Sunnova Energy International

Fourth Quarter and Full Year Ended 2023 Earnings Prepared Remarks

Operator:

Good morning and welcome to Sunnova's fourth quarter and full year 2023 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 as described in our slide presentation, earnings press release, and our 2023 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.

2023 proved to be a formidable test for the residential solar industry. Macro-economic challenges and a rapidly evolving landscape meant that companies who were unable to adapt and tackle these challenges head-on have struggled or exited the market.

While this unfortunate reality for some may have caused apprehension and generated negative headlines, it also presents a silver lining of reduced competition for adaptable companies like Sunnova. We stand apart in this regard, fortified by our scale, robust balance sheet, agility, and forward-thinking approach, enabling us to not only weather the storm but pick up market share and expand margins in the process.

The past few weeks we have seen encouraging signs of improved market dynamics beginning to emerge. Tighter risk premiums reflected in our recent securitizations, coupled with an uptick in overall market demand as we transition beyond the seasonally softer period for customer originations, paints a more optimistic picture than many perceive.

To better position Sunnova for the rest of 2024 and beyond, we have continued to increase our focus on cash generation by pursuing additional margin expansion, exploring potential asset sales, and rapidly implementing cost-cutting measures.

To achieve cost savings, we are continuing to implement a range of initiatives, primarily focused on automation-driven efficiencies. This strategic approach will enable Sunnova to sustain growth without expanding its headcount. Additionally, we have initiated an immediate pause in spending related to select growth initiatives, such as international expansion.

While these initiatives are temporarily on hold, we will remain committed to revisiting them in the future, contingent upon improved market conditions and an improved valuation of Sunnova's equity.

Factoring in these cost reductions, we now anticipate our revised cost structure will result in a decrease of at least 20% in total Adjusted Operating Expense per customer in 2024.

Slide 3 highlights our growth in customer count, power generation and energy storage under management, battery penetration, and expected contracted cash inflows for both 2024 and the remaining life of our customer contracts.

During the fourth quarter, we placed over 34,000 customers into service, which brought our total customer count at the end of 2023 to just over 419,000 and our megawatt hours and solar power generation under management to 1,090 megawatt hours and 2.5 gigawatts, respectively.

Turning to slide 4 you will see, as of December 31, 2023, the expected cumulative nominal contracted cash inflows associated with our customer contracts, over a weighted average remaining life of 22 years, was $16 billion. In 2024 these same contracts are expected to generate $789 million in contracted cash inflows. These inflows are the sum of all expected cash generated from customer lease, PPA, and loan contracts, including those from SRECs and grid services, in-service as of December 31, 2023.

Also on this slide, we provide our expectations of Levered Cash Flows, which, based only on what was securitized as of December 31, 2023, is expected to be $136 million in 2024 and $4.9 billion on a cumulative nominal basis. Cumulative Levered Cash Flows will continue to grow as new assets are added and will grow on a per annum basis as tax equity flips occur and debt is paid down.

I will now hand the call over to Rob, who will walk you through our financial highlights.

Robert Lane:

Thank you, John.

Starting on slide 6, you will see our Adjusted EBITDA together with interest income and principal proceeds equaled $549 million for the year ended 2023, which included a $207 million contribution from Investment Tax Credit or ITC sales.

Excluding ITC sales, 2023 Adjusted EBITDA, together with interest income and principal proceeds, increased by $58.5 million versus the prior year. Since most expenses flow through Adjusted EBITDA, including those that support our loan business, we view Adjusted EBITDA together with interest income and principal proceeds as a more complete picture of our financial performance.

While 2023 ITC sales were heavily back-end weighted due to delayed treasury guidance, we expect a more even contribution of this activity in 2024 as we plan to continue utilizing ITC transferability, primarily from new tax equity partnerships, to diversify our funding sources.

Slide 7 highlights Sunnova's continued ability to efficiently access the capital markets.

In 2023 we added $957 million in additional tax equity funds, entered into over $1 billion in asset backed securitizations, closed a $50 million secured revolving credit facility to support procuring and selling inventory to dealers, closed a $65 million accessory loan facility, and issued a second green bond which, together with a modest equity offering, brought in $466 million in additional capital after fees and expenses. We also expanded our warehouse capacity while securing amendments to keep pace with our origination.

Through February 21st of this year, we have added another $195 million in tax equity and priced two asset securitizations at the tightest spreads we have seen in the past 12 to 18 months.

In our $537 million of liquidity as of December 31, 2023, are both our restricted and unrestricted cash and the available collateralized liquidity we could draw upon from our tax equity and warehouse credit facilities.

Subject to available collateral, we had $835 million of additional capacity in our warehouses and open tax equity funds. Combined, these amounts represent nearly $1.4 billion of liquidity available exclusive of any additional tax equity funds, securitization closures, asset sales, in the money interest rate hedges, further warehouse expansions, or other sources of liquidity during the year.

On slide 8 you will find a summary of our unit economics. As of December 31, 2023, on a trailing twelve month basis, our fully burdened unlevered return on new origination increased to 12% while our weighted average cost of debt decreased to 6.4%, respectively. This resulted in a 5.6% implied spread over the same period, the highest since early 2022.

