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Vivint Smart Home, Inc. (VVNT)

Q2 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon. Thank you for attending today's Vivint Smart Home, Inc. Second Quarter 2022 Financial Results Conference Call. My name is Bethany and I will be your moderator for today's call. All lines will be muted during the presentation portion of the call with an opportunity for questions and answers at the end. [Operator Instructions]

I would now like to pass the conference over to our host, Nate Stubbs, VP of Investor Relations at Vivint Smart Home. Please go ahead.

Nate Stubbs
Vice President-Investor Relations, Vivint Smart Home, Inc.

Good afternoon, everyone. Thank you for joining us to discuss the results of Vivint Smart Home for the three months ended June 30, 2022. Joining me this afternoon are David Bywater, Vivint Smart Home's Chief Executive Officer; and Dana Russell, Vivint's Chief Financial Officer. Also in the room today are Rasesh Patel, COO; and Nitin Abraham, SVP of Finance.

I would like to begin by reminding everyone that the discussion today may contain forward-looking statements, including with regard to the company's future performance and prospects. Forward-looking statements are inherently subject to risks and uncertainties that could cause actual outcomes or results to differ materially from those indicated in any such statements. We describe some of these risks and uncertainties in the Risk Factors section in our annual report on Form 10-K, which was filed on March 1, 2022 and in other filings we make with the SEC from time to time.

The company undertakes no obligation to update or revise publically any forward-looking statements, whether as a result of new information, future events or otherwise. In today's remarks, we will refer to certain non-GAAP financial measures. Reconciliation of these non-GAAP financial measures to the most comparable measures calculated and presented in accordance with GAAP to the extent available without unreasonable effort are available in the earnings release and accompanying presentation, which are available in the Investor Relations section of our website.

I will now turn the call over to David.

David H. Bywater

Chief Executive Officer & Director, Vivint Smart Home, Inc.

Great. Thank you, Nate, and good afternoon, everyone. We appreciate your interest in the Vivint story. We continue to work hard every day to earn your confidence and your support.

My comments today will cover three main areas. First, I'll review some of our key financial and operating highlights for the second quarter. Second, I'll cover some business developments that have taken place since our last earnings release. And third, I'll review our strategic priorities, as we continue to redefine the home experience with technology and services to create a smarter, greener, safer home.

Before I begin, let me take a moment to welcome our new Chief Financial Officer, Dana Russell. We're thrilled that Dana has joined our leadership team. Personally, I have a rich history with Dana, having worked closely with him for seven years at our sister company, Vivint Solar, up until a successful sell to Sunrun in the fourth quarter of 2020. Dana's expertise in building and leading best-in-class finance organizations fits perfectly at Vivint, as we enter our next phase of profitable growth. Though he's only been with us for a very short time, he's already made a very positive impact. Dana will review our financial results and share updated outlook following my comments.

We also have our new Chief Operating Officer, Rasesh Patel, in the room with us today, who joined the company in May. Rasesh has a broad charter that spans operations, technology, product, and customer experience. He is focused on improving the value and functionality of our products and services, delivering industry-leading customer experience and loyalty, and driving the next level of operational excellence and productivity, Rasesh has extensive experience in these areas from his prior role as the Chief Product and Platform Officer of AT&T business, a segment of AT&T with $35 billion in annual revenue. Prior to that, he was a key executive at DIRECTV during their explosive growth period.

Moving on to our highlights for the quarter, I am pleased to report that our strong track record of execution as a public company continued through the second quarter of 2022, as we grew total revenue by over 17% and adjusted EBITDA by more than 23% after normalizing for the sale of our Canadian operations. We originated over 126,000 new smart home subscribers, an all-time high for the second quarter period, with significant contributions from our smart energy partners.

Our last 12-month attrition was 10.9%, which was a 17-quarter low and a 70 basis point improvement versus the prior year. We're extremely pleased with this result and we continue to believe our attrition rate is the lowest among national smart home companies by a significant margin. Our improving customer retention is a result of years of work to improve the overall credit quality of our customers, improve the performance of our products and services and increase the frequency of customer interactions with our platform.

We ended the second quarter with our net service cost per subscriber at an all-time low, a strong indication that we are operating the business efficiently and effectively while delighting our customers. Vivint has more than 20 years of operating history, and we've developed and refined a proprietary cloud-based platform that we believe is the benchmark in the smart home space. Our recurring revenue model has proven resilient during challenging economic times and we believe the peace of mind and security we provide is relevant in any environment.

Another key highlight during the second quarter was the successful divestiture of our Canadian operations for $104 million in cash proceeds. As a reminder, we stopped doing direct-to-home sales in Canada in the first quarter of 2020 due to unsatisfactory new subscriber economics in that part of our business. Our Canadian revenues were generating a meaningful amount of cash flow from operations since we were no longer investing in growth there. However, our lack of investment in Canada made these customers more vulnerable to attrition. So we made the prudent and proactive decision to sell the Canadian business and secure the value of the cash source by putting years of future cash flow from operations safely on the balance sheet and removing the risk of attrition to these customers.

Divesting the business also allows us to sharpen our focus on the exciting growth opportunities that exist here in the US, where Vivint is a leader in terms of revenue and subscriber growth. We plan to invest the resources of the transaction in value-accretive areas that may include to, but are not limited to subscriber acquisition efficiencies, growth in adjacencies, enhancing the customer experience and improving our cost structure. Successful execution in these areas should drive higher customer lifetime value and more durable top line growth, while elevating the cash generation potential of the business.

