ALLIANCEBERNSTEIN®

March 2021

Market Update – Fixed Income Trading Liquidity
For the Week Ended 19 March 2021

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	• During the week ended March 19, the global rates markets were dominated by the US, with the 10-year Treasury selling off another 10 bp while yields on European counterparts were unchanged/slightly higher on the week with the US Treasury-German bund spread 8.5bp wider. • The main event was the FOMC meeting which came in more dovish than market expectations. Chair Powell emphasized that the "fundamental change" in their framework is that actions will be outcome-based. The net effect was clear for rates with curves steepening, led by the 3s10s curve which was 10.5bp steeper on the week. Markets are now pricing in a little more than half a rate hike in 2022 and 2.6 hikes in 2023. • Liquidity in terms of market depth in on-the-run cash 5-year and 10-year Treasuries has improved by 70% from the worst levels on February 26. Market depth in the 30-year part of the curve has improved 55-60% since February 26. Liquidity around economic data and auctions has been challenging at times given the recent backdrop. • The observable bid-offer spread is in line with historical averages in on-the-run bonds. Transaction costs in off-the-run bonds remain wider vs. historical averages. But there has been some improvement in bid-offer spreads vs the prior week - from 12-13 ticks at the February 26 wide levels to 4-5 ticks on March 5 and 2-3 ticks currently compared with just 2 ticks prior to the current liquidity deterioration earlier in February (a tick is 1/32 of a point). Deep off-the-run high coupon bonds have moved from 24-32 ticks wide on February 26 to 6-7 ticks wide currently. • Federal Reserve bond purchases continue at $80 billion US Treasuries and $40 billion MBS per month.	
Investment Grade (IG) Corporates	**US IG** • The positive momentum from the prior week continued within the US investment-grade cash bond market during the week ended March 19.	Bid/ask conditions in the IG market are back to normal

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	• US IG outperformed equities during the week with the index closing 3bp tighter week-over-week. The market saw inflows of $5.43bn despite the continued interest-rate volatility. • Supply slowed down relative to the past two weeks, book coverage improved, concessions lowered from the prior week, and Asia buyers of long-end paper returned in the latter half of the week to a magnitude not seen in months. • Supply was $32bn during the week. The market has already met supply expectations for the month of March. Spectrum-related supply has underwhelmed expectations, with AT&T only issuing $6bn on Friday (vs expectations of $20bn) and T-Mobile issuing in the high yield market, removing a large potential supply overhang. Supply for the week ending March 26 is expected to be $30-35bn. **Euro IG** • The euro IG market was focused on supply and the macro tone during the week ended March 19. • There was a significant uptick in new issue supply with ~30bn EUR and 4bn GBP coming to market. Amid the heavier supply, order books were less oversubscribed and new issue premium crept up, ranging from 0-10bp. This weighed on secondary markets, particularly where new issue concessions were larger. However, while the technicals felt softer, the overall tone was not panicky. • Within AT1 markets, the move wider in rates did little to diminish support for this market, which was only modestly lower. **REIT Preferreds** • Liquidity in the REIT preferred market is typically limited under more normal conditions given the retail nature of the investor base. • 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.	
High Yield (HY) Corporates	**US HY** • Once again, the high yield market traded in line with interest rates during the week ended March 19. The move down in price alongside the rate selloff on Thursday was orderly. High yield bonds were generically quoted down 0.5 point with rate-sensitive names quoted down 1 point. • Secondary market activity was relatively quiet this week. Aside from rates, investor focus was largely on new issue markets, with ~$14.5bn of new issuance pricing across 14 deals. Many deals priced at the middle of initial price guidance, leaving a little room for the deals to perform better off the break. • The spread between CCC and BB-rated bonds was 6bp wider to 306 bp. Energy underperformed on Thursday with the selloff in WTI.	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

