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Q1 2019 Gogo Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen and welcome to the First Quarter 2019 Gogo Incorporated Earnings Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. (Operator Instructions) As a reminder, today's conference may be recorded.

I would now like to introduce your host for today's conference, Mr. Will Davis, Vice President, Investor Relations. Sir, you may begin.

William G. Davis ***Gogo Inc. - VP of IR***

Thank you and good morning everyone. Welcome to Gogo's first quarter 2019 earnings conference call. Joining me today to talk about our results are Oakleigh Thorne, President and CEO and Barry Rowan, 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 may make forward-looking statements regarding future events and the 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 press release filed this morning and are more fully detailed under the caption Risk Factors in our Annual Report on Form 10-K and 10-Q and other documents we have filed with the SEC. In addition, please note that the date of this conference call is May 9, 2019. Any forward-looking statements that we 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. We included a reconciliation and explanation of adjustments and other considerations of our non-GAAP measures to the most comparable GAAP measures in our first quarter earnings press release. This call is being broadcast on the Internet and available on the Investor Relations section of Gogo's Website at ir.gogoair.com. The earnings press release is also available on the Website. After managements' comments we will host a Q&A session with the financial community only.

It is now my great pleasure to turn the call over to Oakleigh.

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

Thanks Will. Good morning and welcome to our Q1 2019 earnings call. A year ago I hosted my first Gogo earnings call, took the job of CEO of the same reason I first invested in this company, a core belief in the value of delivering insight, connectivity solutions and a belief that one can build a solid and profitable business delivering those solutions. Our business proposition is simple; we grow as the usage of in-flight connectivity grows. At this point, I don't think there's much argument about the fact that airborne bandwidth consumption is growing and will continue to grow.

Today's consumers want to connect from their home to the runway to 35,000 feet in the air. The usage is increasing across all our business segments and we expect take rates to continue to grow as in-flight connectivity is no longer a nice to have, but is a must have. Passengers expect it, the aircraft operators want it and airlines and aircraft owners are committed to providing it.

What's even more exciting, Gogo has significant runway ahead of it as both of our markets are largely un-penetrated. Business aviation is roughly 5% penetrated in North America and only 15% penetrated globally. In commercial aviation, we're fairly well penetrated in North America is only about 35% penetrated on a global basis.

So let me do a little retrospective. Last year, there were a lot of questions about whether our vision for Gogo was achievable. I think our Q1 results, which represents our fourth strong quarter in a row, demonstrate that we're making great progress towards answering those questions. This past winter, we flew 22,000 deicing flights to the United States without one incident of degraded system availability due to the deicing fluid. We closed $925 million, we recently closed, $925 million of debt issuances to defer the bulk of our maturities until 2024 and lowered the interest rate in our senior secured notes while creating no dilution for shareholders.

Whether the deinstallation of almost 550 of our old ATG aircraft at one of our largest customers and still managed to grow service revenue while signing up substantially all of our other ATG mainline fleets to upgrade to 2Ku. We've improved profitability in the value we provide to customers; whether it's turnkey or airline directed model. Gogo can and will thrive under either as they both can be cash flow positive for Gogo. We've improved quality, as demonstrated by our 97% system availability in the quarter versus 88% in Q1 a year ago. We've achieved significant cost savings and expect close to $50 million in IBP-related costs reductions this year. And, we dramatically reduced our free cash flow burden with a $75 million improvement this quarter versus Q1 2018 and are now guiding to at least a $100 million improvement for the year.

Driving these results has not been easy and I want to thank and acknowledge the entire Gogo team for our collective efforts. With our significantly strengthened position and solid trajectory, we're ready to go on the offensive and take advantage of the compelling growth and market opportunities in front of us. Now, let me turn to the quarter.

Q1 delivered record adjusted EBITDA; very strong improvement in free cash flow and strong revenue -- and strong growth in our underlying service revenue. Though we had a few one-off benefits that added roughly $11 million to adjusted EBITDA, even when you add those back, adjusted EBITDA would have hit record levels. I want to caution that we expect Q2 to be down significantly but if one backed out the one-time benefits from Q1 and adds them to our Q2 expectations, the two quarters would look fairly similar and both would be record adjusted EBITDA quarters.

We expect Q2 adjusted EBITDA to be our trough for the year as the deinstalls are completed, we expect adjusted EBITDA to pick up from there in the second half. CA service revenue grew a healthy 12%, however, equipment revenue -- sorry, BA service revenue grew a healthy 12%, however, equipment revenue lagged due largely to installation capacity constraints caused by FAA, ADS-B mandates which I'll discuss in a moment. In the combined CA segments, we have service revenue growth despite the deinstalls, partly due to the one-time revenue I noted a moment ago but also because of a nice jump in take rates. That strong underlying service revenue growth, coupled with good cost controls and better than anticipated satcom utilization drove a significant increase in profitability.

