May 2020

Market Update – Daily Fixed Income Trading Liquidity Update 1 May 2020

In the current markets, volatility is at an extreme level and liquidity has become significantly 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 reduced their purchases of US Treasuries to $8bn per day during the week of May 4 (from $10bn per day the week of April 27). • Rate volatility continues to fall, with the MOVE index just 4 points above the YTD lows set in January. • The TIPS market took a breather from the recent rally following the bottoming of energy prices and solid auction demand around last week's 5-year auction. Breakeven inflation rates were lower across the curve, with 10 and 30 year breakevens down 5 bps. Liquidity remains worse due to the oil selloff and Fed tapering—on-the-run 10-year TIPS can be moved at 2-3 tick wide bid/offer spreads but liquidity in off-the-run bonds and longer-maturity bonds can be 3-6x as wide.	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. For the 30-year note, bid/ask is ~2.5x wider vs pre-crisis. Off-the-run Treasury bonds still trade significantly wider than on-the run bonds, but bid/offer has compressed.
Investment Grade (IG) Corporates	**US IG** • US IG cash bonds have been holding up well despite an increase in macro volatility due to month-end index extension flows. • New issue supply remains busy and May is expected to be another heavy supply month. $55 bn in new issues came to market between April 29 and May 1, including a $25 bn Boeing deal across 7 tranches. Subscriptions remain healthy. • Credit curves continue to normalize across the quality spectrum. The long end has begun to steepen with most high-quality names back to pre-crisis levels.	US IG spreads are generically 4x wider vs normal market conditions AT1/Preferreds are 2-3x wider vs normal market conditions

Sector	Liquidity Trading Comment	Bid-Ask Spreads
	• Bid/ask spreads remain wider than pre-crisis levels. Odd-lot liquidity is still improving, but not back to normal conditions yet. **European IG** • Supply levels have begun to pick up modestly in the European IG market, with niche and less well-known names continuing to tap primary markets. Liquidity tailed off toward the end of the week ending May 1 as holidays in Asia and Europe led to lower volumes in the latter half of the week. • In the secondary market, off-the-run names which have had poor liquidity since the selloff began in earnest continue to gain investor focus and are becoming tradeable, despite the modest uptick in primary market activity, as investors scour for value. • 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. **REIT Preferreds** • Liquidity in the REIT preferred market is limited under more normal conditions and has become significantly challenged amid the current crisis. • Dealers are not providing balance sheet capacity to support the market and so trades must be done on an agency basis; trading is therefore limited. • On May 1, trading volume continued to be very light.	
High Yield (HY) Corporates	**US HY** • The tone of high yield in recent weeks has been tied to equities—with high yield closely following equity market moves. • On May 1, the US high yield market was generally down 0.5 to 1 point on light volumes. • The new issue market remains topical with $7.25 bn pricing this week. Demand remains strong. **European HY** • Daily sentiment has dislocated somewhat between cash bonds and equities/the iTraxx Crossover index. After several weeks of outperformance in cash bonds, the market has begun to lag modestly. • The first signs of new issuance have highlighted the constructive market tone. • Idiosyncratic risk is in focus as potential	Spreads are 1 point wider than normal times for BB-rated securities Spreads are 1-2 points wider than normal times for B-rated securities Spreads are 2-4 points wider than normal times for CCC-rated and below securities CDX HY bid/ask is 3-4x vs normal conditions.

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<tr><th>Sector</th><th>Liquidity Trading Comment</th><th>Bid-Ask Spreads</th></tr>
<tr><td></td><td>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.

CDX HY
• CDX HY slightly outperformed the broader macro tone in the two days ending May 1 and flows seem more supportive for the first time in more than a week.
• Trading volumes remain at the lowest levels since the beginning of the covid-19-related selloff as volatility is close to the lows in a month.
• Bid/ask spreads have declined but remain elevated relative to pre-crisis levels.</td><td></td></tr>
<tr><td>Emerging-Market Debt (EMD)</td><td>Hard Currency EM
• Following a quiet start to the week (week of April 27), hard currency EM debt was more “turbo-bid” going into month-end on Wednesday and Thursday with index spreads tightening 30bps over that period to close the week at a 605bp sovereign spread. Oil exporters outperformed following the bounce in Brent crude prices
• PEMEX remained in the spotlight, as the Mexican state-owned oil company exited the Barclays US Aggregate index at close of business Thursday. Spreads hit their all-time wides on Monday April 27 but there continued to be sufficient demand to absorb the passive supply. Bonds traded up on the week with the curve bull steepening, a good sign of normalization.
• Taking stock of the total supply picture, April’s sovereign issuance eclipsed $55bn, making it the largest sovereign issuance month in the history of EM with deals on avg 5x covered and generally trading up (as of May 1).
• Liquidity and price transparency were relatively unchanged week over week in sovereigns and quasi sovereigns, albeit still below average. Liquidity continues to show signs of marginal improvement as dealers get more comfortable operating remotely and balance sheets slowly grow

Local Currency EM
• Local EM rates continue to track macro risk and the moves in currencies.</td><td>EM IG sovereigns are 1.5x wider vs normal market conditions

