Wheels Up, Inc. (UP): Creating The Leading Private Air Travel Marketplace

"Once you fly private, going back to commercial is like going back to holding hands." ~ Warren Buffett

<u>Note: Updated Financials To Reflect UP's first quarter as a public company***</u>

I first wrote about Wheels Up (UP) in February. At the time, the company was still under its SPAC merger agreement with ACBL. Yesterday UP reported earnings for the first time as an independent public company.

Here are the highlights:

- Revenue increased **113% YoY** to $285.5M
- Active Members increased **47% YoY** to 10,515
- Live Flight Legs increased **146% YoY** to 18,234
- Adjusted EBITDA loss of -$8.5M (-3% margin)
- Net Income loss of $29M

As you'll read below, UP is democratizing private flight for the everyday consumer. Democratizing private aviation is a complex problem that requires significant investment in backend infrastructure and demand-side optimization.

Though a complex business, the investment thesis boils down to three key metrics: **Live flight legs, active members, and available aircraft supply.**

The more aircraft UP gets on its platform, the greater number of flights it can provide to its members. In turn, greater availability of flights will reduce average flight costs and drive an influx in new active members on the UP marketplace. Of course, more active members increase the demand for more supply and the flywheel repeats.

UP generated *strong* earnings this quarter and is now a year ahead on their full-year revenue estimates. During the call, CEO Ken Dichter noted that management will use this increase in revenue to reinvest in its platform through increased technology spend.

In other words, the company's deferring today's profits to build a better, more durable marketplace for the future. We *love* that.

Another important note is that UP's newest customer cohorts are spending more than prior cohorts. This stat confirms the company's hypothesis that consumers want what UP is building. And that they're ready to pay *UP* for it.

Finally, UP revised their FY 2025E revenue guidance to $2.1B, giving them a ~1.3x EV/2025E sales valuation.

Let's dive into the business to see why we're so excited about this marketplace.

What if flying in a private jet was as easy as booking an Uber?

Enter, Wheels Up.

Wheels Up connects potential private-flight customers with an available fleet to create a luxury marketplace for private, first-class travel. The company sits at the heart of an antiquated industry ripe for disruption with a digital, Uber-like product.

With Wheels Up, customers can book private aircraft flights by the hour through a seamless mobile app experience. Once booked, the flyers drive to their assigned airport, find their jet, and take off.

Customers love Wheels Up...

The company has connected ~150K passengers to their network of ~1,500 private jets. Wheels Up ranks #1 for on-demand private aviation providers and has 3x as many flights as its closest competitor. They're the number one searched brand online for "private aviation." Finally, Wheels Up sports an 87 NPS rating, one of the highest we've seen.

The company generated $690M in 2020 revenue and plans to hit over $1B by 2021. They should get there barring any further negative COVID-19 developments. For example, extrapolating Wheels Up's 2H 2020 revenue on a run-rate basis gets us $802M in FY sales.

Today, Wheels Up trades at a $2.77B market cap ($8.78/share x 312M fully diluted shares) and $2.32B Enterprise Value. By 2023 the company expects to do $1.4B in revenue and $58M in EBITDA. That means we can buy the business for ~2x EV/2023E Sales and 40x EV/2023E EBITDA.

Our Variant Perception: UP doesn't screen well. It loses money. And it's a former SPAC. Most investors don't fish in these arguably dangerous waters, which is why this great business is so overlooked.

The company is forgoing today's profits to build the best marketplace for consumers and aircraft. As such, investing in UP requires a long-term mindset. Founder Ken Dichter is one of the sharpest operators in the space and has already sold one jet business to Warren Buffett.

UP is focused on capturing high net worth and large scale businesses, but that's not what will create a $50-$100B business.

Lower flight costs will allow millions of middle/upper middle class households to enjoy private aviation.

If UP can reduce costs to capture this part of the market, the company has a shot at becoming the next $50B business.

Ken Dichter: The Man Behind The Company

Ken Dichter is the founder/CEO of Wheels Up.

Before Wheels Up, Dichter founded Alphabet City Sports Records with celebrity/entrepreneur Jesse Itzler. If you don't know who Jesse Itzler is, you should watch his podcast interview with Joe Rogan. Alphabet City Sports Records created and sold songs that fans heard at sports games. Dichter and Itzler sold the company to SFX Entertainment in 1998 for $4.3M in cash and stock.

It was after selling Alphabet City Sports Records that Dichter found the aviation bug. In 2001, again with Itzler, Dichter founded Marquis Jets. Marquis Jets was the first fractional card jet program. In other words, members owned a *piece* of the jet which entitled them to a certain number of uses. By 2007 the company found its groove. Marquis Jets did $700M in revenue with 3,500 customers.

Warren Buffett's NetJets, a Berkshire Hathaway subsidiary, bought Marquis Jets in 2010 for an undisclosed sum.

