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NRG Energy, Inc. (NRG)

Q3 2022 Earnings Call

CORPORATE PARTICIPANTS

Kevin L. Cole
Senior Vice President-Investor Relations, NRG Energy, Inc.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc.

Robert J. Gaudette
Executive Vice President-NRG Business, NRG Energy, Inc.

Elizabeth R. Killinger
Executive Vice President-NRG Home, NRG Energy, Inc.

OTHER PARTICIPANTS

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.

James Kennedy
Analyst, Guggenheim Securities LLC

Angie Storozynski
Analyst, Seaport Global Securities LLC

Michael Lapides
Analyst, Goldman Sachs & Co. LLC

David Arcaro
Analyst, Morgan Stanley & Co. LLC

Steve Fleishman
Analyst, Wolfe Research LLC

MANAGEMENT DISCUSSION SECTION

Operator: Good day and thank you for standing by. Welcome to the NRG Energy, Inc. Third Quarter 2022 Earnings Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. [Operator Instructions] Please be advised that today's conference is being recorded.

I would now like to hand the call over to today's speaker, Kevin Cole, Head of Investor Relations. Please go ahead.

Kevin L. Cole
Senior Vice President-Investor Relations, NRG Energy, Inc.

Thank you, Catherine. Good morning and welcome to NRG Energy's third quarter 2022 earnings call. This morning's call will be 45 minutes in length and is being broadcast live over the phone and via webcast, which can be located in the Investors section of our website at www.nrg.com under Presentations & Webcasts.

Please note that today's discussion may contain forward-looking statements, which are based on assumptions that we believe to be reasonable as of this date. Actual results may differ materially. We urge everyone to review the Safe Harbor in today's presentation, as well as the risk factors in our SEC filings. We undertake no obligation to update these statements as a result of future events, except as required by law. In addition, we will refer to both GAAP and non-GAAP financial measures. For information regarding our non-GAAP financial measures please see the most directly comparable GAAP measures, please refer to today's presentation.

And with that, I'll now turn the call over to Mauricio Gutierrez, NRG's President and CEO.

Mauricio Gutierrez

President, Chief Executive Officer & Director, NRG Energy, Inc.

Thank you, Kevin. Good morning, everyone, and thank you for your interest in NRG. I'm joined this morning by Alberto Fornaro, Chief Financial Officer. Also on the call and available for questions, we have Elizabeth Killinger, Head of Home; Rob Gaudette, Head of Business and Market Operations; and Chris Moser, Head of Competitive Markets and Policy.

I'd like to start with the three key messages for today's presentation on Slide 4. We're narrowing our 2022 EBITDA guidance to the bottom end of the range, as we indicated on our last earnings call and we are initiating 2023 financial guidance in line with our Investor Day plan.

We continued to make good progress on our strategic priorities and have now completed the initial phase of our test and learn program. The insights that we have gained from this process will inform our next phase of growing from our core energy business into adjacent essential home services. Finally, as I committed to you, we are announcing our 2023 capital allocation plan, which includes an incremental $600 million share repurchase program consistent with our long term capital allocation principles.

Our business performed well during the third quarter, which was characterized by extreme price volatility and record load in our key Texas market. I am very proud of our team, which once again achieved another quarter of top decile safety performance despite these challenging market conditions.

As you can see on slide 5, we delivered $452 million of adjusted EBITDA. The entirety of the change compared to last year was previously identified, with 60% coming from asset sales and transitory impact and 40% from the unplanned outage at our W.A. Parish facility. With these results, we are narrowing our 2022 EBITDA guidance to the bottom end of the range. Alberto will provide additional details in his section.

We also made good progress on all our key strategic priorities. We have now achieved our Direct Energy synergy target for 2022 and remain on track to achieve the full run rate of $300 million by next year. We continue to optimize our generation portfolio by retiring uneconomic fossil fuel plants, monetizing non-core assets, and partnering for brownfield development. As part of this effort, we are selling the Astoria site for approximately $200 million in net cash proceeds.

On our growth program, we continue to focus on cross-selling power and gas to our existing customer network. And with respect to our test and learn program, we have gained significant insight, and are ready to start executing on our plan, I will discuss in greater detail later in the presentation. We also have made good progress on our $1 billion share repurchase program for 2022, with $603 million completed today and $397 million yet to be completed.

Finally, today, we're introducing 2023 financial guidance of $2.27 billion to $2.47 billion of adjusted EBITDA and $1.52 billion to $1.72 billion of free cash flow before growth, in line with our Investor Day outlook.

