Operator

Thank you for standing by. Good day, everyone, and welcome to The Boeing Company's First Quarter 2012 Earnings Conference Call. Today's call is being recorded. The management discussion and the slide presentation, plus the analyst and media question-and-answer sessions, are being broadcast live over the Internet.

At this time, for opening remarks and introductions, I'm turning the call over to Ms. Stephanie Pope, Vice President of Investor Relations for The Boeing Company. Ms. Pope, please go ahead.

Stephanie Pope

Thank you, and good morning. Welcome to Boeing's first quarter 2012 earnings call. I am Stephanie Pope, and with me today are Jim McNerney, Boeing's Chairman, President and Chief Executive Officer; and Greg Smith, Boeing's Chief Financial Officer.

After comments by Jim and Greg, we will take your questions. In fairness to others on the call, we ask that you please limit your questions to one. As always, we have provided detailed financial information in our press release issued earlier today. As a reminder, you can follow today's broadcast and slide presentation through our website at boeing.com.

Before we begin, I need to remind you that any projections and goals we may include in our discussion this morning are likely to involve risks, which are detailed in our news release and our various SEC filings and in the forward-looking disclaimers at the end of this webcast presentation.

Now I will turn the call over to Jim McNerney.

W. James McNerney

Thank you, Stephanie, and good morning, everybody. Let me start today by addressing the evolving business environment, followed by some thoughts on our performance during the quarter. After that, Greg will walk through our financial results and outlook and then we'll take your questions.

Starting with the business environment on Slide 2. As the global economy continues to recover, albeit at a slow and somewhat choppy pace, airline industry fundamentals remain intact. Global demand for commercial airplanes is strong and growing. Emerging markets are driving the expansion of airline fleets worldwide, growth that is complemented by the ongoing retirement and replacement cycles for airplanes in developed markets.

Passenger air traffic remains resilient, with airline load factors and utilization rates continuing at or above peak levels. Although cargo traffic remains below long-term trends, it appears that this market is stabilizing and is projected to improve in the second half of the year.

Despite the ebbs and flows of the Eurozone debt crisis, we foresee aircraft financing as broadly adequate throughout 2012. Boeing airplanes are attractive, value-creating assets and sources of financing for them remain broad and diverse.

The high cost of jet fuel remains a key concern for our customers and has them focused more than ever on ensuring that they have the most fuel-efficient airplanes with which to compete, a dynamic reflected in our solid first quarter order total. The combination of strong market demand and our customer preferred portfolio of products and services that delivers superior fuel and operational performance, positions us exceptionally well for the future. Delivering our record backlog faster to speed the flow of new airplanes to customers and open additional positions for sale remains a priority. Production rate increases planned over the next 3 years will increase our output by more than 40% in support of these objectives.

While damage from the recent severe weather in Wichita has not had a significant impact on our operations at our facility there, we are working closely with our major supplier partner, Spirit, as they continue to manage the challenges of their stressed infrastructure. We will continue to assess this evolving situation. However, we believe the impacts to be manageable.

Turning to Defense, Space & Security. Defining U.S. defense -- declining U.S. defense budget and shifting program priorities continue to pressure domestic markets. We were generally pleased with how Boeing programs fared in the President's fiscal year 2013 budget request, which contained strong support for the majority of our programs, including the F/A 18, P-8A, Chinook, Apache and Osprey. We also see clear alignment in the proposed budget and the Defense Department's new strategic guidance with several of our targeted growth areas, including space, unmanned, ISR and cyber security.

We have been anticipating and preparing for a declining defense environment for several years. While the potential for sequestration has created additional uncertainty, we believe we are well positioned for continued success with our portfolio of proven, affordable and reliable systems and services, our focus on innovation and strong execution across our programs and our relentless effort to maximize efficiencies and reduce infrastructure costs.

Furthermore, we continue to foresee significant upside potential in growing international markets where we have made substantial share gains in recent years and expect to generate up to 30% of our revenues just a few years from now. In the first quarter, we went under contract for 84 new F-15s for Saudi Arabia, which will keep the F-15 viable for new sales for many years, and we secured several important C-17 foreign sales. These and other international orders led to a 20% increase in backlog for our Defense, Space & Security business.

Overall, despite pockets of economic uncertainty and U.S. defense budget pressures, the size and strength of our markets remain attractive and growing in the aggregate. Our total company backlog increased $24 billion in the first quarter and is broadly diverse by region, product type and customer. We anticipate this orders trend will continue, and we expect a book-to-bill ratio greater than 1 in both of our main businesses this year.

Turning to the first quarter highlights on Slide 3. We delivered strong operating performance across our core production and services programs in the first quarter, while achieving some key milestones in both Commercial and Defense. Commercial Airplanes generated healthy margins of 9.9%. We delivered 137 airplanes, including five 787s and six 747-8s, and we recorded net orders for 412 airplanes, including 301 firm orders for the 737 MAX. Customer response for the 737 MAX remains very positive. We continue to convert existing commitments to firm orders as planned, with a total of 451 recorded to date.

Key deliveries for the first quarter included the 1,000th 777, the first 747-8 Intercontinental VIP airplane, and I should say Lufthansa will be receiving their first Intercontinental airplane today, if everything goes as planned, and the first two 787 -- 787s powered by GE engines. In addition, the first 747-Intercontinental airplane, as I mentioned, it will be delivered to Lufthansa hopefully today.

The 787s in service with launch customer, ANA, and now Japan Airlines, are performing well, with high dispatch reliability rates and a very favorable passenger response to the features and capabilities of the airplane. We recently transitioned the 787 production line to a build rate of 3.5 per month in final assembly in Everett, marking the second successful rate increase in the past 6 months. Condition of assembly and out-of-sequence work continues to significantly improve as we work closely with our supplier partners. These gains are driving productivity and demonstrating the ability of this production system, which is increasing our confidence as we systematically ramp up to higher rates and reduce the amount of post-assembly change incorporation required on each airplane.

