06-May-2021

NRG Energy, Inc. (NRG)

Q1 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Hello and welcome to the NRG Energy, Inc.'s First Quarter 2021 Earnings Call. Please note that today's meeting is being recorded. During the meeting, we will have a question-and-answer session. You can submit a written question at any time by clicking on the message icon at the top of your screen. Please note that your registered name will be announced along with your question during the Q&A session following the formal portion of the meeting. Guests will not be able to submit questions. Please also note that all participants are in a listen-only mode. If you experience technical difficulties during the meeting, please click on the support link on the broadcast screen.

It is now my pleasure to turn today's meeting over to Kevin Cole, Head (sic) [Senior Vice President] (00:01:02) of Investor Relations. The floor is yours.

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

Good morning. Thank you, Daphne. Daphne, I believe you were referring to may be a different earnings call. So investors please hit star one when you want to ask a question. It's just the normal framework here and so we get on to the call.

Good morning and welcome to NRG Energy's first quarter 2021 earnings call. This earnings call is being broadcast live over the phone and via webcast which can be located in the Investors section of our website at www.nrg.com under Presentations & Webcasts.

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

GAAP and non-GAAP financial measures. For information regarding our non-GAAP financial measures and reconciliations to the most directly comparable GAAP measures, please refer to today's presentation.

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

Mauricio Gutierrez

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

Thank you, Kevin, and good morning everyone and thank you for your interest in NRG. I'm joined this morning by Gaetan Frotte, our Interim Chief Financial Officer. And also on the call and available for questions we have Elizabeth Killinger, Head of Home Retail; and Chris Moser, Head of Operations.

Over the past few months, we have discussed in detail the unprecedented nature of Winter Storm Uri. The impact it had on the entire energy system, the steps that we took to prepare our Texas platform and the support we provided to our customers and communities. Today and with the benefit of additional information, we are providing more clarity on the financial impact to our company; the steps were taken to mitigate this one-time event and reinstating 2021 financial guidance.

We continue to work closely with legislators, regulators and all market participants to introduce comprehensive solutions across the entire energy system to address issues and shortcomings that were apparent during the storm. NRG remains committed to helping our customers and communities recover from the devastating winter storm and to bring solutions that ensure an event like this never happens again. We also want to provide you an update on the progress made in advancing our customer-centric strategy by reorganizing around the customer and strengthening our platform.

I want to start on slide 4, we have now processed 100% of the information received from the mid-April 55-day resettlement and issued all expected invoices to our customers. The updated financial impact from WINTER STORM URI, net of our mitigation efforts, is suspected to be a net loss of $500 million to $700 million. In order to provide you with more transparency to better understand and make your own judgment on how our platform perform, I am going to break down the components of the gross financial impact into two categories: Controllable and uncontrollable.

On the controllable side throughout the event we maintained a balanced position while absorbing very high natural gas prices, operational issues at our plants and protecting our residential retail customers from high electricity prices. In total, our platform was positive $17 million with estimated bad debt primarily from C&I customers accounting for $109 million.

Moving to the three uncontrollable items: First, the recently acquired Direct Energy portfolio had a Heat Rate Call Option with a counterparty that did not perform resulting in a $393 million gross loss. Following the event, we reexamined the entire hedge book from Direct and determined that this was an isolated issue. We're currently engaged in discussions with a counterparty, and if a satisfactory resulted is not reached, we plan to vigorously pursue recovery through all avenues.

Next, we are recognizing a $95 million gross loss due to ERCOT default allocations. These losses comprised of a $83 million cash short pay plus $12 million NPV of the remaining $102 million owned to ERCOT over the next 96 years. As a reminder, ERCOT realized defaults of $3 billion primarily from two regulated co-ops; Brazos and Rayburn. The state legislature appreciates the impact of the co-op defaults in the broader market and is considering securitization as a way to soften the impact to customers and other market participants.

