

Australian Growth Portfolio Performance

Outperformance in Rising Market

The multifaceted character of our investment approach helped to carry the portfolios to modestly index-superior returns. Investors were drawn toward cheap stocks as well as those delivering on earnings promise. In this environment, our winning holdings included James Hardie, Macquarie Group and Downer EDI.

Equities Marched On

Global equity markets continued to mend with strong gains featuring in the September quarter (**Display 1**). The greatest economic hazards appear to have passed and recovery, even if it is uneven, is underway.

Australia's economy also exhibited resilience with 2Q09 GDP bouncing higher than forecast. The warming economic climate was a fillip for the Australian sharemarket—as measured by the ASX/S&P 300 Accumulation Index—which ended the September quarter 21.6% higher. It was a figure towards the top-end of developed country returns.

Sector returns were in tune with economic developments as the financials and industrials components provided market leadership. Financials thrived as market participants concluded that the bad debt situation will be nowhere near as serious as feared. Industrials gained on the back of rising optimism for a host of transport and infrastructure-related names.

Telecommunications and utilities lagged. The government's announcement that it wanted telco behemoth Telstra to separate its wholesale and retail arms rattled shareholders. Utilities' defensive

characteristics meant that it was out of favour in a time of rising risk appetite.

Earnings Deliverers Rewarded

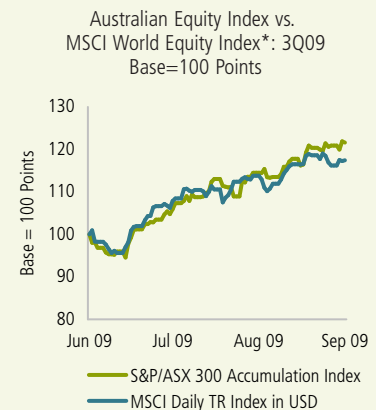
In a complex quarter, sector and stock selection combined to deliver modestly benchmark-superior returns. While investors continued to show a liking for stocks that looked like cheap options on economic recovery, they also became more discriminating and sought out companies that are delivering on earnings promise.

Two of our winning holdings building materials company James Hardie and engineering services firm Downer EDI (**Display 2**) were such earnings deliverers.

James Hardie recently unveiled 1Q10 results revealing striking EBIT margins for the company's key US fibre cement business. Such an achievement in a fragile US housing market confounded market participants. See more on James Hardie in the Portfolio Positioning section of this report.

Downer EDI and its joint venture partner's success in winning a large contract to operate Melbourne's tram system for eight years, on top of the solid volume of work available for engineering services firms generally, boosted the company's shares.

Display 1
Good Times for Local and Global Shares



As of September 30, 2009
*Morgan Stanley Capital International (MSCI) World Index
Source: Bloomberg

Display 2
James Hardie Was Among Our September-Quarter Contributors*

▲ Contributors	▼ Detractors
■ James Hardie	■ ANZ
■ Macquarie Group	■ Resmed
■ Downer EDI	■ Leighton Holdings

As of September 30, 2009
*Overweight holdings only shown
Based on a representative Australian Growth Equities portfolio
Source: Alliance

On the other hand, Macquarie Group, another of our outperformers, is emerging as a success story from 2008's dramas. Macquarie Group is making use of its strong balance sheet to enter into potentially lucrative new activities as well as acquiring attractively valued business overseas to add to its core broking and investment banking franchise.

These statements reflect the performance of the majority of accounts. Individual account performance may vary due to a variety of factors, including benchmark, account guidelines, investment vehicle implementation (if any), fees charged and timing of cash flows.

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Growth Equities Market Overview

Risk Assets Continue to Rally as Signs of Recovery Proliferate

Equity and credit markets rallied further in the third quarter as investors gained confidence that a sustainable economic recovery is under way. We expect a return to modest global economic growth in 2010. As the recovery gains traction, remaining risks and uncertainty are keeping risk premiums elevated and—in our view—attractive.

Risk Assets Rally

Risk assets continued to rally in the third quarter as investors gained confidence that the global economy was emerging from a deep recession and appears on track for a return to modest economic growth. Stocks rallied globally for the second consecutive quarter; the MSCI World Index rose 17.5% in dollar terms and has recouped about half its losses from the peaks of 2007.

