Touchstone Investments®
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International Equities

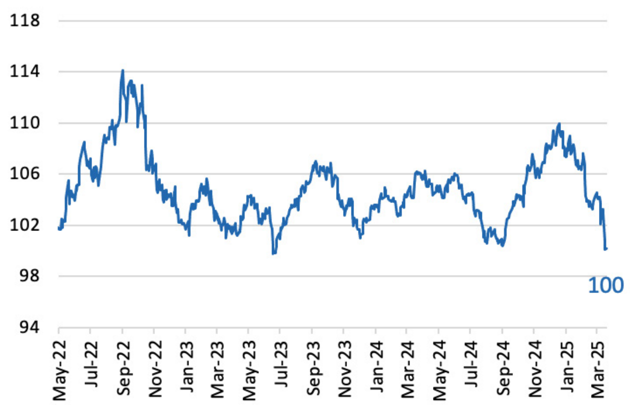
Currency Backdrop

Authors: Crit Thomas, CFA, CAIA / Erik M. Aarts, CIMA / Brian Cheyne, CFA, CIMA

April 14, 2025

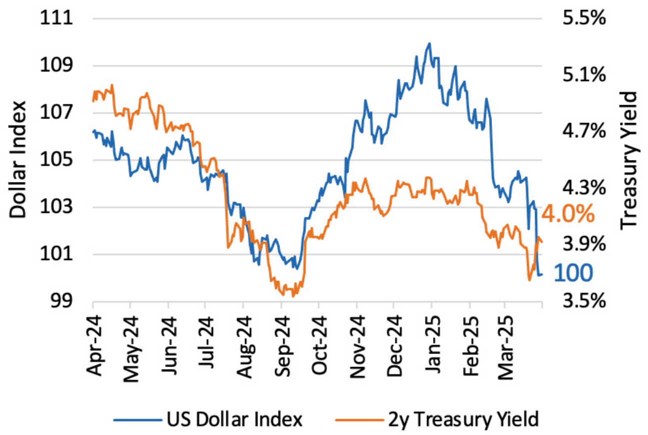
- The recent decline in the dollar is concerning. Up until April 4, its weakness could largely be explained through interest rate differentials. That's no longer the case. While we'd like to attribute the dollar's weakness to short-term noise, there are deeper issues to consider.
- Since April 4, 10-year Treasury yields have risen, even as recession risks have increased. Typically, rising US yields – especially when global rates are flat or falling – support the dollar. But that hasn't happened.
- The dollar dropped sharply on "Liberation Day," when the U.S. announced tariffs that exceeded even those enacted under the Smoot-Hawley Tariff Act. Typically, the currency of the country being tariffed weakens – not the country imposing them.
- "Liberation Day" also brought global uncertainty. Normally, global uncertainty pushes investors toward the safety of the dollar and Treasuries. But this time, with the U.S. being the source of instability, investors looked elsewhere.
- Other unusual signs include falling commodity prices (most commodities are priced in dollars) and a significant decline in the stock market, both of which tend to be negatively correlated with the dollar.
- Most likely, the dollar's decline reflects a negative shift in global sentiment toward the U.S. The dollar is a trending asset, and it may stay under pressure until there is more clarity and resolution around trade policy.

U.S. Dollar Index



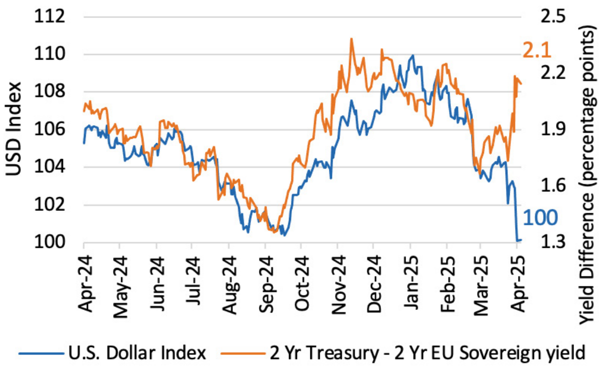
Source: Bloomberg. 1 year of daily data through Apr 14 2025

