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IRDM - Q4 2015 Iridium Communications Inc Earnings Call

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PRESENTATION

Operator

Welcome to the Iridium fourth quarter 2015 earnings conference call. My name is John and I'll be your operator for today's call. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session. Please note this conference is being recorded. Now, I will turn the call over to Ken Levy. You may begin.

Ken Levy - *Iridium Communications Inc. - VP, IR*

Thanks, John. Good morning and thanks for joining us. I'd like to welcome you to Iridium's fourth quarter 2015 earnings call. Joining me on this morning's call is our CEO, Matt Desch; and our CFO, Tom Fitzpatrick. Today's call will begin with a discussion of our fourth quarter results followed by Q&A. I trust you've had an opportunity to review this morning's earnings release, which is available on the Investor Relations section of Iridium's website. Before I turn things over to Matt, I'd like to caution all participants that our call this morning may contain forward-looking statements with the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are statements that are not historical fact and include statements about our future expectations, plans and prospects.

Such forward-looking statements are based upon our current beliefs and expectations and are subject to risks, which could cause actual results to differ from the forward-looking statements. Such risks are more fully disclosed in our filings with the Securities and Exchange Commission. Our remarks today should be considered in light of such risks. Any forward-looking statements represent our views only as of today and while we may elect to update forward-looking statements at some point in the future, we specifically disclaim any obligation to do so even if our views or expectations change. During the call, we'll also be referring to non-GAAP financial measures. These non-GAAP financial measures are not prepared in accordance with the Generally Accepted Accounting Principles. Please refer to today's earnings release and the Investor Relations section of our website for a reconciliation of these non-GAAP financial measures to the most directly comparable GAAP measures.

With that, let me turn things over to Matt.

Matt Desch - *Iridium Communications Inc. - CEO*

Thanks, Ken. Good morning, everyone. Let me start by saying that despite a challenging macroeconomic environment in 2015, our team executed well to meet our full-year guidance. We delivered 2% total service revenue growth and 8% growth in operational EBITDA. Tom will share more detail on these results shortly. I want to begin my remarks with an update on the Iridium NEXT program and then comment on recent activity in our business lines. We're looking forward to launching Iridium NEXT satellites this year, but as you saw in our press release this morning, we've had



to change our launch plan. I want to first say though that Thales Alenia has made good progress in all the technical aspects of our satellites and has remained on schedule with the plan we communicated during our third quarter call.

The issues Thales had with VSAT Ka-band modules appear to be resolved and both the hardware and software are well tested now giving us confidence that our satellites will perform effectively in orbit. Thales is wrapping up qualification on our first two satellites and these will be complete as scheduled next month. Overall, satellite production is steadily rising with about 12 vehicles in various stages of the manufacturing process and Orbital ATK is ramping resources to be able to produce six satellites per month by July helping to ensure that our satellite vehicles will be delivered as needed for each launch scheduled this year. As for our launch schedule, unfortunately Kosmotras informs us that they have not yet received the necessary approvals from the Russian Ministry of Defense, one of the final steps required to launch our satellites from Yasny.

Administrative paperwork was submitted to the MoD some time ago and Kosmotras has been unable to get any feedback on the timeline for sign-off. This is very disappointing as our satellites will be ready and the space head module that holds the satellites on the rocket is complete and already delivered to the Yasny launch site. We've also heard that we're not the only Dnepr launch awaiting approval. There's at least one, a Spanish launch, in the same situation. Given the lack of a firm schedule from Kosmotras at this time, we've made the decision to move forward with the new launch plan. Kosmotras will continue to work on obtaining approvals, but we will not jeopardize the timeline for the Iridium NEXT program. Our first launch has now been confirmed for SpaceX Falcon 9 and we'll consider scheduling the Dnepr launch at a later time when Kosmotras is ready.

We're fortunate to be working with SpaceX as our primary launch provider as they have been very flexible and have agreed to pull forward our initial SpaceX launch from August to July as satellites for the launch will be ready to ship to Vandenberg in June. This will have the effect of moving our first launch out by three months from April on Dnepr to July on SpaceX. This first SpaceX launch will carry 10 satellites rather than the two planned for the Dnepr launch. The remainder of the SpaceX launches would follow our current schedule with the second Falcon 9 rocket launching three months later in October and subsequent launches with SpaceX following approximately every 60 days thereafter. One nice thing about this plan is that it still completes the entire Iridium NEXT constellation in 2017 as scheduled.

I know this new launch plan will prompt some questions as to how this change impacts the Iridium NEXT mission in our corporate outlook and I can state that from a subscriber and investor standpoint, the answer is very little. First, this change does not require any modifications to our credit facility or any regulatory approval. SpaceX has been a great partner, has signed off on this plan, and will be ready to launch in July. Second, a shift in our first launch to SpaceX does not significantly change our cost estimates for the Iridium NEXT mission. Tom will talk about that more in a minute. Third, as I said, the overall launch plan to complete our network in 2017 remains intact. We will feather in the Dnepr launch when Kosmotras is ready and still have our entire constellation operational in 2017. You'll note that the sequencing of events now provides for a three-month period of testing and evaluation of the first satellites launched.

