Touchstone Investments®
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International Equities
Currency Backdrop

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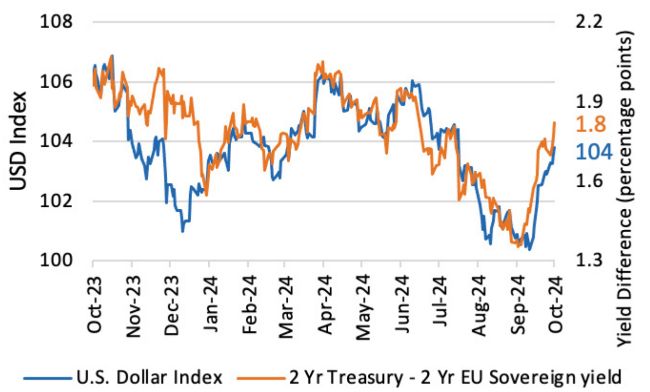
November 21, 2024

- The dollar may retest its 2022 highs. While we initially believed the rally had ended, a GOP sweep introduces factors like deregulation, lower taxes, and tariffs, which could boost the dollar.
- Short-term drivers, such as higher relative interest rates and potential tariffs, favor the dollar despite long-term challenges like fair value measures and a widening budget deficit. The broad dollar has rallied about 5% over the past two months.
- Looking back at the past Trump presidency, the dollar gained nearly 15% after tariffs began to be introduced in 2018. We don't mean to suggest that tariffs were the only factor, but they were important. We are concerned given that the proposed tariff policies outlined during this campaign are significantly greater than seen previously.
- Versus emerging markets, we believe there may be more dollar strength to come. During the last tariff war with China the renminbi fell about 10%. The policy proposals made during this campaign suggest greater pressure on China, but other emerging markets may not fare as well this time due to the increased risk of across-the-board tariffs.
- While we have become more cautious on international currencies, outcomes depend heavily on the implementation of the policy proposals and monetary policy. We will have to wait and see how closely the Trump administration holds to the policy proposals.

U.S. Dollar Index

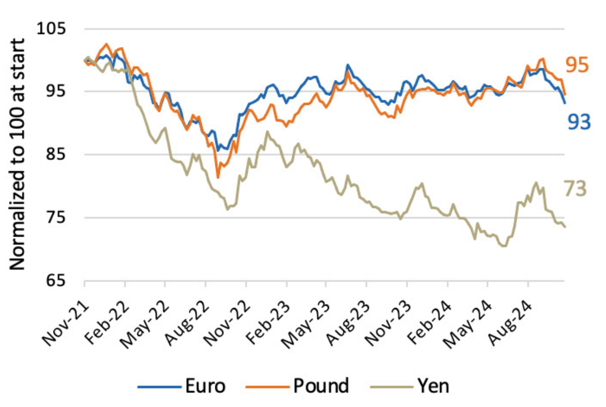
Source: Bloomberg. Daily data since 2022 through Nov 19, 2024

U.S. Dollar Index and Relative Interest Rates



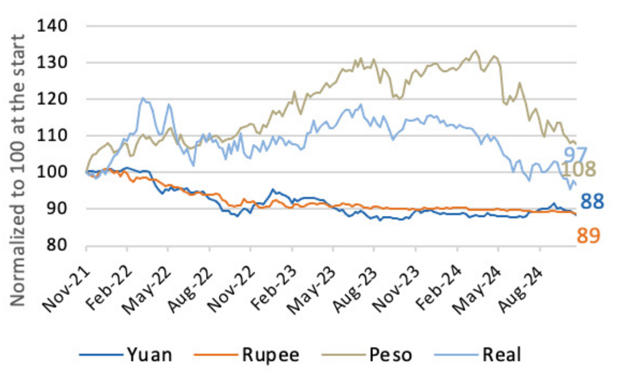
Source: Bloomberg. 1 year of daily data through Nov 20, 2024

Developed Currencies versus the Dollar



Source: Bloomberg. 3 years of weekly data through Nov 15 2024

Emerging Market Currencies versus the Dollar



Source: Bloomberg. 3 years of weekly data through Nov 15 2024

International Equities

Developed Ex-U.S.

