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CORPORATE PARTICIPANTS

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Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

MANAGEMENT DISCUSSION SECTION

Cai von Rumohr  
Analyst, Cowen and Co. LLC

So, can I have your attention? We're going to move on. We're delighted to have with us the Boeing Company, CFO, Greg Smith, and let's see, is a statement up there. The forward-looking statement is up there, so we're all cleared to go.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Okay.

QUESTION AND ANSWER SECTION

Cai von Rumohr  
Analyst, Cowen and Co. LLC

So, commercial demand, give us some color. I mean, we've had strong traffic, have you seen an increase in the level of requests for push-outs or for pull-forward?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. I can't tell you, Cai, that we've seen any significant request. But not – nothing outside the normal. Certainly, a lot of demand near term on the narrow-body, on the 737. So, that's certainly been where we're seeing a lot of near-term demand and request to pull forward and get delivery slots. And we're obviously going up in rate there this year from 52 to 57 and working through the recovery that we've talked about a lot and talked about recently on the earnings call and getting that kind of back to that stability of 52 a month and then we'll go from there.

But I would say, nothing outside the norm that we've seen on deferrals by any means. We're still at an all-time low when it comes to deferrals. And then, just market demand looking at the fundamentals of what's driving the demand and continuing to stay focused. But you said it, I mean when you look at traffic, we're outside of nine years now of continued growth. You saw a very strong 2018.

When you look at 2019 traffic projections and they remain, again, kind of over and above what has been the average. So, we're still in good demand and you're seeing it across the globe. You're seeing the impact of the
growth in the middle class in particular and just the fundamentals again by region and by country remained pretty strong.

Now, obviously we continue to stay very focused on those regions and really make sure we understand what's driving the demand. What kind of passenger traffic by region, by airline but also how much of this demand is growth, and how much of it is replacement. And I'd say our backlog and even as you look forward the next 20 years 43,000 airplanes 40%, 45% of that is replacement. And I think that really plays into what we're offering in the marketplace and in delivering a competitive advantage in economics that differentiates from the current portfolio.

So, you look at the MAX, the demand that's been on the MAX and the economics associated with the MAX can deliver for the customer. 787 certainly, 777X, 777 and so on, even 747-8 as we've seen more demand on the cargo market. But the efficiency that's being brought in the market is certainly driving some of this replacement. And then, as you look forward and again you look year by year, airline by airline, you're still going to see about 40% to 45% of that just being pure replacement, just assets timing out being replaced by much more efficient, that in addition to growth.

Cai von Rumohr  
Analyst, Cowen and Co. LLC  
Right.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President—Enterprise Performance & Strategy, The Boeing Co.

And you look at things like the 787, there's over 200 new routes being flown today with the 787 that didn't exist before. So, it's doing what we said it would do in the marketplace, and it's opening up these markets to allow our customers to be better, to serve again customers in demand that they weren't able to do with prior assets and that to me again is just – that got to be a game changer in the marketplace and something that we got to stay focused on going forward...

Cai von Rumohr  
Analyst, Cowen and Co. LLC  
Right.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President—Enterprise Performance & Strategy, The Boeing Co.

...as we think about offering our products and services across the globe.

Cai von Rumohr  
Analyst, Cowen and Co. LLC  
And so, it certainly looks like a tale of two cities, I mean passenger as you say, the demand continues...

Gregory D. Smith  
Chief Financial Officer & Executive Vice President—Enterprise Performance & Strategy, The Boeing Co.

Yeah.
...little surprise on the upside. But IATA just reported their freight numbers for December and they ended the lackluster year with a decline. So, what's the implication of that? What are you seeing in terms of demand for the 747? Can you keep that alive...

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

...in the 767 and 777 freighter market?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Well, look I think when you look across the installed base in freighters, I think we're over 90% of that installed base today. So, things like the 777 and things like the 747 are serving that freight market extremely well. And we've seen improvement, as you know, in freight over the last couple years, that's created more demand on the 747 as well as on the 777.

