AllianceBernstein®

July 2020

Market Update – Daily Fixed Income Trading Liquidity Update 10 July 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	• 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 committed to purchasing a minimum of $80bn US Treasuries and $40bn MBS every month, with possibilities to increase should circumstances change for the worse. • Global interest rate curves flattened during the week ended July 10, as record long end supply continues to clear with above-average end user demand. • The risk-on tone in stocks led to a further widening of 5-year inflation breakeven rates, further flattening of the breakeven curve, and rate volatility trading lower as measured by the MOVE index. • The liquidity backdrop continues to improve moderately as the $20bln of Fed purchases per week continues to ameliorate investor concerns about covid-19-related US Treasury supply. • Market depth (sourced from BrokerTec data) is about 95% of its pre-Covid19 levels.	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. Bid/ask for the 30-year note, is now also in line with pre-crisis levels. Off-the-run Treasury bonds still trade significantly wider than on-the run bonds, but bid/offer has compressed. TIPs bid/ask is at least 2-3x wider vs pre-crisis levels, and trade by appointment at certain points during the week.
Investment Grade (IG) Corporates	**US IG** • There was mixed performance for US IG cash bonds during the week ending July 10. The IG cash index reached post-covid-19 tight levels on Monday before leaking wider during the rest of the week. However, both primary and secondary flows were quiet ahead of Q2 earnings and as summer sets in.	US IG spreads are generically 2x wider vs normal market conditions AT1/Preferreds are 2-3x wider vs normal market

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	• The Fed's weekly report showed that the Fed purchased $704mn for its secondary market purchase program (SMCCF) between July 1 and 7. This is the slowest purchase pace since the program began and is expected to stay slow if market conditions continue to improve. • The primary market was quiet, with $19bn in new issues coming to market between July 6-10, which continues to help market technicals. Demand was less robust than previous months now that valuations have recovered materially. • Bid/ask spreads remain wider than pre-crisis levels. **European IG** • Secondary volumes remained extremely light. Flows were focused around marginal cash flow trades and new issues, but there seemed to be little changes of risk across the market with liquidity low given overall light volumes. **REIT Preferreds** • Liquidity in the REIT preferred market is limited under more normal conditions but has improved from 2-3 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 continue to recover.	conditions
High Yield (HY) Corporates	**US HY** • It was a slow week in US High Yield coming out of the holiday weekend, with the market better bid throughout the week ended July 10. Activity was especially light on down equity days, with participants hesitant to sell into weakness. • New issues were more active than expected with $7.8bn of bonds coming to market, across 11 deals. This was $3-5bn more than expected, but less than the $10.4bn week average for 2020. • Technicals remain firm with most deals multiple times oversubscribed and priced at the tight end of initial price guidance. • Of note during the week, two smaller deals from storied names (National Group Mining and Blue Racer) were pulled, showing some discipline in the new issue process. • Morgan Stanley estimates $28.2bn will enter the	Spreads are 0.75-1.25 point wider than normal times for BB-rated securities Spreads are 1-1.5 points wider than normal times for B-rated securities Spreads are 1.5-2.5 points wider than normal times for CCC-rated and below securities CDX HY bid/ask is 1-2x vs normal conditions.

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	market via coupons, calls and tenders over the next 3 weeks, affirming a strong technical in the market as new issues enter a summer slowdown. • The index spread was flat on the week, just below 600 bp, compared to March 23 wide levels of 1100bp and pre-covid-19 tight levels of 341 bp on Feb 13. **CDX HY** • CDX HY traded better along with macro tone but once again underperformed both stocks during the week ended July 10. • Trading volumes are trending lower now that summer illiquidity has begun to kick in. Bid/ask spreads have declined but remain elevated relative to pre-crisis levels.	
Emerging-Market Debt (EMD)	**Hard Currency EM** • It was very quiet again for hard currency EM debt during the week ending July 10, as the JP Morgan EMBI Global Diversified Index closed a few bps wider, hovering around recent tight levels of 450 bp, which is ~170 bps wide of YTD tight levels and ~275 bp inside of the covid-19 crisis wide levels. Generically, below-investment-grade bonds were down 1-2 points and investment grade were 3-5bps wider with a flurry of volume on Thursday morning following the sell-off in global macro risk. • Ecuador was the weekly outperformer, trading up after quickly coming to a reasonable restructuring agreement with bond holders. Ukraine and El Salvador underperformed, trading down as the former continued to weaken following last week's failed new deal, while the latter was barely able to price a $1bn new issue at ~100bps of new issue premium. • The primary market churned out ~$4bn across 5 Latin American corporate deals with books ~6x oversubscribed on average. The active start to July followed a record June in which gross issuance was $69bn vs. the 5-year average of $36bn making it the largest June gross issuance on record with 59% of the supply rated investment grade. • After last week's $2bn outflow (largest outflow in EMD in 2 months) this week saw a return to healthy inflows, with hard currency leading the way, another indication of the firm backdrop.	EM IG sovereigns are back to normal market conditions EM HY sovereigns are 1.5x wider vs normal market conditions EM IG corporates are 1.5x wider vs normal market conditions EM HY corporates are 2x wider vs normal market conditions

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<tr><th>Sector</th><th>Liquidity Trading Comment</th><th>Bid-Ask Spreads</th></tr>
<tr><td></td><td>Local Currency EM
• Liquidity is close to normal.</td><td></td></tr>
<tr><td>Asia</td><td>Asia Hard Currency
• Asia hard currency IG credit spreads retreated, widening 1-5 bps on the resurgence of covid-19 cases in Hong Kong.
• Asia High Yield had a weak tone, with supply from China Property, sellers in India HY and Indonesia HY trading down in sympathy with Modern Land’s (MDLNIJ) stressed liquidity situation.
• Liquidity overall was still constructive, and flows were generally two-way; Asia credit was marginally softer.