I know we previously planned for a four month test period following our first launch, but this was not a requirement of our testing plan nor of our credit facility. From the perspective of our engineers, a three-month period for testing and evaluation is more than sufficient to adequately assess the health and functionality of our satellites in advance of our second launch in October, particularly given all the extra time we've had on the ground for thorough hardware testing and the considerable additional maturity of software releases we've been running that will be on the satellites. Clearly changing our launch plan is not the news we expected to be sharing so close to our April launch date. However, we have responded quickly to the events as they unfolded and put in place a solid plan on which we can execute to keep the overall program on track for completion in 2017.

Moving on to our business results, 2015 came in much as forecasted. We achieved our 2015 total service revenue and operational EBITDA guidance and remain on target to achieve our long-term financial guidance. I'm particularly proud of how my team navigated the global economic headwinds and FX pressures of this past year. These forces have impacted so many companies in recent quarters and our results are a testament to the quality and execution of our talented staff. While we don't anticipate a significant change in the operating environment in 2016, we have considered these headwinds in developing our guidance for the year. Aireon continues to gather momentum in advancing global aviation surveillance and signing new customers.



In the fourth quarter Aireon signed a 12-year data services agreement with South Africa based ATNS, which provides air traffic surveillance services for two flight information regions covering approximately 10% of the world's airspace. In the last few days, Aireon also signed a similar agreement with the Civil Aviation Authority of Singapore, their first Asian airspace win. These are more validating data points for Aireon and we continue to believe that Iridium's investment in this venture will be a meaningful source of value creation for our shareholders. To date, Aireon is actively engaged with ANSPs covering almost half the world's airspace and two-thirds of the world's oceanic airspace. This is fantastic progress given the service hasn't even launched yet.

The FAA is also moving in the right direction by making preparations to test and validate space-based ADS-B data from Aireon and working through their procurement decision for their reduced oceanic separation program. Based on their progress and continued momentum, we believe the FAA use of Aireon data is a matter of when not if. Aireon's existing satellite network continues to perform well and delivered an excellent user experience with some of the highest availability numbers we've seen in recent years. On that performance, our subscriber base rose 6% in 2015 topping 782,000 users bolstered by a record 20% growth in our government business. Commercial ARPU declined modestly reflecting the recent pullback in oil and gas and continued strength in the dollar, both of which weighed on usage rates. Our new push-to-talk offering is getting a great reception since its recent introduction.

Our partners in the field who have been testing and using the product are very happy with its capabilities and versatility. PTT caters to new commercial and government users that require the ability to communicate instantly across a defined group of users. Given PTT's unique capabilities, we're seeing interest from public safety agencies to industrial users to governments around the world. We're very excited about this technology and see it as the key area of demand for Iridium. Moving to M2M, Iridium continues to be well positioned in this growing industry. Not only did M2M subs again climb at a double-digit clip in 2015, but we've also continued to sign up important new distribution partners and innovate to provide solutions for their customers. We are currently in the process of rolling out new direct drop in replacements for our small form factor M2M transceivers, which are even more energy efficient and importantly [less costly] to produce.

These improvements coupled with the reliability of our satellite network have made Iridium the provider of choice for mission critical data and telemetry. In 2015 we made strong inroads with heavy equipment OEMs and are looking to extend our position in this space in the broader IoT world in 2016. Slowdowns in specific industries like oil and gas and mining this past year meant that we didn't grow quite as fast as we would have liked, but we feel that we've laid the groundwork for better growth in 2017. In maritime, Iridium Pilot continues to be a good product for us and we expect the GMDSS certification which is proceeding as we expected will expand our addressable market when finalized and give our new Iridium Certus broadband providers another important offering for the tens of thousands of SOLAS class ships.

Regarding Iridium Certus, we're making good progress on the development of this high speed capability and our licensed terminal partners are busy working on new Certus products, the first of which should roll out as early as the end of this year. This competitive global broadband service will offer our partners a unique multiservice product with transmission speeds ultimately up to 1.4 megabits per second after Iridium NEXT is fully deployed. Iridium Certus enhances our competitive position in maritime and also allows us to offer new service capabilities in aviation and terrestrial applications as well. One new service I'd like to call your attention to is called Satellite Time and Location or STL for short. With our partner Satelles, we will soon launch a new trusted time and location service on our network to customers that are dependent on accurate tracking and coordination of assets and data.

The service improves the reliability of GPS data both outdoors and in-building and enables new services that can help fight cyber attacks and authenticate computer users and it's a service that can only be delivered from Iridium's unique network. Revenues from this venture will approach \$1 million this year, but could be 10 times that in 2018 with our partner's successful execution and based on the many opportunities on which we are currently collaborating with them. Finally, Iridium closed 2015 with meaningful subscriber growth and new task awards from the US government. In the fourth quarter, we reached a record 72,000 government users under the EMSS program and also closed \$10 million in task awards including the contract with General Dynamics Mission Systems to create a new next gen secure handset for the US DoD.

This R&D will allow us to bring the latest technology as well as lower costs to the DoD as the only provider of a satellite phone accredited by the NSA for Type 1 encryption. We're really pleased with the ongoing relationship we develop with our largest customer and believe that government subscriber growth illustrates the increasing importance of Iridium as a strategic partner to DISA and supports our view of an expanded relationship with the US government upon contract renewal in 2018. So, 2016 will be seminal year for Iridium and touch off a new chapter of industry leadership

and business growth for our Company and our services. This year we have a series of launches for Iridium NEXT, which will begin to provide our expanding roster of business partners and customers with new satellite capabilities and services to enhance their productivity.

