North Sky
CAPITAL

First Quarter 2019

Quote of the Quarter
(Tax Day Approacheth):
"So far as we know, no pollster has asked the public, "Are you getting your money's worth for the more than 40 percent of your income being spent on your behalf by government?"

— Milton Friedman

Q1 2019 Market Commentary—March Gladness

Overview

- Impact investors are making strong returns and notable companies are being acquired or completing IPOs
- Opportunity zones offer attractive benefits
- Great start to 2019
- North Sky honored by ImpactAssets 50 selection

Strong Impact Exits and Financing Activity

Impact investors are making strong returns in today's marketplace. There has been a great awakening of exit activity lately across key impact sectors, boosting cash returns to investors. Strategic and financial acquirers have been the main source of liquidity, but impact companies are also tapping the public markets through IPOs. In addition to the robust exit activity shown in the chart below, impact companies are also attracting new investment capital to fuel their growth, with many financed by well-known investors (e.g., Amazon/Jeff Bezos) at increased valuations. Noteworthy examples include $1 billion raised by Lucid Motors (electric vehicles), $200 million raised by Plenty (indoor agriculture) and $110 million raised by Stem (energy storage).

Recent Exits

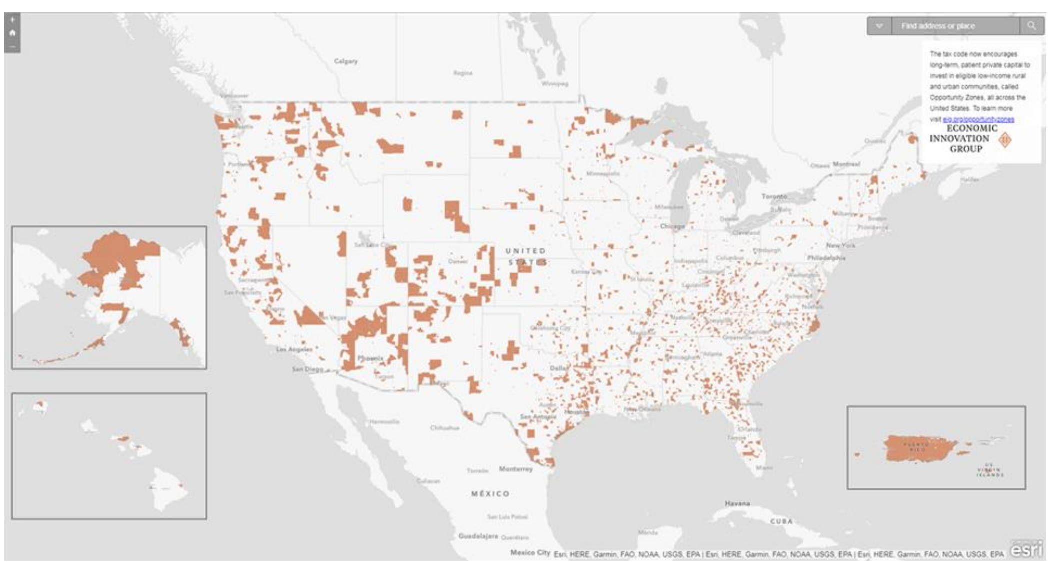
	Company	Acquirer	Deal Size	Company Description
Energy	Deepwater Wind	Orsted (CSE: ORSTED)	$510M	Offshore wind farms
	Click Energy*	Amaysim (ASX: AYS)	$120M	Energy retailer
	Sonnen	Shell (LON: RDSA)		Energy storage
Efficiency	WeissBeerger*	AB InBev (BRU: ABI)	$80M	Beverage waste analytics
	Living Earth*	Bain Capital		Recycling & composting services
	Tendril Networks*	Rubicon Technology Partners		Residential energy management
Food & Agriculture	Florida Food Products*	MidOcean Partners		Natural preservatives
	Agren	Land O' Lakes		Conservation planning software
	Bare Snacks*	Pepsico (NAS: PEP)	<$200M	Baked fruit and veggie snacks
	Good Karma Foods	Dean Foods (NYS: DF)		Flax-based health drinks
	Nature's Heart	Nestle (SWX: NESN)		Natural, organic plant-based foods
Transportation	Agility Fuel Solutions*	Hexagon (OSL: HEX)	$127M	Alternative fuel systems
	Chargemaster	BP (LON: BP)	$170M	Electric vehicle charging stations
	UQM Technologies	Danfoss	$100M	Electric motors for commercial vehicles
	Pure Biofuels*	Valero Energy (NYS: VLO)		Alternative fuel producer
	Nio (NYS: NIO)	N/A (IPO)	$1B	Electric vehicle manufacturer

