



How to buy the world – the limitations of global tracker funds

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Buying the world – the limitations of global tracker funds

Investing in global equity index funds and exchange-traded funds is becoming increasingly cheap. The Amundi Prime Global ETF is available for an ongoing charges figure (OCF) of just 0.05% pa, while the OCF on the UBS Core MSCI World ETF was recently cut to 0.06%.

There's a lot to like about these products. As well as being cheap, they provide ready-made diversification across companies, industries and countries. More importantly, they've worked. With global stockmarkets rising – with the odd blip – since the global financial crisis they've delivered strong capital growth in recent years. These traits have made them popular with DIY investors, particularly at a time when many active funds have struggled.

So why shouldn't investors simply use global ETFs for their equity allocations? Here we highlight some of the limitations of this approach.

Concentration risk

At first glance the MSCI World seems highly diversified at a stock level, with over 1,300 constituents¹. However, the index is weighted by market value, so it is skewed toward its largest constituents, notably the Magnificent Seven of Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia and Tesla. The boom in their share prices means that the skew has become increasingly pronounced.

The chart below shows the percentage of the index in the ten largest constituents. For much of the last 30 years it has hovered around 10%, only going over 15% during the dot-com boom of the late 1990s. However, at times recently it has hit 25%, leaving investors in the index heavily exposed to a small group of companies.

MSCI World - % in top 10 holdings



Source: Morningstar, as at 30 September 2025

That isn't to say any of them are likely to disappear anytime soon. However, the one constant in investment is change.

The table below shows the top ten companies in the index over the last twenty years. Just five of the top ten from 2015 are still there today, and just one of the top ten from 2005 (Microsoft) has kept its place. Predicting the top ten in ten years' time is impossible, but if the past is anything to go by it's unlikely to be the same as today.

• MSCI World – largest 10 constituents over time		
• 2005	• 2015	• 2025
• General Electric Co	• Apple Inc	• NVIDIA Corp
• Exxon Mobil Corporation	• Microsoft Corp	• Apple Inc
• Microsoft Corp	• Exxon Mobil Corporation	• Microsoft Corp
• Citigroup	• General Electric Co	• Amazon.com Inc
• BP PLC	• Johnson & Johnson	• Meta Platforms Inc Class A
• Procter & Gamble Co	• Wells Fargo & Co	• Broadcom Inc
• Bank of America	• Amazon.com Inc	• Alphabet Inc Class A
• HSBC Holdings PLC	• Nestle SA	• Tesla Inc
• Johnson & Johnson	• JPMorgan Chase & Co	• Alphabet Inc Class C
• Pfizer Inc	• Alphabet Inc Class C	• JPMorgan Chase & Co

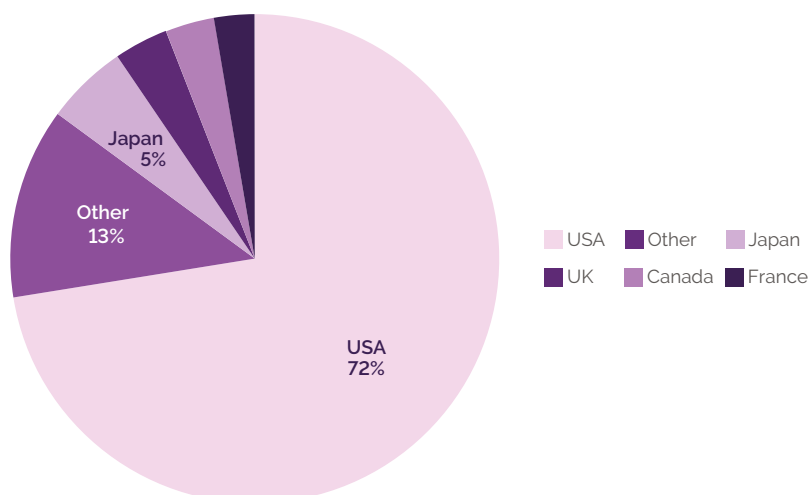
Passive investors can reduce this concentration risk by using a fund or ETF that follows an alternative weighting methodology, such as an equal-weight index. These are more expensive than standard market-cap weighted trackers, but by investing the same amount in each holding they reduce the impact of the largest companies on returns.

Active funds are also typically tilted away from the largest companies, though this varies and some can be highly concentrated.

Geographic risk

The MSCI World might be a global index, but it has become increasingly less global. While it offers exposure to companies from 23 countries, the strong recent performance of the US market means it makes up an increasing proportion of the index – currently this is over 70%. Any reversal in the fortune of US stocks would clearly be damaging for investors in the global index.

MSCI World - Breakdown by country



Source: Morningstar, as at 30 September 2005

Many wrote off the US stockmarket after the global financial crisis of 2007/2008 and have been proven wrong. Thinking that it is unstoppable could prove an equally costly error. Japan's market was also considered unstoppable in the 1980s. As recently as 1994 it made up over 30% of the MSCI World¹. Today it makes up just over 5%.

