Second Quarter 2021

Quote of the Quarter

"There are just two rules of governance in a free society: Mind your own business. Keep your hands to yourself."

— P.J. O'Rourke

A 15-Month Gap

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Introduction

Seven months ago, we returned to the North Sky offices to work together in person. That felt like a milestone. After months working remotely, it was wonderful to feel that in-person camaraderie again. On June 2, we experienced another happy milestone: our first in-person fundraising meeting since March 4, 2020. That 15-month gap seems like a chasm and one we are welcome to have behind us. We are investors, but the essence of what we do is people centric. Sure, we made do in the interim by giving updates in writing and by phone and video, but those interactions pale in comparison to genuine face-to-face meetings. All client-facing team members already have had covid or been vaccinated, so we are ready and eager for more in-person meetings whenever you are!

There is a lot going on today, much of it good but some that gives us pause. First, economic growth has been great in Q1 and Q2, due primarily to the re-opening of business across most of the USA and government stimulus. Similarly, activity has been red hot across the spectrum of fundraising, new investments and exits. Congress is working on a big infrastructure spending package, which will be very beneficial to our sustainable infrastructure funds, and details about the new loan program being managed by the Department of Energy have also emerged—more on both points below.

A brief list of some things that give us pause are inflation (food, housing, energy and materials); a shortage of raw materials for electric vehicles, energy storage and other renewable energy tech (copper, cobalt, nickel, manganese, rare earths/magnets, lithium, etc.); Chinese Communist Party unfair trade practices, environmental damage, human rights abuses (Xinjiang and Hong Kong) and military aggression (Taiwan); and the prospect of new taxes and public policies that may dampen economic growth, job creation, small business formation and technological innovation.

But enough handwringing. The sun is shining, summer is in full swing and we see immense opportunity in the back half of the year!

Market Update

Sustainable Infrastructure

Lawyers, Sun and Money. Infrastructure is top of mind for politicians and investors right now. An infrastructure proposal, the American Jobs Plan, was released by the White House on March 31. Note this plan was a white paper, not a legislative bill, and contained policy support for transportation, renewable energy, electric vehicles, energy storage and broadband/internet connectivity. As of this writing, the White House has announced a bipartisan compromise for a $1.2 trillion infrastructure spending plan over 8 years. The draft plan includes significant funding for water and power infrastructure and EV charging. It remains to be seen whether this plan will ultimately pass Congress, and whether additional clean infrastructure incentives such as an extension of the solar investment tax credit will be included in follow-on legislation. Finally, certain Senators, such as Chris Van Hollen (D-MD, Senate Budget Committee) have begun to question whether the usual August recess is necessary this year. If the recess is canceled or shortened, it would signal an increased likelihood for the passage of new infrastructure legislation.

There are many state level activities that bode well for our sustainable infrastructure investment strategy too. Key trends include legislation or regulatory activity aimed at reducing methane emissions from landfills and wastewater treatment plants ("WWTP") and diverting organic waste from landfills. The trends are interconnected. The solutions are (a) capturing and repurposing methane from landfills and WWTPs—like our investments at the Pt. Loma WWTP in San Diego, the LRI landfill near Tacoma and the Victor Valley WWTP near Victorville (90 miles NE of Los Angeles)—and (b) reducing the amount of organic material placed into landfills and instead diverting such material to recycling centers, WWTP or digesters. One bellwether state effort we are monitoring is California Senate Bill 1383, which would require a 75% reduction in statewide disposal of organic waste relative to 2014 levels by the start of 2025. Part of what is driving this and similar efforts in other states is recent findings that landfills are leaking 2x more methane than previously thought.

Institutional investors are focusing on new investments in infrastructure funds due to (a) their attractive risk/return profiles, (b) the potential to act as a hedge against inflation and (c) to meet ESG, impact or sustainability goals, which are quickly becoming the norm within large institutions. Investors in Europe, Australia and New Zealand have been investing in sustainable fund strategies, including infrastructure, for years. U.S. and Canadian institutional investors have been catching up recently. Many institutional investors today require fund managers to utilize ESG criteria when making investment decisions and in monitoring and reporting on progress within the portfolio. The next step in this trend has arrived: fund managers must prove they are delivering a tangible impact from those investments through regular impact reports, environmental and social benefit metrics and mapping portfolios to the 17 United Nations Sustainable Development Goals (and the various underlying targets).

Similarly, sustainable infrastructure has become a focal point of ESG/impact investors. The need for sustainable infrastructure investment is palpable and evidenced by the agendas of recent conferences such as PEI Infrastructure Investor/Global Offsite, US SIF and Confluence Philanthropy, as well as upcoming conferences like SOCAP.