On our last call, I set out six objectives for the year and I think we made good progress in all six in the quarter. The first was to make steady progress towards turning free cash flow positive in our CA division and we made great progress achieving our first adjusted EBITDA positive quarter for the combined CA segments. We're not forecasting that we'll stay positive for all quarters going forward but at least it's progress in the right direction. Second, was to invest in our BA business to protect our existing customer base and attack new segments. We're making good progress in our plans to achieve these objectives, that objective, and we'll have more to say on that in future quarters. The third was to strengthen our balance sheet. The enthusiastic response to our notes offering allowed us to extend maturities and lower the interest rate on the bulk of our debt without any dilution to shareholders. This validates our decision last November to not refinance our full $362 million convertible bond. At the time, we said that we would deliver improved results that would allow us to refinance without further dilution and we delivered on those promises. We also strengthened our balance ahead of our Gogo 2020+ plan and ahead of our own expectations.

The fourth objective was to invest in our people and improve our -- which we're trying to do with enhanced equity awards, better bonus plans and by presenting a clear and compelling vision for our future. Fifth was to continue maturing our business processes while maintaining our creative problem solving culture. Towards that end, we've been rolling out a number of management processes that were called for as part of our IBP plan announced last July. And sixth, we wanted to get out from under our shell and start to tell our story to the media and The Street and we've begun that by committing to several investor conferences, including three in the next month.

I'm also particularly pleased with our cost control in the quarter where we managed satellite costs well and our IBP cost savings came through in every line of the income statement. As a result of our performance in Q1, we're raising our adjusted EBITDA guidance and tilting our cash flow improvement target in a positive direction. Now let me touch on strategy for a moment. From a strategic perspective, we see some recent advance in trends that reaffirm our asset-like technology agnostic product strategy. First, is the unfortunate Intelsat 29E instance. While we're sorry this happened to our friends at Intelsat, we think this affirms our model in two important ways. First, because 29E was in the Ku constellation -- to other Intel satellites, Intelsat has been able to -- through restoration agreements to satellites belonging to their competitors. We were not on 29E, but had we been, we would have been able to recover quickly.

Second, it highlights the risks airlines run if they rely on a closed Ka constellation of three or four satellites and are meant to cover the entire globe. If one of those satellites is knocked out, that airline could go dark for a substantial portion of the globe until their provider managed to launch another satellite. Given the huge increase in space debris and the risk that poses, it's relying on three or four satellites for global coverage, is like playing Russian roulette with your passengers connectivity needs.

Today, Gogo partners with 12 satellite providers and utilizes 30 satellites and most of our providers can move our usage to another satellite within hours or weeks at most if they were to suffer the same issue Intelsat just experienced. Another strategic trend we think reinforces our asset life strategy is around the development of smaller, more versatile satellites with dynamic beam-forming technology. Today, when we lease capacity, we lease it 24x7. So, we only use it when planes are flying underneath it. This architecture suffers low capacity utilization and is not particularly conducive to the extreme mobility of the aero market where demand moves around the planet at all hours of the day. We're working with our satellite partners on dynamic beam-forming technologies that are far better [tuned] to extreme mobility. That will give us the ability to aim beams where we need them, when we need them, thereby dramatically improving capacity utilization and lower per megabit costs in the future.

Due to our open architecture, we'll be able to take advantage of these and future technology advances much more quickly than our competitors with closed systems. We must build and launch new satellites to achieve the same performance. Another strategic tailwind is the increased interest by airlines in going free. Today we have two airlines very successfully offering free service; Virgin Australia and Japan Airlines. While Virgin Australia is a relatively new development, JAL has offered free for the last three years on its domestic flights and in that time it's moved several points of market share away from its rival, ANA. We believe an increase in the number of airlines going free could meaningfully increase demand and drive substantial growth for Gogo. Given our open architecture, we're well positioned to ramp up capacity as airlines need it and some of the -- that I just described a moment ago, were well positioned to serve the dramatic increase in demand we believe free will drive in the future.

So, we operate in the compelling and dynamic industry with -- technology is shifting airline directive and turnkey models. We believe that Gogo's industry leading and open technology allows us the flexibility to work with our carrier partners in anyway they wish; whether it's free, airline directed or turnkey. And we expect that capability to enable Gogo to remain a market leader into the future.

Now let me dive into each segment for the quarter starting with BA. BA set records for service revenue, ATG aircraft online and ARPU for the quarter. Equipment revenue was not as strong as in the prior year; we shipped 187 ATG units down from 250 to Q1 2018 but we anticipate a rebound in shipments by year-end. The shipments are down for a few reasons. First off; Q1 2018 was unusually strong as pent-up demand for our AVANCE platform was unleashed when we launched the product. Second, this year we underestimated the impact of the FAA's ADS-B mandate in the aftermarkets. ADS-B stands or automatic dependent surveillance broadcast and it's been an initiative to improve traffic safety by the FAA for the past decade. It requires aircraft owners to install ADS-B equipment by the end of this year.

Apparently more owners than we thought procrastinated and the [MRO]'s and dealers are now packed with planes trying to complete the install by year-end. These installs are both crowding out budgets for IFC but also literally crowding out shop floor space as dealers are booked with ADS-B installs. The second issue has to do with timing and mix of the OEM's. A few OEM's have been a little slow moving from our classic ATG product and cutting in our AVANCE platform. So though units are about right, right now we're selling more lower priced classic systems than AVANCE systems for new aircraft.

