



Market Update – Daily Fixed Income Trading Liquidity Update 19 May 2020

In the current markets, volatility has been elevated and liquidity has become reduced across many fixed income instruments including government bond markets. Liquidity management has been a heightened focus for AllianceBernstein for years, as we recognized the reduced liquidity in the marketplace after the 2008-2009 financial crisis. We view liquidity management as a business imperative.

In an effort to provide timely updates for our clients on fixed income market trading liquidity, we have developed the following update, aggregated from our traders towards the end of the New York trading day.

Sector	Liquidity Trading Comment	Bid-Ask Spreads
US Treasuries	<ul style="list-style-type: none"> The open-ended bond purchase program enacted by the US Federal Reserve (Fed) is having a positive effect on liquidity and market functionality. The Fed has reduced their purchases of US Treasuries to \$6bn per day during the week of May 18 (from \$7bn per day the week of May 11). Global rates markets continue to be dominated by supply, central bank actions, and re-opening proxies such as oil and/or vaccine developments. During the first two trading sessions of the week (May 18-19) these drivers have been the catalyst for interest rate volatility to move to the high end of its 1-month range (as measured by the MOVE index). Fed funds markets are no longer pricing in negative rates through the 2021 maturity dates. In speaking engagements over the past week, the Fed has given rates investors clarity that negative interest rates are not planned to be used for at least the next year. On Wednesday May 20, the US Treasury will auction \$20bn of the much-anticipated 20-year bond. This is the first 20-year bond auction since the 1980s. 	<p>Bid-offer spreads for on-the-run benchmark 2- through 10-year US Treasury notes has improved significantly and are in line with pre-crisis conditions.</p> <p>For the 30-year note, bid/ask is ~2x wider vs pre-crisis.</p> <p>Off-the-run Treasury bonds still trade significantly wider than on-the run bonds, but bid/offer has compressed.</p> <p>TIPs bid/ask is 2-3x wider vs pre-crisis levels</p>
Investment Grade (IG) Corporates	<p style="text-align: center;">US IG</p> <ul style="list-style-type: none"> US IG cash bonds traded firmly over the two days ended May 19. Spread levels are now back to early March levels. Shorter-maturity bonds continued to outperform. New issue supply slowed down, with \$23 bn in new issues coming to market between May 18 and 19, dominated by smaller issuers. We expect supply to be quiet for the rest of the week heading into the 	<p>US IG spreads are generically 3-4x wider vs normal market conditions</p> <p>AT1/Preferreds are 2-3x wider vs normal market conditions</p>

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	<p>long weekend</p> <ul style="list-style-type: none"> • Bid/ask spreads remain wider than pre-crisis levels. <p style="text-align: center;">European IG</p> <ul style="list-style-type: none"> • Supply levels have been elevated in the European IG market, with both well-known and niche issuers continuing to tap primary markets. • The decent uptick in primary market activity is diverting attention from the secondary market, causing liquidity to drop a bit there. • Liquidity in the AT1 (subordinated financial) market remains incredibly technical and very bond-/issuer-specific. In spots such as core high-quality issuers, bid/offer spreads were back to pre-selloff levels, but in more niche and second-tier names where dealers have no agenda, it remains wide and subject to the whims of the macro tone. Volumes have been very low. USD-denominated AT1s are proving to be more liquid than EUR-denominated AT1s. <p style="text-align: center;">REIT Preferreds</p> <ul style="list-style-type: none"> • Liquidity in the REIT preferred market is limited under more normal conditions but has improved from 1-1.5 months ago. • Dealers are only providing balance sheet capacity on select issuers, so for many issuers, trades must be done on an agency basis; trading is therefore limited. • Trading volume is trending low since valuations have recovered a good amount. 	
High Yield (HY) Corporates	<p style="text-align: center;">US HY</p> <ul style="list-style-type: none"> • On May 19, the US high yield market was unchanged to slightly better, following a firm day on May 18. • Volumes continue to be light and the focus continues to be on new issues. • Six new issues priced on May 19, totaling \$3.1bn, bringing the week to date total to \$5.3bn. Technicals remain strong as deals are being upsized, pricing has come at the tight end of the expected range, and deals have been multiple times oversubscribed • We expect the primary market to remain active going into the long holiday weekend with 3 deals on the calendar. • Bid/ask spreads remain unchanged <p style="text-align: center;">European HY</p> <ul style="list-style-type: none"> • Daily sentiment has dislocated somewhat between 	<p>Spreads are 0.75-1.25 point wider than normal times for BB-rated securities</p> <p>Spreads are 1.5-2 points wider than normal times for B-rated securities</p> <p>Spreads are 3 points wider than normal times for CCC-rated and below securities</p> <p>CDX HY bid/ask is 2-3x vs normal conditions.</p>

