AllianceBernstein®

ANY QUESTIONS?

ALLIANCEBERNSTEIN LISTENS TO ADVISERS' CONCERNS

As an adviser, you know the importance of listening to your clients. It's equally important for us to listen carefully to the advisers we work with so that we know and understand the issues that you and your clients face and how we might be able to help you deal with them. Below, we answer some of the questions that advisers frequently ask us. If you have a question that doesn't appear here, please get in touch; our contact details are on the back page.

Q: MY CLIENTS HAVE TWO CONCERNS: THE SHORT-TERM OUTLOOK FOR FINANCIAL MARKETS AND, LONG-TERM, THEIR PROSPECTS OF ENJOYING A FINANCIALLY SECURE RETIREMENT. WHAT RESEARCH DO YOU HAVE THAT CAN HELP THEM GET A PERSPECTIVE ON THESE ISSUES?

AllianceBernstein (AB): These issues are separate in terms of time horizon but related from an investment point of view, so you're right—it's important to get a perspective on them. We think the best perspective is summed up in one word: volatility. Why? Let's begin with the short-term outlook.

"WE THINK THE BEST PERSPECTIVE IS SUMMED UP IN ONE WORD: VOLATILITY"

Each quarter, we publish *AB Volatility Insights*, which monitors risks that could cause turbulence in the Australian and global equities and fixed-income markets. During fourth quarter 2017, the long-established disparity between high asset prices and low volatility increased further, reinforcing concerns that investors have become complacent.

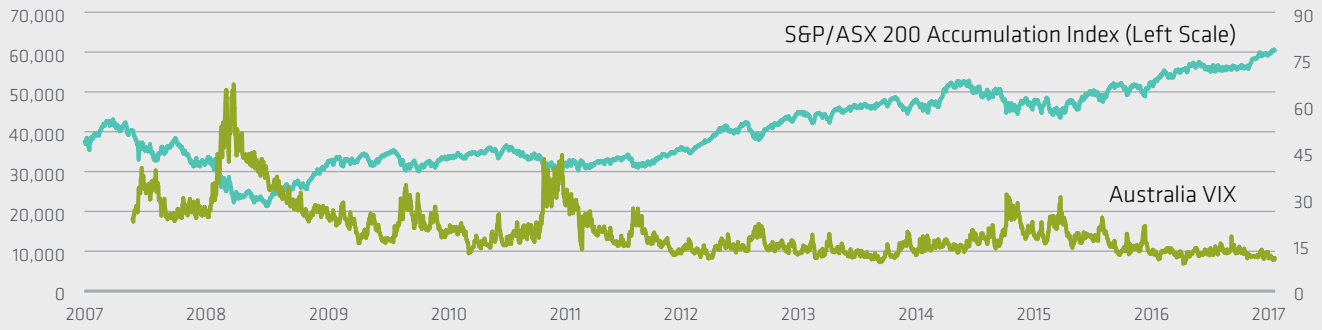
That may be because they're taking comfort from the improving economic outlook. But we see risks that could puncture their mood and cause volatility to increase and asset prices to weaken.

One of these is the geopolitical outlook; another is that central banks will overplay their hand as they wind back the asset purchases which, since the global financial crisis, have helped markets and economies stay reasonably buoyant.

The gap between volatility, as reflected in the Volatility Index or VIX, and equity valuations is a trend to watch (*Display*).

HIGH VALUATIONS, LOW VOLATILITY (VIX) PROMPT CONCERNS

VIX vs. S&P/ASX 200 Index



Historical analysis does not guarantee future results.
Through January 2, 2018
Source: FactSet

As for the long-term outlook, including retirement, volatility is particularly important. Market drawdowns eat into capital. The problem for retirees is that they need investment income to meet living expenses. This drain on their portfolios means that they will take longer than will other investors to recoup their capital when markets recover—if, indeed, they will be able to recoup it at all.

We look at this issue in depth in several research articles, including *Meeting the Investment Needs of Australian Retirees*.

In today's market environment, we see volatility as an important short- and long-term risk for investors; so, to help your clients get a perspective on their concerns, we think a good way to approach the subject with them is by introducing them to the concept of volatility.

"WE PREFER SOLUTIONS BASED ON DOWN-TO-EARTH, TRIED AND TESTED INVESTMENT PRINCIPLES, WHICH YIELD GOOD RESULTS COST EFFECTIVELY"

Q: WHAT KIND OF STRATEGIES MIGHT BE AVAILABLE TO MY CLIENTS FOR DEALING WITH VOLATILITY?