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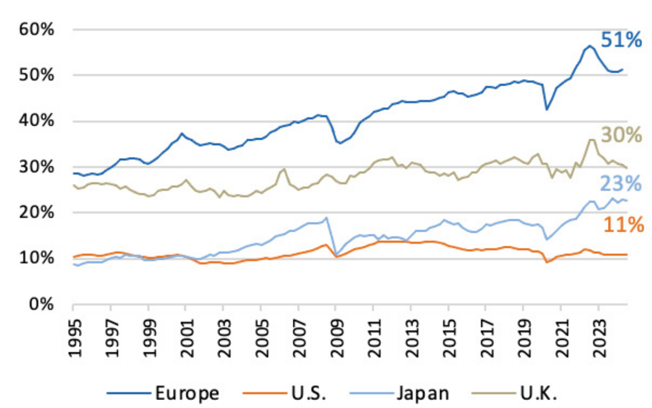
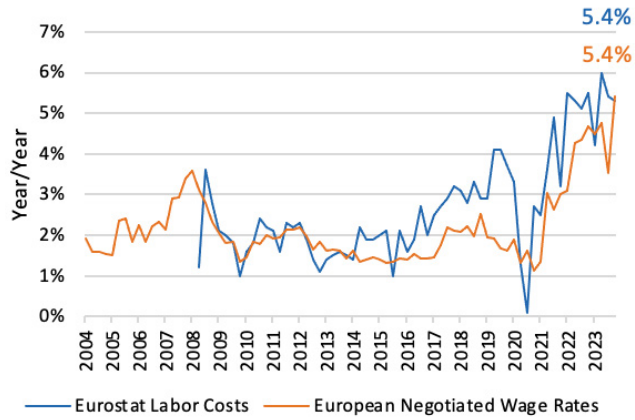
- We remain slightly underweight. Earlier plans to move to neutral or overweight have shifted given recent developments.
- Europe's economy continues to struggle with sluggish growth. The GOP sweep and reduced Fed rate-cut expectations introduce additional headwinds. Many European countries are under pressure to curb fiscal spending, which could hinder growth, echoing the impact of 2010 austerity measures. Tariffs are likely to add more downward economic pressure.
- The ECB has cut rates for the third time by 25 basis points in October and is expected by market indicators to do so again in December. Core inflation in the EU remains above target at 2.7% in October, and services inflation is 4.0% year-over-year. This puts the ECB in a tough spot as they balance weak economic conditions with tight labor conditions, indicated by wage growth. This is expected to keep the ECB on a moderate path for rate reductions.
- Japan has experienced strong equity performance this year in local currency terms, though when converted to dollars more than half of the return goes away. While earnings growth drove local currency returns, earnings growth estimates for 2025 are flat. The negative correlation between currency and earnings in Japan makes it difficult for U.S. investors to participate without hedging.
- Third quarter earnings for the MSCI EAFE index were mixed. 53% of reporting companies beat expectations while 43% missed. A 10% net earnings surprise compares with 58% for the S&P 500 Index. 2025 earnings estimates have fallen 7% since earnings season started. Economic softening in China appears to be contributing to this weaker outlook. 2025 earnings are expected to grow 5%, after 2% growth in 2024.
- We expect to maintain a slight underweight position due to a lack of catalysts for outperformance.