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	<p>cash bonds and equities/the iTraxx Crossover index. After several weeks of outperformance in cash bonds, the market has begun to lag modestly.</p> <ul style="list-style-type: none"> • The first signs of new issuance have highlighted the constructive market tone. • Idiosyncratic risk is in focus as potential defaults/restructurings loom. • Technicals remain broadly constructive, as flows are generally positive, investors are more conservatively positioned and primary issuance remains light. • The market continues to see healthy two-way flows but bid/ask spreads remain elevated. <p style="text-align: center;">CDX HY</p> <ul style="list-style-type: none"> • CDX HY traded mostly in line with stocks on May 19 but continues to underperform CDX IG and high yield cash bonds. • Bid/ask spreads have declined but remain elevated relative to pre-crisis levels. 	
Emerging-Market Debt (EMD)	<p style="text-align: center;">Hard Currency EM</p> <ul style="list-style-type: none"> • It was a slow but strong start to the week for hard currency EM debt as spreads on the JP Morgan EMBI Global Diversified hit a two month-tight level on Monday's close. • Investment-grade EM corporates continue to be well bid as spreads over respective sovereigns remain attractive relative to pre-crisis levels. • Liquidity continues to improve as transaction costs have slightly narrowed over the last week. <p style="text-align: center;">Local Currency EM</p> <ul style="list-style-type: none"> • Local EM rates continue to trade well, converging towards low developed-market rates. • Liquidity is close to normal 	<p>EM IG sovereigns are 1.5x wider vs normal market conditions</p> <p>EM HY sovereigns are 2x wider vs normal market conditions</p> <p>EM IG corporates are 2x wider vs normal market conditions</p> <p>EM HY corporates are 3x wider vs normal market conditions</p>
Securitized	<p style="text-align: center;">CMBS</p> <ul style="list-style-type: none"> • The CMBS primary market is beginning to gather momentum with two new issues in the pipeline. Demand remains robust, as the first of the two deals was partially pre-placed prior to its announcement. • The secondary market remains unchanged, with support at the top of the capital structure and very little in the mezzanine classes, especially below the single A level. Collateral continues to be priced to the worst outcome and bid/offer spreads remain wide. AA/A and BBB bid/offer spreads remain at approximately 3x and 4x pre-COVID levels. • The CMBX market seemed to brush off the news of 	

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	<p>JC Penney's bankruptcy filing on Friday and traded up on May 18-19. Series 6 BBB- and BB are higher by 1.3 and 1.5 points since Friday. Pockets of liquidity are beginning to emerge, and bid/offer spreads are improving, although they remain wide of pre-COVID levels. A.6 is ~2x, BBB-.6 is ~2 x and BB.6 ~4x the normal bid/offer spread.</p> <p style="text-align: center;">ABS</p> <ul style="list-style-type: none"> • Another quiet start to the week as dealers traded \$1.3bn over the first two days of the week of May 18, compared to the 20-day daily average of \$1.09bn. • The focus remains on new issuance as both Honda Auto Loan Receivables and Flagship Credit Auto Trust priced and upsized their securitizations on Monday. Flagship, a subprime auto lender issued AAA to BB credit rated classes, with the BB class clearing at +800/swaps. CNH Equipment Trust priced its securitization Tuesday, and the ABS market continues to set new tights as demonstrated by large oversubscriptions and spread tightening on the few new issue deals that came to market this week. • Liquidity has been slow to come back for subordinated tranches since the credit freeze just over a month ago. Below investment-grade bonds will remain challenged over the medium-term as the market better digests information around how covid-19 is impacting these trusts. • Remittances continue to come in with modifications and forbearance the dominant theme. Cash collections on credit cards are down approximately 7.5% m-o-m, equipment -7%, both prime and subprime auto -10%, and consumer loans -15%. <p style="text-align: center;">CRTs</p> <ul style="list-style-type: none"> • The CRT market continues to plug along. The wall of money looking to invest in the space seems to be driving spreads tighter. This technical seems to have moved in one direction since early April. • Investment-grade rated last cash flow bonds seem particularly well bid. Spreads have tightened the most in these bonds, which ended the week in the low 300 bp range. Newer vintage last cash flow bonds that do not have the benefit of the investment-grade rating are not far behind. They are currently trading in the 400-500 bp range. • Equity tranches are trading in the 800-1100 bp range. B1 bonds with some credit enhancement are 	