AB: There are various strategies on the market, some of them quite sophisticated and, because they incorporate enhancements such as derivatives, potentially costly. We prefer solutions based on down-to-earth, tried and tested investment principles, which yield good results cost effectively.

For example, the basic principle behind the **AB Managed Volatility Equities Fund** is to exploit the low-volatility paradox—that is, the tendency for a portfolio of low-volatility stocks to outperform a more conventional portfolio over time. But to give the Fund its extremely competitive performance edge, Roy Maslen, Chief Investment Officer—Australian Equities, makes some important refinements.

You can read about the strategy and investment philosophy behind the Fund in our white paper, *The Upside of Less Downside: How Defence Can Win in Australian Equities*. From the Fund's inception in March 31, 2014, to December 31, 2017, this investment approach helped the Fund earn a total return (net of fees) of 13.17%[1] annualized, outperforming the S&P/ASX 300 Franking Credit Adjusted Daily Total Return Index (Tax-Exempt) by an annualized 4.62% after fees.

Similarly with the **AB Dynamic Global Fixed Income Fund**, Portfolio Manager John Taylor takes the risk-mitigating and return-optimizing strategy of diversification to a new level through the application of four key investment principles. You can read about his approach in *Bringing Balance to Australian Income Portfolios: How to Take Control of Your Bond Market Returns Without Sacrificing Downside Protection*.

Through December 31, 2017, the AB Dynamic Global Fixed Income Fund delivered total returns (net of fees) of 3.64% annualized since its inception on June 2, 2014. These compare to 2.16% annualized returns for the Bloomberg AusBond Bank Bill Index for the same period.

Both funds charge management fees of 0.55% a year.

1 The return shown here is net of fees and costs, and does not allow for tax or inflation. The return includes an adjustment for franking credits. The benchmark was changed to the S&P/ASX 300 Franking Credit Adjusted Daily Total Return Index (Tax-Exempt), effective March 1, 2016. The Fund's previous benchmark, the FTSE ASFA Australia 300 Index (Tax Exempt), is used for the period March 31, 2014 (the Fund's inception date) to February 29, 2016.

Q: ARE THESE STRATEGIES BETTER FOR INVESTORS' SHORT- OR LONG-TERM HORIZONS? HOW DO THEY FIT INTO A DIVERSIFIED PORTFOLIO?

AB: We regard both these strategies as being particularly competitive over the long term. For example, the capital preservation aspects of the **AB Managed Volatility Equities Fund**, which aims to beat the market by limiting losses to 50% of market downturns while capturing up to 80% of the upside, lends itself to the accumulation phase of superannuation investment as much as to the retirement phase.

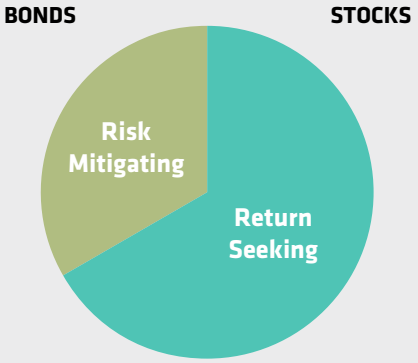
In thinking about how the strategies might fit into a diversified portfolio, it helps to rethink some traditional notions about asset allocation. As the pie chart on the left of the display below shows, this traditional approach is relatively straightforward, with bonds representing the stability part of a portfolio and equities the growth part.

Since the financial crisis and the fall of bond yields to levels below those of equities, however, the relationship between the two asset categories has become more nuanced. Today, it makes more sense to look for return and risk-mitigation opportunities in both equities and fixed income, as shown in the pie chart on the right.

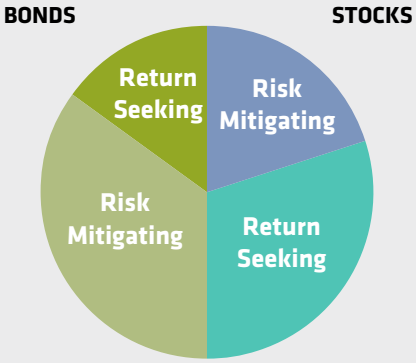
"TODAY, IT MAKES MORE SENSE TO LOOK FOR RETURN AND RISK-MITIGATION OPPORTUNITIES IN BOTH EQUITIES AND FIXED INCOME"

RETHINKING ASSET ALLOCATION FOR TODAY'S ENVIRONMENT

Traditional Portfolio Asset Allocation



How to Think About Allocation Now



Stylised representation for illustrative purposes only.
Source: AB

Doing so helps to improve a portfolio's potential risk-adjusted rate of return—an important consideration for retirees who need high returns to reduce longevity risk and drawdowns caused by sequencing risk.