We are continuously focused on redefining the smart home experience with technology, products and services that create a smarter, greener, safer home, and our integrated platform is the core enabler that allows us to deliver on this mission. We now process more than 1.1 billion events per day across our subscriber portfolio. Our average smart home customer has approximately 15 devices in their home, interacts with their smart home system more than 12 times per day and stays with us for approximately nine years, a number that's increased over time as our customer retention has improved.

We believe our revenue streams are resilient and customer value – customers value the technology and services they receive from Vivint. They are demonstrating this by taking more products, interacting with their systems more and staying with us longer. We continue to install more complex technology in the home, and yet, our net service cost per subscriber continues to go down. A remarkable feat, we believe, is made possibly – possible by our world-class integrated platform.

Smart energy and smart insurance are natural extensions of our smart home business, and we believe they are platforms that will allow us to penetrate and retain more households with smart home technology and services. We believe the additional customer touch points will lead to even lower attrition, longer average customer lifetimes and expanded customer lifetime value. We continue to be encouraged by the progress of our strategic adjacencies. We have seen positive momentum in our smart energy business, where we installed 11.8 megawatts of solar through our partners in the first quarter and ramped to 20 megawatts in the second quarter. Due to the seasonality of our smart energy business, we would expect the majority of our revenue generated from that business to come in the back half of the year, and we remain on track to double the 45 megawatts we installed through our partners in 2021.

Our Vivint sales force and strategic partners who bundle a Vivint smart home system with solar continue to see considerably better sales realization rates than those who only sell solar. And we continue to make progress towards our long-term vision of combining energy production and consumption into an integrated platform that uses artificial intelligence to manage power consumption more intelligently. We believe our nationwide footprint and ability to install our award-winning smart home solution within a day or two of a customer signing up for a solar is a game changer for the industry and for our customers. We believe that as we grow and solidify our go-to-market partnerships, we will prove to be a powerful and differentiated combination to grow and retain smart home customers.

On the smart insurance front, we continue to operate as an agent, selling insurance policies to new and existing smart home subscribers. We continue to progress towards becoming a managing general agent, which will allow Vivint to develop specific home owner coverages and enable us to accelerate growth. Because of our meticulous focus on optimizing the smart home experience for our customers, we've been able to grow faster than our peers in the do-it-for-me smart home segment, while generating higher profits than the alternatives do in the do-it-for-yourself – do-it-yourself segment. We believe that as we continue to leverage the advantages from our intelligent and integrated platform, we will further expand and extend our leadership in the do-it-for-me segment.

In closing, it's been just over a year since I rejoined Vivint. I continue to be impressed with the strength of the business model and the quality of our people. We truly have a world-class group of employees to match what we believe is a world-class platform for growth. We're extremely pleased with our performance for the first half of 2022, especially against the backdrop of a challenging economic environment and of supply chain constraints. We recognize and sincerely appreciate the hard work and tireless efforts of our employees to achieve these results. We're excited about the future as the markets in which we operate are large, expanding and provide significant headroom for further growth.

With that, I'll turn the call over to Dana to further discuss our second quarter results and our updated outlook for the year, which now excludes divestiture of our Canadian operations. Dana?

Dana C. Russell

Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

Thanks, David. Good afternoon, everyone. Let me start by saying how pleased I am to join Vivint, reunite with David and work with the rest of the leadership team. I really believe Vivint provides a unique combination of solid business fundamentals, talented and driven people, great market opportunities and a culture that fosters growth and development. I felt this way when I accepted the job. And two months in, I'm even more encouraged about the prospects for our customers, shareholders and employees. I feel this is a special company with a solid foundation that has tremendous upside.

The remainder of my comments will refer to information in our earnings presentation that was posted to the Investor Relations section of our website at vivint.com prior to this call. Following my prepared remarks, we'll open the call up for a Q&A session.

Our key subscriber portfolio metrics continue to perform well and showed year-over-year improvement in the quarter. During the second quarter of 2022, we had growth in total subscribers of 4.7% versus the prior year period, reaching $1.86 million as of June 30. Normalized for the Canadian divestiture, our year-over-year growth in total subscribers was nearly 11%. Our average monthly recurring revenue per user in the second quarter increased by 4% year-over-year to $68.03. Excluding Canada, average monthly recurring revenue per user was $68.69 for the quarter.

Moving on to revenue and adjusted EBITDA, revenue grew by 15% to $407.3 million in the second quarter of 2022. Normalized for the Canada sale, revenue growth for the quarter was 17.5%. The growth in revenue was attributable to the previously mentioned increase in total subscribers and average monthly recurring revenue per user as well as solid contribution from our smart energy adjacency. We're very pleased with the revenue growth through the first half of the year and we remain on track to meet or exceed our original revenue guidance for the full year, despite the spin-off of our Canadian operations.

Like revenue, adjusted EBITDA grew nicely in the second quarter of 2022, finishing at $189.7 million, up 18.9% from the same period in 2021 at a margin of 46.6%. Normalized for the Canada divestiture, adjusted EBITDA growth was 23.5% year-over-year. The scaling of service costs and lower G&A expenses were the primary drivers of the improved margin performance. We're pleased with the growth in adjusted EBITDA in the face of continued economic challenges and supply chain constraints.

Next, I'll highlight a few metrics on subscriber originations for the second quarter. New subscriber growth was 3.9% compared to the same quarter in the prior period – in the prior year period and was driven by over 4,600 originations through our smart energy partners, a demonstration of the benefits of bundling smart homes with solar. New subscriber growth for the six months ended June 30 was 6.2% and was again driven by originations through our smart energy partners.

