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# Avis Budget Group, Inc. (CAR)

Deutsche Bank Leveraged Finance Conference

# CORPORATE PARTICIPANTS

David B. Wyshner
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*Deutsche Bank Securities, Inc.*

# MANAGEMENT DISCUSSION SECTION

## Chris J. Woronka
*Deutsche Bank Securities, Inc.*

Hi, everybody, I'd like to welcome Avis Budget Group here today.

With us we have the CFO, David Wyshner; and Head of Investor Relations, Neal Goldner. David?

## David B. Wyshner
*Chief Financial Officer & Senior Executive VP*

Thanks very much, and thanks for joining us here today. Really appreciate the opportunity to present, and I want to thank Deutsche Bank for inviting us to their Leveraged Finance Conference again this year.

My presentation today will include forward-looking statements and the usual caveats and disclaimers related to those apply. What I'd like to do today is spend a little bit of time talking about our business overall, and then provide an update with respect to recent trends in our business.

Avis Budget Group is a global leader in the car rental industry. We generate more than $8 billion in annual revenue; have more than 10,000 locations throughout the world; using more than half a million vehicles with our Avis, Budget and Zipcar brands. We typically have a leading position in the markets that we serve.

Our revenues are diversified along a number of different axes. As you can see in the slide here, Avis represents around two-thirds of our volume; Budget, about a third; Zipcar is a small and growing component of our revenues. Our revenues are split almost exactly 50-50 between commercial and leisure business. We generate about two-thirds of our volumes at airport locations and about a third of our revenue now is coming from outside the U.S.

We operate directly in about 20 countries throughout the world, and we operate through licensees in more than 150 countries around the world, giving us a leading position in almost all major markets.

Our results in the first half have been strong. Our adjusted EBITDA grew 21% year-over-year to $330 million, and we've achieved an improvement in our margin as well. That's 75 basis points at 8.1% in the first half of the year.

Some of the key trends driving this in North America have been our ability to grow revenue by growing both rental volumes and pricing. As you could see, in the second quarter, our volume was up 5%, price was up 4%; and this contributed to the revenue growth that we've seen, as well as assisting our earnings and margin improvement over that period of time. The other key driver of our results is fleet costs, which have been more of a challenge so far this year; and I'm going to talk about that a little bit more in a few minutes.

The strength of our earnings and our free cash flow over time has allowed us to reduce our leverage fairly significantly. And what you can see here is a substantial decline in our net debt to EBITDA from 2009 to 2013, even as we acquired Avis Europe in 2011 and acquired Zipcar in 2013.

A number of years ago, we established 3 times to 4 times net leverage as our target. That continues to be our target. And over time we would become more and more comfortable with the lower half of that range, trying to stay in the 3 times to 3.5 times range, but occasionally moving up closer to 4 times when we've had a significant transaction.

For those of you who've been following us over a number of years, our strategic plan hasn't changed significantly over the last several years. The four pillars are the same. They're about strategically accelerating our growth, expanding our global footprint, putting the customer first, and driving efficiency throughout the organization. These pillars of our strategic plan have allowed us to grow our earnings and reduced our leverage significantly over the last few years and are allowing us – and are forming a number of decisions we make in our business every day.

I'd like to provide a few examples of what these strategic pillars translate into in terms of how we operate our business every day and how we go about growing our earnings. To us, strategically accelerating growth is about growing disproportionately quickly in areas that are disproportionately profitable.

On this slide, we present a few good examples of exactly what that means in transactions such as international inbound customers, small business renters, customers who take specialty and premium fleet and customers that are more likely to take ancillary revenues such as GPS rentals, XM satellite radio and insurance and damage waivers.

These customers all tend to be disproportionately profitable in our space because of their characteristics as customers. They're paying a higher price for ancillary revenues or specialty or premium fleet. In the case of international inbound travelers, having more needs for insurance products and being more likely to take GPS, having a longer length of rental, all things that tend to make the revenue per transaction and the profitability per transaction significantly higher.

And what we've done is target our marketing, our customer relationship work, our outreach and our customer retention initiatives, all in ways that are intended to drive additional volumes in these areas. In some ways, we're not focused on growing our overall market share, but we do look to grow our share in areas that we can make a disproportionate amount of profits in.

