you're looking through global investments, it can be difficult to choose between an international stock mutual fund or an emerging market fund. It helps to understand what each one is and their differences so that you can decide whether to use them in your portfolio. Emerging markets are countries with quickly growing economies, such as Brazil, China, India, and Mexico.International stock funds choose the best-performing stocks from a range of developed economies, though many of these are also available domestically.Short-term returns are often higher from emerging markets. International funds can be more stable in the long term.Investing globally provides diversification. Still, conservative investors may want to limit international investments to 20% of their portfolios. Emerging markets are countries with rapidly growing economies that are generally "less developed" than larger or more established nations, such as the United States and Western European countries. Some of the largest countries that are considered emerging markets (by western standards) are China, India, Russia, Brazil, and Mexico. In general, the market risk is higher for emerging markets than that of more developed countries. This risk is usually due to political instabilities, civil unrest, questionable accounting standards, or unstable currencies. However, the higher relative risk generally provides higher potential returns. International stock funds purchase several shares of stocks across developed countries. These funds place the stocks into a collection of funds. Many international funds follow indexes created from the best-performing stocks in broad geographic areas. For example, the MSCI EAFE Index tracks 874 stocks from many countries. Developed countries have more robust and mature economies. Therefore, there is less risk when investing in international stocks, compared to emerging market stocks. Investors may find that many international stock funds invest in the same companies that domestic funds invest in. Some of the top holdings for MSCI EAFE are from Nestle, Novartis, Toyota, Unilever, and Sony. Investors who access foreign investments through international funds reduce foreign investing risks through diversity, indexing, and familiarity. Most investors who are deciding between buying emerging market funds or some other international stock funds are looking for higher returns. Due to the higher relative risk, it's easy to believe that emerging market funds have better returns than international stock funds. This is generally true in the short term, but investors can also see low returns. In the long run, stock funds that don't concentrate on emerging markets tend to generate better returns based on economic stabilizing factors such as monetary policies from central banks and legislation enacted by the government to help consumers and businesses. International stocks can have emerging market stocks mixed within them. The opposite is also true. It helps to study each fund's holdings to understand what you're buying. It's important to remember that the returns of international stock funds and emerging market funds also depend on how they are managed. Fund managers of both types generally try to match an index. One type might perform better than the other over different periods, but the risks will generally remain the same. For instance, the Vanguard FTSE Emerging Markets Index Fund ETF Shares (VWO) price is higher than the Vanguard Total International Stock Index Fund Admiral Shares (VTIAX). Holdings at the top of both types of funds include Tencent, Alibaba, and Taiwan Semiconductor Manufacturing. The international fund has fewer holdings in any of the companies than the emerging market, making it more diversified. Diversification, along with lower prices and steady growth, makes the global fund less risky and higher-returning in the long run. Still, your returns are slightly better with the emerging market fund in the short run. You might get better returns in fewer years with the emerging market funds, but you spend more and take on more risk. Neither investment is "better" than the other. Which is better for your portfolio depends on your risk tolerance, investment strategy, and how much capital you have to dedicate to investing. Whether it is emerging markets or foreign stock, any international or emerging stock fund can be an intelligent part of a diversified portfolio of funds. Relatively more conservative investors may wish to limit their international exposure to 20% of total stock holdings (with 75% and 25% to developed and emerging markets, respectively). However, investors with a higher tolerance for risk may look to expand their international exposure toward the global footprint of 45% international and 55% U.S. Keep in mind that many foreign stocks invest in emerging market countries. Therefore, one good foreign stock fund may already have sufficient exposure to emerging markets. Your strategy and comfort level dictate how you organize your global investments. It is possible to invest in one, both, or neither, depending on your preferences and portfolio. Thanks for your feedback! Credit: pexels.com, Circular economy - a new way of thinkingDeveloped markets, such as the US and UK, have a high level of economic development and industrialization, with a strong service sector and high standard of living.In contrast, emerging markets, like China and India, are growing rapidly and offer significant opportunities for investors, but also come with unique challenges.One key difference between developed and emerging markets is the level of economic growth, with emerging markets experiencing