We have line-fit already for AVANCE at five OEM's and our OEM channel team feels that the cut-ins will be complete at the other four by the end of the year. On the activation front, we're up to 543 L5 customers and 187 L3 customers who are activated and billing with 35% of those customers purchasing streaming plans. A nice synergy between our divisions is our success selling Gogo Vision to AVANCE customers. Vision was originally developed by CA but we've been offering all AVANCE customers a 90-day free trial, and 50% of them have purchased the product. And because of the AVANCE platform software defined architecture, we're able to turn on the IFE product over the air without ever even touching the aircraft. Generally, we're feeling very good about our BA business and are particularly excited by some of the plans we're developing for our NextGen network which we hope to be able to share shortly.

Now let me turn to the commercial aviation division which we'll report in two segments; CA North America, CA rest of world. Overall, we saw a hundred incremental 2Ku aircraft added online for the quarter. The majority of which were new aircraft producing a total 2Ku aircraft count of more than 1100 and a backlog of approximately 900 aircraft.

On the line fit front, before I start discussing the 737 MAX, I'd like to start by saying that our hearts go out to the families who lost relatives on Ethiopian Air 302 and Lion Air Flight 610. That said, at Boeing for the 737 MAX, we're now [offerable] for service bulletin installation. We're working through line-fit qualification testing and we have customers signed up for line-fit delivery. At Airbus, we're line-fit on the 1820 and are still on track to install our first A320's and A330 family line-fit aircraft in 2020.

We had three new airline model inductions for the quarter. The Virgin Australia A330-200 and British Airways C 787-900 and the GOL B737-800 MAX. Now, let me turn to North -- to the North American segment where we saw modest service revenue growth on the surface, but 12% service revenue growth if you exclude the headwind of the deinstalls and exclude the benefit of the software product revenue I discussed earlier.

We expect the previously discussed competitive deinstall program to wind down this quarter as the last 28 ATG aircraft are replaced with a competitor satellite system. The financial effects of that will create a remaining headwind for CA service revenue comparisons through Q2 next year.

We saw one airline flip back to the turnkey model in the quarter from the airline directive model and we expect the second flip as well. These flips will hurt equipment revenue this year but help adjusted EBITDA in the future. CA -- now I'll turn to CA rest of world; our growth engine. We had strong revenue growth in rest of world with service revenue up 39% from a year ago and equipment revenue up 167% from a year ago. The equipment revenue jump is powered by the large number of installations we're making in new airline fleets. ARPA for ROW declined as a result of these new fleets because airlines are reluctant to begin marketing IFC until a substantial portion of the fleet is installed. This point is illustrated by the fact that in the first quarter, 2018, 17% of the equivalent aircraft online in ROW or in new fleets. In the first quarter this year, 45% were in new fleets. And by year-end, we expect that to grow to 55% being in new fleets. That backlog of new fleet installations creates a tremendous opportunity for growth as we look ahead to 2020 and we're starting to see some [green shoots] from that now.

Gross ARPA for new fleets in Q1 was $73,000 for new fleets; up 28% from $57,000 in Q1 last year. So in summary, we feel like we've gotten off to a really good start this year and are ready to take advantage of the opportunities in front of us. And with that, I'll turn it over to Barry.

Barry L. Rowan ***Gogo Inc. - CFO & Executive VP***

Thanks Oak, and good morning everyone. Before reviewing our detailed operating results, I'd like to summarize our key financial accomplishments for the quarter. We've now completely refinanced our balance sheet; strong operational execution is driving significantly improved financial results including underlying service revenue growth and cost structure reductions. And our focus on aggressively managing working capital is releasing cash to the balance sheet as planned. Our outlook for the year continues to strengthen; prompting us to raise adjusted EBITDA guidance and adding greater conviction to achieving at least $100 million improvement in free cash flow over 2018.

I'll now review each of these achievements in greater detail. Late last year we embarked on a two step process to refinance our balance sheet beginning with refinancing $200 million of our convertible notes. As Oak described, Gogo's improving performance and great support from our debt investors enabled us to successfully complete the senior secured notes financing we recently announced. After initially closing on $905 million, we have the opportunity to place an additional $20 million priced above par with no consent fee, bringing the total amount of the senior secured notes to $925 million.

We've also launched the tender offer for the $162 million in convertible notes due in March 2020. These financings achieve several key objectives for the company. First, we extended the maturities on our debt. The previous, earliest due date was March 2020; excluding the 2020 convertible notes, which are the subject of the tender offer, 80% of our debt is now due in 2024. The recently issued 6% convertible notes are due in May of 2022 with the conversion price of $6.00 per share.

While we have the option to extend the maturity of the senior secured notes even further, we opted for a five-year term as the two year non-call period puts us in a position to continue refinancing our balance sheet on better terms based on the accelerating financial performance we are projecting.

It's worth noting that both the recently issued senior secured notes and the 6% convertible notes have been trading above par since closing the transaction. The second key objective we achieved through these financings was that we reduced the interest rate on our senior secured debt from 12.5% to [9.78%]. Third, we retained the flexibility to redeem a portion of our senior secured notes with proceeds of up to $150 million in strategic investments at a price of $103 anytime within the next 12 months. Finally, we have provided for an additional liquidity buffer with an initial $30 million revolving line of credit facility and a provision to double this amount over time based on meeting certain financial ratios.

