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Avis Budget Group, Inc. (CAR)

Q1 2014 Earnings Call
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MANAGEMENT DISCUSSION SECTION

Neal H. Goldner  
Vice President-Investor Relations, Avis Budget Group, Inc.

GAAP AND NON-GAAP FINANCIAL MEASURES

- Our comments will also focus on our results excluding certain items and other non-GAAP financial measures that are reconciled to our GAAP numbers in our press release and in the earnings call presentation

Ronald L. Nelson  
Chairman and Chief Executive Officer, Avis Budget Group, Inc.

BUSINESS HIGHLIGHTS

Performance

- There were a lot of good things to feel good about in our first quarter
  - Strong revenue and adjusted EBITDA growth
  - Margin expansion
  - Doubling of our EPS excluding items
- And all of this despite inclement weather, thousands of flight cancellations, difficult year-over-year pricing comparisons, and numerous vehicle recalls
• But there was one thing that stood out that we feel better than good about, and that is the increased volume and pricing in both the leisure and the commercial segments of our business in North America
• In North America, the positive pricing trends we experienced throughout 2013 continued in the first quarter, with our average rate up 2%, excluding Payless, despite a comp last year that was up 4% overall including 8% on leisure
• In fact, pricing increased broadly y-over-y along a number of different axes both on and off airport in both our leisure and commercial segments, in each of our brands and in each month of the quarter including March, which has the additional challenge of the Easter shift
  o It’s worth calling out our commercial segment where we have been vocal about the need for greater pricing whether it’s rate increases to our existing book of business or through our initiative to shift our mix to more profitable customers and channels
• During the quarter this began to bear fruit as we saw particularly strong growth in our small business segment with revenue up 8%
• Commercial also benefited from the knock-on effect of higher leisure pricing
  o We experienced the lowest level of commercial travelers flipping to leisure rates in at least the past five years because of the continued upward movement of leisure rates

Commercial Pricing

• The net result was a 2% increase in our realized commercial pricing
• It’s been a while since we’ve seen commercial rates at that level
• On the leisure side, we continued to seek pricing wherever available and initiated a number of price increases throughout the quarter with moderate success
• As important, however, is that we’re already getting meaningful benefits for the pricing automation phase of our integrated yield management initiative, which we’ve been developing now for the last two years

Budget Brand

• Today, the system is active in more than 70 markets making us more nimble by enabling us to change prices more frequently and surgically
• The benefits of doing this have been significant particularly for our Budget brand which skews more to leisure customers
• The combination of price increases, yield management activities and a continued focus on changing customer preference for premium vehicles all helped us achieve the 2% increase in leisure pricing in the quarter, excluding Payless
  o We will continue to rollout the pricing automation phase of our yield management system to cover the 100 largest rental markets in the U.S. by the summer and over time to all of our other geographies
• The truth also worth noting, that we achieved our 2.5 points of price growth in North America, excluding currency, without giving up market share
  o We believe our 4% growth in on-airport volume significantly outpaced enplanements growth in Q1

MIX PLAYS

• And while pricing was up nicely, there is more to the story
• Mix plays a big role
Our conscious efforts to shift our mix have been a key part of our strategic initiatives, particularly our focus on accelerating profitable growth.

For example, revenue from our higher-margin, specialty and premium vehicles increased 13% as we continue to make our signature fleet more prevalent on our proprietary websites and provide more premium vehicle inventory to increase upsell capability at our rental counters.

- International inbound, our most profitable customer segment saw revenue increase of 17%.
- Revenue from associations increased 17%, primarily due to our expanded exclusive agreement with AARP, which we announced in August.

Local Market Operations

- And finally, ancillary revenue per day increased 4%, helped by in-car SiriusXM satellite radio product launch, which is significantly exceeding our expectations.
- Changing mix has also been responsible for solid growth in our local market operations.
- A shift in our emphasis from replacement to general use leisure and commercial business, we’ve seen our local market operations grow from $750mm in revenue, delivering little or no margin to more than $1B in revenue generating a substantial contribution margin.
- In Q1 alone, off-airport revenue increased 9% with both higher pricing and volumes contributing to the growth.
- Our acquisitions are also making a positive contribution to our results.
- We closed a small, but attractive acquisition in late February, acquiring our Budget Licensee in Edmonton.

Strategic Growth Initiatives

- This roughly $30mm tuck-in acquisition allows us to participate in the significant growth in the area from the oil and gas industry, while growing our global footprint and enhancing the experience for our Budget customers, again two of our strategic growth initiatives.
- Together with putting the customer first and driving cost savings and efficiencies throughout our organization, the benefits of altering our mix of business and expanding our global footprint have resulted in meaningful growth in revenue and adjusted EBITDA over the past few years.

