AllianceBernstein

January 2021

Market Update – Fixed Income Trading Liquidity
For the Week Ended 8 January 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	• The market has cleared three major risk events and sources of uncertainty in the last 6+ weeks; including the US Presidential election, the Georgia Senate runoff elections and Brexit. Global developed market yields sold off during the week ended January 8 with the US yields being the worst performer, trading higher by 20 basis points. The primary catalyst was the Senate runoff election in Georgia which resulted in both democratic candidates winning the seats, thereby completing the "blue sweep" • Rate curves steepened as the long end led the selloff; the US Treasury 5s30s curve steepened by 10 basis points to 138bps steep. • Away from the long end there was focus on the 5-year point in the curve as well, with many market participants thinking that increased fiscal stimulus will test the current FOMC rate hike resolve, which prior to the blue sweep showed FOMC on hold through 2023. Markets questioned whether the economy may have to deal with higher levels of inflation and price in hikes earlier. • Depth is high in both cash and futures markets. Facilitating large risk transfers can be done without "paying up" for the liquidity • Federal Reserve bond purchases stand at $80 billion US Treasuries and $60 billion MBS per month.	Bid-offer spreads are trading in line with pre-covid levels. Bid-offer spreads have returned to the width seen pre-election with 10-year notes trading ½ of a tick wide and 30-year notes trading 1 tick wide.
Investment Grade (IG) Corporates	**US IG** • Following two weeks of no supply and dealers having roughly $7bn net in risk "lifted" from their balance sheets, technicals in the US IG market were very firm during the week ended January 8 despite the weaker macro tone at the start of the week. The bid for investment-grade bonds remains strong,	Bid/ask conditions in the IG market are back to normal

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	particularly for longer-maturities and higher-beta issuers. • New issue supply overwhelmed expectations with over $50bn pricing during the week. Technicals in the primary market were strong, with deals being multiple times oversubscribed despite pricing with negative concessions on average and performed well in the secondary market. • The positive momentum on flows seen in 2020 continued this week, as the market saw inflows of $5.36bn. • Supply for the week ending January 15 is expected to slow relative to this week, with $25-30bn expected. **European IG** • During the week ended January 8, focus was on the primary market, with ~EUR18.5 bn issued. New issue premiums were generally non-existent, and this was absorbed in the secondary market, but in certain spots this cause a little market indigestion. **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 January 8, the US High Yield market was firm, as risk rallied following the Georgia US Senate runoff election. While interest rate sensitive bonds underperformed the broader high yield index rally following the rate selloff, there were not large volumes actually trading lower. • The primary market priced $8.2bn across 10 deals. In line with the pattern of the past 3 months, deals continue to price inside of initial price guidance with meaningfully oversubscribed books (up to 7.3x). Increased attention from new deals reset existing bonds in the same issuers at lower yield 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

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	• New issuance is expected to continue to print at a moderate pace, but may be spread across more deals of smaller size. • The high yield index was 10bp tighter to 350bp. The spread between CCC- and BB-rated bonds was 34bp tighter to 360 bp. The beta compression was exacerbated by the rate sensitivity of higher-rated bonds. **Euro HY** • During the week ended January 8, trading volumes remained low to start the year as investors awaited what has been well-telegraphed to be a busy primary market calendar in January and February. • Generally, investors were putting residual cash from 2020 to work, while the primary market was slower to turn than other markets and so cash bond spreads ground tighter. Covid-exposed names were the exception, with profit taking over the course of the week as UK lockdowns came into effect and concern grew over new strains globally. **CDX HY** • CDX HY traded unchanged, underperforming both cash bonds and stocks during the week ended January 8. Trading volumes picked up after the holidays, but flows were on the quiet side as attention seemed to be paid to the cash market supply. Bid/ask spreads have declined to pre-crisis levels for "social" sizes.	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 played second fiddle to core interest rates during the week ended January 8. As Democrats took control of the US Senate, Treasury yields spiked 20bp and the EMBI Global Diversified Index spreads tightened 4bp. • Secondary market volumes were below average as market participants assessed the new issue calendar and assessed the implication of rising rates on risk assets. Beta compression continued, as generic sub-Saharan Africa debt was up 1-3points while 30-year Gulf Cooperation Council (GCC) and investment-grade Latin America debt was down ~3 to 5 points (although spreads were ~5bp tighter). • Supply got off to a fast start as the strong technical picture remained intact. Four deals priced in the Latin America sovereign and corporate space for a total of $6.35 bn vs total subscriptions of $24bn, and	EM IG and HY sovereigns and EM IG and HY corporates are back to normal market conditions