With these financings now completed, and based on our current plans and projected cash flow trajectory, we do not anticipate requiring additional capital except as needed to refinance our debt maturing in 2022 and 2024. The strong operational execution Oak described is driving significantly improved financial results. Our 2Ku aircraft are performing well and the cost savings we targeted by the end of 2020 through our integrated business planning process are running ahead of plan.

We're also seeing the benefit from our focus on cash management. Our cash position of $189 million at the end of the first quarter was well ahead of the plan we put in place last fall. During the first quarter, we achieved a $75 million improvement in free cash flow over the prior year. Approximately 40% of this improvement was driven by higher adjusted EBITDA and another 40% from lower airborne equipment spend with the balance coming from improvements in networking capital.

Unlevered free cash flow has also improved substantially. The positive $11 million this quarter represents a significant turnaround from a negative $60 million in the year ago quarter. These achievements add to our confidence in achieving at least $100 million improvement of free cash flow for 2019 versus 2018.

I'll now turn to our first quarter operating results beginning at the consolidated level. Total quarterly revenue of $200 million was at the high end of the preliminary estimated range of $197 million to $200 million. As expected, total revenue declined. The primary reason for this decline is the comparison against the $45 million of equipment revenue recorded in the first quarter of 2018; resulting from one of our airline partners switching to the airline directed model which occurred in conjunction with the implementation of accounting standard 606.

Excluding this impact, total revenue would have increased 7% from the prior year. Importantly, consolidated service revenue increased 9.5% year-over-year. Adjusted EBITDA of $38 million was at the high end of our preannounced range of $35 million to $38 million and meaningfully exceeded both internal and external expectations.

As we noted in our prerelease on April 15, adjusted EBITDA benefited from $7 million in software product development revenue from one of our airline partners, stronger underlying CA service revenue, lower satcom costs and $4 million in delayed operating expenses which we now expect to incur in the second quarter. Even excluding the benefit of the software product development revenue and the delayed opex spending, adjusted EBITDA of $27 million represents Gogo's highest adjusted EBITDA on record. Regarding the quarterly profile of 2019 adjusted EBITDA, we suggest looking at this on a combined basis for the first and second quarters as Oak outlined.

Now let's move to a discussion of the business segments starting with business aviation. After an exceptionally strong 2018, in which BA total revenue grew 21% and segment profit increased 41%, BA results moderated as expected in the first quarter for the reasons Oak explained. Total BA revenue grew about 2.5% from the prior year to $70.5 million and delivered yet another outstanding quarter of bottom line performance. Segment profit margin of 47%. On a year-over-year basis, service revenue grew nearly 12%, all equipment revenue declined about 18% or $3.8 million as last year's results included the final recognition of revenue related to our sign and fly program.

We expect total BA equipment revenue to decline in 2019 versus 2018 as last years 34% growth rate also reflected the highly successful launch of the AVANCE L5 and L3 products. We do expect quarterly BA equipment revenue to be higher than this quarters $17 million level in each of the remaining quarters of the year.

Total ATG aircraft online grew over 11% in the first quarter reaching 5348 and ARPU grew about 1% year-over-year. We expect ARPU growth to trend higher through the year with improving product mix. We continue to believe that total BA revenue will grow in the general range of 10% per year for the next several years. During 2019, we expect this increase to be largely driven by growth in recurring service revenue as we realize the benefit of the significant number of AVANCE systems installed in 2018. We also expect growth in BA segment profit in 2019, however, the growth rate will slow meaningfully from 2018's record 41% growth which reflected significant operating leverage achieved during the year. We continue to expect the BA segment profit margin to be in the mid-40% range this year with significant free cash flow generation.

Now I'll turn to a discussion of our commercial aviation division. Our combined commercial aviation business segments saw improving results largely attributable to strong underling service revenue from an overall increase in passenger usage and the impact of the cost savings initiatives we've put in place. It's worth noting that the CA results are impacted by two primary factors affecting the comparability of CA's results. First, is the impact of the deinstalling airline. This airline switched to the airline directed model during the first quarter of 2018 resulting in the $45 million of equipment revenue I mentioned which was recorded in the first quarter of 2018 that affects year-over-year comparability. In addition, the ATG aircraft deinstallations and changes in business terms are meaningfully impacting our financial performance this year. The second factor affecting the comparability of the results for CA is the switchback to the turnkey model from the airline directed model by other airlines. One airline has already flipped back to the turnkey model this year and another is expected to do the same by the end of the year.

As we have noted previously, an airline switching back to the turnkey model results in a decrease in equipment revenue but is otherwise cash flow neutral to us. CA first quarter total revenue was $96 million, representing a year-over-year decline from the $144 million level a year ago. This reflects the impact of the deinstalls we have discussed. In addition, this comparison is against the $45 million in equipment revenue reported in the first quarter of 2018 I've also described. Importantly, CA-NA service revenue increased 4% to $92 million from the prior year.

Excluding the impact of the deinstalling airline, CA-NA service revenue increased 22%. Service revenue increased 12% if you exclude the $6.8 million impact from the software product development revenue I mentioned previously. We expect total CA-NA service revenue to reach a flat bottom in the second quarter of this year as the deinstallations are completed and we expect it to resume growing next year after we get beyond the negative comps from the deinstalling airline. CA-NA net ARPA for the quarter was $126,000, up 23% from the prior year.

