Aquila Tax-Free Fund For Utah
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Interviewer:
Today we're talking to JT Thompson, portfolio manager of Aquila Tax-Free Fund for Utah. Tax reform legislation, The Tax Cuts and Jobs Act, was signed in December of 2017. What are the most significant impacts of that legislation on the municipal bond market?

JT Thompson:
I think the most significant effect on the municipal bond market is the ending of advance refundings. That has taken between 20 and 40 percent of the market away. Also, the lowering of the corporate income tax. After you looked at credit quality and everything, some corporations may be a little reluctant to buy tax-exempt bonds because they don't get the tax benefit that they did at the higher tax rate.

Interviewer:
Looking at the markets from a national perspective, what are your expectations regarding investor demand for municipal bonds and the supply of bonds available to meet that demand; and are there factors in Utah that impact local supply and demand expectations?

JT Thompson:
Because of the reduction in advance refundings, the supply nationality is going to be reduced by 20 to 40 percent, but the demand is staying strong. We're seeing demand from Europe and Japan continuing in the municipal market, because the total returns on the high-quality credits of the municipal market exceed those of high-quality corporates.

The state of Utah is kind of bucking the trend. We've had an enormous amount of issuance the first couple of months of 2018, and part of that is from – when the law was passed in December, there were a lot of issuers that really wanted to refinance their debt but were not able to because they couldn't meet all the legal obligations to do a market issuance. So, they went to banks and asked if the banks would buy those, and banks bought those bonds with the understanding that, as soon as there was a market deal available, the bonds would be currently refunded.

A good example is Utah Transit Authority. They had a refinancing. They didn't have time to have all the disclosures, so they placed over $100 million with a bank, and just yesterday, they came to the market, refunding the December, 2017 private placement. Therefore Utah – we've had enormous amount of supply as issuers have taken advantage of banks being able to help them out on refinancing their debt.

Interviewer:
After nearly a decade of a very low Federal Funds rate, the Fed has introduced several rate increases. How would you summarize the market activity you've seen related to changes in the yield curve and credit spreads?

JT Thompson:
We've seen a flatter yield curve, but because of demand in the municipal market, we're still very tight on spreads for the lower-quality credits. Until interest rates really spike higher, we're probably in this range for this short time. I expect the high yield (issues) to probably get hit the worst as credit spreads start to widen.

Interviewer:
Given the high quality intermediate maturity profile of the fund, how are you strategically navigating this market?

JT Thompson:
Taking advantage of the flat yield curve and lowering our average life. As the yields in the short end rose higher than the long end, I started buying more in the shorter end, taking advantage of those higher rates than previously were available, and able to reduce our average life by nearly 2 years.

Interviewer:
Speaking of navigation, how is Utah doing in terms of managing public employee pension funding?

JT Thompson:
Way back before the crisis, Utah, because legally they have to have a balanced budget, they decided to go away from the traditional pension; and to all new employees, I believe after 2006, the state employees receive 10 percent of their salary in a 401(k) type of pension. Prior employees are still under the pension, but Utah is one of the states that has nearly a fully-funded pension. So it hasn't been a problem, and going forward, all new employees and all new issuers – they know how much to put in their budget to compensate for pension plans.

Interviewer:
The President introduced his $1.5 trillion infrastructure initiative on February 12th. How might the plan impact the municipal bond market?

JT Thompson:
It's going to be a year or so. They really are trying to work out a public / private type of working relationship, and I think it's going to be very difficult to figure out how those are going to work and how those structures are going to work in the municipal market. So as far as shovel-ready jobs, I don't think you're going to see that. The only thing you would see, maybe, is increased issuance on certain facilities that already have municipal debt against, and the municipality will issue debt without the private participation.

Interviewer:
Thank you very much. For those of you listening, before investing in the Fund, carefully read about and consider the investment objectives, risks, charges, expenses, and other information found in the Fund prospectus, which is available on this site, from your financial advisor, and when you call 800-437-1020.

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