Early last year, we announced the acquisition of Zipcar. For us, it was part of expanding our footprint and our business model through the acquisition. Zipcar operates the largest car sharing network in the world. We see Zipcar as a significant growth opportunity for us. We see growth opportunities in existing markets from new services and from international expansion. We just launched in Paris over the last couple of weeks, which represents our fourth major market in Europe.

We see opportunities for new services such as providing Zipcars at the airport, which we've been doing since last year; and in providing one-way Zipcars as well, which we're piloting in Boston currently, as well as expanding some of the other services Zipcar provides having a wider range of vehicles available and making Zipcars available at airports as well. All of these are opportunities that we seek to continue to grow this brand, which has great recognition and an outstanding brand reputation in its space.

The fourth pillar for us is really about driving efficiency throughout the organization, and there are numerous examples of it. We highlight four of them here, each of which is worth mentioning quickly. In the area of fleet optimization, we're using optimization tools to reduce our acquisition cost, optimize the usage of the vehicle over its life, and then find the right time and place and way to dispose of those vehicles, so as to keep our fleet cost to a minimum.

We've been investing significantly in yield management technology program that's going on right now, that we refer to internally as demand fleet pricing is going to allow us to integrate yield management and fleet sizing in a way that will deliver incremental value. The first phase of it, a robotic that allows us to publish tens of millions of prices each day, ideally by 9 AM Eastern, is generating a significant amount of value for us; and I think will continue to do so. We're looking to roll that out to other parts of the world even sooner than we had previously planned.

The third box here is performance excellence, the process improvement initiative that we launched in 2007. It's been a huge win for us, delivering tens of millions of dollars in benefits as we find ways to improve processes throughout the organization and in virtually every area of our business.

And the fourth area that I highlight here is in the area of acquisition integration, whether it's Avis Europe, Zipcar, Payless or other tuck-in acquisitions that we've had. We've used the integration process to take out cost and drive efficiency throughout the organization. And what's particularly noteworthy is that each of these initiatives is providing eight figure $10 million plus benefits for us, and really helping us drive increased earnings and margin over time.

Another key element of our business model and our results over the last few years has been our ability to generate free cash flow. Our business at its core is a cash business, and we're not currently a federal cash tax payer in the U.S. As a result, a substantial amount of our pre-tax income translates into free cash flow each year. We're targeting $425 million of free cash flow in 2014 and potentially north of $0.5 billion of free cash flow next year. And this means that over the two-year period we could be generating $8 or more free cash flow per share from our operations.

What I'd like to do here is to take a few minutes before I wrap up to provide an update on recent trends in our business. First, in the area of pricing, the best news has continued to be on the North America pricing front. Realized pricing played out over the course of this summer as we had hoped in North America; and our T&M revenue per rental day in September was up year-over-year as well.

We expect to report a price increase of 3% in the third quarter, excluding currency effects, even including a 0.5 point headwind related to growth in our Payless brand. And while Payless does have a negative impact on our overall average pricing, we estimate that Payless's average daily rate will be up mid-single digits compared to last year's third quarter.

On the flip side, used car prices have continued to soften over the last several months, probably more than typical seasonal patterns would explain. Our sense is that the used car market is being impacted by the high level of recalls this year. In particular, recalls caused fewer off-rental cars to be sold in the first half of the year as the industry needed to hold additional vehicles to be able to be able to satisfy peak demand. This new ways may still take a few months to sort itself out in the used car market.

We said on our last call in early August that we expected our per unit fleet cost to tend toward the higher-end of our projection for this year. And at this point, my sense is that we may be slightly above the high end of the $300 to $310 range we had projected. We believe that having program vehicles represent a third of our fleet; and having completed two-thirds of our risk car sales through July will mitigate the effects of recent trends relative to the impact on our competitors. I also expect we will continue to use all levers at our disposal, including car rental pricing, to offset higher fleet cost in order to protect our margins and improve our returns.

