April 2020

Market Update – Daily Fixed Income Trading Liquidity Update 9 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 will reduce their purchases of US Treasuries to $30bn per day during the week of April 13-17 (from $50bn per day the week of April 6). • Market depth has risen to the highest levels since early March, yet is still off the highs from early February. Volumes were at ~60 to 70% of recent averages for much of the week. • 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.	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 performed strongly for the week ending April 9, especially after the Federal Reserve's announcement of their credit facility details. BBB-rated bonds continued to outperform. • New issue supply slowed heading into the long weekend, with $8.5 billion in new deals coming to market on April 8 and none on April 9. Along with the strong tone in the secondary market, demand was strong with deals 6.9x oversubscribed on average. • Credit curves, in particular the 5-year part of the curve, continue to normalize across the quality	US IG spreads are generically 4-5x wider vs normal market conditions AT1/Preferreds are 4-5x wider vs normal market conditions

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	spectrum. The very front end of the curve (1-3 year) has begun to steepen but is still relatively flat compared to history. • Bid/ask spreads remain wider than pre-crisis levels. Odd-lot liquidity is still challenged, but not to the same extent seen a couple weeks ago. **European IG** • The European IG market continues to see heavy supply. Concessions for high quality/ECB eligible bonds have trended down, while lower-quality issuers continue to see larger concessions. Broadly, subscription levels remain high. • As more niche / lower quality issuers bring new deals to the primary market, this continues to improve secondary market liquidity as a new clearing level for risk is re-struck. • Similar to European high yield, conviction levels are waning from the dealer community in the AT1 (subordinated financial) market, given the decent bounce in prices off the lows, particularly in light of the cheap senior bank supply that has come to market. Adding to this, dealers have lightened up their balance sheets heading into the Easter holiday. As such, bid/offer spreads have widened—more so on the offered side. **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 9, 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 April 9, the market was very firm, with select fallen-angels (bonds that were originally investment-grade but have been downgraded to below-investment-grade) rallying in particular amid the news that that the Fed will purchase HY ETFs and certain fallen angel debt. • Bid/ask spreads remained unchanged, but offered sides were indicative only amid market strength and	High yield spreads are 2 to 3x wider than normal times for BB and B securities and 3 to 5x wider for CCC CDX HY bid/ask on April 9 was 7-8x vs normal conditions.

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	the approaching long weekend. Volumes were light as there were few sellers in the market. **European HY** • Amid the US Fed's announcements related to the purchase of certain fallen angel debt, select fallen angels rallied on April 9. • Daily sentiment continues to follow equities and the iTraxx Crossover index, but cash bonds continue to outperform the iTraxx index. In periods of softness in equities/iTraxx there have still generally been buyers of cash bonds. • Some hedge funds expressed a more bearish view in recent days, setting shorts with the expectation for weaker equity/macro markets as the US moves into an expected peak of virus spread. • Light dealer inventories have exacerbated the positive technical in the market as equities/macro products have generally been supported and "real money" investors have looked to spend cash. • Investors are becoming more discriminating among lower-quality issuers, as dispersion increases and restructuring headlines begin to appear. • Dealer liquidity is minimal and has deteriorated as 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. • Overall liquidity remains challenged, but trading is happening. Since the Euro HY market has had no new issuance, it is increasingly hard to put cash to work – it is easier to sell than to buy. However, we expect the new issue pipeline to slowly build with higher-quality issuers if the macro picture remains more stable. The first new issue deals are expected to come during the week of April 13, which should bring more two-way flow to the market. • Bid/ask spreads are still wide, but there is no more panic in the market. Sellers are primarily opportunistic, selling on strength in relative outperformers or rotating out of more challenged issuers. Outflow-driven sellers have not been prominent in the past several sessions. **CDX HY** • CDX HY traded with very firm tone on April 9 following the announcement of the Fed's credit facility details – particularly the surprise that the Fed will purchase HY ETFs and certain fallen angel debt.	