Corporate bonds, commercial mortgage-backed securities and other nongovernment debt also rallied as spreads narrowed.

In sum, a sense of normality is returning to the economy and financial markets. While risk premiums remain high versus historical norms, they have receded dramatically from their heights at the peak of the recent crisis. Liquidity is returning, and credit is becoming cheaper and more readily available as markets normalize. Corporate earnings look to have reached bottom after a two-year plunge, and positive earnings surprises are increasing.

The continuation of extremely accommodative monetary policies has supported the rebound in risk assets: by keeping short-term interest rates low, central banks are essentially raising the opportunity cost of staying in “safe” assets such as cash and short-term government bonds. Still, despite extremely low yields, significant pools of money remain on the sidelines (**Display 1**). Reentry of these funds into the market could extend the current rally.

Recovery Is Under Way

The economic recovery—which began in China and other parts of Asia in the second quarter—appeared to gain speed and traction globally in the third quarter.

Industrial production rebounded sharply around the world (**Display 2**). The Global Manufacturing Purchasing Managers’ Index (PMI) jumped to its highest level since early 2008 in August, and exceeded 50—the threshold indicating expansion—for the second consecutive month. Automakers and other manufacturers are boosting production to restock depleted inventories in anticipation of meeting pent-up demand.

Massive doses of coordinated monetary and fiscal stimulus from governments and central banks around the world have also provided impetus for the recovery—and there is much more stimulus to come. For example, of the US\$787 billion of spending and tax cuts promised by the Obama administration, just a third was budgeted for 2009, with much of the balance due in 2010.

Similarly, while interest rates will eventually have to rise, major central banks are not likely to dramatically reverse course as long as inflationary pressures remain benign.

Is the Recovery Sustainable?

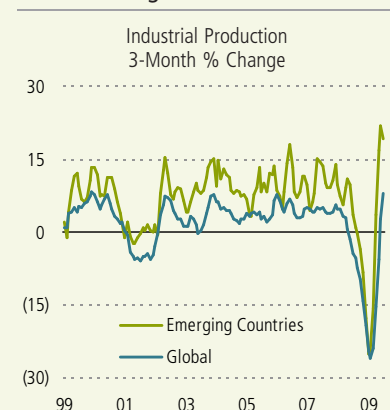
The global economic recovery has been led by China and other countries in emerging

Display 1
Pools of Cash Remain on Sidelines



Source: Haver Analytics and AllianceBernstein

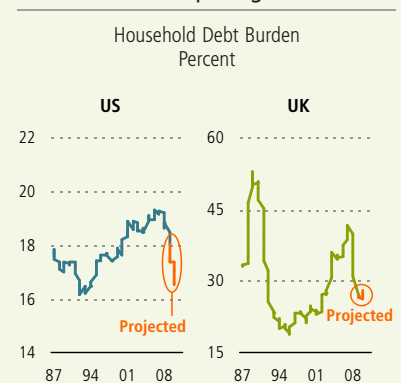
Display 2
Manufacturing Has Rebounded



Through July 31, 2009

Source: Haver Analytics and AllianceBernstein

Display 3
Consumers Are Repairing Finances



US household financial obligations as a percent of disposable income, and UK average mortgage repayment (interest and principal) as a share of average wage; historical data through June 30, 2009; projections through 2010

Source: Haver Analytics, US Federal Reserve and AllianceBernstein

Asia. Many observers wonder if the recovery can be sustained if the US consumer continues to save more and spend less. After all, the American consumer accounts for as much as 70% of US GDP, and in the decade leading up to the recent crisis, the US consumer's borrowing and consumption binge helped underpin global economic growth.

These concerns are not without foundation. Consumer spending remains depressed by stubbornly high unemployment and continued deleveraging. But in our view, these concerns are overstated.

First, consumers in the US and other developed markets, while still under financial stress, have made significant progress over the past year in rebuilding their balance sheets. The portion of disposable income eaten up by debt service has fallen sharply in both the US and the UK since the peak of the crisis (**Display 3, previous page**). In fact, US households have cut this ratio to its lowest level since 2000.

