OCTOBER 2024

Four Investment Controversies

While there is a very active debate between investors about the tactical prognosis for the market, and with good reason, there are also controversies that relate more to market structure. We explore a number of these topics in this note and what they mean for investor positioning.

One of the topics that comes up most frequently in meeting with clients is public sector debt and what it means for markets, the availability of a fiscal cushion in the future and the role of government bonds in portfolios. Concentration of markets is another topic with wide-reaching implications for risk and the opportunity set available to investors. Other topics covered are how high the allocation to private assets can go and de-equitization.

Inigo Fraser Jenkins
Alla Harmsworth

Additional Contributors: Robertas Stancikas, Harjaspreet Mand and Maureen Hughes

This note discusses four investment controversies that are concerned with market structure. We want to get away, in this note at least, from the headline issues of the next step of Fed policy and market direction. Instead, we focus on structural issues that have a very real impact on key investment decisions that allocators need to make.

The issues cover fiscal sustainability, equity-market concentration, public versus private assets and de-equitization. Fiscal largesse, with its consequences for public debt, is here to stay in the US, regardless of who wins the election. Both that and de-equitization represent a twin levering up of the system by governments and corporates.

These issues are key determinants of the investment-opportunity set, the level of volatility that investors should expect, and hence, asset allocation.

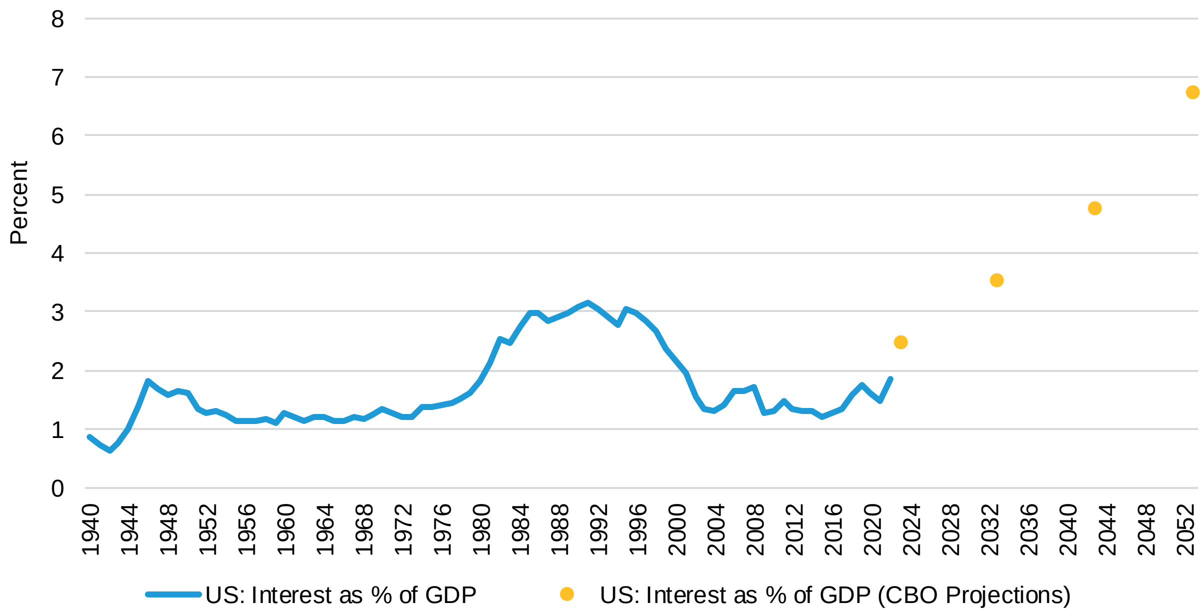
1. "I Still Owe Money to the Money, to the Money I Owe"

One of the persistent themes that pervades conversations with investors this year is debt sustainability. This comes up most frequently in the context of fiscal profligacy in the US and what it implies for debt-service costs. It is, however, a global phenomenon. In Europe, despite a tighter fiscal position, there are nevertheless concerns about sustainability. This is seen specifically in the UK, with the liability-driven investing crisis of 2022, and in France, with the run-up to the 2024 election.

Tactically, the fiscal position supports near-term growth in the US. Strategically, however, it raises a number of concerns. There is no theoretical limit to how high debt levels can go (Japan, after all, surpassed the levels in other developed nations some time ago). However, the future path of interest expense as a share of government spending implies that there are constraints in the future. We hear views expressed in meetings about the risks of this situation for bond markets, although there is no sign of an issue in US debt auctions. We do think that, when outlining capital-market assumptions, it is a reason to expect a higher level of volatility than the norm of the post–global financial crisis era.

There is a broader angle here, too. The extended period of financialization since the 1970s, which included the growth of public debt, provided huge support for financial assets relative to real assets. But alongside the contemporaneous force of globalization, the benefits were unevenly shared. It thus seems appropriate to title this section (and the overall note) in reference to a song from indie group The National. This is not only because of the obvious hint at indebtedness in the lyric that titles this section but also the underlying worry about the social fabric. The leverage in the public sector was taken on to engineer growth, which did not benefit all. It was possible to get away with this levering up because of the large forces that suppressed the cost of debt in recent decades (including demographics, the opening up of China and an apparent need to avoid paying for negative climate externalities). However, those forces have now run their course and cannot be relied on to continue. That lack of a cushion is concerning if an already damaged social fabric is set to endure a sustained period of lower growth.

DISPLAY 1: I STILL OWE MONEY TO THE MONEY, TO THE MONEY I OWE: US INTEREST EXPENSE AS A PERCENTAGE OF GDP PROJECTIONS



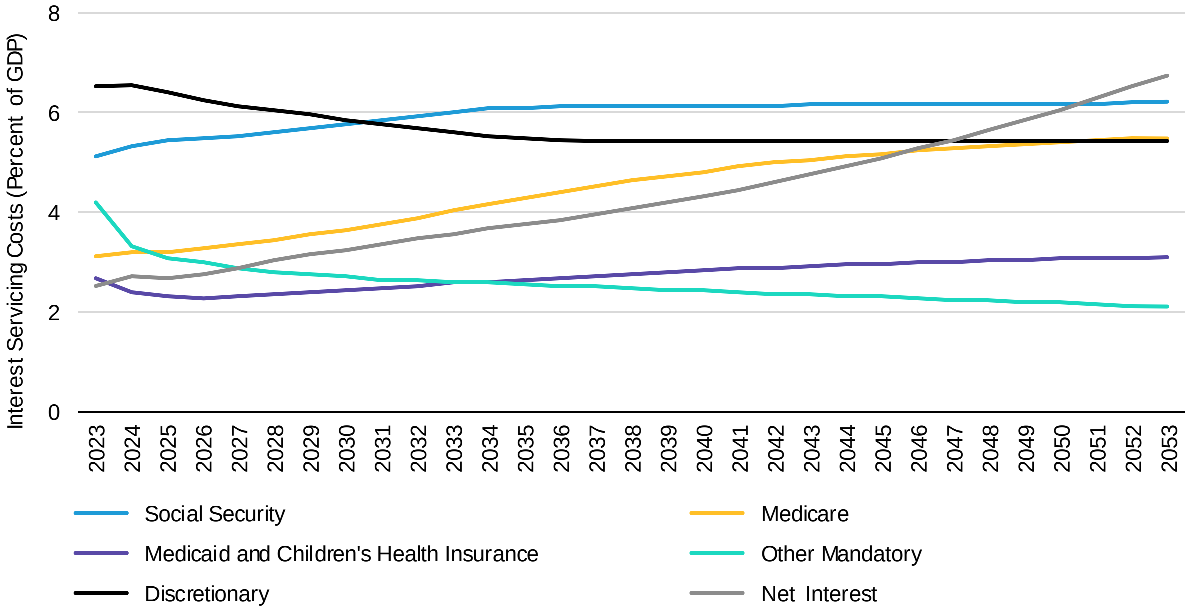
Current analysis and forecasts do not guarantee future results.

As of June 30, 2023

Source: Congressional Budget Office (CBO), Federal Reserve Bank of St. Louis (FRED) and AllianceBernstein (AB)

Display 1 shows the history of interest-service costs in the US and Congressional Budget Office (CBO) projections of their likely future path. It suggests that while these costs are not currently a problem, they are on course to become one. *Display 2* puts interest-service costs in the context of other claims on government expenditures, not the least of which are care costs in the context of an aging population.

DISPLAY 2: INTEREST SERVICING SEEMS SET TO BECOME A PROBLEM



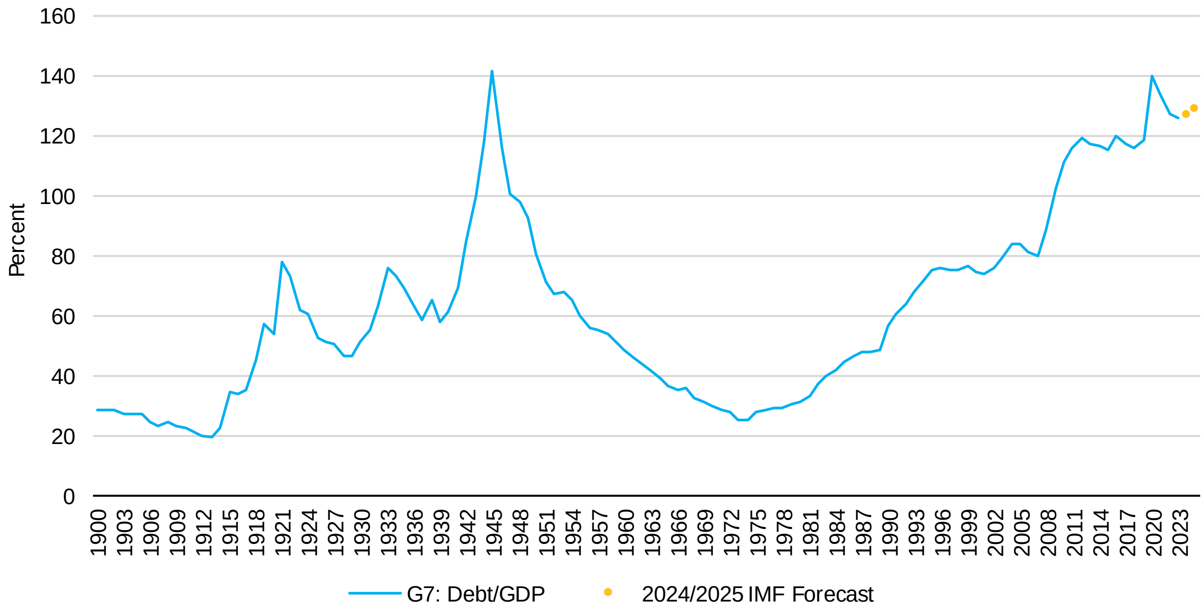
Current analysis and forecasts do not guarantee future results.

