February 2021



Market Update – Fixed Income Trading Liquidity For the Week Ended 26 February 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 February 26, the global rates market sold 	
	off again, with US 10-year Treasury yields higher by 7 bp, German	
	10-year bund yields higher by 4.5bp and UK 10-year gilts continuing	
	their recent underperformance by selling off 12bp.	
	 For the first time in many weeks, the market experienced a hiccup 	
	as the market bear flattened and risk assets sold off. Interest rate	
	volatility, Fed rate hikes and liquidity conditions dominated fixed	
	income markets last week. Rate volatility as measured by the	
	MOVE index was higher by 25% on the week.	
	• There was a dramatic repricing of Fed expectations. Rate futures	
	have pulled forward the first 25bp of Fed tightening up to	
	December 2022 (up from the first quarter of 2023) and the second	
	to June 2023 (up from fourth quarter of 2023). The 5s30s curve	
	flattened by 14bp on the week.	
	 Fed Chair Powell continued to take the dovish road in his 	
	Congressional testimony during the week and similar sentiment	
	was echoed by other Fed speakers during the week.	
	Federal Reserve bond purchases continue at \$80 billion US	
	Treasuries and \$40 billion MBS per month.	
	Liquidity conditions have changed, with bid-offer spreads ending	
	the week wider than they have been since April 2020.	
	• The bid/offer spread of the on-the-run 30-year bond has	
	widened 2 full ticks from previous ½ of a tick wide levels (a	
	tick is 1/32 of a point).	
	• Bid/offer on 10-year notes are twice as wide as last week.	
	• High frequency traders have reduced the liquidity they	
	typically provide which has had an outsized impact on 20-	
	year and 30-year liquidity in the wake of the recent 7-year	
	auction that showed very low end user demand.	
	• Off-the-run bonds are much less liquid – with deep off-the-	
	run bonds that typically trade 2 ticks wide now trading 12-	
	13 ticks wide. Deep off-the-run bonds where the Fed	
	SOMA (System Open Market Account) holds >50% of the	

Sector	Liquidity Trading Comment	Bid-Ask Spreads
	outstanding issue are trading more than 1 full point wide in	
	some cases, since the dealer community has lost the ability	
	to offer them into daily Fed purchase operations (Fed's	
	SOMA can only hold up to 70% of any single cusip).	
	• Depth across the Treasury complex is down significantly. In 30-year	
	cash US Treasuries, depth is 70% lower than the previous week.	
Investment	US IG	Bid/ask
Grade (IG)	• The US investment-grade cash bond market held in well during the	conditions in the
Corporates	week ended February 26, despite the weaker macro tone and rate	IG market are
corporates	volatility. The credit index closed only 1bp wider week-over-week.	back to normal
	 The back-up in rates continued to attract yield-based buyers, but 	back to normal
	there was some profit taking throughout the week and investors	
	lightening up risk ahead of heavy supply expectations over the next	
	couple of weeks.	
	• Supply was in line with expectations of \$30-40bn and continued to	
	be met with strong demand despite small concessions. There was a	
	clear outperformance of 20-year deals this week.	
	• The technicals in the market remain supportive and the market had	
	another inflow of \$4.2bn during the week despite rate volatility.	
	• Supply for the week ending March 5 is expected to be \$40bn+.	
	Euro IG	
	• The euro IG market was softer during the week ended February 26,	
	but overall the market held in reasonably well amid the heightened	
	interest rate volatility. Price action was orderly, suggesting minimal	
	outflows thus far despite total returns in negative territory. Rather,	
	there was tentative buying when yields moved up.	
	• There was a notable divergence between higher-quality euro IG	
	bonds trading on spread in the market and those trading on cash	
	price (e.g., AT1/corporate hybrids), with the latter outperforming.	
	Overall, underlying technicals remained constructive, with liquidity	
	holding in despite the rates volatility.	
	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	US HY	Bid/ask spreads
(HY)	The high yield index spread was flat during the week ended	vary by issuer bu
Corporates	February 26 at 319 bp. Although the week started with dealers	generically:
corporates		generically.
	quoting interest-rate sensitive issuers down, there was little	
	evidence of material selling at lower levels. Most selling on	BB-rated
	Thursday and Friday was driven by ETF arbitrage investors while	securities: 1
	HYG traded largely within a 0 to 30bp discount to NAV.	point, which is ir
	• The new issue calendar was active with \$11.6bn pricing across 18	line with normal
	deals. The rate move began to impact investor behavior through	market condition

