

Winter 2009

CAPITAL MARKETS OUTLOOK

A New Landscape Creates Opportunity

As capital markets wrapped up an impressive year, the economic recovery gathered momentum...and began to take on a different character.

A Strong Year

In retrospect, 2009 will be recorded in the history books as a remarkable year. In the span of 12 months, the stock market experienced both the depths of the credit-crisis-driven decline and the relief of a surprisingly strong—though still incomplete—recovery.

The S&P 500 Index returned 26% for the calendar year, its best showing since 2003. Investors who had the fortitude to maintain their long-term strategies were able to regain a sizable portion of what they'd lost in the downturn, although they had to endure a nerve-testing ride along the way. While full recovery is yet to come, 2009 ended up as a very good year.

New Economic Patterns Emerge

As the economic recovery continues, it's likely to take on a different shape than past recoveries. The tides of the world's economy have changed: Sizable government stimulus packages are bolstering the early stages of the rebound, consumption is becoming more global and a weak dollar is rebalancing capital flows and trade.

As these new patterns unfold, the opportunities and risks confronting investors are changing. While some companies and industries will navigate a path to greater success, others will struggle. This uncertainty creates misvaluations that can be exploited. Strong research, effective security selection and a global perspective will define investment success—particularly in this ever-changing landscape.

Despite a rough start to 2009, the markets had a strong year

Major Index Returns (in USD)
As of December 31, 2009

Equities	Q4	2009
Emerging Markets	8.5% ▲	78.5%
US	6.0% ▲	26.5%
EAFE	2.2% ▲	31.8%

Credit

Global High Yield	5.2% ▲	57.7%
CMBS	3.3% ▲	28.5%
EM Debt	2.4% ▲	34.2%
Global Corp.	1.5% ▲	16.6%

Government Bonds

Japan	0.6% ▲	1.4%
Euro	-0.1% ▼	4.1%
US	-1.3% ▼	-3.6%

Past performance does not guarantee future results. Individuals cannot invest directly in an index. Please see back cover for index definitions. Source: Barclays Capital, FactSet, Morgan Stanley Capital International (MSCI), Standard & Poor's and AllianceBernstein

There is no guarantee that any forecasts or opinions in this material will be realized. Information should not be construed as investment advice.

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What a Difference a Year Makes

As 2009 began, governments around the world were working furiously to stave off financial disaster and an economic free fall. Now, recovery is under way, although it will be a different kind of recovery.

Mounting Signs of Progress

Evidence continues to accumulate that the world is rebounding from a widespread recession. The global economy likely shrank by 2.3% in 2009; in 2010, we expect it to expand by 3.5%, which would represent its best calendar-year showing since before the crisis.¹

The chances of recovery have been improved by a rapid rebound in global manufacturing, which could eventually lead businesses to begin hiring again. New jobless claims have fallen, and leaner companies are increasingly tapping temporary workers to help meet demand—a positive development for eventual full-time job creation.

The US unemployment rate, which surpassed 10% late in 2009, proceeded to register a slight—but welcome—decline. Other labor markets are improving, too: For example, Brazil's unemployment rate fell for a third straight month to 7.4%.² Consumers and businesses around the world are feeling more confident, and banks are growing less wary of lending to individuals.

Some investors fear a relapse as government stimulus has run its course, but the reality is that much spending still remains on tap. Almost two-thirds of the \$787 billion US fiscal stimulus is yet to be disbursed. In China, roughly half of the government's fiscal relief is still on the way—funds for building railways and low-income housing, improving rural infrastructure and tackling a host of other initiatives.³

Interest rates in many major economies remain extraordinarily low, as central banks encourage economic activity. Keeping rates low reduces mortgage rates and other borrowing costs for consumers and businesses. It can also entice bank lending, by enabling banks to borrow cheaply while lending and investing at a higher rate. And it combats risk-averse behavior by making safer, lower-yielding investments relatively less attractive.

Embracing a New Recovery

Massive stimulus efforts are creating a new pattern for this recovery, and so is global consumption. US and other developed market consumers have traditionally led the way back from economic downturns, but the role of emerging market consumers is growing. In the 1990s, emerging markets accounted for 22% of the world's consumption growth. Since 2006, that share has doubled to nearly half and is well-balanced among diverse regions including Asia, Eastern Europe and Latin America.