We continue to be encouraged by the quality of our customers we're adding to the portfolio. And the loyalty of our customer base continues to improve, as evidenced by the overall growth in total subscribers of approximately 11%. Nearly all of the customers originated in the quarter either paid in full or financed purchase of their equipment through one of our financing partners. For the last 12-month period ended June 30, average proceeds collected at the point of sale was $1,642 after the payment of financing fees.

I'll next cover our net service cost per subscriber and net subscriber acquisition cost per new subscriber for the quarter. We continued our trend of year-over-year improvement in net service cost per subscriber dropping from $10.03 in the second quarter of 2021 to an all-time low of $9.29 in the second quarter of 2022. Correspondingly, our net service margin increased from 79% in the second quarter of 2021 to 80.1% in the most recent quarter. These results demonstrate the advantage of Vivint's fully integrated platform. Equipment attach rates, particularly cameras, continue to increase, while net service cost per subscriber continues to drop. The constant feedback loop from our proprietary platform enables us to continuously improve our integrated products and services, leading to fewer customer issues and higher customer satisfaction.

As discussed in prior earnings calls, Vivint now includes fees paid to our financing partners in the reporting of net subscriber acquisition costs for new subscribers. Whether those fees are paid over the term of the loan or upfront at the point of sale, including financing fees, net subscriber acquisition cost per new subscriber for the last 12 months ended June 30, 2022 was $661, up marginally from $604 in the prior year period. The year-over-year increase was driven by higher equipment-related expenses as well as higher MDR fees due to recent interest rate increases.

Another metric we're happy to report is our last 12-month attrition rate. For the period ended June 30, 2022, our attrition rate improved for the ninth consecutive quarter to 10.9%, a 17 quarter low. Our enhanced underwriting standards, improved product and service performance and the high level of customer engagement with our platform continue to drive what we believe is the lowest attrition rate among national smart home companies.

In terms of free cash flow, we generated $62.7 million during the second quarter of 2022, down $12.3 million from the second quarter of 2021. The decrease was primarily driven by a change in the timing of financing fees paid to our lead financing partner. As of June 30, 2022, our balance sheet reflected $299 million of cash on hand and a very strong liquidity position of approximately $658 million.

In conclusion, we're pleased with our consistent execution across our key financial and operating metrics. The fundamentals of the business remain strong, and we're pleased with our momentum going into the back half of the year. The divestiture of our Canadian operations was approximately $104 million of cash forward, which we believe is significantly more cash than we would have generated from these subscribers over the next 10 years and it provides optionality to invest in areas that we believe will drive incremental value for our stakeholders.

Vivint has been securing and creating smart homes for over 20 years and we have a history of exhibiting strength and resiliency through challenging economic times. We're confident that our customers will continue to value the security and smart home solutions we provide. We have long believed the total addressable market for smart home presents a tremendous opportunity and we believe Vivint is the best positioned provider to take advantage of that opportunity.

Despite current challenges in the broader economic environment, we're reaffirming our original guidance, which first announced in connection with our earnings call in February for revenue and adjusted EBITDA. To account for the sale of our Canadian operations, we're adjusting our guidance range for total subscribers by 85,000 or roughly the number of subscribers that were sold. We're also adjusting our guidance range for Q3 cash flow by $17 million on the top end and $15 million on the bottom end to account for the decrease in operating cash related to the Canadian subscribers that were sold.

In summary, we expect to end the year with total subscribers within the range of 1.86 million and 1.92 million. Total revenue within the range of $1.6 billion and $1.63 billion, adjusted EBITDA within the range of $725 million and $745 million, and free cash flow within the range of $35 million and $60 million.

This concludes our prepared remarks for the second quarter. Operator, please open the call for Q&A.

QUESTION AND ANSWER SECTION

Operator: Certainly. [Operator Instructions] Our first question comes from the line of Rod Hall with Goldman Sachs. Please go ahead.

Max Gamperl
Analyst, Goldman Sachs & Co. LLC

Q

Hi. Yeah. This is Max on for Rod. Thank you for taking our questions. The first question is on cash flow and interest rates. And I think you touched on this, but could you walk us through the main ways how Vivint is impacted by rising interest rates and possibly quantify what do you think the incremental headwinds to cash flows that would present? Or is that what the wider free cash flow guidance represents? And then I have a follow-up. Thank you.

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

So, Max, as you probably know, a lot of our debt has a variable component to it. And so we're impacted by rising interest rates associated with change there and then the customer financing options that we provide also have a variable component to them, so both of those things can impact us pretty significantly.

If you quantify that – and let me just give you a little bit of a benchmark here, if we rise by about 1%, 1% increase in interest rate creates about a $26 million increase in interest expense for the company at the current run rates with the current structure. That's a combination of the debt, the outstanding debt as well as the financing that we provided for consumers to buy the products with. And so that's roughly a benchmark on an annualized basis of what that – an increase in interest rates do. So it seems some fairly significant interest rate increases here over the last few months, which have impacted the company. And so we're seeing those kind of interest rate increases in our financial statements there as far as the impact of free cash flow and operating expenses.

The good thing is we've been able to operate and continue to provide guidance here for the full year, which is pretty robust and very close to the original figures that were provided back in February. And we also expect to be able to operate in those ranges, excluding what we talked about from Canada to be pretty close to what we originally guided to. So not optimal in terms of the increase in interest expense many companies are faced with and we're certainly not immune to that either, but we feel pretty good about the position that we're in, in terms of still generating significant free cash flow and feel like we're operating very well along the environment that we originally guided to earlier this year.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.
A

Yeah. I'd add to that, Dana, just to your point, I mean the team has done an incredible job. Our net servicing margins improved. You saw our net servicing cost [ph] went (00:24:52) down.