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	<p>at the tighter end of that range and older Bs that represent the 0-100 slice of 2015 and 2016 deals trade just north of 1000 bp.</p> <ul style="list-style-type: none"> • While bid/ask spreads have come in measurably since the peak of the crisis, they were unchanged week over week. <p style="text-align: center;">Legacy Non-Agency RMBS</p> <ul style="list-style-type: none"> • Legacy RMBS continues to trade through the recent crisis. Since January spreads have widened from ~ 200bp to now in the 1000 bp range, but demand for the sector never really faded. <p style="text-align: center;">CLOs</p> <ul style="list-style-type: none"> • Primary market issuance is the real news in the CLO market. The new issue calendar has opened up for top- and mid-tier managers. • With AAA-rated tranche spreads well inside 200 bp for better enhanced deals, it makes sense for managers to tap the market. At the same time, these levels are still historically wide, making AAA-rated CLO tranches very attractive for banks, money managers, and insurance company investors alike. • The AA- and A-rated tranches have also been oversubscribed on these new deals. • The BBB- and BB-rated tranches have been retained by managers as the market for these securities has not come back. Too many questions remain about loan rating downgrades and how far up the stack that will affect losses and in turn spreads. • Bid/ ask spreads on AAA/AA/A rated bonds have come back to normal; mezzanine bid/ask remains elevated at roughly 2x normal. <p style="text-align: center;">Agency MBS</p> <ul style="list-style-type: none"> • Bid/ask spreads in Agency MBS have returned to pre-crisis levels, driven tighter by the combination of Fed buying and increased investor interest. Bid/offer for lower coupon bonds is just ½ of a tick wide. 	
Money Market	<ul style="list-style-type: none"> • 1-month LIBOR set at 0.171% and 3-month at 0.374%. Prime money market funds saw \$11bn of inflows during the 7 days ending May 18, which has been driving 3-month LIBOR lower. • On Wednesday May 13, Fed Chair Powell reiterated that negative rates were not an appropriate policy tool. He stated that the FOMC feels that current policy tools are working and that there are more tools in the tool kit if need be. Powell mentioned 	

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	<p>that this is one of the few things “all” FOMC participants agreed on and cited other reasons against negative policy rates including mixed evidence of their effectiveness and disrupting the intermediation process (hurting banks). Other “Fed-speak” has reinforced Powell’s message.</p> <ul style="list-style-type: none"> • Government money market fund demand has slowed. Dealers are flush with supply. Repo has climbed to 0.05-0.06% as dealers start to pay up to fund inventory. We’re seeing the pendulum swing as dealers are now going to the Fed’s open market repo operations (at 0.10%) for financing. 	
US Municipals	<ul style="list-style-type: none"> • Very short maturity, high-grade paper continues to be very well bid as buyers are looking for cheap Treasury alternatives. • High-quality bonds continue to trade very well with new issues 5-12x oversubscribed. • There were some signs of life in the high yield space with a true high yield deal coming on May 19 which was 7-10x oversubscribed. However, flows in high yield overall continue to be negative. • Odd lot liquidity remains challenged compared to historic averages, with bids on smaller-sized odd lots trading at 1-4 points below round-lot bidside evaluations. Higher-quality odd lots, especially in shorter maturities, trade 0-2 points below round lot bidside evaluations. High yield or even lower-quality investment grade odd lot bids remain well below round lot bidside evaluations. For context, high grade odd-lots typically trade 0.10-1 points below round lot bidside evaluations under more normal market conditions. 	
Canadian Market	<p style="text-align: center;">Federal</p> <ul style="list-style-type: none"> • Liquidity is best in benchmark issues for block sizes of <=CAD25m; limited liquidity in off-the-run, high coupon bonds but the Bank of Canada buying program will help liquidity in the sector. <p style="text-align: center;">Provincial</p> <ul style="list-style-type: none"> • Liquidity is best in benchmark bonds from Quebec, Ontario and British Columbia • Concessions are requested so dealers will take less liquid positions. • Very limited secondary-market liquidity in oil-generating provinces (Newfoundland, Alberta, Saskatchewan) with Western Canadian Select oil price trading at low levels. • Most dealers will not bid on off-the-run, high 	<p>Federal: bid/ask typically +1 to +2bp but for the long end of the curve, it can be more depending on volatility</p> <p>Provincial: concession of +1 to +2bp and more on size > CAD 25m, particularly at the longer end</p>

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	<p>coupon provincial issues, they will do agency trades. They may not bid for provincial issuers where they have existing balance sheet positions.</p> <ul style="list-style-type: none"> The Bank of Canada’s C\$50bn buying program of provincial debt should support liquidity. <p style="text-align: center;">IG Corporates</p> <ul style="list-style-type: none"> Limited liquidity; many dealers are maintaining low balance sheet inventories, so will not provide bids in many sectors. Trading on an agency basis for high-beta issuers. The market has improved in sectors such as banks. However, there was limited dealer appetite for telecom credits after the new BCE 10- and 30-year issue came to market on May 11. The Bank of Canada’s buying program of corporate debt should support liquidity in the secondary markets for BBB and higher-rated securities. BBB-bonds are trading by appointment, and can trade with large bid/ask spreads – in some cases as big as +25 bp. <p style="text-align: center;">Real Return Bonds (RRBs)</p> <ul style="list-style-type: none"> Trading “by appointment”, but the program to purchase Government of Canada securities in the secondary market – the Government Bond Purchase Program or GBPP – should help liquidity since it will include RRBs. The program begins on May 27. 	

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