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Avis Budget Group, Inc. (CAR)

Q4 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Avis Budget Group Fourth Quarter Earnings Conference Call. Today's conference call is being recorded. At this time, for opening remarks and instructions, I would like to turn the meeting over to Mr. Neal Goldner, Vice President of Investor Relations. Go ahead, sir.

Neal H. Goldner

Vice President-Investor Relations, Avis Budget Group, Inc.

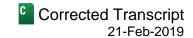
Thank you, Donna. Good morning, everyone, and thank you for joining us. On the call with me are Larry De Shon, our Chief Executive Officer; and Martyn Smith, our Interim Chief Financial Officer.

Before we begin, I would like to remind everyone that the company will be discussing forward-looking information that involves risks, uncertainties and assumptions that could cause actual results to differ materially from such forward-looking statements and information. Such risks, assumptions, uncertainties and other factors identified in the company's earnings release and other periodic filings with the SEC as well as the Investor Relations site of the company's website. The company undertakes no obligation to update or revise its forward-looking statements.

Our comments today will focus on our adjusted results. We believe that our financial performance is better demonstrated using these non-GAAP financial measures. All non-GAAP financial measures are reconciled from the GAAP numbers in our press release and in the earnings call presentation, which is now available on our website.

With that, I'd like to turn the call over to Avis Budget Group's Chief Executive Officer, Larry De Shon.

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Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

Thank you, Neal, and good morning. 2018 was a successful year for our company reporting our ninth consecutive year of revenue growth, increasing adjusted EBITDA by 6% and expanding margins. Our results were particularly strong in the Americas this year with adjusted EBITDA growing 15% and margin expanding 100 basis points. We achieved this by driving profitable revenue growth, including higher underlying pricing, highlighting the benefits of our new revenue management system which we finished rolling out across the United States in Q4. Our results also benefited from a 7% reduction in per-unit fleet costs and higher utilization for the year.

We ended the year on a very strong note by delivering a record fourth quarter profit performance as our Americas segment pursued pricing over volume in the quarter, yielding 2.5% higher revenue per day, our best year-over-year increase in pricing since 2014.

Our strong pricing performance and substantially lower overall per-unit fleet cost enabled us to grow our adjusted earnings per share by 18% and we plan to continue pursuing pricing over volume as we enter 2019 to provide ourselves even more opportunities to improve utilization and increase rate.

I'll let Martin review the quarter and our guidance for 2019. But before doing so, I wanted to spend a few minutes reviewing our overall strategy and highlighting some of our achievements this year, starting with profitable revenue growth. A number of years ago, we embarked on a journey to improve the rental experience we offer customers by making renting a car more transparent, convenient, personalized and seamless.

Today, customers can use our award winning Avis Mobile App to make, modify or cancel a reservation, view available cars and choose the exact car they want before getting to the lot, flash the lights to locate their vehicle, lock and unlock the doors and return it without any assistance right on their mobile device.

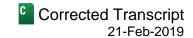
The major upgrades we made to the app in 2018 including enhancing the selection of vehicles for exchange and upgrade, real time tracking of our airport shuttle buses and making ancillary products available for purchase on the app including our new Curbside drop off service, solve everyday problems that make renting a car easier.

We have surpassed 2 million transactions on the app since we launched it just a few years ago and the overwhelming majority of users have told us they are very satisfied with their experience translating into substantial improvements in our Net Promoter Scores for app users, indicating that we are exceeding our customer's expectations.

You should expect us to continue improving the app to further enhance our customers' experience this year as well. In July, we signed an agreement with Amazon to reward customers when they rent a car through Avis, which we later extended to Budget. Customers who book an Avis or Budget vehicle save money on their rental and receive an Amazon gift card valued at 10% of the rental price.

Our relationship with Amazon is progressing well, and we look forward to working with them to keep this momentum going. Also, we made further steps towards optimizing our global network. First, we successfully acquired a number of sub licensees in Germany and North America during 2018. We also acquired Morini, specializing in the rental of light commercial vehicles in Italy and Turiscar, a well-established car rental company in Portugal.

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The additions of Morini and Turiscar last year follow our acquisitions of Maggiore and its commercial vehicle business in 2015, France Cars in 2016, and ACL Van Hire in the UK in 2017, enabling us to grow a substantial European light commercial vehicle footprint in a short amount of time, leveraging areas of existing strength with our Avis and Budget brands.

Secondly, we reintroduced our premium Avis brand to Japan in 2018 and expanded our Budget brand into Taiwan, both through license agreements enabling us to serve new customers in these growing markets.

And lastly, we have exited markets where we feel we aren't making an acceptable return. For example, we disposed a small non-core business in Australia last year, and we are now in the process of fully franchising both China and Brazil. Looking forward, you should expect us to continue to look for opportunities to further optimize or global footprint.

