To Our Clients:

It’s well known that markets, at their extremes, are driven by investor fear and greed. But it’s less well understood that these very different emotions can lead to strikingly similar investor behaviors, especially in the heat of the moment. When either fear or greed begins to unwind, investment opportunity is created, especially for research-driven security selection; we believe that such a period lies ahead.

The More Things Change…

About 15 years ago, in the late ‘90s, the US stock markets were dominated by high-flying technology companies—soon to become a full-fledged investor mania. Prior to the inflation of the “dot-com” bubble, technology companies represented about 10% of the capitalization of the S&P 500. By the time of the market peak in 2000, technology stocks were responsible for more than one-third of the index, which itself was trading at an eye-popping 26 times forward earnings. With greed ruling the day, it seemed that all a company had to do was slap “.com” at the end of its name, and its share price would explode.

Today, six years after the global financial crisis, most financial assets have had strong multiyear runs. Many investors don’t realize that equity appreciation has generally tracked the recovery of corporate earnings. And on a global basis, stocks don’t look particularly expensive relative to their own history despite the gains of the last few years.

Getting less attention is the success of what we call “safety stocks”—those that usually offer higher income and are backed by more-stable earnings and more-predictable business models. Utility companies, for example, prized for their secure dividends, entered 2014 trading at near-record valuation multiples but still managed to lead all sectors of the S&P 500 for the year. Further, both healthcare and consumer staples, also traditionally more-defensive stocks, joined utilities among the top five sectors in the index last year. The evidence is persuasive that investors are willing to pay up for income and stability as they shy away from taking risk: With the pain of 2008 not yet dissipated, fear lingers in the market.

…The More They Remain the Same

The tech-bubble and the post-financial-crisis periods, both extreme, may seem very different. After all, the dot-com craze was dominated by greed, while fear is still present in the current market. But in both cases, investors herded together, chasing returns in popular sectors and industries. When that kind of trend-following dominates markets, as is the case today, history tells us that two things happen: Indexes are hard for active managers to beat, for a time, but opportunity is also created when the emotion that’s driving investor crowding begins to unwind (left display, reverse side).

We saw this in the aftermath of the dot-com bubble when tech darlings fell back to earth and so-called “Old-Economy” stocks rebounded strongly. And now, we believe that the continued recovery of economic fundamentals will once again focus investor attention on capital appreciation rather than safety. In the period we expect to see ahead, research-driven insights and discriminating security selection should trump tracking indexes and blindly following the crowd.
Ahead of Tomorrow

At Bernstein we take great pride in the fact that the core principles that defined our firm when we opened our doors in 1967 remain the same today. But we also know that the needs of our clients and opportunities in the capital markets are constantly changing.

With this in mind, we have introduced and refined many services over the last several years to enhance diversification, smooth volatility, and increase sources of return. In addition, we just redesigned our website with the goals of better connecting our clients to both our research insights and the growth of their assets in accord with their long-term plans.

We’ve also introduced a refreshed corporate logo (see top of reverse side of page), our first update in more than 10 years. We’re proud of our new suit, with a heart and soul underneath that remains as client-focused as ever…and never follows the crowd.

On behalf of everyone at Bernstein, best wishes for a happy, healthy, and prosperous 2015.

Sincerely,

David Barnard

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