Q1 2026 Commentary and Market Outlook

Baird Equity Opportunity Fund

Baird Funds

PORTFOLIO COMMENTARY

Fellow shareholders,

Equities struggled for traction during the first quarter, challenged by the war in Iran, concerns over the direction of monetary policy, and, to a lesser extent, uncertainty over how the uptake of Artificial Intelligence (AI) could negatively impact prominent elements of the broader economy. The Russell 2000 Index posted a 0.89% total return for the quarter. The Baird Equity Opportunity Fund underperformed, generating a net return of -11.39%. *

Following a solid start to the year, equities sold off toward the latter part of the quarter due to the conflict in the Middle East, though the Russell 2000 managed to eke out a 0.89% gain. While our 3-month results did not follow, we are encouraged by the relatively solid performance of small-caps. From a sector standpoint, energy, materials, and industrials led the way. By contrast, consumer, healthcare, and technology – software, in particular – posted notable declines. Sector moves during Q1 were a headwind to portfolio results given our smaller exposure to energy and materials and larger stakes in software and related shares.

Market weakness and sector impacts aside, the war in Iran caused few direct impacts on the portfolio. While a spike in the oil price impacted Norwegian Cruise Line's stock price (NCLH, down 16% in the quarter), it helped boost shares of energy holding Oceaneering International (OII, up 48% in the quarter). Indirectly, however, the war has disrupted the formerly expected path of accelerating economic growth and more accommodative monetary policy, sapping some enthusiasm for small-cap stocks in March. Unlikely just three months ago, it is now a proverbial coin flip whether the next Fed action is an interest rate cut or a hike thanks to elevated energy prices and disrupted supply chains brought on by the conflict.

More impactful to our Q1 performance was the heightened exuberance for all things related to AI. The consensus narrative is that, to reap the benefits of the power of AI, the buildout of necessary infrastructure will last as far as the eye can see. At the same time, a powerful overhang has emerged that AI will render most software companies "damaged goods" or even existentially obsolete as AI agents proliferate and replicate their work for a fraction of the cost. Look no further than the staggering disparity between the performance of semiconductor stocks, broadly perceived to be "AI winners", and software stocks: in the first quarter alone, the iShares Semiconductor ETF outperformed the iShares Expanded Tech-Software Sector ETF by over 33%.

Despite our best efforts in planning for this possibility, including elimination of software names Gitlab (GTLB) and Blackbaud (BLKB), and the fortuitous acquisition of Confluent (CFLT) by IBM, the portfolio nonetheless experienced secondary effects that impacted Q1 results. BILL Holdings (BILL) and NCR Voyix (VYX) represented collateral damage, both selling off with the broader software group despite being much less exposed to the AI-driven fears that have gripped the sector. Both names were among our top three detractors in the first quarter.

In BILL's case, its business model is led by payments, with BILL receiving a percentage of each dollar that it processes in the payment stream between small businesses. This represents the majority of the company's revenue and would be hard to replace with an agent. However, while software subscriptions generate only a fifth of the company's revenue, it hasn't stopped BILL from finding itself as a perceived AI loser, presumed guilty until proven innocent. Even strong results in February and a rumored go-private transaction were only enough to help the stock for a short period of time before revisiting its recent lows.

Similarly, VYX was pummeled despite building evidence that the one-year-old turnaround is entering a more prosperous phase. With a well-regarded new product set, nascent customer wins, a fortified management team and balance sheet, and building business momentum, the stock felt poised to rise from its bargain-basement valuation at the start of 2026. Instead, it was unable to escape the clutches of negative software sentiment, and the stock finished the quarter down 38%. Trading with a roughly 20% free cash flow yield, management is now stepping up its share buyback, which could eliminate over a quarter of the outstanding shares upon completion.

