Expat Investment Advice: Why a Home-Country Investment Portfolio Won't Cut It for Expats—and What Will

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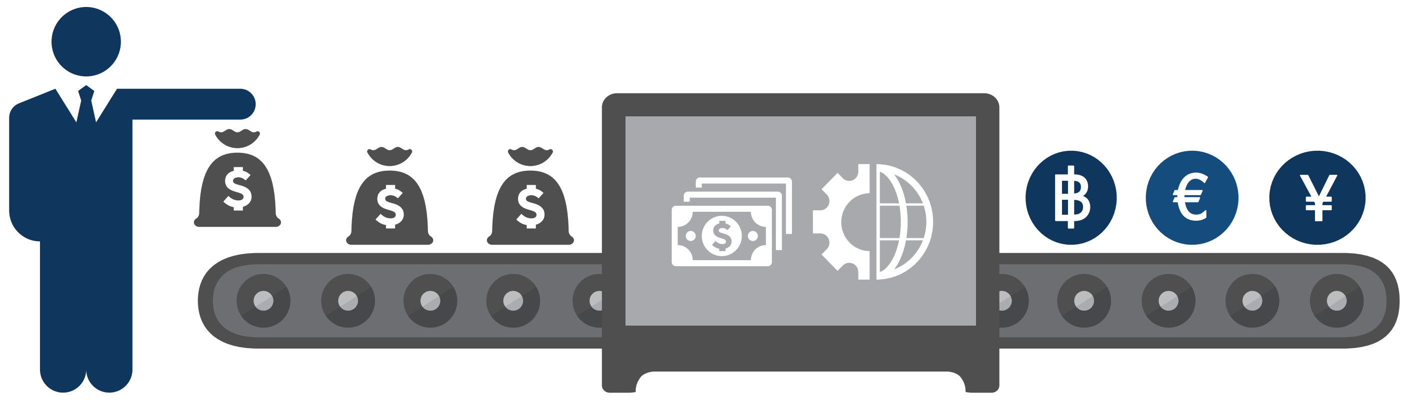
If you live an expatriate lifestyle, your financial interests and obligations may be international or global. You may be paid in a foreign currency, have a spouse who is a different nationality, and have kids who are at home in places as far flung as Bangkok, Shanghai, London, and Chicago. Your home, assets, and liabilities may be scattered, you pay tax in more than one jurisdiction, and you may want the option to retire in a number of places. To match your situation, you want an investment portfolio that's equally global and flexible.

Yet if you seek the advice of a broker or advisor in your home country, you'll probably end up with an investment portfolio best suited for someone living in your home country. For example, the typical investment portfolio may hold 70–90% of equity in your home country's stock market, and hold all of its fixed income investments in your home country's currency. Clearly, this approach doesn't make sense for someone living overseas. Instead, investors with an expatriate lifestyle should consider the following when designing their long-term investment allocation.



Diversify your equity investments globally: As an expat, you may have left a developed, more slowly growing economy to live and work in a faster-growing or emerging one. If your long-term plans include maintaining the flexibility to retire in a number of places, you'll want to maintain global purchasing power. Therefore, you won't want to concentrate too much in your home market where you'd run the risk of receiving either subpar long-run returns or returns that are out of sync with your situation.

In fact, you should avoid overconcentration in any single country equity market—including your country of residence or another seemingly fast-growing economy. This is because while economic growth is an important factor influencing equity market returns over the long run, the two do not move uniformly together in each market, in every year. If you concentrate in any single market, you end up not only increasing the chance that you'll do better than average, but also increasing the chance that you'll do worse. And given the dynamics of investor psychology, which tends to chase popular trends and guru predictions, continually trying to cherry-pick single markets may simply result in compounding poor decisions over time.

So to create a portfolio that will maintain global purchasing power and flexibility, you'll want your equity investments to be globally diversified. This means that you should aim to hold a diversified portion of developed market equity (where multinationals will themselves be investing in emerging economies), and a mixed portion of emerging market equity. For an example or starting point, look to the allocations provided in global equity indices such as the MSCI World Index or FTSE All-World Index.

Should you be concerned with the risk of local currency fluctuations or inflation? While these are real risks, they are less of a concern with long-term equity investments. Market mechanisms for equity prices will tend to correct changes in relative price and currency levels over the long term. And if you can't wait for the long term and need the money in the short run (within the next several years), then this portion of your portfolio doesn't belong in equity investments in the first place.

Match fixed income investments with the economy you'll spend in: Unlike equity investments, your fixed income investments should be more closely in sync with the economy where you intend to spend your savings. Here inflation differentials and currency movements can matter. Retirees with living expenses denominated in a local currency, or others who have near-tern spending plans in a specific currency (say a house purchase in a year's time), will want to work out a fixed income allocation that includes some fixed income denominated in that currency as well as in any other currency or economy where they plan to spend their savings. You can try to hedge the currency risk of your fixed income investments, but keep in mind that there's a cost to hedging. Hedging instruments are generally for a finite period and amount, and therefore hedging is usually more appropriate for specific short-term goals rather than for a long-term portfolio.

Where should you hold your portfolio? In choosing a country or broker to hold your long-term portfolio, you'll want to consider some of the following: the safety of the jurisdiction (including consumer protection regulations), the availability of low-cost investment vehicles such as exchange-traded funds (ETFs) or index funds, online access, cost transparency, quality of customer service, and language capability. In addition, you'll want to consider how your investments will be taxed in that jurisdiction, your country of residence, and your home country.

For U.S. citizens and long-term residents, the best place to hold most of your equity portfolio investments is probably with a U.S. discount broker. Despite the internet ads pushing offshore investing, the cost and choices of investments for U.S. consumers are second to none, and there are significant negative tax consequences for U.S. citizens when they go offshore. For other nationalities, what makes the most sense will depend on your specific situation.

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