Third Quarter 2023

Quote of the Quarter

"The purpose of life is to live it, to taste experience to the utmost, to reach out eagerly and without fear for newer and richer experience."

— *Eleanor Roosevelt*

Light Switch

Overview

- **Introduction**
- **Market Update**
  - Sustainable Infrastructure
    - Lower Middle Market is Less Crowded
    - Public Policy Update
    - IRA Easter Egg
    - Massive U.S. Lithium Deposit
  - Impact Secondaries
    - Factors Pressuring Sellers
    - LP-Led Transactions
    - GP-Led Transactions
    - Parting Thought
- **North Sky News**
- **Upcoming Events**

Introduction

This has been one of the busiest third quarters we can remember. There was no summer slowdown whatsoever for us, and there was a significant increase in investment opportunities and investor inquiries in September—as if someone flipped a switch over Labor Day weekend. We have seen an uptick in interesting infrastructure opportunities in solar, energy storage, renewable fuels, water and green hydrogen. Similarly, deal flow for our impact secondaries strategy has never been greater. Market forces, policy actions and human behavior explain much of it—more details further below.

Several other events were notable this quarter:

RE+ Conference. In mid-September, we attended the RE+ conference, which has become the largest annual energy event in North America. We estimate there were around 40,000 attendees this year! The event focuses on solar power, energy storage and smart energy and draws investors, developers, manufacturers, technologists and policymakers. We met with over 20 developers and added several community solar and energy storage projects to our pipeline of potential investment opportunities. The USA is the world's second largest market for solar, and we expect 35 GW of total installations this year. The conference reaffirmed our bullish outlook for sustainable infrastructure, thanks in part to the "once-in-a-lifetime" uplift coming from the Inflation Reduction Act (IRA). We are happy to also report additional domestic solar panel manufacturing capacity is coming online very soon. Longi, Trina Solar and Canadian Solar are more than doubling their pre-IRA domestic capacity. All told, we believe there is 50 GWs of solar panel manufacturing capacity being built in the USA right now. The conference also showed there is a very strong trend of coupling solar panels with battery energy storage, in part to capture higher pricing available during off-peak hours.

Progress on E-waste. We celebrate the little victories, too. Apple announced its iPhone 15 will use USB-C charging ports, rather than Apple's proprietary lightning port. Apple was responding in part to EU mandates, which require that phones, tablets and cameras use the USB-C charging standard by yearend 2024 and that laptop computers do so by early 2026. The move brings Apple in line with Android phones and soon laptop makers will join them in using the same charging system. Different devices often operate at different power levels as well—e.g., 20W for phones, 40W for tablets and 100W for laptops. That meant different charging "bricks", too. Thanks to improvements in size, efficiency and versatility in power electronics by companies like GaN Systems, a single small "smart" power brick can recognize the device type and supply the appropriate wattage. Soon we can all discard the tangle of cords and power bricks we have in our carry-on bags and replace them with a single cord and small power brick. This move makes life easier, saves money and reduces electronic waste.

Awards. **Environmental Finance** selected North Sky for two additional Sustainable Company Awards for:

- Circular economy transition of the year
- Pollution reduction initiative of the year

These awards honor companies transforming business practices to create a sustainable future.

Market Update

Sustainable Infrastructure

Lower middle market is less crowded. We are very excited about our position in the sustainable infrastructure sector at this moment. North Sky's lower middle market strategy enjoys less competition for new investments compared to more crowded tiers such as utility scale wind and solar where multibillion-dollar funds are fighting to deploy massive amounts of capital in 100+MW projects where $400-600 million capital requirements are the norm. In fact, some of the utility-scale solar and wind projects are so massive that the mega funds are partnering in club deals to fund them. Investors have seen that movie before—vast pools of capital in search of a home—and many did not like the ending. North Sky is upstream from this, focusing on investments in projects that require $100 million or less in total capital and partnering with experienced developers in renewable natural gas, community solar, energy storage and other premium revenue opportunities. Our focus is on building spinning assets with stable long-term cash flows that the big pension plans and mega infrastructure funds want to buy. By design, the assets we are constructing are in high demand once they are operational, at which point we sell them through competitive auctions. This dynamic has the potential to produce IRRs and investment multiples that exceed traditional infrastructure returns. For example, many large pension plans have stated their expected net IRRs from infrastructure are CPI + 3%. With CPI being 6.7%, that equates to 9.7%. Our IRR expectations for investments we are making today is 14+%, which is derived from our prior track record for SIF I-III of roughly 12%[1] net IRR boosted by at least 200 bps thanks to the IRA.

Public Policy Update. Our investment strategy benefits from, but is not dependent on, federal, state and local policies. As such, we closely monitor public policy to ensure our investments capture the benefits of incentives aimed at stimulating investment, promoting sustainability and addressing critical infrastructure needs. We recently authored a Public Policy Update and invite you to read it.

