Q3 2022 Earnings Call

November 2, 2022

Prepared Remarks

PATRICK JOBIN

Thank you operator. Before we begin, please note that certain remarks we will make on this call constitute forward-looking statements. Although we believe these statements reflect our best judgment based on factors currently known to us, actual results may differ materially and adversely. Please refer to the Company's filings with the SEC for a more inclusive discussion of risks and other factors that may cause our actual results to differ from projections made in any forward-looking statements. Please also note these statements are being made as of today, and we disclaim any obligation to update or revise them.

On the call today are Mary Powell, Sunrun's CEO and Danny Abajian, Sunrun's CFO. Ed Fenster, Sunrun's co-founder and co-executive chair, is also on the call today and will be participating in the Q&A session that follows the prepared remarks.

And now let me turn the call over to Mary.

MARY POWELL

Thank you, Patrick.

Wow, what a quarter it has been, I have been looking forward to this call to update you all on what this team has accomplished. We have more than delivered what we said we would – significantly exceeding our guidance on Net Subscriber Value, beating the midpoint of our volume guidance despite disruptions from hurricanes, and achieving a scale of over $5 Billion in Net Earning Assets. Sunrun is now serving 760,000 customers – plus nearly 10,000 households in our multi-family housing projects, which are poised to expand significantly under the Inflation Reduction Act, providing incredible socio-economic and clean energy benefits. All of this while continuing to lead on innovation -- for instance, just yesterday we announced our latest partnership on leveraging our clean energy assets to build a more sustainable and resilient solution for Puerto Rico.

The macroeconomic environment presents tremendous opportunity for us as our 'clean energy as a subscription' model allows customers to leverage, and stack, the latest innovative energy technologies to power their homes and cars while providing them an opportunity to save money. At the same time, the macroeconomic environment has provided an opportunity for us to demonstrate the power of quick decisive action and stellar execution as we laser focus on profitable growth.

In the quarter, we delivered strong results and continued to execute on making Sunrun even faster, better, and stronger in all dimensions of the fundamentals.

First, we are delivering record cost efficiency and expanding Net Subscriber Value, even as we invest in innovation and differentiation.

We grew installation volumes in Sunrun's direct business sequentially at a growth rate 3x the rate of headcount additions, as installation crew efficiency increased by nearly 30%. I am tremendously proud of what our team is doing in the field each and every day for our customers.

We also maintained strong overhead cost discipline, with G&A expenses declining more than 6% compared to last year, and reaching an all-time low of approximately $1,100 per new customer, a 20% improvement year over year, showing the benefits of our scale and disciplined approach to sustainable growth.

We have been adapting to higher interest rates and strategically adjusting pricing as necessary, while still providing a strong customer value proposition. This is against a backdrop of rapidly accelerating utility prices and a long term trend of deteriorating reliability, particularly in California.

As a result of our team's strong execution, we delivered significantly improved Net Subscriber Value in Q3 of over $13,000, exceeding guidance, even when excluding the benefit from the passage of the Inflation Reduction Act and we are guiding to continued increases in our margins for Q4.

Second, we are driving strong profitable growth. We grew new installations by 17% year-over-year, deploying 256 megawatts, exceeding the midpoint of our guidance. We achieved this despite devastating hurricanes in Puerto Rico and Florida that allowed many of our existing customers to power through safely, but impacted sales and installation activities for a number of weeks. Clearly, if not for the hurricanes, volumes would have hit the top end of the range. We are on track to deliver approximately 25% growth for the full year.

Third, we continue to innovate and increase our differentiation. Just this week the board of the Puerto Rico Electric Power Authority approved a groundbreaking virtual power plant contract. Sunrun has continued to lead in the deployment of virtual power plants, adding recurring sources of cash flow we can share with our customers – and most importantly, helping to increase the reliability and affordability of the entire electric system. This is another postcard from the future of the tremendous opportunity in front of us to embrace radical collaboration and to increase the efficiency and reliability of our energy systems around the country.

