

A compelling opportunity: How to reframe international equity allocations

From the Field

Key Insights

- Our data reveal that many advisor models are structurally underweight to international value stocks, and we suggest designing the international developed sleeve in a similar fashion to U.S. equity allocations, balancing the investment approach across styles.
- Among the key factors supporting an investment allocation that takes into account international value stocks are fiscal stimulus, monetary policy, valuations, and earnings growth.
- While international equities have lagged U.S. stocks over the intermediate and longer term, there may be an opportunity going forward for international value stocks to demonstrate better performance and diversify investor portfolios.



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Diversification is a foundational pillar of strategic asset allocation and portfolio design. Diversifying equity exposures across size, style, and geography seeks to enhance performance consistency, which, in turn, could help to lower portfolio volatility.

In February 2025, we published the latest edition of Portfolio Construction Pulse, “U.S. Exceptionalism Drives Advisor Allocations,” a biannual survey of financial professional data based on thousands of client interactions. We found that many advisors are using a balanced approach to diversify their U.S. large cap exposure across value, blend, and growth. (See Figure 1.)

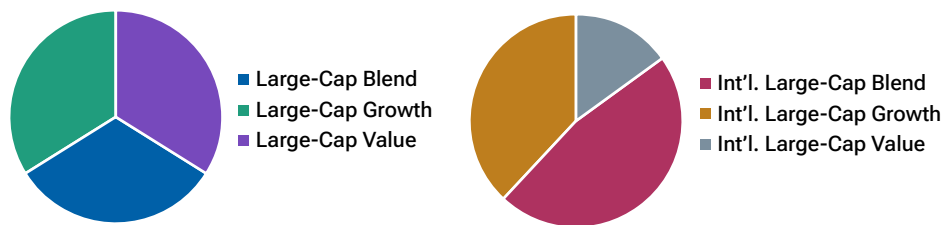
However, this was not the case for their international stock allocations, with international large-cap value notably underweight in advisor allocations. Our data showed that only 17% of advisor models carried an international large-cap value allocation, while international large-cap growth and large-cap blend carried 2.4x and 3.0x the overall weighting of international large value, respectively.

Key factor supporting international value: Diversification

In Figure 2, we highlight the stark differences between sector weights in

Advisors use a balanced approach with U.S. equity allocations but not with international equities

(Fig. 1) Chance of style usage: U.S. Large-Cap Equities vs. International Large-Cap Equities



Source: T. Rowe Price.

the MSCI EAFE Value Index and the MSCI EAFE Growth Index. As of April 30, 2025, the financials sector carried a 22.8% higher weight in international large value when compared with international large growth. Energy, utilities, and real estate are the next three highest relative overweights in value. International large value is underweight technology, industrials, and health care, with these underweights ranging from -16.2% for technology to -8.9% for health care.

These sector weightings point to two takeaways. The first is that value tends to be more cyclical, and the second is that these sector weightings highlight potential diversification opportunities across a full market cycle in light of the different drivers of return for these sectors. It's important to note that as of April 30, 2025, T. Rowe Price multi-asset portfolios maintain an overweight to international large value relative to international large

growth, driven by both fiscal stimulus and relatively favorable valuations.

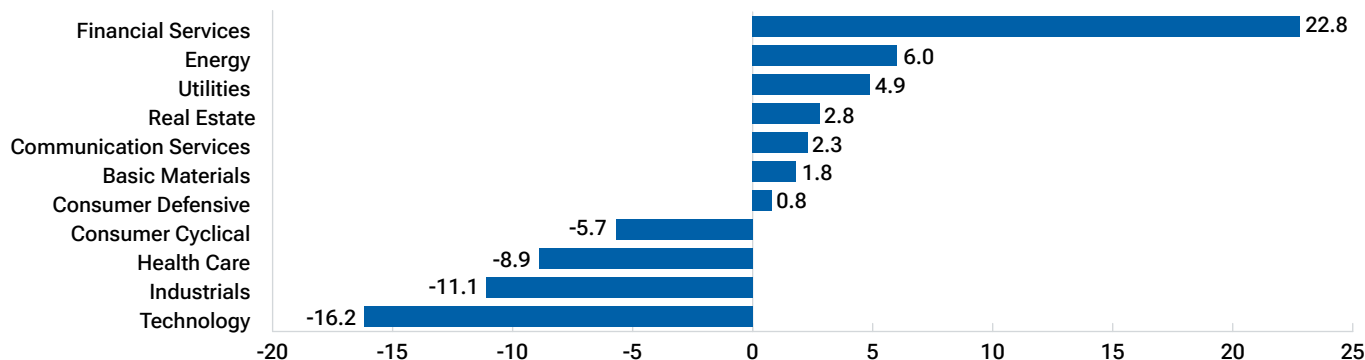
Key factor supporting international value: Monetary policy

Interest rate policy from the European Central Bank (ECB) is another dynamic that may favor international value versus growth. We looked at the period covering January 1, 2000, to April 30, 2025. When the ECB policy rate was equal to or below 0.50% during this period, the one-year forward excess return for the MSCI Value Index averaged -3.20% versus the MSCI Growth Index. During more positive rate environments in which the ECB policy rate was greater than 0.50%, the forward one-year excess return for value versus growth was an impressive 4.40%. The current ECB policy rate is 2.25%, which should leave a healthy cushion in the event of further cuts in rates.