We have embarked on an ambitious process of digitizing our business to drive substantial operating efficiencies to improve margins, starting with connecting our entire global fleet by 2020. Connected vehicles not only allow customers to manage their entire rental experience through the mobile app, they also allow us to streamline our operations and reduce cost. This includes real-time inventory counts, mileage management and automated maintenance notification. Having a fleet of connected cars will enable a more sophisticated tracking of idle vehicles and employing more dynamic fleet planning. Connected cars also enable us to collect critical data including mileage, fuel level and vehicle condition on a real-time basis, resulting in a more efficient workforce, better maintained vehicles and a better customer experience. We had already reached the 100,000 connected vehicle level in 2018. And the agreements we signed last year with Toyota, Peugeot, Ford, Continental and I.D. Systems will take us even closer to our goal of having a fully connected fleet by 2020.

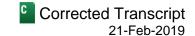
We also announced last year that our data analytics platform now leverages Amazon Web Services cloud-based connected vehicle solution enabling us to leverage advanced data management and scalable analytic capabilities for our connected car platform. Down the road, both private and public organizations that partner with us will be able to access our connected card data to introduce new products and services for connected travelers and inform smart city planning. We have already partnered with Kansas City, and soon we'll be able to stream data through the Avis app providing customers easy access to parking and other helpful information. And we believe we are very well-positioned to collaborate with other municipalities around the globe as they move forward with their own smart city initiatives.

In addition, we have also made meaningful investments over the past few years to lower our costs and position us for the future. For example, we have modernized our core rental and reservation system, our revenue management system, and our digital web sites and mobile app, including the first app in the industry that can actually reserve and rent a car. And we are now working on modernizing our accounting systems to drive efficiencies. We have developed the API capability to quickly integrate with third parties, which is how we got our new partnership with Lyft up and running so fast, and have already moved all of our current partners to our new API.

We launched a first to market online portal complete with rental summary dashboard, rich visualizations and detailed customer reports that provide corporate travel managers with insight into their programs' performance and we are building our next generation platform this year to operationalize the connected car data and enhance the management of mileage across our fleet.

And while we are focused on improving our profitability, we're also investing in innovation for the future. We envision a world where personal mobility will be completely connected, integrated and on demand. Our goal

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therefore is to leverage innovation and build on our position as the leading global provider of mobility solutions for consumers, businesses and cities. That's why we are building on our core competencies, data intelligence and technology to extend our offering and capabilities today.

We believe that in the long term, more mobility use cases will be offered as a service and fleet management capabilities such as ours will be extremely valuable for any sustainable mobility company. Yet there are very few companies that can operate fleets at a global scale.

With a fleet of more than 650,000 vehicles and more than 70 years of experience, we believe we are uniquely positioned to take advantage of the growth of new mobility models as we leverage our fleet management capabilities to provide these services to other companies and fleet owners.

A great example of this is the agreement we signed with Waymo in mid-2017 to offer fleet support and maintenance services for their self-driving car program in Phoenix, Arizona. This partnership allows us to leverage our capabilities and assets to service Waymo cars on the road, ensuring their self-driving vehicles are ready for riders around the clock.

This partnership also allows us to accelerate our knowledge and hands-on experience of autonomous cars for a future when they become fully available in the marketplace and is a good example of how we can leverage our physical properties, global workforce and platforms to drive new business models. We also entered into a partnership to provide fleet management services to ViaVan, a leading provider of on-demand van-pooling services as they expand in the UK.

Another example of how we can thrive as different mobility models evolve is the multiyear agreement we signed with Lyft last year to add thousands of vehicles to the Lyft Express Drive program. We've already launched in Chicago and Atlanta and look forward to expanding to additional cities across North America this year. We signed an agreement with Brightline to make Avis and Zipcar vehicles available at the train stations in Miami, Fort Lauderdale and West Palm Beach. And we made an early stage investment in Fetch, the self-service on-demand truck rental company, and entered into a partnership with them to make Budget trucks available for rent through their mobile marketplace enabling our customers to control the entire rental process right from their smart device.

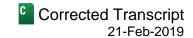
Looking forward, you should expect us to partner with other innovative companies as we evolve our business to meet the opportunities presented by a future where mobility is completely connected, integrated, on-demand, shared and delivered to both consumers and businesses as a service.

So, I hope it's apparent that we are very focused on driving quality growth with technology informing many of our decisions, evidenced by the success of our new revenue management system and the strong pricing our Americas segment delivered, and our Avis app continues to receive accolades from our customers all contributing to the 100 basis point margin improvement that Americas delivered in 2018.

In addition, we've grown a sizable European local commercial vehicle business. We're also making investments in new mobility solutions such as Fetch and increasing our fleet of connected cars to improve the experience we offer customers and lower our cost. And we're innovating to secure our leadership position in the global mobility market.

