REFINITIV STREETEVENTS

EDITED TRANSCRIPT

CAR.OQ - Q2 2023 Avis Budget Group Inc Earnings Call

EVENT DATE/TIME: AUGUST 01, 2023 / 12:30PM GMT

OVERVIEW:

Company Summary

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

CORPORATE PARTICIPANTS

Brian J. Choi *Avis Budget Group, Inc. - Executive Vice President & Chief Financial Officer*

David T. Calabria *Avis Budget Group, Inc. - Treasurer & Senior Vice President of Corporate Finance*

Joseph A. Ferraro *Avis Budget Group, Inc. - Chief Executive Officer & President*

CONFERENCE CALL PARTICIPANTS

Chris Jon Woronka *Deutsche Bank AG, Research Division - Research Analyst*

Christopher Nicholas Stathoulopoulos *Susquehanna Financial Group, LLLP, Research Division - Associate*

John Michael Healy *Northcoast Research Partners, LLC - MD & Equity Research Analyst*

Ryan Joseph Brinkman *JPMorgan Chase & Co, Research Division - Senior Equity Research Analyst*

Stephanie Lynn Benjamin Moore *Jefferies LLC, Research Division - Equity Analyst*

PRESENTATION

Operator

Good morning, ladies and gentlemen. And welcome to the Avis Budget Group Second Quarter 2023 Conference Call. (Operator Instructions) As a reminder this conference is being recorded. It is now my pleasure to introduce your host. David Calabria, Treasurer and Senior Vice President of Corporate Finance. Thank you, sir. Please go ahead.

David T. Calabria - *Avis Budget Group, Inc. - Treasurer & Senior Vice President of Corporate Finance*

Good morning, everyone, and thank you for joining us. On the call with me are Joe Ferraro, our Chief Executive Officer; and Brian Choi, our Chief Financial Officer. Before we begin, I would like to remind everyone that we will be discussing forward-looking information including potential future financial performance, which is subject to risks, uncertainties and assumptions that could cause actual results to differ materially from such forward-looking statements and information.

Such risks and assumptions, uncertainties and other factors are identified in our earnings release and other periodic filings with the SEC as well as the Investor Relations section of our website. Accordingly, forward-looking statements should not be relied upon as a prediction of actual results and any or all of our forward-looking statements may prove to be inaccurate and we make no guarantees about our future performance. We undertake no obligation to update or revise our forward-looking statements.

On this call, we will discuss certain non-GAAP financial measures. Please refer to our earnings press release, which is available on our website for how we define these measures and reconciliations to the closest comparable GAAP measures. With that, I'd like to turn the call over to Joe.

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Thank you, David. Good morning, everyone. And thank you for joining us today. Yesterday, we reported our second quarter results, which delivered over $3 billion in revenue and $737 million of adjusted EBITDA. I want to thank all our employees for their efforts over the past quarter, which built on the strength of our first quarter and sets us up in a strong position to capitalize on the peak summer season.

On our last call, I mentioned that -- in the first quarter, it appeared the industry has returned to normal seasonal trends. That was true this quarter as well, where demand strengthened with each consecutive month, with June being the strongest showing terrific exit trends and positive momentum going into the summer. In general, trends for the quarter was what we had seen pre-COVID and shows that we are no longer in a COVID environment as it pertains to the business dynamics and seasonality. Overall, demand for travel is robust, and we believe the summer of

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

2023 will be one for the record books. But before we get into that, let me tell you about the second quarter, and as usual, let's start with the Americas segment.

The second quarter of 2022 marked the height of the supply-demand imbalance in the rental car industry, which led to historically high revenue per day. If you recall, we were just exiting Omicron. Fleets were challenged and at their lowest levels and travel increased as virus transmissions reduced. The second quarter of last year represented the highest RPD we saw in all of 2022, and there was no doubt that RPDs in the second quarter of 2023 would come down from the second quarter of 2022. The question was around where would rates normalize.

