

THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

GOGO - Q1 2016 Gogo Inc Earnings Call

EVENT DATE/TIME: MAY 06, 2016 / 12:30PM GMT



CORPORATE PARTICIPANTS

Vavara Alva *Gogo Inc. - VP of IR & Treasurer*

Michael Small *Gogo Inc. - President & CEO*

Norman Smagley *Gogo Inc. - EVP & CFO*

CONFERENCE CALL PARTICIPANTS

Jonathan Schildkraut *Evercore ISI - Analyst*

Phil Cusick *JPMorgan - Analyst*

Lisa Friedman *UBS - Analyst*

Dick Ryan *Dougherty & Company - Analyst*

Simon Flannery *Morgan Stanley - Analyst*

James Breen *William Blair - Analyst*

Andrew De Gasperi *Macquarie Securities - Analyst*

Andrew Spinola *Wells Fargo Securities - Analyst*

Carter Mansbach *Jupiter Wealth Strategies - Analyst*

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Q1 2016 Gogo earnings conference call. (Operator Instructions). As a reminder, this conference call is being recorded. I would now like to turn the conference over to Miss Alva, Vice President of Investor Relations and Treasurer. You may begin.

Vavara Alva - *Gogo Inc. - VP of IR & Treasurer*

Thank you and good morning, everyone. Welcome to Gogo's first-quarter 2016 earnings conference call. Joining me today to talk about our resorts are Michael Small, President and CEO, and Norman Smagley, Executive Vice President and CFO.

Before we get started I would like to take this opportunity to remind you that during the course of this call we will make forward-looking statements regarding future events and future financial performance of the Company.

We caution you to consider the risk factors that could cause actual results to differ materially from those in the forward-looking statements on this conference call. These risk factors are described in our earnings press release and are more fully detailed under the caption Risk Factors in our 10-K, which was filed with the SEC on February 25, 2016.

In addition, please note that the date of this conference call is May 6, 2016. Any forward-looking statements we will make today are based on assumptions as of this date. We undertake no obligation to update these statements as a result of new information or future events.

During this call we will present both GAAP and non-GAAP financial measures. A reconciliation of GAAP to non-GAAP measures is included in today's earnings press release.

This call is being on the Internet and is available in the Investor Relations section of Gogo's website at IR.Gogoair.com. The earnings press release is also available on our website. After management's remarks we will host a Q&A session. And now it is my great pleasure to turn the call over to Michael.



Michael Small - Gogo Inc. - President & CEO

Good morning, everyone. Thanks, Vavara. We are off to an amazing start in 2016. We had record revenue of \$142 million, up 23% year over year. We also had record adjusted EBITDA of \$14.5 million, up 76%.

But most importantly we marked the beginning of our next chapter; the era of 2Ku has officially taken flight. The service is flying on AeroMexico as we begin the enviable task of installing the growing number of committed aircraft.

We have massive momentum with 2Ku beginning with our announcement yesterday that International Airline Group has decided to install 2Ku on British airways, Iberia and Aer Lingus long-haul aircraft. IAG is one of the largest aircraft groups in the world and we couldn't be happier to be connecting some of the most iconic brands in commercial aviation.

We also entered the Chinese market by announcing we will partner with Shareco to install 2Ku on 50 Hainan and Capital Beijing aircraft. And in North America we agreed to extend our relationship with Air Canada to install 2Ku on its entire wide-body international fleet.

Lastly, Delta increased their commitment to more than 600 2Ku aircraft bringing our 2Ku awarded aircraft over the 1,000 mark.

I also want to highlight a couple of other developments that are critical to our commercial aviation business and specifically 2Ku. We secured large capacity commitments with [Intelsat] and SES.

We also added the ability to leverage OneWeb's LEO Constellation when it comes online in the next few years, which will have huge advantages in terms of coverage and latency.

We built 2Ku with an open architecture that allows us to take advantage of high throughput satellites, OneWeb and any other new developments that happen in the Ku-band.

In addition to securing a lot more capacity at lower cost, we unveiled our powerful new modem capable of delivering 400 megabits per second. This will make sure the bandwidth delivered to the plane won't be limited by the modem. It also gives us plenty of room for growth.

All this means that 2Ku is getting better even as we are just beginning to install it. Most importantly, these improvements can be implemented on 2Ku installed aircraft seamlessly, which is incredibly important to airlines. It means that our airline partners who choose 2Ku will stay future ready and ahead of the curve.

In both business and commercial aviation our aircraft centric approach to operating this business gives us tremendous advantages.

For example, we are making great progress on the increasing volume of STCs, completion of which will keep us on track to exceed our 75 2Ku installation target this year. This will be a critical step in getting the 1,000 2Ku awarded aircraft installed and generating revenue.

We also signed agreements with Airbus and Boeing to have 2Ku installed on their A350 and 787 aircraft. So now we can offer airlines 2Ku on every major mainline aircraft type.