In our International segment, demand was softer than we had expected this summer, particularly in Europe. We believe this dynamic was consistent with the economic data that are emerging. But this year's demand softness and the fact that demand was relatively strong last year played a role in the car rental industry being somewhat over fleeted in Europe over the summer. This impacted both pricing and our efforts to replace lower margin broker intermediary volume with transactions booking through our own direct channels.

Fortunately, our teams in Europe and Australia have continued to find ways to manage costs and deliver results near our plan for the year, even in the phase of soft demand. In fact, I'm hopeful that we'll be able to report record revenue and record EBITDA in our International segment this quarter. And this is despite an economic environment in Europe that we believe has largely gone sideways over the last year.

And the capital allocation side, we've seen our pipeline of potential tuck-in acquisitions strengthen over the last two months. We currently have three noteworthy transactions that we hope to complete over the next six months or so, up from only one a couple of months ago. I can't say any more about these at this point other than all three would be at prices and with synergies that should allow us to own the business at attractive multiples of EBITDA in relatively short order.

At the same time that our pipeline is strengthened a bit, we've also continued to repurchase shares, buying roughly $60 million of stock in the third quarter. At this point, despite the upward pressure on fleet cost that I mentioned, we continue to expect that our 2014 EBITDA will be somewhere in the $860 million to $910 million range that we projected at the beginning of August, though the higher end of the range certainly looks challenging right now. And finally, we remain committed to achieving our goal of $1 billion of EBITDA in 2015.

In summary, then as we look at our business, we see it being distinguished by strong performance both from an operational and a financial perspective. Our focus on profitable growth is remaining consistent with what it's been in the past, not just growth, but focused on profitable growth. We see multiple opportunities to grow globally both with the Budget brand in Europe and Zipcar, plus organic growth across our brands. And we're generating significant earnings and a substantial amount of free cash flow from our business.

I very much appreciate you taking the time to join us today, and I'd be happy to try to answer questions you may have.

# QUESTION AND ANSWER SECTION

Q

[Question Inaudible] (15:44-16:06).

David B. Wyshner
*Chief Financial Officer & Senior Executive VP*

A

Sure. For folks on the webcast, the question is about the trends and how we're thinking about fleet cost? And as I mentioned, we're currently estimating that fleet cost will be slightly above the range that we had previously estimated, of $300 per month to $310 per month. And what we've seen over the course of the year is a little bit more strength early in the year, February, March, April, than we had expected, and that played out well.

And since that time, as you could see in the overall Manheim Index and particularly the rental risk index that Manheim also publishes, the used car market has softened fairly considerably over the last three months or four months. We see that trend continuing into September as well. And it's moved our per unit costs up probably a couple of dollars above the range we had previously estimated. And it's really being driven by – that change in view is being driven by what we're seeing in the auctions and in the used car market every day.

And I think what we've gone through this year is a situation where we and the rest of our industry has faced an unprecedented number of recalls. And the plans we had at the start of the year to optimize our fleet cost in terms – by getting out of certain cars at certain times in certain places, essentially the optimization we had, had looked at the beginning of year has been challenged by the recalls.

Our ability to stick with those plans and optimize our fleet cost isn't what we would have hoped at the beginning of the year. And I think that's been true across the industry as well as we all try to find ways to hold on to some cars amid recalls in order to meet the demand that's out there and meet the commitments we have to our customers. And I think that probably gave rise to a little bit of the strength we saw early in the year, and now it's expressing itself in more noise and even a little bit of dislocation in the used car market over the last couple of months.

As I mentioned, we're fortunate in that we sold about two-thirds of the risk cars we planned to sell this year in the first seven months of 2014. That really has mitigated our exposure. But as we continue to – as we look at the used car market having softened, that is impacting where we're selling cars currently. And we're making sure we take the right approach in terms of how we think about the depreciation of the vehicles in our fleet going forward.

So that is having an impact on our results compared to where we had expected to be a couple of years ago. And one of the ways we're looking to address that is by continuing to be as aggressive as we can to push for pricing that we realize in our space. And I think the link between – an increase in our most important input cost, the cost of cars is – I think the link between that and pricing is important, and we're going to continue to push for pricing in the context of fleet cost being a bit higher than we've previously anticipated.