Headwind

- Finally, I want to address some questions that have come up about the effects of the severe winter we experienced.
- There are over 100,000 flight cancellations this past winter, not to mention the number of announced manufacturer recalls.
- Despite these headwinds, we were able to honor virtually every customer reservation by keeping the airport locations open to serve our customers, showing cars to where the demand was and offering one-way rentals to help our customers get home when flying simply wasn’t an option.
- This doesn’t happen without an enormously committed workforce and the men and women of our company truly distinguish themselves by delivering under the most adverse of operating conditions.
Volume

- So while it’s hard to quantify the effects of weather precisely, for those reasons we don’t think it had a material impact on our overall results
- If anything the loss of volume and incremental operating costs were substantially offset by increased one-way revenues
- Zipcar, it’s been a little more than a year since our acquisition of the world’s leading car share network and we’re just as excited about the possibilities of this business today as when we acquired it, if not more so
- In the quarter, we took several important steps to grow the business not only on the top line, but also profitably
  - We expanded Zipcar into Houston, at seven new college campuses and made Zipcars available on airport in Minneapolis
- We expanded and enhanced Zipcar’s good, better, best fleet paradigm by making the popular BMW 5 Series available to members and we announced plans to rollout ONE>WAY availability to Zipcar members beginning in Boston

ONE>WAY

- We think this is a big deal on two fronts
- First is the pure business opportunity that ONE>WAY by itself represents
  - It is essentially a new revenue stream for us, and a new service proposition for our members
- And second is the opportunity ONE>WAY represents to produce revenue for what would otherwise be a shuttle cost to move fleet between the airports and the city locations to service peak demand needs
- In New York alone, we will be sharing some 1,500 cars weekly during the summer months to meet the spike in Zipcar’s demand

Zipcar

- As a result, Zipcar had the most profitable first quarter in its history on record revenue
- In the one year since our acquisition of Zipcar, we’ve launched the brand in seven additional metropolitan markets, 30 airports and more than 30 college campuses, shared fleet in 19 markets and increased membership by 11%
- At the same time, we eliminated redundant overhead costs, delivered operational efficiencies and expanded margins, all the while remaining true to its unique member experience and brand promise to ensure that Zipcar remains the clear leader in car sharing industry

International Segment

- In our International segment, volume increased 3% as our initiative to grow the Budget brand in EMEA made further strides, and Apex continued to expand nicely in the Asia-Pacific region
- And despite weak demand in certain countries, we were able to increase our international utilization by 150BPS.
- But what I’m most encouraged by has been our ability to continue to deliver integration synergies in Europe
  - This allowed us to increase our international adjusted EBITDA by $9mm or more than 50% in the quarter, before the effects of currency exchange
Within International, our European operations had several successes in the quarter, growing revenue 3%, excluding currency and Zipcar, despite surprisingly sluggish demand in Germany and the shift of Easter into April this year.

Among the achievements, first, our aggressive expansion of the Budget brand continued, with revenue up over 50% for the quarter.

BUDGET PORTUGAL

In February, we reacquired the rights for Budget Portugal from our former licensee, enabling us now to operate both Avis and Budget in that market in a much more cost efficient manner.

We announced a three-year extension of our highly successful exclusive marketing partnership with British Airways.

Our focus on increasing ancillary revenue per day gained momentum, increasing 8% with upsells up even more, and we continue to consolidate fleet management activities, resulting in record first quarter utilization.

Finally, we continue to make progress in capturing the $100mm plus of synergies we outlined at our recent Investor Day.

In our Latin America, Asia-Pacific region, revenue increased 10%, excluding currency, with gains in both rate and volume.

Our operations in New Zealand had just a terrific quarter, with revenue increases in both Avis and Budget brands, as well as from our Apex deep-value brand.

Australia

In Australia, we’ve taken steps to mitigate the effects of a weak economy.

- First, we aggressively went after inbound volume, which ended the quarter up 10% and helped to offset weak domestic demand.
- Second, we continue to grow Apex, expanding its presence from one market in Australia to five over the past year.
- Third, we took a strong stance in favor of increased pricing in order to generate satisfactory margins and returns.
- Fourth, we actively managed our fleet, resulting in lower per unit cost in the quarter.
- And finally, we’re focused on winning more profitable rentals in the region, including our emphasis on growing our small business rentals.