All told we installed or upgraded more than 500 aircraft across commercial and business aviation this quarter, another Company record. Nearly 50% of our commercial aviation aircraft have now been upgraded to ATG-4 which adds much needed capacity to our North American network.

Q1 has also been incredibly busy for Business Aviation. Gogo Biz 4G is now flying on our test lab and customers are beginning to provision their planes in preparation for 4G's commercial launch in 2017. And with record quarterly profits of \$20 million, BA is off to a strong start in 2016.

To close, we started 2016 firing on all cylinders. 2Ku is now in commercial service. 2Ku awards now exceed 1,000 aircraft. And our financial and operating results continue to set records. We feel better than ever about 2Ku's capabilities. We look forward to the day when the first 1,000 2Ku aircraft are online. And on that note I will turn it over to Norm.

Norman Smagley - Gogo Inc. - EVP & CFO

Thank you, Michael, and good morning, everyone. We had a great first quarter. Total revenue was up 23% to \$142 million. Service revenue grew 24% to a record \$119 million. CA North America and BA combined segment profit was up 29% to \$34 million, while combined segment profit margin expanded to 25%. Adjusted EBITDA increased 76% to \$14.5 million. This was our best EBITDA quarter ever.

Now turning to segment results, CA North America service revenue was up 16% to \$83 million, driven largely by an increase in aircraft online. We ended the quarter with 2,500 North American aircraft online which reflects 130 installs and 17 retirements. We also had 230 net awarded but not yet installed aircraft at quarter end.

During the quarter we installed or upgraded a record 219 ATG-4, almost double our previous highest ATG-4 install quarter. This brings our total ATG-4 aircraft online to nearly 1,200.

To better align our plane count with how we recognize revenue, we are introducing aircraft equivalents, which depicts our plane count by segment based on where the aircraft flies, rather than on which segment the underlying airline contract is associated with. Going forward we will use aircraft equivalents when calculating ARPA.

For the quarter annualized ARPA of 134,000 was consistent with the prior year, but grew 15% year-over-year excluding aircraft we have added since the beginning of 2015, primarily regional jets and aircraft with new airline partners. We also had a large Gogo Vision launch promotion in the first quarter of 2015.

We expect continued ARPA dilution over the next couple of quarters as we finish installing regional jets and launch new airline partners. The dilution from these aircraft will start to diminish as these new fleets become seasoned and as we begin to upgrade Delta planes to 2Ku. We expect ARPA growth to be modest in 2017 and accelerate in 2018 as we get more 2Ku aircraft online.

CA North America segment profit was \$13.8 million, representing a 16% margin, which was up year-over-year as a result of continued strong operating leverage.

Now turning to BA, service revenue was up 41% for the second straight quarter to \$31 million. Total revenue for the quarter exceeded \$50 million for the first time. BA equipment revenue of \$19.4 million was slightly lower due to lower ATG units shipped, partially offset by higher average revenue per unit.

ATG aircraft online increased 23% to nearly 3,700 and ATG service ARPU increased 15% to almost 2,500 per month. Segment profit was up 20% to \$20 million representing a 40% segment profit margin.

Turning to CA rest of world, we installed 35 aircraft and ended the quarter with 237 aircraft online. Total revenue for the quarter was \$4.6 million, up threefold from the prior year.

Our CA rest of world backlog stands at over 600 awarded but not yet installed aircraft, including new wins across the world from IAG, Air Canada and Shareco in China. We expect to install the majority of our awarded aircraft by the end of 2018.

Rest of world segment loss increased to \$19.7 million from \$18 million last year. The increase was due primarily to higher [ED&D] expenses related to 2Ku STC and line fit activities. Q1 CapEx of \$24 million was nearly \$8 million lower than the prior year due to lower airborne equipment purchases and CapEx for the headquarters buildup.



We ended Q1 with \$313 million of cash. As expected, Q1 had higher payments and an additional principal payment under our credit facility. The cash used in the quarter is consistent with our full-year expectations.

To wrap up, our strong financial performance in the first quarter, coupled with increased momentum in the market for 2Ku, give us a strong tailwind for continued growth in revenue and profitability. Operator, we are ready to take our first question.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Jonathan Schildkraut, Evercore ISI.

Jonathan Schildkraut - Evercore ISI - Analyst

Great, thank you, I am here with Rob. I guess a couple of questions. First, I was wondering, Norm, if you could give us a little bit more detail on the equipment revenues in North America for the quarter.

Obviously that came in a little bit higher than we were anticipating. Just wanted to get any color there. And if you can give us some sort of margin color on that as well and then I will come back with a strategic question, thanks.

Norman Smagley - Gogo Inc. - EVP & CFO

Sure. So as we get into new airline deals the structures are accounted for on a deal by deal basis. So we have two agreements where we recognize equipment revenue for sales, one is United which we talked about previously. And the second is AeroMexico for the Gogo Vision installations. We do recognize equipment sales for that particular transaction.