With that, I'll turn it over to Tom for a more detailed financial review. Tom?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

Thanks, Matt, and good morning everyone. I'll get started by summarizing our key financial metrics for the fourth quarter and provide some color on the trends we're seeing in our key business lines, then I'll walk through our 2016 guidance and long-range outlook, and wrap up with a brief review of our balance sheet and our placement of launch insurance. Iridium reported total revenue of \$106.4 million in the fourth quarter, which was up 6% from last year's comparable period. Strong performance in government services accounted for much of this gain while commercial services were also positive year-over-year. Engineering and support revenue was up a solid 33% from last year's period and reflected increased scope of work on government sponsored projects. Operational EBITDA remained strong at \$56.8 million, a 10% increase from the prior year's quarter.

Lower product warranty cost and cost improvements complemented good topline revenue this quarter. Our operational EBITDA margin also strengthened to 53% in Q4, up from 52% in the year-ago period. From an operating viewpoint, we reported commercial service revenue of \$61.3 million in the fourth quarter. This was slightly ahead of the prior year's quarter and is indicative of Iridium's strong market position even in the face of a prolonged pullback in the energy market and continued foreign exchange pressures. In 2015 the dollar strength restrained international sales especially in key markets like Canada, Australia, and Europe where a strong US dollar acts as a price increase to international customers and reduces their purchasing power. Though our commercial subscribers grew 5% year-over-year, net commercial subscribers fell by 2,000 during the fourth quarter with the loss coming entirely from our commercial voice and data business.

The macroeconomic climate has also affected commercial M2M, but this segment of our business still grew at a positive rate. Commercial M2M added 7,000 data subscribers during the fourth quarter and subs were up 10% for the year. M2M now represents 51% of billable commercial subscribers, up from 48% in the year-ago period. Turning to our government services business, we recorded revenue of \$21.1 million this quarter representing 20% year-over-year growth. Our footprint with the US government continues to expand with government subscribers growing 20% year-over-year to a record 72,000 total users this quarter, up from 69,000 in September. As Matt mentioned, Iridium was also awarded a multi-million dollar contract with General Dynamics to provide a next generation secure handset for the US DoD. This is a noteworthy development as Iridium approaches EMSS contract renewal discussions.

In equipment, we realized revenue of \$17.1 million, which is in line with our expectations and essentially flat to the prior year's quarter. Similar to the third quarter, equipment margins expanded in the fourth quarter to 46% compared to 29% in the fourth quarter of 2014. We continued to reap benefits from improved equipment performance, a decrease in Iridium OpenPort warranty provisions, and lower manufacturing costs on certain product lines. These manufacturing efficiencies should stay with us in the foreseeable future. Looking to 2016, we expect that equipment margin will remain in the low-to-mid 40% range. Engineering and support revenue was \$6.9 million in the fourth quarter, up meaningfully from \$5.2 million in the prior year's quarter. The increase was principally driven by several new projects that kicked off in the fourth quarter.

I should also point out that we took a non-cash charge for goodwill in the fourth quarter. This charge is calculated in accordance with ASC 350 and entirely relates to the relationship between Iridium stock price, market capitalization, and the implied fair value of our goodwill. This charge has no operational relevance. Moving now to our financial outlook. We issued 2016 full-year guidance this morning. We forecast total service revenue growth of between 4% and 6% this fiscal year and operational EBITDA of between \$245 million and \$255 million. This compares to service revenue growth of 2.5% in 2015 and operational EBITDA of \$234 million. I'd like to walk you through some of the elements supporting this outlook. First, our government business will be a strong revenue generator in 2016. This should more than offset the sluggishness in our commercial services segment.

We're coming off a record year of growth in our government segment and 2016 will reflect the full-year step-up of our five-year EMSS contract with DISA. As a result, revenue from this contract will rise by approximately \$13 million or 17% for the full year. Second, we expect that the sluggish global environment that impacted 2015 will carry over into 2016 and pressure service revenue growth. Commercial voice and data revenue

contracted by 3% in 2015 on the back of macroeconomic headwinds and the devaluation in the ruble. We expect better comparative performance in 2016 despite no anticipated improvement in the macroeconomic environment. This improvement is driven by a somewhat lessened effect from the ruble devaluation, which represented an approximate \$3 million headwind to sales in 2015.

Also supporting our expectations for improved performance is growth in our commercial push-to-talk offering, which launched in 2015.

Push-to-talk has received a strong reception from our customers and we expect it to contribute meaningfully to revenue this year. In our M2M business, we see solid double-digit growth in subscribers continuing in 2016. As previously mentioned, we proactively renegotiated certain contracts with the service providers in the oil and gas and fishery segments, which lowered prices for specific accounts. These actions will serve as a headwind on 2016 M2M revenues and likely keep our growth rate in line with 2015 results. We expect M2M growth to accelerate in 2017 as these headwinds abate and as we continue to see ongoing growth particularly from heavy equipment manufacturers.

