Overweight Unhedged World ex US Treasuries/Underweight US Treasuries

Recommended since May 31, 2025

Investment thesis: Unhedged global ex US Treasuries outperform US Treasuries when the dollar falls. In our view, the USD is expensive and likely to weaken over the next one to three years as the growth and interest rate edge of the US should moderate. Foreign demand for US assets may also wane given elevated US exposures, expensive US equity valuations, and recent US policies. This trade reflects our negative view on the USD and not the underlying bonds. This position is specifically intended as a way for US-based investors to underweight the USD.

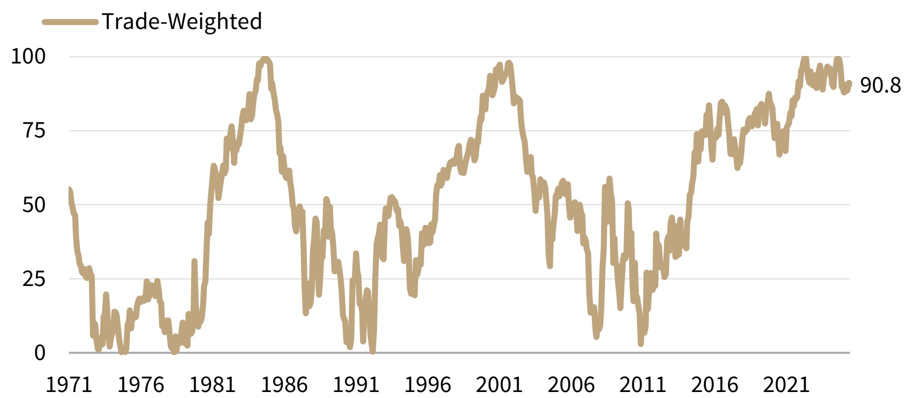
Key support 1: The USD is expensive. Early this year, its trade-weighted real effective exchange hit its fourth highest level since 1971, and it remains elevated. When starting valuations are this high, it typically leads to a multi-year decline in the USD. This tends to support unhedged global ex US Treasuries relative to US Treasuries. Historically, when USD valuations are this elevated, subsequent rolling three-year annualized returns have ranged from -2% to 19%, averaging 7.7%.

Key support 2: We expect USD weakness as secular US advantages fade. The USD's recent strength reflected robust US growth and higher interest rates, but these advantages are set to fade. A more balanced US economy, increased fiscal support in Europe and China, and higher US tariffs—likely to impact the US the most—has narrowed the growth differential between the US and the rest of the world. This has prompted the Fed to resume rate cuts, while other major central banks near the end of their easing cycles. Investors may also reduce exposure to the US at the margin, which has risen with US equity and dollar outperformance, amid growing policy uncertainty.

Key risks: This trade faces two-way risks. US tariffs may have a muted impact, allowing the US to maintain its growth advantage and attract capital. Conversely, a more significant global slowdown could trigger broader weakness and a flight to safety. Both scenarios may support the USD, illustrating the "dollar smile." Implementing this trade incurs a cost, as US Treasuries currently yield 110 bps more than global ex US Treasuries.

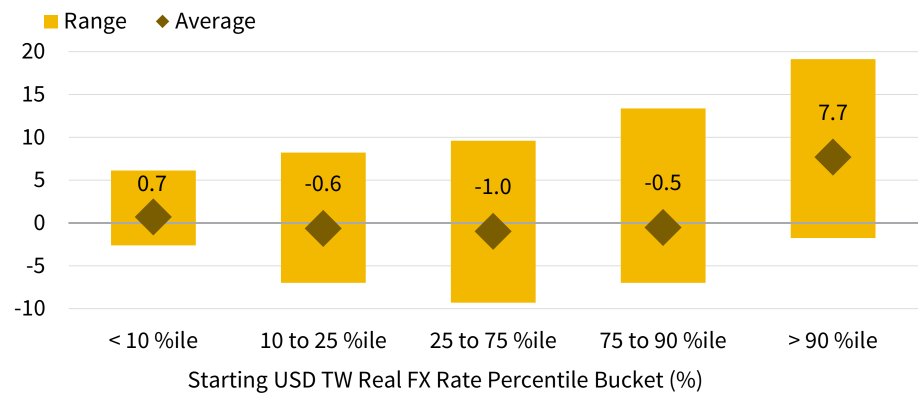
USD basket trade-weighted real exchange rate

June 30, 1971 – November 30, 2025 • Percentile (%)



Relative unhedged world ex US vs US treasury bond returns

January 31, 1985 – November 30, 2025 • 3-yr annualized return (%)



Sources: Bloomberg Index Services Limited, FTSE Russell, MSCI Inc., National Sources, OECD, Refinitiv, Thomson Reuters Datastream, and US Federal Reserve. MSCI data provided "as is" without any express or implied warranties.
Note: Inflation data are as of October 31, 2025.