

AllianceBernstein

Global Thematic Research Portfolio

Market Overview

The world's equity markets bore the brunt of a sharp rise in risk aversion during May, reflecting apprehension about sovereign debt risks in Europe, regulatory uncertainties and moderating growth expectations in China. The MSCI World Index fell 9.58% in US dollar terms.

The month started on a positive note after Greece reached a deal with the European Union (EU) and International Monetary Fund (IMF) for a financial rescue package. But performance declined following weak Chinese manufacturing and US employment data, Moody's warning of a possible ratings downgrade for Portugal, and concerns around Greek crisis contagion effects in the euro area.

The EU attempted to placate investors' concerns by announcing a €750 billion package of loan guarantees and credits and the European Central Bank announced it would buy government and private debt. However, markets fell due to growing uncertainty about the situation in Europe as governments around the area proposed new plans to reduce their deficits. Escalating tensions between North and South Korea, disappointing earnings data from a number of US companies as well as weaker than expected German confidence, Japanese GDP, and US jobless claims also weighed on the market.

Consistent with the pervasive anxiety all sectors finished in negative territory, with the telecom and utilities sectors holding up relatively better. Energy and information technology stocks suffered most.

The US dollar was stronger relative to most currencies, amid the European debt crisis and as investors turned more risk averse. The exception was the yen which gained relative to the US dollar.

Portfolio Commentary

Security selection within the information technology and consumer discretionary sectors contributed to performance during the month. Sector selection was negative due to our underweight positions in the defensive consumer staples, telecom and utilities sectors.

Within the information technology sector, virtualization software solutions firm VMWare advanced amid robust business momentum, driven by the proliferation of cloud

computing. Among consumer discretionary holdings, online movie rental service Netflix added to relative returns. The company continued to benefit from strong subscriber growth, driven by expanding data streaming options and the closure of brick-and-mortar competitors. Analysts have also upgraded the stock based on the addition of the Apple iPad to the base of Netflix-enabled devices. Positive quarterly results lifted shares of Chinese hotel accommodations and airline ticket broker Ctrip.com. Management cited growing corporate travel accounts, greater market share of leisure travel business and expanding hotel inventory control.

Industrials and consumer staples holdings weighed on performance in May. Lithium-ion battery manufacturer A123 Systems fell after a competitor's investor roadshow suggested a deteriorating relationship between A123 Systems and Chrysler/Fiat. We added to our position in the company, based on our research and confirmation from company management that the competitor statements were misleading.

Several energy and materials stocks also detracted during the month. Concerns about a halt in US deep water drilling in the Gulf of Mexico dragged down oil services Schlumberger. While 75% of the company's backlog is deepwater projects, US deepwater exposure constitutes only about 10% of the backlog. According to our research, Schlumberger should have the flexibility to deploy assets to locations unaffected by increased regulation. In the materials sector, agricultural products company Monsanto retreated following ongoing worries about a global oversupply in the glyphosate (weed killer) market. Management indicated it will change its pricing strategy to compete better with generic products. Another detractor was Greenhill. The merger and acquisition (M&A) advisory firm reported lower quarterly figures driven by decreased advisory revenue and less flexibility in management compensation expenses. We believe the M&A cycle remains in its early stages.

Outlook

Uncertainty has returned to the markets on the back of the Greek debt crisis. Although we remain vigilant for signs that underlying conditions have begun to worsen once again, most evidence suggests that the global economic recovery is on a solid footing. Global

Purchasing Managers' Indices point to a robust manufacturing rebound, as well as employment losses in the US and much of the developing world have stabilized. Against this background, we continue to believe the economic recovery in 2010 will likely be stronger than current consensus appreciates, led by massive inventory restocking, emerging market consumption, industrial investment and global reflation.

In our view, one of the main risks going forward is that inflation will exceed expectations, and have barbelled the portfolio to include both some of our higher price to earnings (PE), higher growth thematic stocks, with lower PE inflation hedges in the energy and commodity space.

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