So, again, it kind of goes back to kind of having the right products and services in the marketplace to get the customer – serve the customer and give them a competitive advantage. 777 and 747, no question, are doing that. And we continue to monitor the demand across the globe but – and part of that is looking at what assets are available. So, what assets are parked today that a customer could utilize, and you're either hovering around zero to single-digit availability in the market. So, that certainly can work to our advantage in getting them a 777 or a 747 into their hands in the timeframe that they need it. So, still seeing good demand on freight.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

What's the latest status on the 777 bridge to the 777X and when is the 777X looking like it's going to come into the market now?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. Well, as you now, big focus for us was on the 777 bridge, right. Filling in that bridge between as we ramp down the 777 and move into the 777, that's been the big focus last year, the year before. And we've done a great job. Teams had done a great job in filling that bridge. Certainly freight has also helped in that. So, the focus now is on 777X orders in 2021 and 2022. And that's where the sales team and the campaign reviews are focused today more so than on the bridge. So, I think for the most part, the bridge is somewhat behind us and more of the focus being put on that 777. So, 2019 will be a big focus area and a big objective to get more share on 777X in the marketplace.
Got it. With the orders you have for the basic 777 and the 777X coming into the market in 2020, should we look for combined 777 deliveries the kind of edge up in 2020 and 2021, or how should we think about it?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. I think I mentioned on the call, you'll see a slight increase there as we're bringing the 777X in. And then, feathering the 777 now as I mentioned, we've got good demand on the 777. So, we're really threading that needle in that first year of, I'll say, kind of dual production between the 777X and the 777. And trying to again meet customer demand on the 777 but meet the commitments of the delivery dates on the 777X. So net-net, you'll see a slight increase there year-over-year. I'd say 777X is progressing well in the factory. We got through the static airplane.

We've got airplane number one and two in the factory. Airplane one, power on. So, anyone that follows business closely know that's a significant milestone and we're tracking the first flight this year. So, this will be a big year for 777X. And then, obviously a big year as we move forward into ramping up that production rate.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

So, when we look at the 777X, what are the things we should look at, the milestones we should expect to tell us you're doing okay or you're having an issue?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. Well, I think those early – especially the test aircraft power on, that's a big milestone. Now, getting into first flight, another big milestone. Achieving our test flights and our certification, those are also big milestones that will lead up to that 2020 delivery.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Are you at all nervous, I mean on the biz jet side, it seems everyone who's certifying a plane, they complain of more and more paperwork and things get done later and later. So, is that a concern of yours?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Look, certification is a big part of any development program. But I'd like to think we get well ahead of that and obviously working our way through 737 and all the derivatives of the 737 MAX, the 787 and those derivatives and certifying the last one being 787-10. And so, taking all of that and applying that onto the 777X and trying to do that in the most efficient way possible, ensuring that we've got a game plan out and key milestones that support that and resources that support those milestones in order to achieve that. So, I think we got a good plan in place. I wouldn't tell you that we see anything that's been outside the norm of what we've normally been through in our certification of our other aircraft.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Got it. So, update us maybe on the plans to ramp the 737, you get the 57 I guess maybe about middle of the year. Any residual supplier issues and what are you doing to reduce the risk of future glitches?
Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. Well, I think we've talked about several times and recently on the call, it's been getting stable at 52 and getting the confidence in the rate readiness to go up to 57, which is to plan. So, certainly the market demand is there. We're in a oversold position. So, it's not the market that's driving – is driving the rate increases, certainly in that demand, it's really more in the production system. And the recovery rate now focus has been on CFM. They got a recovery plan in place that takes them to about midyear where they're fully recovered. And so, that's where the resources and time is being focused is on getting CFM back to that recovery plan in order to meet our 52 commitment, but also to meet the long term – longer-term objective of 57, which will take place this year.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

So, Spirit says they're back on track. I've heard less and less of kind of other...

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

...parts suppliers being late. What's your opinion? Are those guys pretty much back?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. I mean I think they're doing a good job. We talked about consistency. So, it's one thing to be at rate, it's another thing to be at rate and be consistent. And when you're operating at 52 a month, minutes and hours matter. So, that consistency of the delivery of the fuselages at the right place at the right time is definitely improved.

So, they're tracking to our production system. And like I said, meeting the load dates which is, of course, you saw that in the recovery last year on the 737 as well. So, doing a good job and I think part of that recovery they've been able to exercise themselves to 57. So again, that gives us more confidence in their ability to achieve that 57.

And rate readiness, you can imagine we're going through the recovery on 52, tremendous amount of effort going deeper into 57 to assure everybody is ready.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Right. So, there's been speculation on this on the street of going even higher going up to 63. What would you have to see to kind of make that decision that you're...

