

Market Update – Daily Fixed Income Trading Liquidity Update 30 March 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 08-09 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	<ul style="list-style-type: none"> The open-ended bond purchase program enacted by the Fed is having a positive effect on liquidity and market functionality. The Fed will lower daily purchases from \$75bln to \$60bln per day across the curve beginning April 2-3. There continues to be good “two-way” trading in the market. Most US Treasury buying comes during the Fed operations. Long bonds continue to trade poorly after the Fed 20- to 30-year maturity purchase operations end at 2pm in NY. Depth in the US Treasury cash bond market has improved and is about 80% of pre-crisis levels in on-the-run bonds. Moving large blocks of Treasuries takes more time than usual. 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. 	<p>Bid-offer spreads for on-the-run benchmark 5-year US Treasury notes are 2x wider vs pre-crisis conditions. For the 10-year note, bid/ask is ~3x wider vs pre-crisis.</p> <p>Off-the-run Treasury bonds may trade significantly wider than on-the run bonds.</p>
Investment Grade (IG) Corporates	<p style="text-align: center;">US IG</p> <ul style="list-style-type: none"> US IG cash bonds traded with a positive tone on March 30, despite another heavy supply day. New issue supply was \$37 bn on March 30. Demand continues to be strong, and the supply has shifted to more lower-quality issuers vs the higher quality names in the past couple weeks. Credit curves remain flat but short-maturity bonds continued to normalize as we saw strong demand in short maturities. Bid/ask spreads remain wider than pre-crisis levels but have trended tighter. 	<p>US IG spreads are generically 4-5x wider vs normal market conditions</p> <p>AT1/Preferreds are 4-5x wider vs normal market conditions</p>

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	<p style="text-align: center;">European IG</p> <ul style="list-style-type: none"> • The European IG market continues to see heavy supply, which has come with large concessions, and deals have been multiple times oversubscribed. • We see a continuation of last week’s theme, that primary market issuance also helped improve the secondary market where liquidity continues to improve, although volumes are light. • In the AT1 (subordinated financial) market, there was guidance over the weekend for larger European banks not to pay equity dividends, which led to the suspension by Rabobank (which does not have equity) of coupon payments on their member certificates. While AT1 prices moved lower, this move seemed like more of a continuation of profit-taking that began Friday evening rather than concern over AT1 coupons not being paid. Consequently, liquidity in 2 to 5m size trades remained intact for the major European banks. <p style="text-align: center;">REIT Preferreds</p> <ul style="list-style-type: none"> • 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 March 30, traded volume was slightly lower than the 20-day average. 	
High Yield (HY) Corporates	<p style="text-align: center;">US HY</p> <ul style="list-style-type: none"> • The tone of high yield in recent weeks has been tied to equities—with high yield closely following equities moves. • High yield cash bonds were up on March 30. • High yield ETFs traded rich vs their NAV again • Of note, the high yield market had its first new issue in weeks – 600 million issued by YUM Brands, about 200 bps cheaper to existing bonds, and 10x oversubscribed. We expect to see more issuance as the week progresses. <p style="text-align: center;">European HY</p> <ul style="list-style-type: none"> • Daily sentiment continues to follow equities and the iTraxx Crossover index, however cash bonds have started to outperform the index, particularly in down markets and in higher-quality credits. • Dealer liquidity is minimal and has deteriorated as 	<p>High yield spreads are 2 to 3x wider than normal times for BB and B securities and 3 to 5x wider for CCC</p> <p>CDX HY bid/ask is 4-5x vs normal conditions.</p>