Finally, we are recognizing a $395 million loss due to ERCOT's management of the grid. Particularly during the last 32 hours when ERCOT kept the market clearing price at the cap despite having more than 10 gigawatts in reserves. Our platform was balanced during this time but nonetheless we were uplifted these extraordinary charges.

To help put this in context for you, over no time in history have this charge exceeded $5 million. The state legislature is considering also securitization for these charges given they are the result of unforeseen and unhedgeable actions by ERCOT. We are focused on supporting the PUCT and ERCOT in the implementation of policies and procedures to ensure the market functions properly in the future. In total, we expect our estimated gross financial losses to be reduced by $275 million to $475 million through bad debt mitigation, recovery of Direct Energy hedge non-performance, ERCOT default and uplift securitizations and one-time savings, resulting in a net loss of $500 million to $700 million. We have a high level of confidence in the net range and seen manageable risks around the 180-day settlements and further bad debt escalations.

Now, I want to take some time and discuss the solutions we're focused on in Texas. We believe they will improve grid reliability, strengthen our markets and more importantly avoid a systemic failure of the energy system in the future. Since the storm, we have actively engaged in discussions with legislative members and proposed various changes to make Texas more resilient. I want to thank the members of the Texas Legislature for their continued leadership on these key issues.

While there are many proposals in the Texas Legislature right now, including many of which we are working actively on, I want to focus here on three concepts that the legislature has made a priority and I believe are critical to ensure what happened in February never happens again: Hardening of the system, improving communication and market design changes.

Beginning with system hardening, weatherization of assets is key to improve the overall reliability of the grid. NRG has a strong and comprehensive winterization program that begins with lessons learned from prior winter seasons and ends with our annual declaration of completion of the winter weatherization preparations to ERCOT and the PUCT by November 30. The implementation of formal winterization rules enforced through penalties and audits is something we support. With that said, one of the biggest lessons learned from this storm is how interactive and interconnected the electric and natural gas sectors are and our focus is not just on hardening the power generation side of the equation, instead we believe the entire system including natural gas needs to be hardened as they say from wellhead to light bulb.

Next, I want to talk about communications. During the storm, the lack of communication between all market participants and stakeholders was unacceptable. Formal coordination between the Public Utility Commission, ERCOT, the Railroad Commission and key stakeholders will greatly improve the amount of information available as well as informed decision making during future events. In addition, improving the dialogue between TDUs during launching events and retailers will greatly improve the amount of information available to customers. Improved communication, coupled with a state-wide emergency alert system, will ensure all Texans can stay informed about the status of the grid during times of emergency.

Finally, regarding market design changes, our focus is on improving reliability through competitive solutions in the energy and reserves markets, not through regulated generation solutions would guarantee profits or a one-size-fits-all capacity procurement. For residential customers, banning indexed wholesale products as we already do as a company is a solution that will protect residential customers from being exposed to the volatile swings in the market. Addressing these three key areas will significantly enhance grid stability and we look forward to continuing to engage with the Texas Legislature in the coming weeks.

Now moving to our regular business highlights on the slide 6, we have excluded the impact of Winter Storm Uri from all our numbers as we have done previously from one-time events. Our intention is to provide transparency to the investment community regarding the recurring earnings power of our business, particularly given this was the first quarter of our ownership of Direct Energy and separating what we believe to be non-recurring impacts of the combined business as a result of Uri. Throughout today's presentation, we have made significant effort to be as transparent as possible, on both the cost of Uri-related losses and the one-time financial impact so that you can evaluate the financial performance in either context. Gaetan will provide additional details later in the presentation.

NRG delivered $567 million of adjusted EBITDA in the first quarter, excluding one-time financial impacts from the storm. This is a 52% increase from the same period last year, primarily driven by the acquisition of Direct Energy. Notably, the addition of Direct Energy's East electric and natural gas businesses helps flatten our quarterly earnings and free cash flow seasonality. As I mentioned before, we are restating our previous financial guidance of $2.4 billion to $2.6 billion for 2021 excluding Uri.