Asia Local Currency
• Asia local currency debt liquidity functioned as normal for the most part during the week ended July 10.
• Indonesian policymakers announced “burden sharing” details, which were on the margin positive to the supply picture. There is still some stress in local currency.
• China rates continued their upward trajectory but stabilized as the 10-year CGB breached 3%.</td><td>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</td></tr>
<tr><td>Securitized</td><td>CMBS
• In the CMBS/X markets, there is little supply expected in the near term and trading volumes are low. Liquidity conditions in both CMBS and CMBX remain the same. CMBS AAA, AA/A, and BBB bid/offer spreads are approximately 2x, 2x, and 3x their historical averages. In the CMBX market, A.6 is ~2x, BBB-.6 is ~3 x and BB.6 ~5x the normal bid/offer spread.

ABS
• The ABS primary market priced three transactions for the week ending July 10, totaling $2.6bn across prime auto loan, cell tower and timeshare. ABS year-to-date supply now stands at $81.1bn compared to $121.9bn recorded in 2019 over the same time period. Deals were well received with good subscription levels and generally priced through initial guidance range. Currently, there are nine issuers pre-marketing for the week beginning July 13 across prime and subprime auto, equipment, floorplan and timeshare ABS.
• Indicative benchmark spreads remained largely unchanged, with noteworthy moves recorded across</td><td></td></tr>
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	the fixed credit card segment which tightened by 2bp on the week, given the scarcity of bonds in the market. • TALF activity has been very limited to date and opportunities are diminishing as spreads continue to grind tighter. June auto sales showed continued recovery albeit at a slower pace. The Manheim Used Vehicle index reached record high in June. **CRTs** • Bid/ask spreads continue to shrink in the CRT market. As the market pulls back to par, bid/ask spread has continued to approach pre-crisis levels, with the one exception being large block trades. Sellers who have large pieces to sell seem to be willing to pay wider bid/ask—roughly ¼ to ½ point—to get trades done. This compression is affecting all aspects of the CRT market. **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** • Significant size has been passing through the CLO market at or around the recent tight spread levels. The top of the CLO stack in particular shows little sign of wear with all this recent volume. Demand remains quite high as most people see the CLO market as having only recovered 60-70% of what it gave up during the crisis. • Bid/ask spreads are all but back to normal, pre-crisis levels. **Agency MBS** • 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	• Money markets have been quiet ahead of the July 15 tax day. Estimates of government money market fund outflows are ~$50bn, which should not materially widen repo rates (3-5bps expected). • This past week saw negative net T-bill supply, tightening T-bill yields 2-3 bps week-over-week. Gross T-bill issuance is still quite large compared to	

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	history, but the outlook for issuance is uncertain given the Treasury's growing $1.6trn operating balance and looming tax receipts. • The commercial paper to T-bill spread remains narrow at ~10 bps. • 1-month LIBOR set at 0.175% and 3-month LIBOR set at 0.275%.	
US Municipals	• The municipal market had a strong week ending July 10. The benchmark curve drifted tighter. High-yield and high-quality issuers with more spread continued to perform well. • With some states choosing to pause or reverse their reopening, there are some fundamental concerns surrounding municipals, but expectation is that there will be support from the government in the form of additional stimulus. • Investors continue to hold a lot of cash so there remains a strong technical in favor of municipals continuing to perform as long as interest rates remain low. • In new issues last week, $11.1bn came to market with strong demand, with multiple deals seeing double digit subscriptions. Large deals included the City of Los Angeles $1.8 bn note and the $2.3 bn University of California deal, split between $1.5 bn taxable and 0.8B tax exempt. • Odd lot markets are seeing the highest demand and lowest haircuts since the crisis began. On average, odd lots are being bid <1 point below round lot levels for all but the smallest odd lots.	
Canadian Market	**Federal** • Liquidity is best in benchmark issues for block sizes of <=CAD25mn; liquidity has improved in off-the-run, high coupon bonds with Bank of Canada bond buying. Comments by central bank Governor Macklem that the BoC will buy at least $5 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 C$600mn at the long end of the curve (increased by C$200mn) should support liquidity at the 30-year part of the yield curve. **Provincial** • Liquidity is best in benchmark bonds from Quebec, Ontario and British Columbia • Concessions are requested so dealers will take less-liquid positions.	Federal: bid/ask typically +1 bp but for the long end of the curve, it can be more depending on volatility Provincial: concession of +1 bp and more on size > CAD 25mn, particularly at the longer end

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	• Secondary-market liquidity in oil-generating provinces (Newfoundland, Alberta, Saskatchewan) has improved with WTI over US$40 per barrel. • 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$29.05bn to date, which should support liquidity. **IG Corporates** • Limited liquidity, particularly during risk-off trading days; 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 of corporate debt (5 years or less) should support liquidity in that market for BBB and higher-rated securities. However, the central bank has only bought C$560mn in corporate securities, indicating the impact is minimal. BBB- bonds are trading by appointment unless there is a new issue. The corporate calendar is expected to be light in July, another factor that could be a detriment to corporate market liquidity. **Real Return Bonds (RRBs)** • The C$400mn RRB auction of the long Canada 0.5% Dec. 2050 on May 27 supported liquidity in the benchmark RRB bond for a limited period. • 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 began on May 27. The BoC bought a total of C$700m with C$100m per line of the 7 Canada RRBs from 2021 to 2047. Even with the central bank buying net C$300m 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.	Large bid/ask spread on BBB- corporates, which are trading by appointment in many cases, particularly in the energy sector. Provincial RRBs trading by appointment only. Dealers do not hold these securities on their balance sheet.