Excluding the impact of the software product development revenue, net ARPA was $115,000 and grew 12% from a year ago. Take rates for the quarter reached an all time high at 13.9%, up 32% from the prior year. This drove the strong service revenue growth as average revenue per session was just 12% lower versus the year-ago period. This in encouraging data as it speaks to the underlying fundamentals of the business and reflects the positive effect of the increased capacity of 2Ku as well as the benefit of third-party revenue. As a result of the service revenue growth, and the impact of our cost controls, CA segment profit grew by $21 million versus the prior year to an all-time high of $23.5 million.

Our cost initiatives drove a 29% reduction in total CA functional spend excluding depreciation this quarter versus the prior year period as these programs are tracking ahead of plan. Looking at the quarterly profile of adjusted EBITDA for 2019, we expect most of the reduction from the first to the second quarter to come from a our CA-NA division as this segment was the primary beneficiary of the benefits affecting this quarter which we've described.

Now let's discuss our commercial aviation rest-of-world segment. CA-ROW total revenue of $33 million was up 72% from the prior year reflecting revenue from the addition of 52 net incremental 2Ku aircraft. Service revenue grew 39% from the prior year. Take rates grew 12% over the prior year to 13.6% from 12.2% and this is in -- despite the anticipated natural APRA dilution from the substantial increase in the number of aircraft undo fleets versus a year ago as Oak described.

The high quality global airlines we have won in recent years, should drive higher take rates and ARPA as they are installed and seasoned. It's also helpful to look at the improvement in these ARPA trends over a longer period of time. CA-ROW ARPA declined 22% for the full year 2018 over the prior year as we've brought on new fleets. For the full year 2019, we expect this rate of decline to be less than half of this level and we expect overall ROW ARPA to begin increasing in 2020 which would be a meaningful achievement considering the number of new fleets being added.

Segment loss in CA-ROW improved about 15% from the prior year period to a $19.2 million loss as we continue to see the benefits of more aircraft utilizing our global satellite network. This operating leverage is demonstrated in the progression of service gross margin which excludes depreciation and amortization expense. Of course this margin is negative in the early years of deployment with only a small number of aircraft utilizing the network. We've made significant strides in leveraging our network through the number of ROW aircraft wins we've achieved and are now deploying. The negative service margin was cut by more than half in 2018 versus 2017 and it reached positive territory for the first time this quarter.

For the full year 2019, we expect to see a continuing reduction in segment losses from the peak level of 2017 as we spread satcom and operating costs across a larger 2Ku fleet and benefit from the reduction in expenditures for major new programs.

I will now conclude with the discussion of our 2019 guidance. Our initial guidance for the year included the impact of one airline switching back to the turnkey model with the resulting reduction in equipment revenue. We now expect two airlines to flip back to the turnkey model before the end of 2019; one of which has already transitioned.

However, based on the strength of the underlying CA service revenue and allowing that there may be some fluctuation between business segments, we are not changing our guidance range for consolidated revenue at this time. Our updated guidance is as follows; total revenue in the range of $800 million to $850 million, unchanged. CA-NA revenue of $355 million to $380 million, no change from prior guidance, was approximately 5% from equipment revenue. This was reduced from the 10% we had provided on our initial 2019 guidance and as a result of airline's changing from the airline directed to the turnkey business model.

We expect CA-ROW revenue of $135 million to $150 million with approximately 30% from equipment revenue; no change from prior guidance for either measure. [PPA] revenue of $310 million to $320 million, again, no change from prior guidance. We are raising 2019 adjusted EBITDA guidance from the previous range of $75 million to $95 million to the higher and narrower range of $90 to $105 million. This implies 37% adjusted EBITDA growth over 2018 at the midpoint of the range.

Again, looking at the quarterly profile, we expect second quarter to be the lowest adjusted EBITDA quarter of the year. Based on our improving cash flow expectations, we're changing the tone of our guidance from approximately to at least $100 million improvement in free cash flow over 2018. We continue to expect unlevered free cash flow to improve every quarter on a year-over-year basis during 2019 and for this metric to be in modestly positive territory for the full year.

Our final guidance metric is an increase in 2Ku aircraft online of 400 to 475; unchanged from prior guidance. As I conclude our prepared remarks, I want to join Oak in thanking our customers, our investors as well as our employees for their hard work in contributing to these strong results.

Operator, we're now ready for our first question.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions) Our first question comes from the line of Philip Cusic with JP Morgan, your line is open. Please go ahead.

Philip A. Cusick ***JP Morgan Chase & Co, Research Division - MD and Senior Analyst***

Hi guys, thanks. Minor distraction right at the right time. So, let's start with the cost savings that have been helping CA quite a bit. Can you detail more for us on what you've done in the last year and how you see the opportunity, not just this year, but going forward in cutting costs?

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

Yeah, I mean it's a little hard to nail one thing Phil because the IBP plan had 102 initiatives, I would guess two-thirds of them had a cost savings element to them and a -- ran across all the functional operations as well as the G&A functions. So, you know, it's very broad-based.

Philip A. Cusick ***JP Morgan Chase & Co, Research Division - MD and Senior Analyst***

Okay, and what about going forward. I'm sorry.