We expect the deleveraging to continue, particularly in the US, as consumers continue to reduce their debt burden and save more. As a result, households should be in far better financial shape—and more willing to increase their spending—by late 2010, when the benefits of fiscal stimulus start to wane.

Second, after a decade of rapid economic expansion, emerging-market countries now contribute more to global GDP than the United States—or the euro area and the UK combined (**Display 4**).

The fact that emerging Asian economies started to rebound in the second quarter before consumption in developed countries indicates that the current recovery in emerging-market economies is driven mainly by domestic demand. In the past, exports were the main driver. In our view, a more balanced global economy is a

healthier one; the shift toward increased domestic demand from China and other large emerging economies is a key ingredient to sustaining global economic growth and addressing imbalances.

In short, weak consumer spending in the US and other developed markets may not be the roadblock to a sustainable global economic recovery that many expect.

A Brighter 2010

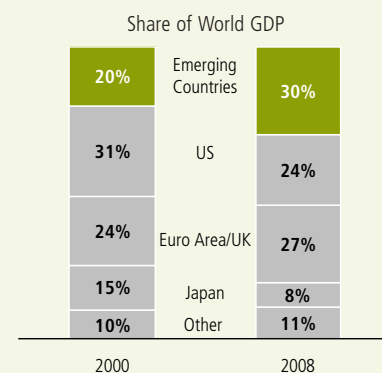
We expect emerging-market economies to continue to lead the recovery in 2010 (**Display 5**). Overall, we expect global economic growth of 3.4%, close to its long-term average. We see US economic growth of 3.5%—higher than the consensus expects but lower than previous periods of recovery following deep economic downturns.

Nevertheless, significant risks and challenges persist for the global economy and financial markets. Many investors worry about how governments and central banks 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 rein in ballooning fiscal deficits (**Display 6**)? If not, inflation could surge.

The transition will be challenging, but the creativity shown by policymakers during the recent crisis gives us comfort in their ability to adjust policy when necessary. In our view, these risks bear close monitoring but do not likely pose an economic threat this year or next.

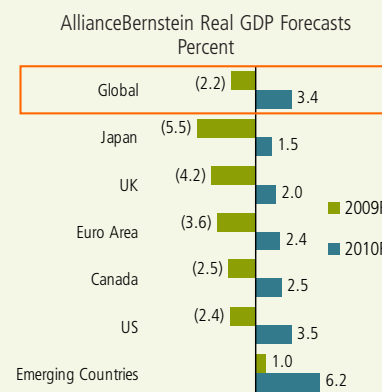
The upside of continued anxiety about the economic outlook is that attractive opportunities remain for active managers to add value. We see sizable opportunity for equity managers to generate excess returns through stock selection and for fixed-income managers to take advantage of the significant return potential in the credit sector.

Display 4
Emerging Markets Increasingly Important



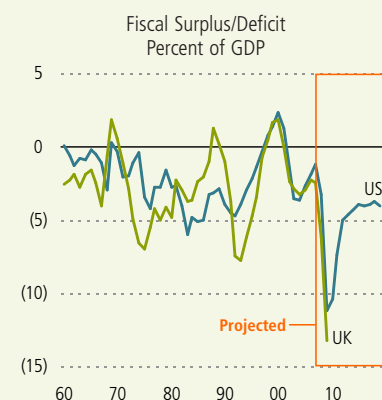
Source: Haver Analytics and International Monetary Fund

Display 5
A Return to Modest Growth



As of October 1, 2009
Source: AllianceBernstein

Display 6
Fiscal Deficits Bear Watching



Historical data through fiscal year 2008; US projections through fiscal year 2010; UK projections through fiscal year 2009
Source: Office of Management and Budget, UK Office for National Statistics and AllianceBernstein

Australian Growth Portfolio Positioning

Preferring Leaders and Innovators

Thanks to skilful cost containment, Australian firms are well-placed to stage a powerful comeback as economic recovery gathers speed. Featuring among our high-conviction positions are companies that we believe are industry leaders and innovators such as James Hardie and Bradken.

