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PRESENTATION

Operator

Good day. And thank you for standing by welcome to the Gogo First Quarter, 2021 Earnings Conference Call. (Operator Instructions) I would now like to hand the conference over to your first speaker today, Mr. William Davis, Vice President of investor relations. Please go ahead.

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

Thank you, RJ. And good morning, everyone. Welcome to Gogo's first quarter, 2021 earnings conference call. Joining me today to talk about our results are Oakleigh Thorne, President and CEO. 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 the conference call. These risk factors are described in our earnings press release, filed this morning and are more fully detailed under the 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 6th, 2021.

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 more information or future events. During the call, we'll present both GAAP and non-GAAP financial measures. We've 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 has been broadcast on the internet and available on the investor relations section of the Gogo website at ir.gogoair.com. The earnings press release is also available on the website. After management comments, we'll host a Q&A session with the financial community only. It is now my great pleasure to turn the call over to Oakleigh.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Thanks, Well and thank you all for joining us this morning and for your interest in Gogo. The first quarter results we announced today and the completion of our refinancing last week, reflect Gogo's strong momentum as we execute on our pure play business aviation connectivity strategy. Today, my remarks will focus on highlights of our first quarter results, business aviation's strong from the depths of COVID, our progress against the strategic initiatives I discussed on our last call. And the impact of the refinancing on our business on a go-forward basis. Let me start off with results. Gogo delivered a really strong first quarter driven by the ongoing recovery of the business aviation market and the strength of our Vox platform. We generated total Q1 revenue of $73.9 million up 4% compared to Q1 2020, driven by a 3% increase in service revenue and a 10% increase in equipment revenue.

The service revenue growth is primarily attributable to a 3% increase in ATG aircraft online hitting a new record high of 5,892 aircraft. Our ability to rebound from the depths of the pandemic to record aircraft online in just 12 months, speaks to the resilience of our team, the strength of our technology and the mission-critical nature of our service to customers. On the equipment side, Gogo grew first quarter revenue 10% year over year, driven primarily by AVANCE L5 sales and supported by some lifetime buys of [Veridium] equipment. We also mark an important milestone, 100% of Gogo's ATG equipment shipments in the first quarter were AVANCE. And as we wind down new sales of our classic ATG product line and customers gravitate to our next generation AVANCE platform. Despite the strong year over year growth, equipment revenue was down 30% sequentially from an extremely strong Q4 2020.

However, Q4 tends to be our strongest equipment sales quarter and given our current strong backlog and pipeline, we predict equipment sales overall this year will significantly surpass equipment sales for 2020 by 20%. The strong (inaudible) sales should drive growth and our high margin, recurring service revenue down the road, as many of the units we shipped have yet to come online. Our 5-year plan targets the additional 400 ATG aircraft online per year, and we expect to greatly exceed that number for 2021. On another positive note, we had very low equipment churn in the quarter. Getting an annualized 98.2% equipment retention rate, which equates to more than a 17-year revenue producing equipment life on an aircraft. This is a significant recovery from our low point of 92.5% in Q2 of 2020. We also achieved strong adjusted EBITDA and free cash flow performance for the quarter, driven by robust equipment revenue, disciplined price controls, and some delayed spending that we'll hit later in the year.

I'm very proud of the Gogo team and what we accomplished in the first quarter. I think it's a harbinger of good things to come and the culmination of a lot of hard work and strong execution over the past 2 years. Now, let me turn to conditions in the business aviation market. Clearly, the pandemic has driven supportive trends in business aviation. Pushing more fliers who can afford it, to fly private out of health concerns and accelerating the Uber-fication of air travel, as more connected passengers turned to charter or time share models to access private aviation. We view [BA] flight activity as a proxy for demand. As growth in flight activity, ultimately drives demand for aircraft, and that will drive demand for connectivity. This is especially true in the corporate and fleet segments, where passengers are insisting on quality connectivity when making their purchase decisions. In order to accurately assess growth in the industry today from pre COVID times, we will compare 2021 flight activity to 2019 activity. For Q1 2021, average daily Gogo flight activity ran at 97% of average daily flight activity for Q1 2019.

However, that modest decline was really anchored by corporate flight departments, who were still well behind the 2019 flight counts early in the year. That all changed in March and April. Corporate flight counts grew from around 70% of 2019 counts in February to 100% of 2019 counts in March and 102% in April. Charter flights grew to 130% of 2019 counts in March and 128% in April. And fractional flights grew to 130% of 2019 in March and 136% in April. This dramatic growth in demand has driven a surge in secondhand aircraft purchases, leaving inventory of for sale pre-owned aircraft at an all time low. It's caused fleet operators to delay aircraft retirements. And it's led very reputable wall street analysts to raise their projections for OEM deliveries by 6% for this year. And another 6% for next year. Gogo is uniquely positioned to take advantage of this opportunity or line fit at all 9 of the major business aviation OEMs.

We have a strong aftermarket network of 120 dealers that sell and install our systems. And 93 STCs that cover installing Gogo equipment on more than 200 makes and models of aircraft, far more than any other broadband [IFC] supplier to the BA market. The other big change in the BA market is the change in passenger behavior. The COVID new normal, has driven our end users to live and work online, and they now require streaming and video conference capabilities inflight as part of the work from anywhere culture. This demand itself in Q1 data consumption on Gogo equipped aircraft, growing 44% from Q1 2019, which translates into a 32% increase on a per aircraft basis. And which in turn should manifest itself in purchase of higher data and service plans in the future. Gogo is well positioned to meet this increased data demand with AVANCE L5, which delivers faster speeds and enhanced network capacity on our 4g ATG network. L5 enables live streaming of video and audio, video conferencing, and other must have applications like VPN.

