ALLIANCEBERNSTEIN®

July 2021

Market Update – Fixed Income Trading Liquidity
For the Week Ended 9 July 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 holiday shortened week ended July 9 was a volatile one for global developed market (DM) interest rates. The US curve traded with a sharp bull-flattening bias into Thursday when 10-year yields touched 1.25% intraday. This reversed on Friday as selling from the Asia-Pacific region pushed yields higher. • Liquidity in terms of market depth in on-the-run cash 5-year and 10-year Treasuries has improved meaningfully from the challenges seen in February 2021. • Observable bid-offer spreads are in line with historical averages in on-the-run bonds. Transaction costs in off-the-run bonds are wider but have improved meaningfully since late February. Longer-maturity TIPS bid offer spreads are 1-2 ticks wide vs. normal levels. • Federal Reserve bond purchases continue at $80 billion US Treasuries and $40 billion MBS per month.	
Investment Grade (IG) Corporates	**US IG** • The summer lull began to set into the US IG market during the week ended July 9, as there was low engagement in both primary and secondary markets. On the back of macro volatility and the interest rate rally, spreads leaked wider throughout the week, with the index moving 3bp wider week-over-week, but the tone improved Friday following the back up in interest rates. • As expected, supply was light, with ~$19 billion pricing and lower engagement than in recent weeks with deals 2.3x oversubscribed on average (vs YTD average of 3x) and pricing with 9.6 bp new issue premium on average (vs YTD average of <1bp). • In the secondary market, flows were mostly balanced and light relative to YTD average flows. Overnight flows were quiet amid the rate volatility. Overall positive momentum on flows continued with $4.3 billion in inflows during the week. • In the week ahead, supply is expected to be in the range of $15-20 billion.	Bid/ask conditions in the IG market are back to normal

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	Euro IG • Euro and GBP IG spreads were unchanged to 1bp tighter with low trading volumes during the week ended July 9. • Flows were modestly skewed to better sellers, predominately after the mid-week move in interest rates. • Supply remained relatively light as summer begins. ESG structures continue to be in focus with ~40% of the week's supply being ESG-related. Overall book coverage was low, and new issue premia increased modestly. Most deals still performed well in the secondary market. **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** • During the week ended July 9, US HY market spreads were 2 bp wider week-over-week to 269 bp. The CCC-BB spread difference was 12 bp tighter to 252 bp. While the technical landscape hasn't changed, there was some price volatility on Thursday amid the broader risk-off sentiment. • In the primary market $1.625 billion priced across 3 deals. New issues continue to face the same positive demand technicals seen all year with deals multiple times oversubscribed and supported in the secondary market. **Euro HY** • In the week ended July 9, the focus remained on primary market supply. Subscriptions suggest investor cash balances are healthy. Underlying technicals are constructive. • The secondary markets remained heavier although seemed to find firming footing as investors are noticing the underperformance of Euro HY vs US HY in recent weeks. **CDX HY** • CDX HY traded weaker, once again underperforming both the macro tone and cash bonds during the week ended July 9. • Trading volumes picked up amid the macro volatility • Bid/ask spreads have declined to pre-crisis levels.	Bid/ask spreads vary by issuer but generically: BB-rated securities: 0.75 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 in line with normal conditions.
Emerging Market Debt (EMD)	**Hard Currency EM** • During the week ended July 9, core interest rates were in focus, index spreads widened by 4 bp, and spreads continued to decompress as EM HY underperformed EM IG by another 4bp.	EM IG and HY sovereigns and EM IG and HY corporates are

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	• Supply slowed in Latin America, but EMEA remained active. Demand from Asia continued apace, helping to stabilize IG credit even as global macro risk teetered. **Local Currency EM** The local EM rates market liquidity has deteriorated amid US Treasury market volatility and central bank policy changes.	back to normal market conditions
Asia	**Asia Hard Currency** • During the week ended July 9, Asia credit primary market issuance was skewed to high-grade issuers due to lower US Treasuries, with USD 7.4 billion printing. Secondary market performance dragged, with 80% of new issuance underwater by end of the week. • There was a softer tone to the market, with a reluctance of buyers in most investment-grade secondary markets. • The China HY property sector continued to be under pressure, with bonds generically down 0.5 to 2 points with the tighter liquidity, but spillover effects to other segments has been minor. **Asia Local Currency** • China's PBOC cut its Reserve Requirement Ratio (RRR) by 50 bp on late Friday afternoon, which few sell-side reports were anticipating, and which led onshore interest rates to tick lower. • Covid cases continue to rise across South East Asia but impact on liquidity in bond and currency markets remains muted.	Liquidity conditions are normal for Asia credit Liquidity conditions are normal for Asia local currency debt
Securitized	**CMBS** • During the week ended July 9, CMBS spreads were little changed week-over-week. BBB-rated classes widened 1bp, while AAA-rated classes remained unchanged. There was no new conduit issuance, but 2-3 new deals are expected in coming weeks. Secondary activity remained modest • With muted primary and secondary market supply, the technical backdrop of the CMBS market remains positive. Bid/offer spreads in AAA to A rated tranches have retraced their post-COVID widening, while BBB rated classes remain 2x the historical average. • CMBX was softer in most series and tranches, albeit on very low trading volume. Summer doldrums seem in place with dealers less likely to take additional risk. Bid/offer spreads in CMBX have retraced their post-COVID widening. **ABS** • The ABS primary market priced one $240mn unsecured consumer loan transaction during the week ended July 9. ABS year-to-date supply now stands at $129.2 billion compared to $81.3 bn over the same period in 2020. The calendar for the week of July 12 has eleven deals totaling $7.4bn in premarketing. • Indicative benchmark spreads remained near cyclical tights. Taking a cue from the primary market, BBB and indicative BB-rated	