Barry L. Rowan ***Gogo Inc. - CFO & Executive VP***

To add to that Phil, I think if you look at this year, as we've described, a number of major projects had their primary investment -- large business behind them including things like the number of STC's we had to put in place for new air frames and the line-fit programs. We're still investing in those but at a lower level. There were also some changes associated with the strategic direction, for example, as we shifted to more of a B2B as opposed to B2C consumer, or marketing approach, we were able to reduce some of the marketing expenses last year as an example.

So going forward, we'll see the benefits of those things as well as really tightening up operational -- all the operational processes as Oak mentioned.

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

Yeah, everything Barry just described were all part of the IBP plan. The other thing I would say, Phil, is there's still some benefit to come from that next year. The 102 or so projects actually run through, are supposed to run through second quarter 2020. So, we'd expect somewhat cost savings coming out of those.

Philip A. Cusick ***JP Morgan Chase & Co, Research Division - MD and Senior Analyst***

Okay, and in the past, you've talked about some of the premier airlines coming online in rest of the world during 2019, can you talk about some of those airlines you bring online and then give us an update on the RFP pace out there? Thanks.

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

Well, one thing I'd say, the big international airlines where we're on [Wi-Fi] in fleet, they install a little slower because wide-bodied planes slide more, you know, with domestic planes it's a little easier to ramp up quickly because the planes are down every night and you can get at them whereas the wide-bodied fleets they often are flying (inaudible). So it's harder to get them into [majors] to get the systems installed. Obviously they're also bigger. So, the ramp is somewhat slower from the time you start installing fleets until you complete. But we're making good progress. You know, I think some of the fleets are getting further along like the British Airways for instance is moving along at a pretty good pace right now.

We have -- we are seeing some good success in international. In Australia we're on Virgin Australia both international and domestic and they've moved to 3 model and their take rates have really taken off and it's encouraging to see a relatively new airline ramp up pretty quickly. So there's a [green shoot] there. What was the second part of your question?

Philip A. Cusick ***JP Morgan Chase & Co, Research Division - MD and Senior Analyst***

Just talk about the RFP's that are out there.

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

Yeah, there are -- I mean, what we've seen in the last year or so is a much more deliberate decision making process on the part of the airlines. You know, a lot of international airlines early on would say, okay, (inaudible) entertainment system on just -- by their IFC system or, you know, a lot of these sales were part of line-fit programs and they just sort of check the box, yeah, give me whoever you want; Boeing or Airbus for IFC.

Now, they've been disappointed in us, I think, that they're getting much more deliberate in that decision making process so the processes are just taking longer. In terms of the pace, you know, I think there's a fair number of RFP's out there, you know, there are not many in the United States but there are a lot in the rest of the world and I don't think the pace has changed much from last year. We're working on a lot and we're hopeful that we're going to win some good ones.

Philip A. Cusick ***JP Morgan Chase & Co, Research Division - MD and Senior Analyst***

Good, thanks guys.

Operator

Thank you, and our next question comes from the line of Simon Flannery with Morgan Stanley, your line is open. Please go ahead.

Simon William Flannery ***Morgan Stanley, Research Division - MD***

Great thanks, good morning. Interesting discussion, Oak, on the Ku opportunities. I was [struck] at the satellite show that a lot of the LEO constellations are highlighting Arrow as one of their top target markets and I was just -- wanted to think about your conversations with them and how you think LEO might increase your options, your cost profile, etc., is that something that's part of your near-term thought process? And then, we've got the airline switching back from airline directed to turnkey; maybe just give us a little bit of insight into what's leading them to do that and, you know, as we go to free, how do you see this evolving more broadly on pricing and so forth? Thank you.

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

Yep. So on LEO's, you know, first of all, we are ready for them if they come. In the Ku [ban] at least, our 2Ku antenna because it doesn't have the mechanical (inaudible) piece, it would have to flip back and forth at a very rapid pace to handle LEO's coming quickly over the horizon because of the flat panel design. You know, we are ready for LEO, should it become economically viable, an important part of our constellation, if you will.

You know, we aren't depending on LEO so, because, I think there's a lot of legitimate questions about whether they get up, most of those revolve around funding. The LEO's that would get up first, if the current progress proceeds, don't really have much dynamic capability, they tend to be blanketing the earth at a relatively even manner which isn't really conducive to extreme mobility. You know, our demand moves around the globe all day long at a pretty rapid pace. So we're looking to increase capacity utilization by being able to aim beams where we want them when we need them.

So, you know, LEO's -- you know, some of the later designs, you know, could handle that. The [Telesat] design does have more dynamic beams then say some of the earlier ones. So, we're not depending on LEO's. I think that's the answer to that piece but we're ready for them should they emerge.

On the turnkey to AD issue, you know, think it's almost kind of a red hair, right? I mean, we're the only company to even have the turnkey deals because of the whole -- because we've been around so long and back in the old days airlines didn't want to pay to put connectivity in. So we have more of an arrangement where we installed it, we needed the space, if you will, in return for royalty and we market it to the customer.

And generally now airlines consider this important enough that they want to take over the distribution and marketing of the product. Some airlines having done that, realize there's a cost and don't necessarily like that cost. So, you know, some of them are -- have asked to move back and we've moved one back and we probably will another. I don't think moving back is going to be a big trend either, to be honest, I think it's always going to be a bit of a mix and that mix is going to depend on the size of the airline, their profitability and their own distribution capabilities.