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah.
Cai von Rumohr  
Analyst, Cowen and Co. LLC

...going to go higher and what's the earliest you might announce that you'll make it?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. Well, look, the market is certainly there and there's no question about that. It really gets to the readiness and your confidence in being able to achieve that level in a consistent and efficient manner. And the longevity, how long can you hold that rate in ensuring that you're executing again flawlessly as you're moving up in that rate. So, my comment on that is get to the recovery at 52, get to the 57 and then we'll assess rate increases from there.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Got it.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

But I don't see this being market driven. It's going to be more about the ability for us in our supply chain, predominantly the supply chain and the lower tier, in particular supply chain's ability to get there any in a timely manner to meet our demands.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Got it. So, your performance on the 787 has been kind of consistently outstanding, but I guess we all know that at some point learning curves start to flatten out. How much more gas is in the tank in terms of how – what kind of cost improvement you can get on the 787?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. Well, to your point, team's done a great job. They've done a great job executing the rate increases and getting to 12 and now on a path to 14 this year. As well as our suppliers, a lot of focus, as you know, on working capital and productivity across the board. And you're seeing some of the benefit of that certainly in the last couple of years and you're seeing some of the benefits of that in the 2019 guidance.

So, it's – there's efforts that will continue with that, but there's also improvement in mix and improvement as we kind of work through these blocks and have step-down pricing within our supply chain. So, when we talk about growing cash flow for the company, that's a key enabler. And over the long term, a key enabler is the 787. So, I would tell you there's still a lot of improvement ahead of us that we've got in our plan and that's again getting to the rate, but also kind of working our way through this model mix and getting more of a better mix within the factory.

And you remember the investment we made on the 787-10 and the 787-9 to get that commonality in place. So, as you have more 787-9s and 787-10s in that mix, you'll see the benefit of that in the production system even more so going forward.
So, again, the team has done a very nice job of feathering the 787-9 in over time, bringing it up to rate, and now, bringing the 10 in and getting that up to rate, and obviously coming down the learning curve in particular in the 787-10 because as that's been introduced in the production system. So, I'd say it's kind of multifaceted elements that will ultimately play out as a – as grow – into growing cash flow in 787 going forward.

Cai von Rumohr
Analyst, Cowen and Co. LLC

So, there's been a lot of speculation also middle of the market playing.

Gregory D. Smith
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yes.

Cai von Rumohr
Analyst, Cowen and Co. LLC

What are the long poles in terms of your having to feel comfortable with going ahead with that program, and I guess engine supplier decision is key...

Gregory D. Smith
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Sure. Yeah.

Cai von Rumohr
Analyst, Cowen and Co. LLC

...what's your druthers, one or two suppliers? And talk to us about that issue.

Gregory D. Smith
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

So, I would say, look, in any of these development programs, there's gated criteria. So, we've got a gated process and we got that goes through technology and obviously into the business case, into pricing, into engine technology and capabilities and efficiency and so on. So, it's very clear gated process we put in place. Now, we've enhanced that gate – those gates. So, put more criteria in those gates based on lessons learned.

So, this has taken the lessons from the past and bringing those into the gated process to try to de-risk the program. So, we got to work through those gates and it's a pass or fail. So, if it's a fail, you've got to kind of go back and meet the criteria. And a lot of people obviously involved in these gates to get through them.

So, we're working our way in maturing our thoughts around these and our confidence in those, and that's going to be the pacing item. All of what you describe staying very engaged the customer, over 60 engaged with the customer, really understanding their needs. But understanding the pricing dynamics, the quantities and so on. Just the kind of near-term needs as well in entry into service. That is one element of many elements that need to be considered in this business case.

And being very clear eyed about what we need to learn from the past and how do we get that into the next program. So, taking the lessons learned off of even 737, it went extremely well. There is lessons learned on that. 777X, I talked about where it is in the factory. There is elements of that gated process in the 777X, and I would
say that you're seeing the benefit of that today. Investing in labs and investing in prototyping and de-risking before you get into a production system.

