Sunnova Energy International

First Quarter 2022 Earnings Prepared Remarks

Operator:

Good morning and welcome to Sunnova's first quarter 2022 earnings conference call. Today's call is being recorded and we have allocated an hour for prepared remarks and question and answer. At this time, I would like to turn the conference over to Rodney McMahan, Vice President, Investor Relations at Sunnova. Thank you. Please go ahead.

Rodney McMahan:

Thank you, operator. Before we begin, please note during today's call we will make forward-looking statements that are subject to various risks and uncertainties that are described in our slide presentation, earnings press release, and our 2021 form 10-K. Please see those documents for additional information regarding those factors that may affect these forward-looking statements.

Also, we will reference certain non-GAAP measures during today's call. Please refer to the appendix of our presentation as well as the earnings press release for the appropriate GAAP to non-GAAP reconciliations and cautionary disclosures.

On the call today are John Berger, Sunnova's Chairman and Chief Executive Officer and Robert Lane, Executive Vice President and Chief Financial Officer.

I will now turn the call over to John.

John Berger:

Good morning and thank you for joining us.

Despite persistent macro-economic headwinds, we made excellent progress against our financial goals for the year by posting strong first quarter results, a summary of which can be found on slide 3. On our previous earnings call, we noted that we expected to capture approximately 12% of our full-year 2022 Adjusted EBITDA, combined with the principal and interest we collect from solar loans in the first quarter. I am happy to report we exceeded that target, as actual financial results were ahead of that goal. While our expenses have increased in total, they have been in line with our expectations, and are necessary at this stage in our evolution to take full advantage of the incredible array of profitable growth opportunities that we increasingly find in front of us. Many of these growth opportunities are not baked into the Triple-Double Triple plan.

Slide 4 summarizes the growth in Sunnova's customers, battery penetration, and dealer network.

In the first quarter of 2022, we added approximately 15,300 customers, an increase of 74% compared to the first quarter of last year. As in prior years, we expect our customer additions to escalate throughout the calendar year and we still expect to meet our full-year 2022 customer additions guidance of 85,000 to 89,000.

In addition to the strong demand for our solar services, we are also experiencing accelerating demand for energy services beyond solar. This includes increased demand for energy services such as, batteries, electric vehicle charging, generators, and load managers, and includes sales to both new and existing customers. We are also seeing a surprising surge in demand from our customers to "up-power" or increase their solar generation capacity with us. It is the rise in these types of ancillary services that is positioning Sunnova to realize the full option value of its customers. While this activity will not increase our unique customer count, it will increase our services per customer, and in turn our Net Contracted Customer Value or NCCV on a per customer basis, moving

us closer to our target of $18,000 to $20,000 in NCCV per customer by the end of 2025. As of March 31, 2022, our NCCV per customer was nearly $10,800.

To properly account for this change in customer appetite, and to ensure we have an accurate and honest customer count, we recently deployed new software to analyze our customer data. This analysis resulted in a reduction in our total customer count of fewer than 3,000 customers from what we reported as of December 31, 2021. This adjustment was driven by a tightening of our customer definition to ensure only homeowners with whom we have an ongoing economic relationship are counted as customers and are counted only once, regardless of the number of services we provide to them. This reduction was not specific to any one period but rather was blended across the decade Sunnova has been in business, and most importantly did not result in any loss in NCCV or require any modifications to previously issued guidance for 2022 or 2023.

Additionally, installing these new stringent customer definitions will allow us to more accurately track, on a per customer basis, the value being created through "up-powerings" that typically coincide with the addition of one or more new energy services. It was these previously "up-powered" customers that drove this customer count adjustment.

Management is focused on increasing cash flow per share by driving up value on a per customer basis as well as growing its overall customer base. We understand that there is unfortunately little consistency in non-GAAP metrics in the residential solar industry. Since Sunnova has gone public, we continue to try to increase transparency and disclosure across the industry. As a result, we know that our definition of a customer is more conservative than that of some of our peers, but our customer definition gives management and stockholders an accurate way of determining value creation. We strongly encourage

investors to make sure all residential energy service providers use the same or a similar customer definition.

Our battery attachment rate on origination for the first quarter of 2022 was 19%. This drop in our battery attachment rate was unexpected but was a timing issue as over the last 30 days our battery attachment rate on origination has been 29%. The first quarter timing issue was driven by a surge in sales from Sunnova New Homes and the northeast region and a delay in our under-writing processing caused by the huge sales volumes in March. Much more importantly, as our battery supply improved as planned, our battery penetration rate continued to grow and reached 12.5% as of March 31, 2022, this is inclusive of over 1,900 battery retrofits we have installed life to date.