This quarter was a powerful demonstration of the value of our existing networked solar and battery systems, providing more than 1 *gigawatt-hour* of energy back to California's grid system cumulatively over 8 days, helping to prevent rolling blackouts during the recent heatwave. We also provided more than

350,000 hours of backup power to thousands of customers in Puerto Rico and Florida during grid outages following the hurricanes.

We also were excited during Q3 to celebrate the unveiling of Lunar Energy, a clean energy technology company that Sunrun invested in to accelerate whole-home electrification. Lunar's first product will be an integrated, next-generation combined battery, inverter and software offering. We are excited by its launch in 2023.

Our electric vehicle charger has also been very well received by our customers. We are benefiting from – and helping enable – the transition to electric vehicles by providing our customers the ability to run their vehicles on renewable, independently-generated affordable energy. Customers who drive electric vehicles need larger systems. These solar and battery – and EV – resources are incredibly valuable for homeowners and the energy system alike.

Our Ford partnership continues to deliver strong initial results. Approximately 1,000 orders for the Ford Charge Station Pro have been placed thus far – with thousands of additional initial conversations – and a high mix of customers want the additional bidirectional home backup capability. Installs are continuing to ramp.

Policy Updates

Shifting gears, let's talk about some policy updates.

On the Federal side, we were of course thrilled to see Congress take bold action to address climate change by passing the Inflation Reduction Act and effectively extending the Investment Tax Credit for ten years and reinstating it back to the 30% level. We were also very encouraged to see the focus on expanding solar to more low-income communities, multi-family properties, and to encourage the adoption of electric vehicles. We believe Sunrun will be uniquely positioned as the leading national provider of solar and storage energy subscription offerings to expand our clean energy services and make it accessible to even more communities.

As I mentioned in my opening comment, we also see tremendous opportunity in the legislation to build even greater socio-economic impact through our work with multifamily housing. Today, I am proud that Sunrun already serves nearly 10,000 households in low-income multifamily housing and we want to dramatically increase the impact we can make in these communities.

On California's pending NEM proceeding, there isn't much to update beyond the chatter everyone is hearing that we may see a new proposed decision within a few weeks. Californians have spoken loud and clear over the last year that they care passionately about their ability to generate, store and use their own clean energy, without being penalized for doing so. Further, repeatedly over the last year we have seen the value these customers, and their clean energy technology, are providing to all other customers of the grid by sharing their energy back with the grid during some of the highest priced periods, and when the grid was literally at a potential point of failure. Therefore, we remain steadfast in our hope that the Commission's forthcoming revised proposal will not just continue to support this consumer-led revolution, but in fact accelerate it. With more radical collaboration between distributed energy resources and utilities, we can demonstrate a more durable, resilient, cost-effective and clean energy grid for all. Keeping solar accessible to all communities in California is imperative for the state to achieve its clean energy goals. Accelerating distributed solar and storage is also critical for California's economy and for grid reliability. For all of these reasons, we do remain hopeful of a reasonable structure so that the entire grid can benefit from advances in technology and customer generated, stored and shared energy.

On trade, we continue to navigate the dynamic environment. The current bureaucratic process from the Customs and Border Patrol continues to cause delays in the timely release of modules currently sitting at the ports, for us and many in the industry, following the implementation of the WRO and subsequent UFLPA regulations. We continue to source high-quality modules and are maintaining adequate supply for current needs, although we would like faster action to reduce import delays.

We support UFLPA enforcement that prevents any forced labor content from entering the United States, while also facilitating legitimate trade without unnecessary delays, so that industry can deploy clean energy, meet consumer demand, and help the United State achieve its climate goals. There is no time to waste.

<u>Concluding Comments</u>

Sunrun has the right strategy and the right team in place to navigate these uncertain times, our value proposition continues to increase as utility rates escalate rapidly and consumers demand affordable, clean and predictably-priced energy. Whether continued interest rate increases or a recession, Sunrun's opportunity to deliver value to our customers and our financial partners remains incredibly strong.

As always, before turning it over to Danny, I want to express my appreciation for the the team I work with every day, and all the Sunrun employees working so hard to create a company that is faster, better and stronger for our customers and communities, setting the highest standards for ourselves, putting people front and center, analyzing mistakes (even when winning) and crushing it on the fundamentals of sustainable profitable growth, customer obsession and innovation. Never has our cause felt more urgent, I so appreciate the Sunrunners and customers who are so key to all that we can achieve together.