To make that demand more affordable, we just announced a new unlimited streaming and data plan, Gogo biz 4g limitless, available to our AVANCE L5 customers. Which allows customers to enjoy the benefits of streaming without the unpredictability of high overages. And Gogo 5G will advance our product offering even further, by supporting multi-device video streaming, truly extending every capability of the remote office into the sky. Based on the strength of our first quarter performance, and the industry tailwind shaping the recovery of the business aviation market, Gogo is raising our 2021 revenue and adjusted EBITDA outlook. And we are giving positive and we're going to achieve positive free cash flow for the first time. Barry will provide more details on that in a moment. Now let's talk about our progress on the strategic initiatives I discussed on our last call.

As background, that's remember that this is aviation is a relatively small market, but it is a highly unpenetrated market that represents a big opportunity for a small company like Gogo.

Of the 24,000 business aircraft in North America, only 28% have broadband and WiFi today. And of the 14,000 business aircraft in the rest of the world, less than a thousand have broadband today. Our strategy is to leverage our 3 unique competitive advantages, namely our proprietary ATG network, our advanced platform, and our strong distribution channels. To strengthen our competitive moats and go after that large white space in the BA market. We intend to do that 3 ways. First, we want to continue to enhance our ATG network by rolling out Gogo 5G. 5G will allow us to aggregate our proprietary license spectrum, the 60 megahertz of unlicensed spectrum to deliver a super fast, high performance link for our customers. I should note that our portfolio of 349 patents, includes patents related to this aggregation technology. We've made tremendous progress on 5G in the quarter. We completed critical design review and flight testing for our airborne antenna.

We completed installation of all 5G core hardware and software on our data centers. And successfully completed our first end-to-end call on the Gogo SIM. We successfully completed acceptance testing of our 5G base station antennas and preparation for test bed installation later this year. And we completed building our prototype 5G aircards in preparation of full airborne equipment prototyping, also later this year. We're still on schedule for service launch in 2022. So as mentioned on our last call, because some production related delays associated with a particular 5G semiconductor chip. Our schedule takes into account the chip manufacturer's current expectations on delivery timing and still projects service launch will take place in 2022.

Our second strategic initiative is to drive penetration of our AVANCE platform, it gives us the ability to integrate future technologies into our customer's existing AVANCE installation, at a much lower cost than buying and installing similar products, new from some other supplier. In essence, AVANCE futureproofs our customer's investment in our hardware by enabling us to add new products, new service levels, new spectrum, and even new networks, primarily with software upgrades, as opposed to expensive in-aircraft hardware upgrades. For example, when Leo satellite networks and ESA and townhouse company come available, Gogo would have the option of offering AVANCE customers access to those networks simply by adding a new ESA antenna on top of a plane. That antenna could plug into the existing AVANCE platform already installed inside the plane. Much like a Tesla, the rest of the Leo upgrade would be achieved with a simple software update to the AVANCE device already on board.

Conversely, if a future competitor offers that same product, the customer will have to rip out existing equipment and install new hardware inside the aircraft, a cost to the customer of hundreds of thousands of dollars and weeks of downtime. Gogo is not committed to a Leo plan, but this demonstrates the type of optionality we get with a relatively modest investment on our part, from the AVANCE platform. To make this point even more clearly, when we upgrade AVANCE L5 customers to 5G, most of the upgrade will be software. The only hardware needed will be one small box and 2 new antennas that fit exactly where the old antennas sit on the outside of the aircraft. Needless to say, we're very bullish on AVANCE. The flexibility to adopt and then integrate new technologies as it evolves, builds competitive moats around our current market position, and also gives us the ability to attack new markets outside of North America. What was exciting about Q1 for AVANCE, was that we grew units online 42% year over year to 1900 units, for 32% of our total aircraft online, up from 23% in Q1 2020.

Our third strategic initiative is around supply chain and manufacturing. In order to drive down costs and enhance quality, we simplify our supply chain by mandating common componentry across all AVANCE devices, whether it's our low cost L3, or fully featured L5, or our future 5G. By mandating common componentry, we drive down the number of FKUs we need to source. Thereby driving up the quantity we purchase of each FKU. This then lowers unit costs and drives up quality by simplifying our inbound logistics and manufacturing. This has proven especially valuable this year, as we've been able to minimize supply chain risk in the face of a dramatic increase in demand during a global supply chain crisis. Currently, we feel that we have enough supply to meet our increase in demand for the next several quarters. Let me finish on the refinancing front. In early 2020, we outlined our value creation roadmap for Gogo.

It focused on first managing our business through the severe impact of the COVID-19 pandemic. Second, completing the sale of the commercial aviation business. And third, executing a comprehensive refinancing to enhance our financial flexibility and position the new Gogo for growth. With the closing of our refinancing last Friday, we've delivered on all 3 prongs of that plan. Our refinancing was an overwhelming success. We achieved approximately $70 million a year in annual cash interest savings, as opposed to the 50 million we had originally targeted. As a result of now having a clear picture of our debt service obligations and given the strong performance of the business, we are now sharing long-term free cashflow guidance for the first time. And Barry will provide more detail on that guidance in just a moment. There are several other very positive aspects of our refinancing that are worth noting. First, by borrowing the term loan B market, we achieved flexibility to refinance, to delever, or to pursue strategic transactions in the future as we see fit. Second, with $200 million of liquidity and our significantly enhanced free cash flow, we'll be able to invest in deepening and widening our competitive moats, and in further delevering our balance sheet. And third, in Q3 we expect to achieve a major milestone when we turn net income and earnings per share positive for the first time, and become what my dad would call a real company. That's an exciting milestone for Gogo.

