Unit Economics Working Group Meeting

PAYGO PERFORM

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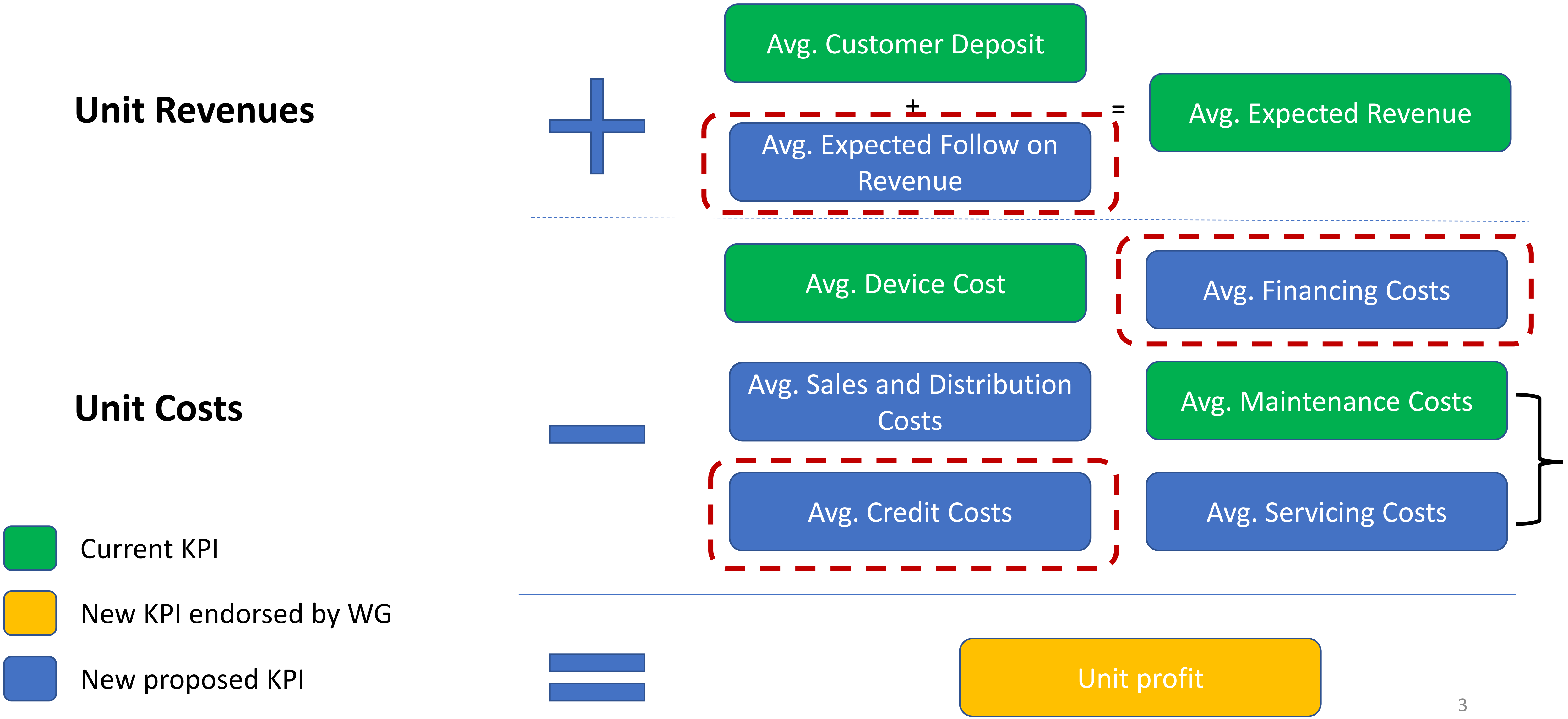
Logistics

- We want this and future sessions to be interactive, open to questions or points of discussion at any time, unmute and speak up at any time
- To minimize outside noise, however, your microphones have been muted on entry. Please keep yourself muted throughout the call unless you have a question
- You may ask a question or make a comment at any time during the call. To do so you can:
  a) Use the Chat box on the right-hand side of the WebEx session.
     - To ensure that your question is seen by the moderator, select “All Participants” from the drop-down menu before sending the question.
  b) Unmute yourself and ask a question remembering to re-mute yourself when done.