It's difficult to see what could end the US dominance, but declines in its tech stocks following the launch of Chinese AI model DeepSeek in January showed how quickly things can change. Much of the US market's rise has been driven by the potential of artificial intelligence, and if this potential isn't fulfilled then it could easily go into reverse.

There are a number of ways to reduce US exposure in a portfolio. The MSCI World consists solely of developed markets, so one is to invest in emerging markets as well. These come with their own risks, but do provide a degree of diversification.

Another popular way of tracking the world at a low cost is via the MSCI All Countries World Index (ACWI). This is similar to the MSCI World index, but also includes emerging markets countries such as China and India. Whilst this provides additional diversification, it's worth noting that the ACWI index still has over 64% invested in US companies¹.

Those looking to up their weight in emerging markets could also consider specialist emerging markets funds, or Asian funds with a high weight in emerging markets.

Funds investing in the UK, Europe or Japan are another way to raise the non-US weight in a portfolio, whilst there are also global ETFs that exclude the USA available at a low cost

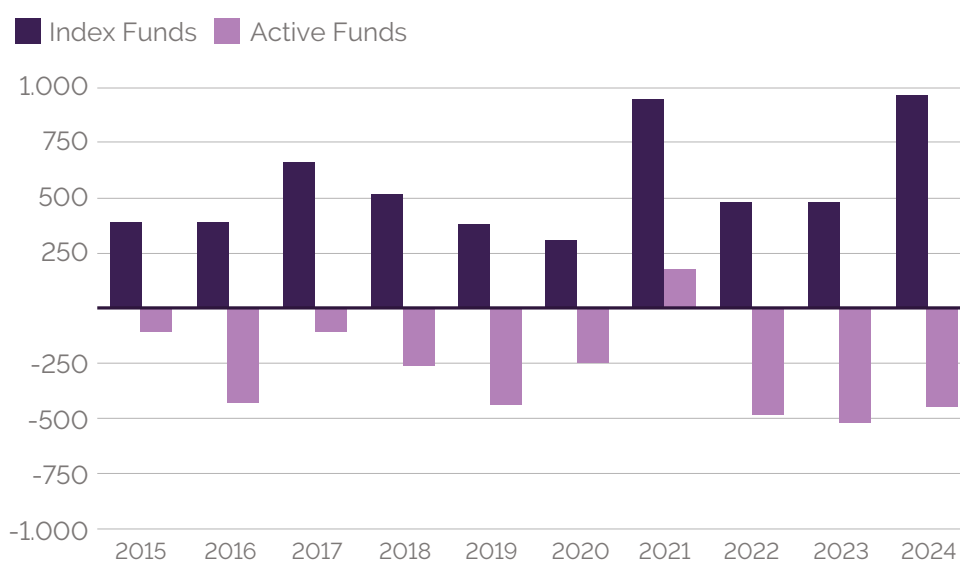
Valuation risk

Another risk of tracking global indices is that their strong rise has left them looking expensive on many valuation measures. This applies particularly to areas of the market featuring heavily in them like the US market, and within that the larger technology stocks mentioned earlier. The combination of high valuations and a concentrated market is a common feature of stockmarket bubbles, including the internet bubble of the late 1990s.

That doesn't necessarily mean we're in a bubble - valuations are subjective, and those large US technology companies could yet justify those valuations with strong growth. However, a particular concern this time is that the increased use of passive funds could be in part driving those high valuations.

The chart below shows net flows into passive and active funds over the last ten calendar years. Passive funds have attracted net inflows every year, whilst active funds have seen outflows in every year apart from 2021.

Global net flows (\$bn) Index funds versus Active funds



Source: Morningstar, as at 31 September 2025

Those flows into passives are going heavily into indices like the MSCI World, which has a high weighting to the US, and the S&P 500, which is all US companies. Any reversal in these flows is likely to see both indices suffer.

This isn't to predict that history will repeat itself, but it makes sense to position portfolios to offer some protection in case it does. Diversifying into cheaper areas of the global index, or even investing outside it altogether, could provide valuable diversification in the event of a change in sentiment.

Conclusion

Global index funds provide a cheap, straightforward way of investing in a large number of companies worldwide. They have also delivered strong performance in recent years.

They are a useful tool, but a blunt one. Leaving asset allocation to the market can tilt a portfolio towards areas that have been successful in the past and potentially leave it exposed to bubbles, whether that be in stocks, sectors or countries. This could lead to heavy losses if those bubbles burst.

No portfolio is without risk, but tilting exposure towards areas of the global index offering better value, or even investing outside mainstream indices altogether, could increase diversification and potentially provide great protection in a sell-off.

Asset allocation is one of the most important parts of investment and requires careful thought. Those in any doubt about the asset allocation in their portfolio should seek professional advice.