Jonathan Schildkraut - Evercore ISI - Analyst

Great, and (multiple speakers).

Norman Smagley - Gogo Inc. - EVP & CFO

(Multiple speakers) are -- yes, go ahead.

Jonathan Schildkraut - Evercore ISI - Analyst

No, you beat me to the punch.

Norman Smagley - Gogo Inc. - EVP & CFO

Okay. We don't give specific margin guidance on a deal by deal basis. So I will refrain on that piece of it.



Jonathan Schildkraut - *Evercore ISI - Analyst*

All right, understood. So listen, I would love to get a little bit more color on what is going on with the backlog. 1,000 planes in 2Ku backlog is obviously a massive number, even relative to the size of the satellite or the overall commercial airline market.

I was wondering I guess if you could give us a little understanding -- there are some numbers here I am having a hard time reconciling. The US backlog -- or the North American backlog is at 230, the backlog for ROW is more than 600 and yet the 2Ku backlog is over 1,000.

And I guess the last time you guys put out a 2Ku backlog it was around 850 and then you added it looks like another 350 from Delta and then the recent agreement looks like 150 and I guess now it is more than 1,000.

And there has been a lot of numbers floating around -- just maybe some clarity here to give us a little better picture would be really helpful, thanks.

Michael Small - *Gogo Inc. - President & CEO*

Hi, Jonathan, it's Michael, I'll give you some clarity there. So the increase from 850 to over 1,000 reflects the IAG announcement, which we said was 130 some. And then some additional Delta aircraft from what had already been included in the 850.

And then don't forget a whole bunch of the 2Ku backlog is for upgrades, they are not new aircraft. So, when we talk about the backlog by segment, those are only for new aircraft, not the upgrade aircraft.

Jonathan Schildkraut - *Evercore ISI - Analyst*

Great, so that is a net new.

Michael Small - *Gogo Inc. - President & CEO*

Yes, net new.

Jonathan Schildkraut - *Evercore ISI - Analyst*

Okay, great. One last question if I may. I think that from our seat, obviously we don't have the visibility into the business that you do. But certainly the conversations we are having, a lot of them revolve around business model and business model changes.

That is Gogo has built a brand in the retail market and people understand and know what that is. But it seems more and more we are hearing that there is a push towards wholesale. And I would love to understand what your perspective is on whether the market will end up retail or wholesale.

And then ultimately, and I think this is the challenge that we have given how nascent the business is on a global basis, how does that impact the way we should be modeling the Company or thinking about forward projections? Thanks.

Michael Small - *Gogo Inc. - President & CEO*

Okay, thanks, great question. And right now the vast majority of our business is the turnkey or retail model. And we see nothing changing rapidly. We do think that as bandwidth gets cheaper it is going to make a lot more options available to different airlines. And so we do think this will evolve.

We also think as our platforms, our software platforms -- so we can empower airlines to do different things -- get more sophisticated, you will also see change. But right now I see nothing imminent, I think it is going to be a pretty gradual process.



Jonathan Schildkraut - *Evercore ISI - Analyst*

All right, great. I will swing back into the queue. Much appreciated.

Operator

Phil Cusick, JPMorgan.

Phil Cusick - *JPMorgan - Analyst*

Two and a little bit as I follow up. So how should we model the satellite commitments impacting cost in the international and domestic businesses? I guess that is first.

And then second, on the business model -- following up a little bit, it seems like the debate is whether you can stream video or not long-term to customers is something people talk a lot about. How do your customers talk about that? How important is live video streaming to your big customers over the next five to 10 years? Thanks.

Michael Small - *Gogo Inc. - President & CEO*

So two issues. One is we just bought a lot more capacity at a much lower price. And did not commit any material additional dollars. So they are very little incremental fixed costs in our new capacity commitments, it is just basically bandwidth is a lot cheaper.

We want to buy enough bandwidth, so we have near-term visibility to capacity. We don't want to buy too much today so we can capture the ongoing declining cost that we would expect in satellite capacity. And then the --.

Phil Cusick - *JPMorgan - Analyst*

Well, so, Michael, on that -- so we shouldn't look for any sort of cost ramp, especially in the international business, because of these commitments? Or not a significant bump?

Michael Small - *Gogo Inc. - President & CEO*

No, not because of these -- it is highly variable. As we bring on the business we will add the bandwidth and we just bought a lot more bandwidth at a much better price. So, we are not taking a big fixed cost risk here and we will continue to buy more bandwidth as the business continues to grow.

Phil Cusick - *JPMorgan - Analyst*

Great.

Michael Small - *Gogo Inc. - President & CEO*

On streaming, yes, everybody wants to stream and we are now in the world with 2Ku where streaming is available and customers will be able to stream the way they want to stream. And I am very comfortable we will be able to meet the needs of an entire aircraft no matter how big the aircraft is.

Anybody can construct a scenario that can prove we couldn't meet that particular crazy possibility, but as we see the world unfolding and the way people want to stream on planes, Gogo will be able to provide that. And we will do it more economically than anybody else in this industry.