Just to remind everyone, on March 17 we temporarily suspended 2021 guidance to reflect the significant uncertainty of Uri. While some uncertainty remains, we believe we have received enough data to provide a range of outcomes. Beyond Uri, we continue to advance our Direct Energy integration plan. Following the close in early-January, we immediately began the integration process, achieving $51 million of our 2021 synergy target. We remain very confident in our ability to achieve both the 2021 and full-plan targets.

As part of the Direct Energy integration and to further simplify our business operations, today we're announcing the designation of Houston as the sole location for our corporate headquarters. Texas is already home to our largest customer and employee base. It's a great place to do business and Houston continues to be at the forefront of energy and technology with one of the most diverse workforces in the country. We will continue to maintain regional offices in the markets that we serve as we expand our business outside of Texas.

We're also making good progress in executing our customer-centric strategy. In January, we closed on the Direct Energy transaction, forming the leading North American integrated energy and home services company, serving a network of 6 million customers. In March, we announced the agreement to sell a 4.8 gigawatt portfolio on non-core fossil assets which helps simplify and decarbonize our portfolio. And since the last earnings call, we increased our ERCOT renewable purchase power agreements by nearly 400 megawatts, now totaling approximately 2.2 gigawatts.

Last on our credit metrics, despite the impact of Winter Storm Uri, we expect to be a 3 times leverage by the end of 2021 after paying down $385 million of debt from cash available for allocation. We're working with the credit agencies to review the impact of Winter Storm Uri on the timing of achieving investment grade ratings. An extension in timeline could give us an opportunity to achieve our metrics either through debt reduction and/or EBITDA growth. I will be providing more details on capital allocation and our full strategic outlook during our Spring Investor Day.

Now turning to slide 7 for our summer outlook, first from a high-level we're expecting neutral to favorable summer weather and continued economic recovery to result in a year-on-year load growth. Despite this load growth, we're expecting reserve margins to be robust resulting in stable to lower power prices. Just to remind everyone high-load, low price is good for our business. As you can see on the upper-left hand chart, NOAA is predicting a slightly hotter-than-normal summer within the eastern Texas markets. We think this outlook to trend towards normal with a positive bias as we near summer.

Moving to the bottom left-hand side of this slide, COVID-related electric demand continues to recover across markets with ERCOT demonstrating resilience. As a reminder, COVID stay-at-home impact on load is most pronounced during the shoulder seasons and less in the summer. From a market perspective, we see 2021 as a recovery year across all our markets. In ERCOT, we expect a return to normal 2% annual load growth with residential usage in ERCOT remaining slightly elevated as stay-at-home trends remain while C&I usage improves throughout the year returning to pre-pandemic levels by the end of the year. In the East, we see similar trends although we believe C&I recovery to the pre-pandemic levels could take an additional 12 to 18 months given stronger stay-at-home trends.

Now as it relates to NRG, we continue to see strong residential load across all markets and we expect to be a relative winner given our multi-brand and multi-channel platform. In ERCOT, we're seeing lower attrition rates and incremental growth opportunities through our multi-channel approach and flight to quality following Uri. In the East, we're also realizing lower attrition, but given the less favorable regulatory framework we depend more on face-to-face sales to win customers. For planning purposes, we are assuming normal customer growth in ERCOT and a slight contraction in the East as it more closely tracks the economic re-openings.

On retail supply cost, we see little risk of sustained high prices this summer given robust summer reserve margins across all our core markets. While it is still early, we're eager for the evolution and implementation of the Biden infrastructure plan as we believe it will amplify the electrification of the economy through smart technology and cleaner energy choices.

So with this positive backdrop, we continue to make good progress in executing our customer-centric strategy as you can see on slide 8. On the Direct Energy integration, this transaction presented a step-change for us as we move closer to the customer by significantly expanding our customer network and home services. During the first quarter, we achieved $51 million or 38% of our 2021 synergy target. We remain very confident in our ability to achieve both the 2021 and full-plan targets and we plan to update this scorecard quarterly in order to provide transparency and keep you informed of our progress. We are on track to close on the 4.8-gigawatt asset sale in the fourth quarter. This is a good transaction for us as it further streamlines our business and addresses terminal value and earnings concerns that otherwise would have [ph] matched (00:19:37) our retail growth. Our portfolio repositioning and optimization is a continuous process.