Capital Allocation

- Before turning to our outlook, I want to review our thoughts on capital allocation.
- As you are aware, our board authorized $200mm share repurchase plan last August, which we immediately began to execute on.
  - Through April, we repurchased more than 3mm shares at a cost of approximately $140mm.
- Last month, our board of directors approved $235mm increase to our remaining share repurchase authorization.
FCF

- Returning cash to shareholders is one of our major objectives for the significant FCF we generate, and as we announced last night, we expect to repurchase between $200mm and $300mm in outstanding shares this year
- We anticipate that a second and equal, if not more important, use for a portion of our FCF will be tuck-in acquisitions
- Examples include the recent acquisition of our Budget licensee in Edmonton, the reacquisition of the right to operate the Budget brand in Portugal, and our purchase of Payless Car Rental last year
  - These transactions offer significant synergies, often with enhanced revenue opportunities, enabling us to generate strong returns on our investment
- But while we’re always actively searching out new tuck-in acquisitions, given the attractive returns they offer, we don’t think we’ll spend much more than $100mm or so on such acquisitions in 2014

OUTLOOK

- Moving to our outlook
- Although, we’re not raising or tightening our guidance this time, I am increasingly optimistic about our business and growth prospects for the remainder of the year
- In North America, we expect volume to increase 4% to 6%, including our Payless and Budget Edmonton acquisitions as enplanements look to grow only a couple of points or so this year

Pricing and Volume

- The growth we experienced in Q1 has continued thus far in Q2, with both pricing and volume up nicely as our strategic initiatives continue to bear fruit
- And I would say that we now expect overall pricing to increase at least 1% this year
  - While we ended up not giving any pricing back in March despite the shift in Easter, we did enjoy the expected pricing benefit in April from its timing
- May is always a challenging month to forecast, but the first week’s results would suggest that overall YTD trends are continuing thereby providing support for our optimism

International Segment

- And while we aren’t expecting commercial pricing to be up 2% for the balance for the year, we do expect at this juncture to sustain at least a 1% gain in commercial pricing for the balance of the year
- In our International segment, we expect to see mid single-digit volume growth in our Latin America, Asia Pacific region, driven again by good growth in New Zealand and bad demand in Australia, and the growth of our Apex brand

Europe

- In Europe, our sense is that the overall economy has stabilized with some countries having good growth, others not showing real signs of recovery, and Germany being somewhat of a head scratcher following a soft first quarter for car rental there
- Ironically, Germany is probably in the best shape of the European economies making the unusual results more difficult to understand
• Nevertheless, we continue to expect International volume to increase 4% to 6% this year, driven by our efforts to grow the Budget brand while increased ancillary revenues and synergies for our European integration efforts should allow us to show solid international EBITDA growth this year

David B. Wyshner
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

FINANCIAL HIGHLIGHTS

Performance

• Today, I’d like to discuss our first quarter results, our fleet costs, our balance sheet and our outlook
• My comments will focus on our results excluding certain items
• As Neal mentioned, these results are reconciled to our GAAP numbers in our press release and in the earnings call presentation on our website
  o This quarter marked our highest first quarter EPS ever coming in at $0.16
• This was double our first quarter 2013 results, principally as a result of higher volume and increased pricing in North America as well as positive contributions from our Zipcar and Payless acquisition

Adjusted EBITDA Growth

• Adjusted EBITDA grew 26% y-over-y to $117mm in Q1 with margins expanding 80BPS.
• Currency effects were $9mm headwind for us, so our local currency results were even stronger than our 26% EBITDA growth would suggest
• Our trailing 12 months adjusted EBITDA now stands at $793mm and for those analysts who run valuation models based on EBITDA before deferred financing fees and stock-based compensation, our trailing 12 months adjust EBITDA would be $46mm higher or $839mm

North American Segment

• Revenue in our North American segment grew 13% in the quarter and was up 6% excluding the acquisitions of Zipcar and Payless
• Total volume increased 7% in Q1 while pricing was up 1%
• Excluding the acquisition of Payless volume increased 4% and pricing was up 2.5% in constant currency

Volume and Pricing Metrics

• On slide 14, we’ve laid out our North America volume and pricing metrics with and without Payless for your convenience
• Leisure revenue increased 7% with volume up 5% in the quarter and pricing up 2%, both excluding Payless
• Commercial revenue increased 5% including a 3% increase in volume and a 2% increase in pricing
• Adjusted EBITDA in North America grew 23% y-over-y primarily due to increased pricing and higher volume, partially offset by a 7% rise in per unit fleet costs that was generally consistent with our expectations for the quarter
Zipcar Operations

- Our Zipcar operations contributed $68mm of revenue, $55mm of which was in North America with the remainder in Europe.
- And Zipcar generated $5mm dollars of adjusted EBITDA in the seasonally slower first quarter.
  - We continue to realize incremental synergies at Zipcar, both through cost efficiencies and fleet sharing.
- Our Payless acquisition, while small, is also delivering strong returns.
- Our $50mm investment contributed $6mm to EBITDA in the quarter.