In terms of the move to free, you know, we have a -- one of the heroes of the airline industry is on our board, named Bob Crandall. I mean, Bob says, you know, one in, all in. So if somebody ends up going free I think there's going to be a lot of pressure on the other airlines to go free. I think that airlines that have a single provider are going to be advantaged in that because they won't have to try and negotiate across multiple providers to get to free. I think that free will actually raise all boats in our industry. The industries taken a [blinking] over the last couple of years from the PR perspective that nobody was going to get profitable and it was a disaster. I would note that nobody is profitable in the ride sharing industry either but people seem to think it's worth investing in. Anyhow, I think that the free could be the tie that raises all boats except for the boats that have holes in the bottom. And I think the companies that can ramp capacity quickly to satisfy their airline customers demands will be more successful as a result of free than others.

Simon William Flannery ***Morgan Stanley, Research Division - MD***

Any update on the NextGen ATG?

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

As I aid in my comments, we're working hard on that and we'll have more to say later. We should note a couple of things; you know, this will be our fourth ATG network. As they say in the Farmer's Insurance ad, you know, we've learned a thing or two because we've seen a thing or two. You know, we've been -- we've basically -- we're at the point of deployment with our NextGen ATG system, the LTE 4G version that we developed with ZTE. We had ten towers installed, we had 50 other towers on their way to be installed and we're flying very successful test flights. But I think, you know, we'd be foolish not to understand the risks in having a Chinese Telco as a partner now, sadly, and we need to adapt to that. So we have been working, frankly we've been working on the NextGen version of something since 2011 and we have lots of different ideas for how to do it and we have lots of very smart engineers who have been thinking about it for a very long time. So, in the time since the first GTE issues crept up last spring, we've been hard at work at looking at alternatives and we'll have more to say about our direct path utilizing those alternatives; hopefully in the not so distant future.

Simon William Flannery ***Morgan Stanley, Research Division - MD***

Great, thank you.

Operator

Thank you, and our next question comes from the line of Rick Prentiss with Raymond James, your line is open. Please go ahead.

Richard Hamilton Prentiss ***Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research***

Yeah, thanks. Couple of questions, Barry, you mentioned you've been working aggressively on the working capital side freeing up some cash also. How much cash do you think you need to traditionally run the balance sheet month in, month out, quarter in, quarter out?

Barry L. Rowan ***Gogo Inc. - CFO & Executive VP***

Yeah, the first part of that Rick, yes, we are working aggressively on that and it's driving the underlying process improvements which is releasing cash through inventory and receivables management primarily. What I would say about the liquidity is that when you look at the projections that we have and including the tack-on that we've done and the $30 million in revolving [ABL] facility that came with this transaction. We expect that our liquidity position is going to be -- remain above $100 million when you include those things. So, our projections are to have a good cushion about the $100 million range.

And in terms of the amount of cash required to run the business, it's certainly below that level meaningfully but we're comfortable with that liquidity position given our current plans and the cash flow trajectory that we're seeing going forward.

Richard Hamilton Prentiss ***Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research***

Okay, and Barry, you mentioned, I think Oak you have in the past, the flexibility and the most recent senior note includes the $150 million in case there's a strategic investment in the next 12 months. Help us understand, one, why is that inserted in there? Is there something actively being worked on in that kind of timeframe? And two, what should we think that that tight universe would be? Is it a customer, is it a peer, is it strategic, is it a financial -- how should we think about what -- to make up the $150 million that you called out on the call?

Barry L. Rowan ***Gogo Inc. - CFO & Executive VP***

Sure, I mean, this is kind of an extension of the conversations that we had last fall. As you know, at that time, we had some inbounds about selling at one of the divisions, or another. For example, those relationships that we've developed through that process have been ongoing. I would say that the nature of the conversations has evolved from an outright sale of the division to something that looks more like a strategic investment in the company that would likely come along in conjunction with some kind of a commercial arrangement. So it's more of a strategic investment that would augment the business, it would enable us to advance the business commercially a well as bring in some capital to the company.

So that amount is an amount that would be meaningful, obviously, to bring in a partner like that. And we wanted to have the flexibility were that to come in as a cash infusion to either pay down debt or add cash to the balance sheet. So being able to call it at [103] gave us that flexibility and our debt holders were, you know, very supportive of that idea as well.

Richard Hamilton Prentiss ***Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research***

If the timeline extends out beyond the 12 months, does it just mean that you put it on the cash or you don't have to worry about the [note-call two] side, I'm just trying to think why the 12 months?

Barry L. Rowan ***Gogo Inc. - CFO & Executive VP***

Yeah, I think the 12 months is for a couple of reasons. One is that those conversations remain ongoing and we will see if we get something done that's going to happen or will probably happen in that period of time. And secondly is with the shorter note call period of two years, we get beyond that then the note -- the benefit of the 103 does come down as you get closer to the note call which is, I think, as you get closer to first call period which, as you know, is at [ARPA plus half] a coupon, so [104.5] or so. So, that as kind of the rational for including that period of time.

