SUNRUN

3Q 2024 Earnings Call
November 7, 2024
Prepared Remarks

OPERATOR INSTRUCTIONS

Good afternoon and welcome to Sunrun's third quarter 2024 earnings conference call. Please note that this call is being recorded and that one hour has been allocated for the call, including the Q&A session. To join the Q&A session after prepared remarks, please press star 1 at any time. We ask participants to limit themselves to one question and one follow-up question. I will now turn the call over to Patrick Jobin, Sunrun's Investor Relations Officer.

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, Danny Abajian, Sunrun's CFO, and Paul Dickson, Sunrun's President and Chief Revenue Officer.

A presentation is available on Sunrun's investor relations website, along with supplemental materials. An audio replay of today's call, along with a copy of today's prepared remarks and transcript including Q&A will be posted to Sunrun's investor relations website shortly after the call. We have allocated 60 minutes for today's call, including the question and answer session.

And now let me turn the call over to Mary.

MARY POWELL

Thank you, Patrick.

And thank you all for joining us today. This was a strong quarter. Sunrun is becoming faster, better and stronger at everything we do, providing a differentiated customer experience and delivering value to the bottom line.

While public markets fret policy uncertainty and changes in the short-term, Sunrun is more confident than ever in our leadership position, differentiated offering, and our ability to generate enduring value. All Americans want reliable, affordable energy and that has not changed.

Our focus is yielding strong operating and financial results. In Q3, in addition to reaching the 1 million customer milestone, we again set new records for storage installations, net subscriber values, and delivered solid quarter-over-quarter growth for solar installations.

We delivered the second consecutive quarter of positive Cash Generation and are reiterating our strong Cash Generation outlook for the fourth quarter and for 2025.

Our primary focus is accelerating our clean energy differentiation, launching additional products and services to expand customer lifetime values, and remaining the disciplined, margin- and customer-focused industry leader, growing Cash Generation in the business for years to come.

Storage-first Strategy & Accelerating Innovation

One way we are executing this higher margin strategy is by leading with our storage offering, which increases the customer value proposition through enhanced resiliency and control, delivers a more sophisticated clean energy platform, and lays the foundation for future value creation from grid services.

We are blazing the trail to a storage-first future, with a nearly 50% share of all residential storage installations in America. In Q3, we installed storage on 60% of our new customers, nearly double the 33% attachment rate a year ago, and a six point increase from levels achieved in Q2. We installed 336 megawatt hours of storage in Q3, up 92% from a year ago, the most we have installed in any quarter. Our fleet of Networked Storage Capacity has reached 2.1 Gigawatt hours with 135,000 storage systems installed.

While still in the early stages of commercializing these important, dispatchable energy resources, we continue to advance programs that generate value for customers, the grid and Sunrun. We now have 16 grid service programs active across the country, with over 20,000 customers participating. These resources are being utilized by the grid and can replace several costly and polluting gas-fired peaker plants. Sunrun is leading in establishing a platform to turn homes and vehicles into smart controllable load that can be dispatched to, and improve, the electric grid.

Most recently we activated New York's largest residential power plant with the utility Orange and Rockland. This adds to our recently announced partnerships with Tesla Electric and Vistra to support the grid in Texas, as well as our other programs in California, Maryland, and Puerto Rico. Our customers are actively reducing the need to overinvest in costly centralized peaking power plants and associated infrastructure. Customers are also benefiting from direct payments for participating in these programs or, in some cases, receiving batteries at discounted prices when subscribing to our service. Sunrun is also earning incremental revenue for enrolling storage systems in these programs. These incredibly reliable, clean energy resources, lower the cost of the grid for all users.

These same storage resources routinely provide financial value to customers by optimizing their use against far-too-complicated utility rate structures while also powering them through far-too-frequent grid outages. This hurricane season again showed the crippling effects of climate change on our country's aging infrastructure. I'm pleased to report, but not surprised at all, that our systems performed remarkably well as they are built to withstand these harsh events. Nearly 3,000 Sunrun storage customers powered through hurricanes Beryl, Helene, and Milton with 100,000 hours of critical backup power during and in the aftermath of these devastating storms. It is so inspiring to hear from many of our customers that while their local grid systems were down for multiple days, they were able to keep their homes powered, and in many instances, share some of that power with neighbors in need.

Lifetime Value Opportunities

A cornerstone of our strategy to increase our differentiation and augment our competitive advantage is to become a multi-product company that offers a suite of clean energy products to new and existing customers in a bundled, easy-to-finance way.

