



## **Q4 2017 Earnings Call**

**March 6, 2018**

### **Prepared Remarks**

#### **Forward Looking Statements**

Thank you operator, and thank you to those on the call for joining us today.

Before we begin, please note that certain remarks we will make on this conference 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 Lynn Jurich, Sunrun's co-founder and CEO, Bob Komin, Sunrun's CFO, and Ed Fenster, Sunrun's co-founder and Executive Chairman.

The presentation today will use slides which are available on our website at [investors.sunrun.com](http://investors.sunrun.com).

And now let me turn the call over to Lynn.

#### **LYNN JURICH**

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

In the fourth quarter we deployed 85 MWs generating \$91 million dollars of net present value, up 35% percent year-over-year. We created NPV per watt of \$1.22, the highest margin in the company's history, highlighting our cost efficiencies and the value of our products. We are now solidly the market leader in the residential sector.

#### **2017 Year in Review**

Q4 caps a breakout year for Sunrun - In 2017 we beat both our full-year NPV margin and cash generation targets. We grew aggregate NPV at almost 50%, deployments at 15% and now have more than 180,000 customers. We gained 4 percentage points of market share while turning structurally cash flow positive,



and we expanded our home solar and battery service, Brightbox, to strong customer reception. We also forged key strategic partnerships with Comcast and National Grid.

### **Summary & 2018 Outlook**

We expect an even better 2018 despite the impact of tax reform and tariffs. We plan to continue our market share gains with 15% growth in deployments and growth in cash generation well above this rate. These results are supported by NPV targets above a \$1/watt and a strong project finance pipeline to turn that value into cash flow.

In the immediate term, we have experienced some external headwinds. Q4 deployments fell slightly short of our expectations due to the wildfires in California.

Q1 is always the toughest quarter of the year. Typically, deployments decline from Q4 levels due to seasonality and the pull-forward in installations from Arizona exacerbated the trend this year. We took a particularly cautious position in Q4 given the unknowns from tax reform and the tariff, but are pleased with where margins have settled out and that the uncertainties are removed. Because of this prudence, we will be able to slightly grow aggregate NPV year-over-year in Q1 but the MW deployment comparison won't reflect the annual growth trend. This means for the rest of the year MWs deployed will grow at about 20% and we expect to approach that number in Q2 with a slightly stronger second half.

We are focusing on our direct business to develop our Comcast partnership and the launch of Brightbox. Although, neither of these are contributing meaningfully to deployments today they will be larger contributors in the second half of the year. The Comcast partnership is on track and we are experimenting to refine our messaging, offer packages, and marketing mix before we unleash broader campaigns.

### **Beyond 2018**

As we've noted before quarterly fluctuations due to the timing of various policy impacts have been the norm over the past 10 years. Most importantly, the foundation is strengthening for Sunrun's sustained long-term growth and market leadership.

The US electricity sector is undergoing dramatic change. Renewable energy and natural gas prices have plunged and demand for electricity is stagnant. Yet, U.S. utilities are on a capital spending binge. That's why during this period of unprecedented declines in the cost of fuel, retail electricity price escalation in our markets has continued to increase at 3% per year for the past 14-years. Even if wholesale prices go to zero, there will be no place to hide and rate escalation will accelerate. Regulators are recognizing the danger of staying on this spending spree and building 30-year infrastructure we won't need in 10 or even



5 years. We already have utilities asking for bailouts of large nuclear and coal plants for which homeowners are forced to pay.

The solution is to increase efficiency of the system while moving to cleaner generation. Distributed solar and batteries can be more flexible, targeted, and offer consumers control and savings. It is what people want and it's the next generation energy system, not yesterday's expensive, bulky, centralized one.

Here is an example of how it works and why residential assets are the unique solution: utilities identify a circuit that is going to need a substation overhaul. Sunrun can aggregate the batteries from about 500 homes in that exact neighborhood and supply energy to the grid when needed. This replaces a multi-million dollar investment. It's a win-win because those households also get to have solar power and a battery, which provides power during outages and offers control over energy costs. We can both help our customers save money and lower prices for the entire electric system. The number of RFPs for these opportunities are growing swiftly.

We have partnered with National Grid to pursue these grid services efforts. We don't expect them to have a 2018 revenue impact but they are foundational efforts for our strategy to build a consumer-centered energy system. We note that the top 20 utilities currently have an aggregate market cap of \$500 billion. Our customer-created utility can be on this list.

