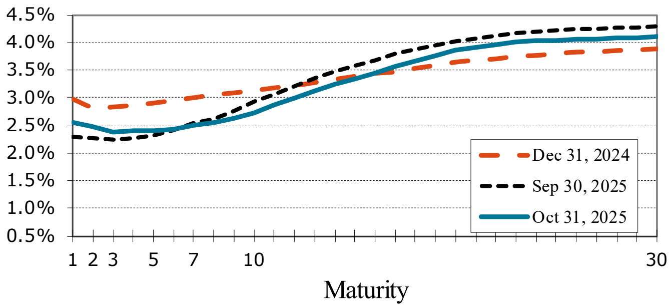
Baird Advisors
Municipal Fixed Income Market Commentary
October 2025

Municipal Curve Flattens as Pace of New Supply Slows

The FOMC cut the Fed Funds rate by 25 bps at its October meeting, yet short-term municipal rates rose while long-term rates declined, flattening the curve. Chair Powell's hawkish tone during the press conference dampened expectations for another cut in December, driving the 2yr yield up 22 bps and the 30yr yield down 18 bps for the month. The 2s–30s slope ended the month at +163 bps, down from a peak of +243 bps in late August, but still 58 bps steeper YTD. Supply remained heavy, with October tax-exempt issuance totaling $51B, although it was 12% below October 2024's levels. Year-to-date tax-exempt issuance totals $455B, a 12% increase over 2024, and only $5B shy of 2024's record level. Demand was also strong, as funds posted $8B of net inflows for the month, bringing the YTD total to $37B, ahead of $32B at this point last year. The municipal market was largely unaffected by the ongoing government shutdown, now in its fourth week. However, if the shutdown persists for several more weeks, some federally dependent sectors such as select housing bonds (e.g. Section 8) and transportation debt backed by Highway Transit Funds could face delayed payments. Despite this, heavy reinvestment demand in November and December from principal and interest payments are expected to exceed the amount of new issuance, supporting the market into year-end.

AAA Municipal Yields



Maturity	12/31/24	9/30/25	10/31/25	1Mo Chg	YTD Chg
1	2.97%	2.30%	2.54%	0.24%	-0.43%
2	2.82%	2.27%	2.49%	0.22%	-0.33%
3	2.83%	2.25%	2.39%	0.14%	-0.44%
5	2.90%	2.31%	2.40%	0.09%	-0.50%
7	3.00%	2.54%	2.50%	-0.04%	-0.50%
10	3.13%	2.92%	2.73%	-0.19%	-0.40%
30	3.87%	4.30%	4.12%	-0.18%	0.25%

State Pension Plan Update

The most recent data indicates state pension funding improved in 2024, with the median funded ratio for state plans reaching 79%, up 3% from 2023, according to The Equable Institute's 2024 State of Pension's report. Strong investment returns reduced unfunded liabilities to $1.3T from $1.4T, though results varied widely; Nebraska led all states with a 108% funded ratio, while Illinois remained the weakest at 52%. While the improvement in state pension funded ratios is encouraging, sustainability depends on consistent contributions and disciplined funding practices going forward, particularly if future market returns fall short of expectations. Despite Illinois' poor state-level results, there are bright spots to note within the state. According to a report by Illinois Policy Institute, the Illinois Municipal Retirement Fund was funded at 95.8% at the end of 2024. This fund covers local employers working in school districts, counties, cities and villages and the plan is designed so the current year's taxpayers cover that year's benefits, avoiding deferred contributions and steep ramp up provisions. In addition, Moody's upgraded the state's credit rating to A2 from A3 in October and highlighted the state's seven consecutive years of balanced budgets, the paydown of bill backlogs and an increase in the state's rainy-day fund – all favorable developments.

Positive Returns for Intermediate and Longer Maturities in October

Yields fell across intermediate and longer maturities in October leading to positive monthly returns for all but the shortest curve segment. Not surprisingly, longer maturities outperformed all other curve segments. By sector, GO and Revenue bonds also outperformed the shorter duration Prerefunded sector for the month. From a credit quality perspective, BBB-rated issues slightly edged out higher-quality issues for the month, while A-rated issues have provided the best performance YTD among all rating categories.

Total Returns of Selected Barclays Municipal Indices and Subsectors

Bloomberg Index/Sector	October	YTD	*Duration*
Municipal Bond Index	1.24%	3.91%	*6.65*
General Obligation bonds	1.23%	3.93%	*6.34*
Revenue bonds	1.26%	3.90%	*6.83*
Prerefunded bonds	0.11%	3.54%	*2.50*
Long maturities (22+ yrs.)	1.83%	2.15%	*10.94*
Intermediate maturities (1 - 17 yrs.)	0.87%	4.61%	*4.89*
Short maturities (1 - 5 yrs.)	-0.12%	3.51%	*2.35*

Bloomberg Quality	October	YTD	*Duration*
AAA	1.22%	3.89%	*6.87*
AA	1.23%	3.87%	*6.55*
A	1.25%	4.09%	*6.56*
BBB	1.33%	3.68%	*7.48*
High Yield	1.00%	2.31%	*7.47*
HY, ex-Puerto Rico	0.92%	2.33%	*7.44*

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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