Lastly, we announced earlier this week, we have hired John North to be our CFO effective March 18. John has a strong auto retail background having spent 17 years at Lithia Motors, most recently as the company's CFO. His extensive background in the automotive industry will serve us well as we execute our strategies on expanding our

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mobility offerings, improving the profitability of our revenue, and growing our alternative channels for fleet dispositions.

At the same time I'd like to personally thank Martyn for stepping in when we needed him and for all of his long years of service to our company. We will miss him and wish him great success in all of his future endeavors.

With that, I'd like to turn the call over to Martyn to discuss our fourth quarter results and our 2019 guidance.

Martyn Smith

Interim Chief Financial Officer, Avis Budget Group, Inc.

Thanks, Larry. And I appreciate the comments. We've done great things at Avis Budget since I joined more than a year and a half ago and I've really enjoyed my time working with you and the team again. I believe the company has a great future ahead of it, and I wish you all the very best.

With that, I'm now going to discuss our fourth quarter and full year results along with our cash flow, liquidity, and outlook for 2019. My comments today discussing changes in revenue per day pricing and per-unit fleet costs will all refer to changes in constant currency, i.e., excluding exchange rate effect. I'll also focus on our adjusted results which are reconciled from our GAAP numbers both in our earnings release and earnings call presentation.

Firstly, starting with an overview of our fourth quarter for the total company, a combination of 3% overall volume growth, strong Americas pricing, and 6% company-wide lower per-unit fleet cost enabled us to grow adjusted EBITDA in constant currency by 4% in the quarter, being up 1% after a \$3 million dollar adverse impact from foreign exchange with adjusted earnings per share increasing by 18% percent.

For the year, we increased revenue by 3% to \$9.1 billion, driven by 4% overall volume growth and reducing company-wide per-unit fleet cost, enabling us to deliver a 6% increase in adjusted EBITDA with margin expanding by 30 basis points for the year. Overall fleet interest expense was up \$28 million primarily due to higher North American interest rates, but was largely offset by an \$18 million benefit from foreign exchange movements. A 28% increase in adjusted earnings per share was achieved through higher adjusted pre-tax income, a lower effective tax rate to 27% and a 6% reduced average share count.

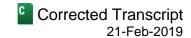
Moving now to a review of our segmental results for fourth quarter beginning with the Americas, 2% revenue growth in the quarter was driven by a 2.5% increase in revenue per day as we consciously chose to pursue pricing over volume, driving higher value rentals as well as the benefit from our new revenue management tool which is now live across the whole of the United States.

Full-year revenue was up 1% over the prior year, benefiting from increased volume and higher underlying pricing, including our solid fourth quarter improvement. In fact, we have now increased underlying pricing on a year-over-year basis for six consecutive quarters, illustrating our ability to drive higher rates per day when industry fleet levels are normalized.

Our yielding approach was particularly evident in the leisure segment this quarter, delivering 6% higher underlying leisure rate per day, with particularly strong increases achieved over the holiday periods. We delivered good volume growth in our marketing and association channels, including our new Amazon agreement which has gone very well since we launched.

Commercial volume was up 1% in the quarter, the second consecutive quarter of positive year-over-year growth, with increases seen in both our contracted and small business segments, while also delivering a 1% higher

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underlying commercial pricing. We also increased length of rental as part of our strategy to drive more profitable transactions.

Moving to costs for the quarter in the Americas segment starting with fleet. We delivered another quarter of substantially lower per-unit fleet costs, the results of both a stronger used car market and our ability to capitalize on it. We continue to improve the sophistication around our data analytics on how we both buy and sell our cars. Leveraging this technology, we took advantage of the strength in the marketplace by selling more cars compared to last year's fourth quarter.

We also did have another record alternative channel performance. As a result of our actions in the strong market, fourth quarter per-unit fleet costs were 7% lower compared to a year ago. Our utilization in the quarter though was impacted by both record manufacturer vehicle recalls as well as the impact of our decision to sell more cars than originally planned. Vehicle interest expense increased 11% in the quarter versus last year, or \$6 million, due largely to the effects of rising interest rates on our U.S. variable rate conduit facility.

Summarizing, strong pricing and lower per-unit fleet costs enabled our Americas segment to deliver a record fourth quarter with margin improving and adjusted EBITDA growing 15%. For the full year, we delivered a good volume growth, higher underlying pricing and 7% lower per-unit fleet costs, partially offset by a \$22 million increase in vehicle interest expense leading to 15% growth in adjusted EBITDA and 100 basis points improvement in margin.

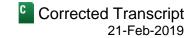
Now for the international segment, where difficult market conditions continued from when we last reported. We grew rental days in the fourth quarter, where particularly strong growth coming from Italy, Spain, and Portugal, including the benefits of the tuck-in acquisitions we closed last year. But while volumes were good, the competitive pricing environment we've seen in Europe persisted, with revenue per day down 5%. Per-unit fleet costs were unchanged for the quarter and we drove a 40 basis points improvement in utilization. To offset the pricing pressure we faced this quarter, we also focused on tight cost control.