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	Euro HY • During the week ended March 19, primary market supply was in focus in euro HY. Deals consistently priced through initial price guidance, saw oversubscribed order books, and generally performed well (1 deal of 6 traded below reoffer). • In the secondary market, the interest rate volatility weighed on the longer-duration, larger-cap credits as seen in previous weeks (down -0.75 to -1.5pt week-over-week), however real selling pressure was rather limited. Notably, there did not appear to be cash raised against new issues. It was predominantly hedge funds and dealers pushing the most duration-sensitive names. • The calendar is expected to remain busy for the next two weeks in the lead up to the Easter holiday, which could lead to some indigestion. • Overall activity levels in secondary markets are not very high, and investors do not seem to have been forced make moves around flows in/out of the asset class. **CDX HY** • CDX HY was unchanged during the week ended March 19, outperforming cash bonds and the macro tone. This was driven by the arbitrage flows between CDX and single names. As the market heads into the roll period, the on-the-run series is expected to come under pressure as positioning is net long in that series. • Trading volumes were above average on the back of increased arbitrage flows. • Bid/ask spreads have declined to pre-crisis levels.	CCC-rated and below: 1.5points which is in line with normal market conditions CDX HY bid/ask is in line with normal conditions.
Emerging-Market Debt (EMD)	**Hard Currency EM** • EM credit continued to show impressive resilience during the week ended March 19 as the JPM EMBI Global Diversified Index closed ~8bp tighter in the face of the US 10-year Treasury touching 1.75%. • Volumes remain muted as market participants digest the unprecedented developed-market interest rate volatility coupled with improved EM technicals such as a recent dramatic pick up in amortizations, a lack of supply expectations and the return of demand from Asia. • Ecuador outperformed, trading up 3.5pt as the leftist candidate Perez dropped his legal claim for a recount on the presidential election. Sub-Saharan Africa oil exporters underperformed with Angola 30-year bonds trading down 2 points following pressure on crude prices. **Local Currency EM** • The local EM rates market mostly tracked US Treasuries. Liquidity remains adequate but volatility is to be expected. • A wave of hawkish central bank surprises in Russia, Turkey and Brazil helped to stabilize EM currency and local rates markets during the week ended March 19.	EM IG and HY sovereigns and EM IG and HY corporates are back to normal market conditions

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Asia	**Asia Hard Currency** • Primary market activity was solid in Asia credit during the week ended March 19, with $4.8bn in issuance and a healthy mix of both high yield and investment grade. Roughly 60% of the new issues were trading “above water” by the end of the week. • Despite impending global central bank decisions keeping the market on its toes and some sharp US Treasury moves, Asia spreads were firm, with a skew to better buying. • Indonesia quasi-sovereign and sovereign spreads tightened 15-20bp, China IG rallied 5-15bp and even China TMT found a bid among the increased regulatory scrutiny. In Asia HY, China Property was up 2-3pts, Indonesia and India HY lagged but were still up 1-1.5pt. Indonesia textiles suffered, falling 2-7pt on rating review concerns. **Asia Local Currency** • Asian interest rates were surprisingly resilient to the selloff in US Treasuries. • Indonesia was +8bp, on the back of a weak auction on Tuesday. The central bank kept rates unchanged. • In Taiwan, the CBC acknowledged that there has been “some kind of intervention” in the currency markets amid the release of the $39.1 bn purchases in 2020. The CBC Governor also raised the possibility of being labelled a “currency manipulator” by the US Treasury, but implied that it will remain business as usual for the central bank.	Asia hard currency IG and HY credit is back to normal conditions. However, interest rate volatility may cause pressure points to appear. Asia local currency debt is back to normal market conditions
Securitized	**CMBS** • During the week ended March 19, CMBS spreads were modestly wider week-over-week as investors paused to re-assess valuations in the face of rising interest rates and a steeper yield curve. 10-year AAA-rated classes were 5bp weaker, while single A-rated classes widened by 10bp. Supply in the secondary market remained modest as $1.9bn of bonds were out for the bid, $737mn fewer than the prior week. • The new issue calendar remains light but two new conduit issues are expected in the coming weeks. • Liquidity remains robust for AAA to A-rated CMBS classes while bid/offer spreads for BBB-rated classes remain approximately 2x their pre-covid-19 levels. • CMBX performance was mixed. Recent vintage series generally outperformed seasoned vintages. Flows were concentrated at the top of the capital stack. Mezzanine tranches continue to trade sluggishly on limited volume. On average, CMBX bid/offer spreads remain unchanged, with CMBX A.6, BBB-.6, and BB.6 bid/offer spreads approximately 2x their historical averages.	

