



Q1 2018 Earnings Call

May 9, 2018

Prepared Remarks

LYNN JURICH

We are pleased to share with you Sunrun's first quarter financial and operating results along with progress against our strategic priorities.

People want the freedom to take control of their energy and improve their family's lives. We are proud to have delivered reliable, clean energy and more than \$200 million in savings to our nearly 200,000 customers.

We put our customers first, helping them learn about solar, find solutions they want, and pave the way to a meaningful relationship with home energy for decades.

In the first quarter we added 9,400 customers representing 68 MW of deployments and generated \$65 million dollars of net present value, up 16% year-over-year. We created NPV per watt of \$1.10 or over \$8,000 per customer.

The last few quarters have solidified Sunrun's leadership position in the industry. Our massive market opportunity continues to expand to support strong growth and increasing customer value. We are entering new geographies and Brightbox home solar and battery service increases our value proposition by providing stored energy to our customers to reduce cost and service reliability, as well as to utilities during peak times when stored energy is a cost effective way to provide resiliency to the grid.

We are reiterating our full-year guidance of 15% growth in deployments and growth in cash generation above this rate. Our annual growth and continued innovation will be achieved while keeping NPV targets above \$1 per watt.

Geographic Expansion

Technology and cost improvements allow us to serve more customers in even more states. Last month we launched in Illinois proving that solar service isn't just for coastal cities - we are growing in the heartland of America. This marks our 8th market entry since early last year.

Also, just a few weeks ago we received the green light from regulators in Florida to offer a solar lease. As many other markets have demonstrated, allowing third-party ownership, or solar service, makes solar accessible to millions of additional homeowners.



Today the California Energy Commission unanimously approved a mandate for all new homes to have solar starting in 2020. California builds over 100,000 new homes annually - for context there were approximately 124,000 new solar customers added in California in 2017. The solar-as-a-service model is particularly well-suited to this market because it can help homeowners and builders add solar for no upfront cost.

Product Expansion

Our Brightbox home solar and battery service continues to gain traction. This superior energy service has been launched in six states and customer demand continues to exceed expectations.

We launched Brightbox in Massachusetts less than three months ago, and already nearly 10% of the time customers we sell to directly are opting to add a battery. With a low upfront cost, Brightbox is a fraction of the cost of the alternative - dirty, noisy diesel generators.

In California, over 20% of the time our direct customers are choosing to add a Brightbox. In certain markets in Southern California, this rate is now above 50%.

Grid Services Opportunities

Our grid services initiatives are paving the way to deliver even more value per customer.

Regulators and utilities are recognizing that home batteries are clean, quick-to-market, targeted and responsive and can be superior to spending on traditional infrastructure.

Sunrun has created a customer base that nurtures long-term loyalty. This base, along with our customer acquisition strength, make us the natural partner to unlock the full value of residential solar for these efforts.

To accelerate our lead, today I am pleased to announce an expansion of our grid services partnership with National Grid. National Grid has provided Sunrun approximately \$8 million for a share in revenues that arise from new grid services contracts that we jointly bid prior to June 2019. National Grid's increasing investment is a signal that this market is strong and near-term opportunities await.

I'll now turn the call over to Bob, our CFO, to review Q1 performance and discuss guidance in more detail.

BOB KOMIN

Thanks, Lynn.



In the first quarter, we increased aggregate NPV by \$65 million or 16% year-over-year. We also increased our cash position while adding to Net Earning Assets, our metric for value to Sunrun shareholders for systems over their remaining lives.

This quarter we are including NPV, Project Value and Creation Costs by customer in addition to unit economics per watt. We believe this is also a meaningful way to express the value and cost of our decades long customer relationships.

NPV

NPV per customer was nearly \$8,100, or \$1.10 per watt, reflecting an improvement of over \$2,000 per customer compared to the prior year.

Project Value

Q1 project value was approximately \$33,800 per customer, or \$4.61 per watt.

As a reminder, project value is very sensitive to modest changes in geographic, channel, and tax equity fund mix. We expect project value will decline slightly over time, but with costs declining more, although in the short run there can be quarterly fluctuations.

Creation Costs

Turning now to Creation Costs on Slide 8.

In Q1, total Creation Costs were approximately \$25,700 per customer, or \$3.51 per watt. Similar to Project Value, Creation Costs can fluctuate quarter to quarter due to changes in geographic and channel mix. Creation Costs per watt were 4% higher year-over-year primarily driven by sales activities in Q1 that support strong Q2 installation growth. We expect Creation Costs will show modest declines for this year even with the module tariff impact and as we continue to invest in new geographies and grid services. We also expect the adoption rate of home batteries to continue to increase, which carries a higher per-watt cost, but also delivers strong NPV.