Exports as a Percent of GDP



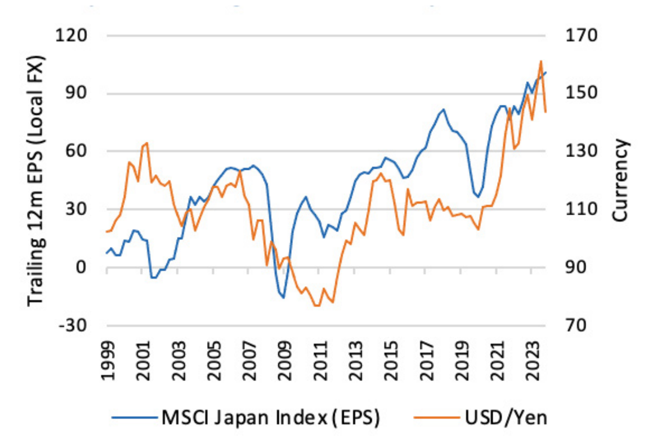
Source: Bloomberg. 30 years of quarterly data: Europe through Jun 2024, U.S. through Sep 2024, Japan through Sep 2024, U.K. through Sep 2024

European Wage Growth



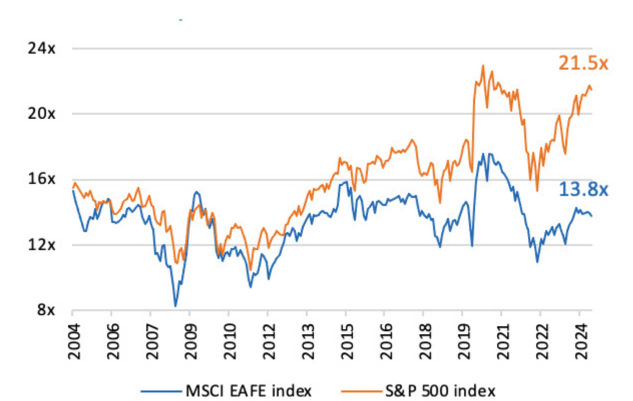
Source: Bloomberg. 20 years of quarterly data: Labor Costs through Sep 2024, Negotiated Wage Rates through Sep 2024

Japan Earnings and Currency



Source: Bloomberg. 25 years of quarterly data through Sep 2024

Forward P/E Ratios



Source: Bloomberg. 20 years of monthly data through Oct 2024

International Equities

Emerging Markets

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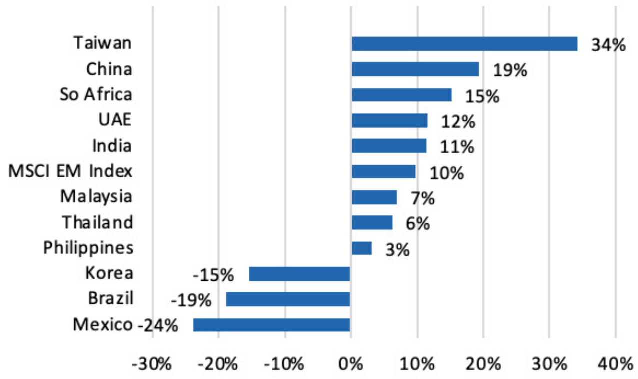
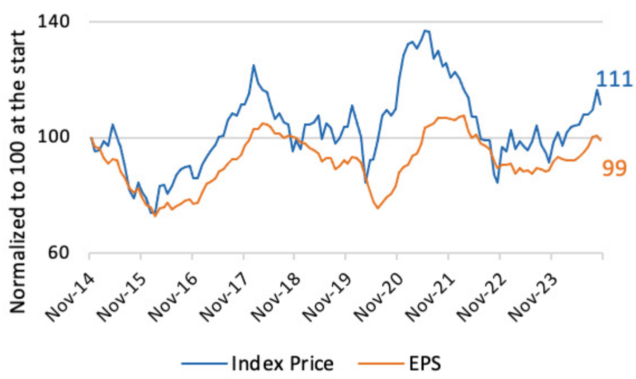
- We shifted to a slight underweight after the U.S. election. Tariff risks and slower Fed rate cuts could pressure EMs, with China most exposed. Historically U.S. monetary policy has had a significant impact on EM, a more hawkish Fed could hinder foreign direct investment inflows. Trump's tariff proposals are much broader, and EM beyond China may be at risk should the Trump administration emphasize the importance of re-shoring production as opposed to near-shoring.
- China's stimulus efforts so far have focused on stabilizing the economy as opposed to stimulating consumer demand. Demand focused stimulus may come with more clarity on U.S. tariff plans.
- The growth picture for neighboring EMs to China has become more uncertain. Third-quarter earnings for India were much weaker than seen in past quarters. Other South Asian countries have sold off on fears of sustained higher U.S. interest rates and tariff concerns.
- Mexico and Brazil have continued to underperform. Mexico has faced both currency and fundamental headwinds. Earnings for 2025 have been revised down 16% over this year. In Brazil, the central bank warned that they could be in a prolonged rate hiking cycle. The inflation outlook in Brazil has worsened given resilient economic growth, tight labor conditions, and fiscal policies that have raised wages and encouraged consumption.
- Despite these challenges, EM valuations remain attractive at 12x forward P/E ratio. We would also note that many of Trump's policy proposals are being taken at face value, yet a review of his first administration suggests actual policies may not be as severe.