We are committed to our business model and we'll continue to provide updates on our progress. Finally, we are preparing for our Investor Day. We continue to target late-spring and given the flexibility afforded by the virtual format, we will announce the event two or three weeks prior to best manage around the Texas resolution.

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

Gaetan Frotte

Senior Vice President, Interim Chief Financial Officer & Treasurer, NRG Energy, Inc.

Thank you, Mauricio. I will now turn to slide 10 for a review of the first quarter results and Uri's financial impact. On the upper-left side of the slide, we have shown our quarterly results and reinstated guidance, after excluding the one-time impact of Winter Storm Uri which we are showing separately on the right. As mentioned by Mauricio, we believe that this better reflects the recurring earnings power of our business following the acquisition of Direct Energy and it is consistent with our established practice of excluding extraordinary events.

For the quarter, NRG delivered $567 million in adjusted EBITDA or $218 million higher than the first quarter of last year excluding $967 million impact from Winter Storm Uri. This increase is driven by the acquisition of Direct

Energy which generate approximately two-thirds of its EBITDA during the winter months, given the seasonal shape of East electric and natural gas load. This seasonality will help flatten NRG's future earnings profile throughout the year. Specific to Direct Energy, we are on track to realize $500 million of adjusted EBITDA in 2021. We are also on track to achieve $135 million of synergies for 2021 as well with $51 million realized in the first quarter and a goal of at least $300 million annual run rate by 2023.

Turning now your attention to the table on the right, the total anticipated gross impact from Winter Storm Uri is now $975 million. The increase since our last communication is primarily driven by the 55-day resettlement information from ERCOT which affected our uplift costs and load estimates and added some incremental reserves for counterparty credit risk, all of which were partially offset by discounting the ERCOT default charges. We continue to pursue [ph] values of spending (00:22:39) solution estimated to be in the range of $275 million to $475 million. This would reduce the economic impact to a net amount of $500 million to $700 million.

From a cash standpoint, based on $150 million of estimated bill credits owed to large Commercial & Industrial customers in 2022, the total negative cash impact in 2021 is expected to be approximately $150 million lower at $350 million to $550 million, including the effect of the offsets previously mentioned. Finally, we are reinstating our 2021 guidance at the original ranges of $2.4 billion to $2.6 billion for our adjusted EBITDA and $1.44 billion to $1.64 billion for our free cash flow before growth.

I will now turn to slide 11, where we are abating our planned 2021 capital allocation. Changes on this slide from last quarter are indicated in blue. Starting from the left on the third column, the net capital requirements for the Direct Energy acquisition was reduced by $38 million based on the latest estimate of the post-closing working capital adjustment.

Moving on to the next column, the estimated Winter Storm Uri capital allocation impact is $825 million, net of anticipated customer bill credit outstanding at the end of the year and would be at $450 million after deducting the midpoint of our estimated mitigation efforts or $375 million. This has reduced our original deleveraging plan in 2021, however we remain committed to maintaining a strong balance sheet and improving our credit metrics over time. Absent any mitigation of such recoveries which are shown in the far right of the chart, the company will still pay down debt by $385 million in 2021 and continue to delever over time to meet its credit profile goals. Importantly, this does not include any deleveraging associated with the sale of our East and West assets which is still slated to close later this year.

Moving on to slide 12, I will start on the left with our 2021 credit metrics. After adjusting our corporate debt balance for the reduction from our 2021 capital allocation and minimum cash, our 2021 net debt balance will be approximately $7.8 billion. This when based on the midpoints of our adjusted EBITDA, implies a ratio of just under 3 times [ph] net debt (00:26:05) to adjusted EBITDA at the end of the year. This notably excludes a one-time impact of Winter Storm Uri which we also expect to be excluded by the rating agencies.