As of June 30, 2023

Source: CBO and AB

Display 3 and *Display 4, page 4,* show the percentage of public debt to gross domestic product (GDP) for the G7 and US, along with the International Monetary Fund's and CBO's projections, respectively, of where debt levels are likely headed in the coming years.

DISPLAY 3: G7 DEBT-TO-GDP LEVEL

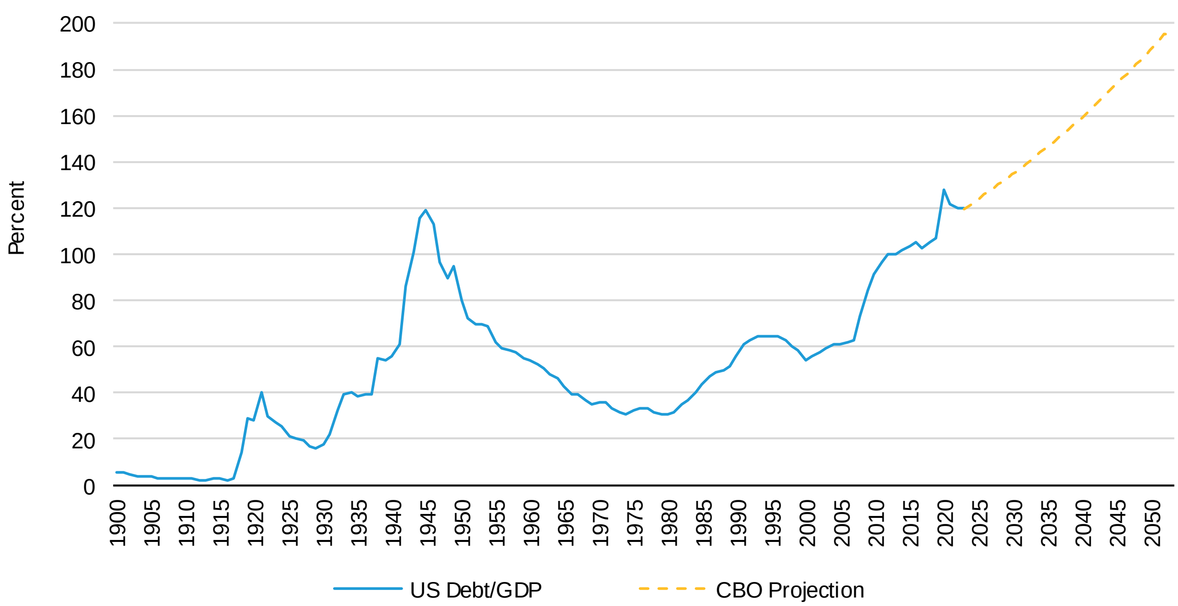


Current analysis and forecasts do not guarantee future results.

As of August 30, 2024

Source: Global Financial Data, International Monetary Fund (IMF) and AB

DISPLAY 4: US GOVERNMENT DEBT-TO-GDP PROJECTIONS



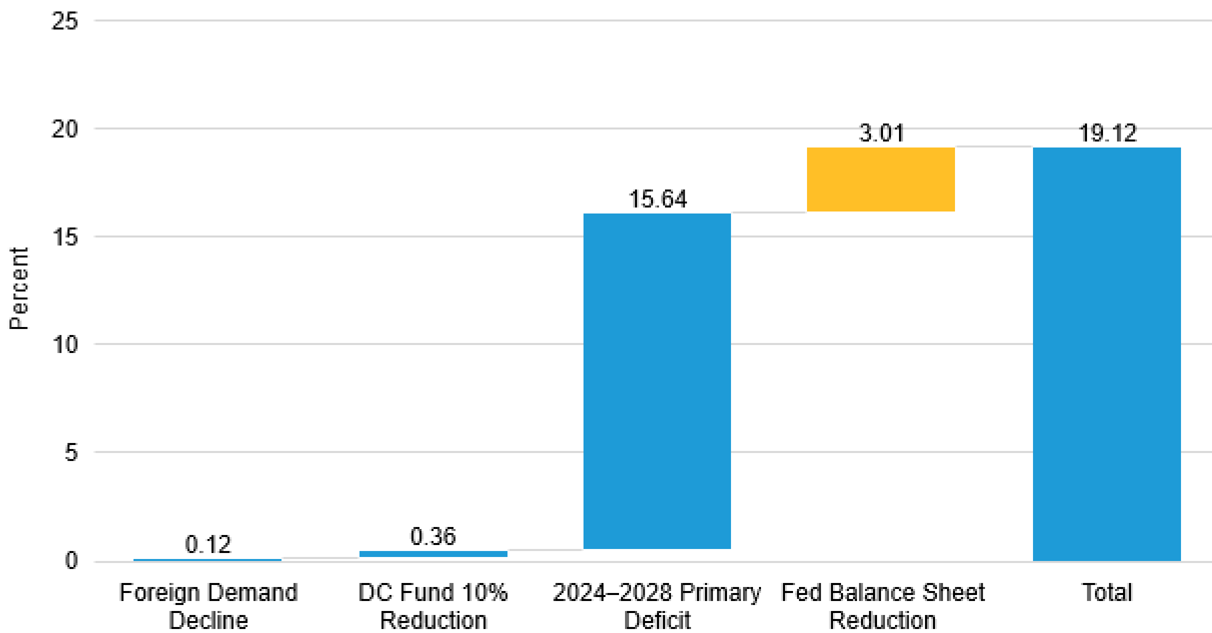
Current analysis and forecasts do not guarantee future results.

As of June 30, 2023

Source: CBO, Global Financial Data and AB

How much does this matter? This state of affairs is broadly known and, despite the hand-wringing we encounter in many investor meetings, it is far from obvious that investors are directly impacted by this issue in the near term. One angle here is the prognosis for the demand for government debt. Unlike equities, where the available stock of listed shares is declining, there is likely an excess supply of government debt (*Display 5, page 5*). Another angle is the conclusion from our recent note on the pension industry that the demand for government bonds from pension systems is likely to decline—a function of the combined forces of greater longevity and higher equilibrium inflation.

DISPLAY 5: SOURCES OF US TREASURY SUPPLY AND DEMAND



For illustrative purposes only.

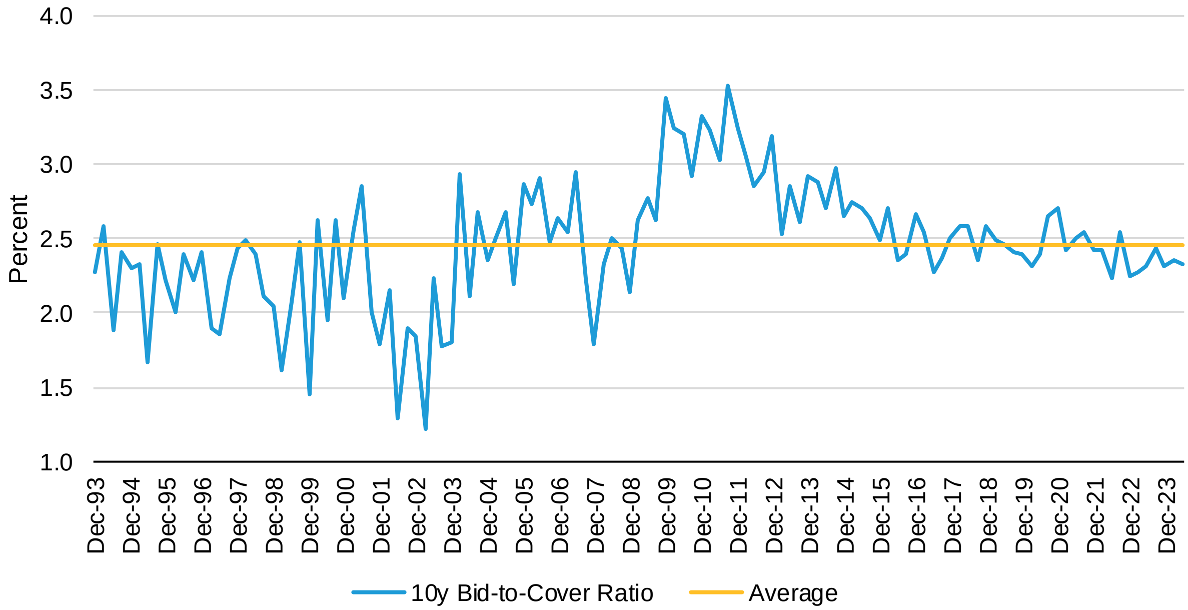
Note: The primary budget deficit is based on CBO estimates from June 2024. Fed balance-sheet reduction estimates assume that QT operation stops at the end of 2025.

As of September 13, 2024

Source: Securities Industry and Financial Markets Association, Thomson Reuters Datastream and AB

Despite the worries that we hear expressed, there is no sign that declining pension demand is presenting a problem so far in government debt auctions (*Display 6, page 6*).

DISPLAY 6: THE DIGESTIBILITY OF DEBT: BID/COVER RATIO FOR US TREASURIES



Current analysis does not guarantee future results.

Through September 10, 2024

Source: Thomson Reuters Datastream, US Department of the Treasury and AB

The consequence for investors is that strategic capital-market forecasts should incorporate higher expected volatility for government bonds and, presumably, the risk that this is expressed in demand for a higher term premium. Specifically, we expect the 10-year forward volatility of US 10-year bonds to be 7.6%, slightly above the post-1950 average of 7.3% and above the 7.1% that was the norm in the decade prior to the pandemic.