We continue to estimate that the first 787 to go straight from final assembly to the flight line without a stop in our modification center will be a unit in the mid-60s rolling out of the factory this summer. Later this week, we will roll out the first 787 assembled in Charleston, South Carolina. Delivery of that airplane from our new Charleston customer delivery center is expected in midyear.

We continue to increase the rate of 787 production. We expect to increase it, I should say, to 5 per month by the end of this year, which tracks to our plan to reach a rate of 10 per month in final assembly by late 2013.

Progress also continues at the Everett mod center to complete work on the airplanes that have come off the line but require further change incorporation work. With dedicated resources in place, we are using proven, repeatable processes to track the scope of work required on each airplane, maximize learning and reduce cycle time. As a result, we are seeing performance improvements with each airplane delivery.

Steady progress has also been made on development of the 787-9, with engineering design tracking to plan in support of first delivery scheduled for the second half of 2013 and first delivery -- first flight, I should say, scheduled second half of '13 and first delivery in early 2014.

I'd be remiss at this point if I'd didn't mention a very proud moment for all Boeing employees that came in March, when the National Aeronautics Association recognized the 787 with the most prestigious award for aerospace excellence, the Collier Trophy. We are extremely proud of the game-changing technology embodied in the 787 and the associated value it provides to our customers. And I'm equally proud of the team that got the job done.

Shifting to the 747-8, the 14 freighters now in service with 5 customers are performing extremely well. Progress on the production side is steady, too, as we continued to transition to reach a production rate of 2 airplanes per month this summer.

In addition to its sales momentum, the 737 MAX achieved a major development milestone in February when we began the final phase of wind tunnel testing. Design details are maturing to plan, and we are on schedule to reach firm configuration in 2013. We are working closely with our supplier partners to ensure successful production rate increases, not only on the 787 and the 747-8, but also on the 737 and the 777. Production rate on the 737 is planned to increase to 38 per month in the second quarter of 2013, and then up to 42 per month in the first half of 2014. Production on the 777 program will increase to 8.3 per month in the first quarter of 2013. These 2 franchise programs continue to generate substantial value for all of our stakeholders.

In Defense, Space & Security, this quarter, we delivered 30 aircraft and 3 satellites, generating solid operating results and margins of 9% across our well-balanced defense portfolio. In February, we marked a 1-year anniversary of receiving the U.S. Air Force contract to build the KC-46A. This program continues to be a successful team effort between the U.S. Air Force and Boeing. Over the past year, the program completed all milestones on or ahead of schedule. In March, we began the Preliminary Design Review with the U.S. Air Force, which is expected to complete later this week.

Additional key highlights in this sector included delivering the first P-8, low-rate initial production aircraft, completing Preliminary Design Review for the Commercial Crew Space Transportation system and the launch of our new 702 small satellite product line with an initial contract for 4 units.

Our total company backlog of $380 billion is close to 5x our current annual revenue estimate. This record backlog positions us for significant growth potential in the years to come, and we continue to improve productivity and competitiveness throughout the business.

Now over to Greg, who will discuss the first quarter financial results and our outlook. Greg?

Gregory D. Smith

Thanks, Jim, and good morning. I'll begin with the first quarter financial results on Slide 4.

Revenue for the quarter was $19.4 billion, up from last year, driven by higher Commercial Airplane delivery volume. Net earnings were $1.22 per share, including $0.11-per-share impact for a reduction in a litigation-related reserve. Operating margins at 8.1% and operating cash flow of $837 million reflect strong performance across our core businesses.

Let me discuss our Commercial business on Slide 5.

Boeing Commercial Airplanes' first quarter revenue was $10.9 billion, up from last year, reflecting a planned and successfully executed increase in airplane deliveries. Commercial operating margins were 9.9%, up from a year ago, reflecting the increased deliveries, strong core operating performance across the business and lower R&D expenses. This was partially offset by higher period costs, which do include 787 fleet support and the dilutive effect of 787 and 747 deliveries.

During the quarter, we extended the accounting quantities on the 777 by 50 units and the 767 by 6 units. The financial impact of these extensions in the quarter was not significant as volume benefits are balanced with anticipated competitive pricing environment.

Gross inventory for the company included approximately $22 billion related to the 787 program, an expected increase of approximately $1.8 billion during the quarter. As we've mentioned previously, we expect gross inventory for the 787 to increase to $24 billion by year-end 2012 as we continue ramping up production rates. But this growth will moderate as deliveries increase.

Included in the work-in-process inventory are the deferred production costs. The deferred balance for the program was $11.9 billion at the end of the first quarter and includes approximately 53 airplanes still in-process. As I stated on the fourth quarter, the deferred production balance will continue to grow as we increase production rates and introduce the 787-9 derivative, peaking at slightly over $20 billion and then declining after the program achieves the planned rate of 10 per month and stabilizes at that level.

Improving profitability on both the 787 and the 747-8 programs continue to be a top priority for us as we proactively work opportunities to offset risks and improve margin. Commercial Airplanes won 412 net orders during the quarter, valued at $21 billion. The Commercial backlog remains strong with over 4,000 airplanes valued at a record $308 billion.

Moving now to Slide 6, and we'll discuss the Defense, Space & Security business. Boeing Defense, Space & Security reported first quarter revenue of $8.2 billion with operating margins of 9%. Boeing Military Aircraft quarterly revenues increased 27% for the quarter to $4.3 billion, driven by the successfully completed key development milestones on the F-15 Saudi program. Operating margins remained strong at 10.1%.

Network & Space Systems revenue of $1.8 billion decreased last year, driven by the expected lower volume associated with the Brigade Combat Team Modernization program. As anticipated, operating margins decreased to 4.1% primarily due to lower volume and program mix in our satellite business.

