AllianceBernstein®

November 2020

Market Update – Fixed Income Trading Liquidity
For the Week Ended 6 November 2020

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 at the end of each week.

Sector	Liquidity Trading Comment	Bid-Ask Spreads
US Treasuries	• Global developed market (DM) interest rates were mixed during the week ended November 6, with US yields modestly lower and curves flatter on a week dominated by the results of the US election. The moves in the US were primarily due to positioning rebalancing as many investors headed into the election positioned for a "blue wave" with shorter duration and curve steepening positions on in anticipating of more spending and stimulus. Core European markets were generally unchanged while Italian and Spanish markets continued to experience spread tightening as risk assets traded well. The 10-year US Treasury to German Bund spread backed off the local high level of 150 bp – the widest level since mid-March – finishing the week at 144 bp. • Federal Reserve bond purchases stand at $80 bn US Treasuries and $60 bn MBS per month. • Liquidity in nominal Treasuries and TIPS widened to 2-3x normal bid-offer spreads following the volatility after the US election. • Volumes post-election were very high vs recent averages. Despite the high volumes, market depth in the Treasury market—defined as the sum of the three bids and offers by queue position, using the top 3 bids and offers in 10-year Treasury notes, averaged between 8:30 and 10:30am daily (Sourced from BrokerTec)—was less than the prior week down roughly 20% following the election as the initial flight to quality and ensuing sell off led to choppy price action.	Bid-offer spreads for on-the-run and off the run US Treasuries are 2-3x pre-crisis conditions. TIPs bid/ask is 2-3x wider vs pre-crisis levels

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Investment Grade (IG) Corporates	**US IG** • The US IG cash bond market performed very well during the week ended November 6, with IG index spreads closing the week 8 bp tighter week-over-week, setting new post-covid tight levels at 117 bp. • The market remains well bid as there seemed to be cash on the sidelines waiting for the US election to pass. • Despite the rally in both interest rates and credit spreads, there was strong demand for long maturities from both domestic and Asia-based investors throughout the week. The 10-year part of the curve was also well-bid and credit curves (both 5s-10s and 10s-30s) flattened. • Beta compression was a theme throughout the week with BBB risk well bid. • IG cash bonds did see small outflows during the week – the first outflow since early April. But technicals remain supportive as supply was muted (only $0.25bn priced this week) and dealer inventory remains light. • Fed purchases under the secondary market purchase program (SMCCF) remained light as they bought only $127mn ($25.4mn/day) over the past week. At the FOMC meeting this week, they did not extend the CCFs or other emergency lending programs which are set to expire on December 31. **European IG** • During the week ended November 6, liquidity was thinner given the US election as most investors remained focused on the results. • Overall, despite the fact that what many considered to be a negative outcome heading into the election is the outcome that materialized, both macro and European IG performed well, demonstrating that investors were generally under-risked ahead of the event. • CDS outperformed cash markets as it had been the mechanism to hedge when macro was soft, effectively reversing the theme of the prior week. **REIT Preferreds** • Liquidity in the REIT preferred market is typically limited under more normal conditions given the retail nature of the investor base. Current liquidity is better than in March and April but is still not back to normal.	US IG spreads are generically 1-1.5x wider vs normal market conditions AT1/Preferreds are 1-1.5x wider vs normal market conditions