Earnings Upgrade Cycle Underway

After about two years of earnings downgrades, a new-found sense of hope is moving through the Australian market stirring expectations of rising earnings (**Display 1**). This shift stems from corporate Australia's generally pleasing results in the recently ended reporting season. Expectations were admittedly low in the wake of last year's tumult. Nevertheless, through a combination of aggressive cost-cutting and a level of underlying demand that defied the doomsayers, managements delivered encouraging results.

A leaner cost base provides many companies with strong operating leverage should the economic recovery prove sustainable, thereby boosting demand for products, lifting revenues and bolstering margins. Laudable as cost containment has been so far, we think that the full benefits are yet to materialise. In tandem with a potential recovery in volume growth, the broad financial impact of many cost savings initiatives could take up to a year to fully translate into better earnings.

This perspective is influencing our portfolio positioning as we have been increasing our exposure to cyclical companies. Confidence in our preferred stocks has been matched with care and therefore our weightings in cyclical companies, including those in the building materials, resources and financials arenas have been rising gradually. Despite recuperating, the global

economy is far from normal. Policy misjudgements could trip up the recovery. Mindful of the possibility for pitfalls, principles of diversification and risk management infuse portfolios.

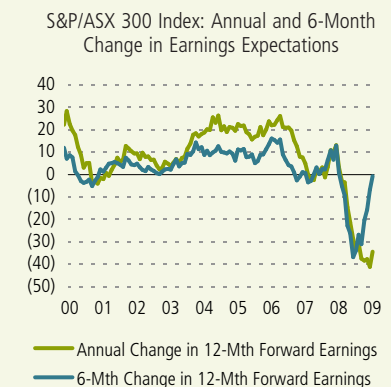
In the following paragraphs, we put the spotlight on innovative companies that are market leaders as well as firms that can exploit improving industry conditions. Building products maker James Hardie is a representative from the first camp. Bradken, which makes capital equipment for the mining and energy industries, and asset manager Henderson are examples from the second category.

James Hardie: Positively Surprising

Building products company James Hardie (Hardie) stirs emotions. Plans to relocate its place of corporate domicile from the Netherlands to Ireland have rankled critics. More provocatively, Hardie's reputation remains sullied because of illnesses suffered by past employees and their families stemming from the days when the company made asbestos-based insulation materials. Our financial analysis captures the decades-long liability associated with the trust that the company funds to treat mesothelioma victims.

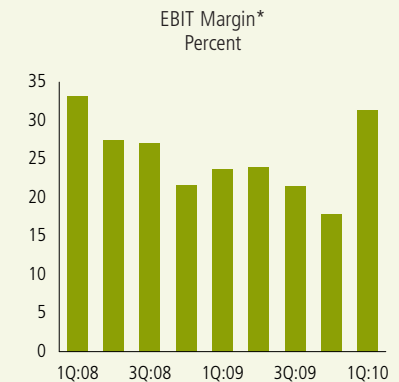
There is also a commercially impressive side to Hardie, according to our comprehensive research. Recently unveiled 1Q10 results revealed EBIT margins in excess of

Display 1
Earnings Expectations Are Rising Again



Through September 2009
Source: Goldman Sachs JB Were

Display 2
Recent Margin Was Attention-Grabbing



As of September 8, 2009
*Earnings before interest and tax for James Hardie's US fibre cement operations
Source: Company data, Credit Suisse

30% for the company's key US fibre cement business. The achievement was ahead of both market expectations as well as recent history. Attaining such a large a margin in a fragile US housing market was especially attention-grabbing (**Display 2**).

The feat, however, should not have been surprising. Hardie is an innovator, a product leader and skilled marketer, in our opinion. Through the current cycle,

those traits in concert with falling pulp and energy prices and deft cost management have been underpinning success.

A longstanding commitment to research and development has helped to make Hardie's fibre cement sidings the industry benchmark. Rather than resting on its laurels, Hardie continues to innovate. A recently released product, "HZ10", created specifically for homes in the seasonally cold and wet US north-east, will give Hardie a presence in a geography where its footprint has been light up to now.