International Segment

- Revenue in our International segment grew 7% in Q1, primarily due to higher rental volumes and ancillary revenues in Europe.
- International adjusted EBITDA was unchanged as incremental synergy benefits and the flow through from revenue were offset by $9mm negative impact on EBITDA due to currency exchange rates.

Truck Rental Segment

- Our Truck Rental segment also had solid results in what is a seasonally slow quarter for this business.
- As you know, we announced a restructuring program in late 2012, to right size our Truck Rental business and position it for substantially higher profitability and over the longer run reduced earnings volatility.
- We completed this restructuring last year and reported $3mm improvement in adjusted EBITDA this quarter, despite a 14% decline in average fleet.
  - Pricing was up 4% with utilization increasing significantly.

Fleet Costs

- Moving now to fleet costs, North America per unit fleet cost increased approximately 7% in the quarter in line with our expectation.
- Since fleet costs normalized in Q2 2013, we still had one quarter remaining of difficult y-over-y comparisons and this was it.
  - We saw a fairly stable and healthy used car market throughout Q1, enabling us to dispose more than 30,000 risk cars at prices slightly above our expectations.
- And we are encouraged by the strength of the wholesale market so far this year.

Retail Partnership with AutoNation

- In Q1, we disposed of roughly a quarter of our risk fleet through alternative channels such as online, direct-to-dealer, and direct-to-consumer, including our retail partnership with AutoNation.
- Our use of alternative disposition channels has increased more than 50% from the beginning of last year.
- And you may remember from our Investor Day that we expect these channels to provide an incremental benefit of at least $250 per car.
  - So selling more vehicles this way can have a significant impact on fleet costs.

Performance Excellence Process-Improvement Initiative

- Another area of our operations that has been vital to our earnings growth has been our Performance Excellence process-improvement initiative.
• PEEx is off to another strong start this year and is touching virtually all parts of our organization
• At Zipcar, PEEx is helping to review existing maintenance procedures to lower downtime and reduce the cost of maintaining a Zipcar
• At Payless, PEEx is replicating existing Avis Budget procedures to lower the cost of service and prepare a vehicle for rental

Europe
• In Europe, PEEx is driving maintenance and damage repair efficiencies, ONE WAY cross border revenue optimization and standardization and efficiency improvements in our shared service center in Budapest
• And in North America, PEEx is helping to roll-out the process changes associated with the yield management initiatives, which Ron discussed, as well as improving the handling of vehicles during their removal from our fleet reducing the downtime between last rental and disposal

Performance Excellence Efforts
• Across our regions, we’re expecting our Performance Excellence efforts to contribute $40mm to $50mm of incremental benefits again this year
• More generally, our focus on improving processes, driving efficiency and controlling costs remains intense
• PEEx is a key part of this focus
• So, are our efforts to relocate and standardize back-office functions in Europe into our shared service center in Budapest, which now has more employees than any other Avis Budget location in the world
  - We’ve also been working to streamline and strengthen our vehicle maintenance activities, which have not only reduced costs, but have had the additional benefit of making us better positioned to handle vehicle recalls
• And the decisions that managers throughout our organization make everyday continue to be informed by our broad-based culturally embedded emphasis on managing costs

Balance Sheet
• Turning to the balance sheet, our liquidity position remains strong with $5.3B of available liquidity worldwide
• We ended the quarter with $841mm of cash, no borrowings under our corporate revolver, roughly $1B of availability under that facility
  - They had unused capacity of $3.5B under various vehicle backed funding programs and our ratio of net corporate debt to LTM adjusted EBITDA at the end of the quarter was 3.6 times

Interest Rate
• We took advantage of attractive financing available to us during the quarter, completing $275mm offering of euro denominated senior notes, due in 2021, with the yield of 4.85%
• We use the proceeds from this offering to redeem a similar amount of our 8.25% senior notes in April
• Given the current level of interest rates, we anticipate calling the remaining 8.25% notes no later than October of this year, which should generate substantial benefits going forward

North America
• Before I wrap-up, I’d like to discuss our expectations for the remainder of this year
- We expect rental dates in North America to increase 4% to 6% and that pricing in North America will increase approximately 1%
- I know some of you are wondering why we aren’t changing our pricing guidance given the strong results we’ve achieved in the first four months of the year, and our ongoing focus on pricing yield management
- There are a few reasons
- First, the tough winter weather clearly created some incremental insurance replacement demand which we think made the industry somewhat tighter fleeted in Q1 than we can assume it will be over the balance of the year