New Community Solar Investment. In the last three quarters, we made new sustainable infrastructure investments spanning renewable natural gas ("RNG"), waste to energy and community solar. Through our personal and professional contacts and network of developers, we are sourcing investment opportunities with base case net IRRs of at least 10-14% and attractive risk profiles. For example, in May we invested in Novel Energy Solutions, an experienced solar developer, to finance the construction of 135 MW of community solar projects, mostly in Minnesota and Colorado. Novel is headquartered in an Opportunity Zone, and we are thrilled to be working with the Novel team, which is led by CEO Cliff Kaehler.

Solar, and specifically community solar, is an area where we have substantial expertise and are using it to create attractive returns for investors. A few months prior to the Novel investment, we exited a successful investment with another community solar developer, U.S. Solar Corporation. We started backing them in June 2017 with capital from our second infrastructure fund. That capital supported the development of a 100+ MW solar portfolio. Prior to that, in 2012, we collaborated on a series of projects with another community solar developer, Clean Energy Collective, including a 32kW community solar project at the Wright-Hennepin Cooperative site in Rockford, MN in September 2013. That was the first community solar project in Minnesota and paved new ground locally by combining community solar power with energy storage. Wright-Hennepin Cooperative refers to this as Project 1 here. All told that project was a terrific Minnesota story: Wright-Hennepin Cooperative provided the land and access to its customers, North Sky provided the financing, Bloomington-based 10K Solar made the panels, 3M manufactured the reflecting panels and Silent Power in Baxter, MN created the energy storage (battery system).

A Conversation with the Department of Energy. Recently we connected with Jigar Shah, the new Executive Director of the DOE's Loan Programs Office. Mr. Shah is overseeing more than $40 billion in loans and loan guarantees available to help build clean energy infrastructure and related manufacturing capability in America. The application process has been streamlined and the scope of qualifying areas span renewable energy generation, energy storage / dispatch / transmission, "clean" vehicles (EVs, hydrogen, natural gas), advanced nuclear reactors, pollution reduction projects, solar panel manufacturing and more.

Like many of us here at North Sky, Mr. Shah grew up in small-town middle-America at a time when US manufacturing was still thriving and before so many of those manufacturing jobs were shipped overseas. The focus of the call was to discuss ways to reinvigorate American manufacturing and create good jobs in renewable energy and adjacent sectors. We also discussed whether there would be "buy American" mandates in any infrastructure bill that is passed. It seems common sense that those provisions be built in, and we are optimistic they will be.

In North Sky's opinion, the USA must have a robust manufacturing capability for solar panels, electric motors, generators, EVs and next gen batteries, with protected supply chains outside of China's influence, so that we can compete globally in the manufacture of renewable energy power systems and electric cars and other transportation. There is an obvious national security interest that we do so too. During our call with Mr. Shah, we also learned that the Senate is discussing a subsidy for US-based solar manufacturers (potentially 14 cents/Watt) and that subsidy could be spread across the entire supply chain: from the producers of silicon ingots to the makers of silicon wafers, modules and solar panels. The goal, it seems, is to make solar panels made in the USA cost competitive with China. It appears there are similar efforts regarding the US manufacturing supply chain for batteries as well. More to come.

Impact Secondaries

CG IV and CG V Update. Our impact secondaries funds continue to make good progress. Clean Growth IV, a 2016 vintage fund, is fully invested and in harvesting mode. Clean Growth V recently made several new and follow-on investments to bring it to 75% invested as of today.

New secondary investment activity is back in full swing and the marketplace is expanding. Two years ago, we determined that the universe of impact secondary opportunities was approximately $90 billion. Today, that universe easily exceeds $100 billion. We are fishing in a big pond and still encounter very few direct competitors.

In recent weeks we have seen an increase in the number of institutional investors seeking to sell LP interests. We surmise this is driven by a belief that private market valuations for underlying companies of PE/VC firms are either 1) now reflective of a more "normal" environment and they are no longer forced to sell at discounted pricing due to covid or 2) fully valued due to the run up in the public equity market (i.e., the publicly traded comparable companies today translate into higher private company valuations today relative to just a few quarters ago).

Many companies within our secondaries funds have been exploring strategic options and are close to choosing an exit route. Some of these exits may be to SPACs but most exits will likely be through a traditional IPO or sale to a strategic acquirer or financial buyer. These attractive companies span several impact sectors including medical devices, waste-to-value, energy storage and better-for-you beverages. We look forward to reporting on these developments in the coming months.

WSJ Interview. Tom Jorgensen was interviewed by Preeti Singh of the Wall Street Journal for a June 6, 2021 article regarding opportunities in the secondary market as the global economy re-opens post-covid. Here is an excerpt from that interview:

"What excites you the most about the secondary market these days?