Now, let me make a few concluding remarks. First, I'd like to welcome Mark Anderson of GTCR to our Board and welcome GTCR as a partner in the Gogo business. GTCR added tremendous value throughout our refinancing process, and because they've had investments in other business aviation companies, they bring valuable VX experience to our Board. So welcome, Mark. Last, at Gogo we are very excited about the opportunity ahead of us as we leverage our ATG network of leading innovative advanced platform and our strength in balance sheet to drive growth and value creation for our employees, our customers, and our shareholders. And with that, I'll turn it over to Barry.

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

Thanks Oak, and good morning everyone. In my remarks today, I'll start by walking through Gogo's first quarter financial performance in more detail, then I'll provide an update on our balance sheet, following our comprehensive refinancing last week, which is a major milestone for Gogo and sets us up for significant value creation going forward. And finally, I'll finish up with some additional context around the updated 2021 guidance and long term targets we announced this morning.

As Oak mentioned, the accelerating recovery in the business aviation market and our unique ability to capture that value drove strong first quarter results. Total revenue of $73.9 million increased 4%, compared to the first quarter of 2020, driven by increases in both service and equipment revenue. These results reflect the continuum of recovery in the business aviation industry and strong sales of Gogo's advanced platform. On a sequential basis, total revenue decreased 4.8% in the first quarter of this year. We have strong growth in service revenue sequentially, however, as expected, equipment revenue declined following the record advance shipments in the fourth quarter of 2020, driven by pent up demand, promotional activity, and general seasonality for equipment.

Let me break down the revenue progression between service and equipment. We achieved record service revenue of $59.4 million this quarter, an increase of nearly 3% compared to the prior year period, due primarily to a 3% increase in ATG aircraft online, and recognition of $1.2 million in service revenue under the network sharing agreement with Intelsat. As a reminder, we have a ten year deal under which Intelsat has exclusive rights to our ATG network for commercial aviation, subject to paying us at least $178 million in revenue share over the term. We expect to generate increased revenue under this agreement over time.

On a sequential basis, service revenue grew more than 4%, due primarily to a 2% increase in ATG aircraft online, higher service revenue from the network sharing agreement with Intelsat, and an increase in average monthly connectivity service revenue per ATG aircraft online, or ARPU, from $3,069 to $3,085. Overall, we're expecting ATG ARPU to continue to rise throughout the year and exceed 2020 results for the full year 2021.

In the first quarter new customer activations as a percentage of total activations increased to pre COVID levels of 65%, which is a positive indicator for the projected growth trajectory of our service revenue. It's important to highlight that since emerging from the depths of the pandemic, we have seen consistent sequential growth in our subscription-based service revenue. This trend is key to our recurring revenue model and will be an important long term value driver. Notably, we expect continued sequential service revenue growth throughout 2021.

Now let me discuss equipment revenue. We generated equivalent revenue of $14.5 million in the first quarter, a 10% increase compared to the first quarter of 2020, driven by increased shipment of our advanced products. As Oak outlined, driving penetration of the advanced platform into our installed base and with new customers is a centerpiece of our long term strategy. It provides the foundation for our expectations of continuing growth in our service revenue annuity stream.

Looking forward, we expect the seasonality we've experienced over the past several years to persist, with equivalent revenue back-end loaded to the second half of the year, and strongest in Q4. There are several factors that drive Q4 sales, promotional activity and trade show timing are 2 contributors, and we also find that some companies wait until the end of the year to get a sense of their financial position before making equipment investments. That trend, combined with our sizable backlog of purchase orders, new orders received in the first quarter, and other indicators, give us confidence that 2021 equipment revenue will grow at least 20% over 2020. We've raised our 2021 revenue guidance to reflect these positive trends.

I'll do a deeper dive into our full guidance update in a few minutes, but first let's focus on profitability. As we outlined last quarter, we anticipate service margins to contract somewhat throughout 2021, mainly due to increased data center and network operations costs. Some of these increased costs are transitional, as they relate to the separation and migration activities following the sale of our commercial aviation business to Intelsat. As mentioned previously, our service margin will also be modestly affected by the financial statement geography change, with Intelsat revenue share being recorded in service revenue instead of cost of service. While we experienced some of that anticipated contraction in the first quarter, service margins remain strong at 76% and we expect this metric to remain in the mid 70% range over the longer term.

Equipment margins rose significantly on a sequential basis following the $2.6 million inventory reserve that was recorded in Q4 2020. We also saw improved product mix, with higher margin L5 shipments in Q1. We don't expect this very high equipment margin to continue through 2021, however we do expect equipment margins for the full year 2021 to be above the 2020 levels.

