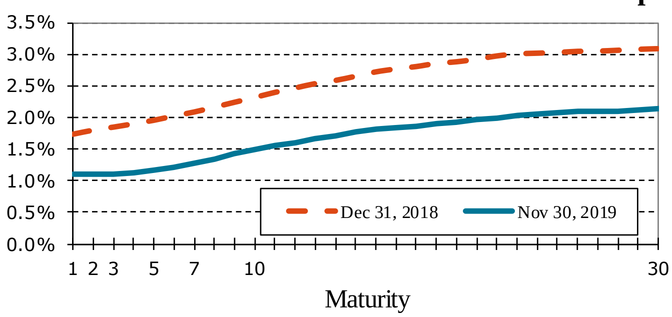
Baird Advisors
Municipal Fixed Income Market Commentary
November 2019

Taxable Issuance Rises Amid Record YTD Fund Inflows

The tax-free curve steepened modestly last month as short-term tax-free rates fell and intermediate-term and longer rates held steady. The bigger story in November was the heavy new issue calendar as supply rose 54% over the same month last year, pushing YTD supply to $378B, 18% ahead of last year's pace. An important part of the rising supply last month was in the taxable municipal sector which comprised 25% of November's total volume. The recent surge in taxable issuance is driven largely by the desire to advance refund outstanding tax-free debt. The low rate environment makes the cost savings possible when outstanding tax-free bonds are refinanced with taxable debt. For many municipalities, taxable debt also offers greater flexibility in how the bond proceeds are used, helping to avoid the stringent IRS restrictions that come with a tax-free borrowing. Demand for all municipal issuance, both taxable and tax-free, remained robust last month. The abundant taxable municipal issuance in recent weeks has led to wider credit spreads on taxable municipals relative to taxable corporates, attracting demand from buyers of more traditional taxable sectors. Also, the late-cycle benefit of an up-in-quality trade into taxable municipals is another reason buyers are readily absorbing the elevated supply. At the same time, demand for tax-free bonds has been consistent and impressive all year and positive flows into tax-free funds continued in November. Total flows into tax-free funds YTD have already set a new annual record of $84B with December flows still ahead.

AAA Municipal Yields



Maturity	12/31/18	10/31/19	11/30/19	1Mo Chg	YTD
1	1.74%	1.13%	1.10%	-0.03%	-0.64%
2	1.80%	1.14%	1.10%	-0.04%	-0.70%
3	1.85%	1.15%	1.11%	-0.04%	-0.74%
5	1.96%	1.19%	1.17%	-0.02%	-0.79%
7	2.09%	1.28%	1.28%	0.00%	-0.81%
10	2.32%	1.48%	1.50%	0.02%	-0.82%
30	3.09%	2.14%	2.13%	-0.01%	-0.96%

Rating Upgrades Exceed Downgrades, States' Spending on the Rise

Moody's reported last month that ratings upgrades exceeded downgrades in the third quarter, bringing the streak to nine consecutive quarters of improvement. In the June through September period, there were 148 Moody's upgrades compared to 78 downgrades and total upgrade volume of $29.1B exceeded the $14.1B of downgraded debt. The Moody's data highlights the solid fundamental credit backdrop in the municipal market currently. Municipalities have benefited from over ten years of steady economic growth and rising tax revenues. States have capitalized on this opportunity to rebuild reserves, with the median state rainy day fund balance rising to 7.5% of general fund spending in FY19 from a low of 1.6% in FY10. Not all the money has been saved, however, as state spending has also been rising. According to the National Association of State Budget Officers, state spending rose 5.8% in fiscal year 2019, the fastest pace since fiscal 2007. Included in this was a 4.2% boost in transportation spending, helped by an increase in gasoline tax rates across several states. Spending on K-12 education, the largest single state expenditure, also rose at a 4.7% clip last fiscal year, beating the 4.1% increase in FY18. Fortunately, the federal government has provided additional funding for states as well. In FY19 federal funding for the states rose 4.7%, faster than the 3.5% or 2.5% federal spending increases in either FY18 or FY17, respectively. The rising federal and state spending will provide support for an extension of the U.S. economic expansion in 2020.

Modestly Positive Returns in November

Although returns were modest in November, they were positive across all segments of the curve and all market sectors. "Risk-on" investors continued to benefit as long maturities marginally outperformed shorter segments of the curve while BBB and High Yield municipal credits outperformed higher quality issues in the month.

Total Returns of Selected Bloomberg Barclays Municipal Indices and Subsectors

Bloomberg Barclays Index/Sector	November	YTD	Bloomberg Barclays Quality	November	YTD
Municipal Bond Index	0.25%	7.21%	AAA	0.26%	6.46%
General Obligation bonds	0.26%	6.95%	AA	0.23%	6.82%
Revenue bonds	0.25%	7.60%	A	0.24%	7.76%
Prerefunded bonds	0.20%	3.40%	BBB	0.41%	9.40%
Long maturities (22+ yrs.)	0.30%	9.98%	High Yield	0.39%	10.35%
Intermediate maturities (1 - 17 yrs.)	0.23%	6.10%	HY, ex-Puerto Rico	0.38%	9.43%
Short maturities (1 - 5 yrs.)	0.22%	3.45%			

Disclosures

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.

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.

Indices are unmanaged, and are not available for direct investment. *Past performance is not a guarantee of future results.*

The Bloomberg Barclays 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 Barclays Municipal Bond Index and do not represent separate indices.

The Bloomberg Barclays 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 Barclays Municipal Bond Index or Bloomberg Barclays 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.