Given the stable industry dynamics we observed in the first quarter of 2023 and the normalized demand pattern we saw building into the second quarter. We believe that if we manage the fleet appropriately, an RPD in the mid-70s would be achievable. That would represent the ninth consecutive quarter where RPD is roughly 30% higher than the RPDs in the pre-pandemic era. The shapes of the graph today are looking more similar to what we saw in 2017, 2018 and 2019, it's just they're transposed 30% higher. And while it might be early to anchor to this new normal, it is clear that the marketplace is back to more seasonally affected trends and stability, which has allowed us to better forecast and plan fleet movements and volume growth.

We were able to grow rental days by roughly 3% year-over-year with June growing 6%. Last year, we saw demand materialize in those locations that supported beach, mountains, or areas of high outdoor activities. And while this was still true this year as well, we did see more robust return to cities, evening out demand, and this continues into the summer, allowing our utilization to be even more evenly distributed. Our utilization increased over 1 point, finishing at 71% with a larger fleet. As we have done in the past, we took advantage of our growth in new cars to exit or rotate out older and high-mileage vehicles at the highest residual values where we saw the opportunity.

As in prior quarters, there was high demand for our used vehicles, and we met that demand as required. Additionally, in advance of the summer season, our Avis brand kicked off their Plan on Us marketing campaign. Our first real media spend in years. In a world of change and uncertainty, we want our customers to know that they can Plan on Us because for 75 years, Avis has had only one plan to make sure you keep yours. It's a natural extension of our iconic 'We try harder' campaign and a commitment we make as an organization to deliver.

In every call since the pandemic began, we've referenced our rigid cost discipline. But cost control and cost cutting are two different things. This marketing campaign is just one example of the deliberate investments we continue to make in areas that we believe will generate outsized adjusted EBITDA benefits. Which is why we are again able to generate adjusted EBITDA margins in the mid-20s on a revenue base of nearly $2.5 billion. On that note, let me provide a few additional income statement results of this quarter.

In the Americas, revenue decreased roughly $140 million year-over-year, comprised of RPD declines of 8%, offset by rental day growth of 3%. Americas adjusted EBITDA during the same period decreased by roughly $410 million, primarily due to headwinds from rate, vehicle depreciation, and vehicle interest. While we believe that these factors will continue to be headwinds throughout 2023, as I mentioned earlier, we are seeing things reach an equilibrium. As you recall, the second quarter historically is a transitional gateway to the summer season with both volume and price increasing month-to-month with June being the strongest on both.

This is exactly what we saw this year. Commercial business supporting the early parts of the quarter with holidays such as Easter and Memorial Day, over indexing on leisure and the later few weeks of June, driven by a start to summer travel and dynamic increases in volume, rate and close-in bookings. As a matter of fact, we saw the highest amount of cars on rent at the end of June than we had ever seen before in any month in the history of our U.S. business. In summary, the Americas segment delivered solid second quarter results and every aspect of our business from fleet positioning to demand pricing to marketing and normalization of historical trends in both volume and price just at a higher pre-pandemic levels, all geared towards taking full advantage of the 2023 summer season.

And as long as I'm speaking about the summer, the exit trends we saw in June materialized early on this summer with the July 4th holiday being the busiest on record and reservation demand increasing with a velocity compared to previous months. I've been around to many of our locations in the Americas, talking to our team members, and I have to say they are ready with staff in place and vehicles to support this increased level of activity. With that, let's move over to our International segment.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

Similar to the Americas, our business operated at a higher level, generating an 18% margin, almost 13% more than a normalized environment of 2019. Volume increased 7%, with inbound travel generating a large part of that activity. Year-over-year rental day growth slowed from 16% in the first quarter to 7% in the second quarter of 2023. Which, similar to the Americas, saw an elevated level of travel post Omicron in the second quarter of 2022. RPD declined 4% year-over-year, the first decline after 8 quarters of growth.

