April 2020

Market Update – Daily Fixed Income Trading Liquidity Update 28 April 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 $10bn per day during the week of April 27 (from $15bn per day the week of April 20). • Rates markets began the week with bear steepening, as the spread between 5- and 30-year US Treasuries steepened by 3.5 bp. The move in bonds so far this week has been futures-led as cash volumes are low ahead of the FOMC meeting Wednesday. • The big recent improvement has been in Treasury market depth, which had fallen by as much as 90+% in the worst of the crisis in March but has recovered to 55-65% of the average depth over the last year. • Rate volatility continues to fall and there continues to be good "two-way" trading in the market. • While still relatively liquid in most contracts, depth in the Treasury futures market is also much lower vs historical averages. Trading in "ultra" contracts is challenging. • The TIPS market outperformed to start the week, with breakeven inflation rates 3-4 bp higher. But 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)	**US IG** • US IG cash bonds have been holding up well despite	US IG spreads are generically 4x wider vs

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Corporates	an increase in macro volatility. • New issue supply remains busy and May is expected to be another heavy supply month. $25.5 bn in new issues came to market on April 27-28, and subscriptions remain healthy. Of note, the first US preferred deal since the covid-19-related selloff began came to market, which attracted very strong demand and traded up in the secondary markets. • 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. • 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 began to pick up modestly in the European IG market at the end of last week/beginning of this week (as of April 28), with niche and less well-known names continuing to tap primary markets. • 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 April 28, trading volume continued to be very light.	normal market conditions AT1/Preferreds are 2-3x wider vs normal market conditions
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 April 28, the US high yield market was mixed,	Spreads are 1 point wider than normal times for BB-rated securities Spreads are 1-2 points

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	with bonds ranging from down 1 point to up 1 point, depending on the issuer. • With no new issues announced, focus returned to solely secondary trading, but focus is expected to shift back to new issues as the week continues. **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. • On the new issue front, the first two deals came to market last week. Netflix issued a BB-rated, 5-year bond with a reasonably small concession (20bp) at 3% yield. Books were 5x oversubscribed and bonds have subsequently traded up. Merlin entertainment (owners of UK theme parks and Legoland globally) issued a B-rated secured deal that was largely driven by reverse inquiry. The deal was upsized, came at 7% yield, and has subsequently traded up. Net-net the first signs of issuance highlight the constructive market tone. • Idiosyncratic risk is in focus as potential defaults/restructurings loom. The latest such events included Hertz hiring restructuring advisors and the decision by Codere (Latin America and European gaming company) to defer April 30th coupons and enter the grace period. Both events caused initial volatility but after being digested neither have resulted in as material a move in prices as might be expected (bonds were unchanged to down 1-2 points). • 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 has been very quiet so far this week (as of April 28) with trading volumes remaining at the lowest levels since the beginning of the covid-19-related selloff. • On April 28, CDX HY underperformed CDX IG after a series of trigger events and the HY/IG spread ratio of 7.15x hit 2009 levels. Bid/ask spreads have declined but remain elevated relative to pre-crisis levels.	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.
Emerging-	**Hard Currency EM**	

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<tr><th>Sector</th><th>Liquidity Trading Comment</th><th>Bid-Ask Spreads</th></tr>
<tr><td>Market Debt (EMD)</td><td>EM had a quiet start to the week on April 27-28. Index spreads were unchanged overall with Latin American sovereigns underperforming following a wave of recent supply in the region
Trading is active in PEMEX as it moves from passive index investors to other investors amid its recent downgrade and impending exit from indexes at the end of the month (Thursday).
Liquidity and price transparency were relatively unchanged week over week in sovereigns and quasi sovereigns, albeit still below average.
Profit taking in the high yield corporate market has subsided, with relatively low volumes across the board.
Local Currency EM
Local EM rates continue to track macro risk and the moves in currencies.
Liquidity is close to normal</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>
<tr><td>Securitized</td><td>CMBS
CMBS activity picked up this week (as of April 28) 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
In ABS, it was a light start to the week (as of April 28) as dealers traded ~$1.3bn for the first 2 days, compared to the 20-day daily average of ~$1.2bn. In</td><td></td></tr>
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	secondary markets, spreads are generally tighter for credit cards and prime auto ABS. The lack of primary supply is a positive technical this week. • On the ratings front, Moody's Investors Service has downgraded and placed on review for further possible downgrade 11 tranches of rental car ABS issued by Hertz and 32 tranches of rental car ABS securities issued by Avis. Overall fleet auto spreads are 50 to 75 bp wider. • The final batch of recent remittance data show forbearance increasing across multiple sectors, partially driven by special forbearance servicing, (i.e. delinquent borrowers automatically moved into forbearance). It remains too early to tell if this is a short-term blip or a long-term trend. **CRTs** • CRT had a slow couple of days to start off the week (as of April 28), with only a 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	

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	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	• Money markets were quiet ahead of the April 29 FOMC meeting. Although largely uneventful for other markets, money markets are watching this closely. Speculation is that the Fed could make technical adjustments to the Fed RPP and/or interest on reserves by 0.05% to get front-end rates off the floor and trading in the middle of the 0-0.25% Fed corridor. • LIBOR continues to set lower as short-maturity markets stabilize. 1-month LIBOR set at 0.40% and 3-month set at 0.76%. • Continued T-bill supply has been met with strong government money market inflows. This is keeping T-bill and repo yields suppressed within the Fed band. T-bill bid/ask spreads are normalizing back to the 2-3bp range.	
US Municipals	• Municipal market weakness continued on April 28. Amid outflows picking back up, Senator McConnell's comments last week on the potential for a state bankruptcy option, and a large new issue calendar on the horizon, there was a noticeable uptick in sale lists in the market. Current conditions have resulted in wide bid/ask spreads for round lots and cheaper than expected clearing levels for sellers. • Odd lot penalties were wider than recent days with larger lots (>100k) seeing 3-4 point discounts from bidside evaluations, while smaller lots (5-15k) saw an average of 6 point haircuts. For context, high grade odd-lots typically trade 0.10-1 points below round lot bid-side evaluations under more normal market conditions. • While new issues that have come over the past few weeks have generally been met with oversubscription, and in some cases tighter spreads than secondary market trading of similar names, the weakness in secondary markets seems to finally be spilling over into the primary space. Deals are coming at significant concessions and still having trouble getting done. Notably, the NY MTA deal that was slated to come this week has been postponed	

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	until next week, which does not read well as to the demand for the upcoming issue. The State of Illinois also announced $2.2bn coming the week after next, which will be another widely watched deal as they are the lowest-rated state at BBB-. • Even with current technical factors weighing on markets, the expanded Fed MLF facility that was announced on April 27 is seen as positive news for the largest portions of the market. The program bifurcates traditional higher-quality muni borrowers from the high yield market. While these high-profile investment-grade issuers already had many tools to get them through the crisis, this Fed program effectively created a giant 3-year backstop in case those tools don't work.	
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 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)**	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

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	• Trading “by appointment”, similar to private placement market	

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