THE MEGAPHONE EFFECT

AMPLIFYING THE IMPACT OF ENGAGEMENT WITH MANAGEMENT

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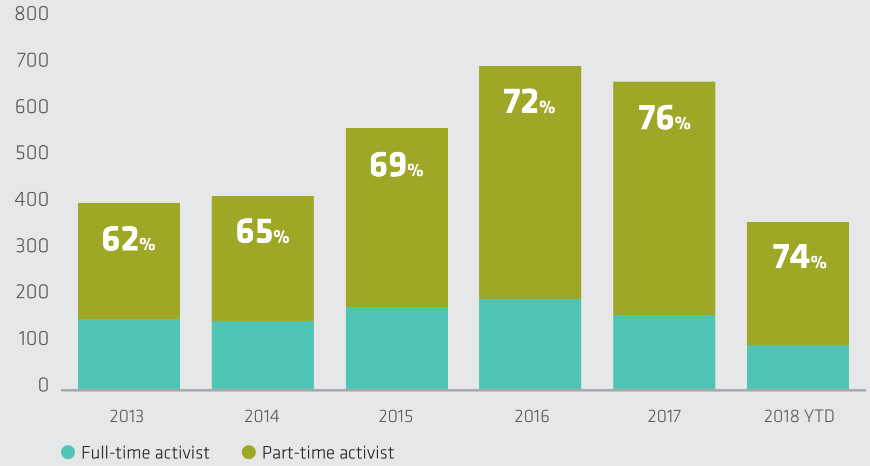
Equity investors are increasingly compelled to engage proactively with the management of publicly traded companies. When it's done right, engagement can help promote important changes in corporate behavior and help enhance shareholder returns. However, engagement tactics commonly used today have significant limitations. By understanding these shortcomings, we believe investors can focus on the right tools for effective engagement that delivers clear benefits for investors.

Industry data show that investors are indeed starting to step up on the engagement front with companies. There are 112 full-time activist funds globally, but 662 investors made public demands in 2017; only 54 of these investors use activism as their main strategy, according to Activist Insight, a data provider on global activist investing. The growth of activism is starting to be driven by the rise of "part-time" activists (*Display 1*).

DISPLAY 1: ENGAGEMENT GROWTH FUELED BY PART-TIME ACTIVISTS
Number of Global Public Shareholder Demands (2013–1Q:2018)



As of March 31, 2018
Source: Activist Insight

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

WHAT'S WRONG WITH ENGAGEMENT TODAY?

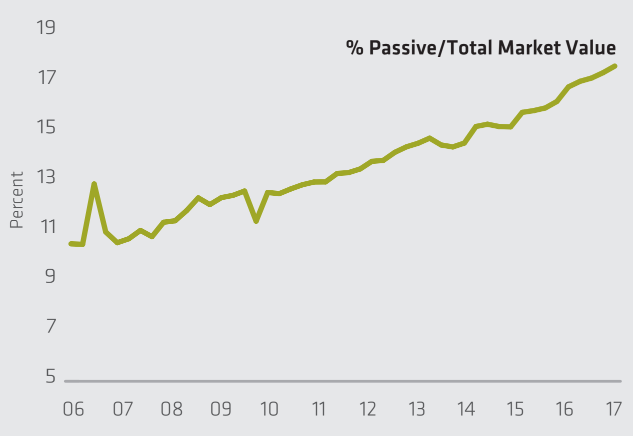
There are two types of engagement today that get the most attention.

First, there is the outspoken activist who frequently wages battle in the media. These types of investors use blunt instruments to make their case, and the dialogue with management is typically antagonistic.

Second, there are index funds or passive equity investors. They have no choice but to be heard, as they now own almost 20% of the outstanding shares of most large US companies (*Display 2*). If they remain silent, it will create an imbalance in the capital markets. However, index funds are not set up to evaluate individual holdings, so they can't really suggest company-tailored operational, capital allocation, or environmental, social and governance (ESG) improvements. What's more, as passive investors, they do not hold the ultimate stick because they cannot sell the stock if their views are not embraced.