As a reminder, our cost stack is not directly comparable to those of peers because of our channel partner business. Blended installation cost per watt, which includes the costs of solar projects deployed by our channel partners, as well as installation costs incurred for Sunrun built systems, improved by \$0.02 year-over-year to \$2.65 per watt.

Installation costs for systems built by Sunrun were \$1.92 per watt, reflecting \$0.22, or 10%, year-over-year improvement.



In Q1, our sales and marketing costs were \$0.75 per watt. We calculate sales and marketing unit costs based on deployed volume in the current period. The increase in sales activities this quarter will lead to a significant increase in deployments in Q2, while the majority of the selling and marketing expense was recorded in Q1. We expect sales and marketing unit costs to decline in Q2 as deployments increase.

In Q1, G&A costs were \$0.30 per watt, approximately flat compared to 2017. In Q1, G&A costs per watt excluded two non-recurring items totaling approximately \$7 million for charges related to establishing a reserve for litigation and an impairment of solar assets that were under construction by a channel partner that ceased operations.

Finally, when we calculate Creation Costs, we subtract the GAAP gross margin contribution realized from our platform services. This includes our distribution, racking, and lead generation businesses as well as solar systems we sell for cash or with a third party loan. We achieved platform services gross margin of \$0.19 per watt compared to \$0.09 in Q1 2017.

Deployments

In the first quarter we deployed 68 MW, slightly above our guidance of 67 MW.

While we don't manage the business for a particular mix between channel partner and direct, our direct business is the platform behind the Comcast partnership volume ramp and where we have focused our initial Brightbox sales and installation efforts and is growing faster than our overall growth rate.

Our cash and third party loan mix was 13% in Q1, in-line with recent levels and consistent with our outlook of low to mid teens.

Liquidity, Balance Sheet & Cash Flow

Turning now to our balance sheet.

Our liquidity position remains strong. We ended Q1 with \$243 million in total cash, a slight increase from last quarter.

We continue to estimate our cash generation will grow faster than our deployments in 2018. In 2017 we generated \$43 million in cash on an adjusted basis. As Ed will describe later on the call, we are working to optimize our existing project debt and expect our cash generation to accelerate as the year progresses.

We define cash generation as the change in our total cash less the change in recourse debt. Also please note that our cash generation outlook excludes any strategic opportunities or accelerated market entries beyond our current plan.



Ed will discuss our capital structure strategy in more detail later on this call.

Early Adoption of New Accounting Standards

This quarter we adopted new accounting standards for revenue recognition and lease accounting, which also required us to recast prior reported GAAP financial results to conform with these new standards. While the standards are mandatory beginning next year, we chose to implement both this year to limit the amount of change to our reported financials.

The changes primarily affect revenue recognition and interest expense with no impact on cash. Our recast 2017 financials resulted in only \$3 million higher revenue which represents less than a 1% impact. EPS improved by only \$0.01.

For a deeper discussion of these impacts, we have provided a supplemental presentation on our investor relations website.

Guidance

Moving on to guidance on Slide 10.

We remain confident in our growth trajectory and are reiterating our guidance of 15% deployment growth for the full year.

In Q2 we expect to deploy 88 MW, reflecting a 16% increase year-over-year.

As I mentioned earlier, we expect to maintain our unit economics above our target of \$1.00 per watt of NPV for the full year.

Now let me turn it over to Ed.

EDWARD FENSTER

Thanks, Bob.

Today I plan to address four topics:

- Our general approach to generating cash flow;
- Our interest rate strategy;
- Our near-term capital strategy and pipeline; and, finally,
- Changes during the quarter to Gross and Net Earning Assets.



Approach to generating cash flow

As Bob mentioned, we report average customer value for the quarter as “project value.” We turn project value into upfront cash by raising tax equity, project debt, and sometimes project equity, against these newly constructed solar systems. Tax equity primarily monetizes investment tax credits. Project debt and project equity monetize recurring cash flows. When the sum of customer upfront payments, rebates and these project finance items exceeds our overall cash expenditures, we generate cash. Net Earning Assets represents the overall estimate of the value expected to be received by Sunrun shareholders after servicing this project-level capital.

