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NRG Energy, Inc. (NRG)

Investor Day

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MANAGEMENT DISCUSSION SECTION

Kevin L. Cole
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Good morning and thank you for joining us for our 2023 Investor Day. Today's scripted remarks will be 90 minutes in length and consist of six sections. First, Mauricio Gutierrez, our President & CEO, will frame the advancements that we have made in executing our consumer strategy roadmap last discussed during our 2021 Investor Day and specifically NRG's unique opportunity to optimize and grow our network of customers while returning significant capital to shareholders, strengthening our balance sheet, and further high-grading and stabilizing our earnings.

Following Mauricio's remarks, Elizabeth Killinger, Head of Home Energy; and Rasesh Pate, Head of Smart Home will unpack the increased scale and scope of our moat to create unique customer value. Next, Rob Gaudette, Head of Business, will discuss how we have further stabilized, optimized, and decarbonized our platform through our unique, diversified supply strategy. And after that, Bruce Chung, CFO, will provide additional details on our enhanced and extended financial outlook. And then finally, Mauricio will provide closing remarks, and then we'll welcome Q&A. At that time, I will prompt those from the investment community wishing to ask a question to dial into the Q&A phone line using the dial-in provided. But please be aware that once you have dialed in, you will need to mute your computers to avoid any echo or feedback.

Lastly, I'll read the Safe Harbor. Today, we will be making forward-looking statements that we believe to be reasonable as of this date. Actual results may differ materially. We undertake no obligation to update these statements as a result of future events except as required by law. Today's presentation refers to both GAAP and non-GAAP financial measures. Please refer to the Safe Harbor information on our non-GAAP financial measures and the reconciliations to the most directly comparable GAAP measures in today's presentation.

And with that, I'll turn the stage over to Mauricio Gutierrez, NRG's President & CEO.

Mauricio Gutierrez

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

Thank you, Kevin. Good morning, everyone, and welcome to our 2023 Investor Day. I want to thank you for joining us today and for your interest in NRG. It was only two years ago that we held our last Investor Day. We are proud to be back to provide you an update on our strategy and our execution plan. Before I begin the presentation, I would like to say that on behalf of the NRG board of directors and management team, we are focused on enhancing shareholder value. We welcome all of our shareholders' views and are committed to productive and meaningful engagement.

As you will hear today, we strongly believe our strategic plan puts us on the best path to create significant shareholder value now and well into the future. We've made great progress on our strategy to get closer to the customer. Since our last Investor Day in 2021, we have increased our customer base by 30%. We have continued optimizing our generation fleet and made improvements to our supply strategy. We have expanded into the smart home sector where we identified a significant and complementary opportunity given the convergence of smart technologies and greater electrification inside the home and we have maintained an efficient operating platform and a strong balance sheet.

Adopting to the rapid change in our industry is not without challenges. We recognized as a company in transition, we need to provide better tools and greater transparency to help you appreciate the full potential of our business. We are committed to doing just that. Today, you will hear about our progress to-date, an update on our strategic plan, and the value creation opportunity resulting from our consumer business.

I want to begin with the key highlights for today's presentation. NRG generates excess cash well beyond what it takes to run our company. With the acquisition of Vivint complete, we now have line of sight to the investment needs of our company going forward. Today, we are revising our capital allocation framework to 80% return of capital and 20% to growth. Consistent with this change, we expect to repurchase at least $2.7 billion through 2025 and are increasing our share repurchase authorization by $1.7 billion. This commitment demonstrates the level of confidence we have in our ability to generate excess cash today and tomorrow. We are also accelerating the achievement of our credit metrics targets by the end of 2025.

Now, moving to our business. Our core integrated energy model is strong and improving. We have made significant enhancements to our supply strategy and customer experience with the objective of delivering stable and durable margins. Recognizing that there is a convergence of energy and smart technologies inside the home, we expanded our capabilities with the addition of a leading smart home technology platform and an attractive subscription base recurring revenue business. We are excited about the benefits that this will create across our entire business. We expect to generate an incremental $400 million of free cash flow between cost synergies and growth by 2025.

Over the years, we have streamlined our operations and I am very proud of what the team has done to strengthen the business through various initiatives like the transformation plan, the direct energy integration, and now Vivint. We have a track record of successful integration and cost management with nearly $900 million of cost savings achieved since 2017. But this is a continuous improvement process that requires constant vigilance. That is why today, we are announcing an incremental $150 million cost initiative to be achieved by 2025.

Finally, we've had a deliberate process to evolve our board composition with a focus on diverse backgrounds and experience in alignment with our strategy. As part of this process, we are currently engaged with our independent search firm and evaluating feedback from our shareholders to bring additional expertise to our board.

Now, moving to the three-part strategic plan, which is focused on operating excellence, disciplined growth, and maximizing shareholder returns. First and foremost, our plan focuses on optimizing our core integrated energy model to deliver durable and stable margins. This includes enhancing our supply portfolio, maintaining cost efficiencies and optimizing our generation portfolio. We recently announced the sale of our minority equity interest in the South Texas Nuclear Project for $1.75 billion. This is a good example on our ability to extract value at the right time. Importantly, this asset sale has limited impact on our supply and stability of retail margins as it generates baseload power, which is abundantly available in the market.

Next in our plan is growing our business via adjacent products and services that make our consumer platform stronger and more durable. Following a period of evaluating business models and learning about new products, we accelerated our expansion into the smart home sector with the acquisition of Vivint. We are going to take a measured and disciplined approach to growth with very clear performance targets and profitability metrics. As part of our revised capital allocation framework, growth investments will be limited to 20% of excess cash.

Finally, we are committed to a clear and transparent capital allocation framework that maximizes shareholder value. Our business is expected to generate $8.3 billion of cumulative excess cash through 2027 after debt reduction. As I said, with more clarity on our business needs, we are now revising our capital allocation principles to increase capital return to our shareholders to 80%.

A robust business with a clear and achievable strategic plan creates an incredible value proposition. We have a consumer business with stable, durable, and predictable earnings that generates significant excess cash that will be allocated in a way that delivers superior returns on a per share basis. A balance sheet that helps navigate different economic cycles and a sustainability program that is embedded in our culture to deliver value to all stakeholders. It is very compelling.

The evolution of our business has been both significant and necessary. At our 2018 Investor Day, we shared our plan to transition from a pure integrated power model to one that was increasingly focused on the customer. We were looking to create greater cash flow stability and access more attractive markets given the trends that we're shifting value away from traditional wholesale power and towards the consumer. In 2021, we further unpack our consumer strategy with a focus on evaluating adjacent products and services that could complement and enhance our energy offering. We kicked off test and learn process that helped inform our expansion into the smart home sector.

Today, we are providing you an update on our progress, the opportunities that we identify and how our consumer platform is positioned to create value during this period of transition in the energy industry. The [ph] trends that inform (00:10:59) our strategy continued to accelerate at a rapid pace. We are experiencing greater electrification of our economy and increasing adoption of smart and connected devices in the home. The most relevant aspect for us is the convergence between the two.

New value opportunities are emerging from EVs and rooftop solar to smart devices on portable batteries. Smart technology is making electricity more controllable than ever before. At the same time, there continues to be a build out of renewable energy and grid scale batteries, which combined with increasing demand side load management, are creating headwinds for conventional power generation assets. These trends support our evolution towards the consumer and the home.

Apart from monitoring trends, over the last two years, we have been running small scale tests in targeted growth markets. This process gave us insights into how to best execute our growth strategy from required capabilities to business model trade-offs. I want to point out a few of the key insights and learnings from this process. The first one and perhaps the most important is that owning the core technology platform inside the home is necessary to access data and control the customer experience.

We learned this first-hand with some of our smart thermostat partners where data, access, and customer relationship became limited. Having a direct customer relationship is how we build brand awareness, reputation, and create stickier relationships. It is something we just cannot outsource. For certain products, we validated that our partnership model provided the best risk reward economics, like in the case of rooftop solar. We also saw that for larger and more integrated products in the home, customers needed an expert partner to help navigate the sales process. This is true not just for solar, but for products like EV chargers and batteries.

Our testing also validated that residential energy demand is going to be more controllable than before, and that creates an opportunity to provide valuable services to the grid and the wholesale market. As part of this test and learn process, we also evaluated the best way to execute our strategy. Two things became clear. First, we needed to enhance and expand the capabilities of our core energy platform to better compete and create customer value. Second, we needed another entry point into the home beyond grid power, given the merging of energy and smart technologies.

Vivint provides us with an end-to-end proprietary smart home technology platform. We can now go deeper into the home and connect all our products and services in an integrated and seamless way. It also provides a rooftop solar cells engine consistent with our partner approach and a direct-to-home consultative sales channel that complements our own sales platform. Beyond these additional platform capabilities, the Vivint acquisition added 1.9 million high credit quality customers with long tenures and recurring revenues across a much broader geographic footprint.

It is important to know that Vivint gives us direct access to customer relationships that were not available through our retail energy outside of Texas. While Vivint provided many of the capabilities that we were targeting, the work that NRG had been doing internally will be critical to maximizing the value between the two businesses. We have made great strides in enhancing our digital customer experience with a more engaging interface and data which increases brand awareness and customer stickiness. We revamped our digital app with additional capabilities like EV and rooftop solar integration, reinforcing the concept that NRG is more than just retail power.