YTD Total Returns (in USD) by Country



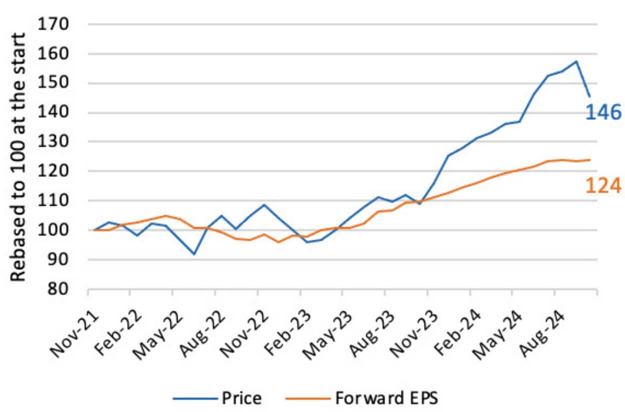
Source: Bloomberg. Data as of Nov 19 2024

MSCI EM Index Price and Forward EPS (in USD)



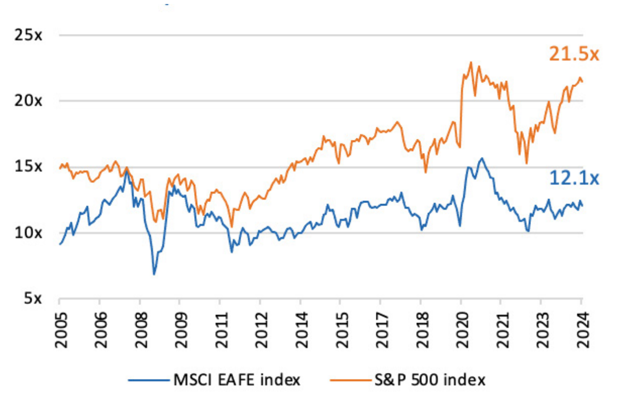
Source: Bloomberg. 10 years of monthly data through Oct 2024

MSCI India Index (local currency)



Source: Bloomberg. 3 years of monthly data through Oct 2024

Forward P/E Ratios



Source: Bloomberg. 20 years of monthly observations through Oct 2024

International Equities

Market Characteristics

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The Indexes mentioned are unmanaged statistical composites of stock market or bond market performance. Investing in an index is not possible.