Unified Framework for Unit Profitability KPIs



Key Issues to Address in Unit Economics

- Based on our prior discussions, there are 4 key issues that have emerged for Unit Economics, which we need to address:
  1) Time Value of Money
     - For PAYGo companies, the revenue will be composed of a stream of payments that will be happening in the future. Therefore, it may be necessary to do the present value of these stream of payments using a discount rate to accurately reflect the revenue earned
  2) Risk of Non-Payment / Default (Credit Cost)
     - There is a risk that the revenue will be lower than expected due to non-payment / default of customers. This effect may captured by the Collection Rate metric in the Portfolio Quality Working Group. Although it is highly relevant in Portfolio Quality, it is also relevant in Unit Economics since it impacts the total revenue
  3) Financing Cost
     - Refers to the cost of financing solar panels that are sold, placed in inventory as well as the financing of the operations
  4) Denominator to Calculate Unit Values

Survey Results for Key Issues – Summary

Key Issue	Proposed Way to Address it	% of Positive Responses – Agreement with Proposed Approach
Time Value of Money	• Take the PV of Avg. Expected Follow On Revenue (when looking at KPI on a long term basis)	71.4% (10 out of 14)
Risk of Non-Payment / Default (Credit Cost)	• Calculation of Credit Cost = [1 – Collection Rate] x Avg. Expected Follow On Revenue	64.3% (9 out of 14)
Financing Cost	• Calculation of Financing Cost = Interest rate on Debt x Avg. Device Cost	50% (7 out of 14)
Denominator for Calculation of Unit Values	• 3 options: (i) Installed Units; (ii) Units in Circulation; and (iii) Other	(i) 28.6% (4 out of 14) (ii) 35.7% (5 out of 14) (iii) 35.7% (5 out of 14)

Time Value of Money – Review of Survey Results

Comments – Not In Agreement with Proposed Calculation
The back-end financing of the portfolio is also in nominal terms. It seems more precise to caveat the output as unadjusted for inflation than to try and find the perfect discount rate for the calculation.
Discounting is going to end up bringing too much confusion and make the KPI harder to read. I would recommend using a "snapshot" view instead. For example for revenue per unit: Total revenue during a given time period (e.g. month) / Total active units during that time period
Nominal cashflow is usually how we assess it. If the IRR is above the discount rate, it's worth looking at. but different investors may have different discount rates, so a positive NPV for one might be a negative NPV for another. IRR and nominal net cashflow is a measure more independent of investors' issues. A common rate is usually 10% discount rate if one is to be adopted.
Since we are probably only discounting 2-3 years of cashflow, not sure it makes a huge difference (vs a DCF valuation calculation). Furthermore, the discount rate is vague. If we need to adjust for time value of money, this can be tackled under financing cost.

Pros

- More accurate representation of the revenue

Cons

- Too much confusion and make KPI harder to understand
- Difficult to determine the appropriate discount rate

Risk of Default / Non-Payment – Review of Survey Results

Comments – Not In Agreement with Proposed Calculation
[1 - Collection Rate] is not an appropriate metric to use because it is not equal to % written off. [1 - Collection Rate] is equal to cash not collected in time.
Similar to my previous comment I believe that anything that include expected or future revenue is going to end up being too complicated. We currently look at it as "Loss due to collection rate" which is calculated as a snapshot view over a given period as: Total billed to clients - Total cash received from clients = Loss dur to collection rate
Imagine a situation where a customers have a weekly plan, and systematically pay 1 week late. They never really fall into the "at risk" group, as they still keep paying regularly without reaching a long period without payment. However, the repayment period will double => causing to increase the financing cost of the PAYGo company. Collection rate will be 50%, but I don't want to have half of my Average Expected Follow-on Revenue to be counted as "Credit Cost", since it is not a cost as it will be repaid. The only additional cost will come from a higher financing cost. For me this collection rate approach doesn't capture the credit cost. PAYGo customers regularly delay their payments, lowering the CR, but only a small fraction of them definitely stop paying, becoming written-off (this is the cost we want to capture)
Apologies, maybe I missed it, it depends if the Collection Rate definition is cumulative or over a particular time period. If the former, then this Credit Cost definition is okay.
i like the approach, but the name "credit cost" is a bit odd. Maybe something more intuitive like "Missed Revenue"