Global Services & Support revenue increased 13% to $2.1 billion for the quarter, primarily driven by higher revenue on integrated logistics support. Operating margins were very strong at 10.9%, reflecting performance improvements on multiple integrated logistics programs.

Defense, Space & Security backlog significantly increased in the quarter to $72 billion, driven by F-15 and C-17 international orders. Over 35% of our current defense backlog represents international business.

Now let's turn to Slide 7 to discuss our other businesses. Boeing Capital generated $38 million in segment earnings in the quarter. The portfolio balance declined to $4.2 billion on normal portfolio runoff and asset sales with no new aircraft volume in the quarter. During the quarter, other segment expense was $79 million, while unallocated expense were essentially flat year-over-year, reflecting the $131 million reduction in the litigation-related reserve, which was offset by higher pension expense this year.

Let's turn to Slide 8 and we'll discuss cash flow.

During the quarter, we generated $837 million of operating cash, reflecting increased commercial deliveries and advanced payments as well as progress payments on the Saudi F-15s. We expect cash flow to build over the course of the year as commercial deliveries increase, and we will continue to execute our disciplined cash management actions.

Turning to cash and debt balances on Slide 9.

We ended the quarter with $10.5 billion of cash and marketable securities. Our cash and debt balances reflect the first quarter repayment of $774 million of BCC debt. Our cash position continues to provide strong liquidity and positions us well going forward. Capital expenditures of approximately $424 million were as expected.

Turning now to Slide 10 to discuss our outlook for 2012. Our financial outlook continues to be balanced, reflecting strong operating performance on our production and services programs and is -- and has consideration for uncertainty and risks associated with ongoing business growth. We are increasing our earnings per share guidance to be between $4.15 and $4.35 per share to incorporate the reduction in a litigation-related reserve. All other financial guidance remains unchanged. Commercial deliveries forecast remains at about 585 to 600 airplanes. Our forecast continues to include a combined 70 to 85 787s and 747-8 deliveries split roughly equally between the 2 programs.

Overall, we're pleased with the first quarter performance as the core operating engine continues to deliver strong results. We expect that performance to continue as we remain focused on production program profitability, rate ramp-up and ongoing productivity improvements.

Now I'll turn it back to Jim for some final thoughts.

W. James McNerney

Thanks, Greg. With a strong first quarter, we've built on our momentum from 2011 and increased our confidence in meeting our goals for 2012. Our priorities and focus for the year remain the same: production ramp-up and profitability across all our Commercial Airplane programs; successful execution of ongoing development efforts on the 787-9, the 737 MAX and the Air Force Tanker; and repositioning our Defense business while extending our core programs and expanding internationally.

Now we'd be happy to take any questions you might have.

Question-and-Answer Session

Operator

[Operator Instructions] Our first question will be from Doug Harned with Sanford Bernstein.

Douglas S. Harned - Sanford C. Bernstein & Co., LLC., Research Division

Jim, when we look at the 787, cost still look very high to us and -- based on deferred production numbers. And presumably, you'll be able to take a step function down in those costs at some point. And perhaps that point is when you get out in the line mid -- line numbers in the mid-60s in order to get the program on a track that's clearly profitable and ensure that your suppliers can uniformly deliver. Well, first, do you expect by midsummer when you get into those line numbers that you'll have high confidence that you're on that track? And what operational and financial goals are you following so that you'll know you're there when you've made it?

W. James McNerney

I -- well, it's a timely question. I just got back from Everett and Charleston, taking a look at the lines. Doug, I think our confidence grows every day, quite frankly, in our ability to deliver the learning curve that underlies our plans. I think we do have a high degree of confidence that the mid-60s line number will be -- will have the production lines flowing exactly the way we want it. And the change incorporation side of Everett is also performing well on those planes that -- where we did have a significant amount of rework. And that is going well, too. I mean, as we modify more planes, there's a learning curve involved there, too. And we are on track with both the regular production and the modification. I would also add that Charleston looks very good, and we -- you're going to see the rollout of the first airplane later this week and delivery this summer. And I think the learning curve progress in both places are giving me more and more confidence every day that the costs that underlie our plans are going to be met.

Douglas S. Harned - Sanford C. Bernstein & Co., LLC., Research Division

But are you expecting, though, that there's a point in time when we should see something that moves significantly lower? What I'm getting at is a lot of times in the early stages in a program, you may not come down on the learning curve smoothly but might have break points that -- you see a drop down and then you reset. I mean, are you looking for something like that?

W. James McNerney

Yes, I think, the -- I'm sorry, go ahead, Greg. You...

Gregory D. Smith

Yes. Just let me just try to take a shot at this, Doug, and give you some perspective. But certainly, when you look at a unit cost -- from a unit cost perspective, from the first airplane that was delivered, say, to like line 60, we're seeing about a 40% to 50% reduction in unit costs. And that's truly coming down that learning curve. Now there's no question it's bumpy when you look at it per unit because some of those airplanes have been in flow longer than others. But when you just generally look at the trajectory, it is coming down the curve that we would expect. When you asked that -- what do we look at specifically, obviously, we're tracking airplane by airplane versus what we would consider our target and budget. We're looking at out-of-position items on every airplane, shortages, condition of assembly, quality, flow time, how many hours we're burning per job versus what we budgeted. And all of that, obviously, given us the confidence to make either the next rate break or overall indicators the production health of the system.

Douglas S. Harned - Sanford C. Bernstein & Co., LLC., Research Division

So by midsummer, you're expecting -- so right now, things are lining up as you would like them to for midsummer when you get to this presumably smoother flow?

W. James McNerney

Yes. Yes.

Gregory D. Smith

Yes.

W. James McNerney

And we'll still have planes in change incorporation at that time, Doug, okay?

Douglas S. Harned - Sanford C. Bernstein & Co., LLC., Research Division

Sure, sure.