higher growth rates, often exceeding 5% per annum.Emerging markets also have a larger share of their populations under the age of 30, which can lead to a more dynamic and entrepreneurial workforce.Related reading: Stock Market GrowthThe MSCI Emerging Markets Index is comprised of 26 developing economies, with China, Taiwan, and India being the top three contributors, accounting for 59.85% of the index.Developed markets, on the other hand, are less volatile and have more complete data coverage, making them attractive for investors seeking stable returns.Credit: youtube.com, Pure Financial Tip: Developed Markets vs. Emerging MarketsThe MSCI World Index consists of 23 developed economies, with the United States, Japan, and the United Kingdom being the top three contributors, accounting for 78.21% of the index.Emerging markets are riskier, with higher expected returns due to factors like population growth, export economies, and industrialization.International investments in emerging markets involve heightened risks related to currency fluctuations, accounting principles, social, economic, or political instability, increased volatility, and lower trading volume.Take a look at this: Bookkeeping and Accounting DifferenceThe MSCI Emerging Markets Index is made up of 26 developing economies, with China being the most heavily weighted at 31.38%, followed by Taiwan at 14.78% and India at 13.69%. Developed markets, on the other hand, have 23 countries in the MSCI World Index, with the US leading the pack at 67.74%, followed by Japan at 6.1% and the UK at 4.37%.Both indices are capitalization-weighted, meaning that larger companies have a greater influence on the index's performance. They also don't include dividends, which can affect the overall return on investment.Credit: youtube.com, iShares MSCI Emerging Markets ETF (EEM): Global growth on trackThe MSCI World Index is a benchmark for developed countries, characterized by well-established economies, advanced infrastructure, and strong regulatory frameworks. Developed markets offer greater stability, transparency, and liquidity compared to emerging markets.Here's a comparison of the two indices:As you can see, the MSCI Emerging Markets Index is heavily weighted in China, Taiwan, and India, while the MSCI World Index is dominated by the US, Japan, and the UK. This can affect the overall performance of the indices, with emerging markets often being riskier but potentially offering higher returns.Correlation between emerging and developed markets can be measured using a correlation coefficient. A correlation coefficient of +1 indicates a perfect positive correlation, while a coefficient of -1 indicates they moved in opposite directions.Diversification is the practice of spreading investments across different assets to reduce risk. This is crucial in investing, as Ray Dalio realized that with fifteen to twenty uncorrelated return streams, he could dramatically reduce the risks without reducing the expected returns.Credit: youtube.com, Understanding Market Correlations by ChartGuys.comA correlation coefficient of +1 means the two indices moved in the same direction, while a coefficient of -1 means they moved in opposite directions. This is based on the 1-year rolling correlation coefficient between the MSCI Emerging Markets Index and the MSCI World Index.Investors can benefit from diversification by spreading their investments across different assets. This can help reduce risk and increase expected returns, as seen in Ray Dalio's approach.Developed markets are economically advanced and have active and easily accessible capital markets.The US, Canada, most Western European and Scandinavian countries, Australia, New Zealand, Japan, Hong Kong, and Singapore are classified as developed markets.Emerging markets, on the other hand, tend to experience fast growth but have less mature and harder to access capital markets.China and India are examples of emerging markets, despite their large economies, due to their lower starting point compared to developed markets.You might enjoy: Hedge Fund vs Private Equity vs Venture CapitalCredit: youtube.com, Investing in Developed Markets vs. Emerging MarketsThese emerging markets are home to global leaders in various industries, such as tech companies like Tencent and Alibaba.Demographics are working in favour of emerging markets, with most of the global growth in the middle class expected to come from these regions over the next 12 years, according to the OECD.This growth in the middle class leads to increased consumption and domestic demand, which are key driving forces behind economic development.Investing in emerging markets comes with higher risk due to geopolitical instability and less transparent capital markets, but also offers potential for higher returns in rapidly-expanding countries.Long-term investors who can handle occasional market turbulence may find emerging markets suitable for their investment strategy.In general, emerging markets account for around 15% of adventurous portfolios and 10% of balanced portfolios, while cautious portfolios hold little or none.Developed and emerging markets currencies differ in liquidity, volatility, and trading volumes, with emerging markets currencies being relatively illiquid and highly volatile. Understanding these differences is crucial for making informed investment decisions in the foreign exchange market. When you're looking through global investments, it can be difficult to choose between an international stock mutual fund or an emerging market fund. It helps to understand what each one is and their differences so that you can decide whether to use them in your portfolio. Emerging markets are countries with quickly growing economies, such as Brazil, China, India, and Mexico.International stock funds choose the best-performing stocks from a range of developed economies, though many of these are also available domestically.Short-term returns are often higher from emerging markets. International funds can be more stable in the long term.Investing globally provides diversification. Still, conservative investors may want to limit international investments to 20% of their portfolios. Emerging markets are countries with rapidly growing economies that are generally "less developed" than larger or more established nations, such as the United States and Western European countries. Some of the largest