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.
A

Yeah.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.
A

I think the team has responded really well in the market and given those inflationary challenges and the interest challenges, I thought they performed really well in the quarter. So being talk about costs, I think the optimization about how we do route optimization, self-help tools that we've been rolling out is reducing our roll out call demands. And there's just been a – I think the technology – the efficiency of the technology and how we continue to tighten that make a better experience with the customers. All those things translate to lower costs and we've seen that in our net servicing cost per subscriber go down to an all-time low.

So [ph] with interest rates were (00:25:32) not in the environment they're in, but I'm really pleased with how the team has operated, and that bodes well for us as we continue to move forward once interest rates are a little more stabilized. I think the core performance of the company continues to impress me and I'm encouraged by what they have still up their sleeves to do over time to continue to make that even better. So a good question, Max.

Max Gamperl
Analyst, Goldman Sachs & Co. LLC
Q

Yeah. That's very helpful. Thank you for all that color. And then as a follow-up, we're wondering if you're seeing any change in the popularity of Citizens financing, given that you offer 0% APR financing. And do you ever expect to move away from this or do you plan to continue to offer this 0% financing? Thank you.

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.
A

Well, that's been a pretty successful thing from my view, as I've entered here in this role of CFO, the 0% financing has been attractive. Now whether or not we'd ever move away from that, I think there's certainly some other options there. Obviously, consumers not being impacted themselves by an interest rate increase bodes well in terms of their ability to get product and to engage with Vivint. And there's certainly some other things that we could look at and do as we go forward. But today, we're pretty happy with that relationship. It's been a very good relationship. That relationship, our contractual commitment for that extends for a couple more years. So we don't see us going away from that anytime in the near future here. And it's been something that's been very successful in terms of being able to generate upfront cash and allow the company to be in a strong cash position.

Max Gamperl
Analyst, Goldman Sachs & Co. LLC

Q

That's very helpful. Thank you so much.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. Thanks. Max.

Operator: Thank you, Mr. [ph] Hall. (sic) (00:27:38) [Max] Our next question comes from the line of Paul Chung with JPMorgan. Please go ahead. Paul, your line is now open.

Paul J. Chung
Analyst, JPMorgan Securities LLC

Q

Hi. Thanks for taking my questions. Nice execution here. So this is your second consecutive quarter with kind of positive GAAP operating profit. Are we on a new trend here? And can we be kind of GAAP profitable for full year maybe by 2023? And then where are you seeing opportunities on the cost base? And should we expect some seasonal uptick here in the second half? And help us kind of sparse out the OpEx related to Canada? And I have a follow-up. Thanks.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

I'll handle the second half of your question. [indiscernible] (00:28:38)

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

GAAP earnings, Paul, benefited somewhat from the sale of Canadian operations. So when we look at the overall profitability for the company, we had about a $25 million gain associated with the sale of the Canadian operation. So that's a one-time event. We'll – we are moving in a good direction. The company continues to improve in terms of its overall profitability, its overall performance. David talked about the efficiency that we're gaining in terms of operations, especially in that service component.

So we expect to continue to see that trend move in a positive direction. I wouldn't want to put a timeframe exactly on that in terms of GAAP profits, but we certainly feel good about the direction that we're heading, and we expect to continue to see improvements over the upcoming quarters.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. [ph] I may look at (00:29:39) that day when that definitely crosses that threshold here in the next future, [ph] hopefully, (00:29:45) not too far off. With regards to the cost reductions that we're going after, Paul, I mean, this is definitely an area of focus for us, with Rasesh coming on and his strong competency in that area, Dana's strong competency, there's a – and the entire team, there's a multitude of things that we're working through that I think will continue to reduce our costs and increase our cash generation that I'm very, very bullish about, and they're pretty significant.

And you think about these certain things, right, just the scale of our solar business now, that's actually performing quite well. And as that kind of comes into maturity, that actually starts to produce a nice profit for us. There's a bunch of products that we're working through right now that will be quite well received by the market and I think are profitable for us, it would be nice.

There's a bunch of stuff around supply chain. You think about the escalation costs that we had this year with decommits and having to put everything on air versus boat as well as the opportunity to go back and stabilize and normalize relationships with our vendors, we spent a considerable amount of money every year on our product. We think it gives us tremendous advantages with our customers, but there's a real opportunity there. And then there's just some real, real innovative things we're doing around self-help and self-fueling that once again drives customer care calls and service visits, possibly a bunch of other stuff.

So, I mean, what I'm really, really excited about. And then also just go to market, channels we go to market. We're exploring and pushing additional channels to market that should be a lower cost to acquire customers. And as that blends in, that's – that will be accretive as well.

So you'll get more details on this over the coming quarters as we move from pilots and all the work we're doing today to where we feel very comfortable sharing the details. But I'm encouraged by that roadmap. It definitely makes me encouraged by our future and I think it will continue to drive our cash generation up considerably and our costs down. So more to come, but definitely very encouraged by that.