DISPLAY 2: RISE OF PASSIVE ADDS TO ENGAGEMENT CHALLENGES

Total Market Value of US Aggregate Ownership Held by Index Funds (Percent)



Through December 31, 2017
Top 1,500 US equity funds
Source: Bernstein Research

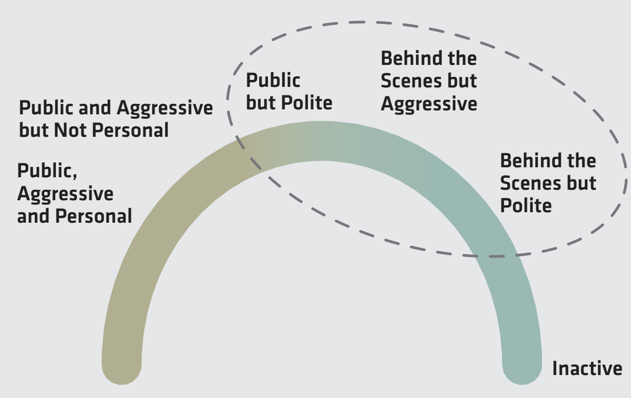
ACTIVE MANAGERS ARE PART OF THE SOLUTION

In our view, active equity managers are best positioned to stimulate change, to promote corporate improvements—and to increase the power of activist investing in the future.

At its core, good activist behavior is all about investing in companies that can improve their returns to shareholders, and helping those companies achieve their potential. Long-only managers, who spend their days researching stocks, should have a competitive advantage given their deep company-specific knowledge and strong industry relationships.

There are many different flavors of activism or engagement—from highly charged, aggressive, personal, public debates like proxy fights to behind-the-scenes negotiations (*Display 3*). But we think the best way for traditional active equity managers to get involved is by a two-way discourse. That doesn't mean investors should be chummy with management; rather, they should be comfortable delivering thoughtful, fact-based suggestions that bring outside perspectives to help companies improve.

DISPLAY 3: EFFECTIVE APPROACHES TO ENGAGEMENT



Source: AllianceBernstein (AB)

ENGAGEMENT IS PART OF INVESTING

Long-only investor engagement is a key component of an active investing tool kit, in our view. Our investment teams engage with company management teams on issues related to strategy and capital allocation almost every day. Last year, AllianceBernstein (AB) analysts around the world met with companies more than 100 times on ESG issues alone. We've used our voice to suggest that companies divest businesses that dilute their focus, refresh an entrenched board, rein in overly generous compensation packages, create environmentally and socially responsible supply chains, and replace underperforming members of management teams. ESG improvements are also becoming an important driver of stock performance, according to MSCI data (*Display 4*).

Voting proxies and deeper one-on-one idea exchanges are two tools of corporate engagement. Like all investment managers, we have institutional views on the major proxy issues. Our proxy policy, available on our corporate website, guides us in this arena. On this front, active and passive managers are equally involved on issues such as proxy access, classified boards, and splitting chairperson and CEO roles.

However, it is on the deeper and longer-horizon engagements that active managers shine. A passive manager is not incentivized to improve a business in the same way as an active manager is. Passive managers' principal focus is to deliver low-cost access to equity markets, so their holdings just match the index weighting for each stock. The emphasis on low fees means that costs must also be kept low. As a result, passive research departments are not staffed with experienced experts that know the ins and outs of each company. That's why index funds are noticeably absent from engagement based on fundamental research. In contrast, active managers invest heavily in research, because choosing stocks based on fundamental analyses encompasses the most important decisions that stock pickers make every day.

DISPLAY 4: ESG IMPROVEMENT INCREASINGLY DRIVES STOCK OUTPERFORMANCE

Portfolio of Improving ESG Stocks*

Relative Returns vs. MSCI World (January 2008–January 2017)

<table>
<tr><th>Yearly Rebalance (%)</th><th>Biennial (%)</th><th>Triennial (%)</th></tr>
<tr><td>0.82</td><td rowspan="2">1.84</td><td rowspan="3">3.16</td></tr>
<tr><td>6.71</td></tr>
<tr><td>–1.35</td><td rowspan="2">3.92</td></tr>
<tr><td>–0.30</td><td rowspan="3">–3.11</td></tr>
<tr><td>–2.78</td><td rowspan="2">–4.45</td></tr>
<tr><td>0.96</td></tr>
<tr><td>–0.23</td><td rowspan="2">1.53</td><td rowspan="3">1.76</td></tr>
<tr><td>0.03</td></tr>
<tr><td>–1.15</td><td>–1.15</td></tr>
<tr><td colspan="3">Total Outperformance for Entire Period</td></tr>
<tr><td>2.71</td><td>1.69</td><td>1.80</td></tr>
</table>

For informational purposes only. There can be no assurance that any investment objectives will be achieved.

As of January 31, 2017

***** Hypothetical portfolio of global companies from the MSCI World Index that have demonstrated improving environmental, social and governance (ESG) ratings. The yearly rebalanced portfolio adds companies with improving ESG scores every year and removes those with deteriorating ESG scores every year. The biennial portfolio rebalances every two years and the triennial portfolio rebalances every three years.