Determining actual asset allocations, of course, is best done by investors with the guidance of their financial advisers. It should be noted, too, that equity and bond strategies are not the only investment options that should be considered for a retirement portfolio: others include, for example, the Comprehensive Income Products for Retirement (CIPRs) now under discussion between the retirement industry and government, together with annuities and property.

But the equity and bond strategies discussed here could go a long way in helping to achieve the three goals of a retirement portfolio—flexibility, risk management and income. For example, if a retiree's portfolio is too defensive overall, such strategies could help increase returns in a risk-aware way. If the portfolio is too aggressive with growth assets, they could help to reduce risk.

LEARN MORE

FOR MORE INFORMATION, PLEASE CONTACT:

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DISCLOSURE

The inception date of the AB Managed Volatility Equities Fund ("Fund") was March 31, 2014. The returns shown here are net of fees and costs and do not allow for tax or inflation. The return includes an adjustment for franking credits. Performance is calculated using the relevant end-of-month Exit Prices and assumes that income is re-invested and that the investment is held for the full period. Accrued franking credits are calculated by dividing the total franking credits expected to be received for a given month, by the Fund's average net assets for that month. Reported franking credit returns will differ from an investor's actual returns due to the calculation methodology described above and because franking credits are only realised upon lodgement of a tax return after June 30 each year. We will provide additional performance calculations for the financial year that includes the effect of franking credits consistent with the Financial Services Council guidance after June 30 each year. Franking credits are included in the calculation of the Relative Returns to allow a comparison with the Fund's franking credit–adjusted Benchmark. The information above may change in the event of error. Numbers may not sum due to rounding. The performance figures are historical and past performance is not necessarily an indication of future performance. See https://web.alliancebernstein.com/funds/au/equity/managed-volatility-equities.htm for further details.

INFORMATION ABOUT THE AB MANAGED VOLATILITY EQUITIES FUND

AllianceBernstein Investment Management Australia Limited (ABN 58 007 212 606, AFSL 230 683) ("ABIMAL") is the responsible entity of the AllianceBernstein Managed Volatility Equities Fund (ARSN 099 739 447) ("Fund" or "AB Managed Volatility Equities Fund") and is the issuer of units in the Fund. AllianceBernstein Australia Limited ("ABAL") ABN 53 095 022 718, AFSL 230 698 is the investment manager of the Fund. ABAL in turn has delegated a portion of the investment manager function to AllianceBernstein L.P. ("AB"). The Fund's Product Disclosure Statement ("PDS") is available at the following link https://web.alliancebernstein.com/funds/au/equity/managed-volatility-equities.htm or by contacting the client services team at AllianceBernstein Australia Limited at (02) 9255 1299. Investors should consider the PDS in deciding to acquire, or continue to hold, units in the Fund. Information, forecasts and opinions set out in this document are not personal advice and have not been prepared for any recipient's specific investment objectives, financial situation or particular needs. Neither this document nor the information contained in it are intended to take the place of professional advice. Please note that past performance is not indicative of future performance and projections, although based on current information, may not be realised. Information, forecasts and opinions can change without notice and neither ABIMAL or ABAL guarantees the accuracy of the information at any particular time. Although care has been exercised in compiling the information contained in this report, neither ABIMAL or ABAL warrants that this document is free from errors, inaccuracies or omissions.

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INFORMATION ABOUT ALLIANCEBERNSTEIN

AllianceBernstein (AB) is a leading global investment management and research firm. We bring together a wide range of insights, expertise and innovations to advance the interests of our institutional investors, individuals and private clients in major world markets. AB offers a comprehensive range of research, portfolio management, wealth management and client-service offices around the world, reflecting our global capabilities and the needs of our clients. As at December 31, 2017, our firm managed US$554 billion in assets, including US$269 billion on behalf of institutions. These include pension plans, superannuation schemes, charities, insurance companies, central banks and governments in more than 45 countries. We're truly global, but we're not just portfolio managers and analysts in one location investing globally. We have an extensive global footprint that we've built over four decades. Our global teams collaborate across asset classes and investment strategies to spark new thinking and deliver superior outcomes for our clients. Every day brings a new set of investment challenges and opportunities. Through our unique combination of expertise, innovative offerings and global reach, we anticipate and advance what's next—applying collective insights to help keep our clients at the forefront of change. This document is released by AllianceBernstein Australia Limited ("ABAL") ABN 53 095 022 718, AFSL 230 698. AllianceBernstein Australia Limited (ABAL) is a wholly owned subsidiary of the AllianceBernstein, L.P. Group (AB).

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