Also contributing to our EBITDA growth in 2016 are a handful of task orders and government related contracts. We estimate that these items will account for more than \$10 million in engineering and support project revenue. Today we are also affirming our long-range outlook. Looking forward, we continue to expect total service revenue of between \$420 million to \$465 million in the full year of 2018. There are a number of factors that give us confidence in this revenue forecast. First, our government services remains a growing business segment for Iridium. As I mentioned earlier, revenue from our EMSS contract will increase in 2016 to \$88 million and remain at this level through three quarters of 2018, at which point we would expect to be in a new contract. We expect that the new contract will provide significant benefit to DISA and incremental revenue to Iridium.

Now in light of strong 20% subscriber growth we achieved with this customer in 2015 and the significant investments DoD is making in our new network infrastructure, we are quite comfortable with this outlook. Two, we forecast close to \$50 million in hosted payload revenue in 2018 based upon terms of our contracts with business partners Aireon and Harris. Beginning this year, we will start to recognize revenue from monthly hosting and data fees based on each of the 66 operational satellites in the Iridium NEXT constellation as they come online. With Iridium NEXT expected to be in operation by 2017, 2018 revenues would only be significantly impacted in the event of a material delay beyond our current schedule. And three, new products are an important component of our long-term revenue growth.

We're very excited about the rollout of Iridium Certus and Satellite Time and Location as well as the traction we're seeing from our commercial push-to-talk offering. We anticipate that Iridium Certus will be fully operational by 2018. With significant industry growth in maritime and aviation tied to broadband services, Iridium [Certus] could generate up to \$100 million in revenues by 2020. We believe that incremental revenue will be realized prior to fiscal 2018 as we begin the installation for Iridium Certus user terminals. Push-to-talk is quickly gaining momentum with customers as well as through the 15 service partners we signed up to develop new applications and expand distribution. We expect large equipment orders with each customer sale as satellite based PTT is a group based offering which has regional and global appeal.

The other components of our long-range outlook which we are also affirming today include expectations for operational EBITDA margin of approximately 60% in 2018, negligible cash taxes through approximately 2020, peak net leverage between 6 times and 6.5 times in 2016 fiscal year, and finally net leverage of approximately 4 times in 2018. Moving to our capital structure and liquidity position. As of December 31, 2015 we had drawn \$1.5 billion from the COFACE facility and had a cash and marketable securities balance of approximately \$389 million. In 2016 we anticipate total capital spending of approximately \$700 million, including approximately \$80 million of capitalized interest. This reflects continued work on Iridium NEXT and the underrun of payments to Thales Alenia in 2015, which essentially pushes right into our 2016 spending plan.

Finally, our placement of launch insurance continues to proceed smoothly. We have bound over 90% of the insurance on our first two SpaceX launches and continue to work these placements. We plan to be 100% bound on these first two launches three months prior to the first SpaceX launch in July. Given the change in the sequencing of the Dnepr launch, we now expect our insurance costs will immaterially exceed the high end of our quoted range of \$125 million. We view this as very manageable. In wrapping up my thoughts, I want to reiterate that Iridium NEXT remains on schedule to complete full deployment in 2017. We are weathering the current economic climate and our business is performing as expected. We are fortunate to have a diverse revenue stream and a strong product platform, which will allow Iridium to grow EBITDA into 2016 despite pronounced macroeconomic headwinds. We look forward to the commencement of our launch program in the coming months.



With that, I'll turn things back to the operator for the Q&A portion of this morning's call.

QUESTIONS AND ANSWERS

Operator

Thank you. We will now begin the question-and-answer session. (Operator Instructions) Andrew Degasperi, Macquarie.

Andrew Degasperi - Macquarie Capital (USA) Inc. - Analyst

First question, obviously this launch of the first two satellites delays things, but I guess what was the purpose of the first launch? Can you maybe help remind us what were you planning to do with those two and maybe let us know in the long history of LEO orbit constellations has this normally been done? Have they launched 10 satellites first at this rate, if you can just comment on that?

Matt Desch - Iridium Communications Inc. - CEO

There's not a lot of history on LEO. LEO constellations, most of that history is our own and the last time we did this 17 years ago or at least our predecessors did it, there was a much more complicated program with three different launch vehicles over three continents with something like 12 or 13 launches over a period of less than 12 months. So, this is a lot simpler and more straightforward approach than we certainly did the last time. Just a little history. Our original plan which we announced six years ago or so on which we developed our program was only to launch on SpaceX and at the time, they thought that the Falcon 9 could handle nine satellites per launch and we were going to have eight launches of nine satellites to make up 72. When we realized that the Falcon 9 actually could launch a heavier load than that, we expanded that with their support to 10 satellites per launch and saw the Dnepr rocket, which if you remember six years ago you were all quite nervous about SpaceX.

We had a very reliable launcher that could launch two satellites and so we signed up with that and added that to our program and slotted it in at that time as the first launch. These are all operational satellites, but thought that it would work out well to launch first two and then we would launch the remainder on the seven Falcon 9 launches. That's been the plan up until literally days ago. Started getting the feeling in December, January as Kosmotras kept telling us that things would be imminent, we'd find out any day now and we kept saying why not, there's not a lot of information coming out of it. But really we just made the decision recently because we just didn't want this kind of uncertainty in our program given our focus on completing the network on schedule.

So, we've really just made the change now to move those first two later in the program or maybe even to the end as the final two spare satellites, we'll see. It doesn't really change a lot. It's a good thing we have a great flexible partner in SpaceX who could move that first launch up a month so that we can still be launching here in five months instead of in two months and really get right back on track with our launch program overall. So, is this normal? I don't know. There's not many people that launch LEO constellations and really how many satellites are launched each time is really a function of the weight of the satellites and all that sort of thing. But this isn't that big of a change really from our overall plan, in fact in some ways it's getting back to the original launch program that we originally started with.