Paul J. Chung
Analyst, JPMorgan Securities LLC

Q

Great. And then a follow-up on the smart insurance platform and kind of timing of becoming a managing general agent and the uplift there once you transition. And then, given the kind of smart insurance is your largest TAM on your slides you're participating in, is this one of the biggest opportunities for growth in your view? Or is there a specific kind of TAM you're targeting? And just any comments on the uplift of this transition? Thank you.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah, great question. I'm actually very encouraged by insurance. We're still moving towards the MGA model. We still plan on being in a state or two by the end of this year. It's been thoughtful. As I mentioned in earlier calls, I'm not looking to insurance right now to be a large growth for us with regards to profit or revenue growth. I view this as an investment that we're making over the next few years that will pay off very nicely down that road.

We're getting a significant lift right now out of smart energy. It's immediate. It's material. It's large. And that has really been a nice addition to our portfolio of what we do. Insurance will feather in over the next few years and I think it'd be quite significant.

What's really interesting about the insurance piece is there's two parts. I like the MGA play, for sure and [ph] the trust build (00:33:14) actually demonstrate to our customers the value of their data to their benefit. So that has got great retention value over time, which I think will just add to what we're already doing and the benefits we're already seeing. So I like that from a customer-centric approach and the value that we bring to them. But what I'm also really interested in is the opportunity to partner with some insurance companies and build to get use as a – another channel to market. And they have a large customer bases that are looking for innovative solutions. And so I look forward to having that play out over time as well.

So insurance is very strategic for us. I'm not reliant upon it in the short-term. I am reliant upon for the long-term value add for our customers and for our shareholders. I think it'll pay off very nicely. And I'm encouraged by multiple benefits that I think it will bring for us. So it is a large TAM and we're excited to tap into that, but it'll be over the next few years.

Paul J. Chung
Analyst, JPMorgan Securities LLC

Q

Great. And then lastly, of course, the new bill passing with Senate, how have your expectations for smart energy projections kind of evolving? Thank you.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. I mean we'll see how that thing finalize as it goes through the legislative process, but nothing but good. I mean, as I mentioned in my comments, it's amazing the amount of interest in this bundled solution that we have. The work that I had done previously have been in solar with Dana. We knew that they wanted to bundle almost the [ph] top of their heat (00:34:50) was smart home. This concept of smart production, smart consumption, they do go hand in hand. And we're seeing a considerably higher sell to install ratio with all of our sales force that sell them together. They're seeing it as well, which just means the customers value it.

So I think the work that's going through the legislation right now is a positive thing. Our goal as a smarter, greener, safer home, and greener means a lot to us. And so I'm hopeful that it'll actually pass through and that we'll see some long-term stability around that going forward. So very encouraged by that.

Paul J. Chung
Analyst, JPMorgan Securities LLC

Q

Great. Thank you.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Rasesh, you got any thoughts on that piece?

Rasesh Patel
Chief Operating Officer, Vivint Smart Home, Inc.

A

No, I think you nailed it, David. I mean with the Senate passing the bill this weekend, we're very optimistic about the demand that will be there for smart energy. And as you said, customers – the smart home product make the smart energy product very sticky from sale to activation. And that's driving small – strong demand from our third-party partners to bundle our smart home solution. And so we look forward to the acceleration in demand driven by the energy bill and we look forward to bundling with our solar energy partners.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Well said. All right. Thanks, Paul.

Operator: Thank you, Mr. Chung. Our next question comes from the line of Erik Woodring with Morgan Stanley. Please go ahead.

Erik W. Woodring
Analyst, Morgan Stanley & Co. LLC

Q

Hey, guys. Thanks for taking my question. Congrats on a really strong quarter. I would just love to get to the revenue guide. Just I think it would be helpful to get some of the puts and takes as we think at least about the second half because, obviously, you're losing 85,000 subscribers from your Canadian operations, call it, roughly 6 months of that. That's $30 million-plus revenue just kind of like back of the envelope math. And obviously, you outperformed 2Q by a fair amount, but left your revenue guide unchanged, which means that there is something that's picking up that slack. So I would just love to hear from you guys what you think some of the puts and takes are that help you keep your full year guide and whether that's on the pricing side, where that might be coming from? And then I have a follow-up. Thank you.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. I think the two major drivers there, Eric, that we're benefiting from is, one, is solar is quite strong. So we've been pleased with the solar growth in the revenue that's brought. And the second thing is the attrition has been incredible. So we've really outperformed there. The ongoing – maintaining that revenue stream has been quite positive for us as well.

So there's other things here and there that have helped us. Like you said, the performance in Q1 was helpful, for sure. But kind of the balance of all of that has allowed us to reaffirm, and probably not a lot of companies that done that, that reaffirm the guidance they gave back in February, to reaffirm our guidance around revenue and adjusted EBITDA. So – and the team has obviously managed the cost quite nicely. So I'm pleased on both the value of the platform, diversification of the platform, the strength of our ecosystem to retain customers better than we thought, and continue to see those new cohorts perform better than they thought they would has been a real avid.

So those are some of the major puts and takes. Dana, do you want to add to that?

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

I think we're seeing an increase...

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Usage.

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

...the usage. And I think the other thing that our attach rates per customer, you're seeing a significant uptick here with the value of each customer meaning more. So I find it interesting as I've kind of come into the company here that the improvements have been made over the last several quarters in the value of these customers, their credit quality, their scores, the ability to buy more product and generate more revenue per customer, I think all those things are positive. And at the same time, as David mentioned, we continue to see lower attrition. So that points to the quality that they're getting and the happiness that they're having as they engage with Vivint. And so I think all those things point to a brighter roadmap ahead and I think we feel quite confident about our revenue streams.

