

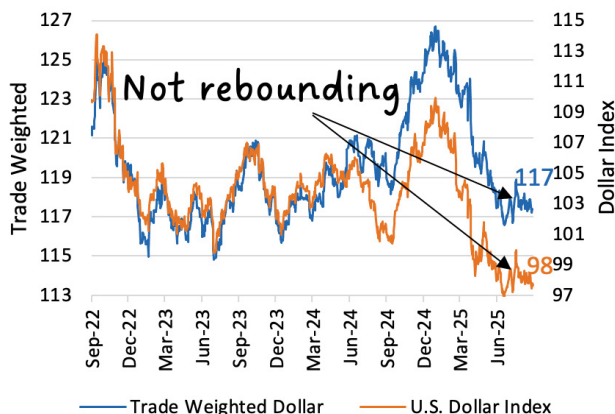


Authors: Crit Thomas, CFA, CAIA / Erik M. Aarts, CIMA / Tim Paulin, CFA

September 13, 2025

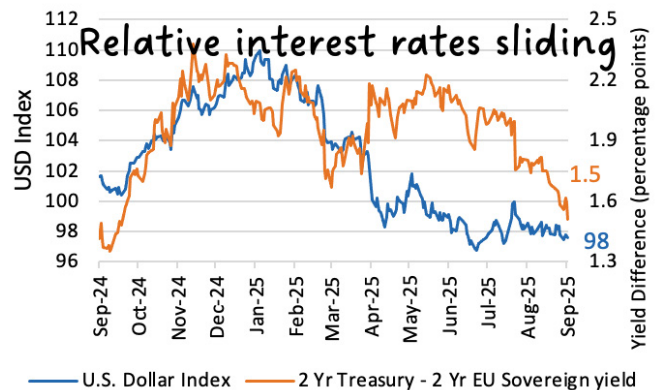
- ▶ **Treading Water:** After a sharp decline in the first half of the year, the U.S. dollar has leveled off. Its next move is uncertain, though the balance of drivers points to a downside bias.
- ▶ **Relative Interest Rates:** Softer U.S. labor data has raised expectations for more Fed rate cuts, while many trading partners' central banks are on hold or leaning toward rate hikes. This makes U.S. assets less attractive to foreigners. Inflation also plays a role (real rates). Tariffs could push U.S. prices higher while putting downward pressure on global prices due to excess manufacturing capacity, further eroding the relative appeal of holding U.S. assets.
- ▶ **Oil Prices:** Since the U.S. became a net oil exporter, the dollar has become positively correlated with oil prices. Higher crude prices improve the U.S. terms of trade, while lower prices have the opposite effect. In other words, the demand for dollars rises and falls with the price of oil. With oil down ~10% year-to-date, slowing economic growth in the U.S. and China (the largest consumers of oil), and OPEC+ boosting supply, the backdrop looks unfavorable for the dollar.
- ▶ **Fair Value:** Purchasing power parity and other valuation measures suggest the dollar is richly valued. While valuation is a poor timing tool, persistent fiscal and current account deficits keep the U.S. reliant on steady foreign capital inflows to fund these deficits, an ongoing vulnerability.
- ▶ **Productivity:** Recent productivity gains may continue with AI adoption. This should be dollar positive.
- ▶ **Sentiment:** The dollar remains the world's reserve currency and safe haven, but sanctions, tariffs, and U.S. policy unpredictability have nudged some foreign bodies toward gold and searching for other substitutes. Still, no credible alternative exists with the size and depth of our debt markets, making this more of a marginal drag.
- ▶ **Summary:** Taken together, the fundamentals point to longer-term vulnerability for the dollar, supporting the case for U.S.-based investors to have strategic allocations in international equities.