In terms of operating expenses, we've been successful in beginning to adjust our cost structure to align with our smaller size and more focused business. In the first quarter, we saw significant decreases in G&A spending due to lower outside services and personnel expenses. This drove a 26% year over year reduction in combined engineering design and development, sales and marketing, and G&A expenses, as these expenses totaled $20 million for this quarter. As we noted in our pre-announcement filing in mid April, this does reflect a delay in certain budgeted operating expenses totaling approximately $4 million that we expect to incur future quarters. Looking at operating expenses for the full year of 2021, we expect OpEx to grow from the low levels experienced in the first quarter of this year, reflecting financing and other expense growth in G&A, increased by G spend as that program continues to ramp, and modestly increasing sales and marketing expenses.

We continue to expect G&A expenses to be relatively flat for 2021 versus 2020, as we deliver on our obligations under the Intelsat transition services agreements. As we've said previously, we expect to reduce G&A, excluding non-cash stock based compensation, by approximately $10 million by the end of 2022. 5G expenses were some of the delayed costs that will be pushed out to second quarter and later in the year. We spent just $1 million in total external 5G development and deployment costs in the first quarter, of which approximately $600,000 was in OpEx and the remainder in CapEx. We continue to expect to spend approximately $12 million in 5G OpEx for external development and deployment in 2021, as reflected in our adjusted EBITDA guidance, although there could be some shifts between 5G CapEx and OpEx for the balance of the year.

Our bottom line performance for the first quarter was strong. Gogo delivered adjusted EBITDA of $33.9 million, a 25% increase over the prior year period, and up 76% from Q4 2020. As a reminder, Q4 2020 adjusted EBITDA was negatively impacted by $10 million for the full year accrual for 2020 cash bonus expense, as well as a $2.6 million inventory reserve, as we previously described. Free cashflow for the quarter was $23.9 million, a 4% increase over the prior year period due to the increase in EBITDA, offset by lower networking capital. Free cashflow for the first quarter of 2021 increased by over $40 million from the fourth quarter of 2020 due to the interest payment in Q4. We expect free cash flow to be negative in the second quarter, due to the higher interest payment prior to the April refinancing, but expect to generate positive free cashflow thereafter. We're pleased with our first quarter results, particularly as they reflect Gogo's ability to drive growth, even through the lingering effects of COVID.

Before I move to a discussion of our guidance and long term targets, I'll touch on our balance sheet position, which now reflects the comprehensive refinancing we completed last week. This represents a major milestone in our transformation to the new Gogo, and creates a step change in our value creation potential. I'll summarize the mechanics of the transactions and then elaborate on some of these benefits.

As we previously announced, in March and April Gogo entered privately negotiated exchange agreements with GTCR and other existing holders of our 2022 convertible notes. Through those exchange agreements, approximately $135 million of aggregate principle amount of the convertible notes were exchanged for approximately 24 million shares of Gogo common stock. In connection with the GTCR exchange agreement, Gogo welcomed Mark Anderson, Managing Director at GTCR, to our Board of Directors. GTCR has been a strong supporter of our strategy, and we truly look forward to continuing to work closely with Mark and the GTCR team as we execute on our shared vision for driving shareholder value.

As Oak described, we completed our comprehensive refinancing transaction on April 30th. We secured a 7 year $725 million term loan B, bearing interest at LIBOR plus 3.75%, with a LIBOR floor of 75 basis points. In addition, we put in place a 5-year $100 million revolving credit facility. We used the proceeds of the term loan B and cash on hand to redeem in full the $975 million aggregate principal outstanding of our 2024 senior secured notes, and pay the redemption premium, accrued interest, and transaction fees and expenses. These transactions have transformed our financial profile, reducing our total debt by $385 million, and we will reduce our interest payments by nearly 2 thirds, realizing approximately $70 million in annualized interest expense savings. These savings will also increase by an additional approximately $6 million, as the balance of the convertible notes mature in 2022 or are converted earlier. This comprehensive refinancing and simplified balance sheet enhances Gogo's free cashflow generation and catalyzes the powerful value creation cycle along 3 primary dimensions.

First, as a result of the transaction, Gogo significantly reduced our annual interest expenses, strengthening our free cashflow. Second, with enhanced free cashflow generation, we have more financial flexibility to invest in strategic projects with attractive returns. And thirdly, our 4 to 5 balance sheet makes us even more resilient against a potential increase in competition, and, as a result, we are well positioned to further deliver our balance sheet to enhance shareholder value returns over time.

Over the long term, our strengthened free cashflow profile is augmented by low ongoing CapEx, significant tax assets of about $800 million in net operating loss carry forwards, and our plan to settle the conversion of the remaining converts in common stock at or prior to their maturity., We currently have approximately 109.6 million common shares outstanding, and approximately $103 million in aggregate principle amount convertible notes outstanding. As of May 4th, we had $100 million of cash on hand. With our undrawn revolver and no current plans to draw on it, we exit the refinancing with $200 million in total available liquidity.

Our team has reason to be very proud of what we've accomplished over the past year through completing the CA divestiture, and in the months since through this additional transformational transaction. Today we are the new Gogo, well-positioned to build on our enhanced financial profile and strong market position to drive long term shareholder value and deliver on a clear, actionable investment pieces.

Now I'll turn to the updated guidance we announced this morning, starting with 2021. Based on the strength of our first quarter performance, we are raising our 2021 revenue and adjusted EBITDA outlook. We now expect 2021 total revenue in the range of $310 to $325 million, increased from the previous range of $300 to $320 million. We continue to expect service revenues to grow at least 15% over 2020, however we now expect equipment revenue to grow at least 20% in 2021, compared to our previous expectation of equipment revenue being relatively flat year over year.