In the US, fiscal support is not going away in this election cycle, but at some point it does need to fade, with consequences for growth. More broadly, this is yet another reason to expect that equilibrium inflation will be higher than in the pre-pandemic period. From an allocation perspective, this points to a need for higher allocations to real assets, and for exposure to inflation hedges that are appropriate for the risk of inflation via depreciation. The blunt bottom line: we do not think it is an overreaction to view the level of public indebtedness across G7 economies as a national security concern.

2. How Concentrated Can the Equity Market Become?

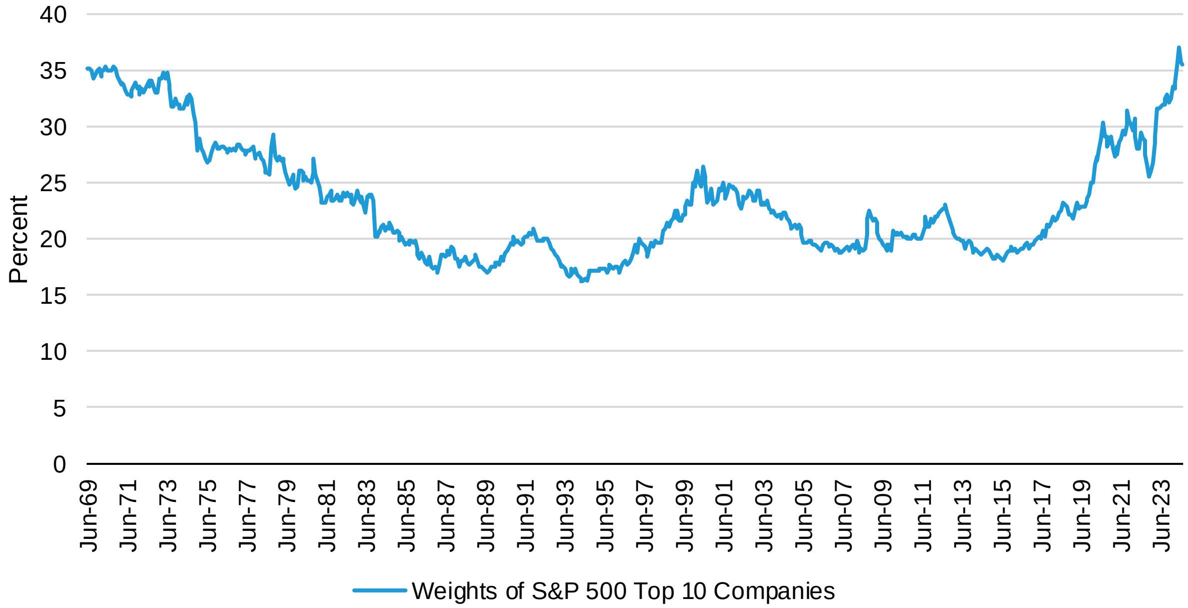
The subject of market concentration has come up in more client meetings over the last year than one cares to count. Even with the recent weakness from NVIDIA et al., and with investors becoming more wary of the Magnificent Seven bandwagon, concentration is still a huge issue. It raises questions about how risky the "passive" market index is, what the opportunity set for investment is, the link between the equity market and the real economy, and the outlook for market returns.

There are really two distinct aspects of equity market concentration: (1) stock-level concentration within the market; and 2) the concentration implicit in the weight of the US versus the rest of the world. Most of our discussion deals with the former, but also discusses the latter to the extent that it is distinct.

Despite all the angst, we have actually been here before. The last time the weight of top 10 stocks as a share of top 500 US stocks was as highly concentrated was 1969 (*Display 7, page 7*). That episode was followed by a prolonged period of decreasing concentration, most notably in the early 1980s, which hit bottom around 1993.

There have been other occasions if one looks further back in time. It is hard to get comparable data with which to draw a continuous series, but there was another major period of concentration at the end of the 19th century that was succeeded by another prolonged period of deconcentration from 1903 to 1925.

DISPLAY 7: SUMMER OF ’69?—WE HAVE BEEN HERE BEFORE
WEIGHT OF TOP 10 COMPANIES AS A SHARE OF S&P 500



For illustrative purposes only.

Through August 30, 2024

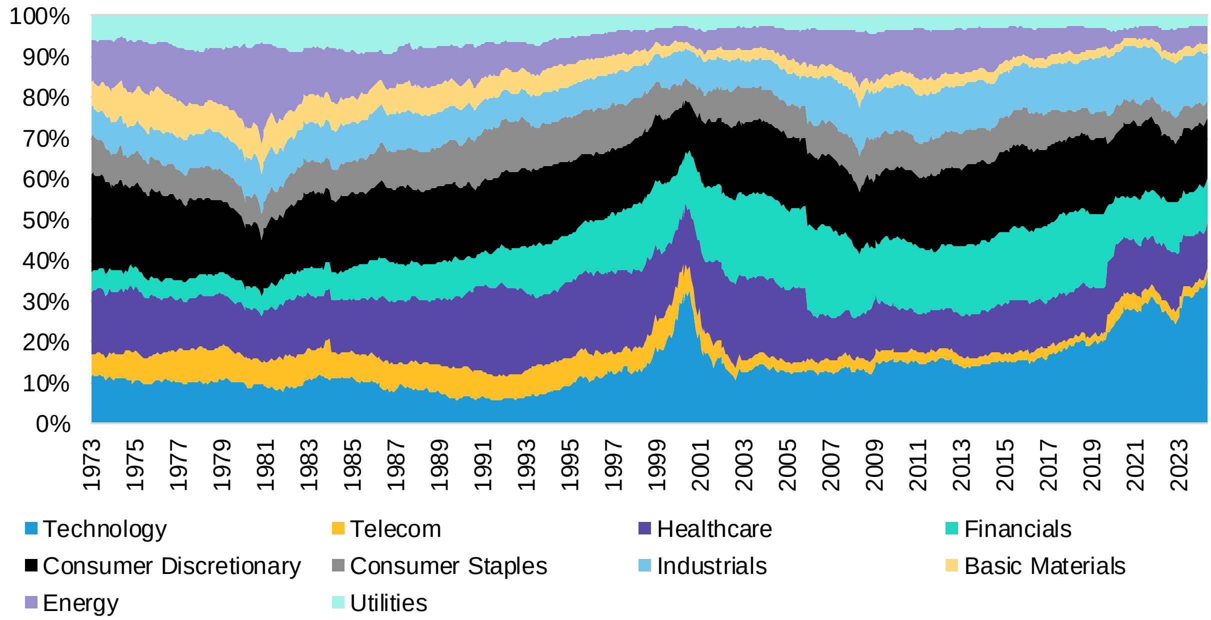
Source: FactSet, S&P and AB

What drove the prior cycles of deconcentration? The first episode was a result of the trust-busting campaign started by President Theodore Roosevelt, when the government used antitrust laws to break up monopolies. Notable victories included the 1904 dissolution of Northern Securities Company, which controlled the main railroad lines from Chicago to the Pacific Northwest; the breaking up of Standard Oil in 1911 into 34 separate entities; and the splitting of American Tobacco into four companies in 1911.

AT&T, General Motors, IBM, Standard Oil, General Electric, DuPont and U.S. Steel drove much of the US equity market’s growing concentration through the 1930s, 1940s and 1950s. Those seven companies remained among the 10 largest companies for the majority of that time. From the late ’60s to the mid-’70s, leadership broadened to the “Nifty 50.” The ensuing deconcentration was at first led by the demise of the Nifty 50. From a sector perspective, there was also a market leadership change from technology and industrials to energy. Later in the period, there was also an element of regulation—for example, AT&T was broken up in 1982.

The extent to which concentration is driven by sector leadership is shown in *Display 8, page 8.* The recent period has been more sector-driven than usual, though some of this is due to the way sectors are defined.

DISPLAY 8: US EQUITY MARKET SECTOR SHARE



For illustrative purposes only.

As of June 28, 2024

Source: Thomson Reuters Datastream and AB

Because there have been only a small number of periods of deconcentration, it is perhaps hard to draw definitive conclusions about what drives them. However, a few salient points stand out. Periods of high concentration are not that unusual, but they also tend to be relatively brief. Periods of deconcentration can take a long time (decades), so betting against mega-cap stocks from a tactical perspective can be very hard—it is more of a strategic reversion. Trust-busting and regulation have often been an element of that process, but so have shifts in sector leadership. For the purposes of the investment careers of most people in the industry today, and of the majority of data sets used to describe what constitutes a "normal" market, it should be noted that the period from the mid-1980s on saw unusually unconcentrated markets until the quantitative-easing era lowered the cost of capital and concentration rose to the high level we have become used to in recent years.

Concentration is mainly a feature of markets where value weighting has become the accepted way to determine both the benchmark and opportunity set. However, public equities are rather unique in this respect (*Display 9, page 9*). True, value weighting is often used to construct bond indices, despite not necessarily being a terribly good idea. Yes, this approach helps with liquidity, but it also gives prominence to companies or countries with more debt. Most other asset classes are not encumbered with this default assumption of value weighting, so they don't have the same concentration issue.

Arguably, a large part of the case for private assets is that they are not forced to measure themselves relative to a cap-weighted index, so they have a more free approach to defining the available opportunity set. For example, the vast majority (by number) of companies with over $100 million in revenues are not publicly listed (*Display 10, page 9*). Likewise, commodities, currencies and real assets don't have the same notion of value weighting. We have long argued that factors should be seen as being fungible with asset classes.[1] What should the natural default weight across factors be? It is likely to be something similar to equal risk-contribution weighting or just equal weighting, but market-cap weighting and hence concentration is not a feature of that asset class. We should remember that cap weighting is a *choice,* not a God-given requirement.

1 See Inigo Fraser Jenkins and Alla Harmsworth, "Asset Classes and Factors: What's the Difference?" AllianceBernstein, November 2021.