Our growth continues to be driven by our rapidly expanding dealer network which as of March 31, 2022 stood at 915 dealers, sub-dealers, and new homes installers. We expect to eclipse our year-end 2022 target of 1,000 dealers in the coming months.

Finally on slide 4 we have updated our information on customer contract life and expected cash inflows. As of March 31, 2022, the weighted average contract life remaining on our customer contracts equaled 22.3 years and expected cash inflows over the next twelve months has increased to $403 million.

Earlier in the month, we published our second annual ESG report, detailing the steps we have taken over the last twelve months to enhance our ESG strategy and reporting. Our new report, titled "Charging Ahead", describes the impact of the growth we have seen this year and how we are integrating ESG best practices into our core business to drive positive outcomes for our business and society.

Building off our first report last year, our next step was to establish a more formal forward-looking strategy. To start this process, we conducted a materiality assessment to identify the ESG topics that

were most important to our business and to our stakeholders. We engaged our employees, investors, community partners, vendors, and other groups to assess ESG-related topics. From this assessment, we identified nine priority ESG topics for our business, as well as others that we consider material. The results of this assessment can be found in our new report.

With our priority topics defined, we engaged leaders from across our organization to ensure strong oversight of these topics and to develop multi-year goals to drive progress. These goals also complement our Triple-Double Triple growth strategy whereby our planned growth in our customer base will allow us to offset 52 million metric tons of CO_2 by year-end 2023.

Finally, we also made progress in enhancing our ESG data and aligning it with leading reporting frameworks. In 2021, we aligned our reporting with the Task Force on Climate-Related Financial Disclosures, or TCFD, reporting guidelines. This was an important step in demonstrating our commitment to climate action as a leading energy company. To continue our alignment with TCFD recommendations, our goal is to complete a Scope 3 inventory for all material categories and to set formal climate targets by year-end 2023. We will also be working to conduct climate scenario analysis to better assess climate risks and opportunities for our business. We look forward to sharing these results in future reports.

Our team is pleased with the progress we have made to date and look forward to continuing to integrate ESG into everything we do. I encourage you to read our new report, which can be found on the ESG section of our investor relations website, and we welcome any questions or engagement on our current strategy.

I will now hand the call over to Rob.

Robert Lane:

Thank you, John.

Slide 8 summarizes our recent financing activity and liquidity position.

The 2022 financing transactions completed to date include $150 million in tax equity funds as well as a well-timed $298 million securitization closed in late February with a blended coupon of 3.1%.

Our total liquidity as of March 31, 2022 was $703 million, down from $831 million as of December 31, 2021, but up from $276 million as of March 31, 2021. This planned utilization of liquidity was driven primarily by the seasonality of cash flows and the expected increased requirement for working capital due to growth.

Included in these numbers are both our restricted and unrestricted cash, as well as the available collateralized liquidity we could draw upon from our tax equity and warehouse credit facilities. Given available unencumbered assets as of March 31, 2022, this available collateralized liquidity equaled $378 million. Beyond that, subject to available collateral, we had $423 million of additional capacity in our warehouses and open tax equity funds. That represents over $1.1 billion of liquidity available exclusive of any additional tax equity funds, securitization closures, or warehouse expansions later this year.

On slide 9 you will see our fully burdened unlevered return on new origination was 9.2% as of March 31, 2022, based on a trailing twelve months. While our returns increased from last quarter, so too did our cost of debt, resulting in an anticipated reduction in our implied spread to 6.0%. As we have discussed before, we model a long-term average for our implied spread in the 500-basis point range to estimate our guidance targets.

As we mentioned on our last earnings call, we and our dealers have been, and will continue to, increase pricing to offset the increased cost of

capital. Taken together, these price increases, the youth of our industry, our increasing operating leverage, and our continued growth in additional energy services will keep margins wider in the near term and position the company to push our implied spread back towards the 600 basis points range this year. As to the progress of these price increases, you can see our first quarter fully burdened unlevered return increased from the prior quarter, and we expect further improvement in Q2.

Slide 10 contains both our Gross Contracted Customer Value, or GCCV, and NCCV. In just three years' time NCCV went from $968 million as of March 31, 2019, to $2.2 billion, or $19.67 per share, as of March 31, 2022.

As we discussed in the Q&A last quarter, regardless of what the proper discount rate may be, NCCV is still a punitive way to view Sunnova's blow-down value and gives us zero value for our platform, customer option value, or growth. Remember, NCCV only includes locked in contractual cash flows and thus excludes any value for growth, renewals, upsells, up-powerings, state or national incentive appreciation, or other upside.