After the Marquis Jets sale, Dichter tried his hand at a tequila business, *Tequila Avion.* The brand won 'Best Tequila In The World' and 'Best White Spirit In The World' at the 2012 San Francisco World Spirits Competition. I mean, come on.

Heck, Dichter even sponsored (through Wheels Up) the horse *American Pharoah* in 2015. You know, the horse that won the Triple Crown.

This brings us to Dichter's latest endeavor: Wheels Up.

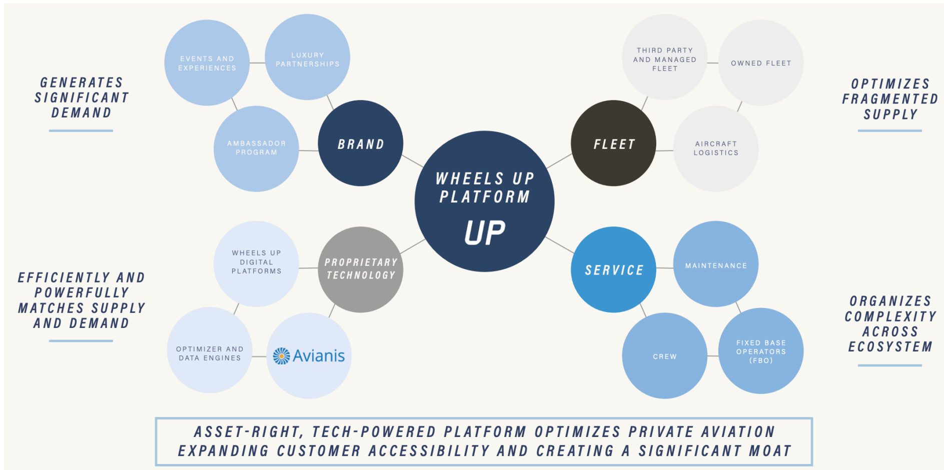
Creating A Harmonious, Win-Win Marketplace

Wheels Up has a simple business model. They connect those that want to fly private to a massive base of unutilized private aircraft. But here's the crazy part: both sides of the marketplace are **incredibly** underutilized.

There are two reasons for this:

1. 90% of people who can afford to fly private don't (based on McKinsey 2020 study)
2. The average private plane sits idle 97% of the time (2019 FAA data)

Let's start on the demand (flyer) side. There are a few reasons to believe that consumers will travel more privately than they did in the past.



First, experiences account for 65% of total consumer discretionary spending. Traveling privately to a vacation destination is quite the experience.

Second, COVID made people realize how much they loved traveling and how much they miss it when they can't. That missing/longing for future travel creates massive pent-up demand for private jet services.

The final demand catalyst also relates to COVID. Consumers might choose wellness/health over the cost of economy/traditional flight. In other words, if given the option (or ability), more people will decide to *pay up* to fly private due to health concerns.

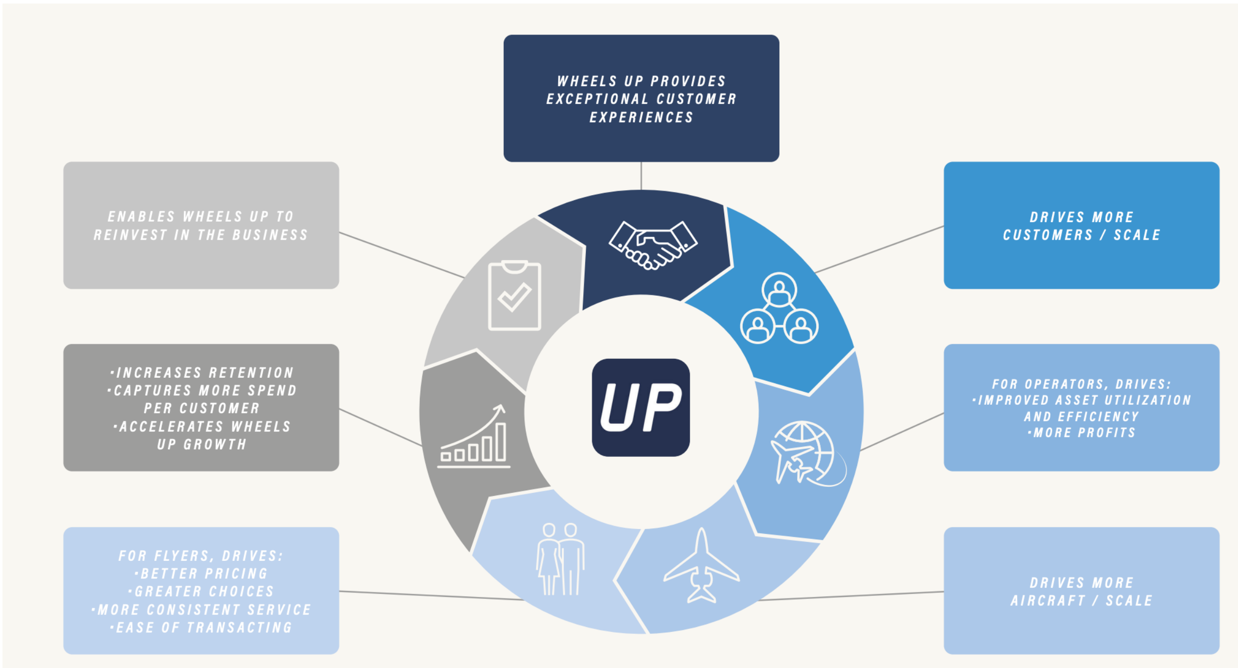
Now for the supply (aircraft operator) side of the equation. The aircraft operator market is highly fragmented. The top 10 operators control 8% of industry capacity. And 1,800+ operators control <10 aircraft. Given the industry's analog-centric booking process, matching demand with unutilized supply was nearly impossible (not to mention expensive).