Bookings
- Second, given the short booking window in our business, we have only a tiny portion of our summer reservations booked at this point, and that summer is a critical period for us
- And third, our up 1% projection includes Payless, which is going to generate a pricing headwind of at least 0.5 point this year
- On the flip side, as Ron mentioned, our commercial pricing is clearly shaping up to be stronger than we had initially anticipated
- The net result is that while we feel good about pricing so far this year, we’ve not yet decided to change our outlook
  - Therefore, as we announced last night, we expect our 2014 revenues to be approximately $8.4B to $8.6B, a 6% to 8% increase compared to 2013
- We expect total company per unit fleet cost to be $295 to $305 per month in 2014
- In North America, per unit fleet costs are expected to be approximately $300 to $310, or flat to up 3% compared to 2013
  - This implies very modest y-over-y changes for the remainder of the year

Adjusted EBITDA and Tax Rate
- We expect adjusted EBITDA to be approximately $825mm to $900mm, and our 2014 pre-tax income, excluding items, to be $455mm to $535mm
- We expect our effective tax rate in 2014 will be approximately 38%, and our diluted share count will be between 111mm and 112mm, including the effect of repurchasing $200mm to $300mm of outstanding shares this year
  - Based on these expectations, we estimate that our 2014 diluted EPS will be $2.50 to $2.95, an increase of approximately 14% to 34% compared to 2013

CapEx
- We project our CapExs to be around $200mm this year, as we continue to invest in our business, particularly our digital presence in North America and Europe, as well as yield management
- We expect our cash taxes to be approximately $70mm this year
- In fact, given the NOL we have on the balance sheet, our corporate interest expense, our anticipated fleet growth and existing tax laws, we don’t expect to be a regular federal cash taxpayer through at least 2017, which is the extent of our current tax planning horizon
  - We could be an AMT taxpayer from time-to-time over the next four years, which should be at a cash tax rate, after applying our NOLs, of only 2%
FCF

- And finally, we continue to expect our FCF to be approximately $400mm this year, absent to any significant timing differences
- As is typical for us, most of that FCF will be generated between July and October

International Operations

- So to wrap up, we achieved higher pricing and increased volume in North America in both our commercial and leisure segments
- Our international operations had several important successes, despite soft economic conditions in certain countries
- And one year after our acquisition of Zipcar, we have made significant advances in our integration and operation of that business
- On the capital allocation front, we’re pleased to have returned $75mm of FCF to our shareholders in Q1 in the form of share repurchases, and we expect to repurchase a total of $200mm to $300mm of stock this year

CONCLUSION

- And finally, we’re well aware that one quarter, particularly Q1, doesn’t make the year; controlling costs, investing prudently in our business, pushing for pricing wherever we can, and delivering benefits from our strategic initiatives, will continue to be our focus in the months ahead

QUESTION AND ANSWER SECTION

Christopher James Wallace Agnew
Analyst, MKM Partners LLC

And thank you for the color on why you weren’t changing pricing guidance, but can I ask on one of the things you mentioned there, that you can’t rely on industry fleet levels being as tight through the summer. Is there any particular reason why you would think that industry fleet levels are going to be loose through the summer, is there anything in particular you’re seeing?

Ronald L. Nelson
Chairman and Chief Executive Officer, Avis Budget Group, Inc.

No, I don’t think there is, Chris. As a matter of fact, industry fleet levels through April and even into May have actually been fairly, fairly tight. I just think that the winter was so harsh and there was so much insurance replacement volume that more than likely got generated. I just think it’s an abundance of caution to do that. I think one of the underpinnings of that view is the fact that volume at the auctions was actually fairly light in Q1, and I think people were holding on to fleet for that incremental demand. But no, there’s nothing specific on the horizon. It’s just being cautious.

Christopher James Wallace Agnew
Analyst, MKM Partners LLC

Thanks. And follow-up with – on fleet costs, with better program vehicle deals this year, you’ve got stronger Manheim or used vehicle index. I know it’s only a proxy, and then you’ve got more vehicles selling through
alternate channels, and Dave had mentioned that there’s a benefit there. I guess I may be a little surprised fleet costs aren’t trending lower, so maybe to ask it this way. If the used car market stays where it is today, is there a potential benefit to lower fleet costs as we head through the year?

David B. Wyshner  
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

Hi, Chris, it’s certainly—some of the things you mentioned, such as selling cars through alternative disposition channels, we had counted on and factored into our guidance. So I wouldn’t see that necessarily changing, or having an impact that changes what we expect for the year. I think the favorability we’ve seen in the Manheim Index and a little bit of favorability we experienced in Q1 certainly have the potential. They continue to move us down closer to the lower end of the range rather than the higher end, I don’t know yet that they could actually move us below the low end.