DISPLAY 9: ASSETS WHERE CAP WEIGHTING IS ASSUMED TO BE THE DEFAULT…AND ASSETS WHERE IT IS NOT

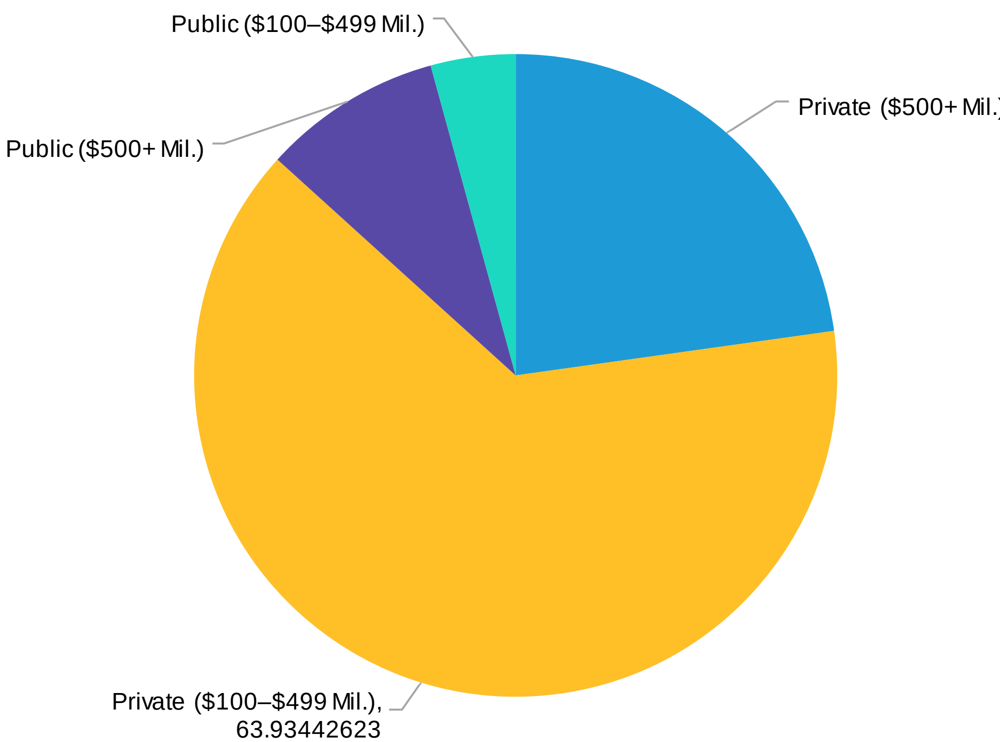
Asset Classes That Use Cap Weighting	Assets That Don't Use Cap Weighting
Equities	Private Equity
Bonds	Private Debt
	Commodities
	Currencies
	Real Assets (Farms, Infrastructure)
	Factors

For illustrative purposes only.

As of September 10, 2024

Source: AB

DISPLAY 10: FEWER THAN 15% OF COMPANIES WITH OVER $100 MILLION IN REVENUE ARE PUBLICLY TRADED



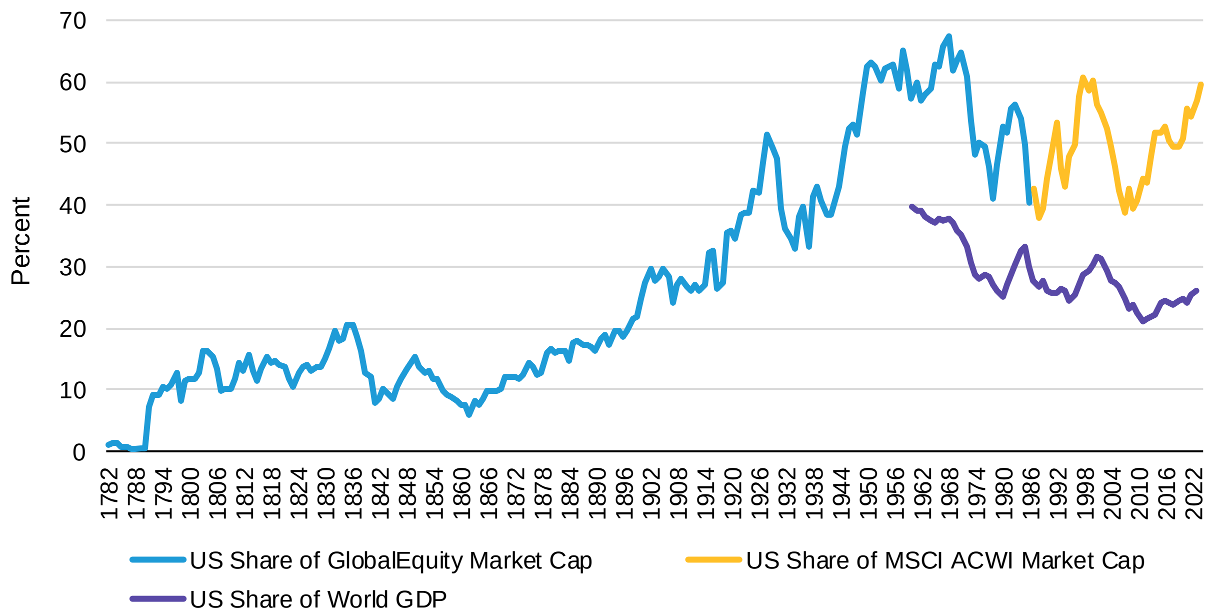
For illustrative purposes only.

S&P Capital IQ data as of December 2022; most recent data from US Census Bureau, *Statistics of US Businesses* (2017), used to triangulate S&P Capital IQ estimates for privately held company counts by revenue band

Source: Bain & Company, S&P Capital IQ, US Census Bureau and AB

Another aspect of concentration is the weight of the US in world indices (*Display 11, page 10*). Some of this concentration reflects the success of mega-cap tech names, but much of it reflects the superior growth of the US compared with the rest of the world. How does this translate into future expectations? The presence of "expensive" stocks with large weightings in the US market means that some of the US country weight is exposed to mean-reversion risk. However, we argue that the influence on the large US weight that comes from superior earnings is much more sustainable. The big downward risks to global growth are shrinking working-age populations, deglobalization and climate change. On all of these issues, the US faces less risk than many other countries. So one should not expect a significant shrinkage in US equity market share anytime soon.

DISPLAY 11: WEIGHT OF THE US IN GLOBAL EQUITY MARKETS



For illustrative purposes only.

Through August 31, 2024

Source: Global Financial Data, MSCI, Thomson Reuters Datastream and AB

Who is to say what the "correct" weight of the US is, anyway? GDP is as good a reference as any. There is a *prima facie* case that the weight of the US in global equity markets looks odd in comparison with global GDP share. The US weight in the MSCI ACWI has risen from 43% to nearly 60% since the late 1980s, but its weight in global GDP has fallen from 28% to 26% over the same period. The ratio of market cap to GDP is sometimes referred to as the "Buffett indicator" for valuation, so this might not seem an auspicious position for the US. However, the use of market cap/GDP as an indicator is of more use as a ratio for a single country over time rather than a comparison between countries. The relative size of the Chinese and US equity markets to their economies is a reflection of how capital is raised to fund growth. It is unlikely that China would adopt a US style of public equity capital raising anytime soon, so again, we think that this element of a relatively concentrated equity market versus GDP will likely remain intact for a long time.

3. What Does This Mean for Investors?

If most of the market move is a function of a handful of stocks, it is very hard to have superior knowledge about them and hard to overweight them. Thus, this recent period of concentration has not been a good environment for active investing. On the other hand, is it great for passive investments? In the sense that the US market happens to have delivered strong returns, passive investors have had a good experience. The cost of not having full exposure to the US in a global portfolio—or of not having full exposure to US mega-caps—would have been devastating for performance, as many investors have now ruefully learned. But on a forward-looking basis, things are not so rosy. The concentration of returns does make an investment in the passive market riskier.

We will get pushback on this point: “Is the market really riskier? I mean, really?” If one looks at realized volatility, aside from a flare-up in August, there has been a surprising lack of volatility in practice. So what is the basis of the claim that *ex ante* risk of a passive market position has risen? We think there are three elements:

1. We think that recent volatility has been odd, and sits oddly with the overall environment. High valuations do not necessarily lead to a market sell-off, but they do point to an increase in volatility. If we layer on the degree of macro uncertainty (in particular the extent to which growth in the US is slowing), then we think there is a strong case that realized volatility will be higher over the next year. We discuss this point in more detail in Deleveraging or Heralding a Recession?.

2. Concentration has a role to play in the risk of a drawdown. In *Display 12*, we show the result of running a simple regression on the two- or five-year-forward drawdown (in the US) on starting levels of the Shiller PE ratio and market concentration. This is a simple model, but it demonstrates that concentration is a predictor of drawdown risk over and above the level of starting valuation. The reason can be thought of as the exposure to the “torpedo risk” of a large company underperforming expectations and having an outsize impact on the index.

DISPLAY 12: EQUITY MARKET CONCENTRATION AND DRAWDOWNS

Two-Year Forward S&P 500 Drawdown Variables	T-Stat
Starting Weight of US Top 10 Stocks	–5.76
Starting Shiller PE Ratio	–9.57
Adjusted R^2	14%

Five-Year Forward S&P 500 Drawdown Variables	T-Stat
Starting Weight of US Top 10 Stocks	–5.99
Starting Shiller PE Ratio	–12.83
Adjusted R^2	22%

Past performance does not guarantee future results.