U.S. Dollar and Treasury Yields



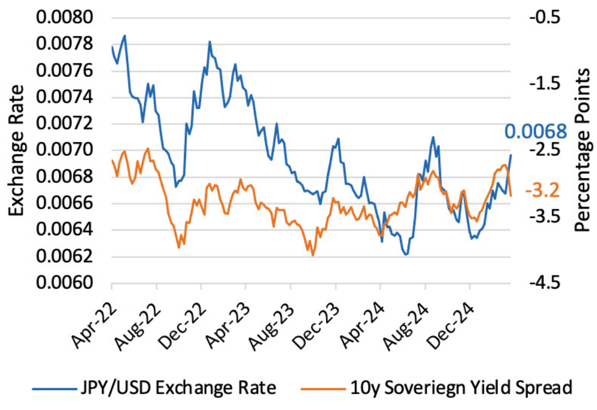
Source: Bloomberg. 1 year of daily data through Apr 14 2025

U.S. Dollar Index and Relative Interest Rates



Source: Bloomberg. 1 year of daily data through Apr 11 2025

Yen/Dollar and Yield Spread



Source: Bloomberg. 3 years of weekly data through Apr 11 2025

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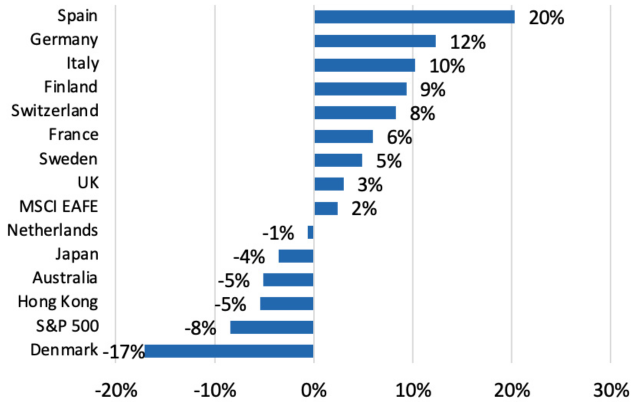
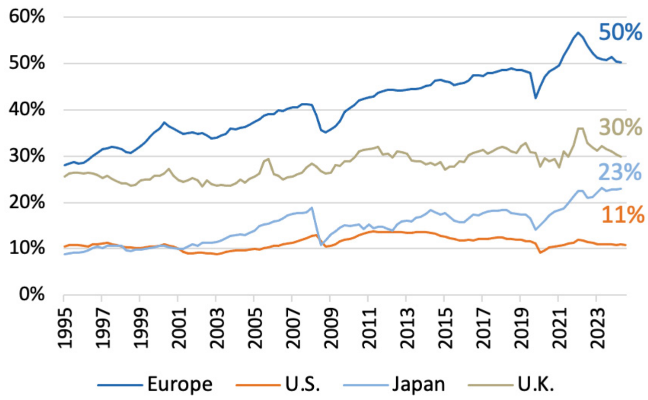
- We reversed last month's tactical tilt toward developed international markets. The April 2 tariff announcement was much larger than anticipated and could outweigh the fundamental improvements we were seeing in Europe.
- After the tariff announcement, the euro, yen, and pound all strengthened. While that's good news for U.S. investors holding international assets, it makes the tariffs even more painful for those countries. Even though some tariffs were paused for non-retaliating countries, a 10% across-the-board tariff remains, as do 25% tariffs on autos, steel, and aluminum.
- Europe responded with retaliatory tariffs related to the steel and aluminum tariffs. We anticipate further retaliation if there is no progress in negotiations. The Trump administration has shown clear animosity toward Europe, and we believe this could be the beginning of a protracted trade conflict. The longer it continues, the greater the potential damage.
- The U.S. is the EU's largest export partner, accounting for about 5% of the EU's GDP. Key industries include medical and pharmaceutical products, autos, and industrial machinery -- industries that support high-quality jobs. The EU's 2025 GDP growth forecast is now below 1%, and recession risks are rising if these tariffs persist or escalate.
- Japan relies less on U.S. exports due to decades of offshoring, but exports to the U.S. still make up 2.3% of its GDP. Japan has been given priority in tariff negotiations. Japan will be put in a tough spot as its largest trading partner is China.
- Bottom-up earnings growth for the MSCI EAFE index is estimated at 7% for 2025. We think that's optimistic given the combination of tariffs and currency strength. Earnings may ultimately decline.