But it's still more than 25% greater than 2019, excluding exchange rate effects. Just like in the Americas, we saw an increase in RPD as we exited the quarter from the levels we saw when we entered. However, there's more to unpack here. First, let's talk about the business mix. When we think of rentals in our International segment, there are three broad categories: domestic travel, which has travel within a country. Then there's cross-border travel, which has travel between countries in EMEA, a German renter renting in France. And lastly, is inbound travel, which has travel from renters originating out of EMEA, an American renting in France. International inbound is a segment where we're seeing strength similar to what other travel companies are reporting, but it's not a large enough segment to overcome the headwinds we're seeing in the core European travel.

Domestic and cross-border travel, which make up over 80% of the rental base is still down over 30% versus 2019. For this reason, we still believe that there's continued opportunity for operating leverage in this region. The return of days is just taking longer than we've seen in the Americas. When it comes to RPD, there is significant year-over-year comp noise to contend with. If you recall, in the first quarter of 2022, International RPD was $50.42 which sequentially grew to $62.69 in the second quarter of 2022.

That 24% sequential jump was due in large part to COVID restrictions being lifted in the APAC region in 2022, and we realized that, that wouldn't be replicated in 2023. This year, we saw RPD grow over 11% sequentially from the $54.28 in the first quarter to the $60.47 in the second quarter of 2023. We view that as a healthy underlying trends and expect sequential growth to continue in the third quarter of 2023. In summary, International's margin performance is strong, showcasing terrific cost discipline. Our International segment was able to generate over $175 million of adjusted EBITDA in the first half of 2023.

That's nearly 10x what the region generated in the first half of 2019 and despite days being down some 20%. That step function change in profitability is a testament to the rearchitecting of costs we undertook during the pandemic, and we believe that this will continue to drive sustainable adjusted EBITDA in the region as business recovers in the second half of 2023 and beyond. Moving on to fleet, where as usual, we'll focus more on the Americas segment. On our last call, I said that while we see -- saw a stronger-than-expected used car market during the first quarter tax refund season, we do not expect gains at those levels for the balance of the year.

That provided to be accurate with used cost strength moderating throughout the second quarter as it normally trends. However, the used car market is still significantly elevated over pre-pandemic levels, and there is an increased demand for our vehicles of our type. We are preparing for an environment where our gains will continue to normalize. The lower gains on sale this quarter versus the first quarter of 2023, combined with the additional new vehicles we inflated meant that depreciation costs in the Americas grew from $128 per vehicle per month in the first quarter of 2023 to $168 per vehicle per month in the second quarter of 2023. We expect this trend to continue throughout the third and fourth quarters, where our monthly net depreciation per vehicle converges with our monthly straight-line depreciation of roughly $300.

Similarly, monthly vehicle interest per vehicle grew sequentially from $83 in the first quarter of 2023 to $96 in the second quarter of 2023, and we expect this trend to continue as well. This is a true cash cost to our business, and we manage it obsessively. We've been consistent in saying that on the margin, we'd rather run out of an incremental vehicle than have an unutilized vehicle on our lot. I believe our fleet growth this quarter reflects that position, and we'll continue to fleet just under demand to optimize utilization and mitigate the headwinds of vehicle depreciation and interest.

As with previous quarters, we continue to look for opportunities to rotate our fleet exiting older, higher mileage vehicles with newer deliveries as this helps to improve maintenance-related costs and increase service levels, which enhances our customer experience. We are pleased with the support we get from our OEM partners to deliver new vehicles, differentiated makes and models all aligned to increase our diversified offerings, and insulate us from any large-scale recalls.

This quarter, our actions were consistent with that rhetoric. We will continue to be consistent going forward. Currently, we believe we are fleeted just under demand for the upcoming quarter in order to optimize utilization and mitigate the headwinds of vehicle depreciation and interest.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

Additionally, we continue to roll out our electric vehicle strategy which centers on an integrated infrastructure at our locations with vehicle offerings from a varied group of manufacturers.