Source: MSCI and AB

IT IS ON THE DEEPER AND LONGER-HORIZON ENGAGEMENTS THAT ACTIVE MANAGERS SHINE.

RESEARCH UNDERPINS EFFECTIVE ENGAGEMENT

Each engagement that we have with a management team begins with deep research. By conducting a detailed assessment of the strengths and weaknesses of a company relative to peers, we can uncover the symptoms of corporate malaise. However, our analysts' collective years of experience in their industries, as senior managers, consultants and investors, allow us to go further, diagnosing the likely causes—and prescribing changes that can yield better performance. The depth and comprehensiveness of this approach allow more productive engagements. In fact, our opinions are generally respected by management teams, and we usually get a hearing even if the management team doesn't agree with our ideas. Moreover, since our goal is to generate superior performance, if management teams don't agree with our perspective, we always have the option to sell our holdings.

The intellectual rigor of active engagement often creates a megaphone to amplify the power of the active manager. If a long-only investment manager's well-researched case is made public, or even circulated privately among investors, passive managers often join, adding silent muscle. Here are some examples of AB's engagement in action:

CASE STUDY 1 : PROMOTING CORPORATE RESTRUCTURING

Sometimes, a company with an attractive underlying business can lose its way. In one case, we had followed a hospitality company for many years, noting that it had been underperforming its peers in terms of growth, margins and valuation. Our hypothesis was that the company was spread across too many businesses. This distracted management from focusing on its core business, confused shareholders about the company's valuation and detracted from optimal capital-allocation decisions.

We brought together analysts who were experts in the company's various businesses across our equities and fixed-income teams. In addition, we spent significant time with the company's former employees, bankers, private equity investors and other industry participants to craft a detailed 23-page document that we presented to the company—not without spirited debate. Over about a year, the company embarked on the exact plan we had proposed to break up the business, simplify messaging and focus on its core business. The company has continued to build revenue and profitability in its core business nicely. We believe that earnings growth and higher valuations from its pure-play businesses should drive stock price performance.

THE INTELLECTUAL RIGOR OF ACTIVE ENGAGEMENT OFTEN CREATES A MEGAPHONE TO AMPLIFY THE POWER OF THE ACTIVE MANAGER.

CASE STUDY 2: RESTRAINING AN ACQUISITIVE COMPANY

Takeover activity can make or break a company. We own part of a healthcare services company whose results were being pressured from acquiring too much, too fast and outside its core areas of expertise. We developed proprietary insights by conducting hospital-level field visits—sometimes accompanied by top-notch expert consultants in the industry—interviewing best-in-class service providers and painstakingly benchmarking government quality metrics at a hospital-by-hospital level.

We engaged with management many times at all levels over a year with several 20+ page documents of analysis in tow, suggesting the company postpone any more acquisitions, buy back stock in the interim with the cash flow, reconsider noncore expansions and revamp some of its operations. Importantly, we questioned both the incentive compensation metrics and quality-of-care progress in the context of our ESG views. So far, the company has implemented some of our suggestions, including hiring outside parties to review its strategic direction. Disciplined acquisitions, aligned compensation and improved service quality generally result in stronger long-term stock price performance.

CASE STUDY 3: SHAKING UP THE BOARD

The structure and policies of a company's board of directors can create risks. So we decided to engage with one of our holdings because its board did not have a mandatory retirement age; at the time, five board members were over 75 years old with an average tenure of 26 years.

Although the company had been an excellent performer both fundamentally and in the market, we were concerned that the governance structure could lead to future problems. During a research meeting, we raised the issue with the CEO and CFO, who were wrestling with the same issue. Our support and thoughts helped prompt management to refresh the board.

THE TIME IS RIGHT FOR EFFECTIVE ENGAGEMENT

As global investors, we are committed to engaging with companies around the world. Our engagements have been around a range of issues, including a company's dividend policy and emerging-market strategy. And we have been asked to present our thoughts to senior management groups to engage in a debate over our ideas.

Of course, not all engagements play out the same way. But we believe the door is wide open for active investors to engage with management teams if they have the right research skill sets coupled with the right engagement skill sets. In our view, this is a rare combination and certainly something passive investors do not possess.

Over time, we believe that the bulk of the responsibility for deep company-level active engagement will fall on traditional active equity managers. A commitment to in-depth, in-house research is essential. It uniquely positions an active manager to leverage company-specific research, analyst backgrounds and industry relationships to drive engagement with management teams, catalyze improvements and ultimately support stronger stock returns.

To engage or not to engage? For active equity managers at AB, there is no question.

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