Phil Cusick - *JPMorgan - Analyst*

So, I guess I should follow up a little bit there. And there is a huge number of variables that could go into this. But can you give us a little bit of color on what that might cost? I mean anybody can support streaming at the right price per bit, but what do you think that costs to support streaming for customers on 2Ku over the next five years as satellite capacity goes up?

Michael Small - *Gogo Inc. - President & CEO*

Yes. So, I am not going to give a cost per bit, but we have said it fell by a factor of 3 relative to our expectations in the last year. And we already had expectations that it would be declining.

And as we sit here and see the performance we are getting from 2Ku today and then we see the benefits of the high throughput satellites, and then we see the benefits of our new modem, and those are very clearly in a roadmap.

And then we see the possibility of the low Earth orbit satellites coming on, we see in a very seamless graceful way we continue to drive the cost curve down and to be able to provide video streaming very similar to the way people experience it on the ground.

Phil Cusick - *JPMorgan - Analyst*

Okay. And then just to go back directly to my question. As you talk to your airline customers, is this part of what they say we need to have this availability, we need to make sure that we don't lock ourselves out of that in case it becomes important?

Michael Small - *Gogo Inc. - President & CEO*

Absolutely. That is exactly it. And from our discussions with, for example, IAG, they literally waited until now to make a decision to adopt in-flight connectivity in a large way because they wanted an answer that was going to work for streaming, it was going to meet the needs of the customers. And I believe they became convinced 2Ku was the answer that finally met their needs on a global basis.

Phil Cusick - *JPMorgan - Analyst*

Thanks, that helps.

Operator

John Hodulik, UBS.

Lisa Friedman - *UBS - Analyst*

Hi, it is Lisa for John. I just wanted to ask two different things. One, any update on American and when they might be making a decision?

And two, you gave a little color on this in the prepared remarks, I know that take rate in CA North America declined last quarter and ARPA actually looked like it was sort of flattish, down slightly year-over-year. I assume that is due to the inclusion of RJ space and I just wondered if you could give us color on what fraction of the base is regional jets now? Thanks.



Michael Small - Gogo Inc. - President & CEO

Okay, so, I will take the first one and we will -- Norm and I together will answer the second half of that. So we have submitted our 2Ku proposal to American and we are awaiting -- still awaiting their response, but we expect to have a long-term relationship with American however they answer on this particular deal comes out.

In fact, we just hit 1,000 aircraft installs with American airlines, (inaudible) to cross that milestone in the first quarter and we are actually upgrading very rapidly to ATG-4 with them. And with the performance of 2Ku in the marketplace, both at is it is flying on AeroMexico and is being adopted by many airlines, we think American will be look at that really, really hard.

Norman Smagley - Gogo Inc. - EVP & CFO

So, Lisa, in terms of color on the ARPA and take rate, etc., the flat ARPA reflects the reduced take rate offset by an increased [ARPS] out of the dilution in ARPA growth caused by primarily RJ's and some new mainlines of a new airline partner represents roughly 20% of the installed aircraft at the end of the first quarter.

Lisa Friedman - UBS - Analyst

Okay.

Michael Small - Gogo Inc. - President & CEO

So we have had very rapid installs over the course of last year. Mostly RJs and new airline partner and between those two it diluted it. And the base, as we pointed out in the press release, the ARPA grew about 15% if you look at same plane sales from the year ago.

Norman Smagley - Gogo Inc. - EVP & CFO

And one thing to keep in mind when you launch a new airline, it takes a while for that airline to season and mature. So it is not in any way reflective of any less quality for any particular new airline, it just takes a while for the customer base of the airline to realize it is available, ubiquitous and to take advantage of the service.

Lisa Friedman - UBS - Analyst

Which airline is this?

Michael Small - Gogo Inc. - President & CEO

We prefer not to mention the airline by name, but it is -- should be able to figure it out.

Lisa Friedman - UBS - Analyst

Okay, thank you.

Norman Smagley - Gogo Inc. - EVP & CFO

But it is true with any airline.

Michael Small - Gogo Inc. - President & CEO

Any airline, yes.

Norman Smagley - Gogo Inc. - EVP & CFO

We are just making a general statement of --.

Lisa Friedman - UBS - Analyst

Okay.

Michael Small - Gogo Inc. - President & CEO

And also what -- you have seen it with -- we saw it with the rest of the world launch too. It took a while, but by the end of about the first year the rest of the world aircraft were having ARPA, as we've had disclosed, at or above what we do in North America. So it just takes a while when you launch a brand-new airline to get up to speed.

Lisa Friedman - UBS - Analyst

Thanks.

Operator

Dick Ryan, Dougherty.

Dick Ryan - Dougherty & Company - Analyst

Norm, looking at OpEx it looks like a nice improvement from Q4 kind of going back to where it was Q3 last year. Can you talk a little bit about what drove that and how we should model that going forward for the rest of the year?