John M. Healy  
Analyst, Northcoast Research Partners LLC

Ron, I want to ask for a little bit more color on the corporate market, really encouraging to see the progress there, I appreciate the color on the trends in terms of the flipping vs. leisure and some of the growth in the SMB market. But I was hoping to get more color on the contractual side of the market, with the larger accounts, are you seeing much different there in terms of the competition, and I know you guys have tried to pullback from some of that competition and kind of lead the industry that way, but curious to know if you’re seeing any more discipline amongst the big contracts that come up for renewal?

Ronald L. Nelson  
Chairman and Chief Executive Officer, Avis Budget Group, Inc.

Well, I think we’ve seen the most progress, John, in the midmarket. I think those are accounts where we’re better able to control pricing and we’ve certainly seen an improvement in all of our midmarket accounts in terms of the percentage that are renewing at equal or higher rates. As a matter of fact in April 100% of the accounts that we renewed were all at equal or higher rates. So, I don’t think that will persist throughout the year, but you know I think we said over the last couple of quarters, 50% were higher and then 60% were higher in Q1.

I think the number was 65% were higher or equal. So it’s slower progress quarter by quarter, month by month. And I think a lot of what you guys think about is, a lot of these contracts are layered in. So you could have some contracts that we entered into two or three years ago that are now coming up for bid and the market level is just different and so even though you’re negotiating a lower price it could well be a market level that’s higher than the price that— it could be a price that’s lower than what you originally entered into even though it may well be higher than the current market level by some modest amount.

Look I think—in general I think the competition is always going to be there for the very large accounts. I think a lot of what we saw in Q1 and what we’re forecasting in terms of our at least 1% in commercial is going to be a function of keeping leisure rates high, keeping flipping low and changing the mix and focus of our business. We’re going to continue to push for rate gains in our very large accounts but I can’t tell you that we’ve made some significant improvement in the real large accounts. But overall, the large accounts are probably a quarter to a third of our commercial book. The biggest gain that we had here is in mid-market and small business.

John M. Healy  
Analyst, Northcoast Research Partners LLC
Okay. That’s extremely helpful. And I want to ask a little bit about the European business. Let me get a little bit more color, and it sounds like you are feeling good about maybe where the market is heading in general. But a little bit more color just in terms of how it feels competitively in Europe, I know there’s been some commentary that some things might be going on with some of your larger competitors there, but just some flavor of how fleets feel over there and just how some of the smaller players seem to be kind of either growing their fleets or maybe they’re retrenching from the market. Just what's happening on the competition in Europe?

Ronald L. Nelson  
Chairman and Chief Executive Officer, Avis Budget Group, Inc.

I think when we look at the European business on a constant currency basis, and you focus primarily on Avis, because it’s significantly larger than Budget at this juncture. You have to conclude that fleets are generally in pretty good sync with demand, because on a constant currency basis, our total revenue per day is up modestly in Avis and we’ve been able to grow volume modestly in Avis. So pretty good proxy for I think the market. Budget is obviously a different story because you’re starting with a different base.

I think the only thing that has really given us a little surprise is Germany is the strongest economy. And while volumes were generally flattish in Germany and up everywhere else, pricing was down a couple of points in Germany and it’s not clear whether it’s a German – a fleet issue in Germany or whether there is just decreased demand that’s driving lower pricing. I think we’re all sort of working hard to understand what it is we can do to turn that around. Germany is an important market for us, but you know where we make all of our money is really in the summer months in Italy, Spain and France. So we’re not horribly concerned about it but we do want to figure it out and make sure we make the right moves with our fleet and with our pricing there to optimize what economic activity is there.

Brian A. Johnson  
Analyst, Barclays Capital, Inc.

You had a chart on slide 16 I found interesting albeit it’s just for trucks. It talked about revenue per vehicle. If you look at that on domestic, it looked like it was up 5% on revenue per vehicle. That’s a metric that balances rev per day with utilization. So I guess more broadly, how are you thinking obviously there is the one way issue but how do you think about utilization as a metric? How do you think about the interplay between utilization and pricing? And then kind of as you kind of rollout all these kind of new initiatives and technologies, is that the metric you’re targeting or is still kind of pricing and volume?

David B. Wyshner  
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

Good morning, Brian, thanks. I think you’re right in how you describe revenue per vehicle as it clearly takes into account both pricing and utilization. I think the direction you’re headed in is the right one. Most of the improvement we’ve seen in revenue per vehicle is driven by the pricing growth that we’ve had but utilization was strong in Q1 and your suspicion is spot on. Our yield management activity we think are helping both pricing and utilization and so it really does show up in revenue per vehicle. And in particular, we think the yield management activities are helping to drive additional volume during the weekly shoulders, during the weekends and in shoulder periods particularly on the budget side. So we are getting some additional utilization as a result.

