PALOS

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Weekly Commentary

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Northland Power's Investor Update on Offshore Wind Power

Northland Power (NPI-TSX) is a Toronto-based power producing company with operations in Asia, Europe, Latin America and North America. NPI owns or has ownership in 3.2 GW (giga-watts) of producing capacity and 2.6 GW under construction. Established in 1987, Northland has a strong track record of developing projects across multiple technologies, a disciplined and rigorous project development approach, and significant inventory of early and mid-stage opportunities that total approximately 20 GW of capacity. Only eight years ago NPI received most of its cash flow from gas-fired generation. Today, NPI sees the "vast majority" of cash flows from renewables and the company is a "top 10 global player" in offshore wind (*source: Investor Update,Oct.2023*).

Last Friday (Sept. 29, 2023), Northland provided investors with an update via a conference where management made it clear that moving forward wind power will be the focus. NPI currently has 10 GW either "operating, under construction or at an advanced stage of development" in offshore wind. Projects currently under construction include the Hai Long project (Taiwan Straits) and Baltic Power (Polish Baltic Sea). NPI's offshore wind assets, including in operation and in development, are expected to produce over CAD$ 1.1 billion of adjusted EBITDA one online (by 2027) according to President and CEO Mike Crawley.

The **Hai Long** offshore project will generate 1.0 GW of power. Construction has commenced and contracts have been secured with high quality, highly experienced contractors. Revenue stability will be bolstered through a 20-year Feed-in tariff (FIT) and a 30-year Corporate Power Purchase Agreement with an **S&P AA-** rated counterparty. Risk will be mitigated with "buffers" incorporated into the contacting schedule and secured long-term contracts with reputable turbine suppliers. Foreign currency risks are hedged. Importantly, the Taiwanese government is very supportive of renewable energy with a target of 20% of power generation coming from renewables by 2025. Project commissioning is expected for the second half of 2025.

Construction for the **Baltic Power** project (1.1 GW) has been fully funded via financing with twenty-five financial institutions. Cash flow stability risk is mitigated through a 25-year Contract for Differences (CfD) revenue agreement indexed to Polish inflation (CPI) and a partnership has been established with **Orlen S.A.,** a large Polish energy company. Similar to Taiwan, Poland has significantly increased commitments to renewables. Coal generation, which currently accounts for about 70% of the power mix, is expected to drop by half to 35% by the end of the decade. Energy generated through renewables "tripled" between 2010 to 2020. The project should be operational by the first half of 2026.

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NPI shares closed last Friday at $21.26, well below its pre-pandemic price level and close to a recent low established in March of 2020. Shares are trading below the "mid-$40's" established in August of 2022. Share prices of companies that are interest rate sensitive have been challenged by aggressive central bank policies that are designed to counter rising inflation. Specifically, this includes the Communications, Utilities and REITs sectors. Rising rates act as a headwind as budgets for growth-oriented projects have risen substantially.

If there's one thing we understand as investors, it's that fundamentals can change quickly. We anticipate that rates hikes will begin to slow, or even begin to fall, as inflation data eventually signals that the economy is slowing, and rates will likely peak. Of course, it's the timing that's tough to predict. In the meantime, NPI shares are yielding 5.5% and a monthly dividend of $0.10 ($1.20 annual) has been consistently paid since December 2017. The dividend was $0.09 from January 2013 to December 2015 before rising by a penny.

NPI continues to expand the growth pipeline prudently, selectively and with value creation at the forefront. Renewables have been facing rising cost pressures, however, there are potential catalysts. Governments continue to encourage the shift to climate-friendly renewables, fossil fuel prices continue to rise, and decarbonization tailwinds will persist. Over the next four years (by 2027), NPI expects to have "approximately 6 gigawatts of assets" operating in wind power which will essentially "double" existing operational capacity according to President and CEO Crawley. This equates to a "17% compound annual growth rate" (CAGR). We view NPI shares are attractively valued. The **Palos Income Fund LP** and the **Palos Equity Income Fund** currently hold shares of Northland Power.

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Chart 1: Palos Domestic Funds versus Benchmarks (Total Returns) [1]	FundServ	NAVPS	YTD Returns
Palos Income Fund L.P.	PAL100	$8.21	2.54%
Palos Equity Income Fund - RRSP	PAL101	$6.67	1.68%
Palos WP Growth Fund - RRSP	PAL213	$10.83	-14.53%
Palos-Mitchell Alpha Fund [3]	PAL300	$10.35	25.70%
S&P TSX Composite (Total Return with dividends reinvested)			3.44%
S&P 500 (Total Return with dividends reinvested)			13.06%
S&P TSX Venture (Total Return with dividends reinvested)			-1.81%
Chart 2: Market Data [1]			**Value**
US Government 10-Year			4.57%
Canadian Government 10-Year			4.03%
Crude Oil Spot			US $90.79
Gold Spot			US $1,848.10
US Gov't10-Year/Moody BAA Corp. Spread			182 bps
USD/CAD Exchange Rate Spot			US $0.7365

[1] *Period ending September 29th, 2023. Data extracted from Bloomberg*

[2] *Fund is priced annually*

[3] *Fund is priced weekly on Tuesdays*

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