To summarize, adjusted EBITDA in our international business was 15% lower in the quarter with a good volume growth, high utilization and strong cost controls being offset by lower rate per day. For the year, 8% volume growth and favorable currency were offset by 3% lower rate per day with international adjusted EBITDA being reduced by \$18 million year-over-year.

Moving now to our cash flow and funding position. Adjusted free cash flow was \$430 million in the year, being higher than our expectation of \$350 million, benefiting from some \$75 million relating to the timing of net vehicle programs, which has already reversed in early 2019. Across the year, we continue to focus on capital allocation with an emphasis on free cash flow year before non-fleet CapEx.

This year, we invested around \$230 million on non-fleet CapEx, up from \$198 million last year, including investments in our new revenue management system, connected cars, our next-generation platform and on our new accounting system. We also invested \$124 million in the year on tuck-in acquisitions and investments, including the purchases of Morini and Turiscar as well as a 40% interest in our licensee in Greece. We bought back 3% of our shares outstanding in the fourth quarter at a cost of \$71 million. For the full year, we repurchased 5.9 million shares at a cost of \$200 million, and ended the year with a weighted average diluted share count down nearly 6%.

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Regarding fleet debt, just this month, we issued \$600 million of three-year ABS notes at a rate of just below 3.6%, lower than our earlier expectations. This offering was eight times oversubscribed illustrating the confidence investors have in our business.

Our financial position remains strong with approximately \$4.1 billion of available liquidity. This comprised ending the quarter with \$615 million of cash, having \$633 million of unused capacity in our revolving credit facility, plus \$2.8 billion of availability under our vehicle programs.

Our net corporate leverage of 3.8 times is three-tenths of a turn lower than at the end of last year and is within our targeted range of 3 to 4 times. We have no corporate debt maturities until 2023 and approximately 90% of our corporate debt is either at fixed rate or is swap to fixed, so our exposure to rising interest rates in our corporate debt is limited.

Now to our 2019 outlook. We expect our overall revenue to be between \$9.2 billion and \$9.5 billion this year. We expect Americas' volume to be between unchanged and up 2% and international volume to grow between 3% and 6% including the annualization benefit of acquisitions closed in 2018.

Revenue per day in the Americas is expected to be up for between 0.5% and 2.5%. We expect international revenue per day in constant currency to be lower by between 1% and 4% partly due to the annualization of acquisitions and further increases in length of rental. We expect our per-unit fleet costs in the Americas to be between 1% and 3% higher and international per-unit fleet costs are expected to be in the range of unchanged to up 2% in constant currency.

We expect vehicle interest expense to increase this year by \$25 million to \$35 million due to higher North American benchmark interest rates. We expect to net currency translation this year to be a headwind of \$10 million to \$20 million due to the strength to the U.S. dollar. As you can see in today's presentation, we expect the impact to be the most pronounced in the first half of the year.

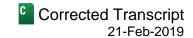
We therefore expect our adjusted EBITDA to be between \$750 million and \$850 million for 2019. Just as a reminder, Easter is late this year, which will have the effect of shifting a portion of the first quarter revenue and earnings into quarter two as well as impacting our Q1 pricing and utilization for both regions.

The government shutdown which not only disrupted federal employees, but our government contract customers as well, will also impact our first quarter results. As a result, these will likely lead to our first quarter EBITDA being down year-over-year.

Non-vehicle D&A, excluding acquisition-related amortization is expected to be around \$210 million and non-vehicle interest expense is expected to be around \$190 million, one, nine, zero. As a result, adjusted pre-tax income is expected to be between \$350 million and \$450 million in 2019. We expect our effective tax rate to be in the range of 27% to 29% and adjusted diluted earnings per share to be between \$3.35 and \$4.20 per share.

Finally, we expect our free cash flow to be between \$250 million and \$300 million after the \$75 million timing effect I mentioned earlier. This has our total free cash generation in 2018 and 2019 combined, averaging around \$350 million per year. One additional point, on January 1, 2019, we adopted a new accounting standard for leases. The only incremental effect, beginning with our first quarter results which we were planned to report in May, will be to bring onto our balance sheet, long-term operating leases in respective rented property locations, to the value of approximately \$3 billion.

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We expect no material effects from this to our adjusted EBITDA earnings or free cash flow. In summary, we grew overall volume by 3% in the fourth quarter, and increased pricing in the Americas by 2.5%.

We expanded margins in the Americas by 100 basis points in the quarter and grew EBITDA 15% through the combination of better pricing and lower per-unit fleet costs.

