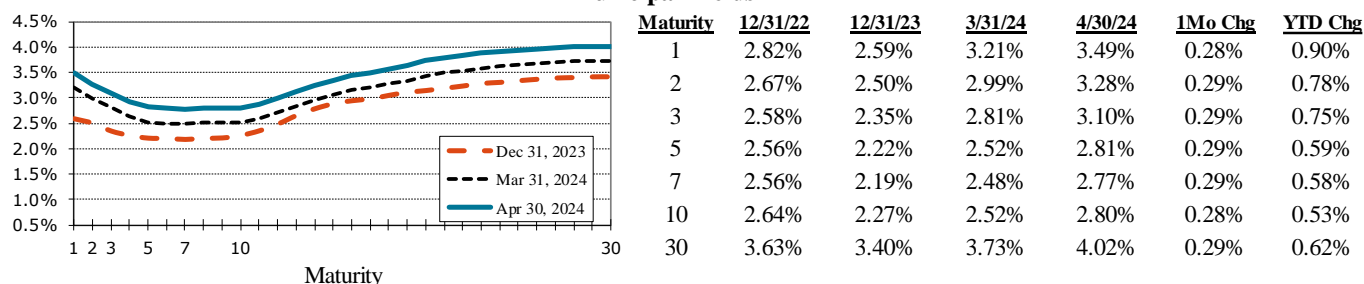


Baird Advisors
Municipal Fixed Income Market Commentary
April 2024

Municipal Yields Continued to Rise in April

Tax-exempt yields rose in April in a near parallel manner, up approximately 29 bps across the curve. Year-to date, short-term rates have risen more than longer-term yields, sustaining the inverted municipal yield curve between 2s10s. Like the Treasury market, municipal yields also rose on the strong inflation data this month with investors now expecting just one Fed rate cut before year end. April also saw continued robust issuance with \$40B of new tax-exempt supply, up 31% YoY and 43% ahead of last year's pace YTD. Demand for municipals remained strong, with \$2.3B of net inflows in April, slowed only slightly by seasonal income tax payments, bringing YTD net inflows to \$9.4B. Looking forward, the municipal market is entering a favorable supply/demand period in which reinvestment demand should easily exceed supply. For example, BofA Global Research estimates there will be \$231B of bond calls/maturities and coupon payments between May and August compared to just \$160B of new supply. If true, then tax-free yields should continue to trade on the rich side of historic valuations relative to taxables through the summer months.

AAA Municipal Yields



Texas MUD Development Boom

Much has been written about select state population declines since the pandemic, but that is not the case for Texas. According to the US Census Bureau, Texas' population grew by 4.7% between 2020 and 2023, relative to 1.0% growth for the US. Population growth drives development and in Texas that development is often financed through Municipal Utility Districts (MUDs). These are primarily residential developments that allow the developer to be repaid for improvements through tax collections as the district grows. Over the past ten years, tax base growth has driven ratings upgrades from Moody's in nearly 100% of their rated MUDs with the median rating now at A3. MUDs are appealing municipal investments in that the debt is issued commensurate with tax base growth, providing attractive property tax support for the debt. In addition, MUD debt issuance requires the approval of the Texas Attorney General with ongoing oversight provided by the Texas Commission on Environmental Quality (TCEQ) which monitors debt levels and tax rates. Of course, the continued issuance of MUD debt relies upon on a favorable housing market and demand for new homes. Fortunately, elevated home prices in the Austin, Dallas and Houston metropolitan areas mean that new residential construction costs are still relatively attractive, fostering further growth and development. Yet, we know that housing has historically been subject to boom-and-bust cycles, especially during previous periods of energy price volatility, so prudent credit analysis is warranted. And as the housing discount between select Texas communities, such as Austin, and home prices in higher cost states (e.g. NY and CA) narrows, we would expect the pace of MUD expansion and debt issuance to slow. In the meantime, barring a significant downturn in the Texas economy, MUD bonds should remain a sector of focus.

Rising Rates Drive Negative April Returns

The increase in yields led to negative returns across the municipal market in April, with the long end of the curve lagging short-end performance as yields rose. Across market sectors, Pre-refunded bonds outperformed other sectors and maintained their YTD lead relative to both GOs and Revenue issues. Of the investment grade rating categories, A-rated bonds performed the best in April, but High-yield municipals beat all credit categories for the month and YTD.

Total Returns of Selected Barclays Municipal Indices and Subsectors

<u>Bloomberg Index/Sector</u>	<u>April</u>	<u>YTD</u>	<u>Duration</u>	<u>Bloomberg Quality</u>	<u>April</u>	<u>YTD</u>	<u>Duration</u>
Municipal Bond Index	-1.24%	-1.62%	6.15	AAA	-1.36%	-2.16%	6.42
General Obligation bonds	-1.26%	-1.95%	5.87	AA	-1.22%	-1.77%	6.03
Revenue bonds	-1.27%	-1.54%	6.40	A	-1.17%	-1.07%	5.99
Prerefunded bonds	-0.15%	-0.24%	2.06	BBB	-1.40%	-0.80%	7.27
Long maturities (22+ yrs.)	-1.69%	-2.42%	10.23	High Yield	-0.61%	0.89%	6.94
Intermediate maturities (1 - 17 yrs.)	-1.03%	-1.32%	4.56	HY, ex-Puerto Rico	-0.56%	0.82%	6.89
Short maturities (1 - 5 yrs.)	-0.35%	-0.54%	2.26				

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.

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