Norman Smagley - Gogo Inc. - EVP & CFO

I think it is fairly representative of what you should expect for the rest of the year. We will see modest increases in OpEx as we continue to focus on the 2Ku rollout as we build our capabilities to execute on that plan. But it should be representative of the year.

Dick Ryan - Dougherty & Company - Analyst

Okay. I think you were working on, what, 15 or so STC programs. Have any of those ticked off yet or how will that spend moderate either second half of this year as you get into 2017?

Michael Small - *Gogo Inc. - President & CEO*

We will for the next year plus, well into next year, have a very aggressive STC program. They will start topping during the course of this year, but beyond the 15 there will be more including, as the aircraft types for IAG, all the way through the A380s and the 787s and the 777s.

At this stage under contract with airlines around the globe we have every major aircraft type in works at the moment.

Dick Ryan - *Dougherty & Company - Analyst*

Okay. And it looks like you included the 50 Shareco planes in backlog. Has that moved to a definitive agreement yet? And Michael, can you comment on your licensing efforts in China?

Michael Small - *Gogo Inc. - President & CEO*

First, we can't disclose anything about the status of Shareco at this stage in the negotiations. And we will of course file any material agreements as required. But until we do we won't comment on that.

And the licensing in China, the China regulatory framework has now been pretty well established and we are seeing movement there. And we would expect over the next few months to have service in China -- in China airspace.

Dick Ryan - *Dougherty & Company - Analyst*

Okay, thank you.

Operator

Simon Flannery, Morgan Stanley.

Simon Flannery - *Morgan Stanley - Analyst*

You provide a little bit of update on the 2Ku install schedule saying you would top 75 this year. I think last year, or last quarter you said you would do around 300 planes next year, you have obviously built your backlog now.

So can you just talk us through I think some of the IAG, the bulk would be done by 2019. Help us understand the pacing of these installs and how to -- if I am British Airways do I have to go to the back of the queue or can you actually increase -- instead of doing five per week you can do 10 per week?

And what are the gating factors beyond the STCs to do that? Is there antenna issues or install crews or is it just getting those planes freed up? If you could just give us -- help us understand how we model that 1,000 planes coming into the business over the next several years. Thanks.

Michael Small - *Gogo Inc. - President & CEO*

We can hire you on our install process there, Simon, I think you named all the issues that you have to take on there to increase capacity.

Yes, as we tried to indicate in the press release, we are looking to go beyond the 75 this year and to accelerate next year. It is clear that our backlog is growing and we need a higher production rate.

The STCs are what gets you to the starting line, but once you are to the starting line you need to make sure the supply chain is there for all the various components. We are working that. The installation crews is perhaps the least of the challenges but we are getting that capacity in place too.

And then aircraft availability is a challenge for the airlines and you have to bring all three together. Our ability to be highly predictable to the airline, so when they make a plane available we do it in the time allotted on the specific dates predetermined is very important to the airline.

So, Gogo is investing heavily in this and we think our aircraft operations, our ability to engineer, certify, install and maintain aircraft is a unique capability. And we don't think anybody else in the history can install, particularly in a retrofit basis, the way we can.

Simon Flannery - Morgan Stanley - Analyst

Okay, so, I think you said before that the 2Ku would really ramp through the year. So is it more of a get through the heavy summer period and then as we enter the fall that is when you will really start cranking on the 2Ku installs?

Michael Small - Gogo Inc. - President & CEO

That is very fair. So there is to gating items to really get before the fall, one is the heavy flying season as just mentioned. The aircraft aren't easily available, particularly the international aircraft, it gets very difficult. And then we have got to get the STCs out of the way. So we expect both those things to be cleared. So September timeframe is when the good times roll.

Simon Flannery - Morgan Stanley - Analyst

Okay and just a quick follow up on air to ground on the business aviation, that was down a little bit. Is this a better -- a good run rate for the rest of the year or were there any particular factors why it was off a little bit?

Michael Small - Gogo Inc. - President & CEO

Their primary -- there is weakness industry wide a little bit in the aftermarket and Business Aviation, but no major factors competitively. We still are extraordinarily strong in that market and we feel very good against our guidance in the BA side.

And I would point out the service -- we are still adding enough -- there it's almost the opposite of commercial aviation. Business Aviation, while there is good plane growth, the ARPA growth has been extraordinary and ended up with a 41% service revenue growth for the second quarter in a row.

Simon Flannery - Morgan Stanley - Analyst

Great, thanks, Michael.

Operator

James Breen, William Blair.

James Breen - *William Blair - Analyst*

Just one on the competitive front. I think there was somewhat of a broad expectation that Panasonic would be the winner in the BA deal and clearly wasn't. Can you just give us some thoughts on what you are seeing competitively outside the US? And have the players changed at all and do you think you've sort of distanced yourself from some of the other competition? Thanks.

