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Tax-Free Fund of Colorado

# Aquila Tax-Free Fund of Colorado Podcast Transcript November 2, 2016

**Moderator:**
Today we're talking to Chris Johns, Portfolio Manager of Aquila Tax Free Fund of Colorado. Chris, through September 30th of this year municipal bond mutual fund inflows totaled $3 billion for the month and $50 billion year to date. It's been reported that foreign buyers and banks are among crossover buyers entering the market, although they have no tax advantage. Do you expect that crossover buyers will remain a factor in the municipal market in your term?

**Chris Johns:**
Yes, we think crossover buyers will be in the market for a while, but their stay is usually temporary. Typically, when we get new entrants into the municipal bond markets that aren't normal participants they enter the market opportunistically but they won't stay for a long period of time. As soon as the relationship between taxable yields and tax free yields kind of normalizes those types of investors will leave the market very quickly.

So those of us longtime participants in the muni market may like it for a while because of the increased liquidity from the new participants. They don't stay around for long, and when they leave they usually leave in a hurry.

**Moderator:**
And how has new issuance in Colorado compared this year to new issuance nationally?

**Chris Johns:**
Colorado has done pretty well this year. We have municipal bond issuance is up about 28 percent through September with a total of about $5.5 billion issued. Nationally it's been a very strong year, approaching a record year by the end of the year, so we've kind of tracked along with that.

The big news in Colorado is going to be that we are on pace to do much more than that next year. Right now, on the November ballot we have over $4.5 billion in school bonds alone on the ballot for November, and if a percentage or more than half of them pass that will set a new record for school bonds in any given year, so our supply may increase sharply later this year and early into the next year.

**Moderator:**
As of September 30th a little more than 20 percent of the portfolio was invested in pre refunded bonds, would you explain the pre refunded designation and why those bonds are such a significant portion of the fund holdings?

**Chris Johns:**
That's a real good question. It's a real important part of our portfolio right now. What a pre refunded bond is, is very similar to the concept of you and I refinancing our house when rates decline. Municipal bond issuers can refinance their older, higher interest rate debt, and when they do that they take the proceeds from the new bond issue and buy treasury and agency securities that will pay off the old bond issue, so that old bond issue then becomes backed by treasury and agency securities and it's exceptionally high quality and very liquid.

So we have such a large percentage of those in our portfolio because as interest rates have declined many of the issuers have refinanced their old bonds. Normally we would sell these bonds and try and reinvest in something with a higher yield, but all these bonds are maintaining their original yields that we bought them at a few years ago, which are much higher than are available in today's market.

So they're providing a great current yield, but probably more importantly what they provide is liquidity, so that if we get into a period of time where interest rates are rising or there's fear in the market, these pre refunded bonds provide a great source of liquidity that we can trade out of very quickly if we need to and very efficiently without having to worry about, you know, trying to find a good bid for the bond. So the high yield and the liquidity are great characteristics that the pre refunded bonds add to the portfolio.

**Moderator:**
How would you describe your overall strategy in the current market environment?

**Chris Johns:**
Well, I would say that right now we're fairly defensive, and what we mean by that is we've, over the last few years, allowed the portfolio to get shorter in maturity and duration, and as interest rates have declined another phenomenon that's occurred is that some of the lower quality bond yields have dropped much more so that at this point in time you're really aren't being paid to take the risk of lower quality bonds.

So we've got a little shorter in maturity, a little bit higher in quality and we're kind of prepared for a period of time where we want to be very careful with what happens in portfolios. So I guess the way we look at it right now is that we want to be flexible, we want to be liquid and we want to be able to take advantage of any opportunities that present themselves should interest rates start to rise a little bit. It seems likely that that could happen maybe even as soon as December of this year, and maybe a slightly upward bias at the entrance into 2017, so we just want to make sure that we're in a position to be able to do that, so we're very liquid and very high quality at the moment.

**Moderator:**
Are you continuing to see improvement in the Colorado economy?

**Chris Johns:**
Yeah; Colorado has been one of the strongest states in the US in the last several years. We've had a tremendous population growth. We've seen employment - or rather unemployment drop to below 4 percent; in September actually 3.6 percent. The Denver area had the lowest unemployment rate of any large US city in September.

And we've seen tremendous improvements in the real estate market, particularly in the Denver metropolitan area, so it's been a very strong economy here. We continue to see population growth; one of the fastest growing states out there so we think that will continue. We believe that the growth in real estate will start to level off because of affordability issues, but the continuing trend of in migration from the rest of the US and job growth; we see that continuing for the next couple of years.

**Moderator:**
Thank you, Chris. 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. Thank you for listening to this podcast.