ALLIANCEBERNSTEIN®

December 2020

Market Update – Fixed Income Trading Liquidity
For the Week Ended 24 December 2020

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 at the end of each week.

Sector	Liquidity Trading Comment	Bid-Ask Spreads

US Treasuries	• Key themes during the week ended December 24:
	  ○ Positive momentum around vaccine distribution is serving as a positive catalyst for risk assets. Domestic equities are making new highs and government bond yields are moving higher as the signing of the latest covid-19 fiscal stimulus measure by President Trump also removed uncertainty.
	  ○ From a liquidity standpoint, trading volumes in US Treasuries are running at 50-60% of their 10-day averages as holiday liquidity and thin trading has taken hold.
	  ○ From a price action standpoint, the trend higher in yield and steeper in curve is how the market has been positioned so there has been little in terms of "pain trades" or "stop outs"
	• Federal Reserve bond purchases stand at \$80 billion US Treasuries and \$60 billion MBS per month.
		Bid-offer spreads for 2 to 10-year maturities are running at their recent averages, but the 30-year point is 2-3x more expensive to transact given the poor liquidity

Investment Grade (IG) Corporates	**US IG** • Flows quieted down materially during the holiday-shortened week ended December 24, with volumes well below recent averages. • Despite the lower volumes the tone was constructive with the IG index closing a touch better to +99 bp. In a trend similar to the prior week, dealers sold ~\$4bn in IG bonds during the week, for a month-to-date total of \$9.5bn bonds sold. • As expected, liquidity continues to thin as dealer appetite remains light heading into year end. • The technicals remain supportive, as the market saw inflows of \$2.53bn and supply is expected to remain muted until January 4. Additionally, dealer balance	US IG spreads are generically 1-1.5x wider vs normal market conditions AT1/Preferreds are 1-1.5x wider vs normal market conditions

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	sheets remain light given the amount of bonds they have sold over the past few weeks. • Bid/ask spreads remain wider than pre-crisis levels. **European IG** • During the week ended December 24, liquidity was very thin as the holiday period caused more muted market trading over Brexit and US stimulus headlines. Overall technicals remain decent. **REIT Preferreds** • Liquidity in the REIT preferred market is typically limited under more normal conditions given the retail nature of the investor base. Current liquidity is better than in March and April but is still not back to normal. • 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.	
High Yield (HY) Corporates	**US HY** • During the week ended December 24, the US HY market was flat on very light trading as the holidays approached. No new issues priced during the week. • The HY index spreads were 2 bp wider to 378 bp. This compares to March 23 wide levels of 1100 bp and pre-covid-19 tight levels of 341 bp on Feb 13. **Euro HY** • During the week ended December 24, liquidity was very thin as the holiday period caused more muted market trading over Brexit and US stimulus headlines. Overall technicals remain decent. **CDX HY** • CDX HY traded a touch softer during the week ended December 24, in line with the broader macro tone. Trading volumes continued to drop as the traditionally slow holiday period began. Bid/ask spreads have declined but remain elevated relative to pre-crisis levels.	Bid/ask spreads vary by issuer but generically: BB-rated securities: 1 point, which is in line with normal market conditions B-rated securities: 1 point, which is in line with normal market conditions CCC-rated and below: 1.5points which is in line with normal market conditions CDX HY bid/ask is 1-2x vs normal conditions.
Emerging-Market Debt (EMD)	**Hard Currency EM** • EM credit index spreads closed the week ~4bp wider during the week ended December 24. Holiday illiquidity – in terms of significantly reduced trading volumes – is in full swing as many market	EM IG and HY sovereigns and EM IG and HY corporates are back to

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	participants have begun their holiday breaks after a tumultuous year. **Local Currency EM** • Liquidity is close to normal.	normal market conditions
Asia	**Asia Hard Currency** • Asia hard currency credit spreads ground tighter in thin liquidity during the week ended December 25; the index spread squeezed by a modest 1bp. • The primary market was quiet, with only one high yield deal pricing. • Liquidity deteriorated due to the largely absent primary market supply and year-end vacations taken by a number of dealers in the market. **Asia Local Currency** • Liquidity in Asia local currency markets thinned during the week ended December 25, as trading activity subsided into the year-end. • China government bonds rallied ~3 to 8bp as the PBOC net injected CNY 370bn into the system via daily open market operations in an effort to keep funding conditions loose into the year end.	Asia IG credit is ~1.5 to 2x wider vs. normal market conditions Asia HY credit is ~1.5 to 2x wider vs. normal market conditions Asia local currency debt is ~1.5 to 2x wider vs. normal market conditions
Securitized	**CMBS** • As expected, both CMBS and CMBX traded sideways on light volume during the holiday-shortened week ended December 24. There were no new CMBS deals and only $611mn of bonds were presented to the market for bid, $2.1bn fewer than the previous week. • Anemic volumes combined with little desire to take risk before year end resulted in CMBS bid/offer spreads remaining unchanged throughout the capital stack. Bid/offer spreads for AAA to A-rated classes have retraced their post-covid-19 widening, while bid/offer spreads for BBB-rated classes remain approximately 2x their pre-covid-19 levels. • CMBX behaved much like its cash bond counterpart. Trading volume was light, and prices traded in a narrow band, leaving bid/offer spreads unchanged. CMBX A.6, BBB-.6, and BB.6 bid/offer spreads remain approximately 2x their historical averages. **ABS** • ABS new issuance is finished for the year, with no new deals pricing during the week ending December 24. ABS year-to-date supply now stands at $175.3	

