AllianceBernstein®

May 2020

Market Update – Daily Fixed Income Trading Liquidity Update 22 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	• 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 $5bn per day during the week of May 26 (from $6bn per day the week of May 18). This was in line with market expectations. • Global rates markets continue to be dominated by supply, central bank actions, and re-opening proxies such as oil and/or vaccine developments. • 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.	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 ~2x wider vs pre-crisis. Off-the-run Treasury bonds still trade significantly wider than on-the run bonds, but bid/offer has compressed. TIPs bid/ask is 2-3x wider vs pre-crisis levels
Investment Grade (IG) Corporates	**US IG** • US IG cash bonds stayed firm, particularly short-maturity and high-beta bonds. A “beta compression” theme dominated this week (ending May 22). • New issue supply slowed down compared to previous weeks, with $50 bn in new issues coming to market during the week of May 18. Supply is expected to be lighter during the week of May 26. • Bid/ask spreads remain wider than pre-crisis levels.	US IG spreads are generically 3-4x wider vs normal market conditions AT1/Preferreds are 2-3x 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>European IG
• It was quiet on Thursday and Friday with holidays in Europe and long weekends in the US/UK.
• There continues to be dislocation in the markets with liquidity very thin in covid-19 exposed names or in the crossover space, where names can go from “bid-less” or “offer-less” very quickly and create large moves in either direction.
• 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.

REIT Preferreds
• 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.</td><td></td></tr>
<tr><td>High Yield (HY) Corporates</td><td>US HY
• The US high yield market remained firm into the end of the week (ending May 22) despite equities moderately selling off. Market strength is attributed to inflows (into both ETFs and open-end mutual funds) as well as an expected slowdown of new issuance.
• The high yield index hit a new post-covid-19 tight level this week of 681 bp (from prior tights set April 17 of 705). This compares to March 23 wide levels of 1100 bps. Pre-crisis tight levels were 341 bps set on February 13.
• The new issue market was again active, but more so</td><td>Spreads are 0.75-1.25 point wider than normal times for BB-rated securities

Spreads are 1.5-2 points wider than normal times for B-rated securities

Spreads are 3 points wider than normal times for CCC-rated and below securities</td></tr>
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	in number of deals (20 this week) rather than amount issued ($10.4 bn). 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 and trading well in the secondary market. • Bid/ask spreads remain unchanged **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. • There has been no new issuance and overall secondary volumes have felt exceptionally light with a focus on credit-specific situations/earnings. • 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. **CDX HY** • CDX HY traded with a firm tone on May 22, but slightly underperformed stocks, CDX IG and high yield cash bonds. • Bid/ask spreads have declined but remain elevated relative to pre-crisis levels.	CDX HY bid/ask is 2-3x vs normal conditions.
Emerging-Market Debt (EMD)	**Hard Currency EM** • Dealers faced a squeeze in hard currency EM debt this week (ending May 22) as dealers with limited balance sheet continued to get further and further short. This drove spreads on the JP Morgan EMBI Global Diversified ~40 bps tighter. • Index spreads closed the week at ~535bps which is ~190bps inside of the crisis wide levels and ~240bps wide to the YTD tight levels. • On the supply front, another large-cap, below investment-grade issuer (Egypt) was able to price $5bn with a >4x covered book, an indication of investor risk sentiment and further corroboration of the squeezed market. • Taking stock of some of the largest movers, sub-Saharan Africa (SSA) was up 10 points in the last week with SSA oil exporters ~30pts off crisis lows. PEMEX was up ~10pts in the last week and ~20pts	EM IG sovereigns are 1.5x wider vs normal market conditions EM HY sovereigns are 2x wider vs normal market conditions EM IG corporates are 2x wider vs normal market conditions EM HY corporates are 3x wider vs normal market conditions