YTD Total Return by Country (in USD)



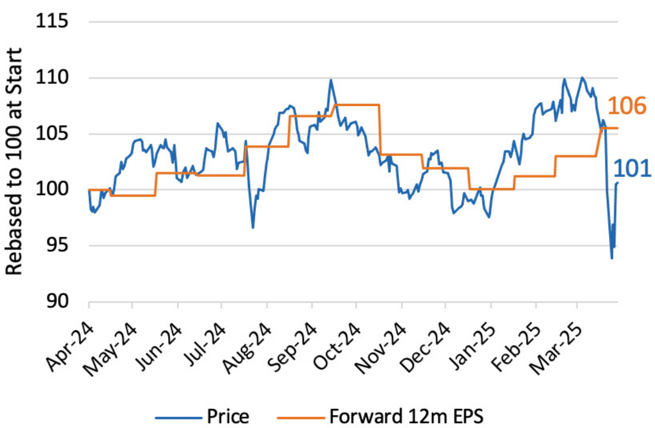
Source: Bloomberg. Data as of Apr 11 2025

Exports as a Percent of GDP



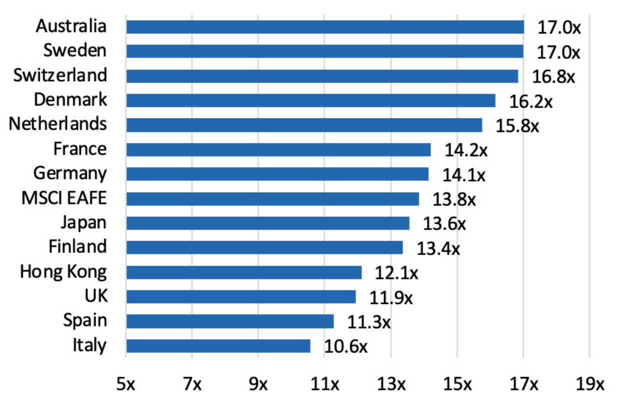
Source: Bloomberg. 30 years of quarterly data: Europe through Dec 2024, U.S. through Mar 2025, Japan through Dec 2024, U.K. through Dec 2024.