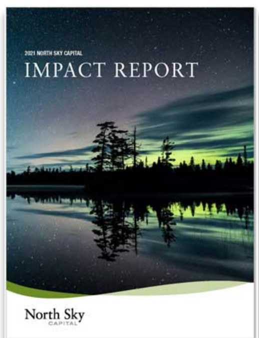
While it may seem counterintuitive, as the secondary market matures, it is becoming more fragmented, which creates unique opportunities to transact outside of highly competitive processes. This is partly driven by a significant increase in secondary advisory firms…and more constituents (LPs, GPs and portfolio companies) willing to consider secondary solutions.

"How do you see the rise of GP-led deals, particularly in the midmarket, shaping the evolution of the secondary market?"

Historically, the GP-led market was characterized by cleanup transactions involving older and typically poor- or mediocre-performing assets in orphaned funds. But the current trend in GP-leds is toward transactions involving higher-performing assets that have achieved the GP's original underwriting case in funds earlier in their natural life cycles. We believe the popularity of these new-style GP-led transactions will continue to drive innovation in the market, creating structures that blend new and old investors and increasing the frequency and consistency of liquidity. However, as with the old-model GP-leds, the potential for misalignment of interest in the new-style transactions is high and conflicts need to be managed carefully by all parties, so participants should continue to pay careful attention to transaction dynamics, incentive structures, etc., when evaluating buy-sell decisions."

For the full interview, click here (subscription).

North Sky News



North Sky released its 2021 Impact Report.

Since 2012, North Sky has published its Impact Report biennially to highlight portfolio companies and projects in its impact private equity and sustainable infrastructure funds that are making a positive social and/or environmental impact. Going forward, North Sky will increase the frequency of its Impact Report to an annual schedule while featuring a deeper discussion of its efforts to support the UN Sustainable Development Goals ("SDGs").

For this and previous years' Impact Reports, along with firm information and other news visit our website.

We are pleased to announce that Rachael Polson rejoined the firm as a Marketing Associate.

As a Marketing Associate, Rachael works across the firm's fundraising, investor relations and public relations functions. During her prior time at North Sky, Rachael served in investor relations and operations roles, where she was integral in new investor onboarding, ongoing investor relations communications, impact report curation and marketing materials creation and maintenance, functions that will immediately be additive to the growth of the firm. Rachael graduated from the University of Minnesota's Carlson School of Management with a bachelor's of science in business.

View the full press release here.

Adam Bernstein and Andrew Harris spoke with IREI's Institutional Investing in Infrastructure about the progress and advancement of ESG significance and reporting in the infrastructure space over the past 10 years.

In the May 1, 2021 i3 article, *ESG: What's in Your Infrastructure Wallet?*, Adam points out that ESG factors have gone from being an ancillary benefit to a pre-requisite for consideration. "Ten years ago, it would be a nice-to-have, and now it's more of an upfront requirement," he added.

The utilization of ESG factors in infrastructure investing is still evolving. "We are seeing a good and healthy dialogue between institutional investors, investment managers and the industry over what is material, what should be measured and what should be factored as risks," Andrew told i3. "And it will take time for that dialogue to play out."

For the full article, click here.

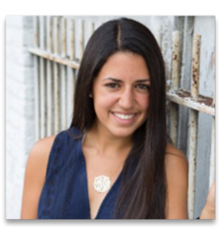
Adam Bernstein spoke to The Wall Street Journal about how the Biden administration's proposed plan for federal infrastructure investment may benefit smaller renewable energy projects and investors.

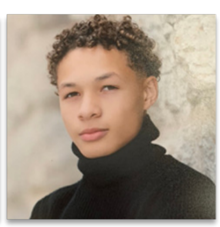
The May 6, 2021 article examines opportunities for private investment in infrastructure in clean energy projects. "A lot of what this does is relieve state and local budgets," Adam said. "Smaller clean-energy projects, in particular, would benefit from this federal investment."

For the full article, click here (subscription).

Tom Jorgensen was interviewed by Preeti Singh of the Wall Street Journal for a June 6, 2021 article regarding opportunities in the secondary market as the global economy re-opens post-covid. For the full interview, click here (subscription).

Gretchen Postula and Adam Bernstein were quoted in a June 9, 2021 FundFire article about institutional interest in the conflux of infrastructure, ESG and impact. For the full article, click here (subscription).





Finally, please help us welcome our two summer interns: Jordan Levy and Drew Irvin. Jordan is a rising senior at UW Madison and Drew is a rising sophomore at the University of Chicago.

View the full press release here.

Upcoming Events

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

October 18-22, 2021 **SOCAP21 Virtual**, Virtual

October 18-21, 2021 **Infrastructure Investor Global Summit Berlin 2021**, Berlin & Virtually

Let's Keep Talking

We are eager to hear from you. Please contact us if you have:

- an interest in impact investing and would like to learn more about how we can help you take the **first step**,
- A desire to learn more about our **sustainable infrastructure investment strategy**
- an existing impact investment that you would like to **sell**, or
- a sustainable infrastructure project in need of **financing**.

For more information, please see our North Sky Capital Firm Brochure.

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