As I mentioned to you, weather conditions in Texas were extreme this past summer, with ERCOT surpassing the old peak demand record 39 times, driven by record heat in the early part of the summer and a strong Texas economy. As you can see on the bottom left of slide 6, power price expectations which are shown in the light blue bars were as wide as I have ever seen them. This volatility was the result of record load, coupled with uncertainty around production from non-dispatchable renewable generation.

Importantly, it took record sustained heat, coupled with low renewable production to materialize into the high, real-time power prices we experienced in May and July. It is worth pointing out that even during these scarcity periods, we never triggered an emergency event, not even once. This is a testament that the Texas grid is strong and working as intended with enough capacity to meet current and future demand.

Turning to the right-hand side of the slide, we continued to see strong demand from our customers with no notable increase in bad debt levels. Retention has also remained strong driven in part by our unmatched insights to pricing and customer preference, which enables us to navigate periods of high price and high volatility. We have also been successful in extending the average term of a new Texas customer contract to two years. This extension is good for both our customers and our shareholders, given it adds stability and predictability to customer bills and our earnings.

On the supply side, our generation portfolio performed well during the summer, while the team managed the impact of the W.A. Parish Unit 8 outage. We were able to expand our maintenance program ahead of the summer, which resulted in better operational performance. Looking ahead, and as I discussed in our last call, we will increase maintenance capital in our plants given higher power prices.

Now I'd like to spend some time talking about our ongoing efforts in moving closer to the customer. We introduced the diagram on slide 7 during our Investor Day to capture our vision of the smart home. As you can see from the table on the right, we have made substantial progress in laying the foundation to execute on our vision to become the leading provider of essential services at home. During the year, we evaluated over a dozen adjacent offerings and engaged in multiple partnership pilots for EVs, home solar and other home services. By starting small, it allowed us to stay nimble while gathering critical market intelligence to inform how we approach these new customer offerings. The result of these programs help validate our assumptions and provides confidence in how to execute our customer-centric strategy.

Now let me put a finer point on our key findings on slide 8. First, the Internet of Things is here and is enabling the smart home opportunity. People are connecting new devices every day with an average of 25 devices per home. This number has more than doubled since 2019 and continues to grow rapidly, resulting in multiple interfaces that don't necessarily interact with each other. Customers want simple, connected and customized experiences. It is clear that a single interface for the home is of increasing importance and customer attitudes around these services are shifting from nice-to-have to need-to-have.

Next, the electrification of the economy through smart technology and clean energy choices is real. We are seeing an increasing number of devices and appliances connected like HVAC, water heaters, battery, rooftop solar and other, in addition to having greater penetration of electric vehicle.

Finally, customers are demanding access to cleaner, affordable and more resilient solutions. This is in part driven by a desire to be a part of a more sustainable future, reinforced by a need for resiliency in the face of more extreme weather. And importantly, this has been accelerated by advancements in technology and policy.

With this integrated ecosystem at home, there is a significant value opportunity, as you can see on the right-hand side of the slide. For NRG, we can offer adjacent products and services that leverages our existing energy operating platform, allowing us to access cost savings and provide superior customer experience. This advantage means broader insights into how customers interact with their homes, which translate into additional margin opportunities and increased brand loyalty.

Now turning to slide 9. In 2023, we will increase efforts to grow our bundled essential products and services through a mix of existing offerings, strategic partnerships, and vertical integration. All of them aimed at making NRG the leading provider of essential services at home.

We are also providing our capital allocation plan for 2023, which is in line with our long-term capital allocation principles. Our plan is to return 50% of our capital available for allocation to our shareholders, with an incremental $600 million share repurchase program, and an 8% increase in our annual dividend. For the remaining 50%, we're allocating $331 million to identified growth investments and reserving $620 (sic) [$628] million to be deployed throughout the year to the highest return opportunity between growth and share repurchases.

So, with that, I will pass it over to Alberto for the financial review.

Alberto Fornaro

Chief Financial Officer & Executive Vice President, NRG Energy, Inc.

Thank you, Mauricio. I will now turn to slide 11 for a review of the third quarter results.

NRG delivered $452 million in adjusted EBITDA, a $350 million decline versus prior year. Similar to our Q2 results, this year-over-year decline was the result of previously announced variances. As shown in the chart on the bottom left side of the slide, $190 million of the decline was from asset sales and retirements, plus the transitory items included in our initial guidance. The remaining $125 million variance is almost entirely due to the replacement power cost related to the unplanned Parish Unit 8 outage and maintenance expenses in the same unit for which we expect reimbursement from the property insurance company in Q4 of this year.