For the year, overall revenue increased 3%, per-unit fleet costs were 5% lower, adjusted EBITDA grew 6% and margin expanded by 30 basis points. We invested in our future by increasing our CapEx, made a number of financially attractive tuck-in acquisitions as well as acquiring 40% of our licensee in Greece. Finally, our funding position remains strong and we have no corporate debt maturities until 2023.

With that, Larry and I would be happy to answer your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from John Healy from Northcoast Research. You may ask your question.

John Healy

Analyst, Northcoast Research Partners LLC

Thank you. Larry, I wanted to ask just kind of a big picture view on capital allocation. I know you guys have done a nice job of balancing, returning capital to shareholders and still investing in the future. But, if I think about everything that's going on in the business, there is a lot of potential and wanted to get your thoughts about capital allocation going forward, if we should expect you guys to continue to shrink the share count a few percent each year or may it make sense to be more aggressive with the type of investments that you're making into businesses like Fetch. And even on the investment side of things, are you looking at mobility from a larger context excluding the consumer and thinking about remarketing, thinking about auctions? There are a lot of changes going on there with some of those businesses and I was curious to know if you guys, as you define mobility, are defining it outside of the rental business itself.

Larry D. De Shon

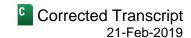
Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

Yeah, John. I think we're keeping our definition of mobility fairly open and broad at this point in time, looking for opportunities that make sense for us that both align with what we know how to do and do well every single day. So from a capital allocation perspective, I don't think we're literally limiting ourselves in any way. We're keeping our options open.

At this time of the year, we're always planning on how we should approach the capital allocation for the year. As you know, we don't buy much stock back in the first, really, at all in the first quarter and really very little in the second quarter. We tend to buy it more in the back half of the year.

We really have to see how our acquisition pipeline matures as we go throughout this year. We have some opportunities that we think that are out there but we want to make sure that we understand that. And yes, we are looking at other types of mobility investments like we made in Fetch.

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So, I think the options are all open. What we want to do is, make the right investments that makes sense for us on improving our profitability in the short term as well as setting us up for success as we look at how mobility will evolve over the long term.

And of course, we always keep an eye to returning free cash flow to our investors as well. So it's a balancing act between where all the opportunities are and what will really drive meaningfully EBITDA opportunities for us going forward but we're leaving our options fairly open and fairly wide.

John Healy

Analyst, Northcoast Research Partners LLC

Great. Thank you, guys.

Operator: Our next question comes from David Tamberrino from Goldman Sachs. You may ask your question.

David Tamberrino

Analyst, Goldman Sachs & Co. LLC

Great. Good morning, Larry, have two questions for you, one a little bit near term and then the next one on the connected car piece. You mentioned in the prepared remarks that you are seeing some weakness from the government shutdown in January. Just trying to gauge how much of an impact that's really having on your business.

I know first quarter is generally seasonally softer. And sounds like with Easter shifted, it's going to be a little bit more softer but I did see one of the trade publications on rental cars saying that rental bookings maybe dropped about 50% year-over-year in January. So, want to see if that's how much we should be thinking about for your business or if that's a little larger than what you actually saw?

Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

Yes. Good morning, David. Yeah. The report on the very large drop in government business, we did not see that kind of drop. What I would say is, if you look at how we trended in the government segment all year long, we did see a change in that trend in January, and then it came back to where it was in February. So, you're right. January is not a huge month anyway, but there was definitely a change in how we've been trending, how we've been growing the government segment all year long, but it's nothing to the effects that, what was in that article.

David Tamberrino

Analyst, Goldman Sachs & Co. LLC

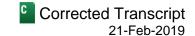
Okay. Good to know. Second, just on the connected car piece, how much, if any, of an improvement are you expecting in your 2019 guidance from being able to recoup more for fuel from accurately gauging it from increasing or improving your operations, improving your utilization as a result of your current connected fleet, or are those benefits still 2019 plus, 2020 beyond?

Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

Yeah. We're actually learning a lot as it relates to connected car. As we get more and more cars in-fleeted with the connectivity, allows us to kind of broaden our scope as far as our operations as the opportunities that are out there in more and more locations. Kansas City is our mobility lab, and so that's where we really focus our

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attention from a learning perspective. And we do see opportunities as we manage the fleet, get assets back faster, particularly those that are overdue. We do see the benefits of collecting gas. It's not exactly where we want it yet. So, we want to get that penetration even higher. So, there is a lot of work that goes into using the technology and then making sure that everything works to the point that you can really operationalize it and maximize the opportunity of it. So, there's a lot of learnings that we go back and we put back in place. There's a lot of learnings that we take from it that we have to then go back and refine our technology, and then we're getting more and more OEMs onto this as well. And then with each OEM that starts to deliver in connected cars there is a learning process that goes back and forth as well.

