Overweight Unhedged World ex US Treasuries/Underweight US Treasuries

Recommended since May 31, 2025

Investment thesis: Unhedged world ex US Treasuries outperform US Treasuries when the dollar declines. We view the USD as expensive and expect it to weaken as the US advantages fade and foreign demand for US assets moderates amid elevated US exposures, rich equity valuations, and recent policy shifts. This trade is intended for US-based investors and reflects our negative outlook on the dollar, not on the underlying bonds.

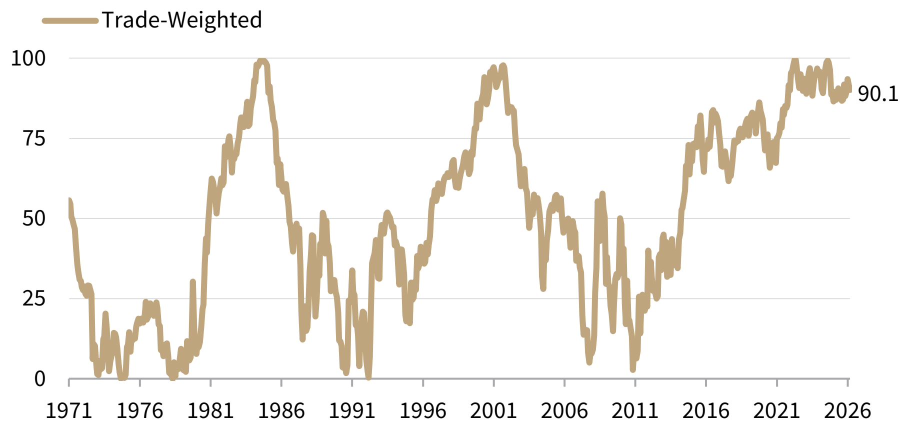
Key support 1: The USD's trade-weighted real effective exchange rate (REER) is elevated. Historically, such valuation levels have preceded multi-year dollar declines, favoring unhedged world ex US Treasuries over US Treasuries. When the USD's REER rises above the 90th percentile, subsequent three-year annualized returns have ranged from -2% to 19%, averaging 6.2%.

Key support 2: Near-term forces could still support the dollar, including the Iran War and US AI leadership, which have lifted growth and rate expectations and attracted capital inflows. But these supports are unlikely to be durable, and we continue to expect a medium-term weakening trend. The dollar remains expensive by historical standards. Relative growth and yield differentials should narrow over time, while foreign investors are increasing currency hedges and may slow record-high purchases of US assets amid elevated valuations, policy uncertainty, and rising investment needs at home. Recent dollar weakness may also provide a release valve for Treasury efforts to manage the yield curve.

Key risks: Advances in AI and productivity could sustain US growth and continue to attract foreign capital, keeping the dollar stronger for longer, and the fragility of peace in the Middle East also remains a near-term risk. Lastly, implementation comes at a cost; US Treasuries yield approximately 140 bps more than global ex US Treasuries.

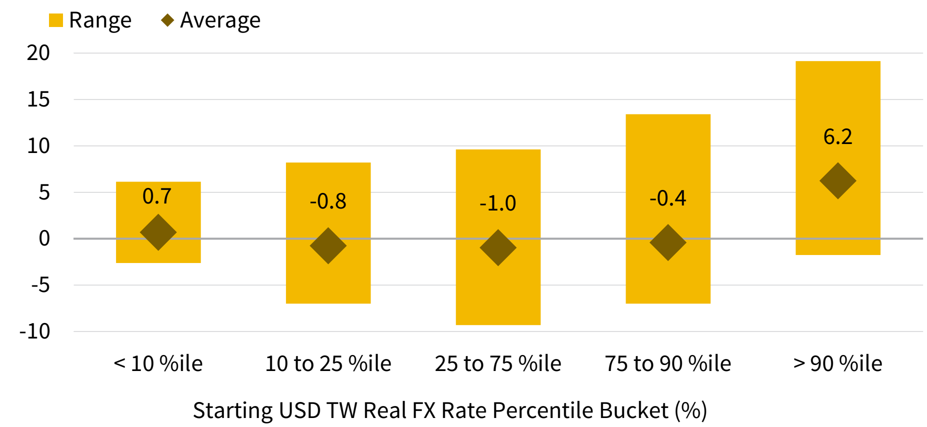
USD basket trade-weighted real effective exchange rate

June 30, 1971 – August 31, 2026 • Percentile (%)



Relative unhedged world ex US vs US treasury bond returns

January 31, 1985 – August 31, 2026 • 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 July 31, 2026.