Sector	Liquidity Trading Comment	Bid-Ask Spreads
	the primary market – new issues this week were modestly	
	oversubscribed at mostly 2-3x, compared with the 3-5x range seen	B-rated securities:
	so far this year. While deals did not struggle to come to market,	1 point, which is
	they generally priced at the mid-point of initial price guidance.	in line with
	Performance in the secondary market was mixed, especially for	normal market
	lower-coupon deals.	conditions
	• The spread between CCC and BB-rated bonds was 8bp tighter to	
	310 bp.	CCC-rated and
		below: 1.5points
	Euro HY	which is in line
	• During the week ended February 26, there were signs of softness in	with normal
	the longer spread duration issuers in euro HY. Selling was focused primarily in larger-cap, tighter-spread BB-rated issuers (such as	market conditions
	Netflix) as well as some large-cap tighter-spread single-B-rated	CDX HY bid/ask is
	issuers (e.g., those in the TMT/Healthcare spaces). There was two-	in line with
	way flow in these weaker-trading names, as late in the week there	normal
	way now in these weaker-trading names, as fate in the week there was anecdotal evidence of investors dipping their toes in the issuers	conditions.
	that had underperformed most. But this was the first sign of the	conditions.
	rate volatility affecting the euro HY market.	
	 Also noteworthy was the outperformance of wider-spread/covid- 	
	exposed issuers as the rotation trade for reflation/re-openings and	
	value was apparent last week.	
	 The new issue market also remained active, with deals performing 	
	as they have all year—book subscriptions remain healthy, most	
	deals came tight to initial price guidance and traded up on the	
	break. Wider-spread issuers continued to outperform.	
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	CDX HY	
	 Continuing the YTD theme, CDX HY once again modestly 	
	underperformed cash bonds and traded 70 cents lower during the	
	week ended February 26.	
	Trading volumes were above recent averages, particularly toward	
	the latter half of the week as is typical in periods of macro volatility.	
	 Bid/ask spreads have declined to pre-crisis levels. 	
Emerging-	Hard Currency EM	
Market Debt	Rate volatility and global macro weakness weighed on EM Credit	EM IG and HY
(EMD)	during the week ended February 26 as the JPM EMBI Global	sovereigns and
	Diversified Index widened 10bp with investment-grade	EM IG and HY
	underperforming high yield by 7bp.	corporates are
	• Selling continued from the Asia buyer base following the Lunar New	back to normal
	Year holiday, further adding pressure to 30-year investment-grade	market conditions
	credit. Corporates in general outperformed, as is typical in bouts of	
	volatility, with anecdotal evidence suggesting most "real money"	
	investors were happy to weather the storm rather than sell	
	corporate bonds they believe will be difficult to buy back.	
	• EPFR flow data turned back to positive although notably the most	
	recent data excludes the second half of the week when fear	

Sector	Liquidity Trading Comment	Bid-Ask Spreads
	that EMB traded at the largest discount to NAV since June 2020	
	(58bps).	
	Local Currency EM	
	 The local EM rates market mostly tracked US Treasuries or German bunds. 	
	 Liquidity is adequate but volatility is to be expected. 	
Asia	Asia Hard Currency	Asia IG credit is ~:
	• Asia credit index spreads tightened by 8bp during the week ended February 26, which was not sufficient to offset the loss from the US Treasury selloff, leading to a total return loss of 0.9%. Despite the macro weakness, performance of Asia credit was resilient overall, with HY outperforming and shedding only 0.1% on a total return	to 1.5x wider vs. normal market conditions Asia HY credit is
	 basis. Primary market supply picked up after the Lunar New Year holiday lull with a total of \$8.8 bn issued mainly in the investment-grade market. 	~1 to 1.5x wider vs. normal marke conditions
		Asia local
	Asia Local Currency	currency debt is
	Asia local currency bond yields spiked across the board on the back	~1.5 to 2x wider
	of a sharp repricing of US Treasury yields.	vs. normal marke
	 Australian and New Zealand government bond yields jumped as much as ~30 to 50 bp 	conditions
	 Thailand government bonds underperformed the region, as yields 	
	bear steepened by \sim 20 to 30 bp, whereas China outperformed with	
	bonds finishing the week only marginally weaker.	
Securitized	CMBS	
	 During the week ended February 26, despite volatility in broader markets, CMBS spreads remained well anchored. Ten-year, AAA-rated debt continues to trade in the swaps + low 60 bp range, while A-rated tranches trade in the +145-165 bp range. The technical backdrop remains positive, with only modest issuance expected in the coming weeks. One deal is in the pre-marketing stage and will price during the week of March 1. CMBX reacted in line with other risk asset markets and widened week-over-week. BBB- classes were lower by 0.25 to 0.75 points. However, the move lower was orderly, and trades continued to be absorbed by the market. 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. On average, CMBX bid/offer spreads remain unchanged, with CMBX A.6, BBB6, and BB.6 bid/offer spreads approximately 2x their historical averages. 	
	 ABS The ABS primary market priced two deals for the week ending February 26 totaling \$1.829bn across equipment and whole business sectors. Year-to-date ABS supply now stands at \$36bn compared to \$39bn recorded over the same period in 2020. 	