Andrew Degasperi - Macquarie Capital (USA) Inc. - Analyst

And just a follow-up, what are the puts and takes in M2M for 2016 that you see? I mean I know a lot of heavy equipment OEMs are hurting, but it seems yours is still a penetration game. Can you maybe let us know what sectors are you seeing growth and what are sort of dragging?



Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

So, one of our biggest service providers is very heavily oil and gas. That's a big negative. It was a negative in [2015] on the back of deactivations. We proactively renegotiated that contract and have said that we saw that as a 2016 headwind. Similarly we've seen some price competition on the margin and most notably in the fishery segment and similarly we've renegotiated a couple of those contracts. So those were the sectors really, it's oil and gas most pronounced and in the fishery segment kind of contract renegotiation. To the contrary, heavy equipment OEMs notwithstanding their business issues, telematics being adopted by heavy equipment manufacturers is an opportunity for them to get more efficient. So, we don't think heavy equipment is a drag. It's ramping a little bit slower than we would have expected, but we have an excellent head of steam there and look for additional announcements of big contract wins there. We feel very good about heavy equipment as a source of growth long term.

Matt Desch - *Iridium Communications Inc. - CEO*

Broad based, remember heavy equipment is all kind of upside to us because we hadn't had any exposure to that segment. So, we're still seeing penetration of that market. It takes time for those companies to ramp and so some of the early contracts we had are only starting to come online in 2015 and 2016, but we're going to continue to see that expand. To add to what Tom said, the personal communicator space has been a very good one for us, there's been some good growth there. I was really pleased to see DeLorme get acquired by Garmin, I think that will only help really in terms of sort of global distribution of that product set.

But really we're having a lot of our partners are growing in the M2M sector, in lots of other smaller sectors; but we just had this heavy exposure at the top of our partner list to the energy sector that sort of weighed down this last year. But I think that effect overall gets diminished as it sort of washes through and the other parts of the M2M industry continue to grow particularly as we get more into 2017, 2018 and we really get the heavy equipment OEM space moving and some of these other technologies in areas that are adopting satellite along with cellular technologies for their space.

Andrew Degasperi - *Macquarie Capital (USA) Inc. - Analyst*

Great. Thank you.

Operator

Chris Quilty, Raymond James.

Chris Quilty - *Raymond James & Associates - Analyst*

Just a follow-up on that heavy equipment issue, it sounds like there's been continued delays. Did you actually get any shipments into OEM customers this year?

Matt Desch - *Iridium Communications Inc. - CEO*

In fact 2015 started to ramp, 2016 will be a better year than 2015 in terms of growth. I mentioned in the past it's hard to announce new wins in this sector because a lot of people like to keep their plans under wraps. So, it's continued to be positive in terms of the interactions and move towards additional OEMs. The trials and demonstrations and technology implementation plans continue on in a number of different companies and I think that they're going to be more falling here in 2016 towards our way. By the way, one point I didn't mention too to Andrew's discussion in the last one. Another potential area of growth for us really is and maybe it's bit more of a market share area, but we still do see a lot of opportunity in what really kind of comes out of the SkyWave acquisition. There seems to be a lot of interest now in diversification in that space that probably we didn't see as an opportunity two or three years ago because we sort of thought it was solidly in a legacy mode with a competitor. But now there's some



pretty major players in that space too that could add significantly a little bit in 2016, but mostly 2017, 2018 are going to be, those are nice growth areas for us as well which we're excited about.

Chris Quilty - *Raymond James & Associates - Analyst*

Tom, following up, can you run through again the dollar contributions that you mentioned regarding hosting fees and timing? And can you give us any update on your expectation that you will receive a one-time hosting fee late 2016, end of 2017 and what the sort of triggers for that are?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

So think the [pot] as approaching \$50 million, I think we quoted \$47 million between data and hosting and that revenue comes in as the satellites get launched. So, there's 66 operational satellites and it comes a very little bit in 2016, 2017, and it'd be the full amount in 2018. There is no triggers. Harris is contracted and it's a contract with Harris. The contract with Aireon, Aireon has said that they intend to get a FAA contract kind of in the latter part of this year and go to market and raise capital and that's how they'll pay us in late 2016 and 2017. In any event, Aireon has made tremendous success and tremendous progress in signing multiple accounts, most recently in Singapore. So, we're highly confident in the collectability of that receivable and so that revenue will be recognized for GAAP.

Matt Desch - *Iridium Communications Inc. - CEO*

Chris, I might want to add to that. The FAA is very, very important to that obviously. But I would say with these growing numbers of contracts from all these other companies around the world, we're seeing really Aireon generating potential significant non-FAA cash flow around the world and that really, as Tom said, gives us a lot of confidence that they are going to have a revenue stream with these 12-year kind of deals that they could raise debt on.