As shown on Slide 11, when we employ tax equity and project debt alone, we realize upfront roughly 90% of contracted project value. When we add project equity, we realize 95-100%. These numbers have remained stable over the last year despite an increase in long-term interest rates. This is because the strong performance of residential solar assets continues to deepen investor conviction in their high quality, lowering the spreads to US Treasuries that capital providers require. As such, overall capital costs are flat to improving slightly.

So far this year, we have amended three project debt facilities to lower debt costs, increase loan-to-value, extend maturities, and/or increase capital commitments. In one instance, we lowered the interest rate and increased the loan to value, resulting in both more proceeds upfront and more cash flow after debt service over time.

Despite these early accomplishments, we are hopeful we can do better yet in the second half of the year when we expect to pivot from the commercial bank market to the public debt markets. In the past, we have financed our assets principally with callable bank debt in anticipation that capital costs would decline. They have, and these call options are now valuable. We currently have about \$1 billion in callable debt that over 2018 and 2019 could see a reduction in cost of between 50 and 100 basis points overall. We are taking early steps to approach the public debt markets in a scalable fashion. For instance, in Q2 we closed an insurance policy -- as is customary in asset-backed-security transactions -- to insure, without deductible, the tax basis in most all of our existing assets, as well as those we expect to place in service over the coming several years.

Interest Rate Strategy

We believe we are well positioned related to interest rates. Although long-term interest rates have increased since the presidential election, the market no longer expects that trend to continue. The forward interest rate curve indicates that long-term interest rates that matter to our business will rise less than 10 basis points over the next three years. Meanwhile, as I mentioned earlier, the spreads we pay to Treasuries are declining.



If -- contrary to current market expectations -- long-term interest rates were to rise meaningfully, we note that there is a very strong historical correlation between growth in residential retail electric rates and interest rates. This correlation exists because most of the cost of residential electricity is the amortizing capital cost of transmission and distribution, rather than energy generation, and regulators customarily pass through to customers changes in utility capital costs. Increasing retail electric rates would allow us to raise customer pricing.

As to our existing assets, we typically lock-in interest rates using 18-20 year swaps. We also have used fixed-rate debt. Our swaps provide 18-20 years of interest rate protection even when individual credit facilities mature earlier. More than 80% of our expected debt service over the next 20 years is subject to swaps or fixed-rate loans.

Near-term capital strategy & pipeline

Switching gears to our upcoming capital strategy, we believe we will achieve the best possible execution by sequencing our transactions first in the public senior debt market; next, if applicable, in the subordinated debt market; and finally, to the extent desired, in the project equity market. As such, we wouldn't expect to execute a project equity transaction any earlier than Q4 of this year. This may concentrate cash generation in the fourth quarter of this year. We still don't expect to refinance into the public markets any seasoned assets -- meaning those operating for at least 5 years -- until early 2019.

Our capital commitments more than support our 2018 growth plans. We have tax equity capacity into 2019 and project debt capacity into Q4 of this year. We have now closed or signed term sheets for three tax equity financings since the new year at terms consistent with our previously-shared expectations.

Gross & Net Earning Assets

Finally, I turn to our installed asset base, as shown on Slide 12. Net Earning Assets rose 9% from Q4 to \$1.3 billion, reflecting a 20% year-over-year increase. Last quarter, I mentioned that the timing of cash receipts on tax and project equity financings impacted Net Earning Assets. Those timing issues have now resolved, but similar quarter-to-quarter variations may occur in the future.

Forward Looking Statements

This script contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act of 1995, including statements regarding our future financial and operating guidance, operational and financial results such as growth, value creation, MW deployed, estimates of gross and net earning assets, project value, estimated creation costs and NPV, and the assumptions related to the calculation of the foregoing metrics, as well as our expectations regarding our growth and financing capacity and our strategic partnerships with



National Grid and Comcast. The risks and uncertainties that could cause our results to differ materially from those expressed or implied by such forward-looking statements include, but are not limited to: the availability of additional financing on acceptable terms; changes in the retail prices of traditional utility generated electricity; changes in policies and regulations including net metering and interconnection limits or caps; the availability of rebates, tax credits and other incentives; the availability of solar panels and other raw materials; our limited operating history, particularly as a new public company; our ability to attract and retain our relationships with third parties, including our solar partners; our ability to meet the covenants in our investment funds and debt facilities; and such other risks identified in the reports that we file with the U.S. Securities and Exchange Commission, or SEC, from time to time. All forward-looking statements in this script are based on information available to us as of the date hereof, and we assume no obligation to update these forward-looking statements.