



WHERE'S THE BEEF?—

The Case for International Stocks

Beef is enjoyed everywhere; but only a few can appreciate the marrow! Remember when every well-bred kitchen owned a set of silver marrow scoops? Today, you can hardly find one in all of London! This is just to say that stock picking requires a bit of detective work... and lots of research.

Do you have the scoop?

Which companies are NOT U.S. owned.

DISPLAY 2
Which One Isn't US Owned?

McDonald's	Banker's Trust	Amoco	MCI Worldcom	Chubb
Burger King	Citigroup	Exxon Mobil	Bell Atlantic	Trans-America
Wendy's	Bank of America	Arco	Sprint	Allstate
Taco Bell	Banc One	Hess	Voicestream	GEICO

Source: Bernstein

The Answer?

Amoco, Arco, Banker's Trust, Voicestream, Burger King, and TransAmerica! If an investor were to stick solely to U.S. stocks, he or she might be missing some significant opportunities.

Over the Long Term, International and U.S. Stocks Run Neck and Neck...

Our research indicates that on a five-year average, returns on international investments (0.9%) have been disappointing relative to U.S. returns (10.7%). At the same time, however, the percentage of pension funds in international stocks has grown from 9.7% in 1996 to 12% in 2000, for a net increase of just under 3%.

However, as you will see in the table below, in the fiscal year-ended 1985, returns of international stocks were identical to those of U.S. stocks, at 14.7%. Between 1985 and 1990, international stocks actually increased significantly while domestic returns took a slight dip. From 1990 to 2000, U.S. stocks fared well, with returns shooting up more than five percentage points and ending the millennium at a high of 18.3%.

During the same period, international returns slipped from a high of 18% in 1990 to 7.1% in 2000. Averaged over the past three decades, U.S. stocks still come out slightly ahead, with an overall return of 12.9% versus 11.4% for international stocks.

Over the long term,
U.S. stocks have outpaced
international stocks
by a slim margin

DISPLAY 6
Long-Term Returns Are Similar

Five Year Periods Ending In (Annualized Return):

	1975	1980	1985	1990
US Stocks	3.2%	14.0%	14.7%	13.1%
International Stocks	9.4	15.6	14.7	18.0

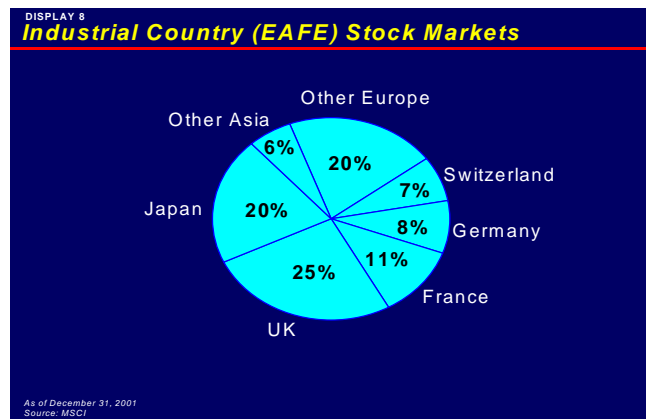
	1995	2000	1970-2000
US Stocks	16.6%	18.3%	12.9%
International Stocks	9.4	7.1	11.4

Source: MSCI and Standard and Poor's

Of Course, Not All International Stocks are Created Equal...

While returns on American and European stocks were comparable over the past decade—at 12.3% and 10.8%, respectively—Japanese returns fell far behind, posting a net loss of negative 6.9%. This is significant since, Japan is a major player on the stage of international finance. Of all non-U.S. industrialized countries, the Japanese stock market accounts for 20% of the total activity. That’s just slightly less than the markets of Germany, France and Switzerland combined. Only the United Kingdom, at 25% of foreign stock markets, is higher.

Here’s how the rest of the
industrialized world (EAFE)¹
has measured up
in terms of market share



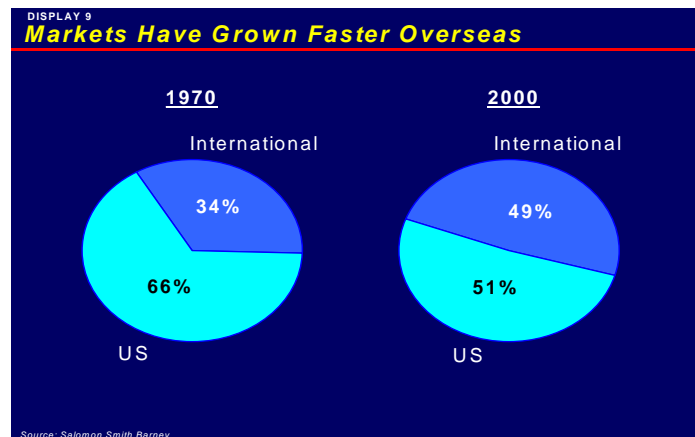
But This is Only Part of the Picture...