So this is going to be an evolution over a long period of time as we improve gas collection, as we improve asset control which then improves our utilization, and a number of other things around, like managing miles for example across the network of our fleet in a much more efficient way than what we could do without it, without the connectivity. And this year what we're doing is we're building out our next generation platform because it's one thing for the cars to be able to generate data. It's another thing to be able to operationalize the data, to be able to use it, and do the right data analytics on it and turn it into action in an automated way. Without that, it's just really a lot of data.

So this is a year that we're dedicating to really building out the technology that enables us to take advantage of what the data can actually do for us. So I would say that the benefits are really more in the longer term. Yes there are some short-term benefits in 2019 which we'll take advantage of but I would really think of it more 2020-2021.

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Analyst, Goldman Sachs & Co. LLC

Understood. That's very helpful. Thank you Larry.

Operator: Our next question comes from Chris Woronka from Deutsche Bank. You may ask your question.

Chris J. Woronka

Analyst, Deutsche Bank Securities, Inc.

Hey, good morning guys. I had a quick, another short-term question, then another one on partnerships. But in terms of the ancillary, do you guys think that turned a corner in the fourth quarter? Did that help your RPD at all and then kind of how do you see that unfolding throughout 2019?

Larry D. De Shon

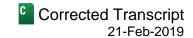
Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

I'm pretty pleased with what the team has done with our ancillary revenue. They've tackled this from a number of fronts. As you know, it was just – it haunted us all year long. We have started to turn that ship now and it's a big ship to turn, I have to say.

But they have put in a number of initiatives not only from new product offerings to automation technology that allows us to sell to the consumer online, running several different tests around different kinds of bundles and packages that might make sense. Some of them do. Some of them don't. So, we learn from that. We keep running different opportunities like that to learn from.

New incentive programs for our rental sales agents that tie in Net Promoter Scores along with the incentive pay, in the test markets we're running that, it's proven to be quite successful. So, we have a number of initiatives that

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are all starting to kind of hit their pace now. And I think collectively come together to really present a better opportunity for us in 2019.

So, I'd say that the ship has kind of now finally starting to turn in the right direction and we're hoping that as we go through 2019 that we'll start to see the benefits of that play out every single month as we continue to kind of grow these opportunities. So, I think we're in the right place. I feel really good about where we sit right now with this program.

Chris J. Woronka

Analyst, Deutsche Bank Securities, Inc.

Great. That's helpful. And then just on some of the initiatives you're working on outside of the core business working with some of the municipalities and such. How do those – what's the nature of those interactions? Is that a pull from or a push from you guys or a pull from them? And how do you kind of see those opportunities in terms of how big the landscape is going forward?

Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

We've been in discussions with a number of municipalities. We have really good relationships through our Zipcar brand who work with municipalities all the time. So, we're in constant conversation with them. So, it's kind of hard to remember kind of where the ideas started. I think some come from municipalities and some come from us.

But there's a lot of excitement, as you know, most big cities are really looking at how they're going to plan for mobility in the future and do it in a planful way that it creates more opportunities for them than havoc or gridlock. So, as we've been in discussions with them there's obviously a role that we can play. Kansas City is probably the most advanced because not only do we have our mobility lab there, but we had a very engaged city that wanted to really work with us as they were also looking at their smart city initiatives. But there are a number of cities out there that we're talking to.

So, we're testing some things in Kansas City now, which allows us to work with the city to push information to consumers that are renting cars there that they might find helpful around entertainment or restaurants or things like that or just information about the city. So, I think we're going to see more of this develop in 2019 and 2020, 2021 as we go forward. But we do get calls from a number of municipalities wanting to talk further about us about where we are on this, and other technology we'll be developing in the pipeline going forward that can help enable this. And of course, this all stems from connected car. This is the root of how we can offer these kinds of things to municipalities going forward.

Chris J. Woronka

Analyst, Deutsche Bank Securities, Inc.

Great. Thanks, Larry.

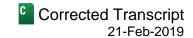
Operator: Our next question comes from Michael Millman from Millman Research Associates. You may ask your question.

Michael Millman

Analyst, Millman Research Associates

Thank you. Just following up, and then another regarding connected cars. Is there some simple minded way, I suppose, for us from the outside to look at your statistics and say, aha, it's working, is that in utilization or it's more

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broad and we have to look at the company as a whole? And second, unrelated, has to do with securitization and asset-backed financing? Have you seen that become more difficult or is it, easy for me to say, just a matter of price? Thank you.

Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

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I'll take the first question and then let Martyn take the second question. Connected car is going to play itself out across a number of different metrics. So there's not just one that you can point to and say okay that's the metric. It'll play out in gas collection. It's going to play out in utilization. It's going to play out in metrics around our assets, around salvage and damage. It'll play out in really everything, every process where we touch the car, from infleeting to de-fleeting, can be impacted by connectivity. So it's going to play out across the operations and it's going to play out also on the revenue side as we use connectivity to start being able to offer services and products to consumers in a way that they find efficient and helpful and useful for them and products and services they find relevant for their motivation for why they're renting.