Chris Quilty - *Raymond James & Associates - Analyst*

Obviously they're going to be able to raise debt much cheaper with an FAA contract, but is there a contractual requirement by Aireon to pay you by a certain date that might force them to raise more expensive debt with the contracts in hand if the FAA continues to delay?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

So, there is a contractual receivable and it bears interest. So, a certain amount of the \$200 million is due and payable currently and it's bearing interest. I don't know that we have disclosed the exact terms of the agreement between Aireon and I really would have to check that, Chris, I don't think we're public with that. What I will say is Iridium is highly confident about the collectability of the \$200 million. To the point where that revenue will be recognized for GAAP, we've done that analysis.

Chris Quilty - *Raymond James & Associates - Analyst*

Okay. And can you give us an update on what you're seeing in the maritime part of the market; Pilot, OpenPort not M2M?

Matt Desch - *Iridium Communications Inc. - CEO*

It's a moving turf. First of all, as you know that product had some problems a couple years ago. I would say that those now not only have been confirmed to be completely resolved, but the perception of the product has really turned around in the industry. I would say our partners are extremely comfortable putting it out there either standalone or as a companion to a VSAT unit and in fact there's a lot of competitive dynamics still created primarily by Inmarsat and their push to the market that encourages people to want to use Pilot in conjunction with other products.



So, we are in a transition period right now I would say so we're not exactly sure how we'll go. We're not forecasting necessarily growth at this point though I would say the last couple of months have been very encouraging and we'll see how that develops over the coming months if we can maintain that kind of positive momentum in that area and if we do, then I think that that will even contribute even more.

But really frankly I'm pleased overall that it's back in the market and that we have a product that's solid. Also though I would say there's an awful lot of activity in the maritime space around Iridium Certus. The new products that will come starting near the end of this year and with sort of a commercial introduction in the maritime space in 2017, that could start generating revenues on an even faster product that delivers more capability, ultimately things like GMDSS. But also not just high speed, but can also maybe support PTT services, can support M2M type services, all on the same kind of terminals. There seems to be a lot of enthusiasm and excitement about a product that really would be the most cost competitive as well as actually the fastest products in the L band space as it relates to standalone or companion product to VSAT system. So, I really think while we're going to do just fine this year in the maritime space; 2017, 2018 look very bright to me in terms of our potential in maritime.

Chris Quilty - *Raymond James & Associates - Analyst*

Got you. Thank you very much.

Operator

Andrew Spinola, Wells Fargo.

Andrew Spinola - *Wells Fargo Securities - Analyst*

Wanted to ask a question on the ARPU in the M2M business. You had a tough compare in 2015 and I think that's mostly sort of cycled through. So I'm wondering you've said that there should be a little bit of pressure on that going forward as the market expands and you go into lower end solutions in the mix, but do you think we could see something maybe more along the lines of like low-single digit declines in M2M ARPU in 2016 or what does the outlook look like for that?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

As we've said for some time, we see the ARPU in M2M as a downward sloping line. What happened to us in 2015 was it was more pronounced and that's oil and gas. One of our biggest providers had deactivations of high-end ARPU customers and so that was a deact and we continued to grow personal communications with DeLorme et cetera. So, what we had was the subs that were coming on were sort of single-digit ARPU and the subs that were exiting were higher ARPU in oil and gas. So, that's what happened to us 2015. 2016 will be down, I don't know it will be single-digits. I don't see it as pronounced as we saw in 2015, but there's still macro pressure there, Andrew.

Andrew Spinola - *Wells Fargo Securities - Analyst*

And another sort of data point question. On the net subscriber losses in voice and data, looks like you typically lose subs in Q4. Is that something related to non-pay disconnects or just the timing of contracts and maybe just a little color on why the bigger loss this quarter?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

I think it's macro. I think if you trend handset sales, handset sales are down, that aligns with sub gain. And so you're right fourth quarter is typically seasonally low, but it's more so because of macro effects we've discussed.



Matt Desch - *Iridium Communications Inc. - CEO*

We've always talked about the fact that our system is primarily used outdoors. Subscribers and applications are a little bit more oriented towards the northern hemisphere than they are in the southern hemisphere winter not just fourth quarter, first quarter typically are slower times and I think as we've gotten larger, that's even gotten a little bit more pronounced. And then it ramps up again in more of the second and third quarters. So, I think it's a normal activity that kind of happens to the M2M industry and to us really.

Andrew Spinola - *Wells Fargo Securities - Analyst*

A very high level question, Matt. It's certainly very interesting that DeLorme was acquired by Garmin, obviously a order of magnitude bigger unit shipments at Garmin than DeLorme, but kind of wondering when I'm thinking about maybe where Garmin goes with that and what types of products they ultimately add satellite communications to. Can you give us a sense of what the cost of adding satellite communications to a device is these days and maybe what the outlook is over the next five years? Is there any possibility that that comes down significantly and we see Garmin start adding this to lots of different types of devices?

Matt Desch - *Iridium Communications Inc. - CEO*

My initial enthusiasm and excitement about the acquisition of DeLorme is more in what I would call distribution expansion because DeLorme was a small company who was executing extremely well, but was still very North American oriented and had started to penetrate in some other markets; certainly it was in Canada, it was a little bit in Europe, and very small amount in places like Australia, et cetera. But Garmin is a global company with global distribution and a brand that is well recognized around the world and they could, I think fairly rapidly we'll see, integrate the growing product line that DeLorme had in other markets that we hadn't seen before. So, that's immediate positive.