By continuing to invest heavily in service and providing a leading customer experience, we are able to monetize opportunities to provide additional products to our large base of customers for decades into the future.

We are demonstrating this potential by testing products through pilots and scaling them once success is proven. On slide 7 we highlight the various initiatives underway to learn from and inform our strategy to provide valuable services to existing customers.

One of the areas where we are seeing tremendous success is offering batteries to existing customers -- nearly 87% of our existing 1 million customer base today does not have a Sunrun storage system. We already have thousands of orders, which have been growing rapidly. One way we are selling the offering is through our Sunrun app. We are seeing tremendous interest from customers in signing up through the app, which positions us to fulfill quickly, simply, and at low cost.

You will hear a lot more about this multi-product strategy and our success providing additional products and services to customers in the quarters ahead.

Industry Leadership

I want to spend a minute on what we are seeing in recent industry data.

We don't manage to market share – we view our leading position in the industry as a natural long-term result of pursuing a customer-first, disciplined growth strategy. There have been periods with irrational competitive behavior – such as pricing and terms loan providers offered a few years ago, and more recently, pricing and terms being offered by certain financing-only new entrants – but our view is that fundamentals always prevail in the long-term. We lead with the best customer experience, underwrite healthy and financially sound business, and grow in a sustainable, strategic way.

The latest data from market research firms highlights that our strategy is indeed leading to strong growth. We have seen our share of residential solar installations nationwide pick up significantly in the last few quarters – from 13% in Q1 to 18% in Q3 – and our residential storage share has expanded to 49% in the US. I'm pleased to see these trends, but more pleased that we are doing it in a way that is generating cash and delighting our customers.

I also want to provide an update on the traction in our new homes business. This division is seeing tremendous growth. Sunrun is now working with 9 of the top 10 new home builders in California, and over half of the top 20 home builders in the US. In September, we signed a multi-year exclusive agreement with Toll Brothers in California.

While the new homes division currently represents less than 5% of our volumes, we expect it to grow at least 50% over the next year. Home builders appreciate our leading subscription offerings, service commitments, and long track record. Our offering can provide new home buyers with immediate value, savings on energy and resiliency from backup storage, without increasing the cost of purchasing the home.

Fundamental Demand Drivers

To sum it up, we are gaining share in a disciplined and sustainable way and are on track to accelerate our Cash Generation in the quarters ahead. Utility rates continue to rise and utility service reliability is deteriorating, while solar and storage equipment costs are declining. Customers remain eager to take control of their energy needs with affordable and resilient solutions to power their lives, the ultimate in independence.

Celebrate our people

Before handing over to Danny, as always, I want to take a moment to celebrate some of our people who truly embrace the power of energy independence and the desire to connect customers to the cleanest energy on earth.

Our leading direct-to-home sales team in Bakersfield and our top installation team in Oahu have delivered some incredible results this quarter on safety, quality, battery attachment rates and customer experience. Thank you so much for all that you do every day to make Sunrun the trusted and beloved clean energy partner for our valued customers. I want to make a specific shout-out to Sterling Hills for your great leadership and achievements at Sunrun. Thank you Sterling!

With that, let me turn the call over to Danny for our financial update.

DANNY ABAJIAN

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 on slide 10.

Volumes

We have now installed over 135,000 solar and storage systems, with storage attachment rates reaching 60% of installations during the quarter. We expect storage attachment rates to remain around this level or slightly higher for the next few quarters. This higher mix of storage continues to drive Net Subscriber Values higher.

During the quarter, we installed 336 megawatt hours of storage capacity, well above the high-end of our guidance and an increase of 92% compared to the same quarter last year. Our total networked storage capacity is now approximately 2.1 gigawatt-hours.

In the third quarter, Solar Energy Capacity Installed was approximately 230 megawatts, at the high-end of our guidance of 220 to 230 megawatts.

Customer Additions were approximately 31,900, including approximately 30,300 Subscriber Additions. Our Subscription mix reached 96% of deployments in the period.

We ended Q3 with just over one million Customers and approximately 858,000 Subscribers representing 7.3 Gigawatts of Networked Solar Energy Capacity, a 13% increase year-over-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 over $1.5 billion, up 22% over the same period last year. We had an average contract life remaining of nearly 18 years.

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

Turning to slide 11.

In Q3, Subscriber Value was approximately $51,200 and Creation Cost was approximately $36,600, delivering a Net Subscriber Value of $14,632. This strong result was from higher battery attachment rates, a higher average Investment Tax Credit level and sequential growth in volumes leading to improved fixed cost absorption.