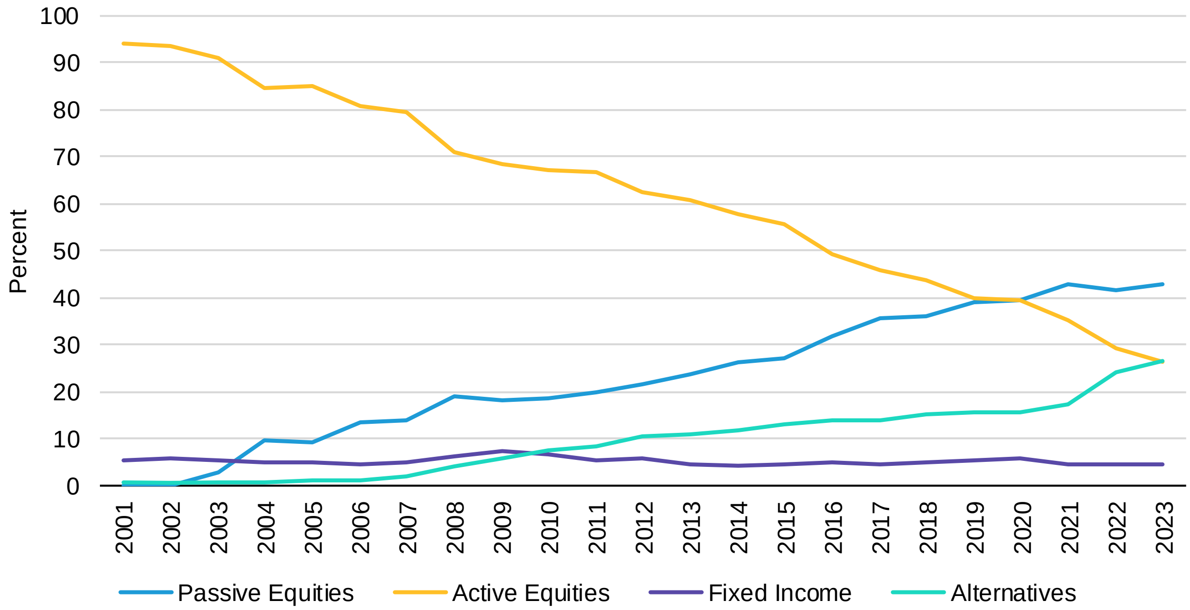
The regression covers the period from June 1969 to August 2024

As of September 15, 2024

Source: FactSet, Robert Shiller’s database, S&P and AB

3. Investors need to bear in mind that they are asking a lot more of the passive index than they have before. When one considers the barbell nature of asset allocation into passive public markets and active private markets, then the passive index is now the largest risk contribution to US pension fund portfolios (*Display 13, page 12*).

DISPLAY 13: RISK CONTRIBUTION FOR US PENSION FUNDS BY ASSET CLASS



Past performance does not guarantee future results.

For this graph we used the capital allocation of US pension plans as the base, and assumed that "alternatives" is a 50/50 combination of private equity and hedge funds. For private equity, we used a public-market-equivalent time series (essentially a smaller-cap, value-tilted index with leverage). For hedge funds, we used the HFRX Aggregate Index. Given the constraints on data availability for alternatives, we used a constant variance/covariance matrix over the full time period, rather than a rolling one. For fixed income, we used the Bloomberg Global Aggregate Total Return Index.

Through December 31, 2023

Source: Hedge Fund Research, Public Pension Plan Database, Thomson Reuters Datastream and AB

The key reason for owning equities is to deliver positive real growth in portfolios, especially in the context of higher equilibrium inflation. This is the core element driving our strategic overweight recommendation on equities. Is there a danger that this goal is imperiled if cap-weighted earnings growth is so divorced from growth in the economy? This is more of an open question: the attribute that equities must deliver in order to be attractive is a positive real return. Past experience suggests that the link to the real economy will reassert itself (albeit slowly) over time.

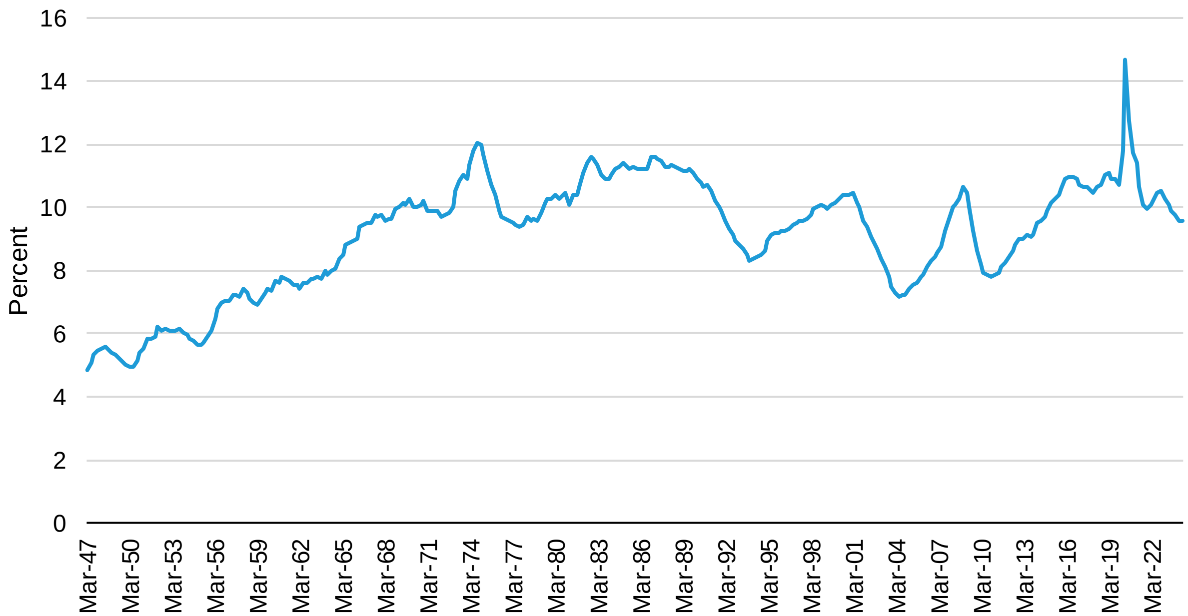
In conclusion, periods of concentration have not tended to persist in the past. To answer the question we posed at the beginning of this section, it seems reasonable to expect that the current concentration will not persist over strategic horizons and that, with time, the market will become less concentrated. Regulation and antitrust-like actions may well be a part of this, though there may also be limits in an age when national tech champions are possibly seen as an advantage in geopolitical rivalries. The concentration does suggest that risk has gone up, in contrast to recent low volatility. Investors with a short time horizon and therefore concerned about drawdowns may wish to compensate for this risk elsewhere in their allocation, but it does not undo the case for equities overall.

4. How High Can the Allocation to Private Assets Go?

Our view is that the migration to private assets is not just a fad, with two types of forces implying that mean private allocations will continue to rise. First, there is demand from investors. We see this as driven by the need for real returns and the hunt for diversification in a world where bonds are likely to be less good diversifiers of equity risk. To be clear, we see the diversifying power of private assets as arising from the ability to access parts of the economy that are not listed in public markets, not arising from stale prices. A second force supporting higher private allocations is supply. In this case, "supply" refers to the capital-raising needs of corporations. With progressively smaller shares of capital in the contemporary economy being raised in public markets or from bank credit, corporations are inevitably looking to private capital.

The size of the US commercial loan market as a share of GDP has been flat for decades and has shrunk over the last five years (*Display 14*). With banks likely stepping back further from credit provision, other sources of funding will have to increasingly step into the market.

DISPLAY 14: COMMERCIAL LOANS AS A PERCENTAGE OF GDP



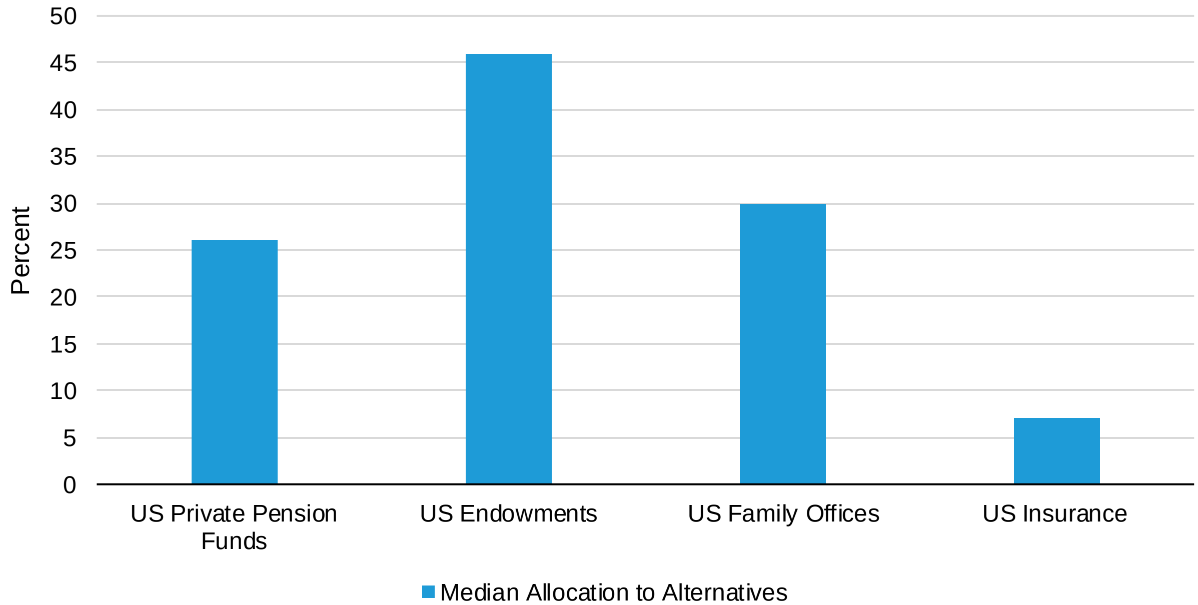
For illustrative purposes only.

Through June 30, 2024

Source: FRED and AB

The significant inflows to private assets in recent years have pushed institutional allocations up (*Display 15, page 13*). For US pension funds, allocations are above 25%; endowments are above 45%. For insurance, the allocation averages less than 10%. For all these categories, the commentary we hear in meetings with investors is that private asset allocation is set to rise.

DISPLAY 15: INSTITUTIONAL INVESTOR ALLOCATION TO ALTERNATIVES



For illustrative purposes only.

As of July 30, 2024

Source: Preqin Pro and AB

The main caveat that we have outlined elsewhere is that we no longer see a case for an illiquidity premium being available, on average, for private equity—the category that has received the lion share of inflows. Thus, we think that the marginal dollar of private capital from here is likely headed into other areas.