On the topic of rating, we continue to work with the agencies to review Winter Storm Uri's impact on the timeline and the requirements to achieve investment grade. We remain committed to strong credit metrics and continue to operate under the assumptions that investment grade ratings will be awarded shortly after achieving the targeted metrics. But we're not controlling this process. And we realize that given the circumstances, it could take the agencies much longer than previously anticipated to be comfortable granting us an IG rating. I would note that if the timeline is extended, it could also give us an opportunity to achieve our metrics either through debt reduction and/or EBITDA growth. Turning to the right-side of the slide, we also wanted to update you on our latest liquidity position, which at $4.1 billion as of a few days ago remains very strong and sufficient to continue supporting our business even during period of stress.

In conclusion, we are reinstating our EBITDA and free cash flow before growth to the original guidance provided in the last earnings call, excluding the impact of Winter Storm Uri. While the storm has impacted our capital allocation plan, we have maintained a strong liquidity position before, during, and after the event while our core business continues to perform as otherwise expected.

With this, I will hand it back to Mauricio.

Mauricio Gutierrez

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

Thank you, Gaetan. I want to provide a few closing thoughts on the slide 14. I recognize that Winter Storm Uri has impacted investor confidence in ERCOT's market design and the durability of our cash flow. But I want to be clear. Given the steps being discussed in the Texas Legislature and the actions by market participants, I don't believe an event like this can happen again. The systemic failure was the result of a lack of winter stress planning, which was then amplified by poor electric and natural gas coordination and protocols to orderly restore the energy system and communicate with customers. NRG is a key pillar to Texas' outsized growth and all stakeholders are focused on addressing winter reliability swiftly and comprehensively. ERCOT's winter planning parameters will be enhanced, grid coordination will be improved and protocols for a large-scale emergency will be established.

Now finally today, following our extensive CFO search. I am pleased to announce that Alberto Fornaro will join our team as Executive Vice President and Chief Financial Officer effective June 1. Alberto is a seasoned finance expert who brings over 30 years of experience and a unique combination of consumer, technology, manufacturing and risk management experience. Alberto joins us from Coupang, the world's fifth largest e-commerce platform where he served as Group Chief Financial Officer and Senior Advisor. Before that, he served as CFO for public and private companies including International Game Technology, a leading gaming company; Doosan, a contract and heavy construction equipment company; and Technogym, the world's second-largest manufacturer of fitness equipment. I believe Alberto's expertise is the ideal fit to enhance our decisive move closer to the customer.

I also want to take a moment to recognize Gaetan Frotte for stepping in as Interim CFO and leading the finance organization during this challenging time. Gaetan is a very important and valuable member of our leadership team. On behalf of everyone at NRG, thank you Gaetan for your leadership and dedication.

So with that Daphne, we'll open the line for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Julien Dumoulin with Bank of America.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

Hey. Good morning, team. Thanks for the time and the opportunity. Thanks for the detailed remarks as well.

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

A

Good morning Julien.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

Good morning. So if I can just rehash a couple of the comments. I know you alluded to them in the remarks a little bit but the $393 million, the counterparty with the Heat Rate Call Option can you expand a little bit on just what that exposure is? Is it a single counterparty and what are the prospects for recovery there as we kind of look forward through presumably what is some sort of process already ongoing if you don't mind.

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

A

Yeah. Julien, so – yes, this is a single counterparty. This is a bilateral Heat Rate Call Option, and I mean the conversations are ongoing. So as you can appreciate, I can't provide a lot of details because of the possible different outcomes that this can take or – but I can tell you is that while we're having I think constructive conversations, we're going to pursue every available means that we have to recover the money that we are owed.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

Understood. And it's a single power plant or is it a [ph] financial counterparty? (00:32:38)

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

A

Yes. It's a single powerful plant.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

Got it. Excellent. And then if I can on the other side of this, obviously there's default allocations, uplift charges et cetera. Can you just clarify what is the legislature looking at across the options and I get that the session isn't over yet and we've got a few more weeks to go. But I just want to clarify again the different ERCOT exposures that you have here. What is on the table here potentially for the legislature? I know you alluded to this in part in the comments but I want to make sure I'm clear about what's included here potentially.