Wheels Up's bet is that if consumers had an easy, comfortable booking experience for private aviation, they would choose to fly more private miles than before. If that's true, it expands the private aviation market for consumers. It creates revenue opportunities for aircraft operators with 97% idle time on their crafts.

The Main Drivers: Members & Fleet Size

There are only two things that matter to the Wheels Up thesis: members and fleet size. Together, these drivers create self-reinforcing feedback loops (i.e., network effects). The company highlights the network effect in the slide below:

More passengers drive improved utilization of unused aircraft, which leads to increased profits for aircraft operators. Increased profits and utilization times drive more planes onto the platform.



More aircraft on the platform means better pricing, greater choice, and more consistent booking service for passengers, which leads to increased passenger retention and more significant spending per customer (read: Wheels Up revenue). Higher revenues allow the company to reinvest into the business to create even better customer experiences, etcetera.

What Makes a Wheels Up Member

Wheels Up has three types of members:

- Business
- Core
- Connect

Members pay initiation fees and annual dues. Core members, for example, pay a $17,500 initiation fee and $8,500 in annual dues. Membership guarantees access to the King Air 350i and all cabin class offerings, as well as the full suite of member benefits and partner offerings. They also pay the per-hour charge to fly.

Wheels Up has 9,181 members as of 2020. They've grown members at a 44% CAGR since 2014. Members can pre-pay for flights, giving pre-paid members certain benefits like priority boarding or preferential aircraft selection.

40% of members bought pre-flight annual blocks for a total of $530M in block revenue (i.e., float).

The Wheels Up Aircraft Fleet

The company has ~1,500 planes at its disposal through a mixture of owned/leased (170), managed (170), and third-party aircraft (1,200+).

Managed aircraft pay Wheels Up a monthly management fee and make their aircraft available to fulfill Wheels Up member/customer flights. As of 2020, it had 55% of its fleet owned/leased, 20% managed, and 25% third-party. By 2025, Wheels Up wants its third-party network to account for 45% of its total fleet, allowing it to scale rapidly without much capital investment.

There is a give-and-take when you increase the percentage of third-party aircraft on your platform. Owned/leased aircraft generate >30% flight margin (flight revenue minus direct flight costs). Managed and third-party aircraft generate between 10-20% of target flight revenue. The goal, of course, is to make up that lost margin in volume.

Keep It Simple: It's Members, Users, & Flights That Matter

There are myriad risks associated with Wheels Up:

- They fail to capture the supply side of aircraft and hemorrhage passenger growth.
- Competition from Blade steals membership on the demand side
- Larger airlines copy Wheels Up with their existing fleet of aircraft

UP can mitigate all these risks if it kick starts its marketplace network effect. More active members will create supply side demand, which will reduce competitive worries as other companies fail to match UP's platform ecosystem.

Plus, at 2.7x next year's revenues, Dichter turning Wheels Up into *yet another* piece of gold is an attractive bet.

Wheels Up is a straightforward company to track because three things matter to its revenue and cash flow: **members, users, and flights.** If the company can increase those three figures, the revenue and earnings will follow.

Margins should expand over time as the company spends less on marketing for those revenue dollars. S&M spend as a percentage of flight and membership revenue has declined from 25% in 2015 to a shade over 5% in 2020.

UP is democratizing private aviation for the everyday traveler. The company is led by one of the most successful serial entrepreneurs in the space armed with a strong balance sheet and growing network effects.

Two-sided marketplaces take time to build. They require cash burn and operating losses, two things most investors abhor. But once established, UP’s platform will reduce the cost of private aviation, unlock a significantly larger TAM than investors thought possible, and become the world’s first $50B private aviation marketplace business.