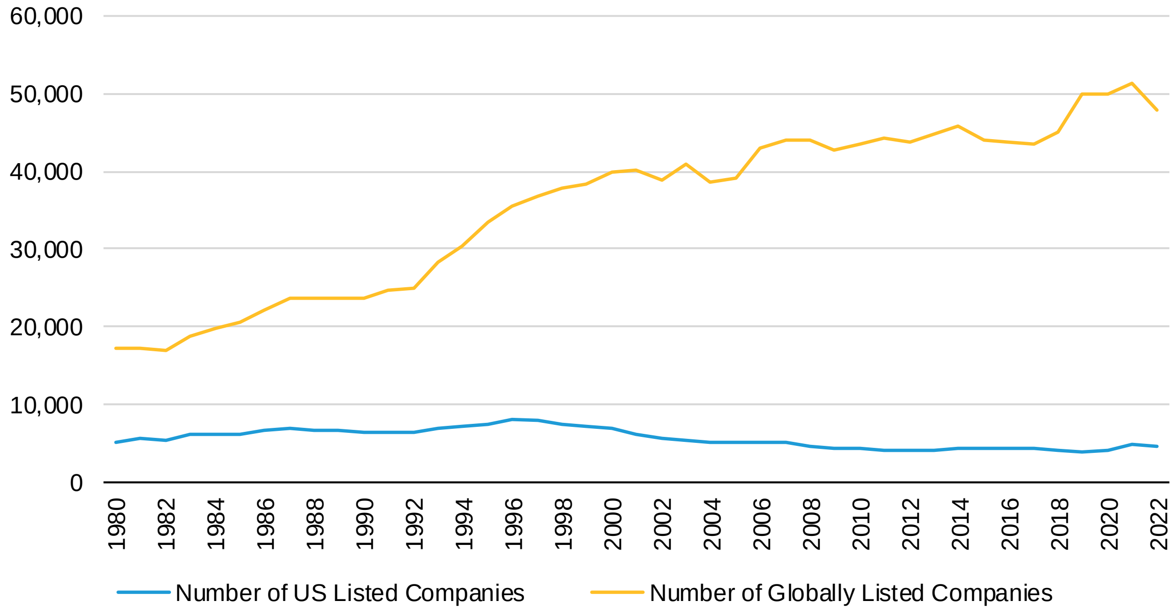
5. De-equitization: How Far Can the Public Equity Market Shrink?

The levering up of the financial system is a recurring theme in this note. We opened with the obvious levering of public finances; we close with a somewhat more subtle levering that comes through a shrinking stock of equity.

The number of listed shares in the world is declining. In developed markets such as the US, the number of companies that are publicly listed has fallen over time. If we include emerging markets, then there has been a trend increase in the number of listed companies (as one would expect in growing economies with capitalist systems), but it has slowed markedly over the last decade (*Display 16*). The real de-equitization story, though, is the reduction in the number of shares for companies that are listed. On this basis, equity markets have become significantly smaller. Yes, the price has gone up, but the number of shares has decreased. For the US, the number of shares has declined by around 2% annualized since peaking in 1996 (*Display 17*).

Even when we include emerging markets, the only meaningful increase in the number of shares for the MSCI ACWI in the last decade occurred around the time a change was made in the index inclusion factor for Chinese equities. We regard that change as not economically meaningful, at least not in the sense of the underlying supply of equity capital. This lack of growth in the number of shares for emerging markets is all the more striking because these markets presumably need capital to fund growth.

DISPLAY 16: NUMBER OF LISTED COMPANIES—GLOBAL AND US

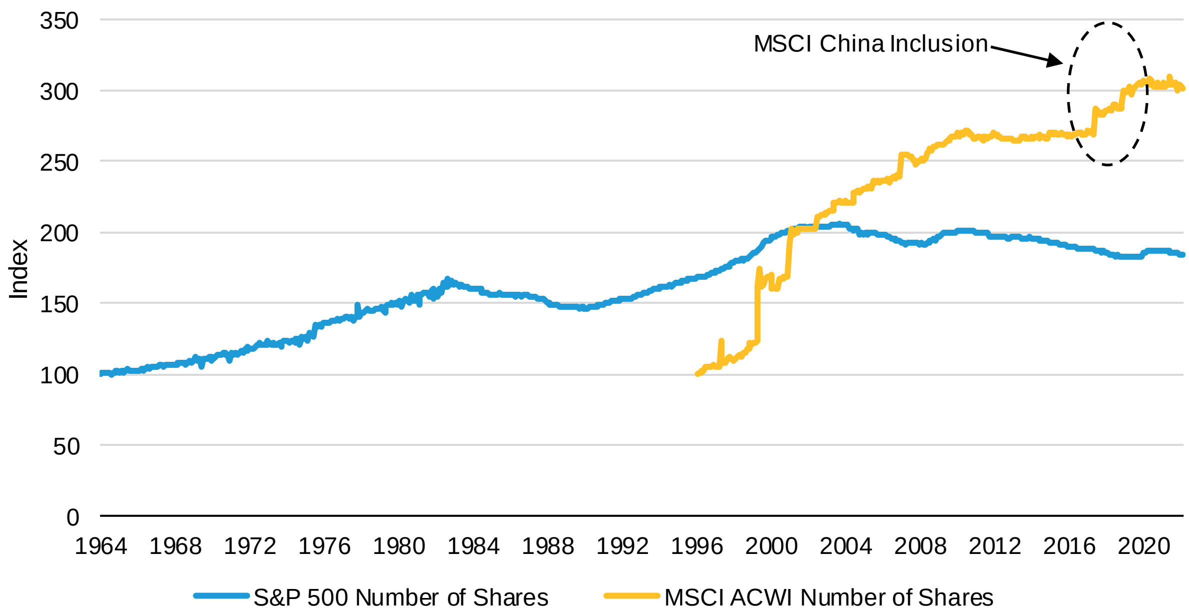


For illustrative purposes only.

Through December 31, 2022

Source: Thompson Reuters Datastream, World Bank and AB

DISPLAY 17: THE NUMBER OF LISTED SHARES IS DECLINING IN DEVELOPED MARKETS AND ONLY RISING IN EM BECAUSE OF AD HOC CHANGES IN THE CHINA INDEX INCLUSION FACTOR



For illustrative purposes only.

The circled area shows the impact of the change in the MSCI inclusion factor for China equities.

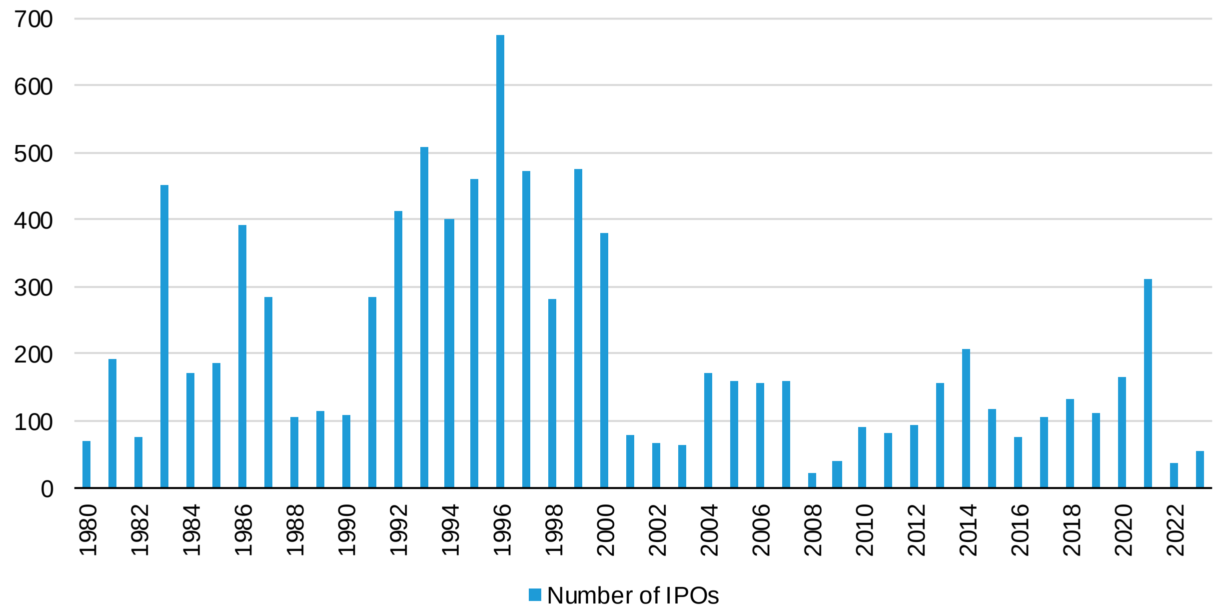
Through February 28, 2023

Source: MSCI, S&P, Thompson Reuters Datastream, World Bank and AB

There are two distinct forces driving this decline—a lack of new issuance and corporate buybacks—making the pattern more likely to persist.

In *Display 18 and Display 19*, *page 17,* we show the number of initial public offerings (IPOs) each year in the US and their size as a percentage of listed firms. The run rate of issuance is 1/10th of what it was in the '80s and '90s. Reasons include firms eschewing the disclosure requirements of public listing and the way that corporate capex has switched from tangible to intangible assets that require less upfront capital. On this latter point, there are tentative signs of a capex renaissance associated with the grid, renewable energy and the infrastructure needs of AI (*Display 20, page 17*).

DISPLAY 18: NUMBER OF NEW IPOS

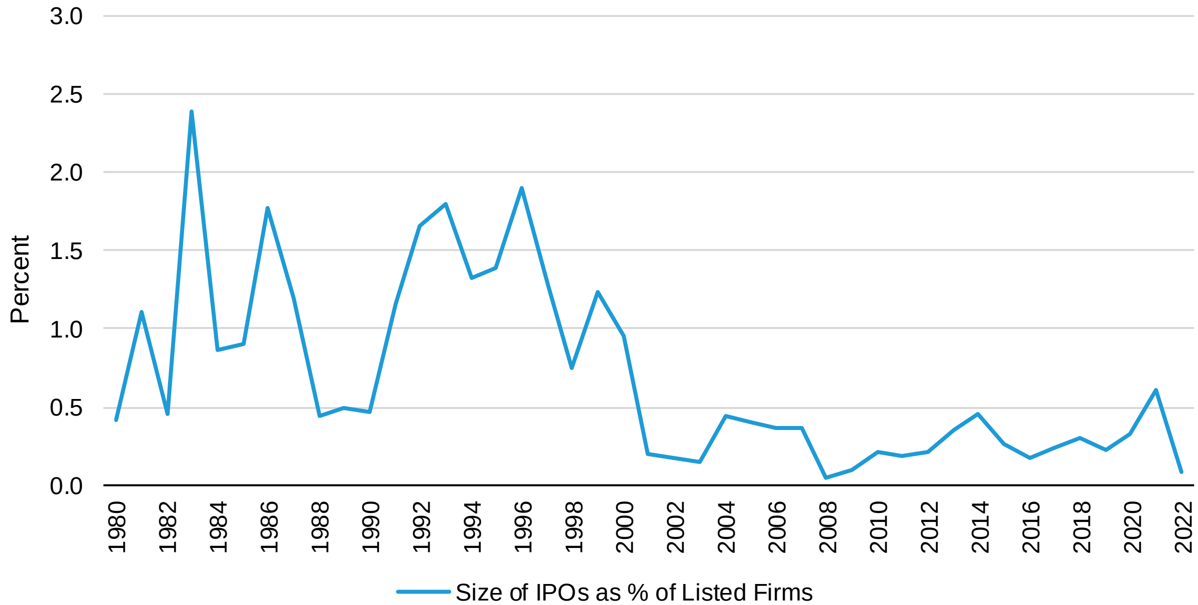


For illustrative purposes only.