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

A

Well, I mean I think the two areas that you should focus is the ERCOT and the uplift charges that I already explained I think in great detail in the presentation. I think everybody recognizes the impact to the broader market that either was an exposure there was on unhedgeable or exposure from co-ops that the rest of the market is basically being burdened with. I think the legislature recognizes that they are prioritizing how they move through these different buckets of, let's call it, buckets of cost. There are a number of bills that are addressing securitization, specifically right now for co-ops and ERCOT defaults, also including some ancillary services and uplifts.

So, I think we are – we have a very positive view on these given the tone of the legislature. Obviously this needs to work through its process. We're going to continue working constructively with them and providing them all the information that they need. But the signs that we're seeing is that they're making progress in addressing these very, very important and concerning issues for all market participants.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

Right. So basically this is the $95 million and potentially the $395 million...

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

A

That's correct.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

...potentially being [indiscernible] (00:34:54).

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

A

Correct.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

Excellent. Sir, if I may just one more quickly. Any preview here as to the metrics that you would be anticipating to disclose here in late-spring, just kind of a sense as to what the initial blueprint might be?

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

A

For the Analyst Day in terms of our customers? I'm sorry. Go ahead.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

Yeah. Whatever metrics you anticipate disclosing. I'm not asking for specific new targets. But what metrics would you anticipate updating here, presumably EBITDA growth, but I don't want to – I'm just curious what's going to be the target [indiscernible] (00:35:31)?

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

A

Yeah. I mean I think on the Analyst Day – yeah. I think on the Analyst Day we want to do three things: Number one is have a conversation around the strength of our core platform and the value that we see and the opportunity that we see closer to the consumer and the customer. So I think customer lifetime value will be something that we will be discussing and how we can leverage our operating platform in providing additional products and services to our customers.

The second thing is I will be also highlighting and reviewing our capital allocation. I mean our framework is very clear. But I think I also need to be mindful that the storm has had and it will have an impact perhaps on the timeline for our investment grade rating. So I think this is something that we will be discussing. I also want to introduce metrics that showcase the growth that the company has had on a per-share basis and I mean that's something that we will be discussing more in detail.

And then finally is our sustainability framework and ESG metrics, particularly the path that we have on decarbonizing our operations. So we already have provided the guidepost through our commitment to the 1.5-degree trajectory. But I also recognize that the investment community would like to see more specificity around it. So this is what I intend to cover on the Analyst Day.

Julien Dumoulin-Smith
Analyst, Bank of America Merrill Lynch

Q

Excellent. Thank you guys for the time. Best of luck in preparing.

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

A

Great. Thank you, Julien.

Operator: Your next question comes from the line of Michael Lapides with Goldman Sachs.

Michael Lapides
Analyst, Goldman Sachs & Co. LLC

Q

Hey, guys. Thank you for taking my questions. I actually have a couple. First of all, can we do a cash flow walk related to Uri? So if I take the $975 million kind of headwinds, how much of that cash has been paid out as of March 31 versus is cash that's going to be paid out over the next couple of quarters?

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

A

Yes. Michael, good morning. I will pass it on to Gaetan.

Gaetan Frotte
Senior Vice President, Interim Chief Financial Officer & Treasurer, NRG Energy, Inc.

A

Yeah. Michael, so the way I would characterize it the gross impact is $975 million, so that's an impact over time. As we've said, the impact in the first quarter is $967 million, and then other times it would be $8 million of incremental cost associated with it. The way to think about it is all of the cost of goods sold portion of that $975 million had been settled by now, all of the gas settlement and all of those things have been done. But obviously on the working capital side, some of the receivables have been issued, the billing has been issued but the cash hasn't been paid yet. And you will probably have noticed at the end of the first quarter that we had a large receivable balance. But then in our liquidity numbers as of a few days ago, our liquidity has gone up significantly which shows the collections that we've enjoyed during the month of April. So, this is the second moving piece. And then the last moving piece is the one we highlighted on page 10, which is the deferred credits and we have estimated this to be $150 million for 2021 with an impact basically deferred into 2022.

