Baird Core Plus Bond Inst BCOIX

A compelling choice for the core plus bond investor.

Morningstar’s Take BCOIX

Morningstar Rating ★★★★

Morningstar Analyst Rating Silver

Morningstar Pillars
- Process: High
- Performance: Above Average
- People: Above Average
- Parent: —
- Price: —

Role In Portfolio Core

Fund Performance

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Return (%)</th>
<th>+/- Category</th>
</tr>
</thead>
<tbody>
<tr>
<td>YTD</td>
<td>0.04</td>
<td>1.14</td>
</tr>
<tr>
<td>2019</td>
<td>10.11</td>
<td>1.17</td>
</tr>
<tr>
<td>2018</td>
<td>-0.51</td>
<td>0.10</td>
</tr>
<tr>
<td>2017</td>
<td>4.65</td>
<td>0.38</td>
</tr>
<tr>
<td>2016</td>
<td>4.73</td>
<td>0.87</td>
</tr>
</tbody>
</table>

Data through 3-31-20

4-01-20 | by Gabriel Denis

The stalwart team helming Baird Core Plus Bond adheres to a disciplined process and benefits from low fees. Our conviction in this strategy’s team and process is unchanged, but under our new ratings methodology both share classes are downgraded to Morningstar Analyst Ratings of Silver from Gold given the presence of other highly rated competitors in the intermediate core-plus bond Morningstar Category (its home following the split of its prior intermediate-term bond category in May 2019).

Lead manager Mary Ellen Stanek heads a well-talented, nine-person portfolio management team composed of five strategic leaders and four midlevel directors, many who have worked in concert since the strategy’s September 2000 inception. An additional strategic leader and 10 dedicated analysts lend further support. While this configuration is not as complex as some of the firm’s largest competitors, the group is deeply collaborative and sticks to investments it can research thoroughly and confidently.

Stanek and her team use a tried-and-true valuation-driven process to outpace the Bloomberg Barclays U.S. Universal Index. A mixture of investment-grade corporate, securitized, and government bonds form the core of the portfolio, and as of December 2019, complemented by a smattering of high-yield (3% to 12% over the preceding decade) and dollar-denominated emerging-markets corporates (less than 3%). When the team ventures into below-investment-grade fare, it prefers to hold a diversified set of well-trafficked names, and it matches the fund’s duration to that of the index; sets strict limits on position sizing; and avoids derivatives, leverage, and nondollar bonds. These constraints allow management to focus on its strengths: security selection and sector rotation.

The strategy’s low fees and risk controls generated a compelling track record from its October 2000 inception through January 2020, a period over which it outpaced both its Bloomberg U.S. Universal index and 85% of distinct peers. Its risk-adjusted return (measured by Sharpe ratio) landed in the top decile of its cohort.

Process Pillar ★ High | Gabriel Denis 02/19/2020
Mary Ellen Stanek and crew have maintained the same transparent, risk-aware combination of security selection and sector rotation to outrun their Bloomberg Barclays U.S. Universal Index benchmark for just shy of two decades. Their thoughtful and straightforward approach earns a High Process Pillar rating.

The strategy has access to the same sectors as its index, a mix of corporate, securitized, and government bonds. Yet unlike many rivals in the intermediate core plus bond category, it treads lightly in lower-quality bonds and forgoes leverage, derivatives, and non-dollar-denominated debt. Instead, the team hunts for investments that it believes offer strong fundamental features, attractive relative value, and fit within its broader macroeconomic views. They keep the strategy’s duration neutral to that of the index to limit rate-driven volatility and facilitate the best expression of its credit opinions.

The team’s size and resources look trim compared with some rivals, but this group limits its pickings to sectors and bonds within its wheelhouse. To date, the managers have avoided subordinated mortgage- and asset-backed fare, emerging-markets sovereigns, and non-dollar-denominated bonds across their portfolios. Design features such as diversification guidelines and rules on position-sizing function as additional risk controls.

A persistent overweighting to corporate bonds, typically occupying half of the portfolio over the trailing 10 years ending December 2019, distinguishes the fund from its benchmark. At the end of 2019, the fund’s corporate credit stake stood at 49%, dominated by financials (19%) and industrials (27%). Though the former decreased as a portion of the portfolio from its 22% the year prior, the team continued to cite strong fundamentals among banks and life insurance companies as supporting an overweight compared to it Bloomberg Barclays U.S. Universal Index.