Demand is increasing, and our key focus is on Airport locations, which additionally deliver the highest RPD and contribution margin. We are still in the early stages of performance in this category. But it's important to our team to set the groundwork to customer demand, vehicle maintenance, and revenue-generating activities, as we know this segment will continue to grow over time. Technology is a key aspect of our day-to-day performance, creating efficiency in the business and allowing for improved customer experience. Over the past 7-plus years, we have continued to iterate our proprietary demand fleet pricing system which gives us tremendous insight on demand down to vehicle location and prices our cars accordingly.

We believe this technology, combined with our pricing team and field experience generates a significant advantage in managing supply and demand. Data analytics, combined with our on-the-ground productivity systems has created efficiencies in our location level throughput, increasing our performance well above levels we experienced in 2019. Modernization of our IT systems have provided benefits, allowing our partners to seamlessly create reservations generating real-time demand and increase revenue while creating stability in our operating environment.

On the customer experience side, a touchless process allows customers to choose their vehicles on their phone or exchange it upon arrival, creating a digital rental agreement, which can be used to exit our facilities through an automated exit gate process.

Facial technology rolled out at a majority of our Airport locations quickly transfer first-time Avis preferred customers to their vehicles, thus bypassing our current counter verification process. In this quarter, we have rolled out an improved budget choice application. Customers upon arrival at a budget facility choose their vehicle from a reserve zone, take a picture of the license plate, allowing a rental agreement to be sent to them digitally for a quick exit at an unmanned exit gate.

This concludes my prepared remarks. But as we're in the middle of the summer season, let me provide a bit of color around just what we're seeing. In a word, things are looking positive. The demand for travel is strong. And the exit trends we saw leaving June continued with the July 4 holiday being the best on record in the U.S. The summer season has always been a time of the year when activities are at this highest level. This year, the peak seems to be larger and more elevated. Bookings are happening closer in, which is what we've seen traditionally as customers are confident in both longer term and closer in travel opportunities.

Pricing in the third quarter will improve sequentially from the second quarter and more aligned with traditional seasonality that we saw last year when it was approximately flat from quarter-to-quarter. We have enough visibility to project that despite some reallocation of demand towards international travel, our Americas segment will deliver the most rental days in the company's history this coming quarter. The industry is appropriately fleeted and we expect this normalized rate environment to continue throughout the summer. All I can say is that our team is ready and everyone is laser-focused on taking full advantage of this favorable environment, and I look forward to showing you what that means on our next call.

With that, let me turn it over to Brian to go through our liquidity and our outlook.

Brian J. Choi - *Avis Budget Group, Inc. - Executive Vice President & Chief Financial Officer*

Thank you, Joe. And good morning, everyone. I will now discuss our liquidity and near-term outlook. My comments today will focus on our adjusted results, which are reconciled from our GAAP numbers in our press release. I'd like to start off by addressing capital allocation. We took a balanced approach to free cash flow deployment in the quarter and preserved optionality on how to opportunistically allocate capital in the second half of 2023.

We voluntarily contributed equity in our fleet by foregoing the refinancings of higher cost tranches of our AESOP term debt as they came due and funded those tranches with cash on hand instead. This benefit is seen in our fleet debt leverage ratios and will mitigate vehicle interest costs, which is adjusted EBITDA accretive. We also repurchased a little over 720,000 of our shares at an average price of $202, bringing our total repurchase for the first half '23 to $146 million. The cash we generated in the first half of the year was significantly higher than the cash we deployed towards vehicle equity contribution and share buybacks during this period.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

We expect to be more active with capital deployment in the second half of the year which aligns with the timing of the majority of our cash generation. We remain in a position to aggressively allocate capital to those areas that best benefit all stakeholders of Avis Budget Group as we identify opportunities. We once again find ourselves in the privileged position of being in the strongest financial standing in the history of our company. Our last 12 months adjusted EBITDA was $3.4 billion. During the first half, we contributed nearly $900 million back into our vehicle programs, deployed over $130 million into investments in our systems, operations, customer experience and electric vehicle capabilities all while having a net leverage ratio of about 1.2x.