US Dollar Indexes



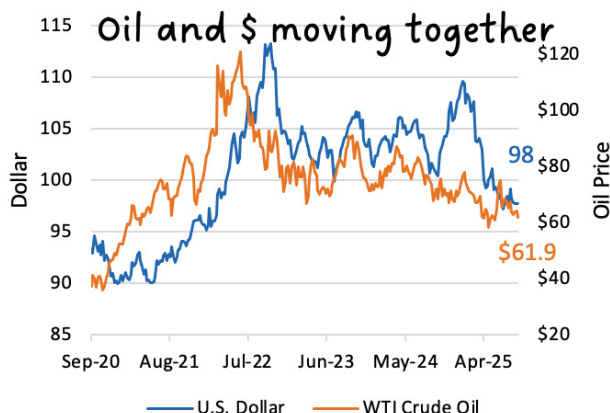
Source: Bloomberg. 3 years of daily data through Sept 11 2025

U.S. Dollar Index and Relative Interest Rates



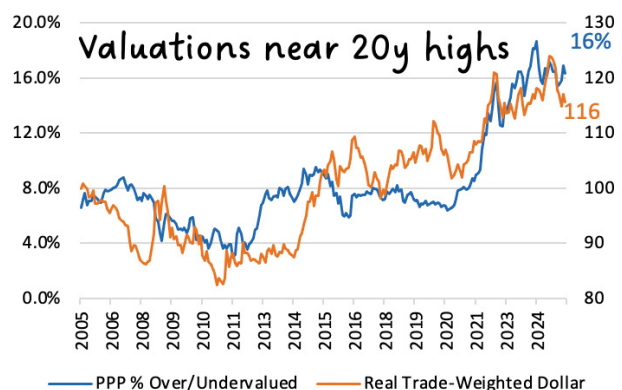
Source: Bloomberg. 1 year of daily data through Sep 10 2025

U.S. Dollar and Oil Prices



Source: Bloomberg. 5 years of weekly data through Sep 05 2025. West Texas Intermediate (WTI) crude is primarily sourced in the U.S. Permian Basin.

U.S. Dollar Valuation Measures



Source: Bloomberg. 30 years of monthly data through Aug 31 2025

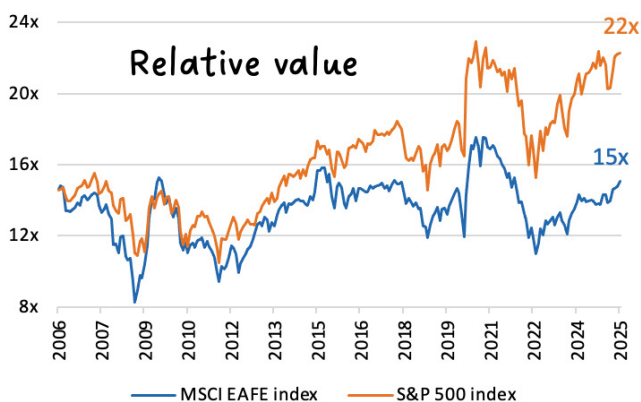


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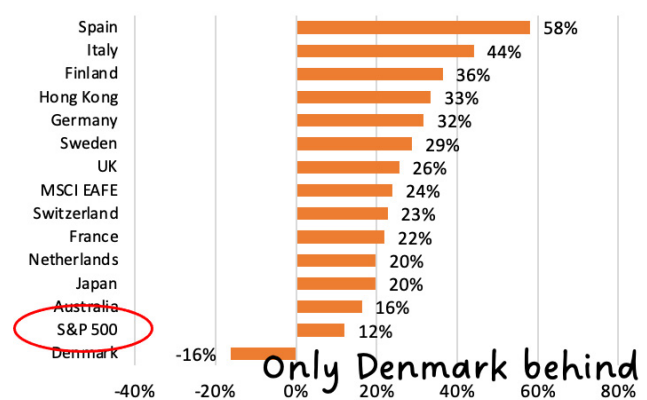
- ▶ We maintain a neutral strategic allocation to developed international equities.
- ▶ Traditional performance drags such as currency volatility and expanding valuation discounts are easing and may even become tailwinds. With these pressures abating, developed international equities are better positioned to compete with U.S. stocks, with earnings and dividends as the primary drivers of returns.
- ▶ By contrast, U.S. equities face several headwinds: stretched valuations, elevated profit margins, and the likelihood of continued slow economic growth, all pointing to more modest longer-term returns.
- ▶ Tariff agreements with Japan and Europe reduced near-term trade fears and were generally received positively by the markets, removing worst-case trade scenarios, at least for now. Nonetheless, both Japan and Europe still face trade headwinds with the U.S. and China.
- ▶ The fundamental backdrop remains mixed. Economic growth in the eurozone has slowed considerably, with business investment being the main drag on growth. And political risks are worth watching in Japan, the UK, and France. Still, global revenue exposure limits the impact of local politics on heavyweights that dominate the index for those countries. Europe's economy is expected to gradually rebound, while Germany's suspension of its debt brake opens the way to fiscal stimulus, and Japan continues to push for shareholder-friendly reforms.
- ▶ Looking forward, we believe a strategic allocation to developed international equities should benefit longer-term investors due to potential diversification benefits, lower valuations, a possible currency tailwind, and less reliance on a narrow set of U.S. stocks.