Solar, David mentioned that, the real power of that is the attach rates that we get with smart home. And so that smart home, especially in channel partners as we're going out there and engaging channel partners, we're just on the cusp of that. That's a thing where we're just sort of seeing the potential there, that we also feel like there's real value there in developing those channels, David alluded to that. So we're quite encouraged about our opportunities here as we go forward, not only do that and generate revenue, but to generate it at potentially lower cost than we have historically. So, over time, I think we can see the best of both worlds [ph] will grow (00:40:21) and some efficiency in our cost structure.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. Well said.

Erik W. Woodring
Analyst, Morgan Stanley & Co. LLC

Q

Awesome. That's really helpful. Maybe as a quick follow-up to that, is there any way that you can help us size kind of for the year then, how to think about kind of the revenue that you get from smart energy that isn't necessarily captured in the ongoing subscriber numbers, but just everything outside of that?

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. So it's about $1 per watt that we do there, right? So for closer to 95 to 100 megawatts, then you'd say is $95 million to $100 million. So pretty strong correlation there and pretty simple math.

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

Yeah.

Erik W. Woodring
Analyst, Morgan Stanley & Co. LLC

Q

Okay. That's really helpful. And then maybe just my follow-up, kind of all in the same bucket is maybe just talk about the puts and takes about you had to cut free cash flow, but you didn't cut your adjusted EBITDA forecast. So why was that? And then, as it relates to free cash flow, obviously, there's kind of a number of temporary headwinds in terms of selling Canadian operations and then some of the financing compares. Can you help us kind of bridge and think about what like a normalized free cash flow would have been this year without some of these one-time factors? And that's it for me. Thanks so much, guys.

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

Yeah. Good questions, Erik. I think the Canadian operations we talked about was generating a disproportional amount of cash because we weren't making heavy investments in that operation. So when you think about that, we've got on those – on that presentation or investor presentations there, $661 of net investment in a new customer, which we were not investing in Canada, so generating a lot of new customers in the US, but not in

Canada. And so there's quite a bit of cash coming out of Canada as a result of those previously acquired customers that we're servicing. The decrease in our cash or free cash flow that we talked about from a guidance standpoint was really solely related to that operation.

Now, in addition to the headwinds associated [ph] with we're seeing that going out, (00:42:44) we just want to reiterate that we thought that was an extremely prudent decision. We weren't investing there. It wasn't an area of growth for us. We have very good opportunities to grow and invest in the US in much more prolific ways than we were in Canada. We pulled forward that cash. It's on the balance sheet. We've secured it. We thought that was the right thing to do. And we really believe that, in our opinion, that we've pulled forward cash that would have equated to over 10 years' worth of operations up there.

So really, really good business decision in our mind to bring that forward and to use that cash in places where we have an opportunity to get better returns.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. When I think about that, just to elaborate a bit, if I was the sole shareholder of this company, I would have done that deal in Canada, 100 out of 100 times. It was just the smart thing to do. I think TELUS was a good partner for us. We're a growth company, always have been. And when we stopped growing in Canada, and we had 100 employees up there, like, wait a minute, we're not growing? And those customers weren't getting new services. They weren't getting new bundled solutions. So we're a growth company, we're a customer-centric company and we're a financially prudent company. So you make sure you take care of those customers. And I think that they now have a growth trajectory with their current owners of that portfolio, which makes sense. Our employees have a roadmap there. And then for us, I just looked at it and we're like, this is the right thing to do, derisk that completely. I think it was great for the acquirer, it was great for us. And like I said, I'd do that 100 out of 100 times. Definitely the right thing to do, prudent thing to do, and that cash is secured now. So...

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

Yes. The second half of that question, Eric, in terms of EBITDA guidance versus the cash impact, so EBITDA, obviously, isn't impacted by interest. That's excluded from those numbers. And so as we've seen those interest rate increases, and that's a fairly significant impact on our cash – on our cash flow from operations, but it's adjusted out in the EBITDA number. So we're not having an impact on EBITDA as a result of those increases in interest rates.

It is an impact in cash, although I think we've mitigated some of that impact through other means and efficiency in our operations. But we feel very good about the EBITDA number. And we also feel like we're in a solid position on our free cash flow as well. I don't know if that answered your question fully or if you have a follow-up there, but there's – the difference between those two really is associated with the interest rate not having an impact on EBITDA.

Erik W. Woodring
Analyst, Morgan Stanley & Co. LLC

Q

Yes. No, that's...

Rasesh Patel
Chief Operating Officer, Vivint Smart Home, Inc.

A

Rasesh, I could add...

Erik W. Woodring
Analyst, Morgan Stanley & Co. LLC

Q

Perfect. Thank you. Yeah, please go ahead.

Rasesh Patel
Chief Operating Officer, Vivint Smart Home, Inc.

A

Okay. I just might add. The kind of forward-looking opportunity for free cash flow generation, I mean, I think we have a number of one-time items that affect us this year in the way of inflation, interest rates as well as one-time hits to some changes to the financing program that were made last year. So if you get into 2023 and you overcome those one-time pressures, and you combine that with the potential we have to be more efficient in customer acquisition costs, in product value engineering, in development of some adjacent services, I am very optimistic about the cash generation potential of this business over the next two to three years. And so I think that's one of the most exciting opportunities that I see in joining the company.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. I think that's a great point, Rasesh. Nitin has pointed out to me, too, who's sitting here that we've had some impacts here in the business associated with supply chain issues, different things. We've tried to meet demand with certain products and had some additional freight costs and other things that have impacted the business and been fairly significant. We've had to work around that. We think a lot of that is behind us from the standpoint of – that's kind of resulted in the impact that we're seeing today. And we anticipate some of that, knowing that those things are going to be there, so it wasn't new, but it's certainly a headwind that we've worked through. And so all in all, I'd say those things considered on top of a couple of other little headwinds there, we've had an extremely solid results and feel very good about the performance and even better about our ability to manage some of those things going forward.