The pace of home battery adoption is surpassing our expectations. Today we announced our Brightbox launch in Massachusetts. At just \$1,000 upfront Brightbox is a fraction of the cost of the alternative - dirty, noisy diesel generators.

Year to date in California, nearly 20% of the time our customers are now choosing to add batteries. This has almost doubled again since Q4, and we expect further penetration throughout the year.

Our massive and growing base of more than 180,000 customers remains our largest strategic asset. We aim to differentiate through the best customer experience at the initial interaction and for decades to come.

I'll now turn the call over to Bob Komin, our CFO, to review Q4 performance and discuss guidance in more detail.

**BOB KOMIN**

Thanks, Lynn.



In the fourth quarter, we recorded the highest NPV per watt in the company's history and exceeded our cash generation and NPV targets.

### **NPV**

NPV was \$1.22 per watt in Q4, resulting in aggregate NPV created of \$91 million, representing 35% growth compared to the prior year.

While NPV per watt can fluctuate from quarter to quarter given business mix, Q4's strong results highlight our leading position and our continued focus on managing the business to drive NPV. We are particularly pleased with the unit economics we achieved this quarter, especially as we invest resources in additional product offerings such as Brightbox, grid services initiatives with National Grid, and in new market entries.

We calculate NPV as Project Value less Creation Costs so let's go through the components.

### **Project Value**

Q4 project value of \$4.52 per watt was 3 cents higher than Q3 and 11 cents higher than last year.

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. As Ed will describe, we expect the impact of tax reform to reduce Project Value by about \$0.10/watt beginning in 2018.

### **Creation Costs**

Turning now to Creation Costs on Slide 13.

In Q4, total creation costs were \$3.30 per watt, an improvement of \$0.11, year-over-year. Similar to Project Value, creation costs can fluctuate quarter to quarter due to changes in geographic and channel mix.

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 \$0.10 or 4%, year-over-year to \$2.61 per watt.

Install costs for systems built by Sunrun were \$1.85 per watt, reflecting a 19 cent, or 9%, year-over-year improvement. Sunrun built installation costs increased modestly from Q3, owing primarily to higher mixes



in strategic growth areas including our Brightbox solution, and new markets which tend to initially have higher costs over a few quarters while we are scaling.

We expect total installation costs to show modest declines by the end of the year even with the module tariff impact and as we continue to invest in new geographies and grid services. We also expect the attachment rate of home batteries to continue to increase, which carries a higher per-watt cost, but also delivers higher NPV.

In Q4, our sales and marketing costs were \$0.53 per watt, an 8% improvement from the prior year, driven by channel mix and our focus on the most cost effective customer acquisition channels.

For the full-year 2017, G&A costs were \$0.30 per watt, flat compared to 2016. We expect to realize further operating leverage in the long-term, with volume growth exceeding G&A cost increases over time although there can be quarterly fluctuations.

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 \$0.15 per watt, flat with the prior quarter and prior year.

### **Deployments**

In the fourth quarter, deployments increased 10% year-over-year to 85 MW. For the full year, we deployed 323 MWs, 1% below our guidance of 325 MWs.

There were several factors that influenced this, most notably the natural disasters in California during Q4. The fires in both northern and southern California not only disrupted the specific areas affected by the fires, but also caused extremely poor air quality conditions for the broader region. The safety of our crews is paramount, and we did not want our crews from the six affected branches installing during unhealthy conditions. I think this was absolutely the right call for us - and many of our partners - to make. We did our best to try to make up this gap later in the quarter, and in other geographies, but were unable to fully mitigate the impact.

Our cash and third party loan mix was 13% in Q4, in-line with recent levels and the prior year, 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 Q4 with \$242 million in total cash - including restricted and unrestricted cash - the tenth consecutive quarter we have been above \$200 million. We generated \$43 million in total cash in 2017 on a normalized basis, exceeding our target of \$40 million. This excludes about \$20 million in accelerated inventory purchases as a partial hedge for the module tariff, along with the \$9 million payment in Q2 for the lead-generation business we acquired in 2015, as I mentioned on the last call.

We define cash generation as the change in our total cash balance after subtracting the change in our working capital recourse debt facility. We estimate our cash generation will grow materially faster than our deployments in 2018. As the year progresses we will be in a better position to be more specific with our cash generation and net earning asset outlook. 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.

### **Guidance**

Moving on to guidance on Slide 15.

We remain confident in our growth trajectory and are guiding to 15% deployment growth for the full-year.