W. James McNerney

But we'll be working that down, which is the second element of the equation. As that gets worked down on plan, and by the second half of the year, you should notice a significant decline in the number of those planes hanging around and delivered to customers. And so it's a combination of both the production line smoothing out beyond line mid-60s and change incorporation planes being delivered, I think, is going to give you the same confidence we have today.

Operator

And next we go to Carter Copeland with Barclays.

Carter Copeland - Barclays Capital, Research Division

Just a clarification and then a question. Greg, on the accounting differences in the quarter. It looks like you have just about just over $1.2 billion. I wondered if you could comment on what the gross amount would have been for the development programs and whether that was materially higher than the net that you reported for the quarter.

Gregory D. Smith

Yes. So on that difference, about -- roughly about 80%, 85% of it was 787 related, if that helps you.

Carter Copeland - Barclays Capital, Research Division

Okay. Yes. And so the remainder would have been 7 4. But what -- on a gross basis, was that in excess of $1.2 billion? And we had negative spending in other programs?

Gregory D. Smith

Yes, yes. So for -- yes. Well, no, there was positive on -- particularly on 777 and 737. That was about $150 million to $200 million.

Carter Copeland - Barclays Capital, Research Division

Okay, great. And you stated briefly that improving profitability on the 87 and the 47 were -- was a focus.

Gregory D. Smith

Yes.

Carter Copeland - Barclays Capital, Research Division

Would you think it's possible? I mean, I'm not thinking short term here. But per that comment, would you think it's possible to increase the reported margins on these programs without seeing block extensions? Is that something that's was in the realm of...

Gregory D. Smith

Yes. Yes, that is. I mean, certainly, block extensions would help. But putting that aside, just to give you some -- I talked about -- on the last call, but we're looking, obviously, within the factory, and some of the stuff we just talked to Doug about. But also within the supply chain, we've got about 300 to 400 different projects in-work right now that are all around profitability. So as those mature -- and some of those, obviously, won't all come to fruition, but the ones that do mature, then we'll put them in the booking rate.

Carter Copeland - Barclays Capital, Research Division

What's the sort of general timeline on those sorts of projects?

Gregory D. Smith

They really range, but we've got a good process in place for identifying them and then bringing them to maturity. But just depending on how complex they are, Carter, depends on how we can get comfortable that we can really capture the productivity that maybe was initially identified as we went through the process. And as I said, we're doing that with our supply chain as well and utilizing our experience with this and some of our lean experts, and bringing them out to the supply chain. And we're going to be doing a lot more of that going forward as we continue to focus on profitability on this program.

Operator

And we'll go to Sam Pearlstein with Wells Fargo.

Samuel J. Pearlstein - Wells Fargo Securities, LLC, Research Division

Can you talk a little bit about your guidance? And you basically said nothing really changed other than this reserve reversal, and yet there was significant upside in the quarter. And I'm trying to think about go -- what's not sustainable? We know the 87 is going to drag down the BCA margin. But the flip side is -- certainly, NSS margin was well below what you're saying it's going to be for the year. So can you just talk about the remainder of the year?

Gregory D. Smith

Sure. Well, as you said, we had a great first quarter and off to a great start, but it's early. When you look at the balance of the year, I think we've got great plans in place to execute. But we do have the, as you said, the dilutive impact on the margins on the 87 and the 47. We've got some plans for investment in some productivity tools. As we get these programs at a higher rate, we're again looking for further opportunity to streamline the production system and lower flow times. Obviously, we got some taxes with those higher deliveries in the back half of the year. And then we do have some provisioning for just risks and uncertainties that are just tied to -- in fact, we got to make another rate break, which, again, I -- we got good plans in place to do on the 87. And we got a 47 rate break coming up. And so we're just kind of provisioning for that as we execute. Now if we execute through that, that'll certainly give us more confidence, and we'll come back to you.

Samuel J. Pearlstein - Wells Fargo Securities, LLC, Research Division

And anything about NSS? Why margins were so low this quarter and why they should recover to kind of 7.5% over the course of the year?

Gregory D. Smith

Yes, yes. I mean, so some of it is volume. It's just BCTM coming down, as we expected. We had fewer launches in the quarter. And then we had a mix between -- on the satellites between government and commercial. And then some adjustments, some small adjustments to EAC. So that's basically it. And we see good plans in place to recover, to be within our guidance for the balance of the year.

Operator

And we'll go to Joe Nadol with JPMorgan.

Joseph Nadol - JP Morgan Chase & Co, Research Division

I'd like to come back to the 87 with just a couple more numbers, probably the only ones you haven't provided. And that's -- could you give us the WIP at the end of the quarter, the total WIP on the 787? And also, I'm wondering, Greg, if you could break out, this might be helpful, the $1.2 billion increase in deferred production costs? Is there any way of breaking that out between units, excess over average and change incorporation? Does that -- I think that might give us a better sense as to how things are tracking. Finally, on the same point, and sorry for the 3-part question, but it's all kind of the same thing, you already gave a nice number of 40% to 50% reduction in unit costs on the 87 over -- thus far. I'm wondering if that somehow you could quantify the improvement you're seeing in change incorporation. Because certainly, it didn't -- it looked like you had some setbacks during the quarter.

Gregory D. Smith

Yes. Okay, let me start there. I mean -- yes. I mean, when you look at those units, as I said, 40%, 50% on average is what we're seeing. On the change incorp airplanes, certainly a lot -- they're all different depending on what condition of assembly and what changes need to put in place. So what we have there is kind of traditional metrics in place about cost per job and how many open jobs are left, et cetera, by airplane, by section of the airplane. And that's where we look at the productivity there of are we achieving the plans that we have in place there or not? I would tell you as of now, we're within our plans. So what we had originally thought that it would take to complete those airplanes, we're coming down that trajectory. So certainly, still a lot of work to do there, but we're making good progress. I would tell you we're trying to take advantage of learning in a nontraditional assembly environment, where we've got the airplanes broken out depending on the number and the complexity of the jobs open, and we've got mechanics assigned to the same job. So an example. If you're assigned to take this wire harness out on this airplane, you're taking it out on future airplanes. And we hopefully capture a learning within, and we've experienced that up to now. So I think we've got that well understood. But certainly, a lot of work in front of us. But I think it's operating very well. Your other question on 787, it's about $22 billion gross inventory.