Our Q3 Subscriber Value and Net Subscriber Value reflect a blended Investment Tax Credit of 37.7% which now includes all three ITC adders.

Total Value Generated, which is the Net Subscriber Value multiplied by the number of Subscriber Additions in the period, was $444 million in the third quarter.

Our present value-based metrics are presented using a 6% discount rate, but our financial underwriting already accounts for our current cost of capital, which was approximately 7.1% in Q3. As a reminder, we have taken this approach historically to enable ease of comparison across periods and have not updated the discount rate frequently. Instead, we provide advance rate ranges that reflect current interest rates, enabling investors to calculate the obtainable net cash unit margins on our deployments. In addition, we provide a pro forma Net Subscriber Value using the capital cost observed for the quarter.

At a 7.1% discount rate, Net Subscriber Value was $10,744 and Total Value Generated was $326 million.

On slide 12 you can see our progress increasing Subscriber Value through higher-value mix and higher ITC levels, while keeping creation costs largely flat, generating expanded Net Subscriber Values. Efficiency improvements and hardware cost declines, coupled with our return to operating cost leverage from strong sequential volume growth, have largely offset the increased costs associated with higher storage attachment rates. We expect these trends will continue into Q4 and 2025.

Gross and Net Earning Assets

Turning now to Gross and Net Earning Assets and our balance sheet on slide 14.

Gross Earning Assets were $16.8 billion at the end of the third quarter. Gross Earning Assets is the measure of cash flows we expect to receive from Subscribers over time, net of operating and maintenance costs, distributions to tax equity partners, and distributions to project equity financing partners, all discounted at a 6% unlevered capital cost.

Net Earnings Assets were $6.2 billion at the end of the third quarter, up $550 million from the prior quarter. Net Earning Assets is Gross Earning Assets, plus cash, less all debt. Net Earning Assets does not include inventory, other construction in progress assets or any net derivative assets related to interest rate hedges, all of which represent additional value. The value creation upside we expect from future grid service opportunities and selling additional products and services to our customer base are not reflected in these metrics.

The recent run-up in Treasury yields is a strong reminder of the value of our prudent risk management approach. We programmatically enter into interest rate hedges to insulate our capital costs from adverse near-term fluctuations. The vast majority of our debt is either fixed-coupon long-dated securities, or floating-rate loans that have been hedged with interest rate swaps. As such, we do not adjust the discount rate used in Net Earning Assets to match current capital costs for new installations.

Capital Markets & Capital Runway

Turning to our capital markets activities.

As of today, closed transactions and executed term sheets provide us with expected tax equity capacity to fund approximately 272 megawatts of projects for Subscribers beyond what was deployed through the third quarter.

We also have over $900 million in unused commitments available in our non-recourse senior revolving warehouse loan. This unused amount would fund approximately 318 megawatts of projects for Subscribers. In July, we expanded our warehouse loan by $280 million to $2.6 billion in commitments, matching the growing scale of the business. Our strong debt capital runway allows us to be selective in timing term-out transactions.

Since the start of the year we have closed four ABS transactions, including three that were publicly marketed. Sunrun's industry-leading performance as an originator and servicer of residential solar assets continues to provide deep access to attractively priced capital.

In September we closed a $365 million securitization of residential solar and battery systems. The oversubscribed transaction was structured with two separate classes of publicly-placed A+ rated notes. The weighted average spread was 235 basis points and the weighted average yield was 5.87%. The initial balance of the Class A notes represents a 73.8% advance rate. The credit spread was 30 basis points higher than our last transaction, and in-line with the overall credit spread environment. Similar to prior transactions, we raised additional subordinated non-recourse debt financing which increased the cumulative advance rate to above 80%.

When we think about our balance sheet, we prioritize a strong cash position and use of asset-level non-recourse debt financing. This strategy provides the lowest cost capital to finance cash-flow producing assets backed by highly creditworthy consumers, and is intended to avoid the use of parent recourse capital to fund our recurring origination activity.

Balance Sheet, Cash Generation & Capital Allocation

Cash Generation was $2.5 million in Q3, consistent with our guidance of positive Cash Generation. Timing of tax credit realization will continue to play a factor in Cash Generation timing as the transferability market grows and matures. The terms of each sale vary depending on the buyer's tax return timing, with some resulting in faster payments but at lower prices, and some with higher pricing but slower payments. Our approach is to optimize first for the best value realization for Sunrun, instead of the fastest payment timing. We executed transactions according to this principle, which delayed Cash Generation from Q3 to future periods.

We expect as the number of participants in the tax credit transfer market increases there will be more predictability in timing, and we will create financing solutions that efficiently bridge this working capital investment, accelerating our realization of cash proceeds over the coming quarters.

