

AllianceBernstein

Global Growth Trends Portfolio

Market Overview

Global markets were down during the month of January, as the market took a pause after a strong 2009 rally. Markets became more skittish as the focus turned to the beginning of interest rate-tightening measures in China and sovereign debt issues in countries such as Greece. For the month, the MSCI World Index fell 4.1% in US dollar terms.

Concerns about economic stability in Greece led to a fresh bout of US dollar strength relative to most major currencies, including the euro and sterling. The yen continued to appreciate relative to the dollar as the Bank of Japan held policy rates at 0.1%.

Most sectors in the MSCI World Index moved lower, with materials and telecommunications retreating most. The health care and consumer staples sectors fared best.

Portfolio Commentary

Security selection detracted from returns, while sector selection was neutral.

Financial stocks reacted negatively to news flow regarding the Volcker Rule proposal, which had a strong impact on some of the capital market-exposed stocks. We also saw some pullback in Asian stocks due to moves by the Chinese government to limit the rate of growth of lending in China. Detractors in the finance sector for the month included ICBC and Goldman Sachs. Several of our energy holdings also detracted from performance this month, including China Coal Energy.

Top contributors to returns included several health care companies, including Gilead, Covidien and Merck. Gilead shares moved higher after reporting robust fourth-quarter results that exceeded estimates on both the top and bottom lines. The company also issued solid 2010 guidance that was above expectations, driven by higher product sales and lower expenses. Covidien reported strong fiscal first-quarter 2010 results that exceeded sales and earnings expectations. The company also raised its annual guidance for fiscal 2010.

Portfolio Positioning and Outlook

Consumer. We continue to be neutral weight in the portfolio with an overweight in discretionary names relative to staples names. We have been adding to higher quality, more stable names as we believe we are heading toward a market that will begin rewarding fundamentally driven companies with solid earnings and cash flow stories.

Health Care. Health care stocks were down slightly in January, but outperformed the overall market. Trading in the portfolio was modest during the month, as we built up certain positions and reduced others mostly related to earnings results and stock movements. Most notably, we completed our exit of Celgene, as major data in December on the company's key drug Revlimid failed to dispel ongoing concerns around growth. We also slightly reduced our position in Amgen after disappointing fourth-quarter results. Finally, we took some profits on Covidien and Merck after strong performance and we added to positions in Medco, Roche and Shire.

Over the long term, health care industries and stocks with consistent stable growth and solid fundamentals tend to demonstrate relative strength. We would continue to favor stocks that exhibit such criteria, particularly those that we believe will exceed consensus expectations. The portfolio is overweight biotech, slightly overweight medical services and medical products, and underweight pharmaceuticals.

Technology. Global technology and telecommunications were among the worst sectors in the market in what was a rocky start to the new year. Broadly positive fundamental results did not support stock performance during the January reporting period, as renewed talk of financial services regulation, concerns about sovereign debt risk in Europe, and sector-specific worries regarding inventory building and recovery momentum peaking all hit market sentiment. The sector sleeve underperformed significantly during the month, on poor industry allocation and stock selection. In particular, an underweight position in Japanese electronics and durables stocks hurt relative performance.

While we reduced sector allocation slightly this month through a reallocation to the industrials sector sleeve, technology remains the largest active sector bet within the combined Portfolio. We are encouraged by the fundamental improvement seen across the sector. While it is true that many technology companies are currently reporting peak profit margins, a cause of concern for those investors looking for peaking momentum, we expect those margins to be sustainable given the decade-long management efforts to lower manufacturing costs (largely through moving production and component sourcing to Asia), manage capacity and control discretionary costs. The facts remain that technology companies exited the year with still-lean inventories, firm pricing and supply constraints, all of which we believe will be further underscored by consumer demand for Chinese New Year and the enterprise recovery trends we have seen spread from servers and storage into software and services. We find the broad fundamental trends encouraging.

Financial. During the month we reduced the capital market exposure due to the lack of clarity in US regulation and reduced positions in Goldman Sachs, Credit Suisse and JP Morgan. Conversely we initiated a position in Wells Fargo where we consider the regulatory risk to be lower while offering exposure to the stabilization in the US credit cycle.

The sector sleeve continues to be positioned in strong secular growth companies that we consider to be long-term winners in their respective industries as we see continued bifurcation between strong and weak players. We have positioned the sleeve to take advantage of stronger equity markets in the near term but have reduced the exposure to capital markets due to regulatory concerns. We continue to avoid institutions with weaker capital bases that may be vulnerable to increased regulatory requirements. We continue to be overweight emerging markets, particularly in non-Japan Asia where we see stronger secular levels of growth.

Energy and Natural Resources. The key driver of commodity prices over the past quarter appears to have been US dollar weakness. Commodities broadly are inversely correlated to the US dollar and this trend has held as the dollar has weakened relative to a basket of its key trading partners' currencies. Our positioning remains resilient as we continue to favor equities exposed to commodities with sound supply/demand fundamentals such as copper and iron ore. Sustainability of price moves remains key as the US and Europe show early sustained signs of emerging from their respective recessionary environments.

Infrastructure. We have modestly narrowed the infrastructure underweight in the portfolio and are still underweight utilities. We are continuing to focus on finding individual names that have best positioned themselves for secular and cyclical growth as the economy begins to recover. The sleeve is still a mix between early/shorter-cycle names that will see economic improvement sooner (transports, short-cycle machinery and autos) and later-cycle companies with stronger secular stories (alternative energy, commodity-focused trading, and machinery companies and diversified industrials with strong energy efficiency and emerging-markets platforms). However, we continue to move the emphasis back toward the later-cycle names, as we see more potential for positive earnings surprises from some of these names. In aggregate, our biggest active weight sectors are in machinery, electrical equipment, automotive and trading companies. Our underweight sectors outside of utilities are mainly concentrated in commercial services, road and rail, and construction and engineering sectors.

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