Texas adjusted EBITDA declined $263 million compared to the third quarter of last year. July was the second hottest month on record dating back to 1895, which drove extreme price volatility and higher load. This amplified the financial impact of the unplanned outage, given the need to replace this power with a mix of higher cost internal generation and market purchases to satisfy the weather-driven increase in demand. Q3 results in Texas were also impacted by higher operating cost in the form of increased maintenance expense. Approximately half of the increase was for work at W.A. Parish Unit 8 that will be reimbursed by insurance in Q4 and the remaining increase from our maintenance program that help insure strong reliability of the rest of the fleet through a volatile summer.

Turning to the East, West and other segments, the year-over-year decline of $52 million was primarily driven by the reduction from previously announced asset sales and retirement and supply chain constraints. Now, after taking those item into account, adjusted EBITDA increased by $111 million compared to Q3 of 2021 from increased revenue rate, natural gas optimization and operations at Cottonwood. Briefly referencing year-to-date results, NRG has delivered adjusted EBITDA of $1,390 million, a $671 million decline versus prior year. The drivers of our year-to-date results are similar to that of the quarter with permanent and transitory items, the unplanned outage of W.A. Parish Unit 8 and increased maintenance expense driving the decline versus prior year.

The free cash flow before growth for both Q3 and year-to-date results have been impacted by reduced year-over-year EBITDA levels as discussed earlier and an increase in net working capital. Working capital requirements increased progressively during the year due to higher gas and power prices and in Q3 due to combined effect of higher seasonal power receivables and natural gas inventory. We have also seen a $32 million increase year-over-year in maintenance CapEx driven entirely by spending to repair the Limestone and the W.A. Parish Unit 8 facility. This increase spend will be recovered by year end through property insurance proceeds.

Next, I want to update you on the achievement of Direct Energy synergies. We have achieved our full year target of $50 million during the quarter and continue to remain focused on achieving the full $300 million run rate next year.

Now moving to the full year 2022 guidance, we are narrowing our adjusted EBITDA range to $1.95 billion to $2.05 billion. In line with my previous comment of success in partially offsetting the $220 million negative impact from Parish Unit 8 unplanned outage, at this time we are at the bottom of the range.

Now, given the implied stronger Q4 results let me provide additional detail. We are expecting over a $200 million increase versus prior year, about $100 million coming from Direct Energy synergies, insurance proceeds for Limestone and Parish and other general cost reduction. The remaining coming from power and natural gas optimization opportunity leading us to make our natural gas full fleet, fully available in Q4.

Now turning to 2022 free cash flow before growth guidance. We are reducing our full year guidance range to $950 million to $1.050 billion, with one third of the reduction from the narrowing of the adjusted EBITDA guidance and two-thirds from the temporary increase in working capital from higher prices and inventories. And so, as we head into the winter season, we made the conscious decision to increase our inventory levels for both natural gas and coal, to provide contingency against the transportation challenges and the potential for extreme winter weather driving a $50 million reduction in the free cash flow for the year.

We have captured the reversal of these higher inventory quantities in our guidance for 2023, which I will discuss later in the call. In addition to the higher inventory quantities, prices for natural gas and power have also increased since the last call, resulting in an additional value of our inventories and net receivables for approximately $140 million, which will be reversed with lower commodity prices. The combined $190 million impact of these factors results in reduced expectation for 2022 free cash flow before growth.

I will now turn to slide 12 for an update on our planned 2022 capital allocation. Consistent with past practice, we have highlighted change from last quarter in blue. Starting from the left, we have updated the midpoint of our free cash flow before growth guidance by $290 million, $100 million for lower EBITDA guidance and $190 million from increases in working capital. As you know, cash generation is a key objective for NRG and our team has been focused on offsetting these negative impacts. We were able to offset a significant portion of those reduction by capturing $212 million of net cash proceeds from the sale of Astoria, allowing us to utilize and distribute capital consistent with our commitments.

Next, we expect to capture an additional $6 million from Winter Storm Uri mitigants related to additional recovery. Next, we continue to make progress in executing our $1 billion share repurchase program. At the end of October, we have $397 million to be completed by around year end. And finally, we have committed $100 million of OpEx and CapEx spend related to our $2 billion growth plan, which when coupled with our investment – other investments, leaves $286 million of capital available for allocation.

Moving to 2023 adjusted EBITDA and free cash flow before growth guidance. We are pleased to announced that our expectation for 2023 aligned with previous target, we are introducing strong 2023 financial guidance of $2.27 billion to $2.47 billion for adjusted EBITDA and free cash flow before growth of $1.52 billion to $1.72 billion. EBITDA guidance includes the full year impact of asset sale and other permanent items that we captured in our guidance for 2022. Although we expect continue impact from coal constraints, we are able to offset those and the other transitory items that impacted our 2022 guidance.

