AllianceBernstein—

Asia Ex-Japan Equity Portfolio

Market Overview

Major developed country markets posted modest gains in January as European sovereign debt concerns eased a little and evidence emerged of a quickening US economic thaw. Sobering news came late in the month as unrest in Egypt raised concerns over political stability in a vitally important geo-strategic region.

Asian equities did not fare quite as well as global equities, with the MSCI Asia ex-Japan Index easing -1.0%. Country returns diverged significantly, with India falling hardest as it slid 13.1%, while Taiwan did best by rising 3.2%. Also notable was the sharp underperformance of a number of South East Asian markets. Continuing the negative trend from late last year, the Philippine, Indonesian and Thai markets (as well as India) lagged their North Asian counterparts.

Inflation concerns were especially pointed in India and Indonesia, two populous countries where a large number of households are vulnerable to rising food prices and governments are sensitive to related political pressures. This helps to explain why the consumer staples and utilities sectors were among the worst performing market components.

Investors worry that Asian governments may intervene to prevent utilities passing on rising costs stemming from higher raw materials prices, and act to restrain the prices of staple foods.

Information technology was the best performing sector, reflecting the brightening global economic picture. Materials inched forward thanks to broadly higher commodity prices.

Portfolio Performance

The Portfolio declined but outperformed its benchmark in January. Positive return contributors came from diverse industries including energy, technology, manufacturing and real estate. Detractors were concentrated in the materials and telecommunications sectors.

Chinese firms led contributors. After being somewhat overlooked last year, Sinopec's shares rebounded as Chinese authorities relaxed price constraints on some of the company's refined products. Additionally, Sinopec's chemicals business is performing soundly, in our judgment.

BYD Electronic, which manufactures handset components and modules as well as assembling mobile phones for the likes of Nokia and Motorola, also had a good start to the New Year. The firm, however, is not a participant in the smartphone craze. Last year, this hurt BYD Electronic as investors worried that the company was in danger of becoming commercially out of touch.

Rather than being swayed by market anxiety, we abided by BYD Electronic. While smartphones may be a fashionable consumer item, there are still large numbers of people who want phones with basic functions. BYD Electronic's cost-competitive wares are ideal for such buyers, we believe.

China Forestry was one of the Portfolio's largest detractors. The company has been suspended pending an investigation by auditors. We are monitoring the situation closely and will decide on our next steps when all relevant information is made available to shareholders. Also detracting was Korean industrial conglomerate, Hyosung and Indian real estate company DLF.

Outlook

The sharp falls suffered by South East Asian markets are starting to make a number of stocks in those countries increasingly attractive and thus it is possible that the Portfolio may undergo a subtle rebalancing in the months ahead. Meanwhile, we remain upbeat about the Portfolio's capacity to generate good returns and enthusiastic about the prospects for cheaply valued stocks in the region, particularly in banks, real estate and consumer cyclicals.

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