And as part of our technology platform, we develop a single view of the customer with a state-of-the-art data lake that allows us to better understand customer behavior on pricing and offers. Our consumer business now has two primary gateways into the home with leading brands in energy and smart home. Not only does this increase our sales capabilities and expand our funnel, but it drives greater diversification of earnings and doubles our addressable market. We now have an entire ecosystem of brands, products, and services connected with a common technology platform. This connectivity gives us cost efficiencies and better insights that allow us to meet our customers where they are with better offers and better experiences. This ultimately creates deeper and more durable customer relationships that translates into a substantial uplift in lifetime value of our customer portfolio.

Moving to the execution of our strategic plan that we announced in 2021. We are making good progress as you can see on the table. We are on track to achieving $300 million of cost savings as part of the Direct Energy acquisition by the end of the year. And we have been optimizing our generation portfolio with the sale of non-core assets. Our energy and home services business has grown substantially with the Vivint acquisition, which brings strong and stable margins, making our consumer platform more valuable. And we are increasing our return of capital now that we know our investment needs. While we still have work to do, these achievements show we are moving in the right direction and we see additional upside ahead.

Let's start with how we're optimizing our energy business with our review of our cost improvement programs. As you can see, we have executed extensive and rigorous cost reduction programs over the past several years, resulting in $900 million of savings. We are currently focused on finalizing the cost savings of the direct energy acquisition, which we expect to complete successfully by the end of the year. The Vivint acquisition provides an additional $100 million of cost synergies, which is the result of combining two public companies with a complementary sales and marketing platform. This process is well underway and we will be providing updates as part of our acquisition scorecard.

Maintaining a cost efficient platform is a continuous process, particularly for a company in transition like NRG. With that in mind, today, we're announcing a new cost reduction initiative of $150 million by 2025. We have identified savings in two areas: creating efficiencies in our generation business after a period of high natural gas and power prices over the past two years, and efficiencies across our expanded consumer platform. I am proud of the cost savings we have been able to achieve. But we need to stay always vigilant of our cost structure, particularly as we continue to evolve our operating platform and optimize our portfolio.

Our supply strategy has also evolved with the markets. One of the big lessons learned from Winter Storm Uri is that diversification of resources is critical to managing supply risk. This means minimizing any single point of failure, whether in a large power plant or a supply arrangement with a single counterparty. Power markets are in transition with increasing amounts of renewables. This increase adds volatility in any single hour depending on whether the wind is blowing or the sun is shining. We have evolved our supply strategy from one where we own every megawatt that we use to serve our customers to one where we diversify our risk and strike the right balance between plant performance risk, counterparty or credit risk, and market risk.

I want to be clear. We will own generation. But we need to make sure it has the right attributes to help manage our customers' power demand and help deliver stable margins to our consumer business. The supply optimization and risk management activities are performed internally by a highly skilled team in our market operations group. This is in stark contrast to many of the retail only providers that outsource this capability to financial institutions on their commercial agreements.

Our risk management and commercial capabilities are core to our business. It's a competitive advantage and a clear differentiator with other market participants. Our generation portfolio is an integral part of our improved supply strategy. We own and operate 13 gigawatts of generation capacity that is diverse in fuel mix, merit order, and geographic location with about 70% located in the State of Texas.

As we think about the future composition of our portfolio, we want to increase the load following capabilities of our supply and continue lowering our emissions with responsible coal retirements. Over the past two years, we continue optimizing our portfolio. Recently, we executed the sale of Astoria in New York and our minority interest in the South Texas Nuclear Project at attractive economics resulting in nearly $2 billion in assets sale proceeds.

One of the criteria for optimizing our portfolio is to increase intermediate and peaking capacity, which is why we're comfortable with the sale of baseload power with STP. We can easily replace the attributes of this asset through market purchases of block power at attractive economics for our business.

We have also made progress in decarbonizing our generation portfolio. We retired 1.2 gigawatts of coal generation in 2022 and have made great strides in our carbon reduction goals, with a 60% reduction in coal ownership since 2015. As we continue to strengthen our supply portfolio, we have 1.5 gigawatts of intermediate and peaking natural gas-fired capacity in various stages of development at three brownfield sites in Texas. Depending on market design improvements and economics, we could bring these projects to market to help manage our retail load.

Moving to the second part of our strategic plan, grow energy and home services. Over the near-term, we have a growth target of $300 million of incremental free cash flow before growth to be achieved by 2025. This growth plan includes a 50% target on cross-selling and bundling energy, smart home, and other services to our existing network of 7.5 million customers. And the other 50% by growing organically power, natural gas, and smart home customers at historical levels. We expect to invest approximately $535 million through 2025 to achieve this growth at compelling returns. Again, we will be reporting our progress and the capital invested to our shareholders as part of our Vivint scorecard.

It's been less than four months since we closed the Vivint acquisition and integration is already well underway. Both call centers are now integrated and cross-selling energy and smart home products. We have been creating awareness of our smart home capabilities on our digital platforms. And in early July, we will start to cross-sell energy through Vivint's digital store. We are ramping our digital and physical marketing campaigns and we will start a robust sales program through the smart home direct-to-home channel, both in Texas and the Northeast.

Early insights are positive, particularly the conversion of customers to both products in key markets. For example, in Texas, we're seeing strong conversion rates from retail power to smart home among customers who are moving. And in the east, where smart home gives us direct access to the customer, we are realizing promising conversion rates from smart home to retail energy. On services we launched a protection plan for Vivint customers with tremendous success. So far, we have enrolled 70,000 customers with an average margin uplift of $10 a month. As you can see, we have made solid progress in 12 weeks by opening up multiple sales channels. The insights we're obtaining are valuable in helping us to personalize solutions for our customers, to ultimately increase lead generation and sales conversion through the most cost effective channel.

As I said before, even in view of this clear progress, we are going to be measured on our growth aspirations and discipline on the return of our invested capital. We will provide frequent updates on our progress. Our near-term opportunity focuses almost exclusively on our existing customer network and businesses as they operate today. But I want to take a moment to talk through some of the longer-term value opportunities we are seeing in 2025 and beyond when we would expect an even tighter integration between our energy and smart home businesses.

First, we will continue to drive better customer economics through margin expansion and customer retention. We will further leverage our operating platform to increase efficiencies and lower the cost of acquisition and cost to serve, which translates into higher customer value. The second opportunity is our ability to grow outside competitive power markets. Our smart home and behind the meter energy offerings gives us access to 60 million additional homes, a significant increase in our total addressable market.

Last, but certainly not least, we are uniquely positioned to participate in residential load control and aggregation. The number of smart and controllable devices inside the home continues to increase, and it will allow companies with the right technology and commercial capabilities to optimize energy usage inside the home and monetize this attribute in the market. It will also provide another tool to help manage our own retail load. We have been managing demand response programs for commercial and industrial customers for years. And we know the powerful impact that it has on balancing markets.

We see these moving more fully into the residential space. And as these programs become more common, NRG is uniquely positioned to act as a bridge between the home and the grid. We will be able to dispatch the home as a power unit and provide instantaneous, flexible capacity to the electric grid. While our focus in the near-term continues to be optimizing our core and integrating Vivint, the long-term opportunities that are ahead of us are very attractive.

Now, moving on to the final part of our strategic plan, increase return of capital. I have already shared the key changes in our capital allocation framework, but let me provide some additional context on our philosophy. Beyond safety and operational excellence, the first use of capital for allocation is to achieve and maintain a strong balance sheet. As you heard earlier today, we will achieve our target credit metrics by the end of 2025. The rest of our excess cash will be available for allocation through our 80% return of capital and 20% growth framework.

An important part of our return of capital and the overall value proposition is our annual dividend. It also helps with broadening our shareholder base. Our policy is to grow our dividend per share 7% to 9% through this planning period. As I said before, growth investments will be limited to 20% of capital allocation. Importantly, investments must meet or exceed our [ph] stated (00:30:03) hurdle rates of 12% to 15% unlevered pre-tax return and exceed the return of buying back our own stock.

With this revised capital allocation framework, let me provide you an update on our five-year financial plan. We expect to generate $8.3 billion in excess cash through 2027 after debt reduction, with 80% to be returned to shareholders. The remaining 20% is available for growth investments, which have been primarily earmarked for the $300 million growth plan and to strengthen our supply portfolio.

The revised framework results in $5.5 billion in share repurchases through 2027 and $1.4 billion in dividends. Our return of capital is an important component of our value proposition. Since I became CEO, we have returned approximately $4.6 billion, almost 60% of our market capitalization today, and we expect to return close to 100% of our current market cap in the next five years.

Our immediate focus will be executing our board-authorized $2.7 billion share repurchase program through 2025. We expect to allocate the remaining capital as cash is earned, consistent with our historical practice. This plan is not just illustrative. It is achievable. Our business is stronger and more predictable, allowing us to return capital to our shareholders in a meaningful and consistent basis.

Before we move to the business review sections, let's see how this all comes to life.

[Video Presentation] (00:32:03-00:33:24)

Elizabeth R. Killinger

Executive Vice President-NRG Home, NRG Energy, Inc.

Thank you, Mauricio. Today, I'll share some highlights on our Home Energy business in North America. Then, talk about how we deliver and can grow with our advantaged go-to-market engine. I'll end with a look at our one-of-a-kind customer experience. We are the market leader in home energy, serving about 5.5 million customers, driving over $10 billion in revenue per year.

We're the number one competitive electricity retailer and the number two competitive gas retailer. When markets are structured for consumers to make a choice, we compete and we win. As you can see, we have a track record of strong performance. We've grown our business over the past decade through organic efforts and through targeted business acquisitions. We've increased average customer tenure and have kept costs in check. You can see in the chart on the lower right that the tenure of our customers has increased to almost six years. Next to that chart, you can see that the operating expense has improved by 16% since the transformation program.