Joseph Nadol - JP Morgan Chase & Co, Research Division

What was the WIP portion of that, though, if you have that? I got the other number off the call. But...

Gregory D. Smith

About $17 billion.

Joseph Nadol - JP Morgan Chase & Co, Research Division

$17 billion. And then of the $1.2 billion in deferred production costs during the quarter, can you break that out between the 2 components? What is unit 50, whatever? And what is fixing up unit #15?

Gregory D. Smith

Yes, most of it is in the factory, not in change incorp.

Operator

And we'll go to Rob Spingarn with Credit Suisse.

Robert Spingarn - Crédit Suisse AG, Research Division

Greg, if we could stay on that topic and maybe throw a few more numbers out now that we have the WIP. I -- if I go back to Q3, it looks like unit cost was a little over $300 million, and deferred production by unit was about 2/3 of that. So let's call it $216 million. And then using the numbers you just gave us, the $216 million has dropped about $10 million a quarter. I calculate $196 million for Q1 in deferred production per unit. And the total unit cost is about $279 million. So down 13%. That $279 million, based on the comment that you made earlier, about a 40% to 50% drop, am I to understand that, that gets down to the $200 million level or $190 million by the time we get to that line number you talk about?

Gregory D. Smith

I mean, it's 40% to 50% from the first delivery to about line 60.

Robert Spingarn - Crédit Suisse AG, Research Division

Oh, that's where I'm getting...

Gregory D. Smith

And that's on average. But I can tell you -- and hopefully, this answers your question, but we're seeing unit cost improvement on the airplane quarter-over-quarter.

Robert Spingarn - Crédit Suisse AG, Research Division

Is -- from a deferred production basis, maybe this is the best way to talk about it, you've done a little over -- about $10 million per quarter. How do you see that curve continuing over the rest of the year by quarter?

Gregory D. Smith

Ask that again, I'm sorry.

Robert Spingarn - Crédit Suisse AG, Research Division

Well, so we've gone down about $10 million per quarter in deferred production on a unit basis. So let's call $216 million in Q3. We're at $196 million in Q1. Does that $10 million start to expand and accelerate each quarter from here on out? How do we think about that $10 million evolving?

Gregory D. Smith

Yes, it does. But as I said earlier, on a -- when you look at it on a unit basis, it's not linear because of the different airplanes that you're delivering. So you're delivering some out of change incorp, you're delivering some out of final line. So it's not -- you're not going to see the linear effect quarter-over-quarter here. But overall, it's -- we're seeing improvement on a unit cost basis.

Robert Spingarn - Crédit Suisse AG, Research Division

Is it fair then, Greg, to ask the question what should the number be on that 60? On that first airplane that avoids the mod?

Gregory D. Smith

What number?

Robert Spingarn - Crédit Suisse AG, Research Division

On line 60. Since that aircraft is now a modless airplane, according to what Jim said, it's -- it doesn't have that stop, that interim stop. What should the deferred production be at that point? You will have gotten the out-of-sequence stuff out of the way.

Gregory D. Smith

Well, I mean, all I can tell you is that on a unit basis, it's a 50% improvement. When you -- that's what we look at as, obviously, we look at the deferred production. But we're looking at improvements and coming down learning curves, we look at it on a unit by unit basis, and that's essentially what we're seeing right now.

Robert Spingarn - Crédit Suisse AG, Research Division

Okay. And then just to finish up on the topic, you said $24 billion at the end of the year in terms of 78 inventory, I think you said?

Gregory D. Smith

Yes.

Robert Spingarn - Crédit Suisse AG, Research Division

What is that number when deferred production stops growing, out a couple of years from now? Which I think is what James guided to maybe a few quarters back.

Gregory D. Smith

Yes, I don't think we've talked about that specifically. What we did talk about is that deferred production will hit about $20 billion at about -- in 2013. And then as we continue at 10 per month, that'll start to burn off.

Operator

And we'll go to Noah Poponak with Goldman Sachs.

Noah Poponak - Goldman Sachs Group Inc., Research Division

I wanted to go back to the -- a few questions ago on the full year outlook. I believe last quarter you said that you expected 20% of the full year earnings to land in the first quarter. And you now have 29% of the full year earnings having occurred in the quarter, 27% if we take that 11 out of the numerator and the denominator. So that would either mean that, one, your full year number is just too low; or two, you had a decent amount for earnings occur earlier in the year than you anticipated. Can you say which of those it is? And if it's the latter, what happened?

Gregory D. Smith

Well, we had -- obviously, we had the onetime on the legal reserve and then we had Saudi. So as you know, we started that contract early, and we reached an agreement. And we were able to meet those milestones and capture that revenue in the first quarter, all in the first quarter. So that was pretty significant, not something that would continue through the balance of the year.

Noah Poponak - Goldman Sachs Group Inc., Research Division

Okay, that's helpful. And just on the balance of the year, the -- to get into the BCA margin guidance, you have to have significantly lower BCA margins than you did in the first quarter. And you've talked about what some of those inputs are. The one I struggled the most with is just the new program period expense. Can you quantify as of now how you expect that to play out through the rest of the year?

Gregory D. Smith

It is purely on fleet support or just in general?

Noah Poponak - Goldman Sachs Group Inc., Research Division

Yes. Well, both if you can.