The landscape is changing in other ways, too. A weak US dollar combined with greater productivity is rebalancing global trade and capital flows, making US exports more attractive in other economies. It's also encouraging some foreign companies to build factories and facilities in the US. Innovations and technological advancements will make some industries obsolete while sowing the seeds for new sectors. Some companies will emerge as leaders while others falter, and a different combination of winners and losers creates an evolving opportunity set for disciplined investors.

Investors should view the new course of recovery as a source of investment potential.

¹AllianceBernstein forecasts as of January 4, 2010. Forecasts may not be achieved.

²Most recent data through November 2009. Source: Haver Analytics

³As of December 31, 2009. Source: CEIC Data, Congressional Budget Office, Recovery Accountability and Transparency Board, US federal agency financial and activity reports and AllianceBernstein

The Big Debate: Exit Strategies

As the recovery progresses, debate intensifies on exit strategies for fiscal and monetary stimulus: How will governments and central banks “unwind” these unprecedented policies?

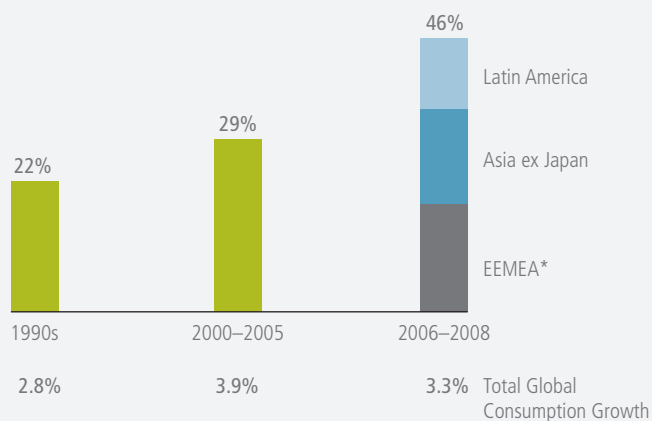
Sizable budget deficits will eventually have to be addressed, and many investors fear governments lack the will to deal with the problem. However, by gradually introducing tax hikes and spending cuts, governments have successfully tackled large deficits in the past without undermining economic growth. And growth itself can help shrink the gap by boosting government tax revenues.

There’s also concern about the future path of interest rates. Short-term rates are being held very low to encourage the flow of capital. As economic activity rises, rates will have to increase to guard against an overheating economy. Some worry that waiting too long to raise rates could cause inflation to spiral out of control; others fear that raising them too far or too fast will choke off recovery. But even if rates climb materially from historic lows—and we believe they will—such an interest-rate environment should still support economic activity.

Other risks are present. Borrowing and lending activity remains subdued, robbing the recovery of needed momentum. Geopolitical flare-ups and stronger global demand could cause oil prices to surge, making it more costly for firms to do business. As we move forward, we’re closely monitoring these developments.

Global consumption is more balanced today than many investors realize

Contribution of Emerging Markets to Consumption Growth



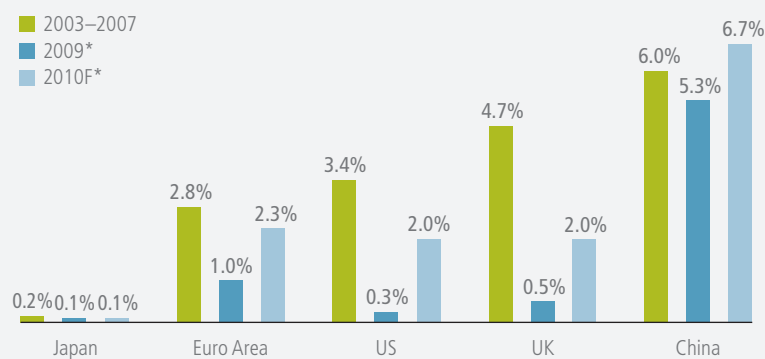
Historical analysis does not guarantee future results.

*EEMEA represents Eastern Europe, Middle East and Africa

Source: Haver Analytics, International Financial Statistics, World Bank and AllianceBernstein

How far and how fast will interest rates rise?