So I think over time, Michael, we'll be able to point to it over time as we start really building it in a big way as we get the fleet that's connected higher and higher percentage each year. And as we take the learnings from Kansas City and start rolling them out into other markets. But we're still very much in the very beginning stages of this as we ramp up the fleet, work with all the different OEMs, work with the third-party suppliers. And as we get everyone kind of in the cadence of the improvements that we want to see across a number of these different initiatives that's when we'll start to see it roll through. But it'll be really across the operation.

Martyn Smith

Interim Chief Financial Officer, Avis Budget Group, Inc.

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And Michael, just on your asset-back question. So we found – we're in the market in the Q3 of last year. And then just very recently, you heard me say earlier about three weeks ago, and we find actually demand is really strong for kind of quality credit. So the higher cost we're booking is to do with the fed curve, it's not to do with the kind of credit spread. So we're finding a really strong demand for the well understood kind of mature credit story. And we continue to issue ABS notes kind of unimpacted by what you kind of read. It's not ABS, but we also did a high yield bond very successfully in October of last year as well. The credit markets are wide open I think for kind of quality.

Michael Millman

Analyst, Millman Research Associates

Okay. Thank you.

Operator: [Operator Instructions] Our next question comes from Hamzah Mazari from Macquarie. Your line is open. You may ask your question.

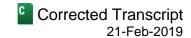
Mario Cortellacci

Analyst, Macquarie Capital (USA), Inc.



Hi, guys. This is actually Mario Cortellacci filling in for Hamzah. Could you talk to, I'm sorry, could you talk about how sustainable these levels of leisure pricing are? And on the commercial side, like we realize that the small business is a little more spot and a little more tied to or at least moving in the same direction as leisure. But on the large commercial side, when does that big contracted book of business turnover?

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Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

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So as far as the leisure side, I think it really, what we've done is we've built a revenue management system that looks and finds opportunities to yield rate when the fleets are aligned in the industry. And so what we saw in this past quarter is that there were a number of yielding opportunities throughout the quarter that allowed us to kind of drive that kind of rate on the leisure side.

Particularly the holiday periods, Columbus Day, Thanksgiving, Christmas drove a very high rate per day over those periods of time. And that's why we built the system and we get smarter with how we use it. And we've now rolled it out in the fourth quarter to the remaining markets in the country. So the entire United States now is on the full system and we'll be rolling Canada out this year and we'll start in EMEA kind of towards the end of this year and into next year.

And so that's why we built the system and we get better and better in how we use it. But it needs to find those quality times, if you will, to find those yielding opportunities and we then yield – we yield farther out in advance to be able to put most of our fleet into the yielding opportunity. So, as long as fleets stay reasonable in the industry, stay kind of tight to the industry, we'll continue to look and find for those opportunities to yield our rates.

As far as the Commercial book of business, look, I was really pleased to see in the fourth quarter that we kind of started to turn the tide on this, which has been a multi-year decline, to have volume up in Commercial and also underlying rate up in Commercial as well. So that's a very good sign going forward. I wouldn't say that we're going to see that perfectly every single month, as we go forward. I think it's still kind of a little bit back and forth, but I think we've gotten through the worst of it as we go forward.

If you take a look at the accounts that we renewed in the quarter, I would say over 50% of them, we renewed at higher rates. But the large, big large accounts still are under a lot of pressure and so the weighted average of the business is still not renewing at a positive rate per-day growth.

So we still have to tackle that. It gets closer and closer, but we are still negative in totality. But small business continues to grow as it is linked into the retail rates. And so we find opportunities also with the mid-market and we just kind of keep pursuing and pushing in all of these segments to grow those segments that can really improve rate per day.

And then at some point here, we've got to cross the line with the decline that's been happening for so many years. We've got to cross the line on Commercial, on the very large Commercial accounts, and start getting them to move forward in a positive way. When you sign these accounts, they're usually around three-year contracts.

Mario Cortellacci

Analyst, Macquarie Capital (USA), Inc.

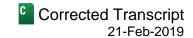
Got you. Okay. And could you give us a sense of your thoughts on potential impact on the used car pricing, given where new car inventory levels are? Or maybe what we could see if incentives pick up on new cars. Just kind of overall, how do you think about residuals going into 2019? And, where do you think they could potentially, I'm sorry, where you could potentially be wrong on those assumptions?

Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

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We put into our guidance where we thought our used car pricing is going to be for next year. So, our fleet cost per unit is going to be next year. But we are expecting residual values to decline. But we've got a lot of things going in our direction, going in the right direction for us as well.

Don't forget we've not fully matured in our ability to sell through alternative channels. And within the alternative channels, we still need to move our segments to be able drive more direct to consumer. So, if you look at the fourth quarter, we moved our alternative channel penetration from 54% the previous year to 67% this past year. But we still have a long ways to go. Within that, we're still selling heavier to direct to dealer although we have been improving our direct to consumer. We have opened lots last year and our retail lots are starting to really get their momentum as well. And we'll plan to open new lots again this year. So, we want to continue driving direct to consumer which will also benefit us.