Forward P/E Ratios



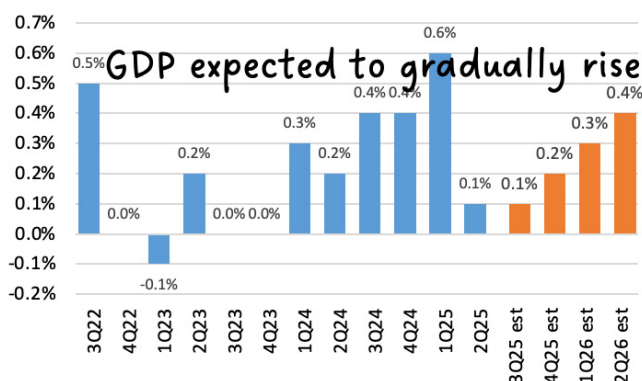
Source: Bloomberg. 20 years of monthly observations through Aug 2025

YTD Total Return by Country (in USD)



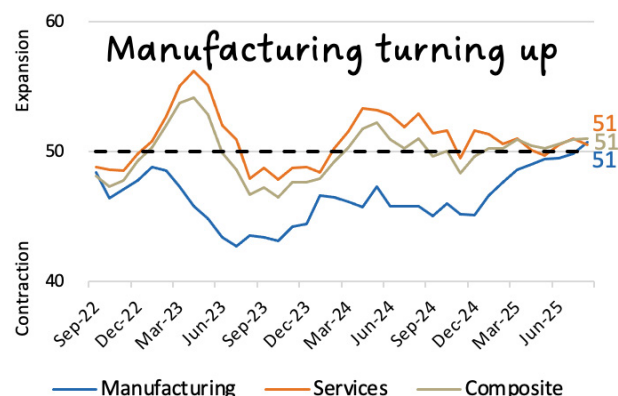
Source: Bloomberg. Data as of Sep 10 2025

Eurozone Real GDP Growth (Q/Q annualized)



Source: Bloomberg. The Eurozone is a currency union that includes the 20 countries that have adopted the euro.