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	average new issue premium of ~7bp with deals on average trading up 50 cents on the break. • Robust inflows continued **Local Currency EM** • Liquidity is close to normal.	
Asia	**Asia Hard Currency** • Asia saw $22.5bn in primary market supply during the week ended 8 January, with $15bn investment-grade and $7.5bn high yield/non-rated bonds coming to the market. • Performance was muted to start the year with investment-grade finishing relatively flat and high yield 8bps wider on the week. New issue performance underwhelmed with roughly 50% of new issues underwater by the end of the week. • China bonds facing US Executive Order sanctions or potential sanctions led the weakness, moving generally 25-50bp wider. • Indian steel and renewables also came under pressure with selling due to tight valuations. **Asia Local Currency** • Asia local currency bond markets had a turbulent week with higher-beta/carry issuers underperforming amid rising US Treasury yields. • Indonesia auctioned 41trn to start the year and despite books being 2x oversubscribed, the bonds failed to gain traction amid looming supply. The majority of interest has come from onshore clients and, as yet, there has been little foreign interest to add at these low yields.	Asia IG credit is ~1 to 1.5x wider vs. normal market conditions Asia HY credit is ~1 to 1.5x wider vs. normal market conditions Asia local currency debt is ~1 to 1.5x wider vs. normal market conditions
Securitized	**CMBS** • During the week ended January 8, CMBS spreads were little changed week over week. 10-year AAA-rated bonds have nestled into the swaps+70bp area, while single A-rated bonds have settled near swaps+175bp. • New issue supply was near zero last week. Only one small single asset/single borrow issue priced. The deal was securitized by a portfolio of multi-family commercial mortgages and all classes priced well through the initial price guidance. The new issue calendar is expected to remain modest for the remainder of the month. • Bid/offer spreads remain unchanged: spreads for AAA to A-rated classes have retraced their post-covid-19 widening, while bid/offer spreads for BBB-	

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	rated classes remain approximately 2x their pre-covid-19 levels. • At the top of the capital stack, CMBX was little changed week over week. However, many mezzanine classes ended the week tighter. Series 8-12 were the best performers, as the BBB- tranches rallied 4-13bp. Trading volume was higher than average for most BBB- tranches. Bid/offer spreads remain unchanged. CMBX A.6, BBB-.6, and BB.6 bid/offer spreads remain approximately 2x their historical averages. **ABS** • The ABS primary market priced no new deals for the week ending January 8. There are five transactions currently pre-marketing for the week beginning January 11, across prime auto lease, prime and subprime auto loans. • The ABS market opened with tighter spreads in the first week of 2021, on sustained positive technical momentum. Benchmark ABS spreads tightened week over week across sectors with 2-10bp tightening recorded across non-prime auto, 5-10bp across FFELP and private credit student loan ABS, 2-5bp across equipment and 1-5bp across the AAA-rated segment of credit card ABS. • 3-year AAA-rated credit card and prime auto loan ABS benchmark spreads are currently at swaps +6bp and +13bp, respectively, while BBB-rated nonprime auto ABS spreads stand at +95bp. **CRTs** • During the week ended January 8, the CRT market was in focus as volumes picked up and spreads rallied across the board. Investor appetite was mixed with very light dealer balance sheets to bring spreads in even during the tumultuous political news of the week. • There was no primary market issuance during the week. There is talk that Fannie Mae will return to the market this year with the new US administration and the potential easing of capital rules for the GSEs around issuing CRTs • Secondary market liquidity remains robust and there is good two-way flow in all aspects of the CRT market. Bid/ask spreads have normalized around pre-covid levels.	

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	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 January 8 was a busy one in the CLO market. The new issue market came back to life with >10 new deals being announced. The progress of these deals seems to be going well with all classes oversubscribed. Interest appears particularly high in the smaller mezzanine classes. Spreads in these classes have tightened roughly 50-70 bp since early December. • 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 money market space has remained resilient through the broader market volatility. • SOFR is setting at 0.09-0.10%. The repo rate is in the 0-0.10% range. The Fed Funds Effective Rate set at 0.09%. • 1-month LIBOR set at 0.13%, while 3-month LIBOR set at 0.23%. • Government money market funds saw $27bn of outflows in the 7 days ended January 8. Prime funds had $2bn in inflows over the same period.	
US Municipals	• During the week ended December 31, high grade municipals outperformed interest rate markets, with benchmark yields wider by 1-4bp for 2024-2026 maturities and 5-6bps wider for 2027 maturities and beyond. • The ratio of AAA-rated municipals/US Treasuries hit new lows on Thursday with 5-year maturities the tightest at 51% and the 30-year spot at 77%, which is typically closer to 100%. • Technicals continue to be strong in the municipal market, given a light new issue calendar last week ($2.9bn overall). Issuers largely stayed on the sidelines waiting to see how the US Senate runoff election in Georgia on Tuesday would play out. Once the results were known, there was continued	

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	compression as higher-yielding issuers, like MTA, Chicago, Detroit outperformed high grade issuers, as the blue wave is seen as positive for those higher-yielding issuers given the expectations of stimulus and implied support. • For the upcoming week, the new issue calendar is beginning to pick up, although still light, with $6.5bn expected. • Odd lot haircuts to round-lot bidside evaluations were in line with where they have been recently: roughly one point for small size (<50k) and around 0.5 points 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$191 billion to support liquidity in Government of Canada markets since the purchase program started on March 27 through January 7. Government of Canada bonds are the most liquid securities in capital markets in Canada as seen in the latest (November) Bank of Canada research. (Note: BOC figures can be revised) **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$13.8 billion in par value year to date through January 7 within their provincial buying program to support liquidity. A continued rise in crude oil prices from current levels could help liquidity in provinces where oil revenues	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. 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. BBB- corporates are trading by appointment,

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	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. • Trading on an agency basis for high-beta issuers. • 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 January 7). BBB- bonds are trading by appointment unless there is a new issue. **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.	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.

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