Gregory D. Smith

Yes. I mean, we expect fleet support to kind of moderate now that we've reached the level from -- going from Q4, Q4 last year to Q1 this year. So that -- we expect that to moderate. But there is some increases in period expense like I talked about earlier that we're expecting in the kind of third, fourth quarter timeframe. That, combined with the dilution, is really what -- what's driving that. And like we said, we're provisioning for some uncertainties as we get through these rate breaks, which we certainly plan to, and we got good plans in place, we'll readdress it.

Noah Poponak - Goldman Sachs Group Inc., Research Division

Can you quantify what the fleet support is and what the other period expense is?

Gregory D. Smith

No. Not yet. I mean, I just -- they're essentially in line with what we had this quarter. And primarily all driven by 87.

Operator

Our next question is from Howard Rubel with Jefferies.

Howard A. Rubel - Jefferies & Company, Inc., Research Division

Okay, I'm going to change the subject entirely, and we're going to talk something called orders and opportunity, okay?

Gregory D. Smith

I think that was our...

Howard A. Rubel - Jefferies & Company, Inc., Research Division

We beat the rest of that to death. The -- you've signed an agreement with Embraer. You've been able to extend the C-17 line. The F-15 capability on the Saudi airplane is better than the U.S. Air Force has today. Could you talk about what you're doing to make that military portfolio more attractive?

W. James McNerney

Well, you've named a couple of things right there. I mean, I think the C-17 affordability and acceptance on a global basis is progressing. The F-18, which you didn't mention, is a highly affordable aircraft. The last multiyear took significant cost out of the aircraft and shared it with our customer. I think our Satellite business, if you look at the market share associated over the last 12 months and also going forward, looks very promising. You've seen an expansion of our product line in the Satellite business to the medium power and the smaller satellites, both of which have good launch orders. I think the Helicopter business remains very committed, too, even in a very difficult budgetary environment, and our position in the Helicopter business is about as strong as you can get. And it's -- and I -- and that's clearly because any conflicts that can be envisioned out there are -- in many ways are buttressed by a strong position to be able to move troops around regionally quickly. There's a -- and then, of course, we've invested significantly over the last few years either through prototyping or external growth and acquisition in cyber, unmanned and ISR. So we're trying to position ourselves well for that world that's coming at us. And when you add it all up, both on market share on the international side is increasing, and our -- the -- and our position within the U.S. budget is strong. And I didn't even mention P-8 and Tanker, which are the 2 growth programs that are on top of all of that. So we feel like it's a down environment in defense. We feel about as well positioned as we could be. And as you know, we're addressing the cost issue very aggressively on top of all of that.

Howard A. Rubel - Jefferies & Company, Inc., Research Division

Well, maybe what I'm -- I don't want to take too much -- but is there anything more immediate? I mean, for example, with Embraer in Brazil. I mean, is there -- I mean, clearly, the Pentagon recognizes a need to improve relationships there, and you've signed some agreements. Is this a foreshadowing of an improvement in your competitive position? Or is this still a long putt?

W. James McNerney

When you talk about -- I see. So...

Howard A. Rubel - Jefferies & Company, Inc., Research Division

F-18 sales to Brazil.

W. James McNerney

Yes, yes. Okay, I...

Howard A. Rubel - Jefferies & Company, Inc., Research Division

Sorry, Jim.

W. James McNerney

So when you say Embraer, you're talking about some localization efforts we've got in Brazil. I see. Yes, I mean, the F-18 Brazil competition is along with similar competition in the UAE and other places. I mean, we have some significant international opportunities. I think we have a good shot in Brazil.

Howard A. Rubel - Jefferies & Company, Inc., Research Division

And then just one quick numbers follow-up. If I look at your pre-R&D numbers on Commercial, Greg, versus a year ago, they're about 300-basis-point difference. Is that most of the period cost and other items you have addressed? Because it sort of masks what would appear to be productivity improvements in the core business.

Gregory D. Smith

Yes, I think you got it, Howard.

Operator

Our next question is from Jason Gursky with Citi.

Jason M. Gursky - Citigroup Inc, Research Division

Just a quick question on the 37 and the 777. Can you talk about both the pricing environment as well as the productivity environment on those 2 programs and what your view is on margin rates for those 2 programs as we move out over the next couple of years?

W. James McNerney

I think the summary on pricing is 777 steady, steady as she goes, capturing value, in many ways a uniquely positioned airplane today and significant productivity associated both with better conversion and with taking up rate. So the margin environment there, I would say, is good and favorable going forward. 37, all of the comments I just made on productivity apply. Significant productivity, both absorption kind of productivity due to increased rate as well as conversion productivity per unit. Slightly more aggressive pricing environment due to the introduction of the MAX and the NEO. So there's launch customer kinds of pricing that have happened in a few cases. But I think at the end of the day, the -- we anticipate about half of that market, which is a big number. And we see a pricing environment that's not too different than the pricing environment we've had historically after we get through some of the launch customer -- loss -- launch customer pricing, which is part and parcel with our business.

Jason M. Gursky - Citigroup Inc, Research Division

Right. So does the -- did the productivity gain offset the pricing pressure so that margins can remain resilient? Or do we see some pressure on margins?

W. James McNerney

Yes. Well, our philosophy is that we don't let pricing get in the way of margins. And the answer to that is productivity. So that's the plan.

Operator

And we'll go to Heidi Wood with Morgan Stanley.

Heidi R. Wood - Morgan Stanley, Research Division

Jim, a question for you. I've been thinking about your product lineup versus what your airline customers seem to want and the sort of growing trend towards up-gauging. Can you talk to us a little bit about what your strategy is to address the airline needs to -- that currently operate 757s on the North Atlantic and the 57 users where they can't replace their planes with A321s or 900ERs? Or if they have to choose, they appear to be leaning towards the A321 versus the 900ERs. What's your strategy to fill that hole?