Michael Small - *Gogo Inc. - President & CEO*

Thanks. Well, we were thrilled with the IAG win and along with Virgin Atlantic we now have a very strong foothold in Europe. We are seeing increasing activity all around the world and we are now operating on four continents and airline engagement and the depth of discussions is increasing.

And we are liking our win rate. And as 2Ku becomes more real, as our aircraft operations capabilities become more evident and the sophistication of our service platforms become more apparent, we think we are going to continue to do very well to continue to ring up wins.

James Breen - *William Blair - Analyst*

And just in general when you look at the fleets that you have won with them and some of the larger planes and some of the long-haul routes, what are your thoughts on the potential revenue from those relative to your base now?

It seems as though it would start to skew the revenue per plane upward given the distance of the flights, even assuming penetration gets a little bit better from here as well.

Michael Small - *Gogo Inc. - President & CEO*

Those could be factors that are helpful. But I think the single biggest factor that is helpful is all the planes being installed now are with 2Ku with incredibly more bandwidth and bandwidth equals revenue. When you have a lot more of it you have more revenue. And so, I am optimistic on that front.

I am also very optimistic that the air, the connected aircraft the more broadly [auto] connected aircraft, not just the connected passenger, is upon us. And we just published our book about that, it is available of any of you would like a copy.

But there is going to be lots of other revenue sources beyond just the passenger. So, lots of bandwidth, increasing revenue sources. Those planes should do well and the rest of our base should do well too.

James Breen - *William Blair - Analyst*

And I guess just lastly, as you talk to the airlines and you sort of think about and sort of partner with them on monetizing the new services you are putting in -- is there a concept there that first-class passengers start to see free Wi-Fi similar to hotel loyalty programs and so forth? Where you would see some immediate revenue from the airlines for those types of passengers and then the rest of it would be pay as you go?

Michael Small - *Gogo Inc. - President & CEO*

Yes, I think that is exactly right. In fact, Japan Airlines, they just launched a 15-minute free program on a lot of their planes where the airline pays for it. So, I do think business models will evolve in this industry, I think it happens more gradually with programs like you described for high-value customers or for occasional sponsorships.



But some of the burden will be moving away from the passenger to other payers. And at the same time the cost of the bandwidth is coming down and the amount of bandwidth available is going up. So, all those things are going to be very good for revenue in this business.

James Breen - *William Blair - Analyst*

Great, thank you.

Operator

Andrew De Gasperi, Macquarie Capital.

Andrew De Gasperi - *Macquarie Securities - Analyst*

First question, I saw an article in the press that Gogo was considering EXIM financing for international airlines. I was wondering, could you give us maybe some more comment on that and how would you structure it? And secondly, are you concerned at all about the ARPA trajectory considering the competition out there? Thanks.

Michael Small - *Gogo Inc. - President & CEO*

I will let Norm take the EXIM, but the relationship is between the airline and EXIM and not us.

Norman Smagley - *Gogo Inc. - EVP & CFO*

Yes, that is right. So, we basically facilitate the work between the airline and EXIM Bank, we are not actually directly involved in the transaction. So, it doesn't really affect us at all and it makes it easier for -- gives another source of financing for the airline, so something that is always a benefit to them.

Michael Small - *Gogo Inc. - President & CEO*

And on the ARPA trajectory, no, I am extraordinarily optimistic about the ARPA trajectory. Bringing more bandwidth is going to ignite ARPAs. As Norm mentioned in the script, as 2Ku bandwidth folds in here the international planes will have it from day one.

But the US planes, some percentage of those will get them but then the rest of the planes on the air to ground network are now on a less congested network because we offloaded. So that is going to be very helpful.

And we are seeing tremendous ARPA growth in Business Aviation where the bandwidth is plenty for those size aircraft. And we are seeing 15% ARPA growth on the planes that have been in the network for a while. The flat year-over-year comparison is due to the dilution of the new aircraft. So the underlying trend is good and the addition of more bandwidth is going to make it great.

Andrew De Gasperi - *Macquarie Securities - Analyst*

Great, thank you.



Operator

Andrew Spinola, Wells Fargo.

Andrew Spinola - Wells Fargo Securities - Analyst

Michael, I wanted to ask you about a comment you made earlier where you said that the satellite contracts don't have a big fixed cost component and are highly variable.

I was just wondering, are these structured like typical take or pays where you are committing a certain amount and it ramps over the next few years or is it even more variable than that?

Michael Small - Gogo Inc. - President & CEO

No, you described the structure of the contracts, they are take or pay. The reason I say it is variable in practice is we haven't committed to a much higher run rate of expense than we incurred today. And as we need more we can just dump contract for it as the business grows.

Ultimately the business judgment is how much to buy and when. You don't want to be cut short in at the near term on capacity -- you have to make sure it is available. But in the long run this is a declining cost business.

Satellite capacity ultimately is a commodity with this and it is going through a period of technological renaissance. And a lot of innovation is happening. So, we fully expect capacity cheaper in the future because the technology gets better. And so, we want to buy it over time with just a reasonable amount of safety stock for the near-term needs.

