Aquila Tax-Free Trust of Oregon

PODCAST TRANSCRIPT

April 2024

Interviewer:

Hello everyone. Thank you for joining us for another installment of the Aquila Group of Funds podcasts. I'm your host, Matthew DiMaggio. Today we are accompanied by Tim Iltz, Portfolio Manager of Aquila Tax-Free Trust of Oregon. Thank you for being here today.

Tim Iltz:

Matt, thank you for checking in.

Interviewer:

Absolutely. And so, we're going to jump right in on a big topic in all of fixed income, which of course is the Federal Reserve (the "Fed") and their decision-making process at the moment. Earlier this year, they decided to sit tight on short-term rates. Seems like the sentiment might be the same here in March. What are you thinking and how is it affecting how you manage the portfolio?

Tim Iltz:

Ahead of next week's Federal Open Market Committee meeting (March 19-20), this week's inflation releases create a bit of a stir. Headline Producer Price Index ("PPI") ended up higher than expected of 0.44% month-over-month, 3.2% year-over-year as a result of an upside surprise from the Core Goods category. Services inflation actually moderated. Headline PPI was also up 0.6% month-over-month and 1.6% year-over-year. Although inflation growth is slowing overall, the labor market remains remarkably tight. With the Fed's continued emphasis on bringing inflation to a sustainable 2%, we think rates will remain higher for longer. And so as a result, we're taking advantage of some of the steepest yield curve right now and going out a little bit longer than we have in the past.

Interviewer:

Great answer, Tim. I want to touch on Municipal-to-Treasury ratios, which, of course, is a great gauge for the municipal bond market. The ratios themselves have been below average for some time now. It seems the only part of the curve would be the long end that's comparable to historical averages. So, what's your take on that and what's going to have to happen to see a big change here?

Tim Iltz:

Although Municipal-to-Treasury ratios are historically rich right now, or they are rich relative to historical values, this is because demand far outstrips supply right now. We've recently seen new issues oversubscribed by over 20 times. Even on the long end, ratios are quite rich versus historical standards, although they are more reasonable as you go out further on the yield curve. We would need to see a substantial increase in issuance for ratios to improve, and even then, with the level of cash holdings around a record level of $6.5 trillion in U.S. money market funds, it's going to take a significant improvement in issuance in order for us to see any type of a change in ratios at this level.

Interviewer:

Great take on the situation, Tim.

It's been my observation that since the bottom of the market a few years ago, we haven't really seen a confident municipal market. Would you say you agree with that?

Tim Iltz:

I respectfully disagree. We've seen rates rally 100, 110 basis points based upon wherever you are on the yield curve from late October, early November. And we're also seeing credit spreads tightening, so significant rallying rates, credit spreads tightening. Furthermore, demand continues to be hyped from municipal bonds and as you pointed out, we're seeing close to the richest U.S. Treasury ratios that we've seen in the past three years.

Interviewer:

Objection gladly accepted. Thank you, Tim.

I want to go into supply. You mentioned demand a little bit and our situation with issuance. The year so far seems to have shown elevated supply year-over-year on a national level, but what's it really going to take for it to pop here? And secondarily, you mentioned demand. Will there be the demand to support additional supply when it comes?

Tim Iltz:

We expect to see issuance increase as municipalities and school districts exhaust their federal stimulus funds. However, we have noted in our credit research that many local governments have been more conservative with their issuance of new debt in recent years with the looming recession. Local governments are planning for some type of economic event and that they're managing their cash very carefully and their debt portfolios also.

Interviewer:

So, since we touched supply on a national level, let's drill down more to the State. When the numbers are quoted, they're typically quoted on the national level, but we know that doesn't trickle down evenly to each state. So how is the Oregon looking for supply?

Tim Iltz:

Oregon issuance is down about 97% through the end of February versus last year for the first two months. We've just seen two small issues during the first two months of the year. The State of Oregon currently has a $578 million general obligation issue planned for April, but currently issuance is very low in Oregon.

Interviewer:

And beyond supply, is there anything else happening on the state or local landscape that would be of interest to investors?