Another way to view NCCV, and why we continue to believe a 4% discount rate is justified, is to look at the undiscounted cash flows. That is, net the nominal cash inflows generated by the contracted energy services we provide against all debt principal, interest expense, tax equity distributions, estimated service costs, and even an estimate for defaults based on current actuals. This full residual cash flow view pencils out to approximately $2.8 billion as of March 31, 2022, which is approximately a 25% premium over our $2.2 billion NCCV estimate.

While investors are understandably concerned about rising interest rates, we encourage you to keep three things in mind. First, the interest expense of our existing debt is locked in, and we do not have any scheduled maturities on our corporate debt until 2026. Second, we have

managed and will continue to manage our fully burdened unlevered returns with a view towards offsetting increased interest rates. Third, our ability to increase unlevered and levered returns is high, driven by the increase in the utility rates, which is our primary competition. But no matter what discount rate one uses in their valuation the fact will remain Sunnova has retained more value, originates assets more profitably, and is accelerating the acquisition of long-term cash flows more quickly than any other company in the industry. As such, we can profitably invest to further increase growth or return capital to shareholders.

We maximize shareholder value through balancing customer growth with healthy margins, increasing services sold per customer, maximizing the amount of power sold to customers, and minimizing losses of contractual cash flows from customer defaults. Sunnova is a technology enabled service business, or a wireless power company, focused on providing customers a better energy service at a better price giving them every reason to pay us for that essential service.

Currently over 10% of our customer base is paying less than half than they would to their monopoly utility for the energy they use to power their homes by being a Sunnova customer due to significant increases in their utility rates. We expect that percentage could reach as high as 50% of our customer base as early as next year as utilities continue to ask for massive rate increases. This, together with our industry-leading customer service, has resulted in default and delinquency rates that are the lowest among our peers in an industry that is already the lowest of any major consumer asset class.

Beginning on slide 12 through slide 14 you will find our guidance that includes our detailed 2022 guidance, liquidity forecast, and our major metric growth plan, the Triple-Double Triple Plan. There are no changes to these estimates as we are keeping our targets unchanged from where they were in our last earnings call.

As of March 31, 2022, approximately 90% and 70% of the mid-points of our 2022 and 2023 targeted revenue and principal and interest we expect to collect on solar loans was locked in through existing customers as of that same day, respectively. This visibility is what gives us comfort in reaffirming our guidance today.

I will now turn the call back over to John.

John Berger:

Thanks, Rob.

Changing consumer energy demands, global security issues, and climate change are creating an urgency to transform the global energy industry. To aid in this critical evolution, we are embracing an equitable, practical, and balanced energy future by providing homeowners the affordable, reliable, and sustainable energy they need.

To ensure Sunnova is the energy service provider homeowners choose to power their energy independence, we will continue to distinguish ourselves by focusing on what differentiates us from the competition - a combination of service, software, and aggregation.

At Sunnova we strive to provide our customers with a superior energy service, one that is more reliable and more affordable than the competition, including the centralized utilities.

Enabling our ability to provide this best-in-class service is our substantial investment in software for dealers, customers, and for aggregation. Some of these software investments automate functions and displace the need for additional hires and increase the productivity of employees and dealers to serve our rapidly expanding customer base. Providing the level of service required for this industry is a significant technological, logistical, and operational undertaking and one that can only be managed by utilizing a next generation software platform. Our

software platform together with our logistics capabilities, supply chain management, billing and collections team, and efficient customer operations, all performed in-house by Sunnova employees, provides us with tremendous operating leverage and a huge advantage over our peers.

It is this combination of software and service that enables aggregation. As we obtain an increasing amount of scale, we can better utilize this combination to enable certain aggregation capabilities which creates additional value for both our customers and Sunnova. Currently, we have multiple grid service programs in place with an estimated contracted revenue of $79 million over the next 20 years, with even more programs in the pipeline to expand that amount.

Bringing these competitive moats together fulfills our expansive, customer-centric vision for the future. With the Sunnova Adaptive Home™, we can provide an energy service offering that integrates solar power, battery storage, secondary generation, roofing, electric vehicle charging, energy and control management technologies, emission credit management, and more to give customers unparalleled energy capabilities and reliability for their homes. We see the Sunnova Adaptive Home™ as the core vision that fulfills the concept of No Net Metering Needed and drives our growth in both absolute terms and on a per customer basis. After almost a decade of building out our service capabilities, we are well positioned to take advantage of the opportunities ahead of us as we help build the home of the future for our customers through continued execution and by making the Sunnova Adaptive Home™ a reality.

With that, operator, please open the line for questions.