Investment Commentary

September, 2018

AQUILA GROUP OF FUNDS

AQUILA® Tax-Free Trust of Oregon

A Shares: ORTFX **C Shares: ORTCX** **Y Shares: ORTYX**

Municipal Market

The trend of demand outpacing supply has continued to dominate the municipal market over the past quarter. Although the municipal yield curve initially flattened over much of 2017, recently the curve has made a parallel shift upward. This year the Federal Reserve has hiked rates three times, with another hike probable in December, which has contributed to a change in investor sentiment and ultimately the parallel shift upward of the muni yield curve. For most of the summer, yields struggled to move higher due to a restrictive supply as the result of overall reduced issuance and the ratio of bonds maturing exceeding the amount of bonds being issued. Through September, the yield curve mostly advanced by about 60 basis points for maturities longer than five years. Shorter maturities rose 40 to 50 basis points in yield. However, yields out past 20 years remain relatively flat with approximately 96% of the 30-year yield curve being captured by 20-year maturities, as investors stretch for longer maturities compromising duration to capture yield.

Credit risk is also being undervalued as investors stretch for yield. Recently we have seen a dramatic narrowing of credit spreads (particularly the difference in yield between BBB-rated bonds and AAA-rated bonds) to the point where we believe an investor is no longer appropriately compensated for lower-rated securities. Credit spreads have compressed by approximately 50% since the bond market's response to the 2016 presidential election, when credit spreads widened as investors expressed initial concern over the new administration and its potential impact. Recent AAA-BBB credit spreads have compressed as narrow as 55 bps, versus over 160 bps, less than two years ago. Over the past month, we have seen some widening in credit spreads due to supply improvements in September.

As with the national municipal bond market, issuance in the Oregon market is down from prior years. The year-to-date issuance of tax-exempt non-AMT bonds in Oregon was down by approximately 50% year-over-year through the end of September. Furthermore, due to maturities and calls, demand remains robust with new issues continuing to price aggressively. As a result, we have seen credit spreads narrow to the point that risk is almost not reflected in prices, particularly for investment grade bonds. Notable issues from the past quarter the Trust has participated in include: the $160 million Corvallis School District General Obligation Bonds, $383 million Salem-Keizer School District General Obligation Bonds and $25.7 million Nestucca Valley School District General Obligation Bonds.

In addition to a tight municipal bond market, Oregon also has tight labor market. Oregon's unemployment rate hit 3.8% in August, which is Oregon's lowest unemployment rate since comparable records began in 1976. In contrast, the job growth rate is actually slowing. The State of Oregon Employment Department recently reported that over the past 12 months, 42,000 jobs were added over the 12 month period through June, resulting in a growth rate of 2.2%. Job gains were materially faster in Oregon from 2013 through 2017, with average annual growth rate of 2.8%. The State has previously commented that growth is slowing as "many employers are facing increasing difficulty hiring workers" due to the tight labor market.

In the housing market, we are beginning to see some slowing in price growth as new supply enters the market and lending rates creep higher. According to data from the Regional Multiple Listing Service, real estate activity shows signs of slowing compared to 2017. Through August, new listings are up 2.9%, closed sales are down 2.0% and pending sales are down 2.1%. As a result, housing price growth in Portland slowed to 5.6% on a year-over-year basis in July, according to the S&P/CoreLogic Case-Shiller home price index, versus 6.0% nationally. Portland's below-average performance is a notable shift from just two years ago, when it led the major cities in home-price gains for almost a year. However, more sustainable growth may be more beneficial to the local economy in the long-run as affordability concerns persist.

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Fund Strategy

The portfolio characteristics of Aquila Tax-Free Trust of Oregon remained defensive over the past quarter with the weighted average maturity lengthening slightly to 7.14 years and modified duration at 4.2 years. Credit quality remained very high with over 88% of the portfolio rated AA or higher. Duration may edge slightly higher as securities mature in the portfolio and proceeds are reinvested in the 10-12 year range. The parallel shift in the yield curve over the past quarter has propped-up interest rates across the curve, creating a better entry point for longer intermediate maturities. We believe our defensive strategy will weather the rapidly changing interest rate environment well. While it is possible the Federal Reserve will raise short-term interest rates again in December, it should not be a major disruption, as evidenced by the market's response to the September rate hike, the third hike this year. We expect a slight upward bias in interest rates driven by Federal Reserve activities for the remainder of 2018. We will continue to closely monitor the shape of the yield curve and only extend when longer intermediate maturities provide greater value. This will allow us to take advantage of higher yields by replacing some securities that we purchased during the very low interest rate environment of the past three years.

The Trust currently benefits from legacy holdings purchased in higher interest rate environments that have been pre-refunded. These high-quality liquid securities provide an attractive current yield and low price volatility for our shareholders and provide the flexibility to reinvest in higher yielding bonds, should interest rates rise. We intend to continue our defensive investment strategy by striving to maintain an intermediate average portfolio maturity, emphasizing investment-grade credit quality and a balanced exposure to callable bonds. Furthermore, we will continue to perform in-depth credit research on all portfolio holdings, as we believe it is critical during the current rapidly changing economic environment.

For specific information about fund characteristics, holdings and performance, please see the Fund Fact Sheet on our website at www.aquilafunds.com.

Fund Facts

Portfolio Managers	Inception Date	Assets Under Management	Number of Holdings
Chris Johns Timothy Iltz	6/16/1986	$577.8M (as of 09/30/18)	258 (as of 09/30/18)

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