Official Interest Rates



Historical analysis and current forecasts do not guarantee future results.

As of December 31, 2009

*2009 at year-end; 2010 forecasts are AllianceBernstein’s

Source: Bloomberg and AllianceBernstein

Improved Revenues: The Missing Piece?

As stock markets regain lost ground, investors look for a revival in revenue growth as the fuel for further gains.

A Broad-Based Market Rally

The broad market upturn that began in early March carried many categories of equity investments along with it. Large-cap and small-cap stocks, growth and value styles, US and international: Each of these segments benefited as the economic recovery began to materialize and investors took a more balanced view of risk and return.

Surprisingly strong earnings played a big part in this revival. Record numbers of companies exceeded analysts' earnings expectations in both the second and third quarters, driving price gains.⁴ But there's been an undercurrent of doubt in this stellar earnings performance. To this point, earnings surprises have largely been attributed to a deep round of corporate cost-cutting.

Revenue Growth Could Be the Next Catalyst

Now, markets are waiting eagerly for a rejuvenation in demand that will drive revenue growth. But where will those revenues come from?

One important source is likely to be renewed capital spending in many industries. As the economy turned downward, companies tightened their purse strings. They curtailed spending and capital investments, holding off on buying new computers and vehicles, and delaying or forgoing a host of other long-term capital outlays.

Companies also slashed inventories, cut costs and reduced payrolls—allowing these leaner businesses to accumulate more cash. As a percentage of companies' market capitalization, cash climbed to levels not seen in more than 20 years.

It's highly unlikely that this situation will remain. Business equipment can't last forever—vehicles break down and office computers must eventually be upgraded. Opportunities will arise—and firms will require cash to seize them. As companies begin to open the tap on spending, it will translate into new sources of revenue for the economy.

Households in developed economies like the US and UK have also been spending less, as they focus on reducing their debt burden. However, the progress they're making frees up additional cash. Consumers, too, will eventually need to replace cars, appliances and other big-ticket items, boding well for renewed strength in household spending in 2010.

One important source of revenues will be renewed capital spending in many industries.

⁴As of November 30, 2009. Source: Brown Brothers Harriman, FactSet, Standard & Poor's, Thomson Reuters and AllianceBernstein

Improving Profits Could Bolster Stock Valuations

With companies operating in much leaner fashion today, increased revenue from even modestly higher demand for goods and services could drive meaningful improvements in profit margins.

As this occurs, profitability, which is currently at a cyclical low point, should begin to rise. The market expects global profits to rise by 29% in 2010 and 21% in 2011 as earnings work their way back toward their long-term trend.⁵ As investors begin to compare stock prices to this future earnings potential, stocks will seem like a more attractive proposition.

But a rising tide won't lift every boat. Companies with stronger fundamentals, more innovative technologies or better strategies will capitalize on a changed economic landscape and move to the forefront. To successfully identify these firms, investors will have to be more selective, with diligent research pointing the way to the opportunities of tomorrow.

Cash levels are very high, despite slow sales growth

Cash as % of Market Cap*
1960–October 2009



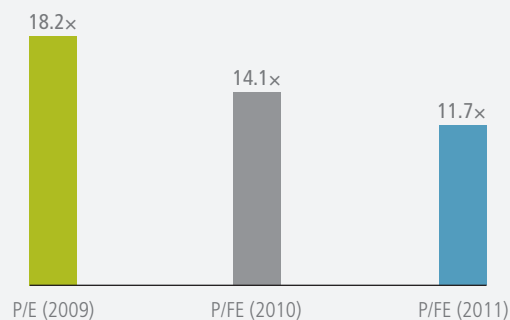
Historical analysis does not guarantee future results.

*US large-capitalization stocks excluding financials and utilities

Source: Corporate reports, Empirical Research Partners analysis, Sanford C. Bernstein and AllianceBernstein

If earnings improve as expected, stocks should grow more attractive

Price to Earnings: 2009, 2010, 2011



Current and future estimates do not guarantee future results.