Given the inflationary pressures that have affected labor and other key input costs during recent years, we're very pleased with these results. So how do we do it? With the relentless focus on the customer and on continuous improvement. We anticipate needs then create efficient, effective and personalized solutions. We innovate and optimize those solutions and our results stand for themselves.

We continue to deliver stable margins year in and year out. The diversity of our geography, brands, channels, products and customer experiences, combined with the execution excellence enable stability in a variety of market and economic environments. We will continue to drive Home Energy in a way that optimizes EBITDA and cash and delivers on our commitments. Now let's talk about how we do it.

An advantage we have in the home energy space is that we don't have to convince people they need the product we sell, and yet they make choices for energy, just like they make other purchase decisions in their households, brand, channel, offer, customer experience and value drive their choices. We strategically architected a multi-brand approach with value propositions that cover the landscape of consumer preferences. Then we built, bought or revised the brands we needed to win. The house of brands you see on the left consists of seven brands that hold a distinct customer promise with a specific job to do, and they operate in the regions where they're needed for NRG to win. This allows us to optimize overall results and deliver in a cost-efficient manner.

Next, let's talk about products. We've expanded our suite of products to meet the full range of customer energy needs. We have about 5.5 million recurring customers. You can see on the wheel on the right that most are buying electricity from us. In Texas, most prefer term contracts with features or extra products that meet their unique preferences. In the East, most are on month-to-month contracts. You'll hear more from Rob later about the approach we use to manage retail supply that aligns with those regional customer differences.

And while most of our customers come to us for Home Energy to start, over 1 million additional products are being sold across our customer base. We provide an enhanced, seamless energy experience for those who want something more from their energy provider, and that includes those with rooftop solar and EV home battery or a smart thermostat, regardless of whether they bought it from us.

The addition of Smart Home to the family supercharges this product suite. It offers deep hardware expertise, a software backbone to connect to, and another entry point for customers beyond home power and gas. And this customer entry point provides even more engagement for many of these enhanced experiences, as Rasesh will show you a bit later.

The third component of our winning strategy is our unmatched multi-channel sales engine. We meet people where they are through a wide range of sales channels to acquire, retain and cross-sell to meet their needs. Voice is an oldie but goodie. And while that channel has experienced significant change since market open, it's our most efficient channel in terms of cost-to-value economics. Prospects reach us through this channel because they know us and they trust us.

Digital is a robust and diverse channel that has grown significantly over the years. We participate in shopping sites where it makes sense, but the majority of digital sales are driven by organic and paid search, display and other marketing efforts. We see an exciting opportunity here to increase efficiency and effectiveness of the distribution of Smart Home within our digital capabilities.

Retail is where we go out and meet people where they are. A handful of years ago, this channel didn't exist for us. Now, on any given day, we could be selling in close to 1,000 locations at familiar retail stores or events where people congregate. The addition of Smart Home will increase the strength of this channel by deepening our partner relationships.

And finally, the direct channel. This is where we take the customer data we have, along with purchase data and behavioral insights to segment and target specific people with a specific offer. This is certainly not new to us, but the at-scale consultative selling approach that Smart Home brings to the family increases our reach in the direct channel.

We continuously optimize the entire customer journey, prospecting, shopping, onboarding, servicing and renewing to deliver value to our customers as efficiently and effortlessly as possible. In our go-to-market engine, we constantly optimize performance using analytics and modeling, including AI and machine learning.

Let me give you a couple of examples of successes we've had recently. We take individual customer-level data and insights and provide a personalized digital experience to showcase good fit options to customers when they're selecting their next plan. The result, renewals in these use cases are up 30% to 70%.

The second example is one where we use geographical information techniques to build out a map to more accurately identify households eligible to purchase select products. This improved the direct mail secondary product campaign by almost 70%. Our team draws inspiration from top brands and identifies opportunities to redefine what customers expect from the companies they do business with. We use a robust voice of the customer platform to gather real-time insights at various touchpoints in the customer's life cycle. We're using tools like sentiment analysis and text analytics and predictive modeling to drive meaningful action and advantaged outcomes. This is the kind of optimization we're doing every single day, and we're excited to start applying these techniques to smart home customers going forward.

Now, our success appears in more than customer counts and financial results. It's recognized by customer comments and consumer industry thought leaders with numerous awards earned each year. Our ability to deliver for our customers drives retention and powers all that we do. It's our focus and our foundation. Our tireless efforts have enabled us to surpass being a leading customer-centric provider in the utility space. And now, we're on par with or better than leading consumer companies far beyond our roots in energy.

One way to illustrate our progress is the journey we've taken with our digital experience. Over the past seven years, we've blazed a trail in retail energy by embracing mobile technology. Here, you can look back to 2016 at the app we first introduced. Customers loved it at the time since we were basically the first in our space to enter the mobile age. Today, our app has moved up to the front page of consumer smartphones because we provide a full suite of features that deliver on the personalized energy experience as customers want and importantly, can't get anywhere else.

First, the electric vehicle integration provides consumers the ability to schedule their charge when it's most economical. And they can see how much it will cost to fill up. Next, the solar integration allows them to know whether they are producing or using power off the grid at any time. And of course, they can still check their electric usage, bill amount, bill pay and renew their contract. Engaged users of our apps across all our brands are steadily increasing month-over-month and some are increasing in a step change way, like by 50% year-over-year.

We've also seen an increase in the customer time spent in app, resulting from our work to optimize the dashboard, add actionable insights, connected device features and even access to secondary products. Give customers value and they will engage and we expect this to get even better with smart home. With additional products and services in the smart home portfolio, we expect regular engagement multiple times more per day, which will help us create even more customers for life.

To demonstrate how we're creating integrated energy experiences, we'd like to introduce you to a family who counts on us for their whole home energy solution. As you'll see in this video, they're an energy-conscious family that has an EV and a rooftop solar system. Have a look at how we're seamlessly bringing peace of mind to their daily routine.

[Video Presentation] (00:43:49-00:44:28)

I hope you noticed, our app has become a personalized, customizable whole home energy control center, and we're not done. Through an agile approach, we continue to innovate and develop new features and integrations designed to meet those ever-changing customer expectations. No matter your energy needs now or in the future, we've got you.

I'd like to pass the presentation over to my colleague, Rasesh Patel, who leads our Smart Home Group.

Rasesh Patel

President-Vivint Smart Home, NRG Energy, Inc.

Thank you, Elizabeth. I am thrilled to share with you today an overview of our smart home business and the incredible opportunity we have ahead of us. The Vivint Smart Home platform is industry leading. We have a large and loyal base of nearly 2 million customers who are highly engaged and use the platform on average 16 times per day. This level of daily engagement drives incredible brand loyalty, and that results in what we believe as an industry best, nine-year average customer life.

And the model has compelling economics. 90% of our smart home revenues are recurring, and we continued to grow subscribers, revenue and margins at an attractive rate. We are in the early days of a big opportunity. About half the homes in the US today have at least one smart device and the number of smart devices per home has grown from three in 2016 to eight in 2023. The market is expected to grow from $35 billion to $45 billion over the next four years, and we are in prime position to capitalize on this opportunity.

We firmly believe that a smart home is much more than a standalone connected device. When you think about the customer experience of buying a series of single-point devices, going through the hassles of installation and setup, multiple apps and a fragmented experience, where things don't work together, you begin to understand just how frustrating the process can be for the customer. Not to mention, standalone devices are a very small part of the industry profit pool.

The smart home platform we offer is an extensive suite of services, all brought together in a seamless and intuitive app experience. We help customers with every aspect of the experience, from a consultative sale to a professional install and ongoing support. This is a scalable platform that expands the value it delivers to consumers over time. Let me give you a glimpse of the experience we offer.

[Video Presentation] (00:47:04-00:48:23)

As you can see from the video, the experience is differentiated. While competitors' cameras record a crime, Vivint's AI-based cameras can help prevent a crime from happening by firing a deter tone when an unknown person approaches the home and shining a spotlight on the perpetrator that follows their movement. If the intruder still doesn't leave, the system can turn on the lights inside the house, making it seem like somebody is home. It's these types of experiences that really drive brand loyalty.

Our smart home platform has been recognized by a broad range of publications as the best in the industry. Forbes calls it a one-stop shop to building a smart home. My favorite comment is from TechCrunch. Like good technology, the experience is magical. What we've seen is that more devices the customer has in the home, the more value they get from the platform, the higher level of engagement that they have. This, in turn, leads to a longer average customer life and expanded customer lifetime value. So as we continue to expand the platform offering, we see an opportunity to increase the engagement of our existing customer base and drive incremental revenue and market penetration.

We have a proprietary, vertically integrated platform that allows us to fine-tune every aspect of the customer experience, and that leads to compelling economics. Over the past four years, the average number of devices in the home has grown, and that has led to higher monthly revenue per customer. Simultaneously, we've been able to decrease the cost to serve those customers and thus expand service margin by 10 percentage points.

This has led to an average customer life extending to an industry-best nine years, all leading to strong growth and economic value. We have grown subscribers by 45% and revenue by 70% over this period, and we believe this flywheel of continuous improvement will continue to strengthen itself as more devices are connected in the home. Later, we'll talk about how the combined platform with NRG allows us to accelerate this flywheel and our product road map.

These improvements have significantly strengthened the unit economics of our business. On average, we spend $750 to acquire a customer and we generate $430 of annual margin over a nine-year customer life. As you could see, our growth investment drives very attractive returns, with cumulative net cash per customer of more than $3,000, and returns of over 50%. We feel very good about the unit economics of the business. And as I mentioned before, they continue to improve on a year-over-year basis.