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	ABS • The ABS primary market priced six deals for the week ending March 19 totaling $4.2bn across private credit student loan, auto fleet, prime auto leases, and prime and non-prime auto loan sectors. Year-to-date ABS supply now stands at $57.5bn (22% higher) compared to $47bn recorded over the same period in 2020. • During the week there was some softness in the primary market, as an auto lease ABS transaction from benchmark sponsor Santander priced wide to the initial guidance range. In addition, some investor fatigue was noticed in the secondary market as investor bid lists crowded the market over the course of a couple of days, though plain-vanilla ABS remained firm. • Indicative benchmark ABS spreads widened slightly in a few areas driven mainly by the high supply. Spreads widened by +1bp across fixed credit cards and by +5bp on BBB non-prime auto loans. Like the prior week, subordinated private credit student loan ABS outperformed once again, and saw tightening on the week by 5bp. The rest of the ABS sectors saw spreads unchanged on the week. **CRTs** • The week ended March 19 was relatively uneventful in the CRT market. Last cash flow bonds caught a bid, particularly high dollar price premium bonds which saw good two-way flow after limited trading in any significant size since mid-February. B1 and MI CRTs remained weak. • Arch is in the market looking to place their first deal of 2021; books are building slowly, illustrating challenges in getting such a deal done in the current environment • Secondary market liquidity remained challenged last week. Dealers seem unlikely to put money to work unless they know they have an outlet with a customer. • Bid/ask spreads widened a bit but remain around pre-covid levels. **Legacy Non-Agency RMBS** • Legacy RMBS continue to trade well. After having widened to the 1000-1200 bp range in March 2020, spreads are currently trading inside 200 bp discount margin. **CLOs** • The CLO market seemed back on track during the week ended March 19. The wider spread levels of the prior week, due to an abundance of deals, seemed to have done a good job of drawing investors back into deals. Oversubscriptions are again being seen on new issues. • AAA-rated spreads for top-tier managers are in the 107-108 bp area; AA-rated spreads are around 155bp; A-rated are 175bp; BBB-rated are 305-310bp; and BB around 650-675bp. • Secondary market spread levels are widening more than the primary market.	

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	• 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 were unchanged and remain well supported, given the Fed purchases of $40bn per month. Bid/offer spreads for current coupon bonds are trading at 1-1.5 ticks wide and the rest of the coupon stack is wider by 3-4 ticks.	
Money Market	• During the week ended March 19, repo (general collateral) began to trade at negative rates and the T-bill curve was negative out to four-month maturities. • For context, since the February Treasury Refunding Statement: o The Treasury General Account has declined from $1.6trn to $1.1 trn o Reserve balances in the banking system have increased from $3.2trn to $3.7trn o Money market fund assets have increased from $4.3trn to $4.4trn o Net T-bill paydowns have been $290bn o QE has continued at $120bn per month This has combined to increase cash and decrease supply in the system. • SOFR continued to set at 0.01%. The Fed repo facility saw an uptake of $27bn and $19bn on Thursday and Friday respectively. • The expiration of the SLR exemption (an emergency measure put in place during the pandemic to unconstrain dealer balance sheets and improve liquidity by excluding cash and Treasuries from the SLR (supplementary leverage ratio) calculation) will exacerbate the situation going into quarter end. Dealer balance sheets will be constrained, not helping liquidity. Primary dealer inventories are at October 2018 low levels and continue to decrease. Additionally, money market funds may see further inflows from the deposits the banks may be turning away. • The Fed is losing equilibrium in the front-end but has somewhat acknowledged that by raising counterparty limits on reverse repurchase agreement (RRP) operations from $30bn to $80bn. This helps establish a firm repo floor at 0%. Further dislocations are expected for at least the next 2 weeks. • Effective Federal Funds Rate set at 0.07% • 1-month LIBOR set at 0.107%, while 3-month LIBOR set at 0.191%. • Government money market funds had $9bn of inflows in the 7 days ended March 19. Prime funds had $6bn of outflows over the same period.	
US Municipals	• Municipals started the week ended March 19 firm but cautious, with healthy demand for the heavier-than-usual $11.8bn calendar. However, persistent interest rate weakness caused municipals to correct on Wednesday and Thursday, underperforming rates: on	