I think the second area where we have an advantage that we are continuing to play out is just the data analytics and the data science we're putting behind our acquisitions and our dispositions. We're just getting a lot smarter about what we buy, what trim levels we buy it in, what colors we buy it in, where we in-fleet it, where we exit it, what time of the year we exit it, what mileage we exit it, down to the derivative. And that's way more science and analytics than we have ever done in the past. And that also is helping us outperform the market.

So, I think a combination of all those things will help us continue to take advantage of the market in the right way. You saw us sell a lot more cars in the fourth quarter this past quarter than we did the previous fourth quarter. We did the same thing in the third quarter. We're taking advantage of the markets when it makes sense and we're trying to sell cars in the right place at the right time. So, all this coming together I think can really help our performance go forward and offset some of the impacts that we might see from residual values declining.

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Analyst, Macquarie Capital (USA), Inc.

Great. Thank you so much.

Operator: Our final question comes from Derek Glynn from Consumer Edge Research. You may ask your question.

Derek J. Glynn

Analyst, Consumer Edge Research LLC

Good morning and thanks for taking my questions. How do you view the trade-off between pursuing pricing versus volume, and how do you balance those two, and are you willing to cede share to generate positive pricing growth?

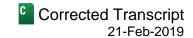
Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

Balance is the right word to use. It is a balance. And we think that we can maintain our share and drive pricing when the fleets are aligned in the industry. And that's what we saw as we looked into the last few quarters last year. So, that's going to be the – that's our goal, that's why we built the system. That's why we built DFP is to continually get smarter and find those opportunities – to find those yielding opportunities when the fleets are going to be forecasted to be just right. And so, the more of those we can find in more markets, on more days of the week, in more car classes, at more lengths of rentals, it matters. It makes a big difference and is way more complicated than any group of revenue management people could ever do without it.



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So, we are being able to look at a lot more markets, make a lot more price changes in the market and be able to forecast further out, which gives us the confidence to hold our fleet in for closer bookings because we believe that they'll be able to yield up when fleets tighten up.

If something happens in the industry where fleets got completely out of whack, then we'd have to reconsider that position. But that's not been the position in the industry now for quite a while. We've been seeing fleets aligned in the industry as you look past all of last year. And we're continuing to see that. So, I think we feel good about the strategy and we're going to continue to pursue the price over volume strategy going forward and that's why we built this system and that's why we've gone through all of this several years of development of this.

Derek J. Glynn

Analyst, Consumer Edge Research LLC

Thank you. Appreciate that color. And just secondly, given the relationship you have with the ride handling companies to send rentals to their drivers and given the size of their platforms, is there an opportunity for you to integrate your full service offering directly within their app? Not for a driver but for a traditional leisure customer who may want a longer length rental?

Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

I'm sorry, you said not for the driver but for?

Derek J. Glynn

Analyst, Consumer Edge Research LLC

Right. But, for traditional leisure customer who may want a longer length rental, just wondering because given the size of their platform and the relationships you already have in place, if there's a way for you to tap into their network through integrating your app directly within theirs?

Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

Yeah. We actually did that with Didi in China. So, we are on their app where customers if they're looking for something that a car hailing solution wasn't the right solution for, then, we were on their app where they could book a rental for a different kind of use case which is what you're referring to.

So absolutely we're open to those conversations and those opportunities. We have a great relationship with the car hailing companies and we continue to work with them. We have integrated onto Lyft's app for their drivers as we roll out the providing vehicles for their drivers as we go forward. As we mentioned, we're already live in Chicago, Atlanta, have a number of cities that we're going to be rolling out as well. And that is the drivers do book it on the driver app directly, it's, we've had full integration through our APIs. So, absolutely, we're open to those opportunities. And like I said, we talk to the car hailing companies frequently about other types of opportunities that we could do together.

Derek J. Glynn

Analyst, Consumer Edge Research LLC

Great. Appreciate it. Thank you.

Operator: For closing remarks, the call is being turned back to Mr. Larry De Shon. Please go ahead, sir.

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Larry D. De Shon

Chief Executive Officer, President, Chief Operating Officer & Director, Avis Budget Group, Inc.

Thanks. So to summarize, a combination of good volume growth, strong pricing in the Americas and lower perunit fleet costs, enabled us to grow earnings and expand our margins in 2018. We have a lot of exciting things going on at our company, only some of which we discussed today. Looking forward, you should expect us to continue to invest in our future by leveraging innovation, to build on our position as the leading global provider of mobility solutions, while also balancing this against our goal to consistently improve our profitability.

With that, I want to thank you for your interest in our company.

Operator: This concludes today's conference. You may disconnect at this time.

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