Over to you, Danny.

<u>DANNY ABAJIAN</u>

Thank you, Mary.

Today I will cover our operating and financial performance in the quarter along with an update on our capital markets activities and outlook.

Turning first to the results for the quarter.

Volumes

In the third quarter, Customer Additions were approximately 35,800, including approximately 25,500 Subscriber Additions. Our Subscriber Additions were 71% of our total Customer Additions in the period, hovering around prior levels during the year. Our recent sales activities, and the benefits from the tax credit adders in the Inflation Reduction Act, which are only available to the solar subscription model, indicate the mix of Customer Additions is likely to shift toward Subscribers more significantly in the quarters ahead. Solar Energy Capacity Installed was approximately 256 megawatts in the third quarter of 2022, a 17% increase from the same quarter last year. Our Q3 installations exceeded the midpoint of our guidance range. Excluding installation downtime owing to Hurricanes Fiona and Ian late in Q3, we would have been close to the high end of our guidance range.

We saw strong customer demand for our products and services in Q3. While we are still adding customers to our pipeline, the increased pace of installations is allowing us to gradually work down our pipeline, which is slightly over one quarter at the end of Q3, down slightly from the prior quarter. We aim to manage sales and installation activities to maintain a pipeline that optimizes our resource planning and customer experience.

We have now installed over 47,000 solar and battery systems. We expect that as we introduce additional battery suppliers and work through our pipeline, battery installations will grow rapidly in the quarters ahead and attachment rates will increase meaningfully. However, current battery supply conditions and longer install cycle times have resulted in lower battery attachment expectations in the near future. Today we are prioritizing allocation of batteries in key markets where they are needed the most for grid reliability concerns.

We ended Q3 with approximately 760,000 Customers and 640,000 Subscribers, representing 5.4 Gigawatts of Networked Solar Energy Capacity, an increase of 21% compared to the prior year. Our Subscribers generate significant, recurring revenue with most under 20- or 25-year contracts for the clean energy we provide. At the end of Q3, our Annual Recurring Revenue, or ARR, stood at $969 million with an average contract life remaining of over 17 years.

Subscriber Value, Creation Cost, Net Subscriber Value & Total Value Generated

In Q3, Subscriber Value was approximately $43,400 and Creation Cost was approximately $30,200, delivering a Net Subscriber Value of nearly $13,300, compared to our prior guidance of over $10,000.

Total Value Generated, which is the Net Subscriber Value multiplied by the number of Subscriber Additions in the period, was $338 million in the quarter.

The significant adjustments we made to pricing over the last six months are driving the majority of our margin expansion from prior quarters. In addition, this quarter, our Subscriber Value reflects the benefit of a 30% tax credit as opposed to 26%, provided by the passage of the Inflation Reduction Act. Excluding this extra tax credit value, Net Subscriber Value still significantly exceeded our prior guidance of over $10,000. Systems placed in service in Q1 and Q2 also benefited from the retroactive increase to the tax credit to January 1, 2022, but we opted not to recast prior quarters' Net Subscriber Values nor to reflect this benefit in our Q3 result.

The magnitude of Net Subscriber Value increase from Q2 to Q3 is significant. If you look at this on an unlevered IRR basis, instead of NPV, the increase equates to an improvement in unlevered IRR of over 200 basis points.

We remain vigilant in optimizing overall sales activities and adjusting our pricing and product mix to deliver profitable growth through a rising interest rate environment. These moves are already producing positive results which you can see in Q3. We will continue to evaluate our customer offering based on incumbent utility rate changes, inflation and the interest rate environment.

Gross and Net Earning Assets, Cash Balance

Turning now to Gross and Net Earning Assets and our balance sheet.

Gross Earning Assets were $11.5 billion at the end of the third quarter. Gross Earning Assets is the measure of cash flows we expect to receive from customers over time, net of operating and maintenance costs, distributions to tax equity partners in partnership flip structures, and distributions to project equity financing partners, discounted at a 5% unlevered capital cost.