Adjusted EBITDA is now expected in the range of $115 to $125 million, excluding $4 million of non-recurring separation and migration costs related to the sale of the CA division. This has increased from the previous range of $105 to $120 million. We continue to expect capital expenditures in the range of $25 to $30 million in 2021, with the majority tied to Gogo 5G. There may be some fluctuation between CapEx and (inaudible) each quarter as required by the accounting guidelines. We also provided 2021 free cashflow guidance, which reflects the impact of the refinancing. We expect free cashflow in the range of $10 to $20 million, including cash interest payments of approximately $71 million. It's important to note that all guidance is for the full year of 2021. Our expectation is that revenue and profitability will be weighted toward the second half of the year, particularly in the fourth quarter. Looking out over the longer term, Gogo has also provided a long-term free cashflow target to reflect the impact of our comprehensive refinancing. We're targeting approximately $100 million in free cashflow for the full year of 2023, following the deployment of the Gogo 5G network in 2022, and expect significant free cashflow growth thereafter, with continuing improvement in our credit profile.

Our other long-term targets remain unchanged. We're targeting at least 10% compounded annual revenue growth from 2020 to 2025, and adjusted EBITDA margins of 35 to 40% throughout the planning period. As our outlook demonstrates, we are stepping into what we believe is a bright future for Gogo, drawing on our strong market position, the strength of our transformed balance sheet, our industry leading product and service platform, and tailwinds in the attractive business aviation industry. Before we open up the call to questions, I'll just reiterate our thanks to the world-class Gogo team. Our progress and strong momentum are a testament to our team's dedication, ingenuity, and unwavering focus on delivering for our customers and reaching our strategic goals. Thank you team. Operator, we're now ready for our first question.

QUESTIONS AND ANSWERS

Operator

Your first question comes from the line of Ric Prentiss from Raymond James.

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

I want to start the conversation on competition. Oak, you mentioned a little bit about [AVANCE] petitions you in case you make a decision on Leo, but we get a lot of questions about competitive dynamics. Obviously there's other air-to-ground potential networks out there. There's LEOs, Viasat, talks a little bit about what they're doing in business aviation, but talk a little bit about how you see the competitive dynamics and your ability to retain new growth share.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Yes, we look at growing units, not necessarily share anyhow. So we don't focus so much on share, but there are 3 general segments of competitors or compliments, depending on how you want to look at them. LEOs we actually view it as more of an opportunity than a threat. They're 3 LEO networks that are in process right now, and probably more to come after that. Obviously you have Starlink, you have Telesat, you have OneWeb, and at least Telesat and OneWeb have (inaudible) pretty clearly that they're going to move in a B2B manner into our segment. And I think we view that as an opportunity to partner with either of them in order to add LEO as a feature of our offering. And frankly, we think that's a pretty big threat to our GEO competitors.

And whether Starlink chooses to go with a B2B model or not, I don't know, but this is a pretty small market. If you think about our whole industry is about $500 million industry on the service side, and they've got much bigger industries to attack and, and frankly, a bigger markets to attack. And then when you think about the investment of having to go deal with 9 OEMs, build a dealer network of hundreds of dealers, deal with a highly fragmented market in terms of sales to the end users, fragmented market when it comes to the number of planes and models that you have to get STCs for, I'm just not sure that Starlink's really going to view this as something they want to go after. I think Starlink has aspirations in the larger aero markets and commercial aviation, and in mil-gov. Those are aimed at larger aircraft, and to the extent that they could fit some of that on a large BA aircraft, they'd probably go after that market segment because it'd be relatively easy for them.

That's not a significant threat to our core markets, I don't think, and I don't think it's anything they're going to get to in any real hurry. So number one, on LEO, we view that as an opportunity, because our advanced platform gives us the ability to add a new bearer quite easily. You know, the necessary condition for accessing LEOs are electronically steerable antennas. And we're obviously looking at doing that, and thinking through that, and how you actually put that on a BA aircraft. And that's essentially all we would need to develop to be able to access a LEO network. And as I said earlier, both Telesat and OneWeb look like they'll enter this business relationships.

We've not approved this plan. We're not there yet, but we're working at it hard. And, if we execute on it, we think it would give us the ability to certainly defend our core market, and expand overseas, which is an area where we don't really have much business today. So that's LEO.

On the GEO front their big weaknesses is, is latency. And I think over time as LEOs come along with much lower latency, the weaknesses of the high latency solutions like GEO will become more apparent to end users. When we were in the commercial airline business, we did a lot of work with an airline in particular, understanding the impact of latency. And we were looking at for future applications that people would be using an aircraft, and setting parameters around customer satisfaction. And about half of the use cases we came up with could not be served with GEO satellite connectivity.

So both our competitors in the satellite world, the GEO competitors have long-term committed plans to launch more GEO satellites. It's going to be very hard for them to pivot to LEO satellites anytime soon. So we actually view that as a weakness. Obviously the GEOs are much more expensive to install than we are, which is a major inhibitor. And in fact, we just given them the (inaudible) of simplicity of our equipment compared to theirs.

That will always be that they are far more expensive than we are. Their service plans tend to be a lot more expensive. You know, Viasat has been discounting to some extent, and trying to come down to what they call, "ATG prices." However, when you really look at their plans, there are a lot of limitations that, I would say, undercut what they're actually saying publicly.