Risk of Non-Payment / Default – Proposed Solution

- Based on the survey responses, it is clear that we need to capture the cost of non-payment/default; however, the definition proposed needs to be refined
- **Proposal:**
    - Risk of Non-Payment / Default Cost = % Written Off x Avg. Expected Follow On Revenue
    - % Written Off = % of total Units that have been written off / defaulted over a specified time frame

Financing Cost – Review of Survey Results

Comments – Not In Agreement with Proposed Calculation
This figure doesn't take into account in how many years you payback the inventory loan. Financing Cost = Total interests / # Devices acquired
This assumes 100% leverage on the device cost, which may not be the case. Also, we should probably use a weighted average of device costs based on the historic or projected sales mix.
Take into account the average time the device remains in inventory
Also need to account for contract length (longer contracts or slower repayment speeds will increase finance costs) and the paydown (or amortization) of the PAYGo loan.
Close, but it doesn’t reflect the length of the financing provided. This formula effectively assumes 1 year, which may not be true. Maybe multiply this by average credit length?
For the early stage companies, inventory is often financed by equity. This needs to be factored in and measured over time. Ignoring it makes the calculation more theoretical/less useful, especially in cases where the company has not yet raised any debt. We should figure out a way to discuss/represent this since it is an actuality.
A couple of things missing: 1) you would need to weight the calculation by the average time to recover that cost based on the payment plan terms. Some companies would recover device cost in 9 months, some in 18 months, depending on their choices around payment plan length. And 2) you are also financing your selling costs since these are borne substantially upfront.

What to use in the Denominator to Calculate the Unit KPIs?

- There are different factors which we could use:
  - **Active Units** = this was the approach used in the initial set of KPIs
  - **Assets in circulation (t)** = All products that were sold, leased or rented to the customer, including assets that have been repossessed or returned, but excluding assets which have been written off
  - **Installed Assets** = Number of assets that have been installed for customers
- **Question: Which one shall we use? Should we select a different value from the options above?**

Units to Use in Denominator – Review of Survey Results

Comments – Other Approach
The question is not clear. Depending on the KPI, we shall use a different denominator.
Perhaps too complicated, but most PAYG companies are still growing and some allowance for growth above the Units in Circulation option would be reasonable.
This is too broad a question. Depends on the KPI. For most, units in circulation makes sense if the metric refers to units actively used by customers and/or in the warehouse. We should discuss this on a metric by metric basis to decide what's meaningful.
For consistency, I think it is safer to not keep changing the denominator when a unit changes status. Cleaner to just include all units that were originally installed in a given cohort, and always use that number, irrespective of the status of those units at a moment in time when calculating a KPI.
I do not believe it truly matters which denominator we use for Fiancing cost it just need to be the same denominator that for all other indicators (revenues and other costs) else we will end up with figures we cannot add together

Additional KPIs to Consider

- Overhead Fixed Costs
  - Although we are not allocating the fixed costs to each unit, we should have a KPI that captures all of the Fixed Costs at a firm level
  - Question: Should this KPI belong in Unit Economics, or be a part of the Overall KPI Working Group?
- Avg. Repossession Costs
  - Questions: Do we need it? How do you define this cost?

Next Steps

- Based on today's call, develop list of KPIs that we have agreed upon, together with their corresponding definitions, and have signoff from the entire Working Group
- Address any additional issues that may still be outstanding and/or any new issues that have come up
- Set up next Working Group Call at end of May / 1st week of June

Additional Questions? Feedback?

Thank You!

To learn more, please visit

https://www.findevgateway.org/organization/paygo-perform