W. James McNerney

Well, I think job 1 is to get the MAX in the marketplace. And as you point out, the MAX-9 and the A321 do fill a lot of that mission. Now admittedly, I think there -- when you compare it only to a 757, there is a -- you've either got to stress this -- the -- A3 stretch in the sense of stretch economically or mission-wise the -9 or the A321 into some of the thicker routes that the 75 is involved with. And I think we're trying to think through exactly how to fill that market. But the largest part of that segment is going to be filled by the larger versions of the narrow-body. But there's some product planning we have yet to do to do it, and we'll announce that in due course.

Heidi R. Wood - Morgan Stanley, Research Division

All right, great. And a follow-up to Jason's question. The -- some of us are hearing anecdotally that the A320 NEO pricing is either at current A320 prices or, in some cases, seems to be below. So did I hear you correctly in terms of what you've intimated on pricing on the MAX that you offset efficiency with possibly deleterious pricing? Is this also -- but is there also embedded escalation help offset that?

W. James McNerney

Yes, it -- I mean, you know the equation. I mean, there are some competitive environments where the price, like it often does in these introductory environments, where the price was pretty aggressive, even more aggressive than an immediate productivity plan to offset the margin we have today. But our judgment is that over the long term, as you look at history and how these kind of pricing environments sort out, even when you're conservative, we feel comfortable that productivity in the long run, on a program basis, can offset the pricing, any pricing environment we see.

Operator

And next we go to Cai Von Rumohr with Cowen and Company.

Cai Von Rumohr - Cowen and Company, LLC, Research Division

This is the first quarter I can remember in history when you didn't have some kind of slip or screwup on the 787. So you've reiterated your guidance for 35 to 42 deliveries this year. Could you give us some color in terms of how that rolls out by quarter? And are there any opportunities, now that you've seen to have it under somewhat better control, to exceed those numbers or be at the upper end as opposed to just getting in at the low end?

W. James McNerney

Lee -- Cai, I would just say overall, as we've said, as we get beyond the engineering change and we stabilize the production base, this business will become more and more predictable in terms of its projected execution. And I'm -- it's -- I don't know whether to laugh or cry at the award you just gave us. First quarter ever. But having said that, we have increasing confidence that as the issue becomes more and more centered on production execution, which this company does pretty well, and we reduce the risk significantly on change incorporation and supply chain, we have growing confidence. Now the guidance we've given you has some back-end loadedness to it, and that's just because that's the way the production ramp is happening and that's the way the learning improvement in change incorporation is happening that Greg talked about. And so I would say while there may be an opportunity to do better than the low end of that guidance, and I think there is, but we're -- the guidance is what it is, I think the ramp nature of it leads us to be conservative and to call it that way as we sit here today.

Cai Von Rumohr - Cowen and Company, LLC, Research Division

Okay. And could you give us some update in terms of your headcount in BCA? Is that -- has that peaked? And what should we look for going forward and the implications for productivity?

Gregory D. Smith

Yes, Cai...

W. James McNerney

Yes, go ahead, Greg.

Gregory D. Smith

It does peak this year. And then as we kind of ramp off down on the development programs and come up more on the production programs and then with productivity, it comes down in 2013. That's the projection right now.

Operator

And we'll go to David Strauss with UBS.

David E. Strauss - UBS Investment Bank, Research Division

You guys had this delamination issue pop up during the first quarter on 87. Can you give us an update how things are progressing there, how many airplanes have had the issue did you fix? Is it taking the 10 to 14 days that Pat talked about, I think, back in February?

W. James McNerney

Yes. I mean, I think the -- as I think we told you then and as we feel today, the fix was understood quickly. It had to do with workmanship. The workaround was quickly identified. I think it is now -- has dovetailed both into change incorporation and the line. I think roughly 14, 15 airplanes have already been reworked. I think in our world, it did have a schedule impact within our month-to-month schedules, which we don't share with you, that doesn't impact our guidance for the year at all. But I would say, understood, fixed, moving forward and we're in good shape.

David E. Strauss - UBS Investment Bank, Research Division

And Greg, you talked about Saudi being a positive in the quarter. Can you quantify how much that was?

Gregory D. Smith

I'm sorry?

W. James McNerney

Saudi.

Gregory D. Smith

Oh, Saudi. About $800 million.

Stephanie Pope

Operator, we have time for one more analyst question.

Operator

And that will be with Rob Stallard with RBC Capital Markets.

Robert Stallard - RBC Capital Markets, LLC, Research Division

Jim, you mentioned in your prepared comments the production rate increases that have planned for the next 3 years at BCA. There has been some industry commentary that perhaps you and Airbus could be oversupplying the market. How do you get yourself comfortable that your customers are not over-ordering and there's not double booked slots [indiscernible]?

W. James McNerney

Well, I mean, obviously, we manage a process that tries to separate the wheat from the chaff implied in that question. I mean, we work very closely with our customers, understand the financeability of what they want to do, understand their fleet plans. In many cases, as you know, Rob, the demand for these airplanes is driven as much by fuel efficiency as it is by supporting growth. So -- and the price of oil, where it is and where most people think it's going to go, a lot of the demand is driven by replacing older aircraft or aircraft that may not have -- and that this may happen -- this may happen to a greater degree today than it has happened before because financial markets remain open to finance these things and this is all about improving the bottom line of the airlines. So it's some growth, particularly in Asia and Middle East, it's replacement in the developed markets supported by financing that's there. Then I would ask all the questions you'd be asking about: Is this a bubble? Is this -- can you support the growth? Are you going to be in business? And if we get to the point of seeing it differently, we'll adjust our plans.

Operator

And ladies and gentlemen, that completes the analyst question-and-answer session. For members of the media, if you have a question [Operator Instructions] I will now return you to The Boeing Company for introductory remarks by Mr. Tom Downey, Senior Vice President of Corporate Communication. Mr. Downey, please go ahead.