So those are the main moving pieces here around the cash. You should assume that based on those, the cash impact on for us for the first quarter is below the $975 million basically. Based on the 10-K, you would be able to reconcile that it's roughly $100 million below that.

Michael Lapides
Analyst, Goldman Sachs & Co. LLC

Q

Got it. So in other words, I'm going to just try and simplify this a little bit. In other words, for the next couple of quarters there's about $100 million of headwind related to the $975 million. That's cash. I'm not worried about earnings here, just cash. So, $100 million outflow related to that. And then the $150 million part more than offsets that this year. But then you kind of pay that back next year. And the mitigants. So the mitigants that you outlined, that's all kind of the $275 million to $475 million. You've got none of that. So any dollar you get is incremental cash flow above and beyond?

Gaetan Frotte
Senior Vice President, Interim Chief Financial Officer & Treasurer, NRG Energy, Inc.

A

Yeah. That's right. That's right.

Michael Lapides
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Okay. Thank you, guys. Much appreciated.

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

A

Thank you, Michael.

Operator: Your next question comes from the line of Jonathan Arnold with Vertical Research.

Jonathan Arnold
Analyst, Vertical Research

Q

Good morning, guys.

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

A

Good morning, Jonathan.

Jonathan Arnold
Analyst, Vertical Research

Q

A quick one on, just as we think about the mitigant range and I think Mauricio you said you felt very confident in the range. Could you give us any pointers as to how significant you feel these different pieces might be, whether they're sort of larger or smaller, and I guess a little more specifically, I mean does the high-end assume recovering most of the Heat Rate Call Option position or I'm just curious if you can give us any pointers within that range?

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

A

Yes, Jonathan. Well, I mean what I would say is we feel confident with this range given the information that we have today and what we try to do is break it down into it's very specific components. So, for example, the first, the bad debt. I mean we're working with our customers either through payment plans or extending the relationship with the customer on an NPV basis. So I would expect that that bad debt number so far, we have – we're seeing really constructive dialogue with them. I mean I already spoke about the Heat Rate Call Option and we're going to explore all avenues on that.

I think the securitization is making its way through the process in the Texas Legislature. We're seeing some positive signs there. That includes both the default and the uplift charges. So I hope that this provides you at least some sense in terms of – about the size of the buckets and where we are in the process. Obviously, we will be updating this number throughout the year as we get more clarity and visibility in any of these efforts.

Jonathan Arnold
Analyst, Vertical Research

Q

Is the one-time cost saving fees significant or a smaller element?

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

A

Yeah. And so, I mean the one-time cost saving as you will all appreciate, I mean we have some cost savings already as part of the Direct Energy acquisition on the synergies. I mean we're making good progress there. Remember, those cost synergies tend to be recurring. What the cost savings that I'm talking about here are going to be more like one-times and the entire organization – I mean, we're not pleased with these results, so the entire organization is looking at the cost structure and we're evaluating what can we do to reduce some of the cost in 2021 without impacting negatively the organization. So – but I wouldn't say that these numbers are led by cost savings. I think you should think about us around the edges and not necessarily the main number.

Jonathan Arnold
Analyst, Vertical Research

Q

Great. Okay. And may I just push you [ph] a little bit (00:43:34) Heat Rate Call Option, are you the only counterparty to that asset or one of many?

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

A

I cannot answer that. I mean this was a bilateral financial deal with one counterparty that we know that they had one plan to bag these financial bilateral agreements. So I cannot tell you what else they did on – with hedging their position.