Tim Iltz:

Yes, Matt. The Interstate 5 Bridge replacement project. It's been awarded a $600 million grant through the United States Department of Transportation's mega program funding. The total project's currently estimated to cost around $6 billion. The State of Oregon and the State of Washington have collectively applied for an additional $2.6 billion from the U.S. Department of Transportation, and each state has placed an additional billion dollars as their share of the project. Currently, the State of Oregon is planning to issue $250 million in bonds over each of the next four two-year budget cycles, as Oregon's down payment on the portion of the project. And then an additional $750 million may end up coming from other sources, with the State planning a major transportation funding package for 2025. Right now, construction is expected to start in 2026, and light rail and express bus service plan is a part of the new bridge.

Interviewer:

That's fantastic. And so, I want to close here by speaking about Aquila Tax-Free Trust of Oregon, how you're currently positioning the Fund, and how you're managing in this environment.

Tim Iltz:

We continue to stick to our tenets of high-quality, intermediate maturity, broad portfolio diversification and local expertise. Our portfolio positioning is shorter duration, higher credit quality, and higher average coupons, which has been relatively advantageous during the current dynamic market conditions with volatile daily changes. Our duration has extended a bit as we take advantage of the higher rates, but we still remain within our guidelines. Given the current shape of the yield curve and recent tightening of credit spreads, we remain cautious in our selection of bonds. Under our overall defensive portfolio strategy, the Fund holds approximately 91% AA or higher credit quality bonds. And credit research remains the cornerstone of our strategy with vigilant monitoring of both issuers and sectors. If a new issue does not pass our credit criteria, discussion stops there.

Interviewer:

And of course, we appreciate all the hard work you and the team do.

That sums up our podcast for today. Thank you everyone for listening. And as always, thanks again for joining us, Tim.

Tim Iltz:

Thank you, Matt.

Thank you for listening to this podcast. . The opinions shared are those of the portfolio manager and do not necessarily reflect those of the Investment Adviser of the Fund.

The Fund seeks to provide a high level of income exempt from state and federal income tax, as is consistent with capital preservation. Past performance does not guarantee future results.

For certain investors, some dividends may be subject to federal and state income taxes, including the alternative minimum tax referred to as AMT. Please consult your tax professional.

Independent rating services such as Standard & Poor's, Moody's, and Fitch assign ratings, which generally range from AAA, highest, to D, lowest, to indicate the credit worthiness of underlying bonds in the portfolio. Where the independent rating services differ in the rating assigned to an issue or do not provide a rating for an issue, the highest available rating is used in calculating allocations by rating. Pre-refunded or escrowed bonds are issued to retire or regain an outstanding bond issue at a specific call date. Until the call date, the proceeds of the bond issuance are typically placed in a trust and invested in U.S. Treasury bonds or state and local government securities.

Modified and effective duration both measure the value of a security in response to a change in interest rates. Effective duration also takes into account the effect of embedded options. The weighted average life, also referred to as weighted average maturity, is a reflection of the quickness with which the principal of an issue is expected to be paid.

A credit spread is a difference in yield between two bonds of similar maturity but different credit quality.

Yield refers to the earnings generated and realized on an investment over a specific period. Yield is expressed as a percentage based on the invested amount, current market value, or face value of the security, and includes the interest earned or dividends received from holding a particular security.

The yield ratio represents the comparison of the expected yield of one bond to the expected yield of another. A yield ratio is important when deciding whether to invest in one bond or another. Generally, the higher yield is considered better.

Mutual fund investing involves risk; loss of principal is possible. Investments in bonds may decline in value due to rising interest rates, a real or perceived decline in credit quality of the issuer, borrower, counterparty or collateral, adverse tax or legislative changes, court decisions, market or economic conditions. Fund performance could be more volatile than that of the funds with greater geographic diversification.

Before investing in the Fund, carefully read about and consider the investment objectives, risks, charges, expenses, and other information found in the Fund's prospectus. The prospectus is available from your financial advisor, when you visit www.aquilafunds.com, or call (800) 437-1020.