So they're stuck still on the large end of the market as the equipment's heavy, and it's large. Viasat's is a little smaller than Inmarsat's. So they've been able to come into the super midsize jets, but that's about it. And we compete very effectively with those guys in the high end, we actually have more jets in the large market and in the super midsize market, than both Inmarsat and Viasat combined. Often, and frankly we are installed on the same aircraft they are, and the customers use us over North America, and use the satellite product in other regions. And now on SmartSky, look, they've got a lot of challenges, I think, they've been around for a long time. They were going to put us out of business any moment since 2014.

And so far, haven't gotten a network running. Now, I'm not saying they won't get a network running. And obviously they're working hard at that, but there were a lot of revelations that came out of SmartSky in the last quarter that would cast doubt on their ability to launch a network anytime too soon. They haven't achieved, at least according to an article 2 weeks ago, they have not yet achieved a tower to tower handoff. And that's a pretty necessary condition for a cellular type system, like an ATG system.

The issues are, not only technological though, you've got to build a distribution network like we have, you've got to build up a sales organization and build relationships at 9 OEMs. You've got to get a solid dealers network. And then you've got to incent those dealers, who invest in developing STCs to install your equipment in hundreds of models of aircraft and dealers, aren't going to really go out there and invest in that unless they're pretty sure they're going to be able to sell those STCs to other dealers, because there's going to be a lot of demand for the product.

And I think that with our 5G product coming out, dealers are going to look at that kind of skeptically, and are going to say, "Gee, looks like Gogo's probably going to have the better product anyhow, so why would I invest in creating those STCs?" Then you got to light up a whole network. So you're going to have high operating costs and all the back haul, they're going to have more power density than we have.

And that means they're expensive. Their back haul is going to be more expensive than ours. So you're going to be burning a hole in your pocket while you're trying to build up. And you gradually, over time, this is not a market that moves at lightning speed. It takes a long time to get airplanes into shops and stalled, and it takes a long time for OEMs to make your (inaudible), et cetera. Just to get the top haul, they've gotten some funding recently, but it's going to take a lot more funding for them to be able to become a real competitor in our belief.

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

It does, very thoughtful answer. I appreciate that. Obviously, you guys spent a lot of time looking at the competitive environment. Follow up question is, you've mentioned the strategic projects, strategic possibilities in the future, then expand overseas. Is that what we should think of is where some of the future might be for Gogo and, don't you face some of those same issues then as far as how do you then develop a dealer network, and sales, and opportunities overseas, if I'm hearing you right, that that might be an opportunity strategically.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Yes, well, we actually already have sales and support overseas because of our old narrowband products. We sell [Aridean] and we sell SwiftBroadband globally. So we have a network already, we would need to expand that somewhat, but that's an incremental investment we could make without too much cost. The way we would probably go at this, and let me back up for one second. We have not committed yet, our Board have not formally approved yet us going after an ESA LEO project or some other options we see on the table.

But the point we've been making is that AVANCEgives us the opportunity to go after those, the option I should say, of going after those opportunities, if we want to. And that's really powerful. I think that as we look overseas, you're going to start obviously with large jets within the ESA LEO kind of apparatus, but once you're there, you can go after the medium sized jets and light jets because the ESA form factor should be smaller and give you the ability to go after those guys. We're particularly good at engineering for small aircraft, that's one of our very core competencies.

And so we, we think there's the opportunity with LEOs to go down market overseas in that market of 14,000 aircraft, which you really can't do as a GEO satellite solution. So that, that would be the tack.

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

Great makes sense. When I said, grow share, that's what I was really getting, is the amount of planes that don't have connectivity.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Yes. The issue overseas is pretty simple, it's just not economic, really in most regions to build an ATG network because, outside of the US is a large geographical area, obviously. And, it's 20 to 30% of the world flight, as the rest are in the US so there's very low flight density. So the CapEx involved in creating ATG networks is pretty insurmountable. You do have an ATG network in Europe, of course, whether it's some density, but all of Europe in total, it's still only 6.5% of all the business aircraft in the world. So not a very big market. (inaudible) So satellite is really going to have to be the solution to the rest of the world.

Operator

Our next question comes from the line of Phil Cusick from JPMorgan.

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

I heard the milestones in 5G, that's great. What hurdles remain in getting that that up and running?

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Well, we need this current 5G chip production to stay on track. And assuming that happens, then all the technology risk is removed, and it's really a function of blocking and tackling. And, our own integration testing and the like, but basically everything else is in our control. Let me put it that way. So we have a great program management organization at Gogo, and they've done an excellent job on managing this risk and reorganizing the project in order to still hit our deadlines. And we feel very good about that.

So we're on track for 2022, as we said. And when it comes to blocking and tackling, we are really good at it. This would be our fourth ATG network, really. We built the first ATG network, then we build a ATG 4, and you have to remember that we were on the verge of launching our first significant upgrade of our ATG system that unfortunately we had a Chinese partner on, back in 2018 when I joined the company, and that was almost complete. And that was working very well. So we did that, and now we've got this. So our team is really good at this. They understand how to do it, and we're very confident in our ability to deliver.

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

Okay. Okay. And you talked about 28% penetration, and we got into this a little bit with Ric a minute ago, but do you think that, that the L3 price points are enough to cover the gamut of planes out there? How high can penetration get from 28% given the price points you have today?