I will now turn to slide 14 for the introduction of our 2023, $1.9 billion capital allocation plan. As Mauricio mentioned in his section our capital allocation is directly in line with our long-standing principles and cadence of allocation. Today, we are starting the conversation by allocating 50% to shareholders through both dividends and share repurchases and allocating a portion of the 50% opportunistic to identified growth, leaving 35% to be allocated throughout the year to the highest returning investments while maintaining a strong balance sheet.

Now moving left to right, we start with the midpoint of our free cash flow before growth guidance, a range of $1.62 billion plus $286 million of unallocated 2022 CAFA, capital available for allocation, totaling $1.9 billion in capital for allocation.

Next, we have allocated $220 million identified for our growth program and $111 million for other investments to fund additional investment to support the integration of Direct Energy, innovation project and small book acquisition. Next, on return of capital. We are allocating $347 million to dividends consistent with our 7% to 9% annual dividend per share growth target and announcing a new share repurchase program of $600 million to be executed immediately following the full execution of our current $1 billion program.

Finally, this leaves $628 million of 2023 capital available for allocation to be allocated throughout the year. We look forward to providing you with updates to our progress throughout 2022.

Back to you, Mauricio.

Mauricio Gutierrez

President, Chief Executive Officer & Director, NRG Energy, Inc.

Thank you, Alberto.

I want to provide some closing thoughts on slide 16. We have made significant progress across all of our key priorities this year, including the Direct Energy integration, portfolio optimization, and our test and learn program and returning capital to shareholders. I'm incredibly proud of the team's efforts and focus over the last 24 months on executing our strategy.

As we look into 2023 and beyond, we remain on track to achieve our long-term goals of high-grading our earnings quality by expanding our customer lifetime value, and providing a compelling annual total return to our shareholders of 15% to 20% free cash flow before growth per share and 7% to 9% annual dividend growth. Our platform is well positioned to deliver strong and predictable results and create significant shareholder value as the leading essential home services provider. I look forward to updating you on our progress along the way.

So, with that, I want to thank you for your time and interest in NRG. Catherine, we're now ready to open the line for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from Julien Dumoulin-Smith with Bank of America. Your line is open.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.
Q

Hey. Good morning, Mauricio and team. Pleasure to be here. Thank you, guys.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.
A

Hey, good morning, Julien.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.
Q

Hey. Good morning. I hope the parade made things okay this morning.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.
A

Well, it disrupted traffic a little bit, but there is nothing like a great celebration after that win.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.
Q

Absolutely. Absolutely. Well, hey, listen, I just wanted to start off strategically here. We've been at it for a little bit here in this transformation, power prices remain relatively higher. How do you think about the state of the generation portfolio overall? How are you thinking about evolving your decision tree on that? Obviously, we saw here in the quarter, but even beyond that, how are you seeing things, whether that's tied to a driven by IRA or otherwise here in terms of optimizing your generation portfolio?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.
A

Thank you, Julien. Well, so let me take a little bit of a step back, because obviously you need to look at the generation portfolio in light of our integrated retail platform, right? I mean, we have said that the goal of the generation portfolio now is to help better supply and serve our customer needs. So, when I think about our generation portfolio, I think about our overall supply strategy. And that is one where we have decided to diversify our supply to have some internal generation, to have third-party PPAs and obviously market purchases. All of those three things make our supply strategy.

Now, with respect to the generation portfolio, as you mentioned, higher power prices have led us to basically self-insure to have greater reliability because the value of each megawatt is much higher today than it was just 10 months ago with higher power prices and higher gas prices. So, that's why you're going to see an increase in our maintenance capital, because we want to make sure that we have greater reliability on our fleet.

Obviously, we're always optimizing our supply. And right now, the value that it provide for our integrated platform is very high. But there is always an opportunity to optimize that generation portfolio depending on market conditions and the opportunities that we see in the market.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.

Q

Got it. All right. Fair enough. I'll leave it there. Let me pivot, if I can, to the other side of this equation. And that is just the guidance and sort of the cadence of the guidance. Obviously, the implied fourth quarter is reasonably elevated, and certainly that's despite some of the ongoing pressure points that we saw in third quarter.