As of June 30, we had available liquidity of approximately $1.1 billion, with additional borrowing capacity of $1.1 billion in our ABS facilities. Our corporate debt is well laddered, with approximately 87% of our corporate debt having maturities in 2026 or beyond, and we are in compliance with all of our secured financing facilities around the world with significant headroom on our maintenance covenant tests as of the end of June.

Let's move on to outlook. As you know, we've made the decision as a management team to forego giving formal annual guidance to allow ourselves the flexibility to make agile decisions as the business environment changes. However, I do want to provide some color around what we're seeing for the third quarter. As Joe mentioned earlier on the call, the summer season is robust. We're taking a measured approach at Avis and expect to fleet slightly inside of the strong demand we're currently seeing.

That should translate to rental day growth of mid-single digits in the Americas segment and high single digits in the International segment. Vehicle disposition gains will moderate, and we expect the convergence between gross and net depreciation to continue. Cost control remains a key area of focus, and we believe you'll continue to see operating leverage net of fleet sale gains. In summary, the travel environment is in our favor, and we're well positioned to take advantage of it.

As Joe mentioned, the summer peak is strong, and we should see sequential RPD growth in both regions, which is what gives us the confidence to say that despite diminishing fleet sale gains, we believe adjusted EBITDA for the third quarter of 2023 will be roughly $850 million. With that, let's open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question that we have comes from John Healy Northcoast Research.

John Michael Healy - *Northcoast Research Partners, LLC - MD & Equity Research Analyst*

Joe and Brian, I was hoping we could talk a little bit about the pricing environment. Obviously, the optics of negative pricing has now shown up. But I'm not really sure that, that should be surprising to us. So I was hoping to talk about your thoughts going into this year about how pricing might trend and how it's actually performed relative to that?

And then as you look out to '24 and '25, what gives you confidence? Because I feel like you're implying a level of confidence that pricing could stay at these meaningfully double-digit levels above pre-COVID levels. So just kind of how you underwrite that thought process and kind of how you get to that conclusion.

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Good Morning John. So it's best to understand pricing to understand from where we came. If you think about last year, as we said in our prepared remarks, there was a high level of travel that occurred right after Omicron and it was at the time where the fleets were at their lowest. Everyone took cars out the year before, and we were all basically trying to get our fleet sizes up as we transition into 2022.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

And because of that period, people there was just a robust amount of travel and traveling at high prices. If you recall last year, I would have to say that for the first time ever people booked car hotel, car, airline, and hotel and in every year prior to that, was always airline, hotel, and car.

So cars were in high demand, and you guys saw all the news that was going on about that. And we enjoy really high RPDs. I think if you think about this year, however, this year, you're going back to a more, and I can't say it enough, seasonal approach to how we manage and view the business.

And the second quarter is always a transitional gateway to the third. You guys know that as well as I do. We get cars in to take care of the summer peak and get prepared for what we consider to be the most elevated part of our demand curve. And in this quarter, we saw prices elevate from the first quarter, which was what we expected and very much, over 2019 levels. And then when you think about how the quarter progressed, April and May, more traditional commercial months, so there's more of a commercial segment dedicated to that group of offerings.

And then once you get to June and you get to the second half of June, when kids got to get off from school and vacation travel starts to continue, you start to see this growth in price. And it all comes because demand starts to elevate. And what we saw was demand was elevating at a very, very high and fast level. So the exit trends that we saw in June were obviously much better than what we saw going into the quarter, and the second plan for June was also elevated to the beginning. As you go into the third, which I think is where your question lies, like, we do believe the sequential opportunity will continue.

Last year, the rates were flat from the second quarter to the third. We couldn't get over the height that we saw in quarter 2. I think this year, you're going to see that whole seasonality spectrum normalize and the prices in the third quarter will be certainly better than the second. And when you think about that going out, I think it has to do a lot with what's the fleet and what's the positioning. And as we said in our remarks, fleets were tight, right. We were just under what our demand was scheduled to be.

