



What goes up must come down

Will the US continue revert to the mean versus international markets?

Update
25 July 2025

In researching how to introduce an article on mean reversion, I stumbled across a lecture given by John C. Bogle, founder of the index fund provider Vanguard, to the Massachusetts Institute of Technology's Lincoln Laboratory in January 1998.

It struck me that there were many parallels with today's investment environment (don't forget, the US was deep into a long bull market that would, in time, accelerate and turn into the dotcom bubble).

The premise of the article was that while some opposing components of the stock market (value and growth, for instance) tend to out- or under- perform each other on occasion, over the long run, they converge and generally exhibit similar returns. In short, they revert to the mean.

One example given by Bogle was US versus international stocks. Bogle looked at data for the 38 years to 1998 using the S&P 500 Index for US stocks and the MSCI Europe, Australia and Far East (EAFE) Index for international stocks.

He found that during the first 24 years of this period, the EAFE index returned slightly more than the S&P 500 (9.7% per year versus 8.4%), before EAFE went on to rout the S&P 500 between 1984 and 1988. In the nine following years, though, the S&P 500 bounced back to form to recover all of its underperformance.

By the end of Bogle's 38-year period, both the S&P 500 and MSCI EAFE had each returned compound annualized gains of 11.5%. "The relative value of each initial \$1 invested by the investor who stayed in the US was worth precisely the same for the internationalist," Bogle said. "Over the long run, then, reversion to the mean has clearly manifested itself in global equity markets."

You can see a version of that in the chart below, which plots the return of the S&P 500 relative to the MSCI World ex-US Index between December 1969 and September 2013, where if the line is above 100, the US is outperforming and if the line is below 100, the rest of the world is outperforming.

We start at 100 at the end of 1969 and the rest of the world outperforms the US for almost three decades, until the US starts to pick up and reverses all its underperformance. The chart starts and finishes at 100, meaning both indices returned the exact same amount.

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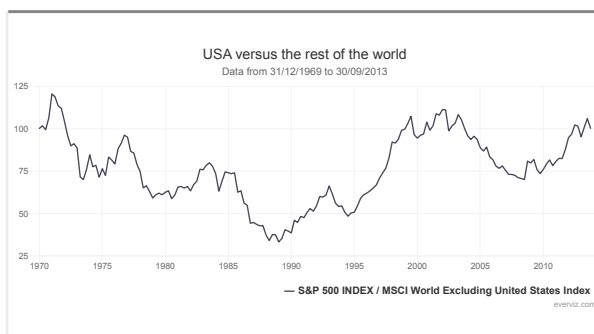
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Fig.1: Going On A Round Trip



Source: Bloomberg

Past performance is not a reliable indicator of future results.

A record to be broken

As a young(ish) person with a relatively low weighting to US markets (around 33% across my SIPP and ISA portfolios), this finding resonated. I still have what I believe is a decent amount invested in the US, but it's a c. 50% underweight versus, say, the MSCI All-World Country Index.

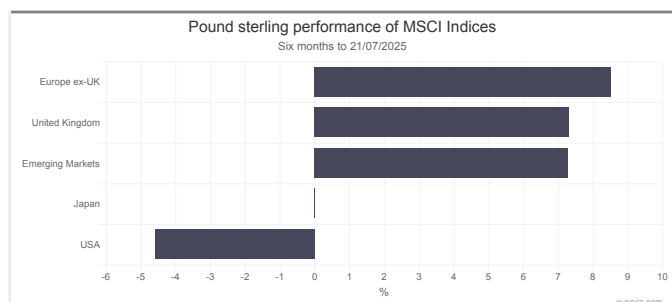


This is broadly because I believe that it will be almost impossible over the next couple of decades for the massive outperformance US markets have produced versus every other asset class, let alone equity region, to continue.

Happily, a cursory glance at my best-performing investments shows that this thesis is coming true, for the time being. Top of my ISA performers are UK funds such as **Temple Bar (TMPL)**, **Fidelity Special Values (FSV)** and **Odyssean (OIT)**, as well as **Montanaro European Smaller Companies (MTE)**. When it comes to my SIPP, **Fidelity China Special Situations (FCSS)** leads the way, ahead of MTE, **Aberforth Smaller Companies (ASL)** and **Fidelity Emerging Markets (FEML)**.

That's certainly a broad spread of different regions and countries outperforming their US counterparts in recent months. Indeed, while the S&P 500 Index returned c. 4.6% in the six months to 21/07/2025 in US dollar terms, the pound sterling denominated Vanguard S&P 500 exchange traded fund (ETF) has shed c. 4.2% in value. By contrast, the Vanguard FTSE 100 and Vanguard FTSE 250 ETFs are up c. 7.3% and 8.3% respectively over the same timeframe.

Fig.2: Six-Month Stock Market Performance



Source: FE fundinfo

Past performance is not a reliable indicator of future results.

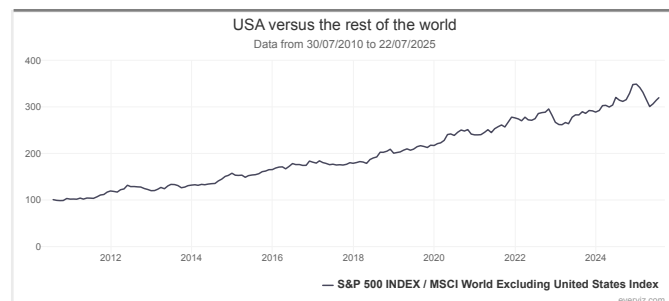
Some now argue that the US is so exceptional it will reinstate its world domination in due course, as soon as President Trump finishes chickening out of every threat he's made since becoming the leader of the free world.

Yet, if one believes in mean reversion, as Bogle did, it seems to me that the scene is set for the US to underperform. Consider the chart below, which shows the return of the S&P 500 relative to the MSCI World ex-US Index for the past 15 years. There's barely been any let up in US exceptionalism. The current short period of outperformance from the rest of the world is bigger than what we've seen previously, but still resembles a tiny blip.

A return to the mean would need a very long period of US underperformance and many will be sceptical that this is even possible. Both corporate earnings growth and GDP growth in the rest of the world, bar a few emerging economies, lag the US by a long shot and America's

technological innovation, not to mention the deepness of its capital markets, may very well continue to surprise us all.

Fig.3: Unbroken Us Leadership



Source: Bloomberg

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Still, Bogle pooh-poohed suggestions that earnings growth (then having averaged 12.6% after inflation for the past 15 years, versus a historical average of 4%) had "moved to a new, distinctly higher, plateau", something many believe is true today.

Then, \$1 of earnings from US equities were selling for \$21, which was well above their long-term average of \$14, leading Bogle to "suppose it's fair to say that our future expectations ought to be held in check". Today, \$1 of earnings from US equities are selling for c. \$22. That could go higher (as it did in the two years after Bogle's speech), but the likelihood is over a longer timeframe it will revert to the mean.

Bogle advocated for a total stock market approach for those in the audience – not only focusing on the S&P 500, but also mid-cap and small-cap stocks – through an index fund wrapper. Interestingly, he said that he saw "no compelling reason to include international equities" in portfolios, though I suspect that's because non-US index funds were harder to come by back then.

Of course, I'm overwhelmingly invested in actively managed funds with only two index funds in my portfolios (and even then they're what you'd probably call 'actively passive'). Still, I remain a believer in mean reversion, just as Bogle was. In his words, "I'm willing to stake my own retirement investment strategy on the fact that it will continue to exist".



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