Can you talk about what that implies for the cadence of results in 2023 here? How do you think about the first half? How do you think about third quarter going forward, given the sort of evolution in your business model? Should the third quarter into the future be perhaps a little bit more depressed, relatively speaking? Can you just elaborate on what the implications are? Maybe that's an Alberto question here.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Yeah. Well, I'll turn it over to Alberto, but let me just give a little framework. I mean, I think the big takeaway, I hope, for everybody is that in 2023, we go back to the guidance or the outlook that we provided during our Investor Day. Our EBITDA guidance and our free cash flow guidance goes back in line with what we provided to you last year. We're turning the page and we're just excited about the opportunities that we have to continue growing our business, our core energy business, but importantly, adjacent products and services. With respect to the seasonality of earnings, I think you should expect us going back to where we were perhaps in 2021. But Alberto, can you provide additional insight here?

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc.

A

Yes. I think more than looking at first half versus the second half, I would say that probably you will see the two critical quarters being the second and the third. And so, you will see probably more balance and more in line, as Mauricio said, with the past and potentially even the fourth quarter this year is higher than the normal. So, I would say, again, probably get back to 2021 profile is what we should expect.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.

Q

Okay. Excellent. And that includes some of these coal dynamics annualized here in the first half and some of the outage dynamics still net-net-net 2021 kind of profile?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Yes. I mean, if you think about some of these coal supply issues, we were very transparent last year when we introduced them. And, the team has done a tremendous job in mitigating this coal supply chain issue, particularly in Texas. I mean, we continue to have something in the East and team is just working through that. But, as I mentioned to all of you when we introduced these, these are temporary. The coal supply chain was significantly stretched because of the very rapid increase in natural gas prices. And I also said with time both coal suppliers and railroad providers scale up again their operations, and that's what we're seeing in our – with our key suppliers.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.

Q

Got it. All right, guys. I will leave it there. Go 'Stros. See you soon.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Go 'Stros. Thank you, Julien.

Operator: One moment. Our next question comes from Shar Pourreza with Guggenheim. Your line is open.

James Kennedy
Analyst, Guggenheim Securities LLC

Q

Hey, guys. Good morning. It's actually James for Shar. Congrats on the update and thanks for taking the questions.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Hey. Good morning.

James Kennedy
Analyst, Guggenheim Securities LLC

Q

So, I guess, just starting with the 2023 capital allocation plan, what are the trigger points, the time line expectations for the balance of the uncommitted capital? Are you potentially looking at more growth as we get through the year, or is this just simply a function of waiting to see how the business performs through the first half?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Well, so two things. The first one is, as I committed to all of you this year, we're actually announcing both our earnings guidance as well as our capital allocation. If you remember, in the past, we used to provide the capital allocation in the fourth quarter earnings call. So the first thing is, we're now providing this, too, much earlier than in the past. The second thing is always, our capital allocation, we try to – the cadence happens – with the cadence when we generate cash, and this is not going to be any different. But as I said on my prepared remarks, the additional excess cash that we have available for allocation will be allocated throughout the year based on the highest return opportunity that we have. 2023, we start executing on our plan, we're evaluating opportunities, but if these opportunities don't yield highest return compared to share buyback, then we will allocate that to share buybacks. Just that simple.

James Kennedy
Analyst, Guggenheim Securities LLC

Q

Okay. And then I guess, kind of a similar question on the growth CapEx. How should we think about the timing and shape of any EBITDA accretion as you ramp up that spend, something that can we get more color on and steps in the coming quarters or just any color there?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Yeah. Well, I mean, remember that, as we execute on our plan, we always have three options, right? We either build them or grow organically, we partner or we buy them – we acquire something. So in the build or organic grow, there is always a lag between when you make the investment and when you receive some of those earnings. And similar to the partner, and I would say, the acquisition that really accelerates earnings immediately, right? So, we're right now evaluating options and our – both our business model and our go-to-market. The one thing that I will say is, as I think about the growth, there are some areas that – first of all, it's a very narrow scope, and I provided that scope in the slide that I presented to you today.

The second thing is there are some areas where we know that we're not going to do it, that the business model is such that we will partner. For example, Home Solar we're not going to go into the entire value chain of Home Solar. We are going to partner. We have a lot of lessons learned here and I have been very clear about that. So the pace of which the earnings are going to come in, it is really going to be dictated by how do we execute our strategy and we go to market. So it will be provided to you in the coming quarters as we start executing those.

James Kennedy
Analyst, Guggenheim Securities LLC

Q

Perfect. I will leave it there. Thank you very much, guys.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Thank you, James.

Operator: Thank you. Our next question comes from Angie Storozynski with Seaport. Your line is open.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Thank you. So, first on the IRA, the Inflation Reduction Act. So I see that there is a $45 million increase in cash taxes in your 2023 free cash flow guidance. And I know that we're still waiting for the IRS to provide some more clarity on cash taxes. But can you talk in general how you see it over the next couple of years?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Good morning, Angie. I'll pass it to Alberto.