Slide 9 provides additional information on our unit economics, which have improved and continue to improve into 2024. We now estimate an implied spread on near-term origination of 600 basis points. Overall, our margins have remained stickier than expected considering the declines we have seen in the weighted average cost of debt. However, we maintain that the long-term expected spread is 500 basis points.

Our weighted average cost of debt, life to date, remains just over 5% as of December 31, 2023. As a reminder, we measure our cost of capital on a yield-at-issue basis, rather than an interest rate basis, as this more fairly captures the effects of any discounts, fees, and capped call purchases.

Slide 10 reflects the strong growth we have seen in our Net Contracted Customer Value, or NCCV. At a 6% discount rate, NCCV was $3.1 billion, an increase of 35% compared to December 31, 2022. Our December 31, 2023 NCCV at this discount rate was $25.26 per share. This represents a greater than twofold increase since we announced our Triple-Double-Triple plan.

Even with this significant increase, our NCCV per share ended the year lower than expected primarily due to the timing of tax equity closures and fourth quarter customer additions coming in slightly below our expectations.

At this time, we have elected to reaffirm our 2024 full year guidance found on slide 12. We will reassess our guidance next quarter once our lower cost structure has had more time to operate.

We expect to capture approximately 15% of our 2024 Adjusted EBITDA together with interest income and principal proceeds in the first quarter, increasing to approximately 20% in the second quarter, 30% in the third quarter, and 35% in the fourth.

Customer additions are expected to be more backend weighted with 15% in the first quarter, 25% in the second quarter, and the balance evenly distributed over the second half of the year. This is mainly due to our new channels as well as growth in accessory and service only sales. Thus, the backend weighting will be more driven by accessory loan and service only customers.

As of December 31, 2023, 90% of the mid-point of our total 2024 targeted customer revenue, interest income, and principal proceeds was locked in through existing customers as of that same day, respectively.

We have updated our liquidity forecast for 2024 and are introducing guidance for 2025 and 2026, which can be found on slide 13. We now expect to generate enough cash in 2024 to provide the working capital needed to hit our growth target for the year while keeping our cash position relatively flat. This will be accomplished through a combination of securitizations and sales, net of operating

costs. As we exit 2024, we expect to achieve an annual run rate of cash generation between $200 million and $500 million. This significant increase in cash generation beyond 2024 is a reflection of our pricing changes, and can further be enhanced towards the top end of the range through improvements in treasury rates, ever tightening risk premiums, and final domestic content guidance.

We are electing to sunset our Recurring Operating Cash Flow metric in favor of Levered Cash Flows in response to investor inquiries around not just the cash flows from in-service and securitized assets but a desire to see the value and costs of our superior customer service model. Levered Cash Flows is the sum of expected residuals from all securitized lease, PPA, and loan contracts, plus all MSA fees, plus expected cash inflows from unpledged SRECs and grid services.

As John noted earlier, we have continued to focus on cost reductions. However, one area that will continue to retain its investment is our collections department to ensure we are maintaining our low per annum capital loss rate, which is unchanged at approximately 25 basis points.

Finally, while we forecast no need for corporate capital through 2026, for good housekeeping purposes we will be putting in place a modest $100 million ATM in the coming weeks and will update the market every quarter of any anticipated usage. We have discussed this ATM before, and to be clear, we do not intend to utilize the ATM between now and our next earnings call. The best time to put tools like an ATM in place is when they are, in fact, a luxury and not a necessity.

I will now turn the call back over to John.

John Berger:

Thanks, Rob.

Sunnova is committed to delivering a comprehensive, sustainable, and streamlined approach to energy financing, servicing, and management for our customers. We are an adaptive energy services

company that has an unwavering focus on innovative technologies, integrated energy solutions, and quality control as evidenced by our investments in our Global Command Center and our Adaptive Technology Center - both designed to optimize our operations and provide our customers with a strong customer experience.

In a world where perceptions are manipulated, we know there are people selectively crafting narratives that paint a picture that is far from the truth, but we stand firm in our commitment to focus on transparency and integrity, choosing to focus on the facts. For example, on Slide 15 you will see as of December 31, 2023 only 0.6% of our customers had an escalated concern, an improvement from 1.1% at the end of 2022. Moreover, in 2023 we saw an 80% improvement in our service response time as the average age of a closed work order went from 96 days as of December 31, 2022 to 19 days as of December 31, 2023. This marked improvement was driven by our investments in our customer service infrastructure which enhanced and strengthened our customer service levels and capabilities.

2024 will be a year of continued growth and transformation for Sunnova, with a continued emphasis on cash generation as a top priority. To accomplish this, in addition to expanding margins and the more aggressive cost reductions we mentioned, we will look to leverage asset sales as a more meaningful source of cash generation coupled with increasing our long-term Levered Cash Flows.

Our commitment to prudent capital management and shareholder value creation remains unchanged. We remain dedicated to evaluating ways to deploy our capital, with an emphasis on both maximizing returns on capital and exploring opportunities to make returns of capital. Over time, we will continue to evaluate the optimal allocation of our capital resources and will not hesitate to take advantage of attractive opportunities in the capital markets and in our rapidly changing industry.

As we look to the remainder of 2024, we are excited about what we are seeing. While there is no denying that what we are doing is difficult; at the end of the day we are transforming the energy landscape,

challenging the status quo, and offering customers greater choice to help meet society's ever-increasing energy demands.

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