

January 23, 2015

Dear clients and colleagues,

Similar to how 2014 ended, European markets continue to be influenced by geopolitical factors (Russia, Greece, terrorist attacks in France). Once again, macroeconomic headlines and central bank policy will dictate market directions for 2015.

We recently had a chance to meet with over 30 European companies at conferences in France and Switzerland. Here are some of our observations from the meetings.

Eurozone

Overall, companies confirmed that they are operating in a relatively unchanged business climate from 2014. Management teams, neither expect a sudden weakening nor a strong acceleration of business. In order to boost revenues, several European companies expect to ramp up their external growth plans. For the vast majority of businesses, growth momentum will remain outside of Europe in regions such as Asia and the United States. From a country perspective, a lack of competitiveness and fiscal pressure should continue to drag down confidence in France, while the political outlook in both Italy and Greece remains uncertain.

European M&A seems to have recovered despite the economic difficulties in the Eurozone. Thanks to a low interest rate environment, M&A financing and debt refinancing will become even cheaper.

Stoxx 600 forward 1 year EPS growth				
	2012	2013	2014	2015
Consensus	9.7%	11.5%	14%	11%
Actual	-4.5%	-2.6%	3%	?

On the earnings side, after a handful of years hampered by EPS disappointment, 2015 could be a positive surprise

for the markets. Firstly, the negative currency headwinds seen throughout 2014 are about to reverse course. For many euro-reporting companies, a weaker euro will have a favorable impact on revenues and EBIT figures compared to last year. Additionally, companies will benefit from lower input costs, such as raw materials and energy costs, driving financial results. Finally, the drop in inflation and interest rates could stimulate consumption and trigger a positive volume effect.

Switzerland

The unexpected end of the EUR/CHF currency peg by the Swiss National Bank was a major topic of discussion with the companies we met. Most of the management teams seemed relatively calm about the rapid strengthening of the Swiss franc, admitting that nothing could be done in the very short term.

This report is provided solely for informational purposes and nothing in this document constitutes an offer or a solicitation of an offer to purchase any security. This report has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient and does not constitute a representation that any investment strategy is suitable or appropriate to a recipient's individual circumstances. Global Alpha Capital Management Ltd. (Global Alpha) in no case directly or implicitly guarantees the future value of securities mentioned in this document. The opinions expressed herein are based on Global Alpha's analysis as at the date of this report, and any opinions, projections or estimates may be changed without notice. Global Alpha, its affiliates, directors, officers and employees may buy, sell or hold a position in securities of a company(ies) mentioned herein. The particulars contained herein were obtained from sources, which Global believes to be reliable but Global Alpha makes no representation or warranty as to the completeness or accuracy of the information contained herein and accepts no responsibility or liability for loss or damage arising from the receipt or use of this document or its contents.

Performance figures are stated in Canadian dollars and are net of trading costs and gross of operating expenses and management fees. Further information about the Global Small Cap Composite is available by contacting the firm. Global Alpha Capital Management Ltd. (Global Alpha) claims compliance with the Global Investment Performance Standards (GIPS[®]) and has prepared and presented this report in compliance with the GIPS. Global Alpha has not been independently verified.



Many companies have taken strategic actions over the years to address their business segments exposed to the Swiss franc. By focusing on profitable niche markets that require advanced engineering processes, these companies have managed to reduce the cyclical nature of their businesses over time. Despite a challenging environment, we believe the combination of Switzerland's strong technological know-how and above-average productivity should allow for continued efficiency gains and product innovation.

Several Swiss companies have a natural hedge in place, where revenues and costs are matched in the same local currencies. Nonetheless, Swiss franc-reporting companies will suffer from a translation impact. We believe that the negative impact on earnings expectations has been compensated for largely by corrections in stock prices since the Swiss National Bank's announcement.

On average, our Swiss holdings have returned -14% in franc terms since last Wednesday. On the other hand, the strengthening of the franc, which has surged 22% and 15% against the Loonie and U.S. dollar respectively, resulted in a slight net positive for Canadian and U.S. investors exposed to our funds.

The weaker earnings growth expectations for Swiss equities could trigger a capital reallocation into the Eurozone or other regions. Swiss companies with significant domestic costs and high foreign revenues are likely to continue to suffer. Other Swiss businesses will look to efficiency-improving programs as they navigate the new environment.

Aside from the focus on the franc while we were in Europe, the Swiss companies we met remain committed to return cash to their shareholders. These companies maintain a prudent cash management approach. Firms also noted that the strengthening of the franc could encourage M&A activity in Switzerland to intensify.

Have a good weekend.

The Global Alpha Team

This report is provided solely for informational purposes and nothing in this document constitutes an offer or a solicitation of an offer to purchase any security. This report has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient and does not constitute a representation that any investment strategy is suitable or appropriate to a recipient's individual circumstances. Global Alpha Capital Management Ltd. (Global Alpha) in no case directly or implicitly guarantees the future value of securities mentioned in this document. The opinions expressed herein are based on Global Alpha's analysis as at the date of this report, and any opinions, projections or estimates may be changed without notice. Global Alpha, its affiliates, directors, officers and employees may buy, sell or hold a position in securities of a company(ies) mentioned herein. The particulars contained herein were obtained from sources, which Global Alpha believes to be reliable but Global Alpha makes no representation or warranty as to the completeness or accuracy of the information contained herein and accepts no responsibility or liability for loss or damage arising from the receipt or use of this document or its contents.

Performance figures are stated in Canadian dollars and are net of trading costs and gross of operating expenses and management fees. Further information about the Global Small Cap Composite is available by contacting the firm. Global Alpha Capital Management Ltd. (Global Alpha) claims compliance with the Global Investment Performance Standards (GIPS[®]) and has prepared and presented this report in compliance with the GIPS. Global Alpha has not been independently verified.