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<tr><th>Sector</th><th>Liquidity Trading Comment</th><th>Bid-Ask Spreads</th></tr>
<tr><td></td><td>Trading volumes increased on April 9, but bid/ask spreads also widened from earlier in the week due to volatility.</td><td></td></tr>
<tr><td>Emerging-Market Debt (EMD)</td><td>Hard Currency EM
Hard currency EM debt experienced a short squeeze on April 9 as index spreads tightened following the Fed’s asset purchase program expansion.
Investment-grade new issuance continued its torrid pace. The week of April 13 is expected to be a busy week of issuance in the Latin American investment-grade sovereign market.
Liquidity and price transparency have improved in sovereigns and quasi sovereigns, albeit still below average. Liquidity in EM corporates remains very low – while corporates rallied along with the rest of the market on April 9, liquidity was as challenged during the rally as it was during the recent selloff.
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
AAA-rated CMBS spreads tightened dramatically on April 9 after the Fed announced that AAA-rated non-agency CMBS issued prior to March 23 would be eligible for inclusion in the TALF program. AAA-rated bonds that traded as wide as s +225 bps on April 8, traded as tight as s +140 bps. However, the rally did not spill over into lower-rated tranches, as A-rated bonds were still trading at >+600, and the market for BBB-rated bonds remained distressed.
Despite the positive performance, bid/offer spreads remain wide and are 4x normal in the AAA-rated space. BBB-rated bonds are roughly 5x wider vs normal conditions, and BB-rated are roughly 7x wider.
CMBX performed in line with other credit markets. There was consistent 2-way flow most of the day, and at times bid/offer tightened, but returned to wider levels toward the end of the day. 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, the Fed’s actions on April 9 led to tighter spreads on AAA-rated bonds on lighter volume ($2.7bn). AAA-rated, 2-year prime auto ABS closed</td><td></td></tr>
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	25 bps tighter for the week, at ~+80 bps. • The Fed confirmed that the rebooted TALF program will include only new-issue, AAA-rated ABS – as "legacy"/secondary-market ABS were not included (although legacy CMBS and CLOs were). • ABS sectors that were left out of TALF eligibility include Verizon Device Payment, FFELP and unsecured consumer loans. Aircraft and esoteric ABS were also not included, but were not expected to be. **CRTs** • Trading in the CRT market has been significantly challenged, partly because of the challenges in the repo/commercial paper market. • But CRTs ended the short week on a very firm tone. The news of the Fed adding CRT bonds as eligible collateral for the Primary Dealer Credit Facility (PDCF) gave the market a reason to rally on April 9 – with even equity tranches (which had not joined other rallies in the past couple weeks) performing well. • Bid/ask spreads remained elevated in equity tranches and were in the 50 to 100 bps range for Last Cash Flow tranches. • Discount margin spreads are still several times their pre-crisis levels. **Legacy Non-Agency RMBS** • 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. **CLOs** • The CLO market also experienced Fed-related spread tightening. The Fed agreed to include AAA-rated tranches of static CLO deals in the TALF program. • Spreads on AAA-rated tranches are now <200 bps; AA-rated ~275 bps; A-rated in the low 400 bps range; BBB in the high 600 bps range and BB-rated ~1200bps. • Bid/ask spreads on AAA-rated bonds continue to be close to normal levels (~1 point); mezzanine bid/ask remains ~3x wider relative to typical levels as dealers remain defensive. **Agency MBS** • Bid/ask spreads vary by coupon, with low coupon	

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	(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	• Another $125 bn in cash management bills (CMB) were announced by the US Treasury on April 9, bringing the total announced to $705 bn. They have also increased their weekly T-bill rolls. The April 9th auction saw 2-*month* T-bills trade with a higher yield (+0.29%) than 2-*year* Treasury notes. • The Federal Reserve's Reverse Repo facility (RRP) for money market funds saw subscriptions fall to $5 bn on April 9 (from $285 bn at quarter end). The Fed has successfully controlled the supply and demand for cash at 0% to 0.10%. There is an unlimited facility to park cash at 0% (the RRP) and the Fed is also still doing $500 bn in Open Market Repo Operations twice daily to provide cash at 0.10%. • LIBOR continues to set lower as funding pressure subsides. 1-month LIBOR set at 0.814 % and 3-month set at 1.22%.	
US Municipals	• The Fed was the major headline in the municipal market on April 9, announcing that they will buy up to $500 bn of notes out to 2 years from eligible municipal issuers. This should provide relief to short-term liquidity concerns. • April 9 saw the fifth straight day of lower yields. The market remains volatile, with 5-10 bps daily moves in benchmark bonds, which were uncommon prior to the current crisis. • There is still a significant amount of primary market supply that has been sidelined as deals were pulled or postponed over the past few weeks. New issue supply totaled close to $5bn during the week of April 6. For the week of April 13, estimates suggest $3.5bn in new issuance scheduled with about $15bn currently on day-to-day status. • Liquidity in high yield municipals remains challenged. • Odd-lot liquidity is still significantly reduced vs several weeks ago. High grade odd-lots are now trading roughly 3-6 points below bid-side evaluations. For context, high grade odd-lots typically trade 0.10-1 points below bid-side evaluations under more normal market conditions.	
Canadian Market	**Federal** • Liquidity is best in benchmark issues for block sizes of <=CAD15m; very limited liquidity in off-the-run, high coupon bonds	Federal: bid/ask typically +1 to +3bp; can be more depending on volatility

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	Provincial • Liquidity is best in benchmark bonds from Quebec, Ontario and British Columbia, but concessions can be high; very limited secondary-market liquidity in oil-generating provinces (Newfoundland, Alberta, Saskatchewan) amid new lows in the Western Canadian Select oil price. • Most dealers will not bid on off-the-run, high coupon provincial issues **IG Corporates** • 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 **Real Return Bonds (RRBs)** • Trading “by appointment”, similar to private placement market	Provincial: +2 to +5bp or more on size < CAD 10m

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