AB Discovery Value Fund

Advisor Class: ABYSX

Market Overview

The Russell 2500 Value Index rose 6.07% during the quarter. US equities rallied throughout the first quarter as recessionary fears ebbed and soft-landing optimism gained momentum, bolstered by tailwinds from US Federal Reserve and global central bank rate-cut hopes, a resilient US economy, and the continuation of artificial intelligence (AI) enthusiasm.

In January, hopes that the Fed might signal an initial rate cut as soon as March diminished as fourth-quarter GDP continued to grow well above estimates, manufacturing activity moved back into expansionary territory and personal spending remained strong. Later in the quarter, rate-cut expectations accelerated and soft-landing optimism in the US prevailed despite firmer inflation readings for January and February. Fed Chair Powell affirmed that inflation was “moving down gradually on a sometimes bumpy road toward 2%,” and the Fed’s quarterly Summary of Economic Projections dot plot continued to show three rate cuts during 2024, suggesting the uptick in price pressures hadn’t shifted its projections. At the end of the month, the Fed’s preferred inflation gauge, the Core Personal Consumption Expenditures Price Index, rose in line with expectations, leaving the door open for a possible June rate cut. Similarly, the European Central Bank is also on track to cut rates as early as June, and ECB President Christine Lagarde acknowledged that discussions about rate-cut timing have begun.

US mega-cap technology companies led the fourth-quarter reporting season as AI enthusiasm continued to underpin better-than-anticipated earnings results. More broadly, factors such as lower input costs, stepped-up efficiencies and cost controls, and previously lowered expectations helped many companies surpass profit estimates. Results were tempered somewhat by an uptick in cautionary guidance for the first quarter and full year 2024 in anticipation of slowing economic growth and weaker consumer spending. But as the quarter closed, the stock market rally broadened as investors gained confidence that the Fed could rein in inflation and begin to cut rates without triggering a recession after it raised its projections for economic growth.

During the quarter, both growth- and value-oriented stocks rose in absolute terms, but growth stocks—led by the technology sector and AI optimism—outperformed value stocks on a relative basis (as measured by the Russell 1000 Growth and Value indices). Sector performance for the Russell 2500 Value was mostly positive, led by energy and industrials. Real estate and communication services were the only negative sectors during the quarter.

Fund Performance

The Discovery Value Fund rose in absolute terms and outperformed its benchmark, the Russell 2500 Value, during the quarter. Both sector and stock selection contributed to relative performance. Stock selection within consumer discretionary and financials contributed the most, while selection in healthcare and technology detracted.

Dick’s Sporting Goods contributed after the retailer reported fiscal 4Q:23 earnings and revenues that beat expectations. The beat was driven by strong same-store sales growth as company level initiatives more than offset less favorable weather.

Gates Industrial, which makes engineered power transmission and fluid systems for automotive and industrial customers, contributed after reporting stronger-than-expected 4Q:23 results. The company’s shares also benefited from the positive 1Q:24 guidance the company gave in a subsequent analyst day.

Criteo contributed after the global commerce technology company reporting 4Q:23 results that exceeded expectations driven by stronger revenue growth in its commerce media business. Also driving the shares was a letter to management from an activist shareholder asking for increased share buybacks and a strategic review of operations.

Shares of Calix detracted despite the broadband infrastructure provider reporting 4Q:23 earnings that beat expectations. Investors were more focused on the company's lower guidance for 1Q:24, driven by a number of customers who had paused their purchases early in 2024 as they waited for more information on upcoming additional subsidies for rural broadband.

Integra LifeSciences detracted after the medical device company reported broadly inline results but offered weaker 2024 guidance driven by supply chain bottlenecks. The company did note that its Boston facility, which had been closed for the second half of 2023 over quality control issues, was on track to be reopened in line with its previously stated timetable.

AMN Healthcare detracted as the nursing staffing company beat 4Q:23 earnings expectations but gave 1Q:24 revenue guidance that missed consensus. Demand for temporary nursing continues to fall from its peak pandemic levels although management indicated they believe this demand is now closer to normal levels.