countries that are considered emerging markets (by western standards) are China, India, Russia, Brazil, and Mexico. In general, the market risk is higher for emerging markets than that of more developed countries. This risk is usually due to political instabilities, civil unrest, questionable accounting standards, or unstable currencies. However, the higher relative risk generally provides higher potential returns. International stock funds purchase several shares of stocks across developed countries. These funds place the stocks into a collection of funds. Many international funds follow indexes created from the best-performing stocks in broad geographic areas. For example, the MSCI EAFE Index tracks 874 stocks from many countries. Developed countries have more robust and mature economies. Therefore, there is less risk when investing in international stocks, compared to emerging market stocks. Investors may find that many international stock funds invest in the same companies that domestic funds invest in. Some of the top holdings for MSCI EAFE are from Nestle, Novartis, Toyota, Unilever, and Sony. Investors who access foreign investments through international funds reduce foreign investing risks through diversity, indexing, and familiarity. Most investors who are deciding between buying emerging market funds or some other international stock funds are looking for higher returns. Due to the higher relative risk, it's easy to believe that emerging market funds have better returns than international stock funds. This is generally true in the short term, but investors can also see low returns. In the long run, stock funds that don't concentrate on emerging markets tend to generate better returns based on economic stabilizing factors such as monetary policies from central banks and legislation enacted by the government to help consumers and businesses. 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Diversification, along with lower prices and steady growth, makes the global fund less risky and higher-returning in the long run. Still, your returns are slightly better with the emerging market fund in the short run. You might get better returns in fewer years with the emerging market funds, but you spend more and take on more risk. Neither investment is "better" than the other. Which is better for your portfolio depends on your risk tolerance, investment strategy, and how much capital you have to dedicate to investing. Whether it is emerging markets or foreign stock, any international or emerging stock fund can be an intelligent part of a diversified portfolio of funds. Relatively more conservative investors may wish to limit their international exposure to 20% of total stock holdings (with 75% and 25% to developed and emerging markets, respectively). However, investors with a higher tolerance for risk may look to expand their international exposure toward the global footprint of 45% international and 55% U.S. Keep in mind that many foreign stocks invest in emerging market countries. Therefore, one good foreign stock fund may already have sufficient exposure to emerging markets. Your strategy and comfort level dictate how you organize your global investments. It is possible to invest in one, both, or neither, depending on your preferences and portfolio. Thanks for your feedback! An important strategy for building a diverse portfolio is to include holdings from a variety of locations, both domestic and international. And when you invest internationally, you have the opportunity to invest in both developed markets and emerging markets. What are developed and emerging markets? There's no standard metric for differentiating between developed markets and emerging markets, but there are a number of identifiable characteristics that are hallmarks of each, says Dan Eye, CFA, head of asset allocation and equity research at Roof Advisory Group, a division of Fort Pitt Capital Group. For instance, developed nations have more advanced economies, better-developed infrastructure, more mature capital markets, and higher standards of living. These are the most economically advanced countries, with highly developed capital markets, regulatory bodies and high household incomes. Most developed markets are located in North America, Western Europe and Australasia. They include countries like the United States, Canada, Germany, the United Kingdom, Australia, New Zealand and Japan. Emerging markets, on the other hand, are in the process of rapid growth and development but they have lower household incomes and capital markets that are less mature than developed countries. They are characterized by fast economic growth but their infrastructure and household incomes haven't caught up yet. "Emerging countries tend to exhibit higher economic growth rates driven by younger populations, higher consumption levels, modernization of infrastructure, and integration with