Historically, one of the challenges of the business model has been free cash flow conversion. But due to the improvements in our unit economics, combined with the key initiatives enabled by the NRG platform, we expect free cash flow before growth conversion to improve from 20% to over 55%. Another attractive feature of the smart home business model is the strong operating leverage, and we expect to see continued benefits as we further scale the business.

With the combined assets of NRG, we are well positioned to deliver on the convergence between energy and smart home. Let me bring this to life for you on just how we plan to do that. First, as it relates to solar, we have already launched an integration with the largest solar inverter companies. This allows our smart home customers to monitor their solar production. Vivint app, we have ramped our solar business quickly. Within the second year of operation, we have become a top 10 solar distribution company, with more than 170 megawatts installed to date and $100 million of revenue in just our second year of operation.

On the HVAC front, we're excited to partner with Airtron, another NRG brand. We plan to leverage Airtron's relationship with national homebuilders such as KB Home, D.R. Horton, and Pulte to pre-position our smart home products when HVAC is installed during the construction phase. We're also working on integrating HVAC monitoring into our smart home platform so that if a customer experiences issues with their HVAC system, we can deliver a concierge experience and offer to send an Airtron technician to resolve their concern without them ever having to pick up the phone. So we really believe we can deliver a superior customer experience with HVAC.

Regarding protection plans, NRG is already licensed to sell protection plan products in all 50 states, with over a 0.5 million active customers across the platform. Since the close of the Vivint acquisition, we have launched the Vivint Protection Plan and have already onboarded more than 70,000 customers on this product. This is an incremental revenue stream that expands customer lifetime value, and we see this as a strong synergy opportunity as it delivers on our core value of delivering peace of mind to customers.

Lastly, I want to turn your attention to energy management. Today, about 20% of our smart home customers have already opted to allow us to automatically manage energy in their homes. And we see this as the beginning of a large opportunity. As penetration grows, we are well positioned to implement residential demand response at scale. The proprietary extensible platform we have developed is the key enabler to us delivering this differentiated customer experience. We have a smart hub within the home that enables integration with virtually every type of sensor, whether it's computer vision, lighting, energy management, solar, security or access management. We utilize a range of connectivity protocols such as Wi-Fi, Zigbee, Z-Wave, Bluetooth and NFC to enable this integration with a broad range of devices within the home.

We're also able to connect with third-party ecosystems, whether it's integrating with Chamberlain on access management for garage door openers or Google Nest for thermostats, or Alexa in Google Home for voice control. Our cloud-based platform allows us to perform integrations with third-party ecosystems and deliver a seamless, integrated experience to customers.

We generate a tremendous amount of data and insights. The platform processes more than 800 daily events per household, which adds up to more than 1.6 billion events per day on an aggregated basis. Through the use of artificial intelligence and machine learning, we deliver a world-class, personalized experience to our customers. This is a scalable and extensible platform that has positioned us to continue to expand the services we offer within the home over time.

In closing, there's real, tangible value to owning this platform. It gives us full control of the product road map. It allows us to own the customer relationship, as well as the data and insights, and it protects our intellectual property. It also unlocks potential value, particularly now as energy and smart home converge.

NRG has a unique platform that spans from generation to retail energy, with an intelligent market trading platform that sits between the two. Bringing the smart home platform to the table allows us to extend our capabilities to residential demand response, capturing the opportunity Mauricio outlined earlier.

Now, let me turn the time over to my colleague and friend, Robert Gaudette, who will provide an update on business and generation.

Robert J. Gaudette

Executive Vice President-NRG Business, NRG Energy, Inc.

Thank you, Rasesh, and good morning. I'm going to review NRG Business, a sales, service and commercial organization that serves our business and wholesale customers. And it runs the diversified supply portfolio that provides the foundation for our customer businesses.

Now let's start with the sales and service organization. This is a large, diverse and effective portfolio. We're the number two power retailer. We're the number two gas retailer, and we're the number three load management provider to retail business customers. While the components are impressive, when taken together on one platform, with unified sales, service and customer operations, we are the leading energy provider to business customers.

We deliver both gas and power providing stability, and our customer base is diverse across multiple industries, products and geographies. While by any measure we are large, we don't focus on volumes or brag a lot, we focus on shareholder value creation, with disciplined margin expectations, judicious credit and risk standards, and principal customer portfolio management.

Some customers or types of businesses don't make sense to us, so we let our competitors serve them. Instead, we focus on the right customer for our portfolio and serve them everything that NRG can do. And that disciplined approach works managing our business. We have a solid history of stable margins, and our customers show that they value our service with high and consistent renewal rates and long relationships, some of those measured in decades.

There are few companies that can bring a business customer power, natural gas and demand response, with expertise in retail and wholesale like NRG. Remember, this is a customer segment that while transactional, it's also insightful. Businesses have led on solar, distributed generation and demand response. We learn and grow with these customers, and then we take what we learn and apply it with the customer base that Elizabeth and Rasesh talked about earlier. By focusing on applying the breadth and depth of the NRG platform to the right portfolio of customers, we've built a business that delivers consistent earnings and insights for the future.

You heard from Mauricio about the strategic moves that we've made, how we continually optimize our asset and financial portfolio to serve our business customers. Earlier, Elizabeth talked about the breadth of home energy, and I just finished talking about the business side. All of our energy customers are served by our diversified supply portfolio. I'm not going to walk you through how that happens behind the scenes. To meet that demand, we use a tailored combination of owned assets, renting attributes and market purchases.

On the left, you see a map of our plant operations. We have 13 gigawatts of generation, located in key locations to serve our customers. The fleet is diverse in geography, merit order and fuel mix. Our 19 generation stations and our plant operations employees who work every day to efficiently and safely operate that generation form one part of the diversified supply strategy for power. We also move around 5.3 BCF a day of natural gas across interstate pipelines and intrastate pipelines, and multiple storage facilities across the continent to serve our gas customers.

In partnership with operations, NRG Business has a dedicated and experienced commercial team, who optimize and build our diversified supply portfolio. Our team has deep industry knowledge, and at the director level, has over 25 years of average experience. Our commercial leadership has seen the market changes that have occurred through deregulation, increasing renewable penetration, and now greater electrification.

An advantage of NRG scale is that we have a tremendous market intelligence mechanism across the value chain. To capture and apply the intelligence we glean from the markets and our consumers, we've expanded our data analytics capability and we continuously improve our models to better drive our collected insights to optimize the portfolio. We think about the next five minutes, the next five days and the next five years.

As we optimize the portfolio, we are also balancing market, operational and credit risks. We have a robust internal risk management capability that enables NRG to consider enterprise risk across all spectrums and to mitigate risks across the portfolio. You've seen what our demand looks like at a high level. Now, I'd like to take that down to one day.

I'm now going to walk you through our supply options, and then we can talk about the criteria we use to make supply decisions, given the amount of intelligence that NRG has. On the left side of the chart, you see an illustrative but typical representation of power demand in a given day. Customer demand rises and falls as daily activity starts and stops, and tensions build into the evening.

The dotted lines represent a deviation from normal load by higher or lower demand because we have to set the portfolio up for both. We think about it in three zones, base. It's pretty flat, lower priced and easy to procure. Intermediate, where demand is moving because of temperature changes or as people wake up or offices open or close. Flexibility is important in supplying intermediate load. And finally, peak, driven by the variance in weather conditions. At times, this can lead to scarcity pricing. We plan for it and we build a portfolio to meet it. The peak portion of the customer demand is where load management has the most value to the portfolio.

Now moving to the middle of the slide, our options are to own, rent or buy. We own generation, chosen for its attributes to meet our customer load. The risk of owning generation is plant performance, but we work to mitigate that risk with our maintenance program and we take plant performance risk into our planning. We also rent some of the components of our portfolio. We use physical and financial products like tolls, heat rate options or power purchase agreements to replicate the attributes of generation.

In addition, renting part of the portfolio has more flexibility around tenure and time periods than owning an asset. The risk of renting is counterparty or credit risk. We mitigate that risk through our credit management program and diversifying our pool of counterparties. And finally, we can and do buy supply. Through the exchange or over the counter, we're buying physical products, sometimes swaps, sometimes options to match our supply portfolio to our expected demand. Like renting, it has counterparty risk. But with exchange-traded products, that is minimized. We use all three options to build our portfolio, and we use the criteria on the right to determine what options we use to build it rather than just short-term buys or 30-year assets.

We're looking to match term of load and supply by blending tenors of products and assets against our retail load profile. We consider the merit order when building our portfolio, to match our load across the hours of the day and the seasons of the year. We consider credit and collateral implications by eliminating a single point of failure through a diverse pool of suppliers and using various tenors and structures. This multi-option approach ensures we have ample liquidity to build our portfolio, and we're always considering carbon intensity to align our portfolio over time with corporate objectives.

Our strategy allows us to build a portfolio that is flexible, nimble, efficient and balanced. Given the criteria I just explained, our generation fleet, the owned part of the supply portfolio, has evolved, including a reduction in our baseload generation. Most of that was the previously announced sale of our portion of the South Texas nuclear plant. From a portfolio perspective, a nuclear plant, because of the nature of its operations, is block power. That block power is readily available through purchasing firm power via the traded markets. And using traded power reduces our tenor exposure and our concentration risk.