Taken as a whole, the total value of international stock markets is, undeniably, lower than that of the U.S. market. It would be a mistake for the investor to rule out the potential profitability of investing in international stocks. Here’s why.

¹ The EAFE (Europe, Australia, and Far East) index from MSCI (Morgan Stanley Capital International) is an unmanaged, market-value weighted index designed to measure the overall condition of overseas markets.

The table below shows that during the past 30 years, overseas markets have grown much more than the U.S. markets. In 1970 for example, of all the industrialized countries, U.S. stocks accounted for 66% and foreign stocks 34%. By the fiscal year-ended 2000, however, international stock markets had climbed to 49% while U.S. stocks dropped considerably, holding a small lead at only 51%.

Foreign markets are catching up quickly



Further, International Markets Dominate in a Number of Key Sectors...

International markets enjoy a large percentage of global market capitalization in these key industries: Consumer Durables (with 78% of global market cap), Auto (71%), Transportation (68%) and Banking (68%).

In addition, if you look at the top-ten return generators in a number of global industries such as Metals and Mining, Beverages, Pharmaceuticals and Diversified Financials, you could be in for a big surprise.

Our research shows that in the best-case scenario, for the fiscal year ended 2001, the top U.S. earner in Diversified Financials was Moody's, with returns of 56.1%. This was a little more than half that of the international leader, U.K.'s Man Group at 91.5%. And in the worst case, in the Beverages sector, Anheuser-Bush's paltry 1% return pales in comparison to Australian Southcorp Holdings' healthy return of 46.2%.

Multinational Corporations are Big...

Texas Instruments, the multinational manufacturer of high-tech gadgets, accounts for 68% of its sales in non-U.S. markets. And by the way, did you know that Coca-Cola and McDonalds sell more coke, French fries, and hamburgers overseas than they do at home!

But while multinationals may have a major part of their business in overseas markets, they do not diversify nearly as well as their foreign counterparts and remain closely tied to the

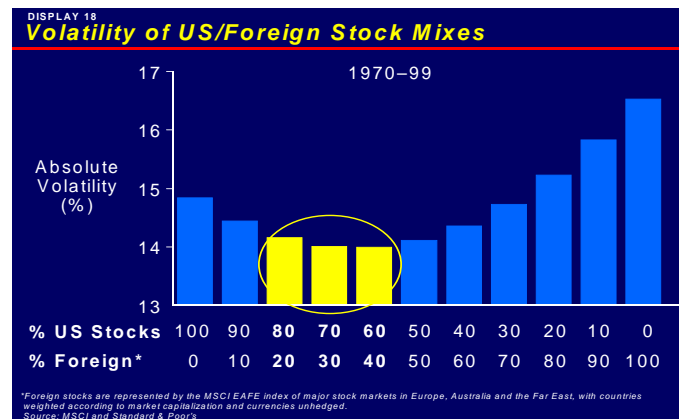
Standard and Poor's 500 index.²

Now this may be just fine when the S&P is doing well, but if it takes a dip—as every seasoned investor knows it will eventually—multinationals really feel it. In fact, all other things being equal, diversification by its very nature maximizes profit potential.

Diversification Pays...

Most investors like to avoid exposure to risk—or at least relish in trying to control it—and the best way to do so is to invest in a combination of foreign and domestic stocks, which will minimize the negative effects of market volatility.

The best mixes tend to be firmly grounded in the U.S. market, with a 20%-to-40% holding in international

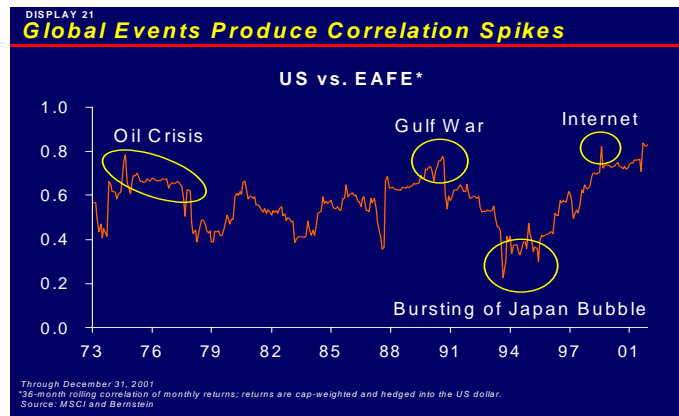


The Rebound Affect...