As of December 31, 2023

Source: Jay R. Ritter, *Initial Public Offerings: Updated Statistics*, May 10, 2024; Thomson Reuters; World Bank; and AB

DISPLAY 19: SIZE OF NEW IPOS AS A PERCENTAGE OF MARKET CAP

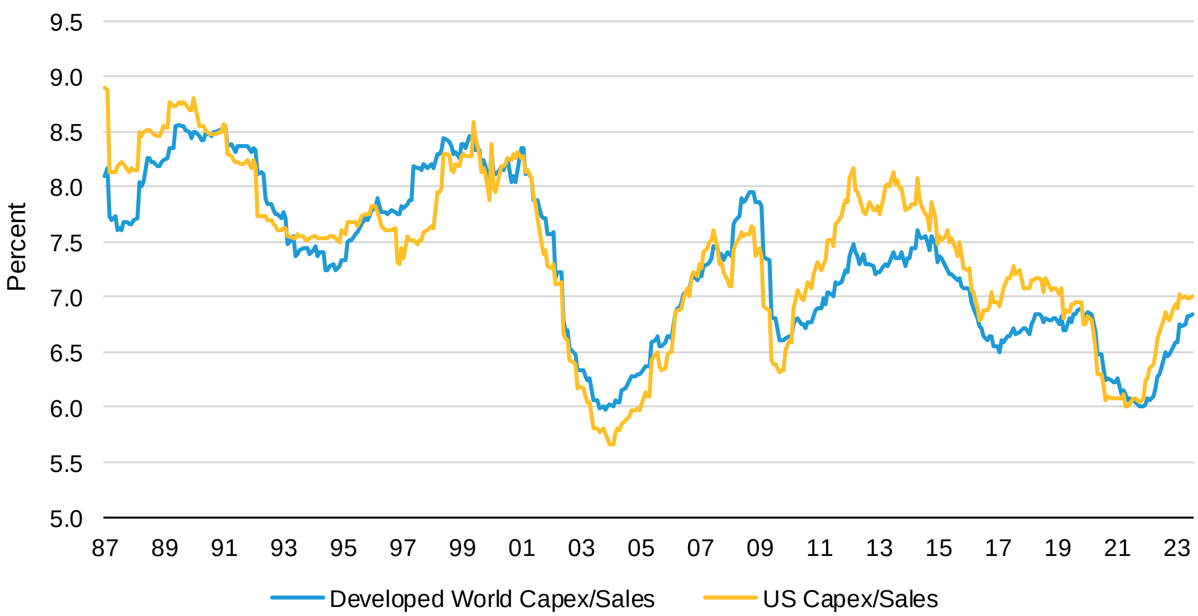


For illustrative purposes only.

Through December 31, 2022

Source: Jay R. Ritter, *Initial Public Offerings: Updated Statistics*, May 10, 2024; Thomson Reuters; World Bank; and AB

DISPLAY 20: TENTATIVE SIGNS OF A CAPEX RENAISSANCE?



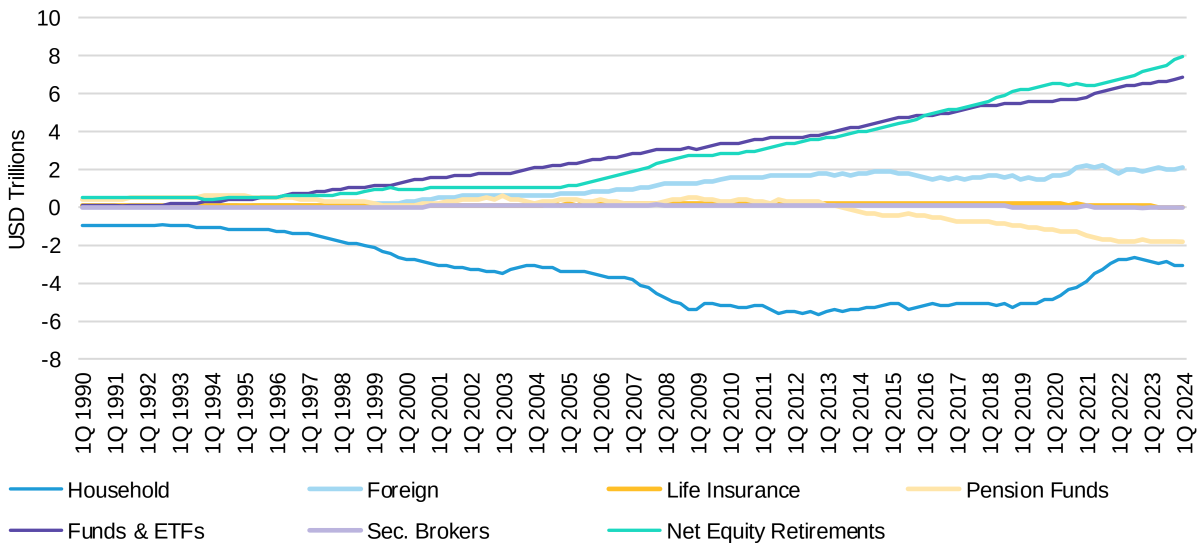
For illustrative purposes only.

Through July 31, 2024

Source: FactSet and AB

The other force at work is, of course, buybacks. Corporations have been the largest source of equity buying for over a decade, outstripping demand from investors (*Display 21, page 18*). Although this trend is further advanced in the US, it is now an embedded feature of all developed equity markets. It is a response to the perceived opportunity set versus the cost of capital, but more fundamentally it reflects a corporate system in which many of the key performance indicators that determine management pay are often couched in per-share terms. This represents a negative externality at the system level—the resilience of the economy is not reflected in incentives at the company level.

DISPLAY 21: CUMULATIVE NET ACQUISITION OF US CORPORATE EQUITIES, 1990–2024



For illustrative purposes only.

Pension Funds: Government, state and local and private pension funds

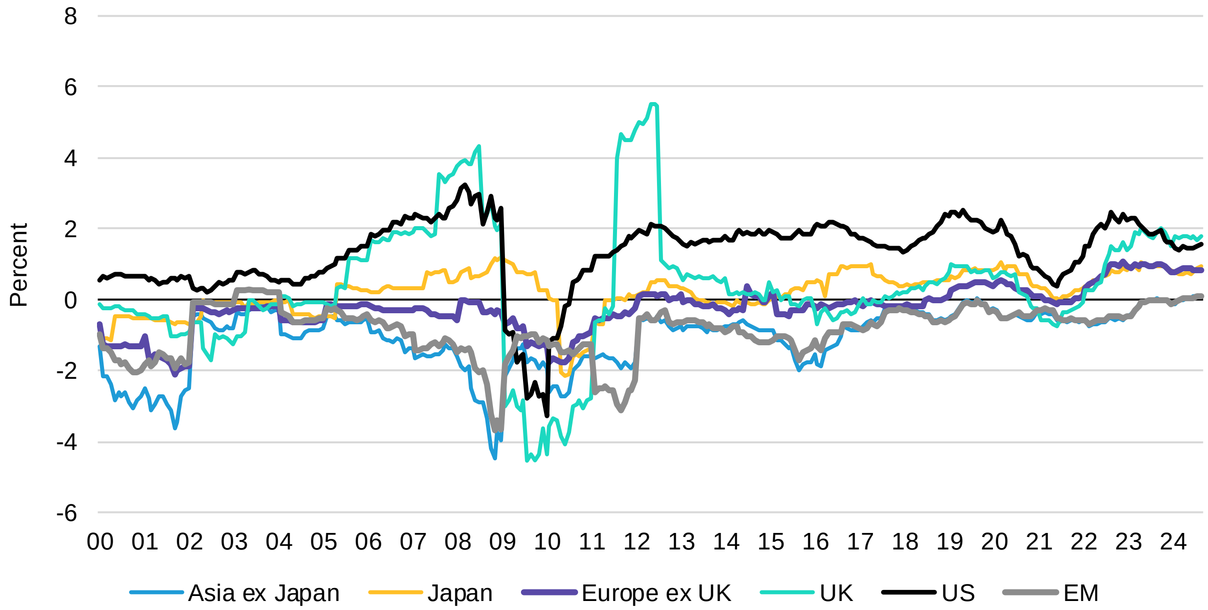
Funds & ETFs: Mutual funds, closed-end funds and ETFs

Through March 31, 2024

Source: Thomson Reuters Datastream, US Federal Reserve Board and AB

Looking across regions, there is a clear pattern of developed markets seeing a shrinking number of shares, but also a slight expansion in the share base (at least historically, if not recently) for emerging markets. There are two ways to estimate thi s. One can either calculate the average net buyback yield over time or compute the change in the number of indexed shares over time. On this basis, while the US saw the strongest consistent shrinkage in the number of listed shares, it was a feature of other developed markets too. Japan, for instance, has had an average net-buyback yield over the last decade of 0.6% annualized and a reduction in the number of indexed shares of 0.4% annualized. For the UK, these numbers were 0.5% and 0.3%, respectively. For Asia ex Japan (dominated by China), the average net issuance yield has been –0.6% over the last 10 years, with the number of indexed shares increasing by 1.4% (*Displays 22 and 23, page 19*).