We've also increased the percentage of our fleet that is in Texas. Using our criteria to evaluate how to build the optimal supply portfolio, we have – find having the right own generation in Texas more important than other regions. Looking forward to the future, we have 1.5 gigawatts of brownfield opportunities in ERCOT that would enable us to capitalize on preferred locations and existing infrastructure. We are well positioned for the market design enhancements in ERCOT. And as we look towards carbon intensity in the portfolio, we've retired coal generation and we've added renewable PPAs, advancing towards our 2050 net zero goal.

On this slide, we're disclosing our hedge position for the home energy business for ERCOT and the East. At NRG, we hedge all of our business retail from the market at the time of execution, so those books are flat and not included here. This is on peak power and megawatt hours. So total home on peak usage.

In ERCOT on the left, you can see that the balance of 2023 is 98% existing load, which is contracted and expected renewal load. And you can also see that our – using our portfolio criteria, we are using our economic generation primarily and market purchases secondarily to cover our exposure. In 2024, you see that 88% of our total expected load is existing. As more of the existing load is renewed, we will add market purchases to optimize the portfolio and more closely align our costs with our revenue rates.

In the East, using the same criteria, we set the portfolio up similarly, but we use market purchases to supply more of the home energy business. Consistent with our practice in ERCOT, we will also increase market purchases to align with revenue rates as renewals happen.

So what do these charts mean? We balance generation and market purchases against load. We manage the current financial exposure while planning for customer demand. We maintain flexibility to adjust our portfolio as our volumes change, and we hedge the business retail exposure through the market at execution.

You can see that we're on a path to decarbonization. We set a greenhouse gas emissions target and have achieved a 42% reduction over the past decade. As an early adopter and leader in decarbonization, our commitment and results speak for themselves. Since our 2014 base year, our CO_2 emissions have decreased from 60 million to 35 million metric tons.

We are always working towards our decarbonization goals. We've incorporated 1.9 gigawatts of renewable PPAs into our supply and retired 1.2 gigawatts of coal in 2022 alone. And remember, that a megawatt that isn't used has the lowest carbon footprint around. We manage 2.5 gigawatts of demand response for business customers. And as you've heard today, the NRG platform, marrying customers and technology has the potential for real residential demand response.

Thank you for your time and attention. I'll now hand it over to Bruce Chung.

Bruce Chung

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

Thank you, Rob, and good morning, everyone. It is great to be here as we discuss our plan toward value creation over the next five years. While I am new to some of you, I am committed to earning your trust through my steadfast commitment to executing our capital allocation principles, strong in-person engagement, and enhancing our disclosures. I fully appreciate the importance of a disciplined capital allocation framework and ensuring that we treat your capital like it was our own. You have my commitment that I will exercise all of my duties as the CFO to hold ourselves accountable for adhering to the capital allocation principles laid out in the plan.

Now, moving on to the presentation. I'd like to start by providing a brief update on our 2023 guidance and capital allocation for the year. We are reaffirming our 2023 financial guidance with adjusted EBITDA of $3.01 billion to $3.25 billion and free cash flow before growth of $1.62 billion to $1.86 billion.

We continue to see strong performance across the enterprise since we reported first quarter earnings. Our integrated energy platform continues to prove resilient through the current low power price environment. Similar to the first quarter, we have seen margin expansion through our unique ability to take advantage of lower market power prices, while resting our power plants to ensure readiness for the summer. Our year-to-date results are strong and we are well positioned for the remainder of the year, particularly for the summer.

Now, turning to smart home. Our business is performing above expectations through the first part of the year. We are seeing strong year-over-year growth, driven by an increase in total subscribers, higher service revenue per user and more product sales. Our net service cost per subscriber continues to perform well, showing significant improvement year-over-year, driven by better product performance and fewer service calls. Finally, attrition remains near all-time lows as customers continue to engage with the platform at ever increasing rates.

Now turning to capital allocation for the year, moving from the left to the right, we have updated our capital allocation waterfall for the estimated $1.63 billion of net proceeds from the sale of STP, bringing our 2023 excess cash total to $3.6 billion. With the additional cash, we will pay down an incremental $500 million of debt in order to stay leverage-neutral given the loss of STP EBITDA and use $997 million for share repurchases as part of our $2.7 billion share repurchase program. We expect $139 million of remaining excess cash in 2023, which we will allocate later in the year.

As Mauricio discussed earlier, one of the tenets of our capital allocation policy is to achieve our target credit metrics of 2.5 times to 2.75 times net debt to EBITDA. This has been a longstanding commitment of our company and we believe it is a critical component to how we manage the underlying risk in our business and operations. We target these credit metrics since they are consistent with investment grade credit ratings and given that our senior secured credit rating is investment grade, we want to ensure that we maintain that senior secured rating.

Thanks to the significant cash flow generated by our plan, we have the ability to deploy some of that cash towards meaningful debt reduction over the planning period. As you can see on the slide, our plan calls for $2.55 billion of debt reduction through 2025. That debt reduction includes the $1.4 billion we intend to delever by in 2023 as I discussed in our updated 2023 capital allocation. This level of debt reduction will ensure that we achieve our credit metrics by the end of 2025, consistent with the commitments that we have made to the rating agencies and our shareholders.

Maintaining a strong and flexible balance sheet has always been a core principle for the company. This is critical in order to ensure that we can remain efficient in managing our capital needs while also maintaining ready access to the capital markets at an efficient cost of capital. We have made a commitment to operating with a strong balance sheet and we intend to execute over the next few years accordingly.

We expect to generate a significant amount of excess cash after debt reduction through 2027. Our plan currently provides for cumulative excess cash after debt reduction of $8.3 billion through 2027. Of that $8.3 billion, we expect to return $6.9 billion back to shareholders in the form of common dividends and share repurchases. These amounts are consistent with our new 80/20 capital allocation framework. I'd like to reiterate that the return of capital amounts are after $2.55 billion of debt reduction and approximately $300 million of preferred dividends.

The other 20% of excess cash, or $1.4 billion through 2027, is earmarked for growth investments in our Home Energy and Smart Home businesses as well as reserving capital for the potential 1.5 gigawatts of brownfield development opportunities. It is worth noting that the amount allocated for growth investments will essentially be funded through cash flows from our Smart Home business. As with all of our growth investments, we only deploy capital so long as the returns are both greater than our return thresholds and the return implied by buying back our own stock.

Here is a roadmap to our 2027 free cash flow per share. As you can see, we expect to double it during the next five years. Going from left to right, our path from $8.50 per share to $12.50 per share by 2025 is straightforward. We have very good line of sight to the contributors of that growth. The combination of debt reduction, cost savings, disciplined growth and share repurchases represents very visible initiatives that we are already executing against.

As Mauricio alluded to, the early results of our cross-sell and bundling initiatives are encouraging. And when coupled with organic growth, consistent with historical trends in our Home Energy and Smart Home businesses, we feel good about our ability to achieve the incremental $300 million of free cash flow by 2025.

Moving along and extending to 2027, the components underpinning the growth between 2025 and 2027 to achieve $18 of free cash flow per share do not change. A continued focus on disciplined growth and return of capital will be the priority. It is not lost on us that a meaningful amount of the free cash flow per share growth will come from share repurchases. This is intentional. We now have line of sight to our growth initiatives and, as a result, we have the flexibility and confidence to allocate more excess cash flow to return of capital.

You will note that the 2023 and 2025 free cash flow per share targets are the same as they were in 2021. There is an important distinction. As you can see, we used a flat $36 share price back in 2021 as an underlying assumption for share repurchases. Given the visibility we now have into our free cash flow growth, we felt it was appropriate to use higher share prices throughout the planning period. I believe this change, while perhaps subtle, is an important one and speaks to the level of confidence we have in the components of our free cash flow growth. I am looking forward to meeting you over the days and weeks to come.

I will now turn it back to Mauricio for his closing remarks.

Mauricio Gutierrez

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

Thank you, Bruce, Robert, Rasesh and Elizabeth. Well done. I want to close by discussing what the path to success looks like for our company and the scorecard you can use to hold us accountable. Our business has evolved significantly. Our actions have made NRG stronger today than ever before. We are now positioned to capitalize on the trends in our sector and the opportunities that are arising from the energy transition.

For us, I see two clear steps in our continued evolution. The first is to deliver on our core energy business and the near-term Vivint goals. The second is the full integration of Energy and Smart Home in a compelling offering to the customer.

As you can see, we are on track with the plan we provided at our Investor Day in 2021. We told you our free cash flow before growth per share target for 2023 was going to be $8.50. And today, we are reaffirming that number, which supports a growth trajectory of 15% to 20% per year. And we are doing it in a responsible way with a strong balance sheet and a robust sustainability program with very ambitious carbon reduction goals. As we execute the plan, we are confident that this will drive enhanced sustainable shareholder value.

We now have a consumer platform of significant scale and scope with 7.5 million customers and counting. We have the technology and the expertise to create unique and compelling products for the consumer. We have a consumer business that delivers stable and recurring margins while capitalizing on the energy transition opportunities. And we have the right team to maximize returns for shareholders and create sustainable value for all stakeholders.

Thank you for your attention and your interest in NRG. With that, I will pass it back to our host, Kevin Cole.

QUESTION AND ANSWER SECTION

Kevin L. Cole
Senior Vice President, Treasurer & Head-Investor Relations, NRG Energy, Inc.
A

Thank you, Mauricio. We'll now open the lines for Q&A. As a reminder, for those from the investment community wishing to ask a question, please dial into the Q&A phone line now using the dial-in provided. Again, please be aware that once you've dialed in, you'll need to mute your computer to avoid any echo or feedback. We'll now pause for exactly 3 minutes to arrange the stage and allow for the investors to dial in. Thank you.