Richard Hamilton Prentiss ***Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research***

Makes sense. The last one for me, to piggyback on Simon's question about the NextGen ATG, I know you've got more to say later, you're happy with your progress you're making, could you help us frame just within zip codes, what might we be talking about as far as capex or opex or physical requirements as you look to roll that new solution out?

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

I think we're looking at maybe a little bit more than we had in the prior solution but, not dramatically different. And we can give more guidance on that down the road.

Richard Hamilton Prentiss ***Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research***

That's good. Yeah, some people are just nervous, you know, what are you talking about, is it a big change out -- that helps a little more than the previous one. Thanks.

Operator

Thank you, and our next question comes from the line of Louie DiPalma with William Blair, your line is open. Please go ahead.

Louie Dipalma ***William Blair & Company L.L.C., Research Division - Analyst***

Good morning. Guys, with the debt refinancing, the deicing and the deinstalls now nearly complete, there have been many references to free cash flow generation and being fully funded in the press release and in the scripted remarks. Do you anticipate being free cash flow breakeven next year; so for 2020? And for actual positive free cash flow generation, the year after, on the fully levered basis?

Barry L. Rowan ***Gogo Inc. - CFO & Executive VP***

Yeah, Louie, we haven't given specific guidance around that. But what I would say is that our outlook for free cash flow continues to improve. I think to your question around 2021, you know, we do expect to be (inaudible) free cash flow positive in the 2021 and in 2020, approaching it. So when you look at the cash flow profile with the liquidity we have now with the improving EBITDA with the benefits of the cash management programs we're putting in place, all of those are contributing to that. So approaching it in 2020, I wouldn't say we'd get all the way there, but then meaningful positive free cash flow generation in 2021.

Louie Dipalma ***William Blair & Company L.L.C., Research Division - Analyst***

Sounds good Barry. And for the full year of 2018, the international part of the commercial division improved segment EBITDA by roughly $12 million and it continued to show solid progress in the first quarter. And Oak, you noted that Virgin Australia is shifting to passenger free which also seems to be a positive development. How should investors think of modeling the international segment in -- as more aircraft come online and as they become more seasoned. Is the $12 million per year an improvement a good number or do you think it could increase beyond that for the next several years? I was just wondering how you guys are thinking about the improvements in that division?

Barry L. Rowan ***Gogo Inc. - CFO & Executive VP***

Sure, let me first talk, Louie, about the drivers of the improvement and then I can maybe frame the -- kind of the expectations there. There are really three primary drivers to improving the rest of the world profitability. The first is increasing number of planes, so as we install that backlog, that will certainly drive that and you're seeing that benefit now as we get better utilization of the network because you have to obviously have coverage around the world as we fly more aircraft we can get better utilization of that coverage and then add capacity as it's required but turns into more of a variable cost as it's required over different parts of the world.

So the first is the planes, the second is the average revenue for aircraft and, as I've described, we're seeing some real improvements there as we get these aircraft installed and expect that to continue as we outlined with the addition of the high quality fleets. And then the third one is the cost structure. So there are some meaningful investments and getting started in the rest of the world and then in addition, we did see the opportunity to drive satcom costs down even further. So the benefit to us is from raw bandwidth cost as well as the utilization and for the reasons that Oak outlined, and we see the significant technology advancements in satellite technology that we do see that really helping beyond what we had expected when we were doing these plans last summer.

In terms of the -- giving you some context for the overall improvement in the burn for ROW, yeah, what we said a while back that we expected 2017 to be the peak year investment in ROW and that has been the case. You see it coming down to $95 million from over $100 million in 2017 to 2018. And you know, we would expect to see an improvement of that order of magnitude this year and then beyond that it will really depend on kind of the ramp in the ARPA for those aircraft coming online because most of them leave the current backlog will be installed as you get out into those (inaudible).

We're growing -- we're growing more optimistic, I would say, on the revenue opportunities there then we were going back last summer for sure. I mean, just to quantify that. We had said going back to last summer that we were projecting -- for purposes of planning, a take rate that was 12.6% in 2022, we're beyond that already so our expectation for EBITDA generation and free cash flow generation has certainly improved.

Louie Dipalma ***William Blair & Company L.L.C., Research Division - Analyst***

Thanks a lot guys.

William G. Davis ***Gogo Inc. - VP of IR***

Last question. That was our last question, thank you.

Oakleigh B. Thorne ***Gogo Inc. - President, CEO & Director***

All right, well, thank you everybody for attending our Q1 2019 earnings call. I'd like to leave you with just a few thoughts. First, we've got a really -- very strong cash flow generating business in DA which has not only a unique competitive advantage but virtue of our own spectrum but also has ample legroom for growth because BA is relatively unpenetrated. Second, rest of world is growing. It's an extremely large and unpenetrated market and with our global 2Ku platform and strong backlog, we think we're well positioned to win share, win our share of the attractive long-haul wide-body market.

Third, CA-NA will return to solid growth in 2020 and its increasing take rates drive ARPA and strong free cash flow. Fourth, we strengthened our balance sheet, as we've noted, and finally, by virtue of our industry leading market share scale, we really believe we're positioned to take advantage of the opportunities in front of us as we look forward to demonstrating that and talking to you about it in the quarters to come. Thank you very much.

Operator

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