Sector	Liquidity Trading Comment	Bid-Ask Spread
	Primary market execution remained strong and deals priced	
	through the initial guidance levels.	
	Indicative benchmark spreads in the secondary market remained	
	largely unchanged at record tight levels during the week. BBB-	
	rated prime auto ABS, BB-rated non-prime auto, and subordinated	
	private credit student loan ABS series all tightened 5bp on the	
	week.	
	• There are eight ABS deals totaling \$7bn that are in pre-marketing	
	for the week ahead.	
	CRTs	
	• The week ended February 26 saw the first week of material pull	
	back in CRT spreads since October 2020. With the curve steepening	
	and 10-year US Treasuries touching 1.6% on Thursday, risk off took	
	hold and extension concerns started to affect levels at the bottom	
	of the stack. This, together with month-end selling pressures led to	
	a somewhat disorderly selloff for February month end. B1/B2	
	bonds were ~1 to 1.5 points off in dollar price, roughly 35-50bp	
	wider in spread. Below-investment-grade, on-the-run, last cash	
	flow bonds were off 8-12 ticks. Seasoned investment-grade bonds	
	were relatively unchanged.	
	• Freddie Mac is marketing the second low-LTV deal of 2021, STACR	
	2021-DNA2, to a skittish market. The deal is one of the largest at	
	1.2bn and reception thus far has been tepid around the price talk.	
	The deal is expected to be announced on March 1.	
	Secondary market liquidity took a pullback midweek, but buyers	
	came out looking for bonds once levels were reset lower. This	
	highlights the amount of money on the sidelines.	
	Bid/ask spreads widened a bit but remain around pre-covid levels.	
	Legacy Non-Agency RMBS	
	Legacy RMBS continue to trade well even through the volatility of	
	the week ended February 26. After having widened to the 1000-	
	1200 bp range in March 2020, spreads are currently trading inside	
	200 bp discount margin.	
	CLOs	
	• The week ended February 26 continued to be busy in the CLO	
	secondary market. Volumes were down week-over-week and the	
	quality of the bonds hitting the market is lower, but supply	
	continues to be met with an equal amount of demand from	
	investors. Levels up and down the CLO stack are unchanged on the	
	week.	
	February was one of the busiest months on record for CLO primary	
	market issuance. And the number of newly opened warehouses	
	continues to accelerate. AAA-rated spreads for top-tier managers	
	are in the 100 bp area; AA-rated spreads are around 140bp; A-rated	
	are 160-165bp; BBB-rated are 280-290bp; and BB around 650bp.	

Sector	Liquidity Trading Comment	Bid-Ask Spreads
	Spreads can be wider for new managers or those who have good	
	long-term track records but fared poorly through covid.	
	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 remain well supported, given the	
	Fed purchases of \$40bn per month. Bid/offer spreads for current	
	coupon bonds are trading at 1 tick wide and the rest of the coupon	
	stack is wider by 1-2 ticks.	
Money	• Since the February 3 Treasury refunding statement, the Treasury	
Market	General Account (TGA) has fallen from \$1.7trn to \$1.4trn. Net	
	paydowns in T-bills were \$96bn during the week ended February	
	26.	
	 Other front-end interest rates are being dragged down with T-bills. 	
	SOFR set at 0.01%. The Fed reverse repo facility (RRP) saw \$11.2bn	
	of usage on Friday. There have been periods where repo has	
	traded at negative levels post-RRP close. T-bill rates are trading	
	tight across the curve and the reserve balances in the banking	
	system increased another \$200bn (currently at \$3.4trn).	
	 Chair Powell acknowledged front-end rates in his testimony to 	
	Congress during the week but as expected made no changes. Relief	
	may come from passing of a stimulus bill (marginal increase in	
	supply) or Fed adjustments to the RRP or the Interest Rate on	
	Excess Reserves.	
	Effective Federal Funds Rate set at 0.07%	
	• 1-month LIBOR set at 0.109%, while 3-month LIBOR set at 0.184%.	
	Government money market funds remained resilient with \$51bn of	
	inflows in the 7 days ended February 26. Prime funds had \$3bn of	
LIC Municipale	outflows over the same period.	
US Municipals	The municipal market was pressured during the week ended Express 26 on the back of interact rates maying unward	
	February 26 on the back of interest rates moving upward.	
	Municipals outperformed Treasuries, but nevertheless municipal	
	 yields moved wider on the week. Beta compression was a theme as AA/AAA-rated municipals 	
	underperformed bonds rated BBB and below.	
	 Odd-lot discounts to round-lot bid side evaluations rose during the 	
	week from 0.5-0.1 point to 1-2.5 points.	
Canadian	Federal	Federal: bid/ask
Market	 Liquidity is best in benchmark issues for block sizes of <=CAD25 	was at least 10
	million. Comments by central bank Governor Macklem that the BOC	cents in the 10-
	will buy at least \$4 billion of Canadian government bonds per week	year area, but for
	until the recovery is well underway should continue to support	the long end of
	market liquidity. The fact that the BOC will buy more bonds at the	the curve, it
	long end of the curve should support liquidity at the 30-year part of	expanded to 20 to
	the yield curve.	25 cents given the
		high volatility. Of
		the run, high