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	• 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 continue to recover.	
High Yield (HY) Corporates	**US HY** • The US high yield market was better bid as the week (ended November 6) began, on light inquiry as investors continued to add risk after month end. The rally caught fire on Wednesday alongside strength in equities, with demand largely driven by ETF arbitrage investors. • Heading into the election, many investors had hedges in high yield in the event of an adverse election outcome; with the market-positive results of the election, many of these hedges were taken off. This created rapid demand/inflows for HY ETFs which traded at a premium to NAV, leading to a persistent bid from ETF arbitrage investors. All of these dynamics caused market prices to reset higher. Trading became more two-sided later in the week. • Apart from the ETF dynamics, the projected election results – particularly a split congress – is being perceived as a "goldilocks" scenario for HY investors. The market expects the Republican-held Senate to limit the magnitude of stimulus/fiscal spending, which caused interest rates to rally. In addition, the market expects a lower likelihood that the Trump tax cuts will be rolled back, which caused spreads to tighten. • In the new issue market, 3 deals priced for a total of $1.25bn, well below the 2020 weekly average of $10.2bn. Deals were well subscribed (2.75-6x) and came tight relative to initial price guidance indicating demand for new issues remains strong despite election uncertainty and mounting covid risks. • The HY index spreads moved 73 bp tighter to 436 bp, the tightest levels post-covid. This compares to March 23 wide levels of 1100 bp and pre-covid-19 tight levels of 341 bp on Feb 13. • The CCC-BB spread was 42 bp tighter to 521 bp. This compares to April 6 wide levels of 1139 bp and pre-covid-19 tight levels of 613 bps on February 13.	Bid/ask spreads vary by issuer but generically: BB-rated securities: 1 point, which is in line with normal market conditions B-rated securities: 1 point, which is in line with normal market conditions CCC-rated and below: 1.5points which is in line with normal market conditions CDX HY bid/ask is 1-2x vs normal conditions.

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	CDX HY • CDX HY traded well along with macro sentiment during the week ended November 6. Hedges put on ahead of the US election were taken off and flows were bullish from Wednesday. • Trading volumes picked up on the back of heightened volatility. Bid/ask spreads have declined but remain elevated relative to pre-crisis levels.	
Emerging-Market Debt (EMD)	**Hard Currency EM** • EM credit staged an impressive ~25bp rally during the week ended November 6, propelled by the bounce in global macro risk following the US election. • The technical backdrop further supported the spread tightening—dealer balance sheets were light, and investor cash balances were high, with inflows during the week further driving demand. EMB—the major EM ETF—logged its largest 1-day inflow since February 2019. • The week saw beta compression, with HY and IG bond spreads compressing ~35bps week over week. **Local Currency EM** • Liquidity is close to normal.	EM IG sovereigns are back to normal market conditions EM HY sovereigns are back to normal market conditions EM IG corporates are back to normal market conditions EM HY corporates are back to normal market conditions
Asia	**Asia Hard Currency** • Asia hard currency credit spreads rallied 9bp at the index level during the week ending November 6, as markets began to price out US election uncertainty. • Primary markets quieted down materially with only five issuers tapping the market to raise USD 1.4bn, all from the China HY sector which tends to be less correlated with the global macro environment. • Offer side liquidity was challenged on the back of the overwhelming buying activity as "real money" investors began to deploy cash on the sidelines, whereas the "fast money"/dealer community scrambled to cover shorts. **Asia Local Currency** • While transaction volumes were reduced going into the election on November 2, activity picked up materially after the election as investors digested the election outcome. • The highlight of the Asian local markets was Indonesia where government bond yields fell ~10 to 30 bps as foreign investors returned to the market	Asia IG credit is ~1 to 1.5x wider vs. normal market conditions Asia HY credit is ~1.5 to 2x wider vs. normal market conditions Asia local currency debt is ~1 to 1.5x wider vs. normal market conditions