As far as satellite, I think is getting into a lot more devices and really the tax, if you will, to put satellite I know five or six years ago was hundreds of dollars; maybe \$150, \$200 in a lot of cases. Now we're talking tens of dollars and in fact when you really talk about chipsets except for a power amplifier which is probably a little bit more expensive than the threshold version that's sort of the more gating factor, all the other stuff really doesn't add that much necessarily to a device. So really the cost of putting satellite is lower and if someone wants to put that into a lower cost consumer like device, it becomes more possible. That's still not going to be. I think though that the goal will be a bit more about adding speed and capability to devices as opposed to necessarily I think in a pure M2M space there'll still be a very low cost, low bandwidth, low space.

But I think as we add Iridium Certus capability, which I know we often talk about the high speed and broadband aspects of it, but it really provides a product line that goes all the way from low to high speed but in a very low power small antenna range can give a number of tens of kilobytes per second, which adds a whole lot of value to a very, very low cost device. And I think there will be a lot of interest in embedding that and really basically the same kind of cost point or price point tax, if you will, as we see with technologies today. So, you get a lot more for the same price. All that being said, could we see that? I think that's up to not just Garmin, but many other companies in the space who are exploring putting satellite in more things, but that's clearly part of our approach and strategy in the world.

Andrew Spinola - *Wells Fargo Securities - Analyst*

Tom, just on the goodwill impairment, what specific acquisitions or businesses is that associated with?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

It's the main business. It relates to the SPAC transaction when the Company came public. Let me just give you the background on that. Under GAAP you have to do a fair value evaluation of your goodwill every year at a measurement date that's determined at the time that the company came public and it just so happens that that measurement date lines up pretty close to the 52-week low of our stock price. If it lined up with the 52-week high, we wouldn't have any impairment. So that's how narrow the rules are and it's very mechanical, you just go through the analysis. I just reiterate



the only economic consequence of this is we won't have to pay the valuation guys every year to do the analysis and so that's a six-digit savings and we're happy about that. Other than that, it doesn't relate to the business whatsoever.

Andrew Spinola - Wells Fargo Securities - Analyst

Your comment on the insurance coming in a little bit non-materially higher than the \$125 million, does that include any associated costs with not having the Kosmotras launch in front of the SpaceX launch or would that create additional increases to the insurance?

Tom Fitzpatrick - Iridium Communications Inc. - CFO & Chief Administrative Officer

That's an all-in number. That's our expectation. That's an all-in number, Andrew. And remember Kosmotras, the reason for that was we're able to eliminate a SpaceX launch. That was the economic benefit of that and then the insurance was a tag along. But the reason for it was if we knocked out, I think there was a net \$50 million savings we quoted on that.

Matt Desch - Iridium Communications Inc. - CEO

And that economic savings remains with the current plan. We still have that so it just changes the sequencing.

Tom Fitzpatrick - Iridium Communications Inc. - CFO & Chief Administrative Officer

The insurance is a trim, it would have been a nice adder, but we still retain the elimination of a SpaceX launch.

Andrew Spinola - Wells Fargo Securities - Analyst

Makes sense. Thank you very much.

Operator

(Operator instructions) Jim McIlree, Chardan.

Jim McIlree - Chardan Capital Markets - Analyst

Can you help me understand how much of the commercial service revenue is coming from Aireon or hosted payloads in 2016? It sounds like hosted payload is going to be close to zero, but does Aireon contribute a meaningful amount of revenue in 2016?

Tom Fitzpatrick - Iridium Communications Inc. - CFO & Chief Administrative Officer

Very small, Aireon contributes. As I said, we view the Aireon receivable as highly collectable and it will generate GAAP revenue very small in 2016, more meaningful in 2017, and then the full amount in 2018.

Jim McIlree - Chardan Capital Markets - Analyst

Okay. I guess I'm trying to understand the guidance on the commercial service revenue, it doesn't sound like things are meaningfully better this year than they were last, but you have a much higher commercial service revenue growth.



Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

Not really. So just look at the guidance, 4% is the government and you just take the government you got the 4% so between 4% and 6% is the commercial. So commercial, as I said in my remarks, the comparative is somewhat better on the back of we had about a \$3 million ruble devaluation. The ruble really fell out of bed in 2015. The comp is down in 2016 versus 2015, but not to the degree so we're going to have pressure, but less than we experienced in 2015. Commercial push-to-talk is the new source of revenue growth. But if you just look at our guidance on commercial revenue, we're not calling for a massive turnaround here.

Jim McIlree - *Chardan Capital Markets - Analyst*

Excuse me, I misspoke, I didn't account for the government properly in my question. And lastly, on the government revenue so the contract ends Q3 of 2018, is that correct? And it kind of sounds like you're positive not just for renewing contracts, but renewing at a higher level. Am I correct on my assumption that you're hopeful that you can get a higher level out of that contract when it expires?

Matt Desch - *Iridium Communications Inc. - CEO*

We're not projecting exactly what we'll be doing. We have a lot of discussions to go through with the government around that, but we have a lot more to offer the government than we had the last time around; brand new constellation, new services, higher speed services new things like Satellite Time Location, there's a lot of interest in the government about PTT and tactical radios are expanding in global. All of that is positive. In addition, I think they are really taking great advantage of the current constellation, current contract to the extent that you can see their subscriber growth is very positive. So, there's really interesting programs that are being developed right now which will really use the network more as well. So, I think it'll be kind of to the extent we get more in this contract, it will be because they get more value and get more capability. So, I mean we feel pretty positive about that whole equation going into that discussion and are even starting to have very preliminary discussions around what that might look like.