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	billion compared to $228.5 billion recorded in 2019 over the same time period. • Secondary market volumes are significantly below average, and spreads were unchanged. **CRTs** • During the week ended December 24, the CRT market was fairly quiet from a volumes perspective. Those investors that did trade continued to add, reaffirming previous week levels. There was some profit-taking from the street before quarter end. • Secondary market liquidity remains robust. **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 inside 200 bp discount margin currently. **CLOs** • The week ended December 24 was quiet in the CLO market. Spreads on the week were unchanged to slightly tighter. Volumes week-over-week were down, given the holiday. • Liquidity remains robust in the CLO market. Bid/ask spreads remain at or around pre-crisis levels. **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	• The repo rate is in the 0.08-0.09% range. The T-bill curve was unchanged week-over-week. • 1-month LIBOR set at 0.145%, while 3-month LIBOR set at 0.24%. • Government money market funds saw $21bn of outflows in the 7 days ended December 24. Prime funds were flat over the same period.	
US Municipals	• The municipal market was quiet during the week ended December 24, as expected. There was no new issuance calendar to speak of and a large number of market participants were on vacation. Despite some interest rate volatility, municipal benchmark yields were unchanged over the week. There was better dealer selling vs buying in the busier first half of the week, as technicals remain strong for municipals into the end of the year.	

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	Expectations are that the market will remain quiet until January. • Odd lot liquidity remains decent, with haircuts to round-lot bidside evaluations just over one point for small size (5k-15k) and around 0.25 point for larger odd lots (50k+).	
Canadian Market	**Federal** • Liquidity is best in benchmark issues for block sizes of <=CAD25 million; liquidity has improved in off-the-run, high coupon bonds with Bank of Canada (BOC) bond buying. Comments by central bank Governor Macklem that the BOC will buy at least $4 billion of Canadian government bonds per week until the recovery is well underway should continue to support market liquidity. The fact that the BOC will buy more bonds at the long end of the curve should support liquidity at the 30-year part of the yield curve. • The BOC has purchased C$184 billion to support liquidity in Government of Canada markets since the purchase program started on March 27 through December 16. Government of Canada bonds are the most liquid securities in capital markets in Canada as seen in the latest (November) Bank of Canada research. **Provincial** • Liquidity is best in benchmark bonds from Quebec, Ontario and British Columbia. • Depending on market tone, concessions may be requested in order for dealers to take less-liquid positions. • Most dealers will not bid aggressively on off-the-run, high coupon provincial issues, they will do agency trades, even with the Bank of Canada's buying program of provincial debt. • The BOC has purchased C$14.2 billion in par value year to date through December 16 within their provincial buying program to support liquidity. Liquidity is affected by reduced personnel during the year end and holiday period and dealers' lack of appetite for increasing their provincial aggregates. **IG Corporates** • The latest Bank of Canada research highlights the lack of liquidity in Canadian corporate bond markets, which can impact pricing; many dealers are	Federal: bid/ask typically 5 cents in the 10-year area, but for the long end of the curve, it can be more depending on volatility (risk off markets) and size outstanding. Off the run Canadas can have a wide bid-ask given small outstanding size in these securities. Liquidity and activity are reduced with calendar year end. Provincial: concession of +1 bp and more on size > CAD 25 million, particularly at the longer end. In risk-off markets, liquidity is drying up and spreads can widen depending on market tone. Liquidity and activity are reduced with calendar year end. BBB- corporates are trading by appointment, particularly in the energy sector. Inventories are

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	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 (focused on securities of 5-years or less) should support liquidity for corporate bonds rated BBB and higher. However, the central bank has bought a relatively small amount of corporate securities to date (C$180 million par), indicating the impact is limited. The central bank has not bought bonds since November (as of December 16). BBB- bonds are trading by appointment unless there is a new issue.	reduced and dealers are not looking to increase their BBB- exposure. Dealers may refuse to bid in a risk off market with gaps in spreads. Liquidity and activity are reduced with calendar year end.
	Real Return Bonds (RRBs) • The program to purchase Government of Canada securities in the secondary market – the Government Bond Purchase Program or GBPP – should help liquidity since it includes RRBs. The last auction was held on December 2 with the FTSE index duration extending by a historical amount of over 1.6 years. On that day, the BOC bought a total of C$434mn with a target of C$75 million per line of the 7 Canada RRBs from 2021 to 2047. Even with the central bank buying net C$34 million of Canada RRBs in December, liquidity remains challenging as dealers hold very limited inventories of these RRB securities. It is noteworthy to underline that the central bank was not able to reach its target purchases in RRBs 2047 and only bought $59 million. Trading in Canada RRBs continues to show a chronic lack of liquidity. Trading a block can only be done on an appointment basis.	Provincial RRBs trading by appointment only. Dealers do not hold these securities on their balance sheet.

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