the global economy," Eye says. "Emerging nations also tend to experience higher levels of political and economic instability." Currently, emerging markets include the so-called "BRIC" countries (Brazil, Russia, India and China), as well as Portugal, Ireland, Italy, Greece and Spain. What are the best ways to invest in both emerging and developed markets? Investing internationally is a smart financial move, but it can be scary to invest your money in companies and regions that are completely unfamiliar to you. One of the easiest ways to incorporate stocks from both developed markets and emerging markets is to purchase shares in managed funds. (For instance, Acorns portfolios include emerging market and developed market index funds like the Vanguard Emerging Market Stock Index Fund and the Vanguard FTSE Developed Markets Index Fund.) Such funds are especially attractive to those interested in investing in emerging countries but nervous about immature capital markets. "U.S.-based investors tend to avoid the headaches and hurdles associated with direct investments in emerging market stocks and opt for exposure to the asset class via passive exchange-traded funds or actively managed mutual funds," Eye says. "Passive ETFs offer investors the benefits of broad diversification and very low investment expenses." Are there risks involved with investing in emerging markets? There are always risks involved in any investment. But the risks of investing in emerging markets are unique, such as risks associated with political and economic instability. There's also the risk associated with foreign currency fluctuations, as declining currency values can cancel out your gains or amplify your losses. In addition, "accounting standards and financial reporting requirements are much less stringent in developing markets," Eye says. "This has translated into misleading and sometimes fraudulent financial reporting." Despite these risks, there are returns to be gained from including emerging market stocks in your investment portfolio. For instance, they offer the opportunity to capitalize on economic growth that is occurring more rapidly than in developed economies. Emerging countries usually also have growing populations to fuel future consumption. And for your portfolio, investments in emerging markets can offer the benefits of diversification by including a class of assets that is not directly connected to the U.S. stock market (and may not experience the same ups and downs). It would make sense that investors should be able to expect higher returns with emerging markets, due to increased risks. "However, that has not been the case over the past decade," Eye says. "The U.S. stock market has dramatically outpaced emerging market indices. While the benefits of higher GDP levels, stronger demographics, and a growing middle class [in emerging markets] are real and observable, those attributes don't automatically translate into superior corporate earnings growth or equity market outperformance." What about developed markets? Like all investments, those in developed market equities also carry both risks and benefits. In general, investing in developed markets means you can benefit from more reliable accounting and financial reporting. In most cases, developed markets offer less risk of sudden political or economic instability. And when investing domestically, you can also avoid the risks associated with direct foreign currency. Despite these benefits, U.S. and developed equity markets also carry risks. Currently, equity market valuations in developed countries are well above long-term historical averages, which makes it more difficult for these markets to absorb unforeseen shocks, Eye says. In addition, "the backdrop of slow economic growth and less supportive demographics in developed countries are a challenge for corporate earnings growth going forward," Eye says. "Developed economies have piled on a mountain of debt over the past decade, which may act as an anchor to economic growth and crowd out more productive spending in the future." Every market, whether developed or emerging, offers both advantages and disadvantages for investors. In fact, those differences are the things that make investing in all types of markets worthwhile: When developed markets are down, emerging markets may be booming, and vice versa. By building a diversified portfolio that includes holdings from both emerging markets and developed markets, you'll be more likely to successfully weather the storms of each market. Acorns portfolios contain a mix of exchange-traded funds with exposure to thousands of stocks (domestic and foreign) and bonds. Sign up here. An emerging market economy is the economy of a developing nation that's becoming more engaged with global markets as it grows. Countries classified as emerging market economies are those with some but not all of the characteristics of a developed market. Characteristics of developed markets can include strong economic growth, high per capita income, liquid equity and debt markets, accessibility by foreign investors, and a dependable regulatory system. It typically becomes more integrated with the global economy as an emerging market economy develops. It can have increased liquidity in local debt and equity markets, increased trade volume, and foreign direct investment. It can develop modern financial and regulatory institutions. Some notable emerging market economies include India, Mexico, Russia, Iran, Saudi Arabia, China, and Brazil. An emerging market economy is transitioning from a low-income, less developed, often pre-industrial economy toward a modern, industrial economy