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Sharp differences in sector weights highlight cyclical nature of international value stocks and diversification opportunities

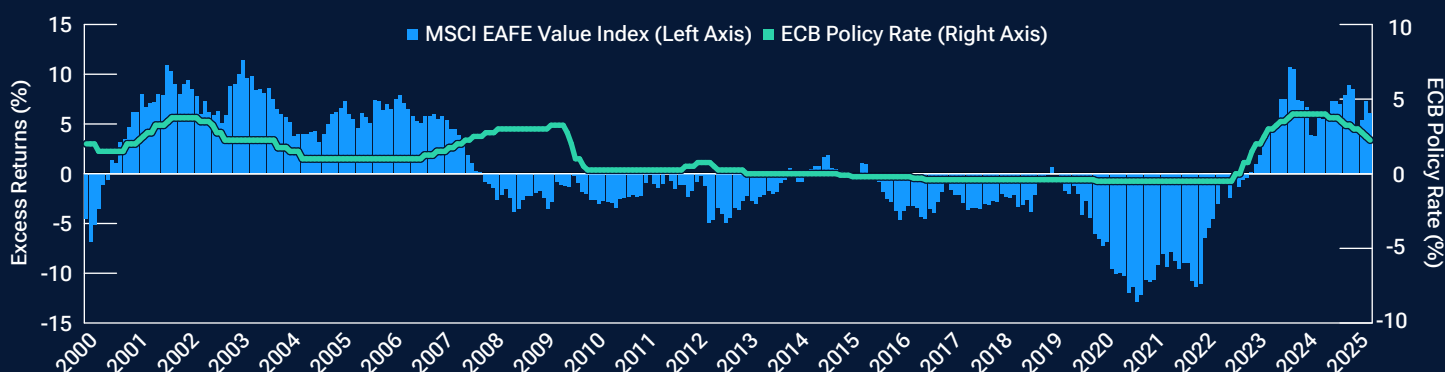
(Fig. 2) Sector weights (%): MSCI EAFE Value Index minus MSCI EAFE Growth Index as of April 30, 2025



Source: MSCI. Analysis by T. Rowe Price (see Additional Disclosures).

Over a 25-year period, international value outperformed international growth when the ECB policy rate was greater than 0.50%

(Fig. 3) Excess Returns: MSCI EAFE Value Index minus MSCI EAFE Growth Index, Rolling 3-Year Returns



January 1, 2000, through April 30, 2025.

Past performance is no guarantee or a reliable indicator of future results. Index performance is for illustrative purposes only and is not indicative of any specific investment. Investors cannot invest directly in an index.

Source: MSCI. Analysis by T. Rowe Price (see Additional Disclosures).

We analyzed rolling three-year returns and the relative performance of the MSCI EAFE Value Index and the MSCI EAFE Growth Index since January 2000. Growth outperformed value for approximately 15 years between 2008 and early 2023, with the outperformance accelerating with the 2020 pandemic. Since early 2023, however, value has started to outperform. A favorable monetary backdrop, relative valuations, and the potential for fiscal stimulus to boost

gross domestic product growth support a scenario in which value may continue to perform well versus growth.