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc.

A

Yes. First of all, Angie, let me say that the increase in the taxes – the tax payment that you see for 2023 are really due to two factors. One, we are forecasting higher net income for the year and therefore higher federal and state taxes. And the other piece is we got the refund for the DE, on the DE side in 2022 that will not happen in 2023 and therefore they are more or less half and half, that explained increase year-over-year. We have – from the IRA, we have factored in our forecast the impact of the 1% taxes on share buybacks. However, there is no impact for the minimum tax because at this moment we don't have any indication that the payment based on 2023 net income will be done in 2023. And so when we have more information regarding when these payments, if any, is due then we will update you.

In general, I would say, as we have said in the past that it's very difficult to do forecasting based on the level of information that we have. But so far, all the indication is for relatively modest impact and also is a temporary impact that we'll recover after a few years. As soon as we get more detail, we will be more precise.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Okay. Thank you. And then separately, also related to the same legislation. So I'm assuming that you are seeing some pickup in renewable power growth, especially in Texas. And I'm just wondering if that means that you should soon announce some additional PPAs, again, given that the availability of especially solar assets should increase in Texas.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Sure. I'll have Rob address that, Angie.

Robert J. Gaudette
Executive Vice President-NRG Business, NRG Energy, Inc.

A

Hey, Angie, good morning. So, when you think about the IRA, you're spot on, right, it provides clarity to the renewable developers. We are in the market all the time, right, so it's not – we've been kind of at this for a while, so there's a couple factors in here that we think about. One is availability for them to get their panels on the ground and get them installed. It's the developers in the pipeline that they're kind of working through. And then the IRA provides them some clarity around their financing. So what I would expect – I haven't seen it yet, but I would expect that some of this clarity starts coming in to more certainty around offers into us and as opportunities show up we'll lock those up as they make sense for our portfolio. But you're right, the IRA should push solar, wind and battery development across all markets in the US.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Yeah, and particularly in Texas when you look at the plan that ERCOT provides and what we're tracking, I mean, most of the new generation is really renewable energy. So this should help and accelerate. We have this capability pretty well. It's a well-oiled machine we have been executing before there was a slowdown and our expectation is it's going to pick up and we have great visibility as to when that happens and also the economics around it.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Okay. And my last question is the maintenance expense in CapEx in 2023. So I understand that you are spending more money in light of the higher level of power prices. But is this a level that we should actually expect going forward? Is this just a one-off year with like some major maintenance or something that was either pulled forward or catchup from previous years?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Well, I mean, I'll ask Alberto to address some of it. I mean, my take – remember, 2023 has two big components, right, I mean, the first one is the money that goes into the Unit 8 at W.A. Parish and then the second one obviously is the increase in maintenance because we want to self-insure given that every megawatt is more valuable with higher power prices. I mean, that's something that the market is going to dictate. What I will tell you is I'm incredibly proud of the team that is so nimble on our generation fleet during years where gas prices were very low, they tightened the valve, they adjusted the maintenance. It was the right decision because not every megawatt was as valuable as it is today. We very quickly pivoted to that. And as I mentioned, we put some capital at work before the summer that yielded really good results. And, we're going to continue to do that. So, Alberto, I don't know if there's anything else you want to say?

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc.
A

Yeah. So I just would like to point you to in the appendix, there is a page in which we highlighted impact on our maintenance CapEx coming in 2022 from Limestone and Parish and also for 2023. Long story short, when you eliminate the impact of these specific CapEx that we have spent, you will see that there is around $40 million to $50 million increase in the maintenance CapEx. And this is really due to the fact, as Mauricio was mentioning, that given the current prices, we think that it is appropriate to increase the reliability of our fleet to basically catch all the opportunities that the current price environment is offering to us.

Angie Storozynski
Analyst, Seaport Global Securities LLC
Q

Great. Thank you.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.
A

Thank you, Angie.

Operator: Thank you. And our next question comes from Michael Lapides with Goldman Sachs. Your line is open.

Michael Lapides
Analyst, Goldman Sachs & Co. LLC
Q

Hey, guys. Congrats on a good quarter.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.
A

Thank you, Michael.

Michael Lapides
Analyst, Goldman Sachs & Co. LLC
Q

I'm looking at slide 14 and I just want to make sure I understand some of this and a little bit of this may be more nuanced. So, the growth plan, the $220 million, can you – what asset – is that for one big asset or is it for lots of little things?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.
A

No, it is a – I mean, this is really to support our test and learn. So, we have identified a number of opportunities and the scope of those opportunities are actually on slide 7, Michael. So, when you look at whether it is solar, storage, electric vehicles, energy management, protection, security, I mean, the scope is really around the essential services. And this is what we have been able to identify today. Obviously, we're working through the execution of our plan and we will provide updates as we – throughout the year.