Healthy Living	nVision Medical	Boston Scientific (NYS: BSX)	$275M	Ovarian cancer detection devices
	SlimFast*	Glanbia (DUB: GL9)	$350M	Clinically proven nutritional products
	Advance Medical	Teladoc (NYS: TDOC)	$352M	Telemedicine provider
	LivHome	Bain Capital		At-home care services
	Allakos (NAS: ALLK)*	N/A (IPO)	$128M	Antibodies for allergic diseases
Education	Sonans*	EMK Capital		College & career education services
	Cambium Learning Group	Veritas Capital	$900M	Research-based education services
	Pluralsight (NAS: PS)	N/A (IPO)	$310M	Cloud-based learning platform
Water	Valor Water Analytics	Xylem (NYS: XYL)		Water conservation for utilities
	FCX Performance	Applied Industrial Technologies (NYS: AIT)	$784M	Flow control and process automation
	EmNet	Xylem (NYS: XYL)		Real-time water monitoring systems
	Aquion	Pentair (NYS: PNR)	$160M	Water treatment equipment

Opportunities in OZ

Opportunity Zones ("OZs") are a hot topic today, and many of our investors have been asking us to form an OZ fund. We expect OZ funds formed this year and next will bring much needed capital to impoverished areas across America, spurring job creation and improving living conditions. Regulatory details are still being finalized but the following is an overview of the OZ program as it stands today.

OZs were created by the Tax Reform and Job Act of 2017 to incentivize long-term private investment in certain low-income communities. So far, 8,700 communities have been designated as OZs across all 50 States, the District of Columbia and five US territories. The areas shown in brown in the map below are all OZs. For an interactive map that you can use to find an OZ near you, click [here](#).



Source: Economic Innovation Group

The program allows private investors to defer and/or reduce their capital gains tax liability from realized investments by reinvesting any resultant taxable profits into an OZ fund within 180 days of realizing the gain. By doing so, the investor may defer its original tax liability until December 31, 2026 and reduce that liability by 10% by holding the OZ fund investment for at least five years, or by 15% by holding it for at least seven years. Furthermore, an investor that holds its OZ fund investment for at least ten years will eliminate capital gains on any capital appreciation resulting from the OZ fund investment. The following diagram is a helpful visualization of the benefits, mechanics and timeline (note, QOF is an abbreviation for qualified opportunity zone fund).

Source: KPMG (tax advisor to North Sky Capital)

To date, most OZ funds have focused on real estate projects that were already in progress. There are many reasons for why these early funds have been so narrowly focused, not least the fact that key aspects of the regulatory framework that would enable broader investment are still being formulated, but we believe the focus on real estate has skewed perceptions about the OZ investment opportunity. At North Sky, we focus on private equity and infrastructure investing, and we believe there are tremendous opportunities in OZs for both asset classes. In private equity, the capital expenditure guidelines are ideally suited for a venture capital or growth equity strategy, particularly for capital- and asset-intensive industries that have tended to struggle to attract earlier stage investors. In infrastructure, the legislation seems well suited for greenfield investments and even select brownfield investments, where significant capex is required to modernize or rehabilitate aging infrastructure. We see exciting opportunities within the following sectors that we already target for our Alliance infrastructure funds:

- Renewable power generation (wind, solar, hydro)
- Waste-to-energy/-value (landfill gas, biomass)
- Energy infrastructure (battery storage, EV charging stations)
- Energy efficiency (C-PACE, micro-grids)
- Water/waste treatment/management (municipal, industrial)

We have reviewed a large and growing number of qualified OZ opportunities over the last 4-6 quarters. As it turns out, through our second infrastructure fund (Alliance Fund II), we already have committed capital to five infrastructure projects that we later realized were in OZs. Given the non-taxable investor base of AF II (among other factors), AF II does not benefit from the OZ fund tax advantages. But the fact that we have already been making attractive investments that would otherwise fit the OZ fund template demonstrates that good returns can be made in OZs even before factoring in the tax benefits. If you would like more information about how opportunity zones work, please contact Andrew Harris at aharris@northskycapital.com.

