

Fourth Quarter 2020

Quote of the Quarter

“United we stand; divided we fall.”

— Aesop

The Promise of a New Year

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Introduction

This year has been highly unusual in many respects. There have been tremendous negative events—COVID, wildfires, job losses, bankruptcies (especially of small businesses), school closures, political mayhem, etc. There were positive events though too. By no means do we mean to diminish the hardships so many people encountered this year, but we are “glass half-full people.” So we will focus on the year’s positive aspects and what investors can do as we all charge forward into 2021.

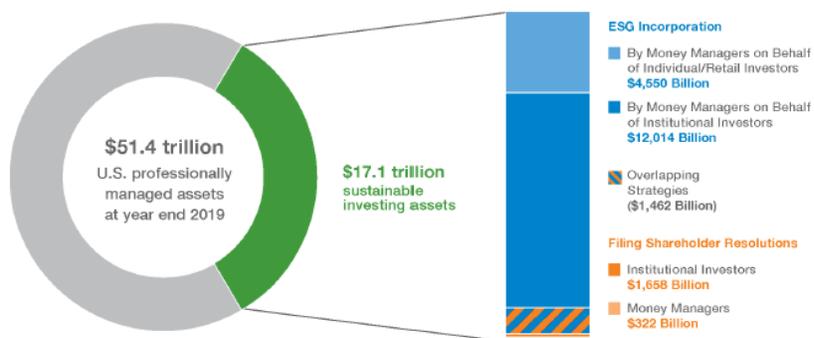
Market conditions for sustainable infrastructure remained strong throughout 2020, despite COVID and the economic downturn. Generally, the pace of new investment and exit activity remained steady throughout the year. There were brief interruptions to some new construction projects across the USA in the spring, followed by essentially a return to a normal construction pace.

Market conditions for impact secondaries were a little choppy than the infrastructure marketplace. COVID significantly slowed investment and exit activity in the first half of the year, followed by a recovery thanks in part to an increase in M&A and IPO activity in the second half of 2020. Furthermore, and seemingly out of left field, [SPAC](#) vehicles became the year’s bright, shiny object, accounting for a total of more than \$70 billion invested across 200+ transactions. Many of these SPACs were in the impact sector, including recent deals such as Cano Health, Luminar (LIDAR for autonomous driving) and STEM (energy storage)—STEM is one of our portfolio companies.

The back half of the year provided many good exit opportunities for impact investors, including us (more on this in the next section).

Another 2020 highlight is that capital flows into ESG/impact vehicles have been on a significant upward trend since 2010 and that trend continued in 2020. US SIF recently released its biennial [impact investing trends report](#), of which North Sky Capital was a lead sponsor. Among other important findings, the report announced that now 1 in 3 professionally managed dollars in the USA are invested with an ESG or Impact mandate. That’s \$17.1 trillion dollars!

Size of Sustainable Investing Assets 2020



Sustainable Investing in the United States 1995-2020



Our 2021 outlook for impact secondaries and for sustainable infrastructure investing (especially greenfield projects in areas like clean energy and waste-to-value) is very positive based on current market conditions including availability of capital, low interest rates, favorable regulatory conditions, and a strong economy.

2020 in Review

Big things happened at North Sky Capital in 2020.

We celebrated our 20th year anniversary as a firm.

North Sky was again selected as one of the impact investment firms recognized by ImpactAssets 50.

We made our first investment out of North Sky Infrastructure Investment Fund (“IIF”), which focuses on sustainable infrastructure within Opportunity Zones. The first investment is a renewable natural gas (“RNG”) project in San Bernardino County, California. Click [here](#) for press release. Other investments are pending including solar, waste-to-value and RNG projects. Our return target for IIF is a 2.5x investment multiple, in addition to the tax-free capital gain after the ten-year holding period. If you would like to learn more about our OZ strategy, please contact [Gretchen Postula](#) or [Andrew Harris](#).

We had significant liquidity events across all our funds. Most notably:

- Our sustainable infrastructure funds sold approximately 170 MWs of operating wind and solar assets spread across Connecticut, Illinois, Iowa, Massachusetts, New York, and Ontario in four separate transactions with strategic and financial acquirers
- Our impact secondary funds benefited from liquidity events involving AquaVenture Holdings (acquired by Culligan), BrightFarms, Energex, HYL A Mobile (acquired by Assurant, ticker AIZ), Limelight Health, Newterra (acquired by Frontenac), Ostara, Rancher Labs, TAS Energy, TPI Composites and many others.

By yearend, we will have also achieved final liquidating events for our prior funds CleanTech I, Direct II and VC IV.

We continued to add to our team—Pat Kay, Ryan Fraser and Shane Collings all joined us in 2020. Pat and Ryan bolstered our infrastructure and private equity investment teams, respectively. Shane was hired as a utility player and specifically to enable us to move our impact reporting from a biennial basis to an annual one.

Mid-year, North Sky was allocated \$30 million in New Market Tax Credits by the US Treasury. This allocation in part speaks to our long tenure in the impact investing and sustainable infrastructure space and successful track record investing in projects that meet the program’s goals of economic development and job creation in distressed areas. North Sky was one of 76 community development entities that received allocations (more than 200 groups applied). Doing business as National Impact Fund, we have reviewed numerous investment opportunities and already completed our first allocation relating to the construction of a peanut shelling plant in Alabama, which will serve farms across multiple states and create many new jobs. We expect to allocate all tax credits by the end of Q1 2021.