So, taking that and even enhancing it further, T-X, MQ-25 taking capabilities and practices that frankly have been proven on those assets. How do you take those? Get them over into NMA and leverage that capability experience of Boeing and apply that to NMA and get your confidence level up that you can actually achieve it on NMA. So, it's probably a long way of saying that there's a lot of criteria and we're being very disciplined, and we're going to go when we're ready. And we're ready.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Got it.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

But we're staying very engaged with our customers throughout this process as you can imagine and we're game boarding out, competitive dynamics and we're game boarding out various scenarios that ultimately I think that's our job. That's what we should do. And we're putting really a lot of rigor and discipline into it. And we're going to continue to do that and this year will be a milestone of deciding whether – as Dennis talked in the call, whether we get the authority and ask for the authority to offer it in the market. And if we do, does that meet our criteria and then from there, there will be a decision whether we formally launch or not.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

It certainly sounds like you're leaning towards going ahead and yet I think the debate is taking a twin and giving it single aisle economics is a non-trivial challenge. You've said if you go ahead, the R&D, the sales holds flat.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

This thing must cost so much money. I find it really kind of hard to believe that if you decide not to go ahead that the R&D, the sales wouldn't come down.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Well, there's a lot of focus on nonrecurring costs in that business case end part of the gate. So, our financial, I'll say, expectations are part of that certainly and the risk profile associated with that. So, that plane rated as a nonrecurring and as well as on the recurring costs. So, that's a key element of this business case obviously and key element of passing through these gates. So, as we said, if we move forward as a percentage of sales to your point, you'll see it very similar to what you're seeing today.
Right.

**Gregory D. Smith**  
*Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.*

But you're also seeing versus – if you look at 2018 versus 2019, you're seeing us making more enterprise investments across the company. And things like prototyping, things like autonomy where we're trying to again get ahead of the curve. And really trying to make some organic and some partnerships in some of these technologies and try to mature them and bring them into our products which ultimately play into winning. Making sure we have a competitive advantage to continue to win in the marketplace and continue to differentiate ourselves on what products we're offering in the market. All this investment in these technologies plays right into that.

**Cai von Rumohr**  
*Analyst, Cowen and Co. LLC*

But still, I mean do you think that the R&D to sales would be flat – are there enough opportunities to kind of keep the R&D to sales flat or is it more – is it sort of a challenge to keep it there without just spending money to spend money?

**Gregory D. Smith**  
*Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.*

Yeah. No, we don't spend money just to spend money, trust me. But I can tell you that it's – the timing of potential new airplanes plays right into the 777X...

**Cai von Rumohr**  
*Analyst, Cowen and Co. LLC*

Right.

**Gregory D. Smith**  
*Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.*

...kind of ramping down. So, again, talk about a lesson learned, concurrent development of big major development programs. So, we're not going to do that and we've made that clear. So, the timing of the R&D is really more back loaded – front loaded on the back end of the 777X development.

**Cai von Rumohr**  
*Analyst, Cowen and Co. LLC*

Right.

**Gregory D. Smith**  
*Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.*

So, that's part of what we're going through to ensure that we maintain that and again being very clear eyed on the risk profile and in the lessons learned of the past. But at the same time, very focused on the customers' needs and desires around that 2025 timeframe. So, feathering that all in and stepping back and again, looking at the efficiency it needs to be driven, looking at the risk profile and us being comfortable with all that put together to meet in that timeframe. And so, that's part of the dialogue that's taking place today.
So, you’ve been much more aggressive than I would have anticipated in terms of your investments. Buying KLXR, the Embraer JV, the Aerion kind of investment.

Gregory D. Smith  
*Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.*

Yeah.

Cai von Rumohr  
*Analyst, Cowen and Co. LLC*

Do you have more to go? What are you trying to do in that area? Obviously, you have a lot of potential firepower, if you want to do more?

Gregory D. Smith  
*Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.*

Yeah. Well, look, I think all of those tied directly to our strategy. So, there is nothing that does not link directly to our strategy. And whether as our strategy in – from a product offering in the marketplace or a capability. And you probably also noticed that there are some of these capabilities that we've looked at organically, we've looked at inorganic, and we've looked at partnerships.

So, our value proposition there is clear about what we want to do, but how we go about doing it, we're trying to be – we're trying to look at risk, we're trying look to be honest about what capability we can develop, how long, what capabilities somebody else has, and can we come up with a business arrangement that's a win-win. Adient seats is a great example.