And when we look back at Q1 and the vehicle recalls that we had, the fact that we achieved improved utilization in the quarter is something we feel very good about. And as you suggested and as I said a big part of that was driven by the yield management initiative, which is helping generate some volume when otherwise cars might have sat.
The last point I’d make is one we’ve made before and that is that we like utilization, other things equal, but it is not our sole focus. We continue to invest in premium and in some cases luxury fleets that typically has below average utilization but higher revenue per vehicle and higher profitability. And as a result, we’re trying to be very careful, never to focus solely on utilization but rather on the role that it plays in the broader calculus of maximizing profitability.

Brian A. Johnson  
Analyst, Barclays Capital, Inc.

Right. Because premium would do well I assume on revenue per available car?

David B. Wyshner  
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

That’s right.

Brian A. Johnson  
Analyst, Barclays Capital, Inc.

And just kind of related to that, it sounds like the benefit you’re getting now is from, as you said, filling the shoulder periods. As you kind of go forward, I mean to what extent is that you’re focus on revenue per vehicle changing the way you might think about the size of the fleet and tuning the fleet size through the quarter?

David B. Wyshner  
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

Sure. And just to be clear, I’d say the utilization benefit is what’s coming through on the weekend. So where the yield management benefits is impacting utilization on the weekends, we think it’s impacting price favorably during the week and during peak periods. And that’s all part of the double benefit we look to get from this.

As we think – if you look at our yield management initiative what we’ve done so far is really pricing automation and that’s the first phase of a multiphase project, and that’s having significant benefits, but the next phase is a greater integration of demand forecasting, fleet planning and pricing in order to be able to adjust those various levers more interactively and more optimally, more surgically than we have in the past. And so what I think you’ll see over the next year or so is that the feedback mechanisms into tweaking of the fleet for us will become more sophisticated over the next year to 18 months, allowing us to do some more of the things that you’re alluding to.

Brian A. Johnson  
Analyst, Barclays Capital, Inc.

And I guess, final question, same topic. Where do you think the rest of the industry is on total industry supply and either using kind of blunt tools to make sure the fleet is right-sized or they use more finer grain technology tools. There’s been one competitor who’s been talking a fair amount about excess fleet in their system for a bit with less visibility [indiscernible] (41:04). So just overall where do you think it is and then kind of, as people kind of buy the same, sort of write the same code, write the same technology, do you see room for that to improve?

David B. Wyshner  
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

On the yield optimization, yield management front, we feel good about where we are competitively and how we’re using the information we have to manage our fleet. I think the work we’re doing, which has required a lot of thinking and building of algorithms as well as management tools and processes is to implement them. It positions
us to be ahead of the curve relative to our competitors and in the future. But I’m not privy to tell the things they may be doing to work on yield management.

Brian A. Johnson
Analyst, Barclays Capital, Inc.

Well, I guess the question is, did you see an improvement in fleet tightness across the industry beyond your own fleet and what’s your doing?

David B. Wyshner
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

I think it’s hard to tell what will happen going forward. Clearly in Q1, I think each of our competitors was working through a different issue, one of them—both, actually, probably, having some incremental insurance replacement demand, and then one working through a fleet integration issue as well.

Adam Jonas
Analyst, Morgan Stanley & Co. LLC

We all really appreciate it. Just to follow up on the tech question. Can you give us a sense of where your tech spending is, in either absolute terms or percentage of sales, or how much is already done for where you’re going to need to go as you transition from legacy systems like Wizard to open architecture and the things you’ve just talked about, and roll out connected car to larger parts of the fleet?

David B. Wyshner
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

Sure, Adam. I think, as we think about our technology spending, it’s an area of focus for us, and we’re investing more there than we ever have before. And I think it takes a variety of different types of spending. First, we’ve been investing in the digital area, our mobile capabilities, whether it’s our apps or our websites. We’ve been doing that both in North America and Europe, and that’s an important focus for us.

We continue to do incremental spending to build additional capabilities here or there through our core systems. We’re investing fairly significantly to increase the longer term nimbleness and agility that we have with our systems, including some very significant work on Wizard to make it more agile, to allow us to be more agile, to implement changes more quickly and at less cost, and that’s a multi-year initiative for us. And I think we’re continuing to look at customer-facing elements of our technology, because we consider that to be very important. Our customers expect us to provide good, solid, reliable, helpful technology to them, and I think we’ve got a number of things that work very well. But we also have other areas that don’t work as well as we’d like, and we see opportunities to improve the customer experience with our spending there.

So as we look at our aggregate $200mm of capital spending this year, nearly half of that, in one form or another, relates to technology.