MSCI EAFE Index



Source: Bloomberg. 1 year of daily observations through Apr 11 2025

Forward P/E by Country



Source: Bloomberg. Data through Apr 11 2025

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Emerging Markets

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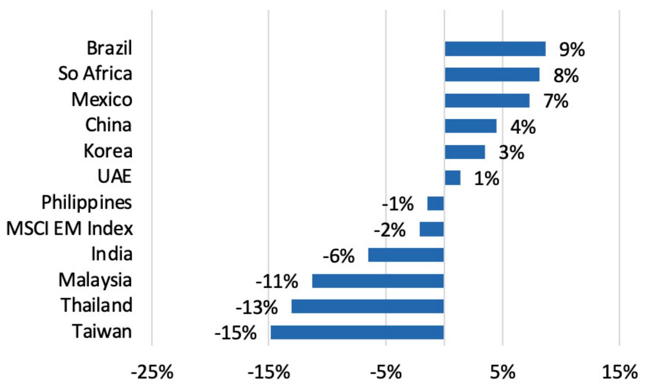
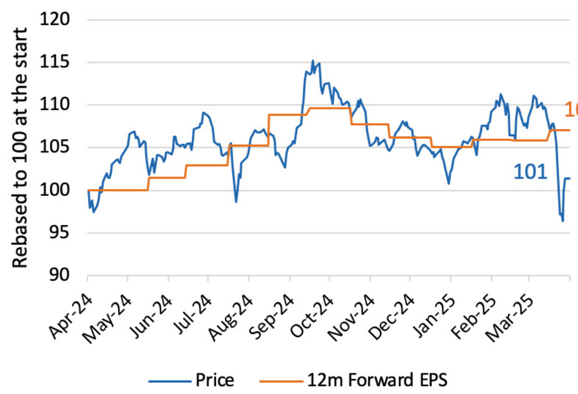
- We remain slightly underweight EM.
- The U.S./China tariff war has intensified. China makes up 28% of the EM index. Tariffs have now reached levels that are likely to effectively halt trade between the world's two largest economies. Exports to the US account for 2.9% of China's GDP. Removal of 2.9% of GDP overnight would have a sizable and negative impact on their economy and the stock market. We expect China to increase government spending to help offset the economic impact.
- India, the second-largest EM weight at 18%, is less exposed to the U.S. (2.4% of GDP). However, it may face pressure to reduce its own import tariffs (which are significant). That could hurt protected industries in the short run and reduce government revenue, as import duties are an important part of India's budget.
- Taiwan (a 17% weight in the EM index) is the most exposed, with exports to the U.S. making up 14.7% of GDP. Many of these exports are semiconductors, which are currently excluded from tariffs. Tariff negotiations are likely to be related to Taiwanese manufacturing production in China.
- South Korea (a 9% weight in the EM index) sends 6.8% of its GDP in exports to the U.S. It has a free trade agreement with the U.S. and is in high level trade negotiations, potentially involving shipbuilding cooperation.
- Greater clarity on tariffs and Fed policy is needed for EM to find direction. We believe our cautious stance is appropriate for now. That said, these markets have substantial long-term potential, and any negotiated trade resolution could spark a rally.

YTD Total Returns (in USD) by Country



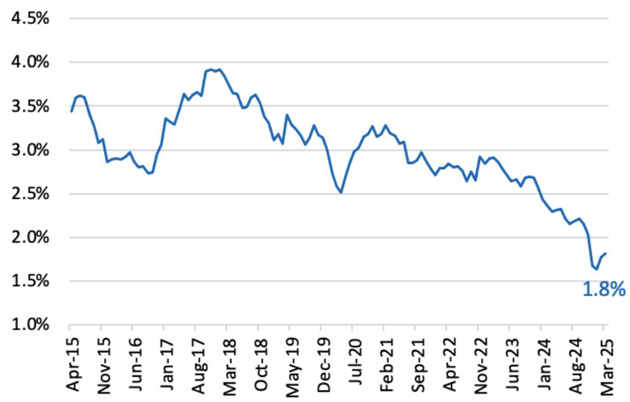
Source: Bloomberg. Data as of Apr 11 2025

MSCI EM Index (in USD)



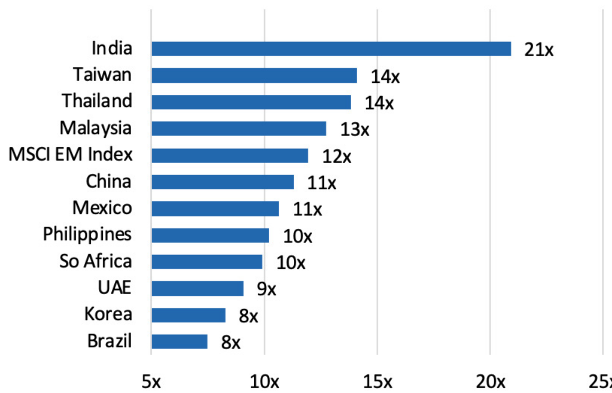
Source: Bloomberg. 1 year of daily data through Apr 14 2025