Michael Lapides
Analyst, Goldman Sachs & Co. LLC

Q

So, let me just – and this might be one for Alberto. So, the $220 million in the growth plan and the $111 million in the other investments, are these all – like when I look through the three statements at this time next year, are they going to flow through CapEx or are they going to flow through cash from operating activities, meaning is it working capital, or do some of these actually weigh on EBITDA until they start generating EBITDA, like your guidance for EBITDA would be higher if you weren't doing this spend?

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc.

A

No, regarding – okay, regarding the other investment, these do not impact EBITDA, they are outside EBITDA. When you look at the growth plan, there is a series of initiatives and we will update you about what is going to EBITDA or not. But for the moment, it's still – as Mauricio said, it's a series of different initiatives, and depending on which one we will prioritize, it will have more CapEx impact or not.

Michael Lapides
Analyst, Goldman Sachs & Co. LLC

Q

Meaning some of the – all right, so the $111 million is all based – about $111 million is all capitalized? And the $220 million, some of it is capitalized and some of it is flowing through G&A or O&M, and therefore – I'm just trying to make sure, because – like, I'm trying to think about recurring versus nonrecurring impacts on EBITDA.

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc.

A

That is a very good question. And what you said is correct, the $111 million, does not impact EBITDA; the $220 million, there are some initiatives that could have an impact on OpEx and others that have impact on CapEx, and we will qualify that in the next quarter.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

And just to put a finer point here, Michael, I mean the $220 million – and I want to highlight the word could impact, right? But as we are in the process of executing and depending on how do we finalize the go-to-market will have an impact on whether it goes to CapEx and OpEx. So, that's, as they say, TBD, to be determined, Michael, but we will provide that transparency as we start executing on the plan.

Michael Lapides
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Okay. Thanks, guys. I'll follow up offline.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Thank you, Michael.

Operator: Thank you. We have a question from David Arcaro with Morgan Stanley. Your line is open.

David Arcaro
Analyst, Morgan Stanley & Co. LLC

Q

Hey, good morning. Thanks so much for taking my questions.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Hey. Good morning, David.

David Arcaro
Analyst, Morgan Stanley & Co. LLC

Q

I'm wondering if you could talk a little bit to customer growth trends that you're seeing and any churn in the business. Are you still seeing kind of a flight to safety in this backdrop, in this high commodity price backdrop? I noticed that there was a slight decline in the total customer count versus the prior quarter. So, I'm curious, any information there.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Sure. Elizabeth?

Elizabeth R. Killinger
Executive Vice President-NRG Home, NRG Energy, Inc.

A

Yeah. Thanks for the question, David. We are really pleased with our performance, the team and the engine during a really volatile third quarter. We did perform – continued to perform in third quarter as we had year-to-date, better than our budget. You may recall from prior discussions, we do generally see customer attrition from large M&A, which was DE, which was very large as well as from small book acquisitions, which we have done a handful of those year-to-date. But the good news is we're performing better than expected on both DE and the customer books.

From a sales engine perspective, we have a very strong engine. Over-performance in the quarter occurred in both our face-to-face and our digital channels, and cross-serve also performed very well during the quarter, better than budget. And from a retention perspective, we also are seeing really strong performance given the backdrop of very high prices from both the cost increases associated with the power to fulfill for them, as well as the higher usage during some of the weather that we experienced. So, really pleased with the attrition during the quarter and looking forward to continuing to deliver for you, guys.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Yeah. And just – I mean, the team does a fantastic job on balancing customer count and margin, and that's what we do every day with tremendous insights from our customers. And as Elizabeth said, both our retention numbers and our bad debt numbers are pretty well in line, very robust. And customer count is just a result of a very intentional strategy around balancing customer count and retail margin. So, I'm very pleased with the team.

David Arcaro
Analyst, Morgan Stanley & Co. LLC

Q

Got it. Great. That's helpful. Thanks. And then, I was wondering if – maybe two quicker ones, but does the 2023 outlook include business interruption insurance proceeds coming in? Wondering how much that might be in the guidance. And then, maybe just a little more higher level, Mauricio. Is there still more to do in terms of portfolio in real estate optimization with where the business currently stands? Is that something you'll be looking at into 2023 as well?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Sure, Alberto?

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc.