Of course, we now live in a world where many markets feel the affects of the economy and events in one major marketplace. Global events and crises (economic and other) do not merely affect different markets individually—they also affect the *correlation* of U.S. and EAFE markets, which further underscores their interrelationship. Correlation refers to the way different investments respond to the same market conditions. Low correlation is better because it makes for a more diversified portfolio, therefore reducing risk.

² A [market-value weighted index](#) of 500 blue-chip [stocks](#), considered to be a [benchmark](#) of the overall [stock market](#). This index is composed of industrial, transportation, utility, and financial companies with a heavy emphasis on industrial companies.

You can see how world events can affect the correlation of financial markets.

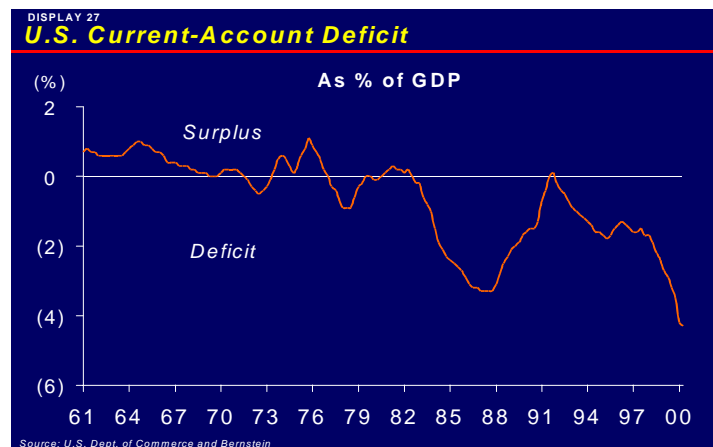


So, there are times when it is clearly advantageous to diversify by altering the proportion of foreign versus domestic stocks in a given portfolio to take advantage of market opportunities (or lack thereof). For much of the past five or six years, foreign returns appear to offer a stabilizing factor to hinder volatility.

Gross Domestic Product ... Favorable for International Investments

One of the best ways to take the pulse of the dollar is by looking at America's gross domestic product (GDP). A decline in GDP, especially into deficit territory, makes foreign investment in the dollar less attractive and lowers its value relative to other currencies, which in turn increases the potential profitability of international stocks. As shown in the display below, for the fiscal year-ended 2000, the dollar was at a forty-year low of negative four percent.

We expect this trend to continue—making it an excellent time to consider foreign stocks



Classic Stock Valuation... Makes Foreign Stocks Attractive

Another classic method for determining the attractiveness of a given stock is its *valuation*. In the United States, even in this time of post Internet-boom caution, we still tend to value

stocks quite high relative to earnings (in fact, many would argue that some stocks are totally *overvalued*).

European valuations, however, are generally much lower than that of most U.S. stocks and the current price-to-cash flow ratio of European versus American stocks makes them extremely attractive. This is even truer with Japanese stocks, which have carried a valuation well below that of U.S. stocks for nearly the past eight years. Perhaps most compelling of all in this context are Emerging Markets stocks, which are consistently valued far below the U.S. standard—although investors must take the natural volatility of these new markets into account when deciding whether or not to their stocks.

Developments in European Economy Bode Well for internationals...

One of the most important occurrences of the new millennium is the long-awaited fusion of most major European markets into one economic entity with the adoption of the Euro. This has given rise to numerous attractive financial opportunities. Take, for example, European pension reform. Starting at zero in 2001, investments in private pension funds have shown a steady increase to date. Based on solid research and projections, we expect growth to accelerate rapidly beginning next year, climbing to a whopping 60 billion Euro by 2008.

But Most Importantly... Where Will Things go From Here?

No one can fully predict the direction of financial markets, and of course, past performance is no guarantee of future returns. Notwithstanding these familiar givens, however, our research has led to some basic conclusions regarding the case for international stocks.

- A diversified portfolio consisting of both U.S. and international stocks is better than one consisting exclusively of U.S. stocks.
- International stocks are attractively valued compared to U.S. stocks.
- A falling dollar and recent developments in the European economy should boost the potential profitability of international stocks.

Stock up on Internationals...

The factors discussed above, coupled with Bernstein's solid foothold in overseas capital markets, create a unique investment opportunity. In order to take advantage of it, we plan to substantially increase our allocation of international stocks over the near term.

Contact your Bernstein Advisor to find out how you can, too!