4th Global Conference on Research in **Social Sciences**

21 - 23 August 2026 Oxford, United Kingdom

Looking Beyond the Home Market: What Iceland Can Teach Us About Long-Term Investing

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Abstract

How much should investors rely on their domestic market? For investors in small open economies, this is an especially important question. Local financial markets are often limited in size, highly concentrated, and vulnerable to country-specific shocks. Investing abroad offers greater diversification but also exposes investors to currency risk. Iceland provides an interesting setting in which to examine this trade-off. This study follows the performance of eight major asset classes available to Icelandic investors over the period 1992–2024. Returns are measured in Icelandic krona, so changes in exchange rates are treated as part of the investment experience rather than something to be hedged away. The sample spans a remarkable period in Iceland's economic history, from financial liberalisation and the banking boom to the 2008 collapse, the years of capital controls, and the subsequent recovery. The results challenge the idea that investors are well served by staying close to home. Although Icelandic equities delivered impressive returns during some periods, the losses suffered during the financial crisis had a lasting effect on long-term performance. Global equities proved to be a more reliable source of long-run wealth creation, while domestic government bonds provided stability when markets became volatile. Gold and foreign government securities offered useful protection during periods of sharp depreciation of the Icelandic króna, although they played a more limited role in long-term portfolio growth. The Icelandic experience illustrates a broader lesson for small open economies. A strong domestic market is valuable, but long-term investment success is difficult to achieve without meaningful international diversification. The findings therefore contribute to the discussion on home bias and strategic asset allocation in countries with independent currencies.

Keywords: strategic asset allocation; home bias; international diversification; Iceland; portfolio management.