IRA Easter Egg. Last year's Inflation Reduction Act (IRA), was a significant policy change in the USA that dramatically boosted expected investment returns for sustainable infrastructure. More than a year later, we are still discovering new benefits within the IRA. The IRA added IRC Sec 45Z, which allows for a Clean Fuel Production Tax Credit (PTC), to support the production of low-emissions transportation fuel. To qualify, fuel must achieve a "greenhouse gas" reduction of approximately 40% (or better) when compared to diesel and meet other requirements. The PTC will apply to fuel produced and sold in 2025, 2026 and 2027. For projects that meet prevailing wage and apprenticeship requirements, or are in the placed in-service safe harbor, the PTC amount will be $1.00/gallon times the "emission factor." Assuming a carbon intensity score of 0 and using our California renewable natural gas project as an illustration, we expect a PTC of roughly $7.60 per MMBtu from 2025-27. That would increase the expected IRR by roughly 150-220 basis points. If the final rules give credit for a negative carbon intensity score, the value of the PTC and the expected IRR would be even higher.

Massive USA Lithium Deposit. A newly discovered lithium deposit in Northern Nevada may be the biggest in the world, worth nearly $1.4 trillion according to Lithium Americas Corp. As we all know, lithium is a key component of batteries that are commonly used for EVs, energy storage, mobile phones and laptops. The deposit is the result of a massive volcanic eruption roughly 16 million years ago. The site, known as the McDermitt Caldera, may contain 20-40 million tons of lithium. Current global demand for lithium is about two million tons per year. The USA imports most of the lithium used in battery manufacturing (and related industries) from Australia and South America, so a domestic discovery of this magnitude is big news.

Impact Secondaries

We live in interesting times. Investors are wrestling with volatility in the stock and bond markets, inflation, high interest rates, the war in Ukraine, sovereign debt at record levels and dysfunctional political systems seemingly across the globe. We wouldn't ever predict, for example, that stocks are going up or down next quarter—that's a fool's errand. But we can say that over the long-haul US stocks have moved up and to the right, and that several factors are pressuring many existing owners of private equity impact investments to sell their holdings, often at steep discounts to NAV. We believe that if you can buy strong assets at good prices or through smart structured transactions that reduce downside risk, then that is a good bet in today's rough and tumble market.

Factors pressuring some to sell their private equity stakes. As we have discussed before, right now feels like a "buyer's market" to us, in part because many big institutional investors are feeling the strain of more cash outflows to new private market investments (private equity, infrastructure, real estate, etc.) than cash inflows from IPOs and M&A liquidity events from existing private market investments. It is no secret that IPO activity has been slow for many quarters. While investment bankers and others are hoping the ARM, Instacart and Klaviyo IPOs signal a re-opening of the IPO window, that remains to be seen. Similarly, M&A exits for private equity managers have also been below the prior trend line. PJT Park Hill, a strategic advisory firm, recently reported in its survey results that 75% of respondents' portfolios were cash flow net negative in 1H 2023—the liquidity slowdown is real. To remain active and maintain vintage year diversification, investors are making new commitments but often to a smaller number of managers. As existing GP relationships become non-core, those holdings go on the chopping block. Secondaries investors are well-positioned in this market.

LP-led transactions. There was a rebound in 1H 2023 for LP-led secondary transactions as buyers sought more diversified portfolios. This was true for both the traditional secondaries market and the impact secondaries market. As discussed previously, we have seen more favorable pricing for impact secondary opportunities due to less competition from other buyers. Our pricing is currently in the 40-60% of NAV range, as compared to 57-70% of NAV as noted in the PJT Park Hill survey for traditional (non-impact) funds. We anticipate discounts for venture and growth equity funds (where a majority of impact funds reside) will remain elevated (favorable) for the next several quarters. We are focusing our efforts where we can use our GP relationships to gain an information advantage to properly assess the future value appreciation potential of a portfolio and price our bid accordingly.

GP-led transactions. Compared to 2022, an increasing number of GP-led transactions have been multi-asset continuation vehicles rather than single-asset continuation vehicles. Prior to yearend 2022, many large secondaries funds were trying to make up for previously slow quarters by making large commitments to big single asset transactions. Those big single asset deals pulled them off track from their overall diversification plans. Recent quarters have seen a reversal—back toward multi-asset deals and thus more diversification. Per Jefferies, single-asset transactions have decreased from ~50% of GP-led transactions in 2022 to ~40% in 1H 2023. The reversal may also be partially due to a GP's desire to generate a greater number of portfolio company exits from legacy funds given the ongoing dearth of M&A and IPO exits.

According to the PJT Park Hill survey, pricing for multi-asset and single-asset continuation vehicles averaged 87% and 96% of NAV, respectively, in 1H 2023. Again, we're seeing more favorable pricing for GP-led solutions in impact companies. Our most recent multi-asset continuation vehicle investment was priced at 82% of NAV and our next single-asset continuation vehicle investment is expected to price at 70% of NAV. With pricing dynamics like this, GP-led solutions will continue to play an important role in the construction of CG VI.