We got good insight from the OEMs on what our deliveries were going to be like and we operate it accordingly. And so prices have improved. Now this whole question about like what's going to happen in 2024, I think, is an interesting one. Right now, we're in the heat of the summer. And we're spending a lot of our time executing and making sure the third quarter is going to be as robust as we think it could be. But I think as you go out, you'll see this more normalization of the seasonality trends that we've been talking about, where the first quarter is about winter and commercial travel.

The second quarter is usually better than the first. The third quarter is usually better than the second and the fourth quarter is kind of a combination of holiday travel and early commercial bookings I think you'll see fleets very much in line during that period of time and pricing will, of course, be coordinating with that.

Brian J. Choi - *Avis Budget Group, Inc. - Executive Vice President & Chief Financial Officer*

John, it's Brian here. Just to add to that. Kind of the normal seasonality that Joe has mentioned, that's kind of what we're expecting for 2024 at this point, but we're still in our early in our planning phases. The one thing that we do know for certain is that interest rates will continue to be a headwind next year, and the used car market is going to continue to normalize, which is as we go through our planning, we're remaining kind of laser-focused on utilization and intent to fleet slightly below demand in order to remain disciplined around return on invested capital.

Operator

The next question we have comes from Stephanie Moore from Jefferies.

Stephanie Lynn Benjamin Moore - *Jefferies LLC, Research Division - Equity Analyst*

I wanted to touch on your comment about the stepped-up media spend in the second quarter, my expectations to continue going forward. Maybe just talk a little bit about the rationality to step up media spend for the first time in some time.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Yes. Look, we haven't spent any real money on talking about our brand in a fair amount of time, I could tell you during my time as CEO and even as the President of Americas, we didn't do a whole lot of that. And I think part of our plan was that we should tell the world about our company. And we picked talking about -- for the past 75 years, we've only had one goal, and that was to keep yours. And it was an extension of our 'We try harder' model that we had for many, many, many years. And I think the time was right for us, right?

We had generated a lot of activity last year. We had generated record profits and it was time for us to talk about our company in a more positive environment than we had in the past. And I think our campaign was done really well. We were on-air TV. We had digital applications. We ran a lot of the airports and we were on for a good period of time. What we do going forward will be all determined about what we think is the right opportunity, and we'll always have that ability to do that. If we wish the brand the model and slogans iconic can always draw off of that should we need it. But we saw -- it was the right time, and it gave us a pretty good balance.

Stephanie Lynn Benjamin Moore - *Jefferies LLC, Research Division - Equity Analyst*

Absolutely. And then just as a follow-up. I wanted to get your thoughts or get an update on how your conversations with OEMs are going for the back half of this year and in 2024, you noted that you did take growth of some new cars in the quarter to rotate out of some higher mileage vehicles. Can you just talk a little bit about those conversations with OEMs and how you're kind of balancing supply availability with new vehicles and also kind of continuing to play and used ultimately, what that could mean for depreciation?

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Sure. I'll start off. Brian, if you want to add something about depreciation. We are in constant communication with our OEMs. And we have relationships that go back fortunately, decades. So we're always talking to them and gaining insights into what they see whether it's going to be, are there going to be vehicle delays, are they going to be on schedule, the types of vehicles that they have coming up, the vehicles that they want to offer to our industry.

And coming off the first quarter, now everyone knew that the MMR index was tweaking up. We've had cars through the pandemic that we wanted to rotate out. I think when you think about the whole fleet dynamic, you start off with, well, how much do you cost to buy a car, how much is -- how do you exit the vehicle, your in-life use. But I think one of the areas that we've been consistent with over the years and why we've had such stability in our overall cost and not a whole lot of imbalance is the fact that we take advantage of the times right to rotate out the older vehicles. Because eventually those cars become commercially unacceptable and lead -- could lead to challenges in the business.

So we did what we thought we needed to do. We rotated out of the cars. We had insight that we were going to get vehicles in to support what we believe our demand. As you see, we had a utilization benefit in the second quarter, which is something that we are really focused on because of the fact that interest costs are so much higher this year. And going out I would say that the OEMs have a measured approach to supply. I think everyone learned last year, especially dealerships, how to sell cars with not having the total amount of inventory that they had in the past.