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	unsecured consumer loan ABS spreads tightened by 20bp to 150 bp and 40 bp to 320 bp respectively on the week. • U.S. light vehicle sales for June tracked 15.4mn SAAR, missing consensus estimates of 16.6mn. The Manheim Used Vehicle Index recorded a sequential decline of -1.3% for the month of June, after a +26% sequential rise for the first five months of the year. **CRTs** • During the week ended July 9, last cash flow bonds were generically unchanged. B! and B2 bonds saw their first sign of weakness following the macro volatility on Thursday. • Secondary market liquidity is robust and bid/ask spreads remain tight, 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** • Generic primary market clearing levels on the week stood roughly at 112-115 bp for AAA-rated spreads; AA-rated spreads at around 165 bp; A-rated at 205bp; BBB-rated at 310 bp; and BB at 625-675 bp with top tier managers pricing at par and lower quality managers needing OID (original issue discount) to print deals. • 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. Current coupon bonds are trading at 0.5-1 tick wide and the rest of the coupon stack is wider by 2-2.5 ticks.	
Money Market	• The Fed Reverse Repo facility (RRP) usage remains high at ~$776 billion. • 1-month LIBOR set at 0.096%; 3-month LIBOR set at 0.133%, a new record low. • SOFR set at 0.05%. The Effective Federal Funds Rate set at 0.10%. • Government money market funds had $15 billion of outflows in the week ended July 9. Prime funds had $16bn of outflows over the same period.	
US Municipals	• In the week ended July 9, the municipal market was firm, outperforming US Treasuries by 2-7bp across the curve. The rate-driven rally was coupled with strong seasonal technicals—investors have extra cash to put to work from principal and interest payments. New issues continue to perform strongly with oversubscriptions typically in double digits.	

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	• Liquidity has been robust with odd lot discounts at or better than pre-covid tight levels.	
Canadian Market	**Federal** • Liquidity is best in benchmark issues for block sizes of <=CAD25 million. Bank of Canada (BOC) is “buying at least $3 billion of Canadian government bonds a week until the recovery is well underway.’’ It should continue to support market liquidity. “Purchases of longer-maturity bonds have a greater impact, dollar-for-dollar spent, by removing more term risk from markets and putting downward pressure on term premiums. Lower term premiums imply lower GoC bond yields, all other things equal.” • The latest BOC balance sheet shows that the central bank continued to support liquidity in Canadian markets (as of July 7). • The Government Bond Purchase Program (GBPP) has resulted so far in $249.92 in net buying (assets minus liabilities minus position at the start of the QE in March 2020). Many banks are expecting a reduction of QE bond buying to $2bn per week after the next BOC meeting. • 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 but will favor agency trades. • The Bank of Canada’s Provincial Bond Purchase Program (PBPP) has ended. Therefore, the central bank does not provide a back stop to the provincial sector. Reduced trading activity during summer months could hinder liquidity. **IG Corporates** • The latest Bank of Canada research highlights the limited liquidity in Canadian corporate bond markets, which can impact pricing; many dealers are maintaining low balance sheet inventories, so will not provide bids in some sectors. • Trading on an agency basis for high-beta issuers. • The Bank of Canada had a buying program (focused on securities of 5-years or less) to support liquidity for corporate bonds rated BBB and higher. As expected, the BOC has end this Corporate Bond Purchase Program (CBPP) on May 25, 2021. Lower corporate supply in summer months could lead to reduced secondary market liquidity.	Federal: bid/ask was at 5 cents in the 10-year area, but for the long end of the curve, it remains relatively wider at up to 15 cents given the recent higher volatility. Off the run, high coupon Canadas were reported to have limited liquidity in volatile periods with much wider bid-ask given small outstanding size in these securities. For example – the latest ultra-long Canada 2064 bid-ask is at 35 cents reflecting its liquidity issues given this is not a benchmark. 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 depending on market tone.

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	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 continued lack of liquidity. Trading a block can only be done on an appointment basis. • In the aftermath of the federal budget there were indications that Canada will issue only C$1 billion in RRBs in the current fiscal year with four actions. This will result in net negative supply (BOC buying program plus maturities less new supply). The last $400m RRB auction in the RRB Canada 2054 bond reflected the net negative supply with a $316m buyback RRB program and estimated $800m + in coupon payments on June 1. • Liquidity remains challenging, trading by appointment, as dealers hold very limited inventories in RRB securities.	BBB- corporates are generally 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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