A

Yes. So, regarding the business insurance proceeds, I can confirm you what we said in the prior call, and basically the negative impact of Parish 8 in the first half of 2023 will be absorbed by the insurance proceeds, as we have factored in our forecast.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

And with respect to the portfolio optimization, again, I mean, this is something that we're looking on a continuous basis. We haven't stopped. I mean, the Astoria sale and Watson is an example of what we're doing. A couple of quarters ago I said that we're going to move into evaluating brownfield development both in our Midwest fleet as well as in Texas. The team has been working on looking at these opportunities. And what I will tell you is also we're looking at potential partnering opportunities because we want to make sure that we – the capital that we use is the right structure. I don't want to create friction in the system if we don't have to. So both in terms of brownfield opportunities and in terms of partnering opportunities, we have been very busy and I hope to give you a more fulsome update in the coming quarters.

David Arcaro
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Great. Thanks so much. I appreciate it.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Thank you, David.

Operator: Thank you. And our final question comes from Steve Fleishman with Wolfe Research. Your line is open.

Steve Fleishman
Analyst, Wolfe Research LLC

Q

Hi. Good morning. Thanks. So, just for the 2022 guidance, the – I think your Texas segment is down $275 million maybe from the initial guide. How much of that is attributed to the Parish, Limestone outages net of any money you're getting back this year?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc. A

Hey. Good morning, Steve. I'll turn it to Alberto.

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc. A

Yeah. It's almost entirely the full amount that we highlighted in $220 million, Steve. So, that's the major...

Steve Fleishman
Analyst, Wolfe Research LLC Q

Okay. And then, $175 million boost in East/West/Other, could you just explain what's driving that?

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc. A

Yeah. So, normally, Steve, we are very conservative when we plan our gas optimization activity this year. Given the fact there has been a lot of volatility, the performance has been very good in that area. And also, obviously, we benefited from some higher margin from prices coming from our generation fleet in the East. But, normally you would see that if we do better in the East is driven by the gas.

Steve Fleishman
Analyst, Wolfe Research LLC Q

Okay. And then, just as we think about the 2023 guidance, are you assuming that that better optimization continues or that that rolls down some...

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc. A

No, we're more conservative

Steve Fleishman
Analyst, Wolfe Research LLC Q

Okay.

Alberto Fornaro
Chief Financial Officer & Executive Vice President, NRG Energy, Inc. A

We're are more conservative.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc. A

Yeah, it's always – I mean, Steve, we always use market as an indication to guide us in terms of the profitability of our portfolio, right? So, if you look at the heat rates for 2023, we use market prices – market heat rates to inform our guidance.

Steve Fleishman
Analyst, Wolfe Research LLC Q

Okay. Thank you. And then just the $397 million of buyback, you intend to complete that fully in the market by year end not – or are you going to do an ASR or something or?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

I mean, our intention is to complete towards the end of the year. And that's basically our plan right now.

Steve Fleishman
Analyst, Wolfe Research LLC

Q

Okay. And then, on ERCOT market structure, I mean it's kind of gotten quiet, but I think there's a lot about to happen. So just to the degree that they put in some kind of dispatchable market – separate market, how are you thinking about how that impacts your portfolio and how you manage that through the retail side?

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Well, I mean a couple of things. And I think you're absolutely right, Steve. It's going to get really busy, I think middle of November. There's going to be a recommendation from ERCOT and the PUCT. We've been working with them alongside throughout this entire time, we've provided our – a number of initiatives. I know that they're evaluating. At the end of the day I think that's also going to be informed by how the Texas grid has operated.

And as I said, I mean, we broke the load record 39 times this summer, and not even once we went into emergency situation. So I think the grid is well – when I look at the pipeline is very robust with lots of new renewable generation, so enough to meet current demand and future demand. So I think that's going to inform some of it. At the end of the day, they end up with some sort of dispatchable product.

We've been working really hard on terms of the brownfield opportunities on our own sites, and obviously that will play really well for participants like us who have sites in good locations already connected to the grid. And I think that gives us a cost advantage that we intend to fully utilize and monetize.

Steve Fleishman
Analyst, Wolfe Research LLC

Q

Okay. Okay. Thank you.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

A

Thank you, Steve.

Operator: Operator: Thank you. And there's no further questions in the queue. I'd like to turn the call back to Mauricio Gutierrez, President and CEO, for closing remarks.

Mauricio Gutierrez
President, Chief Executive Officer & Director, NRG Energy, Inc.

Thank you, Catherine. Well, thank you all for your interest in NRG, and I look forward to continue updating you as we move to our next phase in the company. So thank you all for your attention.

Operator: Ladies and gentlemen, thank you for your participation in today's conference. This concludes the call.