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	<p>more participants shift to work from home locations. Dealer balance sheet usage is increasingly restricted with most trades >2million needing to be done on an agency basis.</p> <ul style="list-style-type: none"> • Overall liquidity remains challenged in both directions (bid/offer) as investor conviction levels are not high and sentiment is skittish around macro moves. • Cash bond markets have stabilized with investors left “better buyers” looking to deploy cash they’ve raised. Bid/ask spreads are still wide, but there is a less panicked tone. Sellers are primarily funding outflows or building up cash balances/reducing risk in the anticipation of further outflows/volatility, but outflows appear to have slowed (although remain negative), and cash balances have been built up. The selling pressure we saw from ETFs has also significantly reduced. <p style="text-align: center;">CDX HY</p> <ul style="list-style-type: none"> • CDX HY traded with a weaker tone on March 30. Synthetics underperformed cash bonds as investors put hedges back on. 	
Emerging-Market Debt (EMD)	<p style="text-align: center;">Hard Currency EM</p> <ul style="list-style-type: none"> • EM continues to exhibit dispersion between oil exporters and non-oil exporters, with exporters underperforming as Brent crude prices fell ~9% on March 30. • Liquidity and price transparency have improved in sovereigns and quasi sovereigns, albeit still significantly below average. Liquidity in EM corporates remains very challenged; most trading has been in sovereigns and quasi-sovereigns <p style="text-align: center;">Local Currency EM</p> <ul style="list-style-type: none"> • For the most part, Local EM prices are tracking macro risk and the moves in currencies. • Liquidity has moved towards normalization 	<p>Bid/ask spreads have tightened from last week’s levels:</p> <p>EM IG sovereigns are 1.5x wider vs normal market conditions</p> <p>EM HY sovereigns are 2x wider vs normal market conditions</p> <p>EM IG corporates are 3x wider vs normal market conditions</p> <p>EM HY corporates are 5x wider vs normal market conditions</p>
Securitized	<p style="text-align: center;">CMBS</p> <ul style="list-style-type: none"> • The last new issue in the CMBS market priced March 11th. In the secondary market, the tone remains firm for the highest quality securities. AAA-rated senior securities’ spreads are now trading firmly inside of s+200. These bonds traded in the low 300s 	

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	<p>only a week ago. Mezzanine classes, whether in the conduit or single asset/single borrower markets, struggle to find a bid.</p> <ul style="list-style-type: none"> • Away from the conduit market, AAA-rated single asset securities continue to trade well. Industrial properties, hotels/resorts with strong sponsorship, and high-quality multi-family are all in demand. • Bid/ask spreads remain elevated: AAA-rated spreads have moderated and are roughly 2x wider vs normal conditions. BBB-rated bonds are roughly 5x wider vs normal conditions, and BB-rated are roughly 7x wider. • Liquidity in the CMBX market continues to improve and bid/ask spreads are narrowing. Series 6 BBB-, considered one of the most liquid mezzanine tranches, now generally trades within a 1.0-1.5 point wide market. Under normal conditions this is as tight as 0.25-0.50 points. However, this is a marked improvement from the 3-5 point wide markets we saw just last week. <p style="text-align: center;">ABS</p> <ul style="list-style-type: none"> • In ABS, 2-year AAA-rated credit card and prime auto ABS tightened another +10bp breaking through +100 bp spread for the first time since March 11th. But more subordinated tranches are still experiencing pressure on spreads amid shifts in loss expectations. • Secondary supply is muted, and the approach of quarter end may further dampen action until Wednesday. Demand has been focused in higher-quality, shorter average life ABS, with limited trading in lower-quality tranches. • While new issues have been sidelined by the market volatility, we expect that TALF 2.0 should help restart the new-issue market as TALF 1.0 did during the Great Recession. But it may not begin until May/June and details remain light. <p style="text-align: center;">CRTs</p> <ul style="list-style-type: none"> • Trading in the CRT market has been significantly challenged, partly because of the challenges in the repo/commercial paper market. • Prices have declined meaningfully amid unknowns about the mortgage market and fears of forced liquidations from REITs and hedge funds. • We have begun to see more “two-way” trading flow in seasoned investment-grade and below-investment-grade last cash flow (lower tranche) bonds 	