*Returns less than one year are not annualized. **The performance data quoted represents past performance. Past performance does not guarantee future results. Investment returns and principal value will fluctuate and shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the data quoted. Returns include reinvestment of dividends and capital gains. To obtain the most recent month-end performance data available, please visit bairdfunds.com.**

All told, our direct and indirect software holdings explain almost three-quarters of the portfolio's underperformance in Q1 despite representing less than one-quarter of our invested capital. Regardless of what we say or how we try to explain it, owning practically anything remotely related to software has proven to be costly thus far in 2026. Moving forward, while we maintain conviction in key positions like NCR Voyix and BILL Holdings, we are not pressing the issue by proverbially "doubling down" given that the sector is currently viewed by many investors as uninvestible due to the threat of AI.

Our top winners during the period were Mister Car Wash (MCW), Oceaneering International (OII), Madison Square Garden Sports (MSGS), and RBC Bearings Incorporated (RBC). After several years of languishing in the public markets, Mister Car Wash advanced when it received a take-private bid in February. Oceaneering benefited from good results – and, of course, being in the "right neighborhood" of energy. Madison Square Garden Sports rose on hopes that the company might spin off its holdings in the New York Knicks, possibly a preliminary step to selling a valuable stake in the franchise which could help close the gap between the stock's current market value and the value of its collection of professional sports franchises. Industrial name RBC Bearings continues to report strong fundamentals, while investor appetite for the sector has pushed its valuation higher.

The past twelve or so months have proven challenging for the portfolio. Our investment team and process remain unchanged. What has changed is the combination of 2025's tariff escalation, 2026's war in Iran, and the light speed advances in AI, which together have ratcheted up the difficulty for traditional bottom-up investors like us. Tariffs and war abruptly elevated economic uncertainty, leading to less overall macro-optimism and diminished excitement (e.g. valuation) for our holdings despite solid fundamental performance. At the same time, the AI infrastructure buildout has offered an escape valve of sorts to investors seeking confidence in a singular growth pillar. For those of us not willing to chase exuberant AI-related valuations, it has proved to be quite the perfect storm.

It may be that the environment remains constant - dominated by news of tariffs and war and whatever else might come, the markets obsessed with a narrow set of companies that trade on price momentum at high valuations with no contemplated fundamental hiccups along the way. It may turn out that the fundamentally sound, cash-generating companies in which we have invested simply see their valuations forever impaired until their terminal value is fully erased.

While plausible, this is not the scenario plan under which we are investing. It seems too easy. Often, such a path is the wrong one to take. In the late 1990's, internet stocks were easy to own. In the mid-2000's, China-leveraged commodity stocks were all the rage. In the early part of this decade – ironically – software-as-a-service (SaaS) names rocketed to new heights. The internet and China are indeed powerful today, but the journey has been volatile to reach this destination. It remains to be seen what the market holds for SaaS stocks now that AI tumult has disrupted its journey. And now AI itself has ascended to the mantle of being revered.

Our belief is that its journey may prove to be more circuitous than currently implied. Not because AI isn't amazing technology; but because the lessons of history tell us to be careful. Recent surveys show there is much consternation beneath the surface of AI's promise, including the fear over lost jobs, apprehension over rising electricity costs due to rising data center demand, and the ever-present "not in my backyard" chorus from those that do not want AI data centers near their homes. In fact, a March Quinnipiac poll found that 80% of those surveyed are concerned about AI, and over half believe AI will do more harm than good in their day-to-day lives. Additionally, AI's current insatiable thirst for components could soon disrupt entire industries' ability to get necessary parts, such as automobiles or consumer products, while sharply rising global energy prices and increasing supply chain constraints create new debottlenecking challenges. None of this will likely affect AI's destination – but it could erect speed bumps along the journey and create unforeseen volatility in AI-related shares and themes.

In 1962, President Kennedy gave a moving speech at Rice University to highlight the importance of investing in the US Space program. His quote that "we do not do these things because they are easy, but because they are hard" has always resonated with me. Over the past thirteen years, our team has often bemoaned taking the hard path of making outsized returns in small-cap idiosyncratic ideas. And while our recent results may call that very strategy into question, our long-term track record emboldens us to not choose the quick fix of chasing momentum at any price. Instead, conviction in our team, process, long-term horizon and most importantly, our portfolio, are unwavering. It might be the harder path forward, but we believe it to be the correct one.