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	off the late April fallen angel lows. Costa Rica was up 8 points in the last week, ~15 points off crisis lows, and Brazil was up 8pts in the last week, ~15 points off crisis lows. • Liquidity continues to improve as transaction costs have slightly narrowed over the last week. **Local Currency EM** • Local EM rates continue to trade well, converging towards low developed-market rates. • Liquidity is close to normal	
Securitized	**CMBS** • The markets in both CMBS and CMBX appeared to stall heading into the Memorial Day holiday weekend. Traders had limited appetite to add risk, resulting in a stagnant market. Most transactions that occurred in the cash market were at the top of the capital stack which remains well supported. • In both CMBS and CMBX, liquidity remains fragile. Bid/offer spreads in CMBS remain unchanged. AA/A and BBB bid/offer spreads remain at approximately 3x and 4x pre-COVID levels. • Transaction volume in CMBX series 6 was average, resulting in little price movement since Tuesday's close. Single A, BBB- and BB prices were unchanged, +0.25 points and +0.50 points respectively. Bid/offer spreads for A.6 is ~2x, BBB-.6 is ~2 x and BB.6 ~4x the normal bid/offer spread. **ABS** • The ABS primary market priced three transactions totaling to $1.5bn during the week ending May 22 across equipment, prime auto loan and subprime auto loan sectors. This brings the year-to-date issuance to $66.0bn compared $104.9bn over the same period last year. All the new issue deals were well-subscribed and most priced at the lower end of the initial price guidance range. • There is one securitization pre-marketing for the short post-holiday week beginning May 26 (Santander Auto Receivables), and three subprime auto lenders have filed "15G" forms, signaling potential future issuance. • ABS indicative benchmark spreads saw relatively strong performance across most sectors. Spreads for credit cards and senior notes of prime auto loan ABS were 5bp and 15bp tighter over the week, respectively. Senior tranches of subprime auto loan	

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	ABS moved 5bp tighter, while subordinated tranches of both prime and subprime auto loans were 10bp tighter. Alternatively, one sector that has been lagging any tightening in spreads is rental car ABS, and on Friday evening Hertz filed for chapter 11 bankruptcy. • On a separate note, the Federal Reserve announced additional details around their TALF program this week. The first loan subscription date will be June 17, 2020 and the first loan closing date will be June 25, 2020. Under current plans, loan disbursements will only occur through September 30, 2020. **CRTs** • 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 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. • While bid/ask spreads have come in measurably since the peak of the crisis, they were unchanged week over week. **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** • 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	

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	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. **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	• 1-month LIBOR set at 0.174% and 3-month at 0.369%. Prime money market funds saw $11bn of inflows during the 7 days ending May 21, which has been driving 3-month LIBOR lower. Government money market funds saw outflows. • Repo continues to trade within a corridor of 0-0.10%. • The Fed minutes reiterated that they are unlikely to employ negative interest rates, and an IOER (interest rate on excess reserves) rate adjustment seems off the table.	
US Municipals	• The municipal market tone continues to be strong, with benchmark yields trading 2-5bp tighter each day during the week ended May 22. • Most new issuance this week was 7-12x oversubscribed, showing the amount of demand and cash on the sidelines. • One state with notable outperformance is California, which has seen spreads tighten significantly – from +30 to 35 bps to +0 to 15 bp, seemingly in anticipation of expected coupon reinvestments in June. • The first true muni high yield deal came to market this week, and it was well received, trading up significantly on the break. Generically, despite some signs of life, high yield munis are still in price discovery mode with many sellers feeling sticker shock on some bid levels vs evaluations, and not trading. • Odd lot liquidity remains challenged compared to historic averages. There was a marginal decrease in	

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	odd lot penalties during the week ending May 22, but they remain generically in a 1-3 point range below round lot bidside evaluations for high quality bonds. For context, high grade odd lots typically trade 0.10-1 points below round lot bidside 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 is helping 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-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. The market has improved in sectors such as banks. • 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. BBB- bonds are trading by appointment. **Real Return Bonds (RRBs)** • The official announcement of a $400mn RRB auction of the long Canada 0.5% Dec. 2050 on May 27 should support liquidity in the benchmark RRB bond. • 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. The BoC will be buying, once per quarter in a reverse auction format, up to $100m notional each of the 7 Canada RRBs from	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, particularly at the longer end Large bid/ask spread on BBB- corporates, which are trading by appointment in many cases and as wide as 25 bp in certain cases. Provincial RRBs trading by appointment only. Dealers do not hold these securities on their balance sheet.

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	2021 to 2047 in the secondary markets.	

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