We have a strong balance sheet with no near-term corporate debt maturities, we have extended our recourse working capital facility maturity to March 2027, and as of today, we have already reduced parent debt by over $100 million since March.

We ended the quarter with over $1 billion in total Cash. Total Cash declined $32 million from the prior quarter, as we consumed $46 million in Cash to repurchase $50 million of our 2026 convertible notes at a discount. We had $133 million of these notes outstanding as of the end of the quarter. We have continued to repurchase this debt into Q4 and currently have $83 million in principal outstanding as of today.

In Q3, of the $143 million increase to our Restricted Cash balance, $133 million relates to establishing a reserve account to repurchase the remainder of our 2026 convertible notes. Establishing this reserve provided us the ability to extend the maturity of our recourse working capital facility to March 2027.

We addressed all of our corporate debt maturities very early in the year. We have no parent capital needs at this time.

Outlook

Turning now to our outlook on slides 17 and 18.

The underpenetrated nature of our industry gives us confidence we can sustain robust growth throughout this decade. In this strong long-term demand backdrop, our priority is to generate cash by continuing to increase customer values through growing our mix of higher-value products and by keeping our costs low.

Storage Capacity Installed is expected to be in a range of 320 to 350 megawatt-hours in Q4. This represents 52% growth year-over-year at the midpoint. This implies over 1.1 gigawatt-hours of capacity added in 2024, an increase to our prior guidance, and 100% growth at the midpoint.

Solar Energy Capacity Installed is expected to be in a range between 240 and 250 megawatts in Q4. At the midpoint, this represents 8% growth compared to the prior year and 7% sequential growth from Q3. This level represents a decline of 17% for the full year, which we believe represents substantial market share gains. We expect year-over-year growth to remain positive in 2025.

Given our emphasis on more valuable product mix, higher ITC levels through optimization of adders, and cost efficiencies, we expect our Net Subscriber Values will increase in Q4 compared to Q3 levels.

We are reiterating our Cash Generation outlook. We expect Cash Generation to be $50 to $125 million next quarter. Because of the discrete large capital transactions inherent to our business, where we ultimately land within this range will depend on project finance transaction timing in Q4.

We continue to expect Cash Generation to be $350 to $600 million in 2025. On slide 18, we have outlined assumptions and sensitivities related to key variables that would affect our achievement. We expect a 45% weighted average ITC level in 2025, and further underpinning our guidance are assumptions of 7.5% average cost of project-level capital, battery attachment rates around 60%, and slight improvements to the timing of tax credit transfers as that market further matures. We expect solar install volumes to grow next year closer to our long-term outlook of 10% to 15%, but our focus will be on margins and Cash Generation as opposed to specific volume attainment.

As we increase our Cash Generation, we will continue to allocate excess unrestricted cash to reduce parent recourse debt and are committed to a capital allocation strategy beyond this initial de-leveraging period that drives significant shareholder value.

With that, let me turn it back to Mary.

MARY POWELL

Thanks, Danny.

I so appreciate the work of the entire Sunrun team, committed to providing customers with a greater sense of independence, stability and security in their own homes, while producing value for our shareholders at the same time, a winning combination.

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, expectations, 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 including its ESG efforts, expectations regarding market share, total addressable market, customer value proposition, market penetration, growth of certain divisions, financing activities, financing capacity, product mix, and ability to manage cash flow and liquidity; the growth of the solar industry; the Company's financing activities and expectations to refinance, amend, and/or extend any financing facilities; trends or potential trends within the solar industry, our business, customer base, and market; the Company's ability to derive value from the anticipated benefits of partnerships, new technologies, and pilot programs, including contract renewal and repowering programs; anticipated demand, market acceptance, and market adoption of the Company's offerings, including new products, services, and technologies; the Company's strategy to be a storage-first company; the ability to increase margins based on a shift in product focus; 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, regulation and policy on the solar industry and our business; the potential impacts of future tax legislation, specifically related to changes in tax credits applicable to the solar industry; the ongoing expectations regarding the Company's storage and energy services businesses and anticipated emissions reductions due to utilization of the Company's solar energy systems; and factors outside of the Company's control such as macroeconomic trends, bank failures, 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 and inflation; volatile or rising interest rates; changes in policies and regulations, including net metering, interconnection limits, and fixed fees, or caps and licensing restrictions and the impact of these changes on the solar industry and our business; the Company's ability to attract and retain the Company's business partners; supply chain risks and associated costs; 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 electrification 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.