Net Earnings Assets were nearly $5.1 billion at the end of the third quarter, an increase of $465 million or over 10% from the prior quarter. Net Earning Assets is Gross Earning Assets, plus cash, less all debt.

Although we did not recast prior Net Subscriber Values as previously mentioned, Net Earning Assets benefited from the retroactive tax credit increase by approximately $40 million in Q3, with more expected in upcoming periods. Even excluding this benefit, we saw strong growth in Net Earning Assets driven by our Net Subscriber Value improvement.

We ended the quarter with $956 million in total cash, an increase of $93 million from the prior quarter.

Capital Runway

We continue to maintain a robust project finance runway. As of today, closed transactions and executed term sheets provide us with expected tax equity capacity to fund, at a 30% tax credit, over 340 megawatts of projects for Subscribers beyond what was deployed through the third quarter. Sunrun also had over $700 million in unused commitments in its $1.8 billion non-recourse senior revolving warehouse loan available at the end of the quarter to fund nearly 300 megawatts of projects for Subscribers. This strong capital runway allows us to be selective in timing our capital markets activity.

Outlook

Turning now to our outlook.

Demand for our offering remains resilient, as we provide customers with affordable, clean and reliable energy. We are prioritizing strong unit margins by optimizing our sales mix and increasing pricing, even while we deliver robust growth. We now expect growth in Solar Energy Capacity Installed to be approximately 25% for the full year. We expect Net Subscriber Value to increase sequentially in Q4 and Total Value Generated to be greater than $1 billion for the full year 2022, an increase from our prior guidance of greater than $900 million.

We will provide views on 2023 on our Q4 earnings call after we finalize our annual operating plan. At this point, our focus is on delivering profitable growth, efficient operations and strong unit margins, while navigating a rising interest rate environment. Put simply, with inflation and increasing interest rates, and pending regulatory resolution in California, a focus on a disciplined strategy is paramount. Our discipline has served Sunrun well for the last 15 years, and we believe will serve the company, and our stakeholders, well in the current economic paradigm.

Interest Rates, Discount Rates & Inflation

Turning briefly to our capital markets activities and outlook.

While the pace of interest rate increases has been unprecedented in recent history, we have anticipated the resulting higher financing costs and raised prices against rapidly increasing utility rates. We remain in a strong position to respond to further volatility in interest rates, as inflationary effects continue to attract customers to our product – one that improves the financial health of households by lowering electricity costs and providing long-term price certainty.

We currently observe our capital costs in the mid-six to mix-seven percent area. Consistent with this cost of capital range, we now expect advance rates on our newly deployed portfolios to be between 75 and 85 percent of contracted Subscriber Values, which are discounted at a 5% rate. This advance rate range is a decline from our previously indicated ranges of 85 to 95 percent last quarter, and 95 to 100 percent at the start of the year. As a reminder, the numerator in advance rate includes proceeds received, net of fees, from all sources – including tax equity and project-level non-recourse debt.

As you may recall, several years ago we used to report Subscriber Value and Gross Earning Assets figures using a 6% discount rate and updated it to 5% when we saw capital costs fall below 4%. We generally prefer not to update the discount rate frequently to enable ease of comparison across quarters. Instead, we provide advance rate ranges that reflect current interest rates, which allows investors to gauge the obtainable net cash unit margins on our deployments.

If capital costs remain elevated heading into 2023, we may adjust the discount rate assumption in our metrics, and update our advance rate range accordingly.

As we've shared before, we regularly enter into interest rate swaps to hedge capital costs on our newly installed customers. We are principally exposed to interest rate fluctuations between customer origination through shortly after installation. Upon installation, our systems are financed with project-level non-recourse debt financing. Nearly all of this financing is insulated from near-term interest rate fluctuations, as our debt is either fixed-coupon, long-dated debt securities or floating-rate debt that has been hedged with interest rate swaps. We ended Q3 with over 90% of our project-level debt with effectively fixed interest rates, with $2.6 billion in fixed-rate securitization debt and $3.1 billion of floating-rate commercial bank debt benefiting from long-term fixed rate swaps.