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	on the back of the broader risk-on rally as well as improved sentiment towards the emerging markets.	
Securitized	**CMBS** • During the week ended November 6, CMBS traded higher in sympathy with other risk asset markets. AAA-rated CMBS were tighter by 7-10 bp, while BBB-rated CMBS tightened 10 bps. • Trading volumes remained low with only $761mn bonds out for bid, versus $914mn the prior week. There was no new issuance. With a modest new issue calendar expected until the end of the year, market technical remain positive. • Bid/offer spreads continue to compress. Bid/offer spreads for AAA to A-rated classes have retraced their post-covid-19 widening, while bid/offer spreads for BBB-rated classes remain approximately 2x their pre-covid-19 levels. • CMBX also traded well in sympathy with the positive macro tone. AAA-rated tranches tightened 5-10bp. BBB- CMBX outperformed equal-rated CMBS and ended the week 20-30 bp tighter. Liquidity remains sporadic and therefore bid/offer spreads have not changed. CMBX A.6, BBB-.6, and BB.6 bid/offer spreads remain approximately 2x their historical averages. **ABS** • The ABS primary market priced two transactions for the week ending November 6 totaling $1.14bn across private credit student loan and unsecured consumer loan ABS deals. ABS year-to-date supply now stands at $165.7bn compared to $213.1bn recorded in 2019 over the same time period. • ABS indicative benchmark spreads remained unchanged on the week, as the secondary market also witnessed muted activity. • TALF loans requested for the November 5 subscription date totaled $26mn, in only the private credit student ABS sector, the lowest recorded for any TALF subscription date thus far. TALF program-wide cumulative loans requested stand at $4.4bn after ten subscription dates with 2 remaining. The total includes $0.4bn across student loan and insurance premium ABS, $1.2bn in CMBS, $2.5bn in SBA and $0.3bn in CLO sectors. • On November 5th, Hertz announced that it had secured commitments for fleet financing totaling $4bn and has filed a motion for approval of the	

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	Hertz Corporation entering documentation for the financing by the US Bankruptcy Court for the District of Delaware. Upon approval, and together with the up to $1bn of Hertz's debtor-in-possession financing that may be used as equity in the fleet financing subsidiary, Hertz will have access of up to $5bn in total funding to support its financing needs. The company also noted that it plans to refresh its rental car fleet in 2021 and anticipates the purchase of approximately 229,000 vehicles. **CRTs** • During the week ended November 6, CRT spreads were unchanged to marginally wider. Dealers' inventory coming into the week was light as they had used the previous week to position for October month end and to get in front of any potential negative US election outcomes. The technical picture in the CRT market remains sound with fairly even buying and selling on the TRACE screens. • Liquidity improved after showing some signs of stress before month end. Depth of bid remains robust, and dealer markets have returned to the normal 5mn x 5 mn size. **Legacy Non-Agency RMBS** • Legacy RMBS have recovered back to pre-crisis levels. After having widened to the 1000-1200 bp range in March, spreads are currently trading at or around 200 bp discount margin currently. **CLOs** • There was little to no change in the CLO market during the week ended November 6 given election uncertainty. The market seems to have "taken a breather" to see where things shake out in Washington. • Spreads in the primary and secondary markets were unchanged for both AAA-rated and mezzanine deals. The basis between where top-tier and lower-tier managers are executing their liabilities has also leveled off at around 10-15 bp. • Liquidity remains robust in the CLO market. Bid/ask spreads remain at or around pre-crisis levels. **Agency MBS** • Bid/ask spreads in Agency MBS have returned to pre-crisis levels, driven tighter by the combination of	

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	Fed buying and increased investor interest. Bid/offer for lower coupon bonds is just ½ of a tick wide.	
Money Market	• There was a muted response in the money markets during the week ended November 6, despite all the recent volatility around the elections. • Government money market funds saw outflows of $10bn in the 7 days ended November 6. Prime funds saw $12bn in outflows over the same period. • Focus is on the US Treasury's refunding statement and its impact on T-bill issuance. The Treasury's recent refunding statement expects an operating cash balance of $800bn by the end of Q4 2020 and Q1 2020; this balance is now ~$1.7trn. Other factors in play are the probability, size, and timing of additional fiscal stimulus, debt ceiling suspension expiring in July 2021, and the Treasury Borrowing Advisory Committee's recommendation to shrink current T-bill share to 15-20% of its debt outstanding (currently 24% or $5trn). An abrupt reduction in supply due to any of these factors could meaningfully richen front-end markets bringing T-bill rates, repo rates, and Fed funds lower. Expectations in the market are for a T-bill net paydown in the range of $400-800bn in 2021, and $1-1.1trn in 2022. • 1-month LIBOR set at 0.13% and 3-month LIBOR set at 0.21%. SOFR has been setting at 0.09-0.10%.	
US Municipals	• The muni market rallied strongly during the week ended November 6, following the post-election fixed income rally, and held onto gains throughout the week even as US Treasuries backed up on Friday. By the end of the week, benchmark AAA-rated bond yields had declined as much as 12bp in 10-year maturities and 15bp in 30-year maturities, bringing muni-to-Treasury ratios below 100% across most of the curve for the first time since the pandemic began. • While a "blue wave" scenario—resulting in higher tax rates and a big stimulus bill—was perceived to have been the best scenario for municipals, the overall environment is still broadly positive for municipals post-election. • With money managers generally maintaining extra cash balances in the expectation of volatility, many investors rushed to put money to work amid the broad risk-on rally and favorable technical picture. • Fund flows remain strong, with the primary municipal ETF recording its biggest single-day inflow	