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	the week, shorter-maturity municipals were wider by 10-12bp, and maturities from 2025 and beyond were wider by 14bp. • Illinois GO priced $1.26bn of bonds on Tuesday after accelerating from Wednesday as a result of heavy demand. The deal saw $16bn of orders with oversubscriptions of 11-24x and spreads tightening 10-20bp on the break. Other higher-yielding names that came to market during the week, such as NY Thruway and Guam, saw heavy subscriptions and repriced tighter even amid the weakness in the broader market. • Odd-lot discounts to round-lot bid side evaluations are ~0.25 point for lot size of 110k+, 0.5-0.75 pt for 20k-100k; and ~1-1.25 pts for 5-15k lots.	
Canadian Market	**Federal** • Liquidity is best in benchmark issues for block sizes of <=CAD25 million. 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$225.9 billion to support liquidity in Government of Canada markets through March 17. According to the latest BOC research, Federal debt is the most liquid sector within the Canadian fixed income markets. **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$17 billion in par value year to date through March 10 within their provincial buying program to support liquidity. The BOC has cut their maximum weekly take out to $350mn from $500mn and the buying program is done only once per week. Dealers expect this purchase program to mature on May 7, 2021. • A continued rise in crude oil prices from current levels could help liquidity in provinces where oil revenues will be pushed upward – Alberta, Saskatchewan and Newfoundland. **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 maintaining low balance sheet inventories, so will not provide bids in many sectors.	Federal: bid/ask was at 3 to 5 cents in the 10-year area, but for the long end of the curve, it remains relatively wider at 15 cents given the recent higher volatility. Off the run, high coupon Canadas were reported to have limited liquidity in this high volatility period with much wider bid-ask given small outstanding size in these securities. Provincial: concession reported to be above average on size > CAD 25 million, particularly at the longer end. In risk-off markets, liquidity is drying up and spreads can widen

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	• Trading on an agency basis for high-beta issuers. • The Bank of Canada's $10bn 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$240 million par as of March 17), indicating the impact is limited. The BOC has announced that they will cut the maximum size of their tenders under the purchase program, reducing the max amount to C$50mn from C$100mn previously • Recent conversations with the deputy BOC governor indicated that they view the bond-buying program as a "back-up" facility. They do not see a current need to intervene to provide liquidity to the BBB- corporate market. Based on lack of intervention and deputy governor comments it is expected the program will be cancelled on May 7, 2021. **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. • Trading in Canada RRBs continues to show a lack of liquidity. Trading a block can only be done on an appointment basis. • Of note, the last $300mn auction of RRB 0.5% Dec 2050 was done on February 10. On that day the central bank was not able to buy its maximum of 6 Canada RRBs for a total of $450mn with a target of $75mn per line item (from 2026 to 2047 maturities). In December, the BOC bought net $34mn in RRBs compared with $122mn in February (BOC buying program less new supply). • Liquidity remains challenging as dealers hold very limited inventories in RRB securities.	depending on market tone. BBB- corporates are trading by appointment, particularly in the energy sector. Inventories are 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. Provincial RRBs trading by appointment only. Dealers do not hold these securities on their balance sheet. Bid-ask is not a reliable indicator for trading.

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