Andrew Spinola - Wells Fargo Securities - Analyst

Makes sense.

Michael Small - Gogo Inc. - President & CEO

And one transponder or one -- once the business gets to scale, once you have global coverage you can actually buy in relatively small increments. The big fixed cost is getting started, getting global coverage before you have the first plane flying. But after that it is really quite a variable expense for us.

Andrew Spinola - Wells Fargo Securities - Analyst

I think on the previous call or in other presentations you talked about maybe giving -- outlining your future roadmap for the ATG network and relatively soon. I am just wondering if there is any update on that or any changes in your thinking.

Michael Small - Gogo Inc. - President & CEO

Yes, there are some changes in our thinking driven by two factors. One is the performance of 2Ku has been better than anticipated, the costs have been lower.

So, 2Ku is going to take more of the burden and there will be a smaller role for air to ground. But a very important role, that will be for the smaller aircraft, Business Aviation and the regional jets. So first factor 2Ku doing really well.

Second factor is there has been a delay in 14G and it is still uncertain whether it will happen. So, we have been exploring alternatives and we are going to get -- we are very close to bringing to market those alternatives or explaining to the market what those alternatives are.

And I think these alternatives will be lower cost in 14G and can be implemented in a more graceful way over time, so not only lower expense but not all at once. So we are getting close to making that disclosure on what our next-gen solution is.

Andrew Spinola - Wells Fargo Securities - Analyst

Got it. Thank you very much.

Operator

Jonathan Schildkraut, Evercore ISI.

Unidentified Participant

Hi, this is Rob. In the context of bandwidth costs and competing directly with satellite providers, could you discuss the difference between ownership economics and the ability to negotiate with various providers against each other, and the economics of shared infrastructure?

Michael Small - Gogo Inc. - President & CEO

Ownership economics are terrible (laughter). You have got to make a huge investment at a point in time and pray it lasts for 15 to 20 years as a superior alternative. We prefer to have an open solution. We put the most efficient antenna on the plane and then watch the satellite innovation happen. And as each generation comes along, we take advantage of the lower and lower costs.

I would also point out that a high percentage of the cost structure in this business is in the aircraft operations and the platform services. So you can have a satellite, but you've still got to do those other two functions. So you need a really, really good margin on your bits if you own the satellite if you are going to support the other things that take some of this business.

So, I am a big believer and I am quite confident we have chosen the right path in our open architecture and taking advantage of all the satellite opportunities out there -- not just at the moment where you have negotiating power if you can take advantage of a lot of choices, but over time so you capture the innovation.

Jonathan Schildkraut - Evercore ISI - Analyst

Great, thank you.

Operator

Phil Cusick, JPMorgan.

Phil Cusick - JPMorgan - Analyst

Sort of under the same category, how do you think about the per bit difference between LEO and GEO and how does it change your model?



Michael Small - Gogo Inc. - President & CEO

So, LEO advantage is per bit to some degree, but it is also lower latency. It is less than 1,000 kilometers or 600 miles versus 22,000-plus miles above the earth for GEO. So you've essentially taken the distant latency to zero there by comparison and that is going to be the real advantage of LEO.

The second advantage of LEO is because it is closer antenna size can get smaller, you don't need a big antenna because the satellite is closer.

So -- and then I would say the cost per bit potentially can be lower. Ultimately that will be determined by what each of those satellites cost. I think there is a lot of room in the current objective of what that industry is striving for so they can even miss their objectives and still have a bit advantage.

A final advantage is -- of LEOs is they tend to congregate towards the poles. They actually have the strongest coverage in the polar regions. Our assumption is, at least initially, we are going to use both GEO and LEO when they get it.

When LEOs first arrive you don't switch very often between the two networks, but you would at times switch between the two networks. And once again, I know I'm sounding like a broken record, but that is the advantage of our open architecture and the 2Ku antenna.

And as we sit here today we are doing engineering work to make sure it can gracefully work across both a GEO and LEO Constellation.

Phil Cusick - JPMorgan - Analyst

Okay. And under the header of what have you done for me lately, the IAG announcement -- that is great, but how should we think about your RFP pipeline today?

Michael Small - Gogo Inc. - President & CEO

So, as I think I just mentioned, it is active out there, the airlines now know they have to get into this game and we are operational on all the continents where there is real activity. And so, I expect continued announcements this year and I do think a very high percentage of the world's leading airlines make decisions over the next couple years.

Phil Cusick - JPMorgan - Analyst

And how should we think about your cash and liquidity given the additional announcements?

Norman Smagley - Gogo Inc. - EVP & CFO

So, Phil, we have over \$300 million of cash on the balance sheet, so obviously no immediate need for cash. We have seen, as we have talked about on the call, a big increase in demand for 2Ku and we've talked about our goal to accelerate deployment.

So, to run those plans through and to truly accelerate and adopt the increased demand for the 2Ku system, at some point we will need some additional capital.