Eurozone: IHS Markit Diffusion Indexes



Source: Bloomberg. 20 years of monthly data through Aug 2025

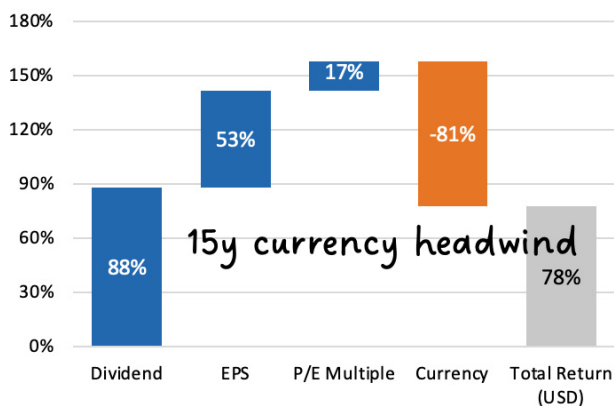


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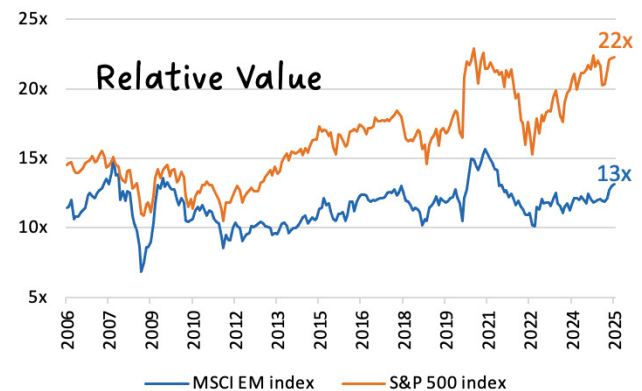
- ▶ We have a strategic weight in emerging market (EM) equities, reflecting a balanced risk/reward profile versus U.S. equities.
- ▶ As with international developed markets, currency and valuation headwinds are easing, meaning they are less likely to weigh on returns, they may even enhance returns. With these headwinds easing, we see dividends and earnings driving EM equity, putting them on more even footing with U.S. stock return drivers.
- ▶ Expected Fed rate cuts should support emerging markets as they give EM policymakers more room to stimulate growth and could boost capital flows. Historically, EM has outperformed both U.S. and developed international stocks during Fed easing cycles.
- ▶ EM also provides significant exposure to the technology sector (the largest EM index weight) and AI. The index includes key companies in the global AI semiconductor supply chain. And investors gain exposure to China's differentiated approach to AI (open source), which may broaden the investable universe by spreading AI adoption more rapidly and widely.
- ▶ Looking ahead, we believe EM earnings appear well-positioned to rival U.S. earnings over the next decade, supported by favorable demographics and a more growth-oriented index composition. Valuations remain compelling, with broad discounts to the S&P 500 on earnings and book value (India being the main exception). Lower labor costs and less saturation in technology and services create room for future operating leverage.
- ▶ EM investing is not without risks. Tariffs are likely to remain a growth headwind while China's economic growth is slowing. Heightened political uncertainty seen in several countries is also something of a constant for EM.
- ▶ In summary, EM equities should remain a strategic holding, offering diversification and long-term growth potential, despite ongoing risks.

MSCI EM Index Return Composition



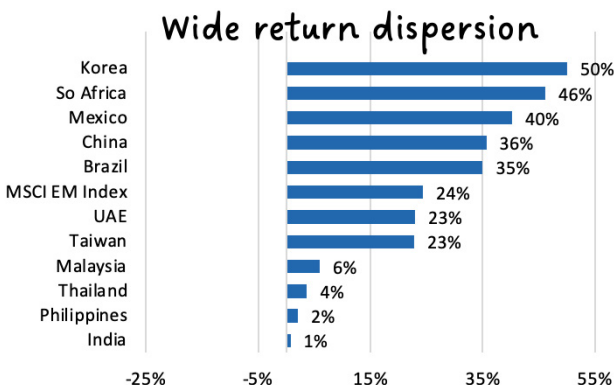
Source: Bloomberg. Cumulative total returns over the last 15 years through Aug 2025

Forward P/E Ratios



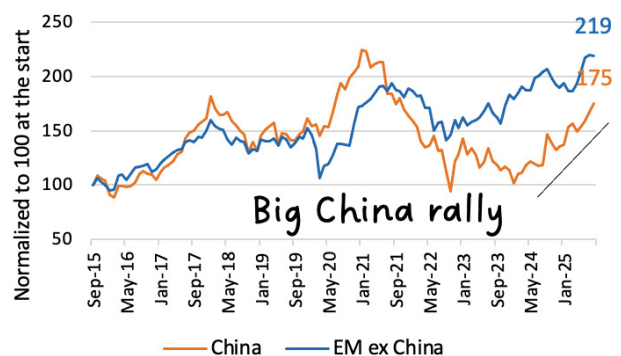
Source: Bloomberg. 20 years of monthly observations through Aug 2025