And I think that's what you're going to see going forward. I mean, the autonomous sites talk about what they think new car supply is going to be or how many cars are going to get sold in the United States next year. And this year, it seems to me like there's going to be a slight uptick, but kind of in line with what you saw this year. Brian, do you want to talk about depreciation.

Brian J. Choi - *Avis Budget Group, Inc. - Executive Vice President & Chief Financial Officer*

Yes, sure. You noticed right now the trends in depreciation ticking up, and this is because as we exit our older model vehicles and in fleet newer model vehicles the cap cost is much higher. We expect this trend to continue. And because we take a return on invested capital approach to all of

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

our decisions here, we understand that we're going to have to be disciplined in terms of both the quantity of cars we buy and what we pay for those cars.

The best way to protect depreciation and residual values is to make sure that you purchase the cars correctly and we need to ensure that our purchase price has a cushion to the retail purchase price. So that's what we're focused on. We do this every single year, and we're making sure that we optimize our portfolio purchases for next year.

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Listen, I'll just add one thing. There's still demand for used cars. And there's a $20,000 benefit between the price of a new car and used car, which is always attractive. And the used car inventory is light because of off-lease vehicles and plus trades. So there's still going to be demand to sell our cars going forward.

Operator

(Operator Instructions) Next question we have comes from Chris Woronka from Deutsche Bank.

Chris Jon Woronka - *Deutsche Bank AG, Research Division - Research Analyst*

Appreciate all the details so far. You guys obviously did a terrific job on fleet management, as always, during the quarter. But the question is really on what you're seeing in the industry landscape. And we know that at least one of your peers is bringing back more fleet. Of course, they were severely challenged last year. And so the question, I guess, Joe, is it seems like with you guys fleeting more under demand, the implication is your -- you want to hold pricing integrity for the whole industry and you're willing to maybe forego a little bit of volume for that. Is that directionally, correct? And just what are you seeing out there with the peers?

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Chris. Look, I think over the years, if you look at how we manage our supply and demand, you've seen a very consistent approach to our utilization curves, and I'm talking going back many years pre-COVID. And that has not changed. I think there's a lot of rigor in our business and our company on how we manage those two. How we manage supply as compared to demand. We said in our opening remarks that we forgo a rental if we're going to have a car sitting on the sidelines, right? I'm not going to hold the car for that just one incremental rental a week. So we look at that.

That being said, we also understand that we have the largest peak in the year occurring right now. So our fleet is in line with that high level of demand. Now what normally happens after we get out of July and possibly early August, is that we start to trend our fleet sizes down to deal with the seasonality of demand that occurs between August and the end of the year. And as you go out, the third quarter is October is largely about commercial business and then the November, December period is about more or less holidays. And our fleet size will go down according to that demand curve that we see so that we open up next year in the right spot.

And then next year, we start building upon on demand. I think as I said earlier, the OEMs are for rather disciplined on their approach sure they want to sell cars just like every other year. But right now, last year was -- the car sold to the industry was at its lowest point in the past 6, I think. And so there's expected to be more demand -- more cars sold this year, but not to the levels it was previous years.

Brian J. Choi - *Avis Budget Group, Inc. - Executive Vice President & Chief Financial Officer*

And Chris, just to add to that, listen, we can't comment on the strategy of our competitors. But just speaking for ABG, I think we can say we don't manage to optimize market share. We managed to optimize profitability.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

Chris Jon Woronka - *Deutsche Bank AG, Research Division - Research Analyst*

Okay. Fair enough. And then I guess as a follow-up, maybe we can go back to fleet management a little bit in terms of -- I think I probably have asked this question on prior calls, but just the way that you're managing the fleet in terms of whole period and buying used cars selectively and changing your mix and things like that and cascading things through ride share. I mean the question is, do you think we're at a structurally lower level of straight-line depreciation going forward relative to, say, 2019?