Erik W. Woodring
Analyst, Morgan Stanley & Co. LLC

Q

Awesome. Thanks for all the color, guys.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

You're welcome.

Operator: Thank you, Mr. Woodring. Our next question comes from the line of Brian Ruttenbur with Imperial Capital. Please go ahead.

Brian Ruttenbur
Analyst, Imperial Capital LLC

Q

Yes. Thank you very much. Just to get a summary real quick. Can you provide the adjusted revenue, EBITDA and attrition for Canada for this quarter and with or without versus last quarter and last year?

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

Nitin, did we have a slide or anything on that in the deck. That may be something, Brian, that maybe Nate or Nitin can help us with, we could put up after in terms of numbers and throw out there. I don't have that off top of my head, but we certainly can provide that.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

I have one. I do know that the attrition in Canada [indiscernible] (00:48:55) US...

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

Yeah.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

...which is a function of what we said earlier, not growing there and not being able to bring new product and services there, you would expect that to be higher. And we had seen that growing, a year or two ago, it was the same almost in the US and then it's gotten to 14% and then higher. So it was definitely growing at a rate that was going in the wrong direction as our core business, [ph] which you know... (00:49:16)

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

Yeah. And you can see that – with those components on our presentation, that investor presentation. Nate's broken some of that out. So you can see the individual components of Canada. You can also see that our growth rates were larger once we exclude Canada out of those numbers, most of the metrics were better as a result of not growing in Canada and having growth elsewhere. But I think we can break out the individual impact there in Canada for you, if need to be.

Brian Ruttenbur
Analyst, Imperial Capital LLC

Q

Okay. And then just as a quick follow-up. How are you passing along these higher costs? One point that you make is that roughly for every 100 basis point move in the interest rate environment, it negatively impacts free cash flow by, I believe, $26 million. Are you passing a certain percentage of that along to your customers and the new customers?

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

No, we really haven't. I think there's the option to do some of that through price changes and other things, which we have not done, but most of that impact has resulted in economics that have been impacted as a result of those interest rate increases.

Now, where we've done a really good job is being more efficient in the way that we've done other activities within the company. And certainly, the service cost is a kind of a bellwether mark that we can point to and say that was exceptional, been well done. We've been careful about our other cost structures, but we continue to invest and we're investing for growth. So I think we continue to believe that we have a potential to grow. It's not like we're pulling back reins or making reductions. We haven't announced any kind of overall reductions, and David, you can talk to that, but we continue to be optimistic and continue to invest, as portrayed thereby our customer acquisition investments there in the presentation there.

Brian Ruttenbur
Analyst, Imperial Capital LLC

Q

Great. Thank you very much.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Thanks Brain.

Operator: Thank you, Mr. Ruttenbur. Our next question comes from the line of John Mazzoni with RBC Capital Markets. Please go ahead.

John Mazzoni
Analyst, RBC Capital Markets

Q

Congratulations on the strong results. Thanks for taking my question. I'll keep it quick. Just as we think about attrition, could you give us some color on why it's been trending much better than expected? And also, how should we think about attrition going into the back half of the year? Thanks.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Thanks. Yeah, I'll take that one. When I think about attrition, John, I think there's three key drivers. So we talked about two of them quite a bit, not the third. So let me about the two obvious ones. I think our underwriting criteria and the strong credit history that we have with our employees – I mean, with our customers is tight over time. So I think that's actually just proving out well against what we modeled. So I think that our underwriting has gotten quite strong.

I think that the service and the performance of the system has gotten much tighter. I know for me personally, I was gone for five years. I had the old Vivint system back in 2013, 2014. I was reinstalled last year. Personally, I was delighted. I remember I was just – I was like, wow, this is the technology, and just all of the alerts and actually trying to prevents when I'm actually doing something wrong, and just the use cases with my family was finding in the system is quite a remarkable.

I remember when Dana showed up and we installed his system, he called, and he goes, this is phenomenal. The professional install was incredible, the technology is incredible. I got friends and family all asking for a system. So I just think that that's the second thing. That continues to get better. We own that technology. We own that feedback loop on how we find it was rubbing the customers wrong and what's delighting them. We can either eradicate and fix or we can reinforce. So I just think that's getting better.

I think the third thing is the consumer financing. When we went to consumer financing several years ago, the hypothesis was that at the end of your five-year contract when you finish paying off the equipment, your bill essentially drops in half. And what we have to do over those five years is to bring enough value to them and additional value so that when their bill drops in half, they're like, holy cow, I'm still getting all of this value, and essentially, I'm paying half what I was paying before. And I think that when you think about attrition and you think about everything we got going on, I think that's playing out. And we're just finding consumers saying this is well worth it around efficiency in my home, around productivity in my home, [ph] enjoyment of (00:54:33) my home.

And now we're bringing these new services around bundling other things with them, I think they're finding great value. So I think those are the big three for me. Anything that you're going to add to that?

Dana C. Russell
Chief Financial & Accounting Officer, Vivint Smart Home, Inc.

A

I would say one thing, John, your question about how does this look going forward here. Some of this is correlated, as David mentioned, to the end of the contract period. So that five year life on those contracts, as those contracts mature, there is some variation and some increase at times with attrition. But as I've been educated by the team here and looked at the results here lately, it seems like you're bending that curve a bit and we're getting much better results where we would have expected on prior year's numbers to be higher from an attrition rate standpoint just because of the timing of those contracts coming [indiscernible] (00:55:35) there. Now we're seeing the attrition still be lower.