YTD Total Returns (in USD) by Country



Source: Bloomberg. Data as of Sep 10 2025

Total Returns in USD using MSCI Indexes



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



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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							EPS Growth Estimate	
	Aug 2025	YTD	2024	2023	2022	Index Weight	2025	2026
MSCI EAFE	4.3%	23.3%	4.3%	18.9%	-13.9%	100%	NA*	NA*
MSCI United Kingdom	3.7%	24.7%	7.5%	14.1%	-4.2%	14%	-4%	9%
MSCI Japan	7.0%	18.1%	8.7%	20.8%	-15.7%	22%	-3%	10%
MSCI Europe	3.4%	26.0%	1.0%	22.7%	-16.7%	55%	-1%	11%
MSCI EM	1.5%	19.6%	8.1%	10.3%	-19.2%	100%	NA*	NA*
MSCI China	4.9%	29.2%	19.7%	-11.0%	-21.8%	25%	1%	15%
MSCI India	-2.2%	-1.0%	12.4%	21.3%	-6.2%	16%	5%	17%
MSCI Taiwan	-0.8%	15.7%	35.1%	31.3%	-29.5%	19%	11%	16%
MSCI Korea	-1.9%	42.6%	-23.1%	23.6%	-28.9%	11%	17%	18%

Valuations								
	P/E (TTM)	Percent Rank	P/E (FTM)	Percent Rank	P/CF	Percent Rank	P/S	Percent Rank
MSCI EAFE	17.0x	51%	16.5x	84%	10.6x	83%	1.6x	98%
MSCI United Kingdom	14.1x	43%	14.0x	63%	8.7x	43%	1.5x	86%
MSCI Japan	18.2x	54%	17.8x	70%	10.5x	82%	1.3x	100%
MSCI Europe	17.0x	45%	16.5x	83%	10.9x	83%	1.7x	95%
MSCI EM	15.4x	67%	15.0x	91%	10.9x	92%	1.7x	83%
MSCI China	14.6x	62%	14.2x	73%	12.7x	84%	1.5x	53%
MSCI India	25.4x	85%	24.7x	87%	18.8x	90%	2.7x	86%
MSCI Taiwan	18.8x	59%	19.7x	89%	12.8x	74%	2.0x	77%
MSCI Korea	12.4x	59%	11.5x	65%	6.6x	59%	1.0x	94%

Fundamentals								
	Dividend Yield	Percent Rank	Profit Margin	Percent Rank	ROE	Percent Rank	Net Debt / EBITDA	Percent Rank
MSCI EAFE	3.0%	48%	10.1%	97%	11.1%	74%	1.7	12%
MSCI United Kingdom	3.4%	41%	10.9%	86%	10.4%	35%	1.2	19%
MSCI Japan	2.1%	73%	7.7%	99%	9.6%	91%	-1.2	9%
MSCI Europe	3.1%	53%	10.4%	99%	12.4%	73%	3.0	6%
MSCI EM	2.5%	46%	11.3%	92%	12.9%	65%	2.0	76%
MSCI China	2.1%	31%	11.0%	50%	11.9%	39%	3.2	98%
MSCI India	1.3%	27%	11.4%	63%	14.9%	38%	2.3	39%
MSCI Taiwan	2.5%	34%	10.8%	87%	17.8%	95%	0.1	4%
MSCI Korea	1.9%	62%	8.5%	94%	9.0%	47%	2.7	44%

For Index Definitions see: [TouchstoneInvestments.com/insights/investment-terms-and-index-definitions](https://touchstoneinvestments.com/insights/investment-terms-and-index-definitions)

*Local currency earnings estimates are not available for broad indexes with a mix of currencies.

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



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 Tim Paulin, CFA – Senior Vice President, Investment Research and Product Management, 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.

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