As of December 31, 2009

Price to forward earnings measures a company's current stock price divided by earnings estimates. It is used to compare current earnings to estimated future earnings. If earnings are expected to grow in the future, the forward P/E will be lower than the current P/E.

Source: FactSet, MSCI, Thomson I/B/E/S and AllianceBernstein

⁵Consensus estimates as of December 31, 2009.
Source: Thomson I/B/E/S

Municipal Bonds May Be Safer Than You Think

Bond investors have been bombarded by media reports on the weakened financial condition of state and local governments. However, our research indicates that the municipal bond market won't collapse under the weight of budget shortfalls.

These are clearly difficult financial times for state and local governments. They depend on economically sensitive tax revenues like personal income, sales, and corporate income taxes. These revenues decline during national recessions and grow in times of plenty. But during each downturn, governments have ultimately responded with balanced budgets—either by increasing taxes or cutting costs.

Experience suggests the vast majority will respond to current fiscal pressures in a prudent way and on a timely basis. This is a big reason why we don't expect a significant increase in municipal bond defaults.

There's also a wide variety of municipal bonds backed by other, more stable revenues from essential services like water systems and electric utilities. These bonds provide insulation against current economic conditions, and offer valuable diversification.

Research and Selectivity Will Be Critical in Taxable Bonds

Taxable bonds have posted extraordinary returns since mid-March, when capital markets were stumbling and only the safest investments were in favor. Investors were so leery of risk that they demanded a substantial amount of extra yield to choose any bond sector that exposed them to credit risk.

As this high anxiety began to ebb, nongovernment bonds flourished:

For the full year, emerging-market bonds returned 34%, high-yield bonds 58% and investment-grade corporate bonds 17%.⁶

Going forward, opportunities in these sectors will have to be realized more selectively, by applying research and careful security selection to identify the countries, sectors and companies that offer the greatest relative potential.

Municipalities have been taking actions to balance budgets

State	Revenue Enhancements?	Expense Cuts?
California	✓	✓
Florida	✓	✓
Georgia		✓
Illinois		✓
Massachusetts	✓	✓
New Jersey	✓	✓
New York	✓	
Pennsylvania	✓	✓
Texas		✓
Virginia	✓	✓
Washington		✓

As of October 2009
Source: AllianceBernstein

⁶Past performance does not guarantee future results. Individuals cannot invest directly in an index. Please see back cover for index definitions. Source: Barclays Capital

The Value of Staying the Course

A bleak opening chapter in 2009 gave way to an extended stock rally that produced the best yearly return since 2003. It was powerful evidence that well-designed investment strategies can bounce back.

Once the details of 2009 have faded from memory, history will show it to be a strong calendar year for equity markets...and a stark contrast to the year that preceded it. One of the worst years ever for stocks was followed by one of the best—a potent reminder of how important it is to stay invested, even through very difficult times.

Many equity investors suffered steep losses in the extended downturn that started in October 2007, and they've yet to regain all the ground they lost. The market's 73% return from its bottom has allowed investors to recoup a little more than half of the wealth they lost in stocks. Investors who had faith in the market's ability to bounce back kept their money at work instead of abandoning their long-term strategy.

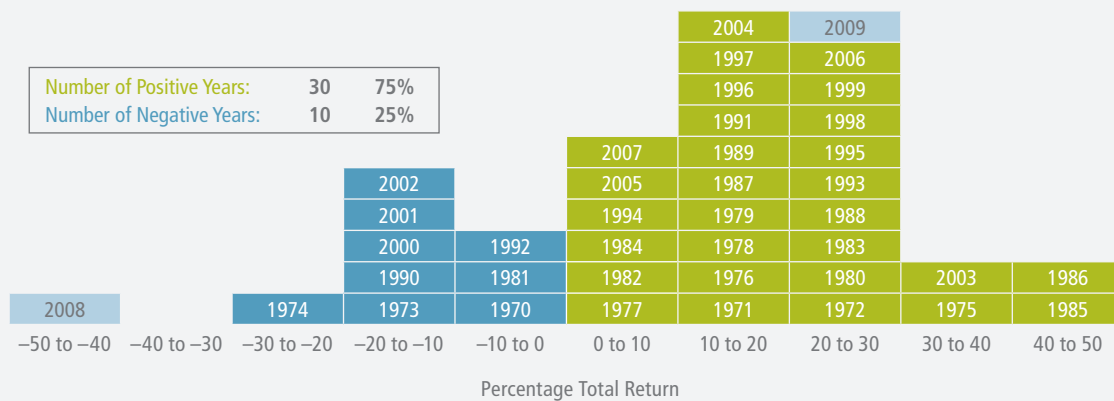
Those investors are better off today than they were 12 months ago.