[Break] (01:18:40-01:21:41)

Operator: The 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, team. Can you guys hear me okay?

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

Hey, good morning, Julien. We can loud and clear.

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

Excellent. Wonderful. Thank you guys for the time. Look, maybe just the first big question here is what exceptions are being reflected in the contribution on EBITDA or FCF for Vivint here? I mean, obviously, a lot of focus here today. Your cash flows and implied buybacks are clearly ahead of expectations. But the question embedded within that is how much growth is contemplated from Vivint to achieve this?

Can you speak to what needs to be achieved within Vivint to achieve these consolidated targets? You've identified integration by the end of this year. What else needs to be done to achieve these Vivint targets, if you can elaborate a little bit?

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

Sure. So, Julien, there is two primary drivers. The first one is the $100 million cost synergy that we have Vivint. And then the second one we announced today – well, we announced the $300 million grow plan that we have. If you recall, I think we provided a free cash flow before growth guidance of EBITDA close to $140 million for this year. And that's going to grow during this planning period by about a 30% CAGR, so very robust improvement on cash flows. And as a matter of fact, it's going to generate enough to actually fund our growth plan.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.

Q

Got it. Any more articulation that you can provide around what's reflected within those assumptions for Vivint to achieve that 30%, for instance?

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

A

Sure.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.

Q

Is this just the integration synergies, really?

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

A

Yeah. Well, I mean, it's both, the integration synergies, the grow of the company and, as part of the integration of synergies, remember, I mean, we're focused on reducing the cost of acquire because we have – we're going to leverage the common operating platform. We're going to be looking at combining the two public companies and then we're going to be focusing on optimizing the 7.5 million customer network that we have to achieve the growth targets that we already identified.

So when you put all that in context, it's a pretty significant cash flow improvement for Vivint over the planning period. And I mean, not only that, as I said, I mean, I think one of the things that perhaps sometimes get missed is that the cash flow that Vivint is going to generate is going to fund our entire growth for this period. But Bruce and Rasesh, anything else that you want to add?

Rasesh Patel
President-Vivint Smart Home, NRG Energy, Inc.

A

Yeah, I'd give you more color, Julien. There's four things that are really driving the cash flow expansion. The first is improving unit economics. And as you saw from the presentation, customers are buying more and, simultaneously, we're reducing the cost to serve customers, and our margins have improved by 10 percentage-points.

The second thing, as Mauricio referenced, is reducing customer acquisition cost. We've been able to reduce the cost of product through value engineering. As the supply chain environment has normalized, freight, transportation costs, logistics have come down. So we're reducing the cost of acquisition.

The third is we're instantiating new revenue streams. As Mauricio mentioned, we launched the Vivint Protection Plan three months ago and that's incremental revenue stream for the business. And we already have 70,000 customers enrolled in that. We have additional pricing optimizations we're doing that are high margin.

And the last is, as Mauricio referenced, it's around the cost synergies that come with the consolidation. And so when you put those four things together, we feel really confident. We've got the playbook to improve the free cash flow generation of the business.

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

Got it. All right. Fair enough, guys. Thank you. If I can, just pivoting to the other question here. I mean, you guys alluded to this board refresh here. What does that entail? I mean, obviously, the Chair said he fully supports Mauricio and the wider team here. But at this point, what is the board refresh? I know we've talked about this perhaps over the years, but as it stands today and given the context, how are you guys think about approaching that?

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

Well, I mean, as you mentioned that, Julien, this is an ongoing refreshment process that we started a couple of years ago. I mean, if you look at the results that we've had, we actually have 50% of our directors have been – are new over the past five years. And we have focused on people that bring relevant experience to the strategy and to our business. So that's a process that is going to continue. And we are always open to listening to our shareholders. If there is good candidates, we will always evaluate them and take them into consideration.

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

Got it. Understood. And just lastly here, quickly, housekeeping quickly. How are you guys trending on 2023? I mean, obviously ERCOT's been hot and maybe not super peaky in pricing. You talked about this hedge percentage being north of 100%. I mean, what does this all translate to in terms of trends and sort of a downpayment on this execution across the longer term?

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

Sure. So, so far, our power plants have performed really well during this heat wave, as well as our hedges. As you referred to, our hedges are actually a little bit higher than our expected load, which is something that we discussed and we talked about. We were going to be leaning long going forward to make sure that we plan for any changes on weather.

So, so far, this has been really good for our company. High load and more tempered prices is really good for us. I feel very confident that we're on track to deliver the commitments and the results that we expect for the year as we, today, ratified our guidance ranges.

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

Got it. All right, guys. And just actually, just super quickly, on the buyback [ph] bit (01:27:57), what share price are you assuming there? I know it's ratcheting up. I just want to make sure we can clarify that here.

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

I mean, that's an excellent point and I'll let Bruce know. But I think we have actually high graded our path of free cash flow before growth CAGR that we presented this time around compared to 2021. Bruce?

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

Yeah, Julian. So just to answer your question, with respect to 2023, we are assuming an underlying share price for the remaining buyback in 2023 of $36. But when you take that into account with the previous buyback that we had done over the course of last year, that gets you to a weighted average of about $38. From that point on, we then use an assumption of growing the share price that we use for share repurchases in 2025 and 2027, based on the midpoint of our 15% to 20% free cash flow before growth per share guidance.

Julien Dumoulin-Smith
Analyst, BofA Securities, Inc.

Q

Okay. Got it. So [ph] 17.5% (01:28:58). Got it. Excellent, guys. Thank you.

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

A

Great. Thank you, Julien.

Operator: Please stand by for our next question. The next question comes from Angie Storozynski with Seaport. Your line is open.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Thank you. So we wanted buyback stock and they're back. [indiscernible] (01:29:25)

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

A

Good morning, Angie.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Good morning. So I guess the first question because I feel like we've had this sort of a reset in expectations a couple of times for the last couple of years. So can we assume that we're done, meaning you now have everything you need to grow the business in the direction you desire, there's no additional service or add-on that is needed, feel you have scale and you can just focus on cost cutting and internal growth?

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

A

That is exactly right, Angie. We now have all the pieces that we needed to strengthen our consumer platform and move in the direction where we're seeing the trends of electrification and smart technologies inside the home. That has given us the clarity that we needed to have our investment needs. And that's why we pivoted to the 80% return of capital and 20% of growth. So, what you're seeing today in our plan is what we're going to be focusing on executing. And as you can tell, it creates tremendous amount of shareholder value.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Okay. I'll hold you to it in a year or two if that's the case. Now, moving on, so just one point, throughout your presentation today, you were talking about the success of cross-selling your services, especially as your customers are moving to different houses. So, what happens over the next year or two if there is a meaningful slowdown in the housing market and you don't see that migration. Again, Texas might be different, but again, how will that impact your growth expectations?

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

A

Well, I mean, there is a number of avenues for our margin expansion. It's not just targeting people who are moving houses, but as I mentioned today and Rasesh, we have an opportunity to cross-sell across our different brands between energy and smart home. We launched the Protection Plan, and so far, it's been an incredible success and that's only happened for three months. And we expect that is going to continue growing tremendously at very low cost of acquisition and service.

So, we actually feel very confident that we're going to achieve our $300 million growth. 50% is going to come from organic growth and 50% is going to come from cross-sell and bundling, which, we are already seeing tremendous results. But I want to let Elizabeth and Rasesh perhaps comment a little bit on it. Elizabeth?

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

A

Yeah. So, Angie, your question about movers. The bulk of our energy subscribers come in from movers in Texas, but outside of Texas, it's not a mover base because, often, the first month is with the regulated utility. So, that, actually, if we do have an economic downturn outside, we still believe that our multi-brand, multichannel strategy for energy will be strong.

Rasesh Patel
President-Vivint Smart Home, NRG Energy, Inc.

A

Yeah. And I'll just add to that, for the smart home business, on the organic side, there has been a meaningful slowdown in housing activity over the past 12 months, given the interest rate environment. As you've seen, we've grown subscribers by 9% in revenues by 14%. And so, we're in a large and growing market. And we believe Vivint has plenty of penetration opportunity within that. And so, we expect strong single-digit subscriber growth and double-digit revenue growth.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Okay. And then, just the last one for me. So, investors clearly care about eye AI-driven growth or anything that's AI-driven, so how – I mean, I'm assuming that, for example, you could have some benefit from this higher loan growth. But how about on the cost side? You have these, customer service centers – I mean, call centers, is there a way to have like a step change on the cost side on the back of AI?

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

A

Rasesh, why don't you start and then Elizabeth on our call centers. Rasesh .

Rasesh Patel
President-Vivint Smart Home, NRG Energy, Inc.

A

Yeah, absolutely. That's a great question. And to hit that dead on, we have seen over 26% reduction in our service cost per customer, and that's – once we acquire a customer, that is really the primary cost that we have. And so, you've seen a robust improvement in margin. I think we are just at the onset of that opportunity.

And AI plays sort of a dual-sided role for us. I think it can significantly help us reduce our operating costs, but, too, AI plays a meaningful role within our product environment. And it's helping us grow engagement, within our product environment, which is in turn helping customers buy more and stay longer. And so, it's a terrific margin opportunity for us as the technology continues to mature.

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

Yeah. And Angie, we use AI and machine learning for all kinds of things. There is a cost element to actually give our the folks who interact with customers more information at the point that they're talking to a customer, and that will help us solve customers' questions or challenges faster, which ultimately, will reduce costs.

