



Aquila Tax-Free Fund For Utah

Podcast Transcript

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Candace Roane:

Hello, everyone. Welcome to another Aquila Group of Funds podcast. I'm your host, Candace Roane. Joining me today is JT Thompson, Portfolio Manager of Aquila Tax-Free Fund for Utah. In this podcast we'll cover Utah's economy, the municipal market, the Biden administration spending plans, and interest rates. Welcome JT.

JT Thompson:

Welcome.

Candace Roane:

Let's start with an update on Utah's economy. How has revenue fared over the past year through the pandemic?

JT Thompson:

Well, very interesting. The Utah State Tax Commission issued a report recently and they took eight months pre pandemic from July 1st 2019 to March 1st of 2020, those tax receipts. And then they took from July 1st 2020, which is during the pandemic to March of 2021. And total receipts pre pandemic were over \$7.1 billion in those eight months. During the pandemic, the tax revenue was \$8.8 billion or an increase of almost one and a half billion or nearly 20%. So tax revenue from a tax revenue standpoint, actually the State of Utah did better than most states during the pandemic, actually was more revenue. They see that their budgets and I personally look at it as, as there's a lot of professional jobs, a lot of high tech jobs that probably weren't lost during the pandemic and that helped with the income tax area of the tax receipt. The snowfall this year, ski season, Utah relies heavily on tourism. Snowfall was average. I think ski days, there hasn't been one, but it'll probably come in at average or slightly below average. And the uptick were in state and national parks during the pandemic of a lot of people just wanted to get out of the house. And so, visiting the state and the national parks, we had heavy attendance at those parks. Housing prices have soared. It seems like everybody wants to buy a house now. The average price of a home in Utah is now \$405,000. Last March it was \$338,000. So, you can see the increase in housing prices and there is an awful lot of construction going around. Lumber prices have increased greatly and in some areas shortages of lumber. So all in all, I think Utah was able to come through the pandemic in good shape.

Candace Roane:

Good to hear the Beehive State is still faring very well as always. Looking back at the municipal market over the past year, where have you seen the most recovery, JT.

JT Thompson:

The most recovery. At the start of the pandemic, everybody wanted high quality municipal bonds. So anything AA or better everybody, they were buying that because they wanted safety. They were worried what's going to happen to tax receipts and everything. And, so they drove the prices of the AA and AAA bonds higher, which means lower and lower yields. But, as the dust started to settle and you know, some states were saying that their tax revenues weren't quite as dire. Then everybody, as we know, treasury rates were rock bottom and, so people started to look for yield and lower rated bonds. Over the last six, seven months have outperformed the highly rated bonds. People are reaching for any type of yield and ignoring the risks. So, that's the area of the market that is probably outperformed is the lower rated bonds. When you start looking at maybe some sectors higher-ed in Utah, steady enrollment was steady, even though there wasn't a lot of in-person classes. Utah Valley University actually had an increase in enrollment which is the largest university now in the system. The University of Utah, they all did well, steady, as far as enrollment goes. Transportation area in Utah is supported by sales tax. Mainly I think the high price for used cars. I think there's a little bit of nervousness still for people to get into mass transit and be in a car loaded with people and seem to be buying vehicles to get to work in Utah. A lot of businesses that have been local have started to have everybody come back into the office. So, we're seeing more and more people going to the offices. Another one: hospitals. There's only two hospitals in Utah that have issued municipal debt, the University of Utah Hospital, which is a teaching hospital, really the jewel of the medical field in Utah, and Intermountain Healthcare, which is an independent non for profit hospital. And, both have been doing fine. No, downgrades or on credit watch at all. Both of those are AA1, AA+ rated hospitals. And other than late summer, early fall, there was a spike in ICU units were filling up. Outside of that, the hospitals have not had a lot of pressure due to COVID.

Candace Roane:

Let's talk about stimulus. The Biden administration has proposed a significant amount of spending this year. We had the American Rescue Plan that was signed into law in March, making it the sixth policy response to COVID-19. Congress is currently weighing the American Jobs Plan and the American Family Plan. Another part of the Build Back Better Program is expected to be proposed very soon. How do you see all of this government spending coming together and impacting the municipal market across the nation and in Utah?