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

It's hard to imagine for me, 10 years from now, that there's a plane without connectivity. So that's how we look at it. There are markets like general aviation, which is not in that 28% share total addressable market. But there are markets like general aviation and the general turboprop market, that when you look at them, you say, "Okay, I understand that certain turbo props that are not charters that aren't that profitable or whatever are not addressable today." But I think that ultimately they are addressable. So we believe all planes will be connected in 10 years' time. And yes, there may be lower price points that get you there, but L3 is pretty cheap. It's around $30,000 at an entry point. You can buy a pay-as-you-go plan, that if you don't fly that much, you don't pay anything. You can buy pretty low cost, what we call it core plans and then you can upgrade over time.

You can upgrade the equipment easily. There's 3 stages of L3. There's core, and then there's 2 more enhanced stages after that. So you can come in pretty cheap and grow and we're getting a lot. We're getting some success in the light end of the market, no question, and in the turboprop market. So we think we've got some good openings there and yes, we'll keep learning and figuring out better ways to penetrate more of those markets. But so far we're making some pretty good progress.

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

Okay. And last one, anything you can give us on the status of conversations with the remaining convert holders, next.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

That's really a Barry question, but I'll answer it because it's a really easy question financially. We're not talking to them right now. There's not that much incentive for us at this point to convert them. We'll convert them at maturity or if they can make a compelling economic case to us to convert them, we will.

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

Yes, I think that's right. With the database, the reason we did it previously was we wanted to get them converted, because it really enhanced the financing we did. It helped assist in getting an upgrade for example. But now, as I've mentioned, that incentive is no longer there in the same way that it was before.

Operator

Your next question comes from the line of Scott Searle from ROTH Capital.

Scott Wallace Searle - *ROTH Capital Partners, LLC, Research Division - MD & Senior Research Analyst*

Barry, congratulations on all the work you've done over the past year. It's nice to see you guys becoming a real company. So Barry, just real quickly, I'm not sure I missed the number, but did you give a number for Intelsat contribution in the first quarter? And I just want to clarify on the component availability, it sounds like you guys have sufficient inventory to carry you through this year. Just want to confirm on that front.

And then, as it relates to 5G and the 5G upgrade, I'm wondering what the cost is, both in terms of moving the existing AVANCE installed base and upgrading that to a 5G solution. And as you look at now, it sounds like there is an uptick in terms of new jet orders. I think you said 6% this year and next year. What do you think the attach rate for that is, in terms of connectivity, and particularly in the turboprop market, which has been an under-penetrated area? I mean, how deeply penetrated do you think that could be over the next 3 to 5 years?

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

Yes, let me take your first one right here. Intelsat, Scott, which is a state program. So it was about $1.2 million for the first quarter. And as you know, the minimum amounts start relatively modestly and then grow from there. And it did, as we talked about, have some impact on the service margin. It makes a couple of points difference in service margin because of that geographic shift on the financial statements, from being a contract cost of service to revenue. Oak, I'll let you take the other questions.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Yes, the analyst projection is a well-known investment bank who's got somebody on this call and that has a very good business aviation analyst. And they've raised their projections of 6% on deliveries this year and 6% next year. So that, a lot of those units will be installed with IFC. It might not always be go-go. Some of those would be larger jets that might only have the satellite solution in them. So I can't give you an exact number on what we think we would get out of those 6% today, but we can go dive deeper into their numbers and give you some projections if you'd like. A lot of turboprops coming out today do come with IFC. There's not a lot of new turboprop deliveries, but most of them would have some IFC in them.

Scott Wallace Searle - *ROTH Capital Partners, LLC, Research Division - MD & Senior Research Analyst*

Got you.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

What was the other?

Scott Wallace Searle - *ROTH Capital Partners, LLC, Research Division - MD & Senior Research Analyst*

Oh, sorry, component availability in terms of your comfort level.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Yes, we have a pretty good line of sight through the next couple of quarters and being able to fulfill our demand. And we're still working on making sure we have a supply secured after that, but the benefit of our sourcing strategy and our common componentry is that, a, we don't have to secure that many different SKUs, which is good, makes it a lot simpler; and b, for each SKU, we order a lot more of them. So they're more important to our suppliers.

So that gives us a fair amount of leverage in terms of trying to get to the front of the list when it comes to getting supply. So our team's working extremely actively and they have very good tracking and all this kind of stuff. So we don't take all of that into inventory, as that would build up our inventory. Our working capital needs a lot, but we secure it and as far as how far out we're good, we're good out a couple of quarters and are trying to finish that up through the end of the year. So we're feeling pretty good about it.

Scott Wallace Searle - *ROTH Capital Partners, LLC, Research Division - MD & Senior Research Analyst*

Got you. And last, if I could, Oak, you answered a lot on the competitive landscape, but SmartSky has certainly made a lot of headlines talking about their IP and intellectual property position. I'm wondering if you could just quickly address, are there any concerns that you have related to your IFC solution and its ability to operate in a 5G environment, handoffs or otherwise, that has any concern for you as it relates to the patent position?

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Yes, we're not concerned. I mean, we study every one of their patents in a lot of detail, make sure we understand them, and we don't believe that they have any valid patent that we could be found infringing upon. Now, they do have patents that we don't think are valid, because they've ignored prior art. But that's a different issue. So we have more patents than they do, if you want to know who's got the biggest patent list. We do, we have 349. We've been in this business a very, very long time. And we've been thinking about a lot of different ways to do ATG for a very, very long time. And there's nothing they're doing that we haven't already thought about. Yes, I'll put it that way.