So, look, we decided we want to play in that. We want to play in the life cycle to support Stan's business and the service objective. What's the best – what are our alternatives to do that? You could buy a seat manufacturer, you could become one, or you could partner. We chose to partner. And on that – and address that marketplace together in a business arrangement that's kind of a win-win. You'll see others like on APUs, similar type approach. You'll see others where there's more organic because we believe that we can get – that we have enough capability that we can ramp that up if we stay focused on it and get the right people – dedicated people and leverage the enterprise to be able to come to market in a timeframe that we're expecting.

So, think of it as capability gaps looking through the life cycle lens as well now, much more than we ever have. And what are those key kind of enablers and capabilities we want, and what's the best way to go about doing them. At the same time, being prudent, right? And being smart with the capital and not stepping away from our commitment on capital which has been on deployment. Look, invest in the enterprise. We're addressing a great marketplace across the board and we want to keep winning in the market. So, make the right investments in the production system, in around efficiency, on derivative aircraft, on next-generation technology things like MQ-25, T-X, MH-139, things like that, making those investments.

And then, deploying our capital back to shareholders, dividend repurchase, and then partnerships M&A. So, meeting our commitment on the deployment and being consistent with our deployment efforts is what you should expect from us going forward. But we're very prudent on how we go about doing it very disciplined. And we've got good processes in place and control.

So, where we've committed to spend money on R&D and you get six months into it, and you realize maybe that's not as good maybe as we thought it was, we're stopping. We're reallocating that because something that's even
sees more potential going forward. So, putting things like that in place that are really allowing us to be very efficient with our capital and very timely around capability needs we want and when we want them in the market.

So, you're going to continue to see a mix. You're going to continue to see again organic but you're going to see partnerships and you're going to see some – if there's M&A opportunity that meets all that criteria, and we see a value proposition, KLX being an example there, then we're going to go about doing it.

What I would tell you, we're doubling down on integration. So, if you look at the amount of effort and the operating rhythm around integrating KLX, I would argue, it's far greater diversity in the past. That's intentional.

Cai von Rumohr  
**Analyst, Cowen and Co. LLC**

Got it.

**Gregory D. Smith**  
**Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.**

Absolutely intentional. And holding ourselves accountable to that original business case. And don't take your eye off that commitment we made to ourselves, to our board and to our shareholders. And if we see ourselves weaning off of that what's driving to get on it fast and figure out how to win it, how to change it. So, when you – I think if you were inside, you saw the discipline around that, that's the kind of thing you should expect from us because again, we're treating these dollars very valuable.

Cai von Rumohr  
**Analyst, Cowen and Co. LLC**

Right.

**Gregory D. Smith**  
**Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.**

And we have choice. We're going to make the right choice and when we want to execute it flawlessly.

Cai von Rumohr  
**Analyst, Cowen and Co. LLC**

Got it. So, one of the complaints suppliers over the years have had about Boeing is that they're very insensitive to value engineering proposals, which I can understand...

**Gregory D. Smith**  
**Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.**

Yeah, yeah.

Cai von Rumohr  
**Analyst, Cowen and Co. LLC**

...just because there's risk of certification. You need to put your engineers to work.

**Gregory D. Smith**  
**Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.**

Yeah.
Cai von Rumohr  
Analyst, Cowen and Co. LLC

And yet Spirit talks about this arrangement where when you do that thing, you share 50/50. So, there's more financial incentive for you. Is that a move you're trying to push across your supply base?/

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Definitely. Yeah. Definitely, and into your point, that requires an investment on our behalf, right? I mean there are some great ideas out there that end up coming back to us that may require a design change or a change to a tooling or a method. We've got to have an infrastructure in place that's assessing those and in agreeing that again there's a value proposition, there's a business case there to do that and we got to do it in a timely manner and turn it around and get it back in the supply chain and we all win.

I would tell you that the investment in that and that's really partnering for success far greater than it's been in the past. We've got people, this is what they're doing day in and day out and assessing this. And look, not all of them pay off. Some of them may look like on the surface to be a game changer but when you get deeper and you really look at what's real investment going to take place, it's the risk. Maybe it's a 737 and you're at this kind of a rate. You don't want to put that at risk, so how do you bring it into the production system and not add to that.

So, you're absolutely right. That's a big push and you're seeing companies like Spirit that's a great example of everybody's winning. It's making them better. I truly believe there's a multiplier with all their other programs that they work on in driving some of these efficiencies. It makes us better and ultimately allows us to compete and win in the marketplace.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

So – but like what's the reception on suppliers, I mean are there other kind of arrangements like Spirit's that essentially are 50/50 cost split.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. I think they vary...