Jim McIlree - *Chardan Capital Markets - Analyst*

Okay. That's very helpful. I think that's it from me. Thank you.

Operator

Jim Breen, William Blair.

Erik Rayner - *William Blair - Analyst*

This is Erik Rayner for Jim Breen. I just have a quick question around the long-range outlook. Obviously you affirmed the long-range outlook for 2018 so that implies some substantial acceleration in 2017 and 2018. So, just wondering if you can provide a little bit more color on what gives you confidence that you can attain that service revenue level in 2018 and just some of the puts and takes and timing of new products, et cetera? thank you.

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

As I step through so the biggest slug is approximately \$50 million of hosted payload related revenues from contracts between us and Harris and us and Aireon and that revenue comes in as the satellites are launched and will be \$50 million of revenue that we have 2018 that we don't have currently. We also expect growth from new products, commercial push-to-talk which was launched this year to great fanfare. We're excited Iridium Certus essentially makes us a player like we never have been before in maritime aviation even terrestrially in terms of being able to offer data speeds

that are faster than the competition. That's a whole new game for us and we've quoted \$100 million kind of an opportunity in 2020 and we see some of that revenue in 2018 bolstering our growth. So, that's the kind of --.

Matt Desch - *Iridium Communications Inc. - CEO*

We also mentioned Satellite Time and Location being a significant expansion given our contracts there and the potential for that growth if it's used, we'll generate quite a bit more revenue as a result of that as well. And then of course the government while it's a step-up to 2018, it will stay at this level till that time but we just talked about that as well.

Erik Rayner - *William Blair - Analyst*

Great. Thank you very much.

Operator

Chris Quilty, Raymond James.

Chris Quilty - *Raymond James & Associates - Analyst*

Staying on the DoD subject, you had said last year that you thought there could actually be some upside to the DoD contract beginning this year. Do you still believe that's a possibility and is that included in your forecast?

Matt Desch - *Iridium Communications Inc. - CEO*

There is some growth of these what I would call out-of-projects that go beyond the current EMSS contract, new services and capabilities as we get embedded in new systems and those generate revenues outside the contract and I think there's some of that this year and there's expectations that will continue to expand in the future because it's not just all about the EMSS contract. Then of course you also saw our R&D and our services revenue with the customer, it varies quite a bit year-to-year, but that's been generally up here recently as we have these additional contracts to do things like a new handset, gateway expansions, and resiliency improvements, and other things we're seeing in that kind of activity which adds revenue as well even though it's a little different margin revenue.

Chris Quilty - *Raymond James & Associates - Analyst*

And for Tom, as the push-to-talk business starts to ramp-up, how is that going to impact how you recognize your ARPU and subscriber count?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

It will be treated just like a handset. It will be blended in commercial voice and data.

Chris Quilty - *Raymond James & Associates - Analyst*

Positive or negative mix?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

No, it's accretive to ARPU.

Chris Quilty - *Raymond James & Associates - Analyst*

Substantially or modestly?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

I would say the raw number is substantially, but you got a very big base of subs so it's not going to move the needle just because of the weighted average. But it's a nice ARPU piece of business for us.

Chris Quilty - *Raymond James & Associates - Analyst*

And fair to assume that these are going to be longer-term contracts than the sort of traditional one year?

Tom Fitzpatrick - *Iridium Communications Inc. - CFO & Chief Administrative Officer*

I don't know that the contract will be, but this is a very sticky customer.

Matt Desch - *Iridium Communications Inc. - CEO*

And the whole concept obviously of PTT is the workgroup itself, the talk group becomes very valuable into itself because you want to be part of that talk group because it has value to be really intrinsically to a group of people. So yes, you're right, I think that that means that these kind of customers end up being longer term. So yes, we're enthusiastic about that.

Chris Quilty - *Raymond James & Associates - Analyst*

And just to clarify, do you have any commercially launched customers or are you still kind of beta stage?

Matt Desch - *Iridium Communications Inc. - CEO*

We are in the commercial stage right now. There are customers, there is revenue moving on initial customers, and there is quite a few customers looking to start their business soon and a growing funnel of opportunities. These like anything else, they do take longer. The nice thing is you add customers at tens or hundreds or in some cases even higher than that at a time, but they like to go through trials and evaluations and RFQs and all that sort of thing. So, I think some of those will take a little longer to ramp and in some cases to really hit, but when they hit they kind of hit in chunks.

Chris Quilty - *Raymond James & Associates - Analyst*

Alright, good. Thank you, gentlemen.

Matt Desch - *Iridium Communications Inc. - CEO*

Any other questions, operator?



Operator

We have no further questions at this time.

Matt Desch - Iridium Communications Inc. - CEO

Thanks, everyone. We'll see you next quarter. Obviously our story as you can tell is a transitional one here to Iridium NEXT. We're really excited about getting these launches started albeit on a slightly different plan, but really it still completes the network in 2017 and the financial transformation we're driving in this Company to 2018 is still very much intact and getting closer and closer every day. So, thanks for joining us and we'll see you next quarter.

Operator

Thank you. Ladies and gentleman, this concludes today's conference. Thank you for participating. You may now disconnect.

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