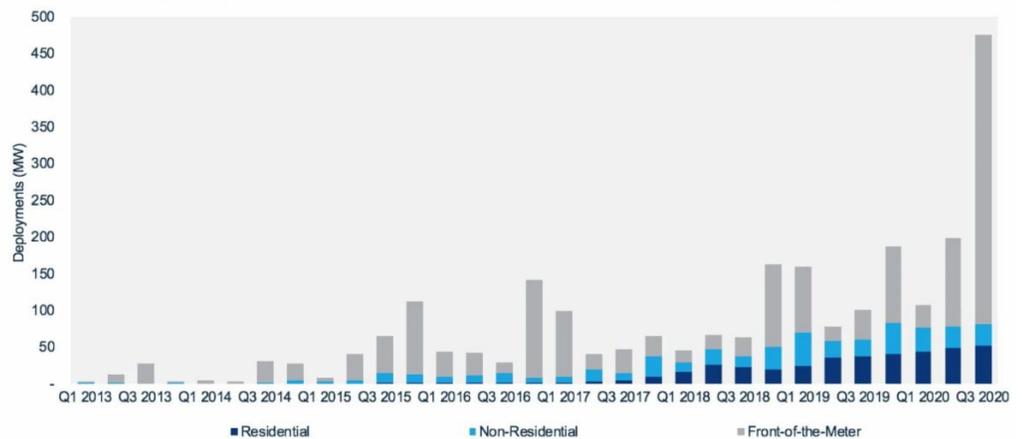
We moved our headquarters from downtown Minneapolis to a larger location, effective December 1. Our new address is **701 Lake Street East, Suite 350, Wayzata, MN 55391**.

Looking Forward

Sustainable Infrastructure: We focus on investments in clean energy, waste and water projects. Right now, we are particularly bullish regarding new investment opportunities in renewable fuels and waste-to-value. Our most recent investment was in a RNG project in California. Several other similar projects are under review now. Also, the number and quality of energy storage opportunities we have been seeing has increased. Energy storage is an area that has been rapidly growing. According to Greentech Media: “Annual deployments are expected to more than double in 2020 overall and nearly triple in 2021.” Experts predict the energy storage market will reach 7.5 gigawatts in 2025—6x the size of 2020 installations. We are reviewing solar plus storage opportunities within a few specific states that have supportive regulatory frameworks.

U.S. Q3 2020 deployments reached a staggering 476 MW

Record-shattering deployments in California redefined the market's scale - and required big edits to our Y-axis



Source: Wood Mackenzie / ESA U.S. Energy Storage Monitor

Looking ahead at prospective solar investments, we are closely monitoring the availability of tax equity. In a broad sense, using tax equity within the financial structure of infrastructure projects improves the returns for equity and equity-like investors such as North Sky. Two factors are currently influencing the availability of tax equity: COVID and an imminent step down in the investment tax credit (“ITC”) from 26% of qualified capital costs in 2020 to 22% in 2021. In anticipation of this step down, we initiated several projects, including the purchase of solar equipment, to meet the safe harbor rules that should enable use of the 26% rate for these projects. As for COVID’s impact, note that the availability of tax equity is generally correlated to the profitability of large financial institutions. COVID reduced profitability for many of the most-active tax equity providers in Q2 and Q3, reducing their demand for tax credits to offset their profits (i.e., the supply of tax equity for projects went down). Despite these two factors, we observed a rebound in the tax equity market in Q4—good news.

We are also monitoring legislative activity at the state and federal level, including federal efforts to either extend the ITC for solar projects, or replace the tax credits with cash grants. In November, a bipartisan bill was introduced in Congress by Rep. Mike Levin (D-California) and Rep. Dave Schweikert (R-Arizona) proposing these favorable measures. While we are not in the business of predicting what Congress will do, it seems more likely than not that these measures will be included in the various tax, energy and infrastructure efforts of the incoming Congress.

Impact Secondaries: The secondaries market is dynamic. We continue to see good investment opportunities across traditional secondaries, GP-led fund restructurings, single asset restructurings and preferred equity financings. On the flip side, we expect to exit existing holdings primarily through M&A (trade sales and SPAC acquisitions) and perhaps an IPO or two for some of the more recognizable brands in the food/beverage and healthcare sectors.

Holiday Greeting

We are blessed to have the support and collaboration of our investors, the institutional consultant community, wealth managers, lawyers, accountants, service providers, friends, family and others who are our personal and professional lifeblood. We recognize your significant contributions and offer our gratitude and thanks to you all. We wish you a Happy Hanukkah, Merry Christmas and a happy, healthy and prosperous New Year.

Let's Keep Talking

We are eager to hear from you. Please contact us through the below hyperlinks if you have:

- an interest in impact investing and would like to learn more about how we can help you take the [first step](#),
- capital gains that you are thinking about [reinvesting](#) in an Opportunity Zone,
- an existing impact investment that you would like to [sell](#), or
- a sustainable infrastructure project in need of [financing](#).

Upcoming Events

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

February 3 – 5, 2021 [Sorenson Winter Summit](#), Salt Lake City, Utah

March 2 – 4, 2021 [Confluence Philanthropy Advisors Forum and Climate Summit: Reset 2021](#), Virtual Event

June 1 – 3, 2021 [Confluence Philanthropy 11th Annual Practitioners Gathering](#),
Location TBD

June 14 – 16, 2021 [US SIF Forum 2021](#), Chicago, Illinois

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