While investment-grade credit forms the core of the portfolio, it may also hold up to 25% in below-investment-grade debt. The portfolio has not come close to breaching that limit, and has averaged around 8% over the preceding decade, with that exposure dipping to 3%, its lowest level over that time frame, by year-end 2019. That shift was underpinned by the team’s observation of increasingly tight spreads in the high-yield corporate sector, and a significant portion of those credit-quality holdings are nonagency mortgages.
The strategy maintained a modest allocation to dollar-denominated emerging-markets bonds (2.5%) at the end of 2019. The team continued to prefer large, multinational corporate names to sovereigns, with the largest stakes in Mexico (0.7%), China (0.5%), and Brazil (0.4%).

Performance Pillar | Gabriel Denis 02/19/2020
Over the core team’s tenure from October 2000 through January 2020, its 5.9% annualized return landed in the best quintile of distinct rivals in the intermediate core plus bond category and nearly 70 basis points ahead of its Bloomberg Barclays U.S. Universal Index. Its risk-adjusted return, as measured by the Sharpe ratio, lands in the top quintile of that same cohort. Shorter trailing periods, such as the three- or five-year marks, exhibit similar results.

Relative to its Bloomberg Barclays U.S. Universal bogy, the strategy’s overweighting in corporate bonds has contributed to outperformance during credit rallies and generated minor but surmountable trouble during credit sell-offs. Yet the team’s judicious attention to valuations and risk-mindedness have helped it surpass less cautious rivals over the long haul. During the most painful period of 2008 (September through November), the strategy’s 4% tumble lagged its index but outperformed nearly 70% of its rivals. In more recent stress periods, including the commodity-related sell-off from June 2015 through February 2016, this offering trailed its more conservative index but comfortably outpaced its typical, more flexible, distinct category peer. During the 2018 fourth quarter broad market sell-off, the fund outperformed around 60% of its rivals.

People Pillar | Above Average | Gabriel Denis 02/19/2020
While lacking the expansive analyst benches of some of the larger players in the fixed-income space, this nimble team benefits from seasoned leadership and a tight-knit, collaborative investment culture. It earns an Above Average People Pillar rating.

Baird Advisors CIO Mary Ellen Stanek heads a well-tenured, nine-person portfolio management team, composed of five members of strategic leadership and four mid-level leaders. Six of these nine have been listed on the strategy since its September 2000 inception date, with a further three added over 2019. Ten analysts, focusing on credit, securitized, and portfolio-risk research, and an additional strategic leader complete the effort.

The team’s strengths lie in its experienced leadership bench, cohesive culture, and mindfulness about its limitations. This team does not pursue highly credit-sensitive or esoteric investments that would require resources beyond those that currently exist to support the strategies. Stanek has also been proactive in expanding both the team’s roster and resources. While many of the senior leaders on this bench are far along in their careers, the team doesn’t foresee immediate changes to its leadership ranks, and the naming of several mid-level leaders to the strategy suggests they are well positioned to take the reins in the future.

Price Pillar | Gabriel Denis 02/19/2020
It’s critical to evaluate expenses, as they come directly out of returns. The share class on this report levies a fee that ranks in its Morningstar category’s cheapest quintile. Based on our assessment of the fund’s People, Process and Parent pillars in the context of these fees, we think this share class will be able to deliver positive alpha relative to the category benchmark index, explaining its Morningstar Analyst Rating of Silver.
Important Disclosure Information

Performance data quoted represents past performance. Past performance does not guarantee future results. Investment return and principal value of an investment in the fund will fluctuate so that an investor's shares when redeemed may be worth more or less than their original cost. The fund’s current performance may be lower or higher than the performance data quoted. For performance current to the most recent month-end, please visit bairdfunds.com. Carefully consider a fund’s investment objectives, risks, charges, and expenses before investing. For a current prospectus and summary prospectus, containing this and other information, visit bairdfunds.com. Read it carefully before investing.

The Morningstar Analyst Rating™ is not a credit or risk rating. It is a subjective evaluation performed by Morningstar’s manager research group, which consists of various Morningstar, Inc. subsidiaries (“Manager Research Group”). In the United States, that subsidiary is Morningstar Research Services LLC, which is registered with and governed by the U.S. Securities and Exchange Commission. The Manager Research Group evaluates funds based on five key pillars, which are process, performance, people, parent, and price. The Manager Research Group uses this five-pillar evaluation to determine how they believe funds are likely to perform relative to a benchmark over the long term on a risk adjusted basis. They consider quantitative and qualitative factors in their research. For actively managed strategies, people and process each receive a 45% weighting in their analysis, while parent receives a 10% weighting. For passive strategies, process receives an 80% weighting, while people and parent each receive a 10% weighting. For both active and passive strategies, performance has no explicit weight as it is incorporated into the analysis of people and process; price at the share-class level (where applicable) is directly subtracted from an expected gross alpha estimate derived from the analysis of the other pillars. The impact of the weighted pillar scores for people, process and parent on the final Analyst Rating is further modified by a measure of the dispersion of historical alphas among relevant peers. For certain peer groups where standard benchmarking is not applicable, primarily peer groups of funds using alternative investment strategies, the modification by alpha dispersion is not used.

