

AllianceBernstein

## Global Conservative Portfolio

### Market Overview

During November, both global equities and global bonds advanced. The fixed-income market, as measured by the Barclays Capital Aggregate index, continued its positive trend in November, returning 1.29%, while equities, measured by the MSCI World Index, rose 4.1%.

In a turnaround, US Treasuries led the rally, followed by mortgages with an excess return of 0.40%. Spreads were flat or slightly wider for other sectors. The agency mortgage-backed security (MBS) sector benefited from the purchasing support of the Federal Reserve. The Fed's purchase program crossed the US\$1 trillion level in November and will continue toward the US\$1.25 trillion target by March 2010; the level of purchasing has easily outpaced the net issuance in the sector. In addition, prepayments have been subdued, resulting in more predictable yields and cash flows for MBS. This added to the attractiveness of the MBS yield advantage. After seven months of positive excess returns, investment-grade corporates underperformed US Treasuries, posting an excess return of -0.08%.

The US economy continued to show signs of recovery, with positive news from manufacturing, employment, housing and consumer confidence data. Manufacturing activity continued to rebound with the Institute of Supply Management's business barometer increasing to 56.1 in November; the highest level since August 2008. This indicates accelerated business activity and rising sales, which should continue to support the economic recovery in 2010.

### Portfolio Commentary

The short duration portfolio generally matched its benchmark for the month. Exposure to commercial mortgage-backed securities, asset-backed securities, investment-grade corporates and agency MBS were modest positives, offset by non-agency securities. During the month we generally maintained our spread product exposure given attractive valuations. The sleeve's duration exposure was underweight to the benchmark.

Both European and US corporate credit spreads were much quieter throughout November following the high magnitude of spread tightening witnessed in the previous few months. We still had positive

performance from our overweight positioning in investment-grade corporate credits; however, our overweight to non-investment grade credits was a mild detractor. Risk appetite was somewhat hampered, especially toward the end of the month, following the debt problems in Dubai. Our overweight to commercial mortgage-backed securities was one of the main detractors for performance as investors were cautious in their stock selection.

We continue to remain overweight the Australian dollar, which posted the strongest returns for the Portfolio within the currency selection sector. Australia continues to weather the global economic downturn well and raised its interest rates yet again at the end of November, making it the third hike in a row. Our overweight in the Hungarian forint and Brazilian real were only modest contributors.

We remain overweight the US in our country- and yield-curve positioning, which was the main contributor to the outperformance in this area. We continue to be overweight Europe and Canada, which was also beneficial to returns.

Pharmaceutical company Merck was a top contributor to equity returns, following the close of its acquisition of rival Schering-Plough and its confirmation of financial targets for the combined company. Relative performance was also helped by our position in Sprint, which paid off US\$1 billion in debt and benefited from optimism about the company's ability to improve subscriber losses. Home improvement company Lowe's also contributed.

Among individual detractors, Credit Suisse pulled back on profit taking. Automaker BMW reported disappointing third-quarter results as losses continued to mount in its automotive business, although volumes were aided by aggressive price cutting. A broad pullback in the Japanese market hurt automaker Nissan. Japanese stocks moved lower due to ongoing yen appreciation, a spurt of equity raises and concerns about the financial difficulties of Japan Airlines and potential credit losses.

## Outlook

We think the medium-term outlook for company earnings is improving. We continue to take advantage of attractive valuations across a wide range of sectors while continuing to invest in companies with strong balance sheets and clearer earnings visibility. With the economy and banking system on firmer footing, we continue to increase the value portfolio's exposure to economically sensitive companies that look undervalued relative to their earnings power under more normal business conditions. Our research has also identified stocks that currently offer a rare combination of attractive valuations and resilient cash flows.

In the growth portfolio, we shifted assets from the technology sleeve to the health care sleeve during November, sourcing half from telecommunications holdings and half from technology. The move reflected a rebalancing of assets after substantial outperformance by technology this year and significant underperformance in health care. Our expectation is that health care stocks will see a positive sentiment shift as the US Congress passes health care reform legislation in the coming months.

After the moves, technology remains the largest active sector bet within the growth portfolio, reflecting our expectation that technology will remain a leadership sector in a global economic recovery.

We expect emerging-market economies to continue to lead the recovery in 2010. Overall, we expect global economic growth of 3.4%, just short of its long-term average. We see US economic growth of 3.5%—higher

than the consensus expects, but lower than most recoveries from prior deep recessions.

Nevertheless, significant risks and challenges persist for the global economy and financial markets. Many investors worry about how governments around the world will wind down their massive fiscal and monetary stimulus programs as their economies recover. Will they have the discipline to tighten monetary policy and reign in ballooning fiscal deficits? If not, inflation could surge. In our view, these risks bear close monitoring, but do not pose an economic threat this year or next.

The upside of continued anxiety about the economic outlook is that attractive opportunities remain for active managers to add value. We see opportunities for fixed-income managers to take advantage of the sizable return potential in the credit sector.

We have adopted an underweight exposure to mortgage pass-through securities, instead preferring US commercial mortgage-backed securities. The portfolio is invested with a neutral in terms of interest-rate exposure. We have our biggest overweight exposure in Europe. We remain underweight the UK and Japan and overweight US. We continue to be largely overweight investment-grade corporate credits.

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