EM HY sovereigns are 2.5x wider vs normal market conditions

EM IG corporates are 2.5x wider vs normal market conditions

EM HY corporates are 3.5x wider vs normal market conditions</td></tr>
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	• Liquidity is close to normal	
Securitized	**CMBS** • CMBS activity picked up this week (week of April 27) as sellers took advantage of the recent tightening to shed risk. Most of the action was at the top of the capital structure and despite the increased flows, there was no shortage of demand. Bonds were easily absorbed, and spreads tightened on the follow. • The single asset/single borrow market continues to trade well, especially office buildings and hospitality properties with strong sponsors. As opposed to the conduit universe, investors are dipping their toes into the mezzanine tranches of these deals. • Bid/offer spreads remain elevated at 20bp for 10-year AAA-rated bonds or approximately 4x normal. Illiquidity persists below the single A-rated level and bid/offer spreads remain stretched at the BBB-rated level at 5x pre-COVID levels. • Volumes in CMBX.6 remain depressed. As a result, the index is trading in a very narrow range. Due to the lack of transacting, liquidity has not improved, and bid/offer remains unchanged. Bid/offer spread for CMBX A.6 is ~2x, BBB-.6 is ~3 x and BB.6 ~5x the normal bid/offer spread. **ABS** • The ABS primary market did not see any new deals priced during the week of April 27. One Main Financial Issuance Trust (OMFIT), an unsecured consumer loan transaction, priced late last Friday (April 24) and contributed $750mn to the year-to-date supply tally of $55.7bn. In comparison, there was $82.4bn in ABS supply over the same time period last year. A few deals are currently in the pipeline for the week of May 4, but none have been officially announced for pre-marketing. • Secondary indicative spreads were unchanged to slightly tighter on the week across asset classes, building on the positive tone from the prior weeks. Credit card, prime auto loan and stranded asset ABS spreads saw a 5bp tightening on the week, while non-prime auto tightened in by 10bp and student loans and equipment were unchanged from the prior week levels. **CRTs** • CRT had a slow week (week of April 27), with only a	

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	few bid lists of any notable size. • One area that has seen trading is the seasoned B1 space, where bonds are trading in the 1000dm area. The majority of "real money" accounts continue to be buyers at these levels; the only sellers seem to be hedge funds harvesting gains. • The market for early fixed severity deals continues to decline as there has been no indication from the head of the FHFA that they will change the language in those deals to support investors. • While bid/ask spreads have come in measurably since the peak of the crisis, they've been stagnant this week given the lack of trading volume. **Legacy Non-Agency RMBS** • 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. **CLOs** • Spreads for tranches at the top of the CLO capital structure continue to march tighter. • The new issue calendar continues to expand as more and more managers are looking to dust the cobwebs off deals that would have come in early March had Covid-19 not come about. New issue AAA deals seem to have settled around 190dm. • Bid/ask spreads on AAA-rated bonds continue to be close to normal levels (~1 point); mezzanine bid/ask remains elevated at roughly 2.5x. Buyers have not come back into the market for BBB and below like they have for the rest of the stack. **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	
Money Market	• Despite speculation, the Fed kept the RRP and IOER rates unchanged leaving the Fed Funds and repo corridor at 0.00-0.10%. Fed Funds is trading at 0.05%, SOFR (repo index) set at 0.04% (as of May 1). • LIBOR continues to set lower as short-maturity markets stabilize. 1-month LIBOR set at 0.30% and 3-month set at 0.54%. • T-bill supply is becoming old news. Continued cash management bill (CMB) issuance and outsized weekly rolls of the 1-, 2-, 3- and 6-month tenors are	

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	becoming the new norm. During the week of May 4, the first CMBs issued during the crisis will mature. T-bill bid/ask spreads are normalizing back to the 2-3bp range. • There is good liquidity in the repo market, with repo rates holding tight in the middle of the 0.00 to 0.10% range.	
US Municipals	• The muni market had a weaker tone throughout the first half of the week of April 27 on the back of Senator McConnell's comments last week on the potential for a state bankruptcy option, a pick-up in mutual fund outflows, and a heavy new issue calendar building as municipalities look to raise debt to deal with budget hits due to Coronavirus. This weakness caused yields to rise across the entire curve and underperform the US Treasury rally by end of day on Wednesday. With muni/Treasury ratios above 200% in most spots and broader fixed income markets trading firmer, we did see some buyers dip their toes back in on Thursday and Friday, mostly led by SMA accounts that are not experiencing the same flows as the mutual fund complexes. By Friday, the benchmark pared its weekly losses as broader buying emerged. • In terms of liquidity, odd lots remain difficult to sell without taking a significant concession from round lot pricing. In general, <1mm pieces are still receiving bids anywhere from 3 to 6 points below round lot bidside evaluations, with the smallest pieces at the top end of that range or wider. • The high yield market remains in price discovery mode as many sellers are still not willing to hit the bids they are receiving. High yield odd lot liquidity remains challenged with it very difficult to solicit a bid. • For context, high grade odd-lots typically trade 0.10-1 points below round lot bid-side evaluations under more normal market conditions.	
Canadian Market	**Federal** • 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. **Provincial** • Liquidity is best in benchmark bonds from Quebec, Ontario and British Columbia • Concessions are requested so dealers will take less	Federal: bid/ask typically +1 to +2bp but for the long end of the curve, it can be more depending on volatility Provincial: concession of +1 to +2bp and more on size > CAD 25m,

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	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 coupon provincial issues, they will do agency trades. • The Bank of Canada's C$50bn buying program of provincial debt should support liquidity. **IG Corporates** • 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. However, the market has improved in telco and bank sectors. • The Bank of Canada's buying program of corporate debt should support liquidity in the secondary markets for BBB and higher-rated securities; BBB- are trading by appointment. **Real Return Bonds (RRBs)** • Trading "by appointment", similar to private placement market	particularly at the longer end