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	<ul style="list-style-type: none"> • Discount margin spreads are still at very wide levels – multiple times their pre-crisis levels, but have narrowed a bit – tightening has been most pronounced for seasoned (earlier vintage) investment-grade last cash flow bonds but there has been modest tightening in newer vintage last cash flow bonds as well. Equity tranches have more challenged liquidity with limited trading. Bid/ask remains wide at roughly 2-3x normal. <p style="text-align: center;">Legacy Non-Agency RMBS</p> <ul style="list-style-type: none"> • Legacy RMBS continues to trade through the recent crisis. Since January spreads have widened from ~ 200bps to now > 1000 bps, but demand for the sector never really faded. <p style="text-align: center;">CLOs</p> <ul style="list-style-type: none"> • After challenged liquidity in recent weeks, trading has improved in AAA-rated tranches. Liquidity in lower-quality tranches remains challenged. Bid/ask spreads remain 2-3x wider relative to typical levels. <p style="text-align: center;">Agency MBS</p> <ul style="list-style-type: none"> • Agency MBS spreads are tighter week-over-week. • Bid/ask spreads vary by coupon, with low coupon (2.5%) TBAs back to historical averages, and the rest of the coupon stack trading much wider, at 2-6x higher vs pre-crisis levels 	
Money Market	<ul style="list-style-type: none"> • The Treasury started issuing “cash management” T-bills (CMB) to begin funding the \$2 trillion stimulus—this wasn’t expected until after quarter-end. The \$114bln in net new supply was a welcome relief and pulled most bills out of negative territory. The 3-month bill auctioned at 0.085% while the 6-month bill drew 0.10%. As anticipated, this supply has already started to widen the government money market curve. • Most of this new issuance does not settle until after quarter-end which did not help “same-day” or “cash settle” liquidity, making it a continued challenge to put money to work. Limited dealer inventory in governments and no additional dealer repo resulted in \$237bln done at the Fed reverse repo facility (RRP). • LIBOR set slightly lower: 0.985% on 1-month, 1.433% on 3-month. Recent rises in LIBOR levels reflect short-term funding stresses. • No material difference in the CP market challenges. 	

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	<p>Most paper trading remains primarily overnight or one-week term, and mainly high-quality issuers.</p>	
US Municipals	<ul style="list-style-type: none"> • Tone in the municipal market was a bit softer on March 30. • After weeks of postponed deals, there is strong demand for high-grade municipal new issues. A \$150 million AAA-rated deal that came on March 30 tightened 12-15 bps and books were 10x oversubscribed. • Liquidity in high yield municipals remains challenged • Odd-lot liquidity is still significantly reduced vs several weeks ago and was a bit worse on March 30 compared with last week. Odd-lots traded 2-8 points below bid-side evaluations; compared with 1-4 points below last week. For context, high grade odd-lots typically trade 0.10-1 points below bid-side evaluations under more normal market conditions. 	
Canadian Market	<p style="text-align: center;">Federal</p> <ul style="list-style-type: none"> • Liquidity is best in benchmark issues for block sizes of <=CAD15m; very limited liquidity in off-the-run, high coupon bonds <p style="text-align: center;">Provincial</p> <ul style="list-style-type: none"> • Liquidity is best in benchmark bonds from Quebec, Ontario and British Columbia, but concessions can be high; very limited liquidity in oil-generating provinces (Newfoundland, Alberta, Saskatchewan) amid sharp decline in Western Canadian Select oil price • Most dealers will not bid on off-the-run, high coupon provincial issues <p style="text-align: center;">IG Corporates</p> <ul style="list-style-type: none"> • Limited liquidity; many dealers forced to reduce balance sheet inventories, so unable to provide bids in many sectors. • Trading on an agency basis for high-beta issuers. However, market has improved in telco and bank sectors. • Liquidity limited even in higher-quality, senior bank deposit notes <p style="text-align: center;">Real Return Bonds (RRBs)</p> <ul style="list-style-type: none"> • Trading “by appointment”, similar to private placement market 	<p>Federal: bid/ask typically +1 to +2bp; can be more depending on volatility</p> <p>Provincial: +3 to +5bp or more on size < CAD 10m</p>

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