

May 3, 2019

Dear clients and colleagues,

Recently, Global Alpha spent a day meeting several small cap Austrian companies. The reasons for investing in Austria are plentiful. First of all, as an industrial nation with strong purchasing power, it is among the world's richest countries. Austria is the fourth-wealthiest country in the EU with a GDP per capita of over \$51,000. In 2018, the Austrian economy grew faster than the Euro area, with GDP growth of 2.7% compared to 1.9%.

Austria benefits from a high level of stability, both politically and socially, which means there are virtually no labour strikes by its highly educated workforce. The country has a dual training education system. Upon completion of the compulsory schooling period, 40% of young people train in an apprenticeship occupation while another 40% choose higher education in a vocational education and training school or college. This leads to one of the lowest youth unemployment rates in Europe.

Austria is an innovative country, as exemplified by its significant investment in R&D – the second highest in Europe after Sweden. Over 3% of GDP is invested in R&D. Almost half of R&D investment comes from the private sector, the public sector accounts for around one-third and the balance comes from abroad and the private non-profit sector. The Austrian government is helping to make the country an internationally competitive business location by offering a 14% R&D credit as well as other attractive group taxation schemes.

Exports are essential to the Austrian economy, with the key export commodities being machinery and equipment. Most exports go to other European countries, with Germany the largest destination. However, the country's reliance on Germany is diminishing. In 1992 40% of Austrian exports went to Germany compared to 30% today. Around 15% of exports go outside the EU, and the US is Austria's second largest trading partner.

One of the reasons the Austrian economy has recently outperformed Germany is the diversification of its exports. In addition, Austria is more exposed to Central and Eastern Europe (CEE) – the growth area of Europe. Last year CEE economic growth was 4.3%, and it is forecast to grow 3.5% in 2019. International companies view Austria as an ideal location to coordinate their CEE operations as they benefit from the Austrian stability while being exposed to the most dynamic region.

As well as attending the conference to generate new investment ideas, we took the opportunity to get an update from one of our current Austrian portfolio holdings.

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Palfinger is a leading global hydraulic lifting, loading and handling system manufacturer. The Company enjoys diversified industry exposure to both cyclical and non-cyclical sectors, which has enabled it to achieve consistent growth at good margins. Palfinger wants to remain as the leader in lifting solutions, defending its number one position in loader cranes as well as forestry and recycling cranes. Palfinger is also entering new markets such as truck-mounted forklifts and crawler cranes. The company has undergone some restructuring in order to improve its competitive position. Restructuring of its North American operations was completed last year, and the Maritime business will be completed this year. The parts and services segment should grow as a percentage of sales, potentially providing upside in operating margins.

Another Austrian holding in the portfolio that exhibits the quality of innovation solutions is Schoeller-Bleckmann, an equipment supplier to the oil and gas industry. SBO makes downhole tools and equipment for directional drilling and well-completion applications. The company is the global leader in the manufacture of non-magnetic steel collars. Rig count trends in North America should mean its operations in the region are at least stable in 2019, while international operations are expected to continue to grow as well.

In Austria you can find global market leaders within industrial niches, such as Schoeller-Bleckmann and Palfinger, and we believe Austrian stocks merit a place in any well-diversified portfolio.

Have a good weekend.

The Global Alpha Team

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