DISPLAY 22: NET BUYBACK YIELD BY REGION

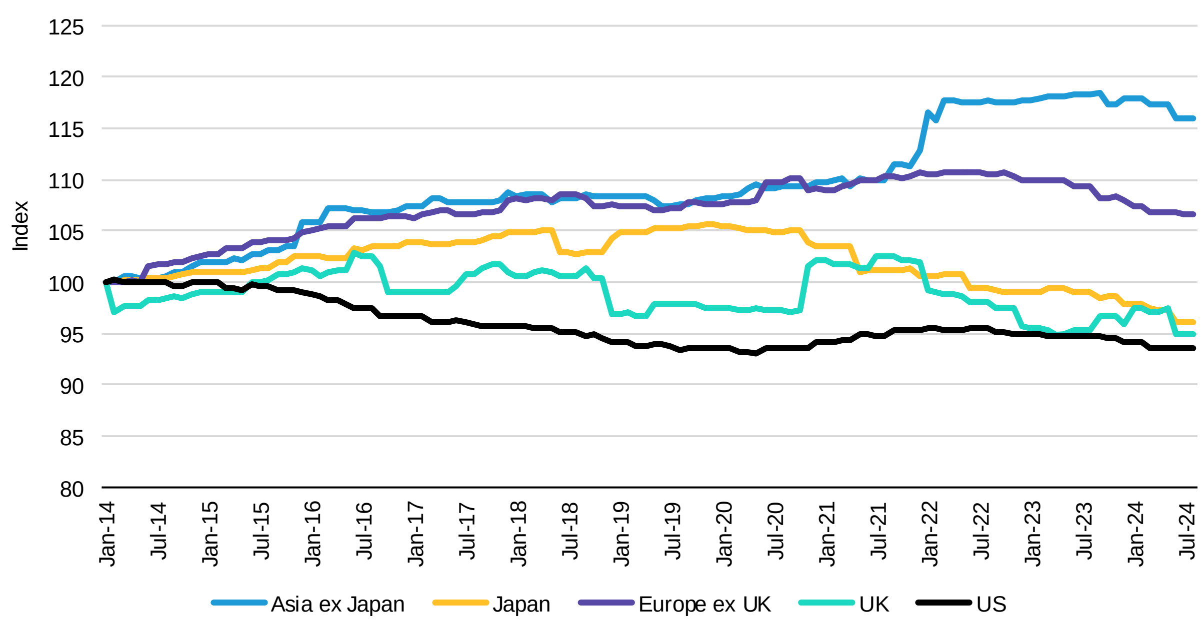


For illustrative purposes only.

Through September 9, 2024

Source: FactSet and AB

DISPLAY 23: QUANTIFYING DE-EQUITIZATION (CHANGE IN NUMBER OF SHARES BY REGION)



For illustrative purposes only.

Through August 31, 2024

Source: MSCI, Thomson Reuters Datastream and AB

Is the stock market actually shrinking? One client in a recent meeting rejected that assertion from us, because market cap has continued to rise as prices have gone up much faster than the number of shares has come down. We think that the number of companies and shares does matter, because their reduced number implies scarcity. But even if one rejects such a view, the increase in total market cap in recent years is really just a happenstance of a recent bullish history. Thus, in forming forecasts of equity returns, we think this reduction in supply is an important pervasive factor.

Public equity (along with bank credit) had been the major source of capital to fund growth since WWII. However, in the contemporary economy, the role of public equity (and bank credit) is shrinking.[2] The net reduction in the supply of equity, buybacks in particular, are an example of levering up the system. This is not isolated and must be put in the context of other levering up taking place in parallel. The level of public debt/GDP has gone up in a straight line since the ending of the gold standard in the early '70s. The presence of a cushion of liquid equity capital is, we would argue, a public good, and its removal creates negative externalities. As with the growth of public debt, there is no theoretical level that constitutes a definitive problem. It just makes the system less robust.

If governments wanted to curtail this process, there is one blunt option: a tax on buybacks. This approach occasionally appears on the political radar in different countries. Most recently, the Liberal Democrats in the UK issued a manifesto prior to the general election calling for a 4% tax on buybacks.[3] They didn't get in, but the effort is an example of politicians perhaps starting to notice the issue. A more subtle approach would be to steer management's key performance indicators away from per-share metrics that can be manipulated by buybacks. As both these options appear to be unlikely prospects at the moment, public equities are likely to continue to benefit from the steady tailwind of a net reduction in supply.

2 See Inigo Fraser-Jenkins et al., *Fund Management Strategy: What Is the Point of the Stock Market (in a Capital Light World)?* Bernstein Research, April 17, 2019.

3 Liberal Democrats, "A Share Buyback Tax to Boost Growth and Fund Public Services," May 31, 2024.

Nashville	**New York**	**London**	**Singapore**
501 Commerce Street Nashville, TN 37203 United States (615) 622 0000	66 Hudson Boulevard East New York, NY 10001 United States (212) 969 1000	60 London Wall London EC2M 5SJ United Kingdom +44 20 7470 0100	One Raffles Quay #27-11 South Tower Singapore 048583 +65 6230 4600
Tokyo	**Toronto**	**Sydney**	**Hong Kong**
Hibiya Parkfront 14F 2-1-6 Uchisaiwaicho, Chiyoda-ku Tokyo, 100-0011, Japan +81 3 5962 9000	200 Bay Street, North Tower Suite 1203 Toronto, Ontario M5J 2J2, Canada (647) 375 2803	Level 32, Aurora Place 88 Phillip Street Sydney NSW 2000 Australia +61 02 9255 1200	39th Floor, One Island East, Taikoo Place 18 Westlands Road Quarry Bay, Hong Kong +852 2918 7888

For Investment Professional use only. Not for inspection by, distribution or quotation to, the general public.

The value of an investment can go down as well as up, and investors may not get back the full amount they invested. Capital is at risk. Past performance does not guarantee future results.

Important Information

The information contained herein reflects the views of AllianceBernstein L.P. or its affiliates and sources it believes are reliable as of the date of this publication. AllianceBernstein L.P. makes no representations or warranties concerning the accuracy of any data. There is no guarantee that any projection, forecast or opinion in this material will be realized.

The views expressed herein may change at any time after the date of this publication. AllianceBernstein L.P. does not provide tax, legal or accounting advice. It does not take an investor's personal investment objectives or financial situation into account; investors should discuss their individual circumstances with appropriate professionals before making any decisions.

References to specific securities are provided solely in the context of the analysis presented and are not to be considered recommendations by AllianceBernstein. AllianceBernstein and its affiliates may have positions in, and may effect transactions in, the markets, industry sectors and companies described herein.

MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indices or any securities or financial products. This report is not approved, reviewed or produced by MSCI.

Note to All Readers: The information contained here reflects the views of AllianceBernstein L.P. or its affiliates and sources it believes are reliable as of the date of this publication. AllianceBernstein L.P. makes no representations or warranties concerning the accuracy of any data. There is no guarantee that any projection, forecast or opinion in this material will be realized.

Note to Readers in Canada: AllianceBernstein provides its investment-management services in Canada through its affiliates Sanford C. Bernstein & Co. LLC and AllianceBernstein Canada, Inc. It should not be construed as advice as to the investing in or the buying or selling of securities, or as an activity in furtherance of a trade in securities. **Note to Readers in the United Kingdom:** Issued by AllianceBernstein Limited, 60 London Wall, London EC2M 5SJ, registered in England, No. 2551144. AllianceBernstein Limited is authorised and regulated in the UK by the Financial Conduct Authority (FCA). **Note to Readers in Europe:** This information is issued by AllianceBernstein (Luxembourg) S.à r.l. Société à responsabilité limitée, R.C.S. Luxembourg B 34 305, 2-4, rue Eugène Ruppert, L-2453 Luxembourg. Authorised in Luxembourg and regulated by the Commission de Surveillance du Secteur Financier (CSSF). **Note to Readers in Switzerland:** This information is directed at Qualified Investors only. Issued by AllianceBernstein Schweiz AG, Zürich, a company registered in Switzerland under company number CHE-306.220.501. AllianceBernstein Schweiz AG is a financial service provider within the meaning of the Financial Services Act (FinSA) and is not subject to any prudential supervision in Switzerland. Further information on the company, its services and products, in accordance with Art. 8 FinSA can be found on the Important Disclosures page at AllianceBernstein.com. **Note to Readers in Australia and New Zealand:** For Institutional Investor use only. Not for inspection by, distribution or quotation to, the general public. This document has been issued by AllianceBernstein Australia Limited (ABN 53 095 022 718 and AFSL 230698). Information in this document is intended only for persons who qualify as "wholesale clients," as defined in the Corporations Act 2001 (Cth of Australia) or the Financial Advisers Act 2008 (New Zealand), and should not be construed as advice. **Note to Readers in Hong Kong:** For Institutional Investor use only. Not for inspection by, distribution or quotation to, the general public. The issuer of this document is AllianceBernstein Hong Kong Limited (聯博香港有限公司). This document has not been reviewed by the Securities and Futures Commission. **Note to Readers in Japan:** For Institutional Investor use only. Not for inspection by, distribution or quotation to, the general public. This document has been provided by AllianceBernstein Japan Ltd. AllianceBernstein Japan Ltd. is a registered investment-management company (registration number: Kanto Local Financial Bureau no. 303). It is also a member of the Japan Investment Advisers Association; the Investment Trusts Association, Japan; the Japan Securities Dealers Association; and the Type II Financial Instruments Firms Association. The product/service may not be offered or sold in Japan; this document is not made to solicit investment. **Note to Readers in Singapore:** For Institutional Investor use only. Not for inspection by, distribution or quotation to, the general public. This document has been issued by AllianceBernstein (Singapore) Ltd. ("ABSL", Company Registration No. 199703364C). AllianceBernstein (Luxembourg) S.à r.l. is the management company of the Portfolio and has appointed ABSL as its agent for service of process and as its Singapore representative. AllianceBernstein (Singapore) Ltd. is regulated by the Monetary Authority of Singapore. This advertisement has not been reviewed by the Monetary Authority of Singapore. **Note to Readers in Taiwan:** For Institutional Investor use only. Not for inspection by, distribution or quotation to, the general public. This document is provided solely for informational purposes and is not investment advice, nor is it intended to be an offer or solicitation, and does not pertain to the specific investment