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Okay.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

...by supplier. They frankly vary by size and timing of opportunity.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Right.
Gregory D. Smith  
Chief Financial Officer & Executive Vice President - Enterprise Performance & Strategy, The Boeing Co.

And so, they're different across the board, but to your point it's a commitment on our behalf to understand and look at every idea with them together because I would argue there's inefficiencies between us. Look at how many contracts throughout certain suppliers and look at the requirements within those – is there opportunity to streamline some of that? Because there's a cost associated with that by the time it hits the supplier. Standards, so let's look at standards and let's look at industry standard. Is there an opportunity there? I'll say kind of methodology that's applied that we're dictating. Is there an opportunity there?

Suppliers buying their own material. I mean can we leverage the buy of the Boeing company? Suppliers buying their own tooling. Can we leverage the buy across Boeing and pick suppliers that we know are proven and efficient and timely? How do you leverage that? And so, there's things like that we're doing and have done and we'll continue to do that again ultimately I think make everybody better. And at the end of the day, it's about us competing to win in the marketplace and getting our customers the best products and services available.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Got it. So services, you talk of a lot of investments you've made.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President - Enterprise Performance & Strategy, The Boeing Co.

Yeah.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Your margins already are good. They're like 15% plus. Can you hold them at that level or can you improve them while you do make all these investments?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President - Enterprise Performance & Strategy, The Boeing Co.

Yeah. Well, look, the whole margin I'll say kind of objectives has been not as much about incremental year-over-year. It's been more about look, what should we – what's the market? What's the competitive dynamics as far as what are the competitors whether it's in the supply chain or achieving a margin? And ultimately, what should we expect from ourselves? When you look at the risk and reward, what should we expect from ourselves?

So, it's been a change in mindset around benchmarking ourselves against not just necessarily people in the industry, people outside the industry, and culturally being extremely open minded to any good idea, and not the resistance point of they're different. There is what element is the same and where you can leverage that. So, I've talked about this and Dennis talked about this before, but functions, so we look at a cost of the function across, benchmarked ourselves, looked at centers of excellence.

Yeah. And there was the day that we were paying the bills out of 21 different payment centers. And also merged company, rather a bunch of different divisions being added on, we pay at a one place. That's one example of going to places where they have achieved centers of excellence, learning from it and applying it and also bringing the cost structure down, and in fact to being in the marketplace efficiently. So, we're trying to look at this completely different, and you've seen some of the benefit of that I think over the last couple of years of just setting
a different bar for ourselves, and finding the path to get there and leveraging – by the way, leveraging best practices in our own company.

We've got programs that are achieving levels of working capital and profitability that are top quartile. So, how do you leverage that and bring that across Boeing and how do you incentivize the workforce on both sides to do that? One score. So, everybody’s compensated on one score. Free cash flow, earnings and revenue. And each of us individually on our behaviors is rated on how we’re playing to make Boeing better. That's a way to do that.

So, going across the aisle and the 787 folks going out to the Chinook folks. And the Chinook folks going out to the satellite division. And I would tell you that there is some incredible best practices in our own factories, or in our own functions or support functions or tooling applications, technology. We can leverage internally even more. Never mind even going out in benchmarking So, there are some real stars in the company that we've got to kind of rally behind and take that and share. Champion times is a great example on 787 to achieve this mindset of what's the best time that we've had on a wing body joint as an example. And getting consistently at that time and then achieving to get to a new level.

Taking that mindset in that methodology and the tools and putting on F-18, putting on F-15, putting that on Apache and things like that, but having an enterprise that is focused on winning is Boeing. Not winning as a program, not just winning as a division. Winning as a Boeing and you will be rewarded accordingly because we'll all win.

And I think the compensation structure aligns exactly to you all and our stakeholders. There's clarity around how you achieve those objectives. And it's our job to meet those expectations and then be smart with the capital.

So, do all that and be smart about the capital. Invest in the future, invest in key technologies, partner, and then build out capabilities that you think you can differentiate yourself and big focus on the life cycle. Big focus on the life cycle, which is again a great opportunity for us. But I believe they got – and we all do believe, a big opportunity for our customer. We should be able to serve the customer better.