We expect the company's business model to remain robust and thus believe that it can maintain margins at levels that will outpace market expectations. Moreover, when the US new homes market does rebound, Hardie's cost-control skills will give it enviable earnings leverage, in our view.

Volume Growth to Drive Bradken

Bradken's two main business lines, making consumables (parts such as digging teeth for massive industrial shovels and components for iron ore crushers) and rail wagons for mining companies contribute around 60% of annual revenues. The consumables business provides annuity-like revenues; parts replacement occurs regularly. Rail wagon manufacturing is a more commercially volatile activity, but in good times can be a potent earnings booster.

We bought Bradken earlier this year at a provocative price after being reassured by intensive research that the market's misgivings about the stock were overdone. Worries that the company was burdened by excessive debt and that Chinese raw materials demand would remain subdued proved to be unduly pessimistic.

In fact, as we anticipated, because of its balance sheet soundness, Bradken did not need to raise capital. Coupled with this, thanks to the Chinese government's massive economic stimulus program, which includes an ambitious infrastructure

build-up and modernisation program, Australian coal and iron ore export volumes have kicked up (**Display 3**). Consequently, key Bradken clients such as BHP Billiton and Rio Tinto need more rail wagons to carry coal and iron ore to ports.

Local developments are also assisting Bradken's cause. Competition in the Australian coal transport market is heating up as other Bradken clients Pacific National and Queensland Rail become more active in states where they have previously had a low profile. As its clients grow, so also does the need for Bradken's wares.

Despite favourable industry trends, investors have assigned Bradken with a lower valuation than other engineering services-based firms such as United Group and Downer EDI. We believe this understates the company's prospective earnings and are therefore glad to own Bradken.

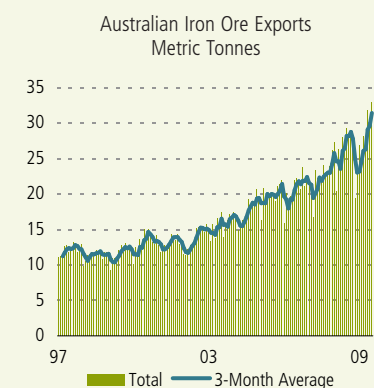
Henderson Builds Up

UK-based asset manager Henderson Group (Henderson) has reinvented itself over a number of years. Whereas it was once an underperforming equities manager largely confined to the institutional arena, it has grown into a diversified firm with a varied, high-margin product stable and excellent cost-control. Consequently, it is well-placed to thrive as asset markets recover, we believe.

Acquiring retail-focused asset manager New Star earlier this year strengthens Henderson's presence in an area where the firm was underweight. New Star was bought in the pits of the investment cycle at an attractive price, in our opinion. Naysayers anticipated a massive outflow of funds and integration headaches.

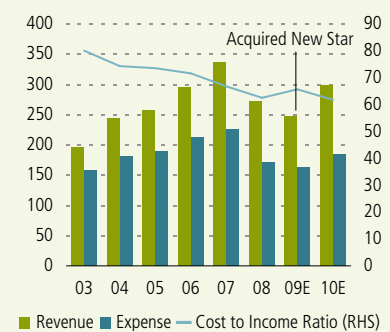
Instead, the acquisition has been a success story. Funds under management retention and cost efficiencies have surpassed expectations. Henderson's management of costs generally has impressed us (**Display 4**) as the compa-

Display 3
Iron Ore Exports Have Kicked Up



Through July 2009
Source: ABS

Display 4
Henderson's Good Cost Management



As of September 30, 2009
Source: Company reports and Alliance Growth analysis

ny's skills in this arena appear to be ahead of many peers, according to our research. Retail investment margins are around 50% greater than institutional margins and therefore the New Star acquisition is an all-round margin booster for Henderson. New Star's product line-up is being broadened by Henderson as new funds are being launched. In fact, Henderson's product stable in general is commercially attractive, in our view. It is diverse, spanning equities, fixed income and property, as well as increasingly skewed to higher-margin products such as hedge funds and private equity. The breadth of the product line-up means that the company has broad leverage to asset market recovery. It's another reason why we like Henderson.

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