But the key thing to remember is as we invest in 2Ku deployment every dollar goes into that generates a very high return for us creating a lot of shareholder value. So the faster and broader deployment that we can do, it's really good thing for us.

Michael Small - Gogo Inc. - President & CEO

So the bottom line, it is apparent there's a lot of business out there for us to go get.

Phil Cusick - *JPMorgan - Analyst*

Do have capacity at the debt side or you think you would have to raise equity to do that?

Norman Smagley - *Gogo Inc. - EVP & CFO*

We think we can tap all the markets that are open, debt and equity.

Phil Cusick - *JPMorgan - Analyst*

Got it, thanks, guys.

Operator

Carter Mansbach, Jupiter Wealth Strategies.

Carter Mansbach - *Jupiter Wealth Strategies - Analyst*

Good morning, gentlemen, congrats on another solid quarter and really great work on IAG and Delta Ku orders. So my question is more not about numbers but more about sentiment.

So Ku is clearly the next best thing, but over the last few years as the Internet has become cumbersome, Gogo's legacy product has become sluggish. And clearly there is a negative connotation around Gogo as a product.

So, my question is this -- how will Gogo go about changing the sentiment? Will you guys do a marketing campaign or will you allow the airlines to take over the word Wi-Fi on their planes and take the focus away from the Gogo name?

Michael Small - *Gogo Inc. - President & CEO*

So, at this stage -- well, some of what you described, Carter, at the end is the airlines are branding more and more the connectivity on the plane and we are supporting it and I think the world understands that it is powered by Gogo.

But in today's world your product is your brands. And at the end of the day, until we make it faster and meet the needs of the customer, both the airline and their passengers, we are going to have the reputation we currently have in the marketplace, which I think you reasonably described.

2Ku is important, we get it out there, we are bringing more bandwidth, we will bring the best solution to the marketplace so there will be no better choice than the Gogo solution. And the gap between Gogo and the ground will essentially be gone with 2Ku. We will replicate a ground-like experience in the sky and that is what we need to do to make people love Gogo again.

Carter Mansbach - *Jupiter Wealth Strategies - Analyst*

Sure. So as that rolls out do you see yourself doing any type of branding campaign like this is not your daddy's Gogo or something like that?



Michael Small - *Gogo Inc. - President & CEO*

I don't think you need to spend -- there is only one way you do it is to make it real in the marketplace and deliver the bandwidth people want. And then our customers will Tweet, Facebook and let the world know. That is literally how the world works these days. And to (multiple speakers) --

Carter Mansbach - *Jupiter Wealth Strategies - Analyst*

You have got it.

Michael Small - *Gogo Inc. - President & CEO*

-- to tell them it's good when they don't think so doesn't help.

Carter Mansbach - *Jupiter Wealth Strategies - Analyst*

Fair enough. Hey, listen, congrats on a great quarter. I look forward to speaking to you in the future.

Operator

Andrew Spinola, Wells Fargo.

Andrew Spinola - *Wells Fargo Securities - Analyst*

Michael, I wanted to follow up on a comment you made about one of the benefits of excess supply is that you are able to get good pricing, but that the owner's economics right now are terrible for the satellite companies.

One of your major providers is in pretty difficult financial shape and has already cut back on some of their investments. Your other provider is primarily a video service provider. And I think as they see the economics on these [HTS] investments they may not decide to continue to invest.

And on the flipside, the KA band guys are clearly investing and if not accelerating. And I'm wondering if you've put any investments into developing a KA band antenna or a dual band antenna to protect yourself from any potential pullbacks from the Ku providers in the HTS space?

Michael Small - *Gogo Inc. - President & CEO*

Yes, first, we have a lot of confidence and the Ku ecosystem and in fact it is a far larger ecosystem and expect continued investment there. And the satellites will continue to operate independent of any balance sheet issues out there in the industry.

But to the second point your comment, at the end of the day Gogo is just looking to get the best service to the planes in the sky, the lowest cost bit, the highest-quality, most reliable bits to the plane. And we will do whatever it takes and go wherever that leads us.

Today we don't see a real benefit in spending a lot of money against a KA solution. But if it turns out, for whatever reason, that ecosystem gets going and has true global coverage and the redundancy and all the things we are looking for, then we will adopt KA.

I don't see that as imminent, but it is something we will do. And Gogo has gone from air to ground to satellite and back again. We take care of airlines and we find the best capacity wherever it may be at any point in time.



Andrew Spinola - Wells Fargo Securities - Analyst

I appreciate the color, thanks.

Operator

Thank you. And that was our final question. I would now like to turn the call back to Michael Small for any further remarks.

Michael Small - Gogo Inc. - President & CEO

Okay, well thank you, everyone. The era of 2Ku is off and running and we couldn't be happier with the way it is going. So thank you all for your time today and we look forward to talking to you in the near future.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes today's program. You may all disconnect. Everyone have a great day.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2016, Thomson Reuters. All Rights Reserved.