with a higher standard of living. An emerging market economy is one that's transitioning into a developed economy.Emerging market economies typically feature a unified currency, stock market, and banking system. They're in the process of industrializing.Emerging market economies can offer greater returns to investors due to their rapid growth.They also offer greater exposure to some inherent risks due to their status.Emerging markets typically adopt reforms that are seen in developed markets over time. Investors seek emerging markets for the prospect of high returns because these markets often experience faster economic growth as measured by gross domestic product (GDP). Higher returns usually come with much greater risk, however. Risks can include political instability, domestic infrastructure problems, currency volatility, and illiquid equity because many large companies may still be state-run or private. Local stock exchanges might not offer liquid markets to outside investors. Emerging markets generally don't have highly developed market and regulatory institutions like those found in developed nations. Market efficiency and strict standards in accounting and securities regulation are generally not on par with advanced economies such as those of the United States, Europe, and Japan. Emerging markets typically have a physical financial infrastructure, including banks, a stock exchange, and a unified currency. A key aspect of emerging market economies is that they adopt reforms and institutions like those of modern developed countries over time. This promotes economic growth. Emerging market economies tend to move away from activities that are focused on agricultural and resource extraction toward industrial and manufacturing activities instead. Their governments usually pursue deliberate industrial and trade strategies to encourage economic growth and industrialization. These strategies include export-led growth and import-substituting industrialization. Export-led growth is more typical of economies that are considered emerging because it promotes more engagement and trade with the global economy. Emerging market countries also often pursue domestic programs such as investing in educational systems, building physical infrastructure, and enacting legal reforms to secure investors' property rights. Frontier markets are usually smaller than emerging markets with lower per capita income, less market liquidity, and less industrialization. They offer attractive investment opportunities but frontier markets are considered riskier for investors than emerging markets. Emerging market economies are classified in various ways. Levels of income, quality of financial systems, and growth rates are all popular criteria but the exact list of emerging market economies can vary depending on who you ask. The International Monetary Fund (IMF) classifies 20 countries as emerging markets. Morgan Stanley Capital International (MSCI) classifies 24 countries as emerging markets. Standard and Poor's (S&P), FTSE Russell, and Dow Jones also vary slightly in their classification of countries as emerging markets. A country can be removed from the list by either upgrading it to developed nation status or downgrading it to a frontier nation at any of these institutions' discretion. Developed nations may likewise be downgraded to an emerging market as was the case with Greece. Frontier markets such as Qatar and Argentina may be upgraded to emerging markets. An emerging market economy is generally considered an economy that's transitioning into a developed market economy. It has rapid GDP growth, growing per capita income, increasing debt and equity markets liquidity, and an established financial system infrastructure. Classifications differ but the so-called BRICS countries represent five emerging markets with major economic growth and opportunities for investment: Brazil, Russia, India, China, and South Africa. The GDPs of these countries have increased steadily from 2000 through 2023. Data for 2024 isn't yet available.That trend is expected to continue through the years ahead. They can make good investments due to their propensity for rapid GDP growth compared to more mature markets but investing in emerging markets can be risky due to potential political instability, lack of dependable information, currency fluctuations, lower liquidity, and investment volatility.Investors should carefully weigh potential risks and rewards before making any investment. Countries that are classified as emerging market economies are those with economies that are transitioning into being developed. They have a unified currency, stock market, and banking system, and they're in the process of industrializing. Emerging market economies can be attractive to investors due to their rapid growth and greater returns but they also involve greater exposure and risk due to political instability or currency fluctuation. When you're looking through global investments, it can be difficult to choose between an international stock mutual fund or an emerging market fund. It helps to understand what each one is and their differences so that you can decide whether to use them in your portfolio. Emerging markets are countries with quickly growing economies, such as Brazil, China, India, and Mexico.International stock funds choose the best-performing stocks from a range of developed economies, though many of these are also available domestically.Short-term returns are often higher from emerging markets. International funds can be more stable in the long term.Investing globally provides diversification. Still, conservative investors may want