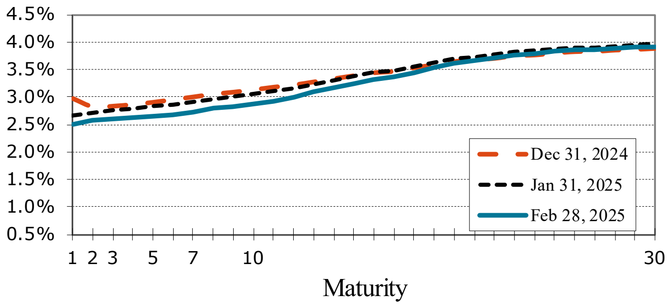
Baird Advisors
Municipal Fixed Income Market Commentary
February 2025

Tax-exempt Yields Fall and Supply Remains Robust

Tax-exempt yields fell in February, continuing the favorable trend that began in January. Short-term and intermediate yields declined the most, steepening the curve. Short and intermediate rates fell 14 - 18 bps, the 30yr yield fell 4 bps and the 2s10s curve narrowed slightly to +32 bps. The demand for municipals was strong throughout the month, evidenced by $4.4B of net inflows to tax-free funds/ETFs, bringing YTD inflows to $6B. Even short-term funds continued to see inflows, a reversal of the outflows seen in 2024. All other segments of the market experienced positive flows. The solid demand helped the market digest another month of heavy issuance. $38B of tax-exempt municipal supply came in February, up 33% from the same month last year which brings the YTD supply 23% above last year's record pace. Amid the flurry of news emerging from the Trump administration, we are monitoring potential tax policy and/or federal funding changes being considered. It was encouraging to see a House bill submitted that would restore tax-exempt advance refundings, perhaps signaling broader support for municipals, but it is still early in the process. Approximately 36% of total state revenues come from the federal government, according to Bank of America, so any budget cuts at the federal level are likely to have consequences at the state and local level as well.

AAA Municipal Yields



Maturity	12/31/23	12/31/24	1/31/25	2/28/25	1Mo Chg
1	2.59%	2.97%	2.65%	2.51%	-0.14%
2	2.50%	2.82%	2.71%	2.56%	-0.15%
3	2.35%	2.83%	2.76%	2.60%	-0.16%
5	2.22%	2.90%	2.83%	2.65%	-0.18%
7	2.19%	3.00%	2.91%	2.74%	-0.17%
10	2.27%	3.13%	3.06%	2.88%	-0.18%
30	3.40%	3.87%	3.96%	3.92%	-0.04%

Risks and Opportunities in Higher Education

February brought news that Northland College, a small, private school in Ashland, WI will close at the end of the semester. This story is not uncommon across the higher education landscape. Many small, private schools face the same concerns: falling enrollment (Northland's enrollment had declined to less than 300 students), consistent operating deficits and declining balance sheet assets. The most recent projections from the Western Interstate Commission for Higher Education, completed in 2024, indicates the number of high school graduates is expected to peak in 2025 and then decline through 2041. Added to these challenges are potential tax law changes targeting large college endowments and a potential decrease in Federal research grants. Higher education institutions received over $100B in aid to help them recover from the Covid-19 pandemic, and those funds helped many schools delay some tough decisions resulting in the pace of mergers and acquisitions increasing as aid rolls off. Despite the challenges, there are some bright spots. Of public universities rated by S&P, only 10% carry a rating of BBB+ or below, and while that number is 48% for private universities, the vast majority are rated investment grade, with only 10% rated below IG. Further, 84% of S&P's ratings for universities at the end of 2024 had a stable outlook. The experience and strength of the management team and their ability to right-size budgets and manage the loss of pandemic aid is critical to evaluating higher education credits. Diversification of issuers/universities is important as the sector includes debt from schools like Harvard and Yale to lesser-known schools that attract a steady stream of students. Strong fundamental credit analysis can help investors identify both the risks and opportunities in the space.

Positive Returns in February

February returns were positive, as yields fell across the curve. Intermediate and long maturities outperformed short maturities. By sector, GO and Revenue bonds had near equal returns and both outperformed the shorter duration Prerefunded sector. Across the quality spectrum, returns were similar, with A-rated bonds slightly underperforming all other rating categories. High-Yield continued to outperform investment grade issues.

Total Returns of Selected Barclays Municipal Indices and Subsectors

Bloomberg Index/Sector	February	YTD	*Duration*	Bloomberg Quality	February	YTD	*Duration*
Municipal Bond Index	0.99%	1.50%	*6.28*	AAA	1.01%	1.57%	*6.50*
General Obligation bonds	1.01%	1.47%	*5.93*	AA	1.00%	1.41%	*6.11*
Revenue bonds	1.00%	1.52%	*6.48*	A	0.96%	1.57%	*6.28*
Prerefunded bonds	0.51%	1.16%	*2.44*	BBB	1.03%	1.83%	*7.19*
Long maturities (22+ yrs.)	0.98%	1.06%	*10.08*	High Yield	1.25%	2.02%	*6.64*
Intermediate maturities (1 - 17 yrs.)	0.98%	1.67%	*4.76*	HY, ex-Puerto Rico	1.29%	2.01%	*6.60*
Short maturities (1 - 5 yrs.)	0.61%	1.15%	*2.34*				

Disclosures

Fixed income is generally considered to be a more conservative investment than stocks, but bonds and other fixed income investments still carry a variety of risks such as interest rate risk, credit risk, inflation risk, and liquidity risk. In a rising interest rate environment, the value of fixed-income securities generally decline and conversely, in a falling interest rate environment, the value of fixed-income securities generally increase. High yield securities may be subject to heightened market, interest rate or credit risk and should not be purchased solely because of the stated yield.

The Bloomberg Municipal Bond Index is a broad-based, total-return index. The bonds are all investment-grade, tax-exempt, and fixed-rate securities with long-term maturities (greater than 2 years). They are selected from issues larger than $50 million. The components listed below the Municipal Bond Index (long maturities, intermediate maturities, short maturities, prefunded bonds, general obligation bonds and revenue bonds) are subsectors of the Bloomberg Municipal Bond Index and do not represent separate indices.

The Bloomberg High Yield Municipal Index includes bonds with a par value of at least $3 million and must be issued as part of a transaction of at least $20 million. The maximum rating for inclusion is Ba1/BB+/BB+ using the middle rating.

For more information about the Bloomberg Municipal Bond Index or Bloomberg High Yield Municipal Index, please visit https://index.barcap.com/Home/Guides_and_Factsheets.

Municipal securities investments are not appropriate for all investors, especially those taxed at lower rates. The alternative minimum tax (AMT) may be applicable, even for securities identified as tax exempt. Past performance is not a guarantee of future results.

Ratings are measured on a scale that ranges from AAA or Aaa (highest) to D or C (lowest). Investment grade investments are those rated from highest down to BBB- or Baa3.

Robert W. Baird & Co. Incorporated.

This is not a complete analysis of every material fact regarding any company, industry or security. The information has been obtained from sources we consider to be reliable, but we cannot guarantee the accuracy. Indices are unmanaged and are not available for direct investment.