But there's a tremendous opportunity that we're capitalized on today and the potential for the future is remarkable, and that is creating more value. Putting that right offer in front of the customer with the right components helps us expand our margins and also creates efficiency and tenure on the back side of that. So, we have plenty today, but there's a tremendous opportunity going forward for how we use those tools.

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

So, Angie, when you think about AI and the impact on our business, it's not just in helping us reduce cost, but it's also helping us increase retention, which at the end of the day increases lifetime value of the customer and will be reflected in a higher multiple for our own valuation. So you need to think about it in those two sides.

Angie Storozynski
Analyst, Seaport Global Securities LLC
Q

Great. Thank you, guys.

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

Thank you, Angie.

Operator: Please stand by for the next question. The next question comes from Steven Fleishman with Wolfe. Your line is now open.

Steven Fleishman
Analyst, Wolfe Research LLC
Q

Yeah. Hi. Good morning. Can you hear me okay?

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

Hey, good morning, Steve. How are you?

Steven Fleishman
Analyst, Wolfe Research LLC
Q

Yeah, good, Mauricio. Thank you. So, just I guess, could you just remind me, as we go forward, how you're going to segment the company? Are we going to be able to kind of track, Vivint separate from the other customer businesses or how should we think about that?

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

A

No, I mean, that's an excellent question. And as a company in transition, we recognize that greater disclosures, and helping you value the company and giving you key value drivers is very significant. We are committed to doing that. And I think, today, we provided you a lot more information that we had in the past.

So, we are actually in active conversations right now in terms of how do we – what are the key performance metrics that we need to provide to you? And also, if that has an impact on how we're reporting segments, so we can make it as easy as a price times quantity that will help you better value the company and better value the potential of the company. So, you are completely correct, Steve, that I mean, this is something that needs to evolve as our business is evolving. And we need to make it very clear and very easy for you to value and understand.

Steven Fleishman
Analyst, Wolfe Research LLC

Q

Yeah. No, that would be helpful. I mean, yes, a lot of disclosures, very helpful on the bottom line and the return of capital, all that stuff. And so, obviously it's like, all right, well, how are things tracking in the business in terms of customers and margins? I know you get margins directionally, but there's not like actual dollars there. So, is that something you're thinking about doing?

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

A

Absolutely, Steve. I mean, when I think about it, you have a consumer platform that has very stable margins. On the energy side is supported by our generation portfolio and our commercial operations. And on the smart home side is our cost of acquisition that basically gives us access to a subscription type of revenue model for nine years on average. We're going to be providing that level of specificity and the drivers behind it, so you can actually model it in a much simpler way. We recognize that as a company in transition, it gets sometimes difficult, and we're going to be evolving our disclosures as we evolve our company.

Steven Fleishman
Analyst, Wolfe Research LLC

Q

Okay. And then, one kind of simple question just on maybe more for the Vivint side. It's just a lot of the devices and such as part of Vivint like, you can just – I would think the consumer could just buy them themself and put them on and use them. So, kind of as I think about the consumer doing that versus having Vivint do that for them – and could you just give us some color on like, why would I have Vivint do it instead of just buy it myself?

Rasesh Patel
President-Vivint Smart Home, NRG Energy, Inc.

A

Yeah, you bet. It's a great question. First and foremost, we segment the market into those two primary segments. There's a segment of consumers that don't want to climb ladders and pull out a drill. They want an end-to-end service. And we take care of everything for them, from a consultative sale to a professional install and provide an end-to-end service.

And these are a high-value customers. As you could see, we capture a very healthy service revenues from this customer base. We have 90-plus percent of our revenues are recurring, and it's a nine-year customer life, which in the consumer services space that's not just best brand loyalty within the Smart Home segment, you can compare us to really any consumer services company and the model has very, very strong brand loyalty.

As you said, there is a segment of consumers that is comfortable and that are tech-savvy in being able to set the platform up themselves. And we can pass on some of the economics and the cost savings to the consumer, and so more to come. But I think on our first quarter earnings call, we mentioned Vivint Basics. And we believe we've got a differentiated customer experience that resonates with consumers. And we plan to expand our addressable market by making that product available to that DIY segment that you're referring to. So, we think we can play in both worlds.

And similar to other services business in the wireless industry, you have postpaid and you have prepaid for upmarket, downmarket. And clearly, postpaid, the full-service offering is where the margin and the economic value lies, but you can raise brand awareness and you can capture more of the addressable market through the downmarket offering. And so, we think we can play in both.

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

A

But I think there is a great opportunity, Steve, on the DIY side and with the DIY solution that we have as an entry point with customers that perhaps they don't want to talk to us on the full-service and then high-grade them with providing them an exceptional experience and additional products and services. So, now that we have this DIY solution, it will allow us to establish that engagement, that conversation with our customers and start moving them to a professionally monitored, but more importantly, a full service smart energy solution to that customer that allows us to access deeper margin opportunities and create longer-lasting relationships with the customers.

Steven Fleishman
Analyst, Wolfe Research LLC

Q

Okay. I'll let others ask. Thank you.

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

A

Thank you, Steve.

Operator: Please standby for our next question. The next question comes 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 question.

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

A

Hey. Good morning, David.

David Arcaro
Analyst, Morgan Stanley & Co. LLC

Q

I was wondering if you could elaborate a bit on the core areas of the cost-cutting potential in that $150 million initiative. What's your confidence level in achieving that? And how deep are you digging to get that? I'm wondering if there's further cost reduction potential beyond after you achieve that $150 million?

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

A

Yes. So let me just take a little step back and tell you what we have right now. We have the $300 million cost synergy of Direct Energy, which we're going to be achieved by the end of the year, and we actually have clear line of sight. And then, we have the $100 million cost synergy with Vivint, which we already talked about, primarily focused on the combining two public companies. And now, that they're part of a larger sales and marketing organization, their cost efficiencies to be accessed.

Now, if you remember a couple of months ago, when I had clear line of sight that we were going to achieve the $300 million cost synergy for Direct Energy, I said, once we finalize that, we're going to be evaluating at our cost efficiency metrics. And we're going to be communicating that to you in various additional opportunities. So, we actually have identified $150 million of cost initiatives that we are starting today to be delivered by 2025.

There is two main areas that we're actually looking at. The first one is recognizing that we have a much broader consumer platform. It allows us to access economies of scale and scope. And I know, Rasesh, Elizabeth myself, we're going to be looking at how do we further integrate those groups and access those cost efficiency opportunities.

The second one is really around our generation portfolio. I think everybody recognizes that the last couple of years, we have seen a significant increase in natural gas prices that have resulted in higher power prices, which we've seen an increase in capacity factors and utilization of our power plants, which that drives higher maintenance spend. As I look at the future prices, I have seen a significant decrease in natural gas prices. We expect a reduction in utilization, and therefore, we're going to be recalibrating our maintenance spend on our generation portfolio. And so, those are the two main things that we're going to be focused on.

Again, we have a very, very robust cost efficiency program. We have a dedicated team for the past six years that have been responsible in executing these cost initiatives. Every year, we look at our cost efficiency metrics. We evaluate that against the market conditions and the economic opportunity. And we also have really strong governance. We report the progress on each of our cost initiatives to our Board of Directors every quarter. And we actually validate – is validated by our internal audit team. So, very, very, very robust cost efficiency program in our company.

David Arcaro
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Got it. Thanks. That's very helpful color. And then, secondarily, I was wondering if you could give a little bit more detail on the improvement in the free cash flow before growth conversion, going from that 20% up to 55% in the Smart Home business. Could you talk about just maybe what are the biggest opportunity, I guess, maybe the low-hanging fruit to get there? It's a very big improvement, and so wondering if you could maybe quantify what the biggest initiatives are.

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

A

Sure. Rasesh , Bruce?

Rasesh Patel
President-Vivint Smart Home, NRG Energy, Inc.

A

I can start, and then Bruce can add color. But the first and foremost is we have significantly improved the unit economics of the business, and that is always continuous to do, but we've done a bulk of the lifting over the past 12 months. And as you can see, our service margin is expanded from 69% to 79%. And so, that expansion in margin, obviously, is very good in terms of it translating to cash, particularly, over a nine-year customer life.

The second thing that I would point you to is that we have taken deliberate steps to reduce customer acquisition cost. And really those come in three forms. The first is a reduction in the cost of the product itself. The second is a reduction in transportation and logistics and a normalized supply chain environment. Obviously, what we experienced through the COVID period is largely a reset itself. And so, expanding unit economics, reduced customer acquisition cost.

The third piece is really around added revenue streams. We talked about Vivint Protection Plan. We've launched a pricing optimization initiative. And this third screen has almost all margin. And so, the things that we can do with our existing customer base and further engaging them is powerful. And then, the last is a maniacal focus on costs. And you've seen the incredible reduction in the unit service cost. But we're looking at every aspect of the business from G&A to all overhead costs, and we've seen a reduction.

And the last thing I'll add is, consumer services business like this have really strong operating leverage. And as could see, we've grown our subscriber base by 40% over the last four years and that has translated into 70% revenue growth. And so, as we further scale the business, R&D, product, there are a lot of costs that are fixed, and that translates into leverage. And so, we feel – I mean, I personally feel very confident about our ability to deliver on that metric.

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

A

David, the only thing I would add is as you recall, when we announced the transaction, we had guided to Vivint free cash flow of $110 million at that time for 2023. Based on our first quarter earnings call, we did increase that to $140 million for 2023. So, right off the bat, you've seen a 30% increase in the free cash flow at Vivint. And we would continue to expect that to continue to prove out in the future based on all of the initiatives that Rasesh has just talked about.

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

A

So the momentum is good the last couple of years, but I think that it's going to be accelerated by leveraging these combined consumer platform that we have. And there is multiple ways that we can do that.