We look forward to sharing another update in three months.

Respectfully,

Joe Milano

Baird Equity Opportunity Fund (Q1 2026)

PERFORMANCE

Periods Ending March 31, 2026	Total Return (%)		Average Annual Total Returns (%)					
	QTR	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception	Expense Ratios (Net/Gross)*
Equity Opportunity Fund Institutional Class (net)	-11.39	-11.39	2.35	5.46	4.44	6.40	7.07	1.25 / 1.73
Equity Opportunity Fund Investor Class (net)	-11.46	-11.46	2.15	5.26	4.24	6.16	6.82	1.50 / 1.98
Russell 2000 Index	0.89	0.89	25.72	13.05	3.77	9.88	9.85	

Inception Date: 5/01/2012. Returns less than one year are not annualized. ***The performance data quoted represents past performance. Past performance does not guarantee future results. Investment returns and principal value will fluctuate and shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the data quoted. Returns include reinvestment of dividends and capital gains. To obtain the most recent month-end performance data available, please visit bairdfunds.com.*** *The Net Expense Ratio is the Gross Expense Ratio minus any reimbursement from the advisor. The advisor has contractually agreed to waive its fees and/or reimburse expenses at least through April 30, 2026, to the extent necessary to ensure that the total operating expenses do not exceed 1.50% of the Investor Class's average daily net assets and 1.25% of the Institutional Class's average daily net assets. Investor class expense ratios include a 0.25% 12b-1 fee.

TOP 10 HOLDINGS (AS OF 12/31/2025)

Company	% of Fund
NCR Voyix Corporation (VYX)	7.2
BILL Holdings, Inc. (BILL)	6.3
Sportradar Group AG (SRAD)	5.9
Globalstar, Inc. (GSAT)	5.2
Norwegian Cruise Line Holdings Ltd. (NCLH)	4.5
Cadre Holdings, Inc. (CDRE)	4.3
ZoomInfo Technologies Inc (GTM)	4.2
Mister Car Wash, Inc (MCW)	4.1
RBC Bearings Inc (RBC)	4.0
NeoGenomics, Inc (NEO)	3.8
TOTAL	**49.5**

INVESTMENT TEAM

Investment Professional	Years of Experience	Team Since	Coverage Responsibility
Joe Milano, CFA Portfolio Manager	29	2013	Generalist
Chip Morris, CFA Analyst	38	2014	Technology
Scott Barry Analyst	28	2014	Consumer Discretionary & Consumer Staples
Ben Landy Analyst	16	2014	Industrials & Materials
Scott Mafale Analyst	9	2021	Healthcare

Investors should consider the investment objectives, risks, charges and expense of each fund carefully before investing. This and other information is found in the prospectus and summary prospectus. For a prospectus or summary prospectus, visit bairdfunds.com. Please read the prospectus or summary prospectus carefully before investing.

Prior to December 12, 2021, the Baird Equity Opportunity Fund was managed in accordance with a different investment strategy. Greenhouse Funds LLLP became the Fund's subadvisor effective December 12, 2021. The performance results shown are from periods during which the Fund was managed by the Advisor prior to the retention of Greenhouse Funds LLLP.

As a non-diversified fund, the Fund may invest a larger percentage of its assets in a smaller number of companies compared to a diversified fund, which increases risk and volatility because each investment has a greater effect on the overall performance. The Fund focuses on small- and mid-cap stocks and therefore the performance of the fund may be more volatile, less liquid and more likely to be adversely affected by poor economic or market conditions than investment in larger companies. The fund may invest up to 15% of its total assets in the equity securities of foreign companies. Foreign investments involve additional risks such as currency rate fluctuations, the potential for political and economic instability, and different and sometimes less strict financial reporting standards and regulations.

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The Russell 2000® Index is a capitalization-weighted index representing the smallest 2,000 companies in the Russell 3000 Index, ranked by total market capitalization. Indices are unmanaged and are not available for direct investment.

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