Jonathan Arnold
Analyst, Vertical Research

Q

Okay. And then just maybe a slight follow-up to that, I mean Mauricio any sense of what the opportunities are like to perhaps adding customer books or something larger, would you consider picking up any assets that might become distressed here [indiscernible] (00:44:30) of customer refocus?

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

A

I mean we're always going to be opportunistic about that and we have a – I think we have a pretty long and proven track record of buying books, distressed books at value. Our goal right now is to integrate Direct Energy. I think that was a pretty large acquisition that we made last year and all hands on deck there to achieve the goals that we committed to our investors and I mean the returns are very compelling, so we're going to be focusing on that. But having said that, I mean if there is very something that is, from a value standpoint, very, very compelling I would characterize it more as just buying books as opposed to anything else, and we'll just going to be very, very opportunistic about that.

Jonathan Arnold
Analyst, Vertical Research

Q

Okay. Great. Thank you very much.

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

A

Thank you, Jonathan.

Operator: Our final question comes from the line of Ryan Levine with Citi.

Ryan Levine
Analyst, Citigroup Global Markets, Inc.

Q

Hi. Thank you for taking my question. I was trying to...

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

A

Hey. Good morning, Ryan.

Ryan Levine
Analyst, Citigroup Global Markets, Inc.

Q

Good morning. In terms of the Houston headquarters decision, can you provide some color as to why you made that decision, what the tax implications are and from a real estate perspective, if there's any assets that you're looking to monetize and any [ph] digital (00:45:57) proceeds that you expect to yield from that decision?

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

A

Yeah. I mean if you recall we've been running a dual headquarters now for quite some time. And I think in the spirit of simplifying our business operations and also as part of the Direct Energy integration, this was already on the works for quite some time. Obviously, the Winter Storm Uri impacted the timing of the announcement. But I think just from a simplification and cost optimization standpoint, this is really – this was all part of our plan.

I think one thing that is important to note is as we're thinking about the return to the office, we all appreciate that remote work is going to be more prevalent in the future and we've gotten very comfortable with that. We've been running our company in a very efficient way. So I would expect that as we re-imagine the workspace of the future that hybrid and remote work will be more prevalent. And we actually have inside the organization something that I call Workplace 21, which is really a group of – a committee that is thinking through our real state needs, what are we going to do in terms of which employees need to work remote, hybrid, in-person in the office, how do we think about maintaining the culture of the company through these new way of working, how do we extend some of our corporate values like safety and well-being beyond the offices and into homes. So I mean this is very comprehensive.

We, as a company are going to be flexible with our employees. We recognize that in order to attract the best talent, we have to keep up with technology and the means by which our employees are more fulfilled and satisfied. So I'm very pleased with the move. I think as I said on my remarks, I mean Houston is an incredible city in terms of leading the energy transformation in terms of technology. They have a very diverse workforce. Many of our customers or the majority of our customers already reside in Texas. Many of our employees are already there. So, I think this is just formalizing something that really has been happening now for quite some time.

Ryan Levine
Analyst, Citigroup Global Markets, Inc.

Q

I appreciate that. In terms of trying to quantify some of the financial impacts of the decision, is there any color you could provide realizing that some of the details haven't been fully determined around additional cost savings or benefits in terms of a financial statement impact of that decision?

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

A

I mean I would say that they were part of the plan around simplifying the organization and the Direct Energy integration, so they're embedded to some extent on the synergy targets that we already provided to them. I mean we're going to maintain regional offices because with the Direct Energy acquisition, we actually grew significantly outside of Texas. It's not going to have – we don't expect to have any tax implications in the current locations that we have. I mean Princeton is going to continue to be a pretty major hub in our operations and so I don't expect any negative impact.

Ryan Levine
Analyst, Citigroup Global Markets, Inc.

Q

Okay. Appreciate it. Thank you.

Operator: I will now turn the call back over to Mauricio Gutierrez for closing remarks.

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

Thank you, Daphne. Well, thank you for your interest in NRG and we look forward to speaking with all of you at the Spring Analyst Day. Thank you.

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