David Arcaro
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Great. That makes sense. Thanks so much.

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

A

Thank you.

Operator: Please standby for our next question. The next question comes Angie Storozynski with Seaport. Your line is open.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Thank you. Just one follow-up. So, I'm trying to compare the pitch of Vivint from the December pitch until now. And it seems to me that, initially, you were just planning to focus on basically cost efficiencies. I mean, basically that's how I saw it. At least now if I look at the bar chart showing me cash flow per share generation, there's this big growth component that is associated with growth investments. So, is it that you're just being more aggressive, now that you know the platform and you see early results of the cross-selling, and thus, there is this view that the growth can happen sooner than expected?

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

A

Yes, Angie. So, we indicated earlier when we announced Vivint, the cost synergies. And then, we said, there are revenue synergies. We put a $300 million target at the time of the announcement of the acquisition. And since then, we actually have now focused specifically on how we're going to achieve that, and that's what we have communicated today. So, now we feel very comfortable with a clear line of sight in terms of how we're going to deliver the incremental $300 million of free cash flow before growth by 2025.

There is actually a group that is focused both on the cross-selling and bundling and leveraging the expanded sales and marketing capabilities of the company. And then, the second one is continuing growing our energy and smart home services at historical level. So, the Vivint acquisition was not only predicated on their very strong subscription-based model and the 2 million customers, and the technology platform that we got, but an access of the cost synergies.

But importantly, it makes our consumer business so much better. We can actually take our energy customers, cross-sell with smart home, have a greater margin expansion opportunity, and importantly, extend the average duration or tenure of those customers from six years, which we have today in energy to nine years. So, that is a significant enhancement and strengthening of our core NRG platform through the Vivint platform.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

But again, I'm just trying to gauge if this is – you were very conservative when you were acquiring the platform and so the last four months showed you examples of that growth materializing on the revenue side happening much sooner than expected. Hence, that revenue growth driven cash flow benefit that is being realized between now and 2025 versus previous purchasing like the low costs through 2025 and then the revenue growth associated with Vivint really happening beyond 2025.

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

A

No, Angie. I think we could have done a better job in being a lot more forthcoming, clear, about the growth potential that Vivint represents for the entire consumer platform that we have. And now, we have completely fully unpacked that potential and the impact on our financials for the next five years, which now represents these free cash flow before growth trajectory that is within that 15% to 20% that we guided and probably is closer to that 20% in this planning period at, as Bruce said, much higher share price in our share repurchases assumptions. So, we feel really, really good about the plan and about the growth that Vivint represents combined with the core energy platform.

Angie Storozynski
Analyst, Seaport Global Securities LLC

Q

Okay. And just one last one. So, Elizabeth, I think you – back in December, you mentioned a certain percentage of the assumption for that cross-selling opportunity that was just, I forget – 2% to 3% of buying [indiscernible] (01:54:59) cross-selling. I mean, do you have examples, again, based on the last four months of what that percentage is in that example that you have seen thus far? I mean, is it tenfold that number? I mean, again, how is it tracking versus your original expectation?

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

A

Well, I mean, I'm going to let Elizabeth talk about that. But so far, the insights that we have on the pilots that we're running are incredibly encouraging. So, Elizabeth?

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

A

Yeah. I think, Angie, the way to think about it is we've been running these trials and Rasesh's team and my team have been working very closely together to figure out what works and what doesn't work. And that's really the purpose of 2023, is to understand where we should focus, so that when we get to scale, we're focusing on things that work. And I would say what we're seeing so far is consistent with the expectations that I had.

Rasesh Patel
President-Vivint Smart Home, NRG Energy, Inc.

A

Yeah, I would agree with that. And I think, the synergies come beyond just cross-sell. The Vivint Protection Plan was a great example. NRG was licensed to sell extended warranty products in all states, and we were very quickly able to mobilize and capitalize on that opportunity and develop that incremental revenue stream.

And so, NRG beyond its energy business also has other services businesses. Airtron as a brand is an NRG company. It's one of the largest HVAC installers in the country. And so, as HVAC's being installed in new residential construction, we have an opportunity to pre-position the Smart Home service. And so, there are a number of opportunities, I think, that sit below the surface. And as Elizabeth said, we're being very deliberate about, hey, which ones create a strong economic value? Let's prioritize those and let's mobilize around those.

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

A

But let me just put a little bit more, I guess, as they say, meat on that bone. In the first three months since we launched the Protection Plan at Vivint, that 70,000 customers that we added $10 a month per customer, I mean, that is like really, really strong performance. And when I look at the conversion rates between Energy and Smart Home and a Smart Home and Energy, although they still are on pilot, and I'm seeing double digit, anywhere between 10% to 20% conversion, so very strong numbers. Again, these are just pilots. But so far, we are very pleased with the results that we're seeing. And this is just the testing, as Elizabeth was describing, to figure out what actually works and what doesn't work with consumers. But so far, we're very pleased with the results.

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: Please stand by for our next question. The next question comes from Durgesh Chopra with Evercore. Your line is open.

Durgesh Chopra
Analyst, Evercore Group LLC

Q

Hey, guys. Thanks for the update. I appreciate it very much. All my other questions have been answered, just one sort of housekeeping question for me. Can you comment on the cadence of the share buyback? How should we think about you executing on that $2.7 billion share buyback through 2025, just any color on timing, please. Thank you.

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

A

Yes. Good morning, Durgesh. And as we have done in the past, we allocate capital when we get the cash. That has been our practice. That's going to continue to be our practice. Obviously, I am completely aware of the undervaluation of our stock. We want to get and start buying back our shares as soon as possible. That's the focus. That's the priority. And we're going to be executing on that. But is there anything else, Bruce, you want to...

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

A

No. I mean, Durgesh, obviously, in 2023, one of the big drivers for our ability to execute on share repurchases is closing the STP deal, where we'll obviously get a big slug of cash to be able to execute on that. I think once we do get that, we would expect to be in a position to hit the market as quickly as we could with the benefit of this proceeds. So that's certainly the priority for now.

Durgesh Chopra
Analyst, Evercore Group LLC

Q

Understood, guys. Thanks so much.

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

A

Thank you, Durgesh.

Operator: Please standby for our next question. The next question comes from Ryan Levine with Citi. Your line is now open.

Ryan Levine
Analyst, Citigroup Global Markets, Inc.

Q

Good morning.

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

A

Good morning, Ryan.

Ryan Levine
Analyst, Citigroup Global Markets, Inc.

Q

Hi. In terms of the 20% that's being targeted for investment, why is the 20% the right number? How did you arrive at that? And what type of opportunities are you prioritizing as you look to allocate that capital?

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

A

Yeah. So after we closed on the Vivint acquisition, we actually looked at the needs of the company to achieve that 15% to 20% growth on our free cash flow before growth per share. And we identified the $300 million growth opportunity through 2025. We're going to be allocating $535 million to that.

And then, we have reserved about $700 million to potential development of natural gas mid-merit and peaking facilities here in Texas. And this is really as a result of the market design changes that we have seen that seem to be really attractive for dispatchable generation, in addition to a very advantaged loan program that has been signed and could potentially be available to us.

And then the remaining is just to fund the continued growth in 2026 and 2027. So, we have now line of sight. That's why we felt very comfortable pivoting from our 50/50 to now 80% return and 20% growth.

Ryan Levine
Analyst, Citigroup Global Markets, Inc.

Q

Okay. One follow-up on that, in terms of longer term, as the business continues to evolve, are you looking at adding more software product offerings or other things as you further integrate into the customer?

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

A

Well, let me just say that from now until, let's say, 2025, the focus is really to optimize our network of 7.5 million customers. And doing the cross-sell, bundle and organic growth that we have quantified as $300 million of incremental cash. But the goal has always been to bring all our Energy products and Smart Home products into a common platform, so we can deliver a seamless experience with the customer that allows us to access that incremental margin and increase the tenure of our customers. That's where we want to be in 2025 and beyond.

So when you think about incremental software, I think of more as an engaging consumer platform. With customers that now include an Energy offering, a Smart Home offering, that will allow them to not only make their homes more efficient and reduce the cost, will allow us to be able to activate demand response, now, on the residential side, like we have done it with commercial and industrial customers and monetize that value in wholesale markets. And importantly, the more you make the home more efficient, it's also good for the carbon footprint of the customer and for NRG. So, as you can see, there is multiple win-wins as we integrate these into this common technology platform with the digital interface. That's how I think about the software aspect of this.

Rasesh Patel
President-Vivint Smart Home, NRG Energy, Inc.

A

Let me see, If I could just add. The Vivint platform has the ability to do OTA software-based updates. And so, just like your iPhone or your Tesla car, once we have a customer engaged, we can provide software-based services over the air. We launched sort of a DVR service for every customer that had a camera. And it is monetized into an incremental revenue stream where customers pay us $5 a month to get access to their clips. And so, as we continue to move forward, we will leverage that ability to develop additional services. And the beauty of software-based services, as you know, is it's really all margin.

Ryan Levine
Analyst, Citigroup Global Markets, Inc.

Q

Great. Thanks for taking my question.

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

A

Thank you, Ryan.

Operator: That concludes the Q&A portion of today's event. I will now pass it over to Mauricio Gutierrez for closing remarks.

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

Well, thank you very much for your interest in NRG. We are very excited about the plan that we have put forward today that creates tremendous, tremendous shareholder value.

And I look forward, me and my colleagues to see you and meet with you in person in the days and weeks to come. Thank you for your interest in NRG.