Sector	Liquidity Trading Comment	Bid-Ask Spreads
	 The BOC has purchased C\$213.6 billion to support liquidity in 	coupon Canadas
	Government of Canada markets since the purchase program	were reported to
	started on March 27 through February 24.	have limited
	 Liquidity at the end of February was limited/difficult with dealers 	liquidity in this
	avoiding taking positions in Canadas as volatility resulted in losses,	high volatility
	limiting their risk taking on their balance sheet.	period with much
		wider bid-ask
	Provincial	given small
	 Liquidity is best in benchmark bonds from Quebec, Ontario and 	outstanding size
	British Columbia.	in these
	• Depending on market tone, concessions may be requested in order	securities.
	for dealers to take less-liquid positions.	
	 Most dealers will not bid aggressively on off-the-run, high coupon 	Provincial:
	provincial issues, they will do agency trades, even with the Bank of	concession
	Canada's buying program of provincial debt.	reported to be
	 The BOC has purchased C\$16.4 billion in par value year to date 	above average or
	through February 24 within their provincial buying program to	size > CAD 25
	support liquidity. The BOC has cut their maximum weekly take out	million,
	to \$350mn from \$500mn and the buying program is done only once	particularly at the
	per week. Dealers expect this purchase program to mature on May	longer end. In
	7, 2021.	risk-off markets,
		liquidity is drying
	liquidity in provinces where oil revenues will be pushed upward –	up and spreads
	Alberta, Saskatchewan and Newfoundland.	can widen
		depending on
	IG Corporates	market tone.
	• The latest Bank of Canada research highlights the lack of liquidity in	
	Canadian corporate bond markets, which can impact pricing; many	BBB- corporates
	dealers are maintaining low balance sheet inventories, so will not	are trading by
	provide bids in many sectors.	appointment,
	Trading on an agency basis for high-beta issuers.	particularly in the
	• The Bank of Canada's \$10bn buying program (focused on securities	energy sector.
	of 5-years or less) should support liquidity for corporate bonds	Inventories are
	rated BBB and higher. However, the central bank has bought a	reduced and
	relatively small amount of corporate securities to date (C\$210	dealers are not
	million par as of February 24), indicating the impact is limited. The	looking to
	BOC has announced that they will cut the maximum size of their	increase their
	tenders under the purchase program, reducing the max amount to	BBB- exposure.
	C\$50mn from C\$100mn previously	Dealers may
	Recent conversations with the deputy BOC governor indicated that	refuse to bid in a
	they view the bond-buying program as a "back-up" facility. They do	risk off market
	not see a current need to intervene to provide liquidity to the BBB-	with gaps in
	corporate market.	spreads.
	Real Return Bonds (RRBs)	Provincial RRBs
	The program to purchase Government of Canada securities in the	trading by
	secondary market – the Government Bond Purchase Program or	appointment
	GBPP – should help liquidity since it includes RRBs.	only. Dealers do
		not hold these

Sector	Liquidity Trading Comment	Bid-Ask Spreads
	• Trading in Canada RRBs continues to show a lack of liquidity.	securities on their
	Trading a block can only be done on an appointment basis.	balance sheet.
	• Of note, the last \$300mn auction of RRB 0.5% Dec 2050 was done	Bid-ask is not a
	on February 10. On that day the central bank was not able to buy	reliable indicator
	its maximum of 6 Canada RRBs for a total of \$450mn with a target	for trading.
	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.	

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