Adam Jonas
Analyst, Morgan Stanley & Co. LLC

And is that going forward going to grow in line with sales, or greater than sales, so that you get a yield on it and try to compensate for that?

David B. Wyshner
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.
I wouldn’t be surprised if it were to grow, maybe a little bit ahead of sales. The opportunities we see to invest in technology and generate a significant return are really quite good. And as long as those continue to be there, we’re going to take advantage of those investments. And the one reason I’m cautious on that is that I do think the work we’re doing on Wizard and our other systems will actually allow us to be more efficient in the technology spending that we’re doing. And so that may allow us to do more at essentially the same percentage of sales.

Adam Jonas
Analyst, Morgan Stanley & Co. LLC

Great. And just a follow-up on Zipcar on airport, very interesting initiative, and I don’t know if you are in a position to share, and I know – I’m sure it’s starting very small, but based on what you have running now, can you give us any more color on length or revenue per rental or rates, or maybe how big this can go? And also, are these cars, is there an agreement with the airport to pay kind of 11% type concession fee, or is it just the cost of the short-term parking in the facilities that the airport’s compensated for? Thanks.

Ronald L. Nelson
Chairman and Chief Executive Officer, Avis Budget Group, Inc.

Yeah, no. We do pay a concession fee on the airport rentals for Zipcar, and we’re in 30 airports now. I think there’s probably at least 20 more that we think we can profitably put cars there. I think, in terms of the number of cars that we’re renting, it’s small, very small, compared to number of Avis and Budget cars that we’re renting. But I think – the thing that has really captured all of our thinking is the fact that these cars rent for relatively significant premium over Avis and Budget rentals.

Now part of it, obviously, is the all-inclusive nature of insurance and gas and T&M, but part of it also is the service proposition that it offers to Zipcar members, I mean they simply get off the bus. They go right to their car. They swipe their smartcard and they’re off and running. And I think there’s a lot of good customer experience learning that’s coming out of this that’s going to impact both of our brands longer term. My sense is, and I don’t know the number exactly, but the LORs for the Zipcar airport rentals are probably shorter than the LORs for Avis and Budget, probably because of the premium, but I think that answers your question.

Afua A. Ahwoi
Analyst, Goldman Sachs & Co.

Just two from me. First on the ancillary revenue, can you maybe talk about what sort of product you’re seeing a lot of traction. I know for a while you talked about how the supply of the GPS has may be reached its penetration potential, but maybe what else is driving such strong growth there. And then on the pricing, I know sometimes you give maybe either a one month in color, is there any color on what April was. And then also how much does your new yield management system add into pricing or what benefit do you think you’re getting from that? Thank you.

Ronald L. Nelson
Chairman and Chief Executive Officer, Avis Budget Group, Inc.

Well, those are a lot of questions. Let me see if I can remember them. I think on the ancillary revenue side, Afua, sort of order of value in terms of aggregate dollars is LDW, loss damage waivers and then GPS, and then roadside protection and then the new SiriusXM radio product launch that we’ve had. I think where the real growth on a percentage basis has been, has been in the XM radio. We’ve now equipped something like 200,000 of our cars with factory-installed XM radios, that can be activated at the counter and the growth in that product has been fairly significant.
I think in Europe, it’s a little different. I think upsells are contributing a fair amount to the ancillary revenue. They have just begun the ancillary sales training throughout some of the markets, that is giving people the tools to be able to drive ancillary revenue growth. So I think we’re seeing pretty good growth across all of the products there and I think we probably will for the next three years or four years. I think in North America, it’s probably more dependent on product launches than it is new products over the course of the next couple of years.

David B. Wyshner  
Chief Financial Officer and Senior Executive Vice President, Avis Budget Group, Inc.

And on the pricing side, April was strong. And as we’ve said in our opening comments, I think it was consistent with our first quarter trends plus the benefit of the Easter shift. And as a result of Easter moving, which actually creates a lot of noise in the comparables. It’s hard to make a lot of sense out of the overall April number, but the trends appear to be pretty consistent and we do believe our yield management initiative was a contributor to that the same way it was in Q1.

Ronald L. Nelson  
Chairman and Chief Executive Officer, Avis Budget Group, Inc.

CLOSING REMARKS

- So let me just – before we close, I think it’s important to reiterate what I believe are the key points from today’s call
- We had an excellent start to the year with volume, pricing, margins and earnings all increasing
- The used car market has been stable enabling us to sell the cars we want at prices slightly above our expectations thus far and the positive volume and pricing trends we experienced in Q1 continued into the second
- As we benefit from our yield management system, our continued shift in mix towards higher yielding segments and the shift of Easter
  - We have a full investor calendar this month and next and hope to see many of you doing our travels.