In summary, the market dynamics for secondaries are favorable and even more so for specialist strategies like Clean Growth. We look forward to capitalizing on the above-mentioned dynamics in the coming quarters.

Parting thought. We have noticed a trend about new investors who join us for CG VI. Investors from the USA, Canada, UK/Europe, Brazil and elsewhere are often using us either as their "first" impact investment or as their "last" impact investment. The "first" investment group typically has recently created an investment allocation for impact investing and wants to jump right in via a secondaries fund to obtain an instantly diversified impact portfolio with multiple managers, vintage years and impact sectors. Secondaries also tend to provide quicker capital deployment, shorter hold periods and discounted pricing entry points for attractive assets. This "first" investment group is also strategically seeking to benefit from the reverse J-curve of a secondaries fund as they begin to make their next commitments to new private equity and infrastructure impact funds (with normal J-curves). On the other hand, the "last" investment group usually is working in reverse order. The "last" group typically has had an impact investment program for many years, slowly building up a portfolio of venture capital, growth equity, buyout, private credit and infrastructure impact funds. They now have a pretty mature impact portfolio. As they assess their progress, they naturally compare it to their non-impact alternative investments portfolio and realize they are missing something—a secondaries fund. That leads them to us as the cherry on top.

Conclusion

Regardless of the negative global news headlines, the sustainable infrastructure and impact secondaries sectors were very active in Q3. We are in a goldilocks period with this combination of investor interest, actionable investment opportunities and tremendous policy support. We are now heading into the busiest time of the year in terms of deal volume and looking forward to it.

North Sky News

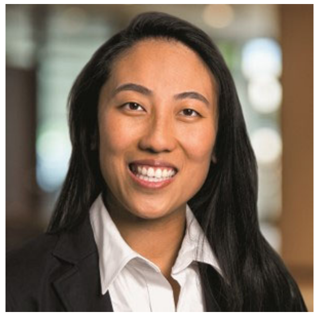
Scott Barrington recently discussed with *WSJ Pro Private Equity* why corporate venture units may be rethinking their investment strategies—and the opportunities this presents in secondaries.

Read the full article here.

BLUE HOUR VENTURES

North Sky Capital's Clean Growth Fund VI is pleased to announce the acquisition of a limited partner interest in Blue Hour Ventures I, a 2017-vintage fund with 11 active portfolio investments.

Read the full press release here.



Lucy Fan explains why lithium-ion battery technology is ripe for disruption, especially for longer-duration energy storage solutions. Listen to her comments on *Infrastructure Investor*'s Podcast, "Energy Storage Goes Beyond Lithium-ion."

Listen to the podcast here.

Tom Jorgensen spoke with *Private Equity International* to discuss challenges and opportunities with secondary deals in the healthcare sector.

Read his thoughts in PEI's 2023 Healthcare report here.

North Sky Capital is pleased to announce it has been recognized by Environmental Finance's 2023 Sustainable Company Awards in two categories: "Circular Economy Transition of the Year" and "Pollution Reduction Initiative of the Year."

Read 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 13	WAVE 7th Annual Women in Alternative Investments Career Forum, New York
October 18-19	Carmo Companies Private Markets Texas Meeting, Austin
October 23-25	SOCAP23, San Francisco
October 31-November 1	PEI Impact Investor Summit: North America, New York
November 29-30	Infrastructure Investor America Forum 2023, New York
November 30-December 1	With Intelligence Women's Private Capital Summit 2023, New York
December 4-5	Carmo Companies Private Markets Florida Meeting, Miami Beach

Let's Keep Talking

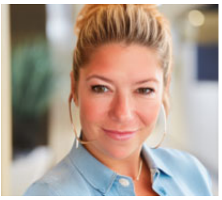
We are eager to hear from you. Please contact us if you have:

- an interest in impact investing and would like to learn more about how we can help you take the first step,
- 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.

Scott Barrington
CEO & Managing Director
(612) 435-7170
sbarrington@northskycapital.com

Gretchen Postula
Managing Director & Head of Investor Relations
(612) 435-7177
gpostula@northskycapital.com



Erika Gucfa
Managing Director
(401) 837-6221
egucfa@northskycapital.com

[1]Net IRR is as of 6/30/23 and pro-forma based on SIF IV's terms and conditions. The prior infrastructure funds had different fees, terms and structures than SIF IV. For details of how this pro-forma IRR was calculated, see additional disclosures in the SIF IV Offering Memorandum or request information from gpostula@northskycapital.com. The performance of the prior infrastructure funds is shown for illustrative purposes only and is not indicative of the future results of the Fund. PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS.

CONNECT WITH US