Great Start to 2019

The new year is off to a great start. We continue to see superb investment opportunities within our impact secondaries strategy. Impact secondaries fall into two pools: a roughly $5B sized pool of pre-recession funds and a greater than $90B pool of post-recession funds. The latter pool is increasing due to growth in existing portfolios and as new funds are being formed, including some very large private equity funds in recent years. Both pools are diversified across energy, food, water, transportation, manufacturing and the built environment. The post-recession pool also adds sustainable consumer products, healthy living & aging, poverty alleviation and education, among others. This is a target rich environment for us! Further, our average discounts to net asset value ("NAV") for investments purchased in Q3 18, Q4 18 and expected for Q1 19 were 45%, 40% and 49%, respectively. So, we continue to pay about 55 cents for each dollar of NAV we are buying.

Our two prior impact secondary funds (Clean Growth III and IV) are in the harvesting phase and are enjoying significant liquidity of late. CG III now has a 0.7x gross DPI (distributions to paid-in-capital) and is hovering in the mid-teens for a net IRR. CG IV has just entered the harvesting phase but is already at a 0.3x gross DPI. CG IV has a 90+% net IRR but we expect that to moderate as the fund matures.

We are now at the 10-year anniversary of the March 2009 bottom of this bull market. Naturally, a few investors have inquired what impact an economic downturn would have on our impact secondaries strategy. The answer is basically twofold: (1) for our current funds it would slow the return of capital to investors, elongate the holding period and reduce the IRR and (2) for new capital being put to work in impact secondaries, it would very likely increase both the supply of opportunities available to us, as well as further reduce the prices we must pay. As to this second point, when given lemons, we are adept at making lemonade!

We also are finding attractive investment opportunities for our infrastructure strategy (clean energy generation and storage). Investment returns for solar projects have fallen slightly as the solar installation marketplace continues to mature. Returns also ticked down briefly due to tariffs imposed on Chinese solar panels but the industry is so resilient that returns have since rebounded. Minnesota, Massachusetts, New Jersey, North Carolina, South Carolina and California continue to offer good returns for solar installations, and increasingly for energy storage projects. Many states have also recently increased their targets for renewable energy—some through the passage of laws and others by decree from the state's Governor. Hawaii and California now have laws requiring their energy be generated entirely from renewables. A dozen other states are considering similar measures, including Minnesota, Wisconsin and New Mexico. Such measures would boost the opportunity set for the funds we manage.

North Sky Named to 2019 ImpactAssets 50

We are honored to have been selected for the 2019 ImpactAssets 50 list, recognizing our commitment to making a positive impact through investments! North Sky Capital was also named to this list in 2018.

Per the ImpactAssets website: "This annually updated list is a gateway into the world of impact investing for investors and their financial advisors, offering an easy way to identify experienced impact investment firms and explore the landscape of potential investment options." Click here for more information.

Upcoming Events

We are regular speakers and attendees at key industry conferences.
We hope to see you at these upcoming events:

April 5	**Yale Impact Investing,** New York, NY som.yale.edu/about/events
April 8 - 10	**Solar & Storage,** Austin, TX financetexas.solarenergyevents.com/
April 9 - 10	**Responsible Investment Forum,** New York, NY events.frallc.com/events/
May 1 - 2	**Total Impact Philadelphia,** Philadelphia, PA totalimpactconference.com/total-impact-philadelphia-2019
June 10 - 12	**US SIF Annual Conference,** Minneapolis, MN ussif.org/2019conference

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