Our playbook for navigating difficult and rapidly changing capital markets conditions is one I passionately developed leading our project finance efforts for over a decade prior to assuming the CFO role. The longstanding relationships we have cultivated with many capital providers in multiple markets, our reputation as a high-quality sponsor, and the consistently strong payment performance trends of our customers through multiple economic cycles, makes me confident we will continue to deliver the capital necessary to fuel growth both in expansionary and recessionary times.

With that, let me turn it back to Mary.

MARY POWELL

Thanks, Danny.

I could not be more confident in the strength of the Sunrun team to execute on our mission and adapt to the changes around us. We have an enormous opportunity ahead of us to become the trusted, beloved provider of clean, affordable and reliable energy across America, and will continue to focus all efforts on operating efficiently and growing profitably while building for massive scale to lead the market forward.

Before we open the line for questions, I want to again express my deep and sincere appreciation for the big-hearted, ambitious team of employees at Sunrun, the customers we are blessed to serve and the many partners who work with us every single day to deliver on our mission.

With that, Operator, let's open the line for questions.

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Forward Looking Statements

This communication contains forward-looking statements related to Sunrun (the "Company") within the meaning of Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act of 1995. Such forward-looking statements include, but are not limited to, statements related to: the Company's financial and operating guidance and expectations; the Company's business plan, trajectory, and expectations in 2022 and beyond, market leadership, competitive advantages, operational and financial results and metrics (and the assumptions related to the calculation of such metrics); the Company's momentum in its business strategies, expectations regarding market share, total addressable market, customer value proposition, market penetration, financing activities, financing capacity, product mix, and ability to manage cash flow and liquidity; the growth of the solar industry; the Company's ability to derive value from the anticipated benefits of partnerships, new technologies, and pilot programs; anticipated demand, market acceptance, and market adoption of the Company's offerings, including new products, services, and technologies; expectations regarding the growth of home electrification, electric vehicles, virtual power plants, and distributed energy resources; the Company's ability to manage suppliers, inventory, and workforce; supply chains and regulatory impacts affecting supply chains; the Company's leadership team and talent development; the legislative and regulatory environment of the solar industry and the potential impacts of proposed, amended, and newly adopted legislation and regulation on the solar industry and our business; the ongoing, anticipated, or potential impacts of the COVID-19 pandemic and its variants; expectations regarding the Company's storage and energy services businesses, the Company's acquisition of Vivint Solar (including cost synergies), anticipated emissions reductions due to utilization of the Company's solar systems; and factors outside of the Company's control such as macroeconomic trends, public health emergencies, natural disasters, acts of war, terrorism, geopolitical conflict, or armed conflict / invasion, and the impacts of climate change. These statements are not guarantees of future performance; they reflect the Company's current views with respect to future events and are based on assumptions and estimates and are subject to known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements to be materially different from expectations or results projected or implied by forward-looking statements. The risks and uncertainties that could cause the Company's results to differ materially from those expressed or implied by such forward-looking statements include: the Company's continued ability to manage costs and compete effectively; the availability of additional financing on acceptable terms; worldwide economic conditions, including slow or negative growth rates; volatile or rising interest rates; changes in policies and regulations, including net metering and interconnection limits, or caps and licensing restrictions; the Company's ability to attract and retain the Company's business partners; supply chain risks and associated costs; the impact of COVID-19 and its variants on the Company's operations; the successful integration of Vivint Solar; realizing the anticipated benefits of past or future investments, partnerships, strategic transactions, or acquisitions, and integrating those acquisitions; the Company's leadership team and ability to attract and retain key employees; changes in the retail prices of traditional utility generated electricity; the availability of rebates, tax credits and other incentives; the availability of solar panels, batteries, and other components and raw materials; the Company's business plan and the Company's ability to effectively manage the Company's growth and labor constraints; the Company's ability to meet the covenants in the Company's investment funds and debt facilities; factors impacting the home electricification and solar industry generally, and such other risks and uncertainties identified in the reports that we file with the U.S. Securities and Exchange Commission from time to time. All forward-looking statements used herein are based on information available to us as of the date hereof, and we assume no obligation to update publicly these forward-looking statements for any reason, except as required by law.