And you know, the thing that Mark's guy did that was smart early on, and we did it also, was figure out how to access unlicensed spectrum. And they have this, it's a regulatory loophole, I'll call it, that allows us to use regularly unlicensed spectrum. And we can do the same thing. If you can't patent regulatory loopholes, because that's about the most original thing they've done. So back to the patent front, we're not concerned. They may find that the only way that they can convince investors that they have something that's monetizable is to sue us over intellectual property. But I think that would be a mistake on their part.

Scott Wallace Searle - *ROTH Capital Partners, LLC, Research Division - MD & Senior Research Analyst*

Great. Congrats on the quarter.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Thank you.

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

Thanks again, Scott.

Operator

Your next question comes from the line of Simon Flannery from Morgan Stanley.

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

You've talked about the number of planes growing 400 a year, and the opportunity to get into some of the smaller planes that we were talking about. So how does that influence your thinking on what happens to DARPA? You've got the data growth continuing. You've got some of these new unlimited plans, but what are all the puts and takes on that over time? And then, thanks for the free cash flow guidance. How do you think about what you will spend that hundred million plus on over the next few years, balancing between paying down more debt, strategic investments, M and A, return of capital? What are the priorities as you get into 23 and beyond?

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

Yes, Simon, I'm happy to take the -- on ARPU, you asked about the puts and takes. There are several drivers there, a couple that will push that up over time. And one that may reduce it over time. So first, people tend to move toward more unlimited plans. So we have seen that progression over time. They want to have predictability in their bills. They want to have access to the full services. So that's one thing that tends to lift DARPA.

The second one, over time, is clearly 5G. Because of the enhanced performance of 5G, we're very confident we'll be able to press that at higher levels, reflecting that value. So that would lift DARPA over time as that 5G network is deployed.

On the downside, as we get into smaller aircraft, they tend to spend less as you'd expect on a monthly basis. But having said that, the price per megabyte is still attractive, and that's a very under-penetrated market. So that presents a really attractive market for us. So it makes sense to continue to go after that market, but we do expect ARPU to raise over time. Particularly as you look at the deployment of 5G.

On the uses of cash, on the hundred million dollars of free cashflow, our first priority is to continue to deliver. So we've made a major step forward on that with the sale of CA and then using those proceeds to pay down debt. We still want to continue to deliver. And then out over time, we'll have to evaluate that when we get through the full deployment of 5G and as we are generating cash, we'll see what those priorities are. But, it puts us in a great position to be able to even frankly, think about those decisions at this point.

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

And what is that end-state target leverage, do you think, Barry?

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

Yes, we haven't really set that, but we will look at that as we continue to unfold the business. And as I said, get on the other side of the 5G deployment. But we'll take a careful look at how to balance leverage against shareholder returns and come out with something probably more specific as that unfolds over time. But right now we haven't set that. There's not a decision to make at the moment.

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

Great.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Simon, we don't see a need to lock ourselves into something when we don't know what conditions will be 18 months from now. Let's wait and see. In terms of the investments, the opportunities that we sort of have on the drawing Board are much lower investments than 5G. So I don't want people to think that we're looking at those kinds of heavy lifts again. And our requirements for those are that they give us significant competitive advantages, and that they have a very high return on invested capital. So we're going to have a pretty high bar on investments.

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

And Simon, I would just add one piece on the ARPU question too. As you know, we talked about revenue growth annually of at least 10%, and that's split between additional planes coming online, round numbers about 8% of planes coming online, additional aircraft online, about 3% ARPU growth over time. So that's basically the mix. And historically, those 2 things have obviously been the drivers of the improved revenue over time, also.

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

I missed that, 30 then you're on the ARPU, or is that more as the 5G kicks in?

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

Yes, it does step up when 5G, kicks in because that is really a step function in the increase in ARPU. But if you look at it on a compound basis, it's the 3% number.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

And Simon, just to make it really clear, yes, we will have more customers with lower ARPU than the average, and we're going to have more people above, but it's all going to drive growth for us. And as Barry points out, on per megabyte basis, it's going to be very profitable. So that's why the overall ARPU number only goes up at 3%. But you've got growth at both ends of the curve, so.

Operator

Your next question comes from the line of Louie DiPalma from William Blair.

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

I just have one quick one since it's already 8:37, but in terms of your future plane growth, how much of your growth is expected to come from retrofits versus line-fits. And related to this, over the past year, do you have an estimate for how many of your ATG system shipments were to the OEM channel versus the aftermarket dealer channel?

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Yes, generally speaking, it's about 60% aftermarket, 40% OEM. Barry, you have it for the most recent quarter of the year. It's been more heavily aftermarket recently.

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

Yes. So if you look at it historically and kind of a go forward basis, Louie, the OEMs as a percentage of ATG equipment revenue in the fourth quarter was, as Oak said, skewed more in the 20, 25% range for OEM. In the first quarter, it was about 40% OEM. And as we look at it on a go-forward basis, if the OEM percentage we'd expect to be in that kind of 30 to 40% range.

Operator

And there are no further questions over the phone line at this time. Presenters, you may continue.

Oakleigh Thorne - *Gogo Inc. - Chairman, President & CEO*

Well. Okay. This will conclude our call for today. Thank you everyone for your participation. Bye-bye.

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

Thanks all. Take care.

Operator

Thank you for today's conference call. Thank you for participating. You may now disconnect. Have a great day.