Outlook

Smaller-cap stocks and value stocks more broadly have struggled versus larger-caps and growth for the past two years and much of the past eight years. Despite this underperformance, fundamentals have remained strong among these companies with solid earnings and cash flows. As a result, valuation of smaller-cap value stocks relative to larger-cap growth is now at a discount not seen since the peak of the tech bubble. The questions investors are asking as they look at value stocks are twofold. Why is this occurring and what will drive a recovery for the asset class? We believe the key to both questions lies in earnings.

Despite the market's improved confidence that the Fed's efforts to tame inflation will not push the US economy into a recession, investor concerns remain. The most tangible manifestation of this has been the exceptional performance of a small number of mega-cap stocks with immense scale or perceived connection to trends such as artificial intelligence. Investors look at these companies as having earnings profiles that can grow regardless of how the US economy performs. In contrast, smaller-cap value stocks have underperformed dramatically over the past two years as investors remain concerned that a sluggish US economy will drag their earnings down.

The breadth and magnitude of this sell-off has created a provocative set of opportunities in smaller-cap markets. To be clear, some smaller-cap value stocks do have more cyclical exposures and will see negative earnings revisions in a slower growth US economy. Others, however, have much stronger earnings profiles. Specifically, we believe stocks with strong quality characteristics or those with exposure to dramatic shifts occurring in the US economy are well positioned in the current environment.

Stocks with attractive quality characteristics such as industry leading business models, high profitability or strong balance sheets can leverage these strengths to outpace weaker competitors and grow earnings. They can invest in new projects or businesses more easily and more cheaply than their highly levered competitors—a key differentiator given the higher level of interest rates. Further, their strong profitability points to competitive advantages in market share, cost structure and capital usage, which will all be sources of earnings growth in a more uncertain climate.

We believe that companies with exposure to the emerging trends of onshoring and energy transition and security also enjoy advantages over less well positioned peers. Our research suggests that the shift in the US economy away from globalization will require considerable spending in infrastructure to make supply chains and energy sources more secure. The scope of this spending is significant given the underinvestment in these areas over the past several decades. While some of this increase will come from politically dependent stimulus programs, much of it is broader based in nature driven by a desire to de-risk vital supply chains and improve energy reliability.

Top Ten Holdings*	Portfolio %
Builders FirstSource	1.93
Dick's Sporting Goods	1.70
PVH	1.68
First Citizens BancShares	1.65
Nexstar Media Group	1.51
PulteGroup	1.50
Bath & Body Works	1.48
Jones Lang LaSalle	1.46
The Middleby	1.45
MasTec	1.42

Please refer to the following legal disclosures.

*Based on a representative account as of 03/31/24. Holdings, characteristics and weightings (which are equity only weightings and excluding cash) will vary over time. They are provided for informational purposes only and should not be deemed as a recommendation to buy or sell the securities mentioned.

A WORD ABOUT RISK

Market Risk: The market values of the portfolio's holdings rise and fall from day today, so investments may lose value. **Capitalization Size Risk (Small/Mid):** Small- and mid-cap stocks are often more volatile than large-cap stocks—smaller companies generally face higher risks due to their limited product lines, markets and financial resources. **Foreign (Non-US) Risk:** Non-US securities may be more volatile because of political, regulatory, market and economic uncertainties associated with such securities. Fluctuations in currency exchange rates may negatively affect the value of the investment or reduce returns. These risks are magnified in emerging or developing markets. **Derivatives Risk:** Investing in derivative instruments such as options, futures, forwards or swaps can be riskier than traditional investments, and may be more volatile, especially in a down market.

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.

Investors should consider the investment objectives, risks, charges and expenses of the Fund/Portfolio carefully before investing. For copies of our prospectus or summary prospectus, which contain this and other information, contact your AB representative. Please read the prospectus and/or summary prospectus carefully before investing.

Investment Products Offered: Are Not FDIC Insured | May Lose Value | Are Not Bank Guaranteed

The Russell 2500 Value Index represents the performance of small- to mid-cap value companies within the US.

An investor cannot invest directly in an index and its performance does not reflect the performance of any AllianceBernstein portfolio. The unmanaged index does not reflect fees and expenses associated with the active management of a portfolio.

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