JT Thompson:

Well, it'll be interesting how the final versions come out. I feel the effect on the muni market, especially issuance will be minimal. The municipal markets and municipal bonds are issued to build hard assets, not fill budget gaps, which is a lot different than the federal government issuing treasuries to fill budget gaps, corporations, issuing debt to fill gaps, et cetera. Municipals, for the most part, securitize a revenue stream. So you're building schools, you're building hospitals, you're building court houses, you're building electric generation facilities, et cetera. Hard assets where people can see the flow of revenue to pay off those bonds. And, if you try to issue a municipal bond without a source of revenue that will secure those bond payments, usually it doesn't get done in the municipal market. That's what's unique about the municipal market than all other fixed income markets. So, I don't see any municipality issuing bonds to for a social program. That will be coming from federal, or state funded social programs, not for the municipality to issue debt to fund those programs. The closest thing that we have in the municipal market to issuing bonds for a social program is unfunded pension liabilities. They usually have to be taxable municipal bonds. And, you still have to show how the state revenue is going to pay off those pension bonds, or nobody will even buy the pension bonds. So in Utah, especially, I know that budgets, its amendments, constitutional amendments, you have to have a balanced budget and cities and the state have worked on balanced budgets. I don't see any real effect in the municipal market. With all of the spending packages there has to be a way, a vehicle, to pay for them and for the most part, it looks like increases in taxes, whether its capital gains or personal income or corporate income. Higher taxes are beneficial for the municipal market. Municipal bonds are a great vehicle for investors looking to have an investment that is free from federal and state income taxes.

Candace Roane:

I expect, if we see tax increases tied to some of the spending, we will definitely see an increase in desire for tax exempt investing. Let me get your thoughts on rates. Investors are certainly watching interest rates and thinking about inflation right now. Today is April 28th, and at the end of last week, the 10 year yield was around 1.5% falling almost 5% over the past month, but it was up 70% for the year. What are your expectations for the next several quarters around rates, inflation, Fed policy? And JT, how do you have the portfolio positioned at the moment?

JT Thompson:

Okay. The first quarter of 2021 was the worst quarter for the 10-year treasury since the 1980s. And we all know what rates were doing in the 1980s. What the difficulty have is price discovery is nearly impossible right now with all this stimulus, from the Fed and foreign central banks. It's very difficult to find out where rates should be. For example, you talked about the US. Treasury was at a 1.50. Well, in Portugal, their 10 year rate is about 44 basis points. In Greece, they're about 94 basis points for their 10 year. And what that tells us, is that the U.S. economy has a higher risk of default than Portugal or Greece. That's not a real fact. It's again, central banks and everybody pouring money into the fixed income market and driving rates lower than normal. So, it's hard to say where should the rates be in not only the United States, but worldwide. Should they be lower? Should they be higher? So that's the difficulty in managing a portfolio now with all of the stimulus, with the Fed and central banks in buying, to try to figure out exactly how to manage a portfolio in this time. What we have found is a high quality intermediate maturity fund mitigates a lot of the uncertainties existing in the markets. The Aquila Tax-Free Fund for Utah is positioned with nearly 82% of the Fund in AA rated or better municipal bonds or municipal bonds backed 100% by the U.S. Government. And the Fund has an average life of less than 10 years. So we believe that we will be able to mitigate a lot of the market uncertainties going forward by where we are positioned on the yield curve and high quality.

Candace Roane:

As always, thank you JT for joining me. Appreciate all of your insights. Thanks.

JT Thompson:

Thanks.

Disclosure:

Thank you for listening to this podcast. The opinions shared are those of the portfolio managers and do not necessarily reflect those of the Advisor or Subadvisor of the Fund.

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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 principle 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.

Taxable equivalent yield is the return that is required on a taxable investment to make it equal to the return on a tax-exempt investment.

For certain investors, net investment income tax, known as NIIT may apply. NIIT is a 3.8% tax established by the patient protection and affordable care act that applies to the lesser of, the net investment income, or a taxpayer's modified adjusted gross income above an applicable threshold amount.

The acronym PERS (P-E-R-S), stands for public employee retirement system. The acronym PERA, (P-E-R-A), stands for public employees' retirement association. CARES Act Stands for Coronavirus Aid, Relief, and Economic Security Act.

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.