to limit international investments to 20% of their portfolios. Emerging markets are countries with rapidly growing economies that are generally "less developed" than larger or more established nations, such as the United States and Western European countries. Some of the largest countries that are considered emerging markets (by western standards) are China, India, Russia, Brazil, and Mexico. In general, the market risk is higher for emerging markets than that of more developed countries. This risk is usually due to political instabilities, civil unrest, questionable accounting standards, or unstable currencies. However, the higher relative risk generally provides higher potential returns. International stock funds purchase several shares of stocks across developed countries. These funds place the stocks into a collection of funds. Many international funds follow indexes created from the best-performing stocks in broad geographic areas. For example, the MSCI EAFE Index tracks 874 stocks from many countries. Developed countries have more robust and mature economies. Therefore, there is less risk when investing in international stocks, compared to emerging market stocks. Investors may find that many international stock funds invest in the same companies that domestic funds invest in. Some of the top holdings for MSCI EAFE are from Nestle, Novartis, Toyota, Unilever, and Sony. Investors who access foreign investments through international funds reduce foreign investing risks through diversity, indexing, and familiarity. Most investors who are deciding between buying emerging market funds or some other international stock funds are looking for higher returns. Due to the higher relative risk, it's easy to believe that emerging market funds have better returns than international stock funds. This is generally true in the short term, but investors can also see low returns. In the long run, stock funds that don't concentrate on emerging markets tend to generate better returns based on economic stabilizing factors such as monetary policies from central banks and legislation enacted by the government to help consumers and businesses. International stocks can have emerging market stocks mixed within them. The opposite is also true. It helps to study each fund's holdings to understand what you're buying. It's important to remember that the returns of international stock funds and emerging market funds also depend on how they are managed. Fund managers of both types generally try to match an index. One type might perform better than the other over different periods, but the risks will generally remain the same. For instance, the Vanguard FTSE Emerging Markets Index Fund ETF Shares (VWO) price is higher than the Vanguard Total International Stock Index Fund Admiral Shares (VTIAX). Holdings at the top of both types of funds include Tencent, Alibaba, and Taiwan Semiconductor Manufacturing. The international fund has fewer holdings in any of the companies than the emerging market, making it more diversified. Diversification, along with lower prices and steady growth, makes the global fund less risky and higher-returning in the long run. Still, your returns are slightly better with the emerging market fund in the short run. You might get better returns in fewer years with the emerging market funds, but you spend more and take on more risk. Neither investment is "better" than the other. Which is better for your portfolio depends on your risk tolerance, investment strategy, and how much capital you have to dedicate to investing. Whether it is emerging markets or foreign stock, any international or emerging stock fund can be an intelligent part of a diversified portfolio of funds. Relatively more conservative investors may wish to limit their international exposure to 20% of total stock holdings (with 75% and 25% to developed and emerging markets, respectively). However, investors with a higher tolerance for risk may look to expand their international exposure toward the global footprint of 45% international and 55% U.S. Keep in mind that many foreign stocks invest in emerging market countries. Therefore, one good foreign stock fund may already have sufficient exposure to emerging markets. Your strategy and comfort level dictate how you organize your global investments. It is possible to invest in one, both, or neither, depending on your preferences and portfolio. Thanks for your feedback! Adding international stock exposure is one of the first steps toward a diversified portfolio. Even minimalist investors usually carve out a portion of their portfolios for non-US stocks as a supplement to domestic stocks and bonds.At this point, however, even committed globalists have to acknowledge that adding non-US equities has detracted from the returns of a US-only portfolio, even as it has modestly reduced risk. In the 2024 Diversification Landscape report that I recently completed with Amy Arnott and Karen Zaya, we found that foreign stocks' correlation with the US market has also increased over the past three years.Whether non-US stocks will fail to earn their keep in the future is an open question, however. As the US market has grown increasingly concentrated in the large-growth square of the Morningstar Style Box, especially in technology stocks, investing in non-US equities provides exposure to sectors that are underrepresented in total US market indexes today. Moreover, developing-markets equities have demonstrated a lower correlation with the US market than the developed markets' correlation, albeit with higher levels of volatility. This suggests that investors venturing overseas should make room