Key factor supporting international value: Valuations

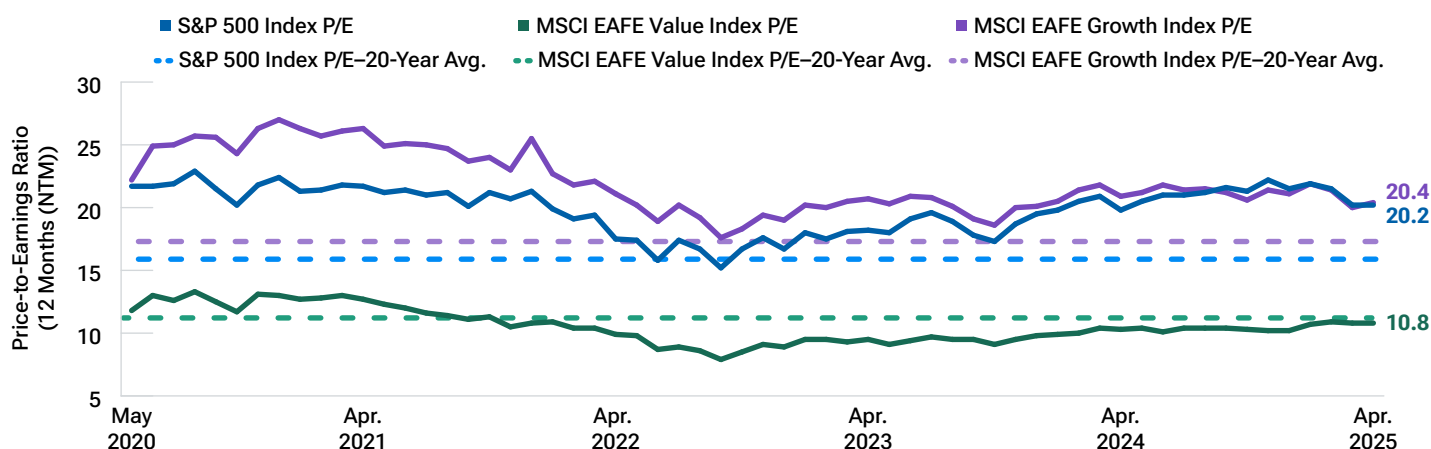
Our data suggest that advisors recently have pulled back from international allocations in moderate-risk model portfolios, with the average allocation

dropping 1.8 percentage points since 2023. We note, however, that as of April 30, 2025, the S&P 500 Index is trading at a 26.3% premium to its 20-year average forward price-to-earnings ratio. At the same time, the MSCI EAFE Growth Index is trading at a 17.9% premium to the same ratio.

In contrast, the MSCI EAFE Value Index is trading at a -3.0% discount to its P/E ratio. From a capital markets standpoint, this may serve as a tailwind to international

International value stocks trade at a discounted historical P/E ratio, while international growth stocks still trade at a premium

(Fig. 4) Price to Earnings (P/E) Valuations: S&P 500 Index, MSCI EAFE Growth Index, MSCI EAFE Value Index



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Sources: Standard & Poor's, MSCI. Analysis by T. Rowe Price. See Additional Disclosures.

performance with historically low relative valuations combined with underweight portfolio allocations.

Key factor supporting international value: Earnings growth

Earnings growth for the MSCI EAFE Value Index was particularly strong in 2022, with a 12.4% earnings per share growth besting both the S&P 500 Index and the MSCI EAFE Growth Index. Over the last three years, relative earnings growth has changed hands and favored growth equities—another argument for a broadly diversified portfolio exposure. For 2025 and 2026, however, the MSCI EAFE Value Index is forecast to see 7.9% and 9.2% earnings growth, respectively. Realizing these growth projections would provide a notable performance catalyst given the low level of starting valuations.

While subject to uncertainty and revision, the fiscal stimulus and corporate reforms that we see in Europe and Japan offer a level of confidence in the credibility of these estimates. The largest of these stimulus measures is a plan passed by Germany that allows for potentially unlimited borrowing for defense spending, while creating a €500bn 10-year fund to drive infrastructure investments. Mitigating this, however, are the ongoing and significant risks emanating from the global tariff war and its impact on potential recession scenarios.

How to reposition international value stocks

While international equities have lagged U.S. stocks over the intermediate and longer term, there may be an opportunity for international stocks to demonstrate better performance and diversify investor portfolios.

There are practical ways to implement international value in models:

- Since many advisor models have an existing international large-cap blend and/or international large-cap growth allocation, there could be an opportunity to pair a dedicated international large-cap value allocation into the sleeve.
- For advisors who prefer to utilize global strategies, pairing a global value strategy would serve the same function as above. One crucial step would be to monitor the ratio of U.S. versus international equities so that the overall international allocation settles at the desired level.

There's also a strategic asset allocation case to be made to diversify international large-cap equities in a more balanced manner. Given the large underweights we see to international value in advisors' model portfolios, there may be an opportunity to reposition existing equity allocations against a compelling backdrop of potential catalysts, including valuations, fiscal stimulus, monetary easing, and restructuring.

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Important Information

Risk Considerations

All investments are subject to market risk, including the possible loss of principal.

Diversification cannot assure a profit or protect against loss in a declining market.

Growth stocks are subject to the volatility inherent in common stock investing, and their share price may fluctuate more than that of a fund investing in income-oriented stocks.

The value approach to investing carries the risk that the market will not recognize a security’s intrinsic value for a long time or that a stock judged to be undervalued may actually be appropriately priced.

International investments can be riskier than U.S. investments due to the adverse effects of currency exchange rates, differences in market structure and liquidity, as well as specific country, regional, and economic developments. These risks are generally greater for investments in emerging markets.

Past performance is no guarantee or a reliable indicator of future results. All charts and tables are shown for illustrative purposes only.

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