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	since July. The new issue calendar remains light as most deals were pulled ahead of the US election. • Liquidity remains firm with most odd lots receiving bids 0.5 to 1.5 points below round-lot evaluations, depending on piece size.	
Canadian Market	**Federal** • Liquidity is best in benchmark issues for block sizes of <=CAD25 million; liquidity has improved in off-the-run, high coupon bonds with Bank of Canada (BOC) bond buying. Comments by central bank Governor Macklem that the BOC will buy at least $4 billion of Canadian government bonds per week until the recovery is well underway should continue to support market liquidity. The fact that the BOC will buy more bonds at the long end of the curve should support liquidity at the 30-year part of the yield curve. • The BOC has purchased C$158.6 billion to support liquidity in Government of Canada markets since the purchase program started on March 27 through November 4. In coming weeks liquidity could be negatively impacted by the US election.	Federal: bid/ask typically +0.5 bp but for the long end of the curve, it can be more depending on volatility (risk off markets) and size outstanding. Off the run Canadas can have a wide bid-ask given small outstanding size in these securities.
	Provincial • Liquidity is best in benchmark bonds from Quebec, Ontario and British Columbia. • Depending on market tone, concessions may be requested in order for dealers to take less-liquid positions. • Most dealers will not bid aggressively on off-the-run, high coupon provincial issues, they will do agency trades, even with the Bank of Canada's buying program of provincial debt. • The BOC has purchased C$11bn in par value year to date through November 4 within their provincial buying program to support liquidity.	Provincial: concession of +1 bp and more on size > CAD 25 million, particularly at the longer end. In risk-off markets, liquidity is drying up and spreads can widen depending on market tone.
	IG Corporates • Limited liquidity, particularly during risk-off trading days can impact pricing; 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 and telecom companies. • The Bank of Canada's buying program (focused on securities of 5-years or less) should support liquidity for corporate bonds rated BBB and higher.	BBB- corporates are trading by appointment, particularly in the energy sector. Inventories are reduced and dealers are not looking to increase their BBB- exposure. Dealers estimate bid/ask could be as high as +20 bp on BBB-. Dealers

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	However, the central bank has bought a relatively small amount of corporate securities to date (C$160 million par), indicating the impact is limited. The central bank did not purchase additional bonds in recent weeks (as of November 4). BBB- bonds are trading by appointment unless there is a new issue. • It should be noted that corporate traders are unlikely to increase their inventories ahead of the November 3 US election, which could also lead to dislocations in liquidity.	may refuse to bid in a risk off market with gaps in spreads.
	Real Return Bonds (RRBs) • The C$400 million RRB auction of the long Canada 0.5% Dec. 2050 on September 2 provided liquidity in the benchmark RRB bond for a limited period in the benchmark RRB bond. • The next auction will be held on December 2. The program to purchase Government of Canada securities in the secondary market – the Government Bond Purchase Program or GBPP – should help liquidity since it includes RRBs. The program began on May 27. The BOC bought a total of C$700mn with C$100mn per line of the 7 Canada RRBs from 2021 to 2047. Even with the central bank buying net C$400mn of Canada RRBs, liquidity remains challenging as dealers hold very limited inventories, if any, of these RRB securities. Trading a block can only be done on an appointment basis.	Provincial RRBs trading by appointment only. Dealers do not hold these securities on their balance sheet.

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