In Q1 we expect to deploy 67 MWs, consistent with the historic seasonal patterns in our business and driven by some market-specific timing. As we pointed out over the last few quarters, we saw strong demand in Arizona ahead of policy changes, which caused some demand pull-in that results in tougher sequential and year-over-year comparisons in early 2018. This means beyond Q1 MWs deployed will grow at about 20%, and we expect to approach that number in Q2 with a slightly stronger second half.

We are also focusing on our direct business, which is the platform behind the Comcast partnership volume ramp and where we have focused our Brightbox sales and installation efforts, and both will be larger contributors in the second half of the year. The increased adoption of Brightbox is exciting given the additional customer value propositions and differentiation, but as markets launch it also carries longer cycle times. As I mentioned earlier, despite the headwinds from tax reform and the import tariffs, we expect to maintain our unit economics at or above our target of \$1.00 per watt of NPV for the full-year, testament to Sunrun's competitive position, operational and NPV discipline, investment in advanced products, and strong financial market execution.

Now let me turn it over to Ed.

**EDWARD FENSTER**



Thanks, Bob.

Today I want to touch on three items.

- First, I will review the changes during the quarter to Gross and Net Earnings Assets;
- Second, I will discuss the impacts of tax reform; and
- Third, I will discuss the finance market, which is the most robust we've seen in the Company's history;

### **Gross & Net Earning Assets**

Turning first to our installed asset base on Slide 16, Net Earning Assets was roughly flat in the quarter at \$1.2 billion, reflecting a 16% year-over-year increase.

Non-recurring items of about \$50 million depressed net earning assets in the quarter.

First, we experienced impacts in the draw timing of tax and cash equity financings. Our primary objective is to optimize for the lowest long-term cost of capital. We focus first and foremost on the best execution of our financings, which can materially affect the timing of our total cash balance at any specific quarter-end measurement date.

Second, we have estimated the total expected impact of corporate tax reform.

Finally, we purchased tax equity investors' stakes in a couple early and unusual funds, allowing us to retire our most expensive piece of debt and placing us in position to execute refinancings on advantageous terms in the ABS market.

In addition, the net cash proceeds from the closing of a term loan B in Q4 reduced net earning assets, but generated cash. Because we reinvested this cash into working capital, such as inventory to hedge the solar panel tariff, we have not yet seen the corresponding increase in cash. We expect working capital investment will peak in Q1.

### **Tax Reform**

I turn now to a discussion of federal tax reform and the impacts to Sunrun.

Most importantly, the Investment Tax Credit was unchanged, which is no surprise given the bipartisan support for solar. In fact, Congress newly extended tax credits for several renewable energy technologies in the budget bill that immediately followed tax reform.

For the existing fleet of assets, we estimate that all changes from tax reform, taken together, will reduce Gross Earning Assets by about \$13 million, or less than 1%. Tax reform also resulted in a \$33 million



GAAP benefit, reducing our Q4 income tax provision. Because we enjoy a tax net operating loss carry forward of \$700 million, this benefit, like our overall income tax provision, is non-cash.

We continue to see strong availability of tax equity. Based on a transaction we signed up after tax reform, as well as ongoing discussions, we estimate that proceeds from tax equity transactions will decrease by about 10 cents per watt, slightly better than our prior guidance. This reduction occurs because the depreciation we deliver to tax equity investors is less valuable at a lower corporate income tax rate.

Despite impacts to project value from tax reform and to cost from tariffs, we believe we can generate a strong NPV of at least \$1 per watt in 2018 as a result of continued operational improvements and our strong competitive position.

### **Project Finance Environment**

I turn now to my final topic, project finance and capital markets strategy.

As always, we continuously consider options to balance our goals of maximizing long-term equity returns with delivering upfront cash flow, while minimizing our exposure to changes in base interest rates.

Based on the increasing acceptance of the residential solar asset class, and overall strong market conditions, we see opportunity to reduce our capital costs in 2018, both on new and existing debt transactions. Across all components of our capital stack, current market conditions support spreads that are 50-100 basis points lower than our average 2017 transaction. Based on market conditions today, we expect in 2018 to continue to deploy a mix of subordinated, or term loan B, debt, and cash equity financing.

Finally, I note we have tax equity and back-leverage capacity into Q3 of 2018, including tax equity which was negotiated in 2018, after tax reform. We are pleased with overall project finance conditions and our relative position.

I'll now turn the call back to Lynn.

### **LYNN JURICH**

Thanks Ed.

Let's open the line for questions please.

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## **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 bookings and deployments, 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.*