We know our products and services better than anybody should. And I believe we do. We've made the big investment upfront and this is a great opportunity to be more intimate with your customer and really understand where they need help and where we can enable them to better and I think service is a great opportunity to do that. So, we're excited about it. The team had great a year, last year as you saw on services. And I'll tell you, Cai, if you go to Plano, Texas, you'll see a very motivated excited group because they’re seeing more and more potential. And you're seeing sales campaigns now where we're looking at the whole portfolio. You're seeing sales representative scorecards that not only have orders but also have service share, winning in the market on services. So, big push for us I think, the market's there, it's a $2.8-trillion market and we've got single-digit shares.

So, to your – back to your point about investment or even just management, time and attention, we're putting a lot in 777X. And we think it's a big game changer, big growth engine for us. But again, ultimately we should be able to serve the customers on our own assets in particular better than anybody.
That's been the focus.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

So, no Boeing interview would be complete without a discussion of cash flow.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Absolutely.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

So, from everything you're saying, it kind of sounds like 787, things get better; 737, things get better. Tanker, things get less bad. 777X, we peak in terms of paying this year and then it gets better. I know you'll tell me that cash taxes go up, but they're really a function of the improvement in the 787. So, for every $1 you pay you probably get $4 of benefit on the cost side. So, at one point, Dennis said cash flow goes up through 2021 not just through 2020. Is that still the same or if it's not, like what's there that [indiscernible] (37:15)?

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Yeah. we used to say that in 2020 we realized, wow, 2020 is right here in front of us.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Right.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

But yeah, I mean, look, there's opportunity to continue to grow cash flow going forward. This is very much about execution.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Right.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

It's right at the core. And you talk about a lot of the moving pieces. So, 737, going up to 52 and getting to 57. That's a driver. 787, 12 to 14 but also getting the mix right. Getting the more of those 787-10s in and more of the 787-9. That's a big driver. The supplier stepped down in the blocks on the 787. It will add to the cash flow. And again, you'll be delivering at a higher rate as well as the progress payments associated to that.

777X as we talked about, 777X is the use of cash as we're building those early test aircraft and static aircraft but that'll start to turn as we get into 2020 and we start delivering access. And that's the big enabler obviously throughout that. I talked about service growth and again the conversion on cash is pretty close to earnings there
but we’re going to make more investments in services. And then defense, again similar conversion rate to earnings but you're going to see modest growth.

So, when you kind of net all that together, you can see where the upside is. Where is there headwind, cash taxes. No question about it. As we get more profitable on a unit basis, we’ll pay more in cash taxes. So, that's more of a headwind going forward. And then, on a dollar basis, a little bit more on R&D year-over-year. So, as a percentage of revenue will be flat, but absolute dollars will be slightly more over time. So, when you kind of step back and look at this again right where I started, this is very much an execution.

It's doing what we said we would do. Obviously, there's market dynamics that we need to take into account and we do. We're very clear right about trade and we're very clear right about our backlog and our order book going forward. And I told you 777X orders, that's the big enabler for cash over the long term, not near term. Selling into 14 a month on the 787 that will ultimately again drive the 14 a month that will drive the cash flow.

But I'd say those are the fundamental big moving pieces. There's a lot of ebb and flow quarter-to-quarter and year-over-year, and I mentioned Q1 will be the lowest quarter of the year and a lot of that is seasonality but some of that is the 737 recovery as we came off a big December.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Right.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Expect a light January and then that on 737 deliveries and then that'll start to pick up in Q1. So, there's always fundamental shifts quarter-over-quarter. But when you step back and look at the big levers, those are fundamentally it. So, I'll tell you what, the team is absolutely focused on those what we call kind of big rocks and doing – reaching those milestones, driving the efficiency and very focused on cash ultimately cash and efficiency, back to not only how we're generating the cash but being very prudent about how we're deploying it as well. And really ensuring that we're meeting our commitments to ourselves and to all of our stakeholders that there's a solid return tied with that deployment, so that consistency you should expect from us going forward. So, we've got a pretty exciting 2019 in front of us. I'd say in front of us but we’re deep into it.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Sounds good. Hey, that was terrific.

Gregory D. Smith  
Chief Financial Officer & Executive Vice President-Enterprise Performance & Strategy, The Boeing Co.

Thank you.

Cai von Rumohr  
Analyst, Cowen and Co. LLC

Thank you very much.
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