China 10 Year Government Bond Yield



Source: Bloomberg. 10 years of monthly data through Mar 2025

Forward P/E by Country



Source: Bloomberg. Data as of Apr 11 2025

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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

	March 2025	YTD	2024	2023	2022	Index Weight	EPS Growth Estimate 2024	EPS Growth Estimate 2025
MSCI EAFE	**-0.3%**	**7.0%**	**4.3%**	**18.9%**	**-13.9%**	**100%**	**-1%**	**7%**
MSCI United Kingdom	0.7%	9.7%	7.5%	14.1%	-4.2%	14%	-9%	3%
MSCI Japan	0.3%	0.5%	8.7%	20.8%	-15.7%	22%	8%	8%
MSCI Europe	-0.4%	10.9%	1.0%	22.7%	-16.7%	54%	-6%	9%
MSCI EM	**0.7%**	**3.0%**	**8.1%**	**10.3%**	**-19.2%**	**100%**	**12%**	**11%**
MSCI China	2.0%	15.1%	19.7%	-11.0%	-21.8%	28%	16%	6%
MSCI India	9.4%	-2.9%	12.4%	21.3%	-6.2%	18%	25%	11%
MSCI Taiwan	-11.5%	-12.6%	35.1%	31.3%	-29.5%	17%	24%	26%
MSCI Korea	-0.8%	5.2%	-23.1%	23.6%	-28.9%	9%	29%	32%

Valuations

	P/E (TTM)	Percent Rank	P/E (FTM)	Percent Rank	P/CF	Percent Rank	P/S	Percent Rank
MSCI EAFE	**15.3x**	**23%**	**13.4x**	**51%**	**9.7x**	**62%**	**1.6x**	**98%**
MSCI United Kingdom	13.3x	30%	11.4x	41%	8.2x	31%	1.4x	77%
MSCI Japan	13.7x	17%	13.5x	31%	8.3x	42%	1.1x	94%
MSCI Europe	16.4x	38%	14.0x	71%	10.7x	82%	1.7x	95%
MSCI EM	**15.1x**	**62%**	**11.4x**	**66%**	**10.3x**	**86%**	**1.6x**	**79%**
MSCI China	14.8x	65%	10.1x	54%	12.3x	80%	1.4x	48%
MSCI India	25.2x	85%	20.9x	84%	18.8x	91%	2.7x	87%
MSCI Taiwan	17.6x	49%	12.5x	61%	11.5x	66%	1.9x	72%
MSCI Korea	9.7x	17%	8.0x	18%	5.2x	20%	0.8x	81%

Fundamentals

	Dividend Yield	Percent Rank	Profit Margin	Percent Rank	ROE	Percent Rank	Net Debt / EBITDA	Percent Rank
MSCI EAFE	**3.1%**	**57%**	**8.2%**	**87%**	**10.9%**	**70%**	**1.5**	**7%**
MSCI United Kingdom	3.7%	53%	7.2%	51%	10.8%	39%	1.0	14%
MSCI Japan	2.4%	84%	7.3%	99%	9.7%	91%	-1.0	11%
MSCI Europe	3.0%	53%	8.4%	89%	11.9%	66%	2.8	4%
MSCI EM	**2.8%**	**66%**	**9.7%**	**73%**	**12.1%**	**53%**	**2.0**	**80%**
MSCI China	2.5%	58%	10.1%	37%	11.7%	36%	3.0	99%
MSCI India	1.2%	25%	10.3%	67%	15.8%	51%	2.5	52%
MSCI Taiwan	2.6%	39%	10.2%	83%	15.4%	93%	0.2	11%
MSCI Korea	2.3%	85%	7.3%	83%	8.2%	41%	2.6	45%

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 March; EPS growth estimates based on consensus bottom-up analyst estimates.

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