ALLIANCEBERNSTEIN®

July 2020

Market Update – Daily Fixed Income Trading Liquidity Update 3 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. • The shortened holiday week ended July 2 saw global developed market rates selloff a few basis points amid low volumes as per typical of summer trading sessions. • Stocks traded higher and textbook "risk-on" price action played out in steepening of yield curves globally, tightening of peripheral European bond spreads, and TIPs putting in solid performance with 5-year breakevens widening.	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** • US IG cash bonds performed well on the back of firmer macro tone during the week ending July 2. • The primary market was quiet, with $17 bn in new issues coming to market between June 29-July 2, which continues to help market technicals. • Bid/ask spreads remain wider than pre-crisis levels.	US IG spreads are generically 2x wider vs normal market conditions AT1/Preferreds are 2-3x wider vs normal market

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	European IG • Very quiet as the market wound down into the US 4th of July holiday. 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** • Secondary volumes were quiet during the shortened week ended July 2. • With the increase in covid-19 cases and associated equity market volatility, there was some selling of travel-related issuers as momentum investors reduced risk. • New issues were light relative to prior weeks with \$3.8bn of bonds coming to market, dominated by ~\$2bn of issuance from Thyssen Elevators • It continues to be a sellers' market as most deals are multiple times oversubscribed and priced at the tight end of initial price guidance. **CDX HY** • CDX HY traded better along with macro tone but underperformed both stocks and CDX IG during the week ended July 2. • 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.	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.
Emerging-Market Debt (EMD)	**Hard Currency EM** • It was very quiet again for hard currency EM debt during the week ending July 3, as the JP Morgan EMBI Global Diversified Index closed the week 14 bps tighter following the strong tone in global macro risk. • With secondary market volumes still quite limited, focus continues to be on the primary market.	EM IG sovereigns are back to normal market conditions EM HY sovereigns are 1.5x wider vs normal market conditions

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	Corporate issuance has continued at a brisk clip with 5 corporate deals pricing, generally multiple times oversubscribed and trading up on the break on average. **Local Currency EM** • Liquidity is close to normal.	EM IG corporates are 1.5x wider vs normal market conditions EM HY corporates are 2x wider vs normal market conditions
Asia	**Asia Hard Currency** • Asia hard currency credit spreads remained relatively flat in the week ended July 3, as the market was caught between hopes of post-COVID economic recovery and fears of rising infections. • In the primary market, 7 issuers raised ~USD 2.3bn last week, a meaningful decline from the preceding weeks, due in part to public holidays in Hong Kong (July 1: HK SAR Day) and the US (July 3: observed Independence Day) • Liquidity was constructive and flows were generally two-way; Asia credit was firm, but otherwise little impacted by the China equities rally and onshore rates selloff. **Asia Local Currency** • Asia local currency debt liquidity functioned as normal for the most part during the week ended June 26. • The Indonesian rupiah saw some volatility after the "burden sharing" headlines between the Finance Ministry and Bank Indonesia, but reaction in local currency bonds was limited. • China rates were relatively stable after the Dragon Boat Festival holidays in the previous week despite continued supply of government bonds.	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
Securitized	**CMBS** • The CMBS/X markets saw anemic trading volumes and little desire to add risk as investors approached the 4th of July holiday weekend. There is little supply expected in the near term. 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 one subprime auto loan transaction for the week ending July 2, totaling	

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	$118.3mn. ABS year-to-date supply now stands at $80bn compared to $190bn recorded in 2019 over the same time period. • Benchmark ABS spreads remained unchanged for credit cards on the week and tighter for prime and subprime autos, benefiting from the lack of primary issuance and dealer inventory levels at the lows. • There are four issuers pre-marketing for the week beginning July 6. **CRTs** • Similar to other markets, trading volumes were anemic heading into the holiday weekend. • Two new issues from Freddie Mac and Arch Mortgage Insurance priced during the week ended July 2, the first since the covid-19 crisis hit. Participation was strong and syndicates were able to tighten spreads from their initial price thoughts and meaningfully increase deal size, indicating the pent-up demand for the sector. • Bid/ask spreads continue to shrink. 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	

<table>
<tr><th>Sector</th><th>Liquidity Trading Comment</th><th>Bid-Ask Spreads</th></tr>
<tr><td></td><td>Fed buying and increased investor interest. Bid/offer for lower coupon bonds is just ½ of a tick wide.</td><td></td></tr>
<tr><td>Money Market</td><td>There were $55bn in flows out of government money market funds over the 7 days ending July 2. There were $7bn out of prime funds over the same period. These outflows help explain slightly higher repo rates, although levels are not materially different.
The commercial paper to T-bill spread remains narrow at ~10 bps.
1-month LIBOR set at 0.165% and 3-month LIBOR set at 0.27%. SOFR set at 0.11%</td><td></td></tr>
<tr><td>US Municipals</td><td>The muni market was unchanged amid light secondary trading volumes over the shortened holiday week ending July 2.
In the primary market, deals continue to be well-received with oversubscriptions in the 5-10x range. New issue volumes are back to expected levels with $46bn issued in June.
Overall tone in the market continues to remain positive supported by a strong technical backdrop with reinvestment capital received from coupon and redemption payments and 7 consecutive weeks of inflows.
Odd lot liquidity continues to slightly improve. On average, high-grade odd lots are generally being bid 0.5 to 2 points below round lot levels, with high yield odd lots receiving 1 to 3 point haircuts.</td><td></td></tr>
<tr><td>Canadian Market</td><td>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
Provincial
Liquidity is best in benchmark bonds from Quebec, Ontario and British Columbia
Concessions are requested so dealers will take less-liquid positions.
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</td><td>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</td></tr>
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	trades, even with the Bank of Canada's buying program of provincial debt (C$4.77bn purchased 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$130mn 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.

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