for emerging markets as part of their non-US allocations. Recent Performance TrendsEven though diversifying into non-US stocks makes intuitive sense and modestly reduced the standard deviation of a US-only portfolio over the past three-, five-, and 10-year periods, doing so has often detracted from returns for US-based investors. In eight of the 10 calendar years from 2014 through 2023, the Morningstar Global Markets ex-US Index lagged the Morningstar US Market Index. Non-US stocks held up better than US stocks in 2022 amid a bear market induced by the Federal Reserve's aggressive campaign of interest-rate hikes. But that was a modest victory, and short-lived. As mega-cap US technology stocks led the market again in 2023, non-US stock indexes failed to keep up. The Morningstar Global Markets ex-US Index gained about 16% in 2023, compared with a 26% return for its US counterpart.The Morningstar Emerging Markets Index gained 12% in 2023 versus an 18% gain for the Morningstar Developed Markets ex-US Index. Emerging markets also fared worse than developed-markets equities in the 2022 bear market. Although stocks in Latin America have been a bright spot recently, China's economic slowdown has weighed heavily on broad emerging-markets indexes.From a diversification perspective, most international-stock benchmarks, especially those in developed markets, have been closely tied to the US market over the past three years, as shown below. Developed-markets equities, especially European stocks, have had the tightest correlation with US equities. Meanwhile, emerging-markets stocks have tended to have lower correlations with US stocks, and those correlations have generally trended down since 2000. Source: Morningstar Direct. Data as of Dec. 31, 2023. The small subset of European stocks from markets classified as emerging have had the lowest correlation with the US market over the past three years, with correlations declining significantly in 2022 and falling further still in 2023. (At the end of 2021, the three-year correlation of the Morningstar Emerging Markets Europe Index with the US market was 0.82; by the end of 2023, it was just 0.16.) That steep drop in correlations owed largely to Eastern European equities' sharp losses following Russia's invasion of Ukraine in early 2022. Such stocks are just 1.3% of the broader Morningstar Emerging Markets Index, however, and they are a negligible slice of the Morningstar Global Markets ex-US Index. Longer-Term TrendsWhile non-US stocks, especially those from developed markets, have exhibited a high correlation with the US market in recent years, that hasn't always been the case. As shown below, correlations between the US and international markets have been lower in some previous periods, such as from 2004 through 2008, when the US dollar was generally on the decline. If the greenback goes into another longer-term slump, or if the US sinks into recession but other major non-US markets manage to avoid one, it is conceivable that correlations between US and international markets could again drift lower. Source: Morningstar Direct. Data as of Dec. 31, 2023. Longer-term correlations also demonstrate that emerging markets generally have a lower correlation with US stocks than developed markets do. That's because the types of industries that are especially prominent in emerging markets, particularly energy and basic materials, have declined as a percentage of the US market. In addition, the Chinese economy, which represents roughly 30% of major emerging-markets indexes, follows a different economic cycle than the US does. Finally, emerging markets are more likely than developed markets to be affected by country- and region-specific geopolitical events—political instability, wars, and currency devaluations—that have little to do with the US. Taken together, those features suggest that emerging-markets equities' low correlation with US stocks won't be as fleeting as some of the other correlation trends.Portfolio ImplicationsWhile investors who have diversified internationally haven't much benefited over the past decade, their portfolios have been slightly less volatile relative to a US-only portfolio. The 10-year standard deviation of the Morningstar US Market Index is 15.5, whereas the standard deviation of the Morningstar Global Markets Index, which includes both US and non-US names, is 15.0. Japan, in particular, has exhibited milder volatility than the US market and other major non-US markets.Moreover, the US market has become increasingly growth-tilted: 29% of the Morningstar US Market Index lands in the technology sector, for example, whereas just 12% of the Morningstar Global Markets ex-US Index does. That has been a boon for US-only investors as technology names soared for most of the past decade. But in a period in which lower-priced stocks lead the way, non-US stocks could outperform and help diversify US exposure. Non-US indexes feature a heavier emphasis on traditional value sectors, including energy, basic materials, and financials. Because emerging markets have generally had a lower correlation with the US equity market than the developed markets' correlation, investors seeking diversification may want to make sure their foreign-stock allocation includes at least some exposure to less-developed markets. And while some specific regions have been better portfolio diversifiers than others, most investors will probably want to shy away from investment vehicles that focus solely on a particular geographic region.The author or authors do not own shares in any securities mentioned in this article. Find out about Morningstar's editorial policies.