Tom Downey

Thank you. We will continue with the questions for Jim and Greg. If you have any questions after the session ends, please call our Media Relations team at (312) 544-2002. Operator, we're ready for the first question. And in the interest of time, we ask that you limit everyone to just one question, please.

Operator

And we'll go to Jon Ostrower with The Wall Street Journal.

Jon Ostrower

A question about the prospective takeover of American Airlines or merger between U.S. Airways and American Airlines there. Can you give some thoughts on what that order -- how would that merger, rather -- may mean for your order backlog? Obviously, there's -- U.S. Airways, which has been heavily leaning towards Airbus for the last, more than a decade. And can you just kind of share your thoughts on what it may mean for actually reaching 42 a month and really holding there for a while on narrow-bodies?

W. James McNerney

Well, obviously, we'll confront whatever environment we find. But I think the -- American is working through the process now, and they -- and we support them emerging from this thing as a stronger airline. If at that point, a merger makes sense to the 2 managements of the company, we'll support that as well. Obviously, U.S. Air does have more Airbus airplanes than Boeing airplanes right now, and American has got more Boeing airplanes than Airbus airplanes. And that's because of the missions they fly. So we've seen mergers before. If it happens -- it's not clear that this one's going to happen, by the way, in our view. But if it does, we'll confront the environment that we've confronted before and we tend to do pretty well.

Operator

Our next question is from Chris Drew with The New York Times.

Christopher Drew

Can -- if we can go back to Tanker for a minute. As you look back now over the past year, do you have a -- any better sense of why Airbus didn't bid lower as a first -- EADS didn't bid lower, first question. And then the second, there's been various stories about whether it was costing you, how much more it might be costing you or the government than you expected. And if you could sort of address where all that stands now.

W. James McNerney

Well, it's hard for me to know exactly why Airbus bid what they did or didn't. I think -- or EADS in this case. The -- I will say we were aggressive, as I have said, and we worked our supply chain very, very hard and got the same kind of commitments from them that we, in turn, were making to the Air Force, which is a fixed-price development environment. So a lot of elbow grease, a lot of working with partners in advance to get to a number that we thought was aggressive but responsible. We have known all along that the tightest part of the program for us will be the development phase, which is what we're in right now. But we're hitting every milestone. I believe, based on what they've said publicly, our customer is happy with the progress. We're focused on it every day. And there's no doubt that this is an aggressively bid program, but the war fighter and our customer is benefiting from our efficiencies. And the last thing I'd say is that we brought together the Defense side and the Commercial side of our company together more aggressively than we've been able to do historically, and we took a lot of inefficiency out of teaming together as One Boeing to get this pricing capability where it should be, as well as working with our supply base. So elbow grease is the answer to your question.

Operator

And next we go to Mike Mecham with Aviation Week.

Michael Mecham

I'd like to follow up a little bit on the situation with where you are in 737 MAX. Also, where you have been hit and how, from the situation in Wichita. Which programs, if there is any particular program, stands out as perhaps taking the most problem with this, if you can?

W. James McNerney

Sure. I mean, just an update on the 737 MAX program. We're on schedule. We have got the statement of work that we're going to do and not do. We'll have firm configuration next year. We think we struck the right balance between containing the work statement to reduce risk and providing the new engines and some other tweaks that bear only on the efficiency of this airplane for our customers. So we're feeling good. I think Wichita, the -- as you know, the Spirit operation supports a number of our programs. The -- where they have the most content is the 737. And they've been back to work full-time starting this Monday after roughly a week's delay. And we are cautiously optimistic that there will be no material impact to our programs, any of our programs, this year. And we'll update you if any of that changes.

Michael Mecham

Is there any part of this natural disaster situation in Japan and elsewhere that has caused the company to rethink? Or have you launched any rethink of your various facilities around the world? And just exactly what threats they're under and how they and you need to respond?

W. James McNerney

Well, I think you've seen us take some moves to diversify our manufacturing base somewhat. Charleston is an example. And that's -- that is an element of the thinking.

Operator

Our next question is from Brendan Kearney with Post and Courier.

Brendan Kearney

Jim, 2 quick questions. First, you said that the first delivery from South Carolina will be midyear in summer. Is that different from the June and second quarter estimates that other company officials have offered? And second, you noted you were here in Charleston yesterday. Are you making a return trip to Charleston this week for Friday's rollout? And which musician do you hope to hear perform at that event?

W. James McNerney

No, no, I didn't -- as to the first part of your question, the -- no, no change. I mean, it's -- those are one and the same comments. I'm just using slightly different wording. The -- and Jim Albaugh will be leading the entourage on Friday.

Tom Downey

Operator, we have time for one last question this morning.

Operator

That will be from Steve Wilhelm with Puget Sound Business Journal.

Steve Wilhelm

I just had 2 quick questions. One is, could you characterize the production lines in Everett and Charleston and just how they're different? What ways that they're approaching things differently or the learning curves are different because of their experience? And is -- that's one question. And then secondly, there's been a lot of rumors about your turbo fan option for the MAX. I just wondered if you could address that.

W. James McNerney

Yes, I mean, I think the point of the 2 production lines in Everett and Charleston is more that we're trying to make them the same than we're trying to make different. We're trying to leverage the same processes, the same learning across our company. So leaving the change incorporation side of Everett aside for a second, the 2 production lines, as we envision them and as we're managing them, are -- we're trying to duplicate and learn rather than separate and be different. The -- what was the second part of your question?

Gregory D. Smith

The gear turbo fan.

W. James McNerney

The gear turbo fan, the -- yes. The -- right now, as I think we've announced many, many times, we are working exclusively with CFM on the MAX, and we're very happy with the development there. We're confident that we can meet the targets that our customers need and that we've promised them. So that's our plan going forward.