The Analyst Rating scale is Gold, Silver, Bronze, Neutral, and Negative. For active funds, a Morningstar Analyst Rating of Gold, Silver, or Bronze reflects the Manager Research Group’s expectation that an active fund will be able to deliver positive alpha net of fees relative to the standard benchmark index assigned to the Morningstar category. The level of the rating relates to the level of expected positive net alpha relative to Morningstar category peers for active funds. For passive funds, a Morningstar Analyst Rating of Gold, Silver, or Bronze reflects the Manager Research Group’s expectation that a fund will be able to deliver a higher alpha net of fees than the lesser of the relevant Morningstar category median or 0. The level of the rating relates to the level of expected net alpha relative to Morningstar category peers for passive funds.

For certain peer groups where standard benchmarking is not applicable, primarily peer groups of funds using alternative investment strategies, a Morningstar Analyst Rating of Gold, Silver, or Bronze reflects the Manager Research Group’s expectation that a fund will deliver a weighted pillar score above a predetermined threshold within its peer group. Analyst Ratings ultimately reflect the Manager Research Group’s overall assessment, are overseen by an Analyst Rating Committee, and are continuously monitored and reevaluated at least every 14 months.

For more detailed information about Morningstar’s Analyst Rating, including its methodology, please go to https://shareholders.morningstar.com/investor-relations/governance/Compliance--Disclosure/default.aspx.

The Morningstar Analyst Rating (i) should not be used as the sole basis in evaluating a fund, (ii) involves unknown risks and uncertainties which may cause the Manager Research Group’s expectations not to occur or to differ significantly from what they expected, and (iii) should not be considered an offer or solicitation to buy or sell the fund.

The Morningstar four-star rating for the Institutional Class Baird Core Plus Bond Fund is the overall rating received among 530 Intermediate Core-Plus Bond Funds. The fund received four stars for the three-year period among 530 Intermediate Core-Plus Bond Funds, four stars for the five-year period among 442 Intermediate Core-Plus Bond Funds and four stars for the ten-year period among 331 Intermediate Core-Plus Bond Funds, as of March 31, 2020.

The Morningstar Rating™ for funds, or “star rating”, is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The Morningstar Rating does not include any adjustment for sales loads. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star.

The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics. The weights are: 100% three-year rating for 36-59 months of total returns, 60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10-year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods.

The average annual total returns for the Institutional Class of the Baird Core Plus Bond Fund as of March 31, 2020, are 6.23% for the one-year, 3.39% for the five-year and 4.60% for the ten-year periods and 5.73% since its September 29, 2000, inception date. The expense ratio of the Institutional Class is 0.30%.
The average annual total returns for the Barclays US Universal Bond Index as of March 31, 2020, are 7.15% for the one-year, 3.35% for the five-year and 4.05% for the ten-year periods and 5.12% since the fund’s inception.

The Barclays U.S. Universal Bond Index represents the union of the U.S. Aggregate Index, U.S. Corporate High Yield Index, Investment Grade 144A Index, Eurodollar Index, U.S. Emerging Markets Index, and the non-ERISA eligible portion of the CMBS Index. The index covers USD-denominated, taxable bonds that are rated either investment grade or high-yield. Some U.S. Universal Index constituents may be eligible for one or more of its contributing subcomponents that are not mutually exclusive. The index is unmanaged and is not available for direct investment.

The Fund may invest in mortgage- and asset-backed securities which may be subject to prepayment risk and thus may be more sensitive to interest rate changes than other types of debt securities. The Fund may also invest in U.S. dollar-denominated securities issued by foreign issuers which involve additional risks including political and economic instability, differences in financial reporting standards and less regulated securities markets. Non-investment grade bonds involve greater risk of default and bankruptcy than investment grade securities. While the U.S. government has historically provided financial support to various U.S. government-sponsored agencies, no assurance can be given that it will do so in the future if it is not obligated by law. A bond’s market value may be affected by changes in interest rates – generally, when interest rates rise, the bond’s market value declines and when interest rates decline, its market value rises (“interest-rate risk”). Duration risk is the risk associated with the sensitivity of a bond’s price to a one percent change in interest rates. 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.

This reprint must be accompanied with performance data current through the most recent quarter. For Morningstar ratings data and Fund holdings current through the most recent month-end, as well as credit quality profile current through the most recent quarter-end, please visit www.bairdfunds.com.

© 2020 Morningstar, Inc. All Rights Reserved. The information contained herein: (1) is proprietary to Morningstar; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information. Past performance is no guarantee of future results.