Q

[Question Inaudible] (20:02-20:14).

**David B. Wyshner**
*Chief Financial Officer & Senior Executive VP*

A

Sure. The question is about the restructuring that we completed in our Budget Truck business. And last year we did spend a lot of time and resources toward restructuring that business, reducing our dealer network a bit, to take out portions of our dealer network that weren't profitable for us and refreshing our fleet in the U.S. and shrinking the size of that fleet.

What we've done is modestly shrunk the Budget Truck Rental business to focus on its more profitable elements. And I think – and at the same refresh the fleet, so that we're providing the quality of vehicle rental experience that we want to be providing and that our customers expect. I think we're starting to see the benefits of that now. We don't have a large amount of our own capital tied up in that business. We're generating a significant return on the capital we do have there. And we see the opportunity for that business to continue to be a nice, relatively small contributor to our earnings going forward, but probably not an area that we'll devote a lot of additional capital to.

It now represents less than 5% of our business. But the work that our team has done to strengthen that business and to make it a nice, small contributing component of our business has really been outstanding. And I think we feel good about having it as a small component of our overall portfolio going forward.

Q

[Question Inaudible] (22:09-22:20).

**David B. Wyshner**
*Chief Financial Officer & Senior Executive VP*

A

Sure. The question is about our M&A pipeline. And I mentioned in my comments that we do have three transactions going on currently. They're all transactions that I'm hopeful will happen. Typically, we wouldn't talk about them at this point in the process for a variety of reasons related to the nature of that process.

But I thought it was important to mention because at the beginning of August we made the statement that our pipeline was [ph] light (23:02), we only had one transaction going on, we didn't expect to spend more than $50 million on tuck-ins over the remainder of the year. And it seemed as soon as we said that at the beginning of August, the opportunities on the M&A side strengthened over the course of August. And so, I wanted to use this as an opportunity to provide an update on what we're seeing there.

The transactions that we look at from an M&A perspective are primarily tuck-ins of one variety of another, often in the areas of licensees or areas where we currently operate and would see an opportunity to add locations and volume and perhaps a co-branding. And you've seen these from us over time whether it's the acquisition of Payless, which was its own brand, or some of the Budget acquisitions we've done in Europe. Over the last few years, we've added Portugal, Belgium, Luxembourg and Italy. All are areas where we operated Avis directly, but didn't operate the Budget brand. So we had significant opportunities for synergies.

And I think as we look at additional transactions, they do have the ability to vary in size quite a bit from those that are relatively small to those that are a little bit larger, even larger than Payless, which was a $50 million deal for us. But the common theme for these transactions is an ability to achieve the significant synergies, to buy them at a price that's reasonable, but to make the purchase price really attractive through the integration of their operations and their fleet with what we currently do. I think we're excited about the opportunities we see out there. And I guess I'm in the unusual situation of wanting to mention them, but not really being in a position to provide particular details about the individual transactions right now.

Q

[Question Inaudible] (25:34-25:47).

**David B. Wyshner**
*Chief Financial Officer & Senior Executive VP*

A

The question is about the international expansion and whether it would be a franchise. By way of background, we currently have licensee joint ventures or franchise joint ventures in several key growth markets for us. Those exist in Brazil, in China and in India, where we're at least a 50% owner of our licensee in each of those markets. Our focus has been very much on extending the reach of our brands in those markets.

And while we never say never to the possibility of adding something outside of our brands, I think we see significant opportunity to grow our brands and our presence in that space. And I would expect that to be our primary focus over the next few years. But we do look at opportunities when they come up. We try to be thoughtful in analyzing opportunities wherever they arise. And if the right opportunity arose, we could look at other structures as well.

But to be clear, our focus is on our existing brands and growing Avis, growing Budget and growing Zipcar's presence in markets throughout the world. The opportunity that Zipcar represents in markets in Europe, in Australia, in Zealand, in parts of Asia is really going to be quite significant over the next several years. And I think it's an area we're going to look to invest in.

**David B. Wyshner**
*Chief Financial Officer & Senior Executive VP*

Okay. Again, thank you very much for coming, and thank you again to Deutsche Bank for having us.