So there's – we believe that the overall trend is going to stay in a positive direction that we've seen. There may be a slight uptick on a specific quarter associated with contracts being at the end of a life, but we do believe that we're going to be in a better situation and continue to see these downward trends where attrition continues to improve and that we're not going to see a reversal of that, any significant reversal of that certainly over a longer timeframe.

Rasesh Patel
Chief Operating Officer, Vivint Smart Home, Inc.

A

And I would just add to that, being at a 17-quarter low at 10.9% just demonstrates the power and the brand loyalty that our platform has. To put into context, the average life of the Vivint customer is now 106 months, approaching nine years. And so there aren't many platforms that generally that type of brand loyalty.

And to give you a little bit more color into the attrition trends, our involuntary attrition is running right on plan. But where we're really seeing the favorability is on voluntary attrition. And that gives us good confidence that the cohort of customers that are – that originated on the [indiscernible] (00:57:01) platform and are now coming off contract has a much higher stickiness than we had originally expected, and that bodes well for our sort of go-forward expectations around interest.

John Mazzoni
Analyst, RBC Capital Markets

Q

That's great color. Thank you, again.

Operator: Thank you, Mr. Mazzoni. Our next question comes from the line of [ph] Uman Abdullah Khan (00:57:29) with Evercore. Please go ahead.

Q

Hi. Thank you for the question. This is [ph] Abdullah Khan (00:57:37) dialing in on behalf of Amit, who's unable to be here today. So it's great to see your average monthly recurring revenue per user grew quite nicely this quarter. And I wanted to ask whether you could talk about some of your efforts to continue to expand it? And how do you think this KPI can trend long-term? And longer term, what kind of contribution to your growth profile do you see from growth in your installed base versus new subscriber growth? Thank you.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Yeah. [ph] Abdullah, (00:58:06) I appreciate the question. I'll take the first half of this, and let Dana and Rasesh add to the back end of that. One of the key things that we view a customer as is it's not once and done upfront and then you see what happens in the next five years. The amount of upselling that occurs throughout those five years has actually gotten quite good. So that's been nice to see that improve as we continue to sell a little bit.

And then the other thing is you're seeing solar play in there. It does not include at all in that section. So once again, us being able to go meet with customers and share new ideas, new products, new services, but it's really the attach rate. So cameras, for example, continue to be strongly attached, like the demand for cameras just continues to grow and grow and grow. The use cases that our customers are using and discovering for the system continues to expand as we share those and we've understand use cases.

And then just the frequency of the interaction, I think that [ph] frequency of customer (00:59:07) interaction that shows there's a demand there, they're always seeing about our system. They're always using our system. And so when we do a service call and somebody says, hey, you're on the camera on that back part of your house. They're like, hey, I'd love add that additional RMR charge.

So I think it's really use and scope of what we're doing has been driving kind of that average monthly. Dana, I don't know if you want to add, Rasesh, or?

Rasesh Patel
Chief Operating Officer, Vivint Smart Home, Inc.

A

Yeah. You bet. I'd just add that our service revenue is up 26% year-on-year. And so we feel good about the ability to drive more engagement on the platform as we have service interactions with customers. And as David referenced earlier, there are going to be some exciting product announcements that we have coming into 2023 that will open up even more opportunity to drive further engagement of the Vivint customer base into those new product categories.

And so I mean, if you think about the smart home and the connected platform, I think we're in the very early days of fully being able to realize the power of controlling every aspect of your home through this type of platform. And so as we continue to open up that opportunity, we're really refining the organizational capabilities to drive those engagement interactions through our service platforms, so both on the customer service side as well as during in-home service business.

David H. Bywater
Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

I mean the most – the thing I'm most excited about of the whole company is [indiscernible] (01:00:36) down to one thing, it's engagement. It's the engagement that customers have. When we talk about those 12 times per day, it was 11 just, I think, a quarter ago or two quarters ago. So it continues to grow up, go up and up and up. And if you've got the engagement working in your favor, other positive things come along, usage, growth and so.

Q

Awesome. Okay. Thank you.

David H. Bywater

Chief Executive Officer & Director, Vivint Smart Home, Inc.

A

Thank you.

Operator: Thank you, Mr. [ph] Khan. (01:01:11) There are no additional questions waiting at this time. I would like to pass the conference back to David Bywater, CEO, for any closing remarks.

David H. Bywater

Chief Executive Officer & Director, Vivint Smart Home, Inc.

Thank you. I appreciate that, Bethany. Just in closing, once again, I appreciate you guys' interest in the company. I appreciate our employees. I think they did a phenomenal job in Q2. There was so much headline news around all of the headwinds. And we definitely felt them, but our team did a great job of responding. I think they're focused on the customers, they're focused on how we delight them better and the fundamentals of the business. I think we've got a great roadmap going forward. For me, I'm excited about our roadmap and encourage for us to execute.

I think the one thing we've done since we've been a public company is we've consistently executed and we've done what we said we're going to do. I expect that to continue the case going forward. So our employees, I message them to continue to execute and deliver on our promises. Hopefully, you guys see that come through.

So appreciate you guys' interest, and we'll take after – calls afterwards one-on-one. Thanks so much, guys.

Operator: That concludes the Vivint Smart Home, Inc. second quarter 2022 financial results conference call. I hope you all enjoy the rest of your day. You may now disconnect your lines.