Of course, the way forward won't be without plenty of twists and turns. While the long-term path of equity markets has been upward, the journey has often been interrupted by bear market declines—sometimes substantial ones. As long as stock markets exist, there will be exhilarating rallies and harrowing sell-offs.

That's why it's so important to work with a financial advisor. Design an investment strategy that's appropriate for your long-term financial goals. Consider your asset allocation carefully. And once you've set your strategy in motion, check in regularly to ensure that your portfolio still makes sense for you.

One of the world market's worst years—2008—was followed by one of its best

Annual Stock Market Returns—MSCI World Index



Past performance does not guarantee future results.

As of December 31, 2009

Individuals cannot invest directly in an index. Please see back cover for index definitions.

Source: FactSet and MSCI

Your investments are important to you—they're your means of reaching your financial goals and achieving better outcomes in life. At AllianceBernstein Investments, we're committed to putting our research to work for you:

- Exploring the opportunities and risks of the world's capital markets and the innovations that can reshape them
- Helping investors overcome their emotions and keep their portfolios on track

- Defining the importance of investment planning and portfolio construction in determining investment success

We've designed AllianceBernstein Research Insights as a foundation to help investors build better outcomes. Speak to your financial advisor to learn how we can help you reach your goals.

There is no guarantee that any forecasts or opinions in this material will be realized. Information should not be construed as investment advice.

Diversification does not guarantee a profit or protect against loss.

For the chart on page one, emerging market equities are represented by the MSCI Emerging Markets Index; non-US developed equities by the MSCI EAFE Index; and US equities by the S&P 500 Index. Global high yield is represented by the Barclays Capital Global High-Yield Index, US CMBS by the Barclays Capital Commercial Mortgage-Backed Securities (CMBS) Index, emerging market debt by the Barclays Capital US Dollar Emerging Markets Index and global corporate bonds by the Barclays Capital Global Corporate Bond Index. Euro, Japan and US government bonds are represented by the Barclays Capital Euro Treasury, Japan Treasury and US Treasury indices, respectively. Please see the index definitions below for further description.

Index Definitions: The **Standard & Poor's 500 Index** includes 500 US stocks and is a common measure of the performance of the overall US stock market. The **MSCI EAFE Index** (Europe, Australasia, Far East) is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the US and Canada. The **MSCI World Index** is a market capitalization-weighted index that measures the performance of stock markets in 23 countries. The **MSCI Emerging Markets Index** is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. It consists of 26 emerging market country indices. The **Barclays Capital US Dollar Emerging Markets Index** includes USD-denominated debt from emerging markets in the following regions: Americas, Europe, Middle East, Africa and Asia.

The **Barclays Capital Global High-Yield Index** provides a broad-based measure of the global high-yield fixed income markets. The **Global High-Yield Index** represents that union of the US High-Yield, Pan-European High-Yield, US Emerging Markets High-Yield, CMBS High-Yield and Pan-European Emerging Markets High-Yield Indices. The **Barclays Capital Commercial Mortgage-Backed Securities (CMBS) Index** tracks the performance of US dollar denominated commercial mortgage-backed securities publicly issued in the US domestic market. The **Barclays Capital Global Corporate Bond Index** tracks the performance of investment-grade corporate bonds publicly issued in the global market. The **Barclays Capital US Treasury Index** includes fixed-rate, local currency sovereign debt that makes up the US Treasury sector of the Global Aggregate Index. The **Barclays Capital Japan Treasury Index** includes fixed-rate, local currency sovereign debt that makes up the Japanese Treasury sector of the Global Aggregate Index. The **Barclays Capital Euro Treasury Index** includes fixed-rate, local currency sovereign debt that makes up the Euro Treasury sector of the Global Aggregate Index.

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