Total Net Returns in USD

	October 2024	YTD	2023	2022	2021	Index Weight	EPS Growth Estimate 2024	EPS Growth Estimate 2025
MSCI EAFE	**-5.4%**	**7.3%**	**18.4%**	**14.0%**	**11.8%**	**100%**	**-2%**	**5%**
MSCI United Kingdom	-5.5%	9.1%	13.0%	-4.8%	18.5%	14%	-10%	3%
MSCI Japan	-3.9%	8.3%	21.5%	-16.3%	2.0%	23%	21%	0%
MSCI Europe	-6.0%	6.1%	21.6%	-17.3%	16.5%	48%	-7%	8%
MSCI EM	**-4.3%**	**12.2%**	**10.1%**	**-19.7%**	**-2.2%**	**100%**	**16%**	**14%**
MSCI China	-5.9%	21.9%	-11.3%	-21.8%	-21.6%	25%	18%	9%
MSCI India	-7.6%	16.2%	21.3%	-7.5%	26.7%	19%	32%	16%
MSCI Taiwan	3.7%	35.5%	31.3%	-29.1%	26.8%	19%	38%	17%
MSCI Korea	-7.5%	-12.0%	23.6%	-28.9%	-7.9%	10%	19%	23%

Valuations

	P/E (TTM)	Percent Rank	P/E (FTM)	Percent Rank	P/CF	Percent Rank	P/S	Percent Rank
MSCI EAFE	**15.2x**	**22%**	**14.6x**	**48%**	**9.7x**	**64%**	**1.5x**	**97%**
MSCI United Kingdom	12.8x	23%	11.8x	31%	8.0x	21%	1.3x	69%
MSCI Japan	15.2x	28%	15.1x	50%	8.9x	58%	1.2x	97%
MSCI Europe	15.4x	26%	15.1x	58%	10.4x	76%	1.5x	91%
MSCI EM	**15.9x**	**73%**	**13.4x**	**70%**	**10.8x**	**91%**	**1.6x**	**75%**
MSCI China	13.1x	43%	10.7x	32%	10.9x	69%	1.3x	39%
MSCI India	26.8x	94%	24.8x	96%	20.0x	96%	2.9x	93%
MSCI Taiwan	23.6x	75%	19.3x	90%	14.8x	87%	2.2x	86%
MSCI Korea	13.3x	66%	9.7x	12%	6.3x	52%	0.8x	82%

Fundamentals

	Dividend Yield	Percent Rank	Profit Margin	Percent Rank	ROE	Percent Rank	Net Debt / EBITDA	Percent Rank
MSCI EAFE	**3.1%**	**61%**	**8.0%**	**84%**	**10.5%**	**66%**	**1.5**	**7%**
MSCI United Kingdom	4.0%	67%	7.0%	45%	9.9%	30%	1.0	14%
MSCI Japan	2.2%	77%	6.8%	94%	9.3%	84%	-1.1	10%
MSCI Europe	3.2%	61%	8.4%	90%	11.9%	67%	2.7	5%
MSCI EM	**2.6%**	**53%**	**8.8%**	**54%**	**11.2%**	**36%**	**2.1**	**90%**
MSCI China	2.4%	51%	9.1%	17%	10.9%	28%	2.9	97%
MSCI India	1.1%	19%	10.1%	64%	15.9%	51%	2.5	51%
MSCI Taiwan	2.3%	32%	9.3%	70%	13.7%	79%	0.3	12%
MSCI Korea	2.2%	82%	6.3%	73%	8.1%	40%	2.6	40%

For Index Definitions see: TouchstoneInvestments.com/insights/investment-terms-and-index-definitions

Source: Bloomberg. Percent ranks are based on 30 years of monthly data as of the end of October; EPS growth estimates based on consensus bottom-up analyst estimates.

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The Touchstone Asset Allocation Committee (TAAC) consisting of Crit Thomas, CFA, CAIA – Global Market Strategist, Erik M. Aarts, CIMA – Vice President and Senior Fixed Income Strategist, and Brian Cheyne, CFA, CIMA – Senior Investment Strategy Specialist, develops in-depth asset allocation guidance using established and evolving methodologies, inputs and analysis and communicates its methods, findings and guidance to stakeholders. TAAC uses different approaches in its development of Strategic Allocation and Tactical Allocation that are designed to add value for financial professionals and their clients. TAAC meets regularly to assess market conditions and conducts deep dive analyses on specific asset classes which are delivered via the Asset Allocation Summary document. Please contact your Touchstone representative or call 800.638.8194 for more information.

A Word About Risk

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