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

I'll start and give you kind of how we do it. And then Brian, you can comment. When I think about how we deal with the day-to-day on fleet, it starts with what we anticipate is coming with new cars and also centers around what we believe demand is going to be like. We will always react to favorable environments in the car selling market. We have systems that allow us to anticipate where the car is best going to be sold in a geographic location what level of trim needs to be on that car to be sold at a proper benefit to us and what time of the year is best to sell that car, specific car, not just a car in general.

And we work through that, and we have modeling that we do with outside companies that help us determine residual values over the short and longer haul. And that hasn't changed. And if you see, we took out cars in the early part of the year, we took out cars in the second part when residual values were at their best, and we'll continue to rotate our fleet because we believe that, that's a true aspect of maintaining some consistency and overall fleet cost.

So you don't have any blowups that would say, you have cars and you rent cars that are problematic. As far as our as how we cascade cars, -- we have a good number of brands that we do that with. Obviously, we have Avis and Budget, and we have Payless, which we cascade cars too. And we have this very interesting and growing ride-hail segment that we also allocate vehicles too.

And that has helped. Along with that, Chris, we've developed over the years, mileage optimization, which is a tool that is seamless to our team. But it allows the evening out of mileage. So we don't have these large discrepancies of 1 or 2 cars having an abundance of miles and own it for a short period of time. That technology has helped us to maintain an even level of mileage accretion over the totality of the fleet. And I think the other thing is about segments of business. What segments accrued the least amount of miles, which will determine your overall cost per car. And we've capitalized on growing commercial segments that do that.

Some commercial accounts, rent a car for 4 days, park it in a corporate office for those days do very little mileage, monthly rentals are also a segment that does little mileage, and we try to accelerate some of those.

Brian J. Choi - *Avis Budget Group, Inc. - Executive Vice President & Chief Financial Officer*

Yes. Chris, in terms of the gross like the straight-line depreciation, you'll see when our Q was posted after this call is roughly 280 this quarter. That's not too far off from where we were on a gross debt straight-line in 2019. So despite significantly higher cap costs, we're managing like you said, with all the things that you had mentioned, the cascading, extending the useful life of vehicles to still be around those 2019 straight-line debt levels.

But when we think about carrying cost of cars, you have to factor in vehicle interest as well, and that's significantly above where it was in 2019. It was like kind of in the mid-50s in 2019, and now we're guiding to it's going to be over $100. That's a real cash cost to having the vehicles as well. So we're always kind of managing making sure that we get the appropriate return on capital for our fleet.

Operator

Next question we have comes from Chris Stathoulopoulos from SIG.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

Christopher Nicholas Stathoulopoulos - *Susquehanna Financial Group, LLLP, Research Division - Associate*

Joe I am wondering if you could dig into the comments on cross-border here, perhaps provide a little bit more detail with why you think it's weaker or at least at this point in the cycle?

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Yes. Look, I think when you talk about cross-border, you have to think about some of the elements of it. If you're looking at cross-border from -- into the Americas, that's at really high levels, right? So there's a whole lot of travel coming in from Europe, Asia Pac, South America the Caribbean, et cetera.

That's really strong. And it's over a really strong base last year. So that has not -- we have not seen that slow down. As a matter of fact, we anticipate that being strong throughout the summer and into the fall, quite frankly, as I think as you -- the question may be about European travel. The reverse, the Americas into Europe is very strong. People have booked far in advance, and that has been really solid. Similar to what the airlines are seeing I think that the European travel that we called out is the inter-country travel. If you remember last year, Europe was shut down pretty much. And when it opened, there was a whole abundance of people going back to see family and friends and maybe some commercial and leisure travel.

That peak was hard to overcome. We believe that as you go forward, some of that would start to moderate as well.

Christopher Nicholas Stathoulopoulos - *Susquehanna Financial Group, LLLP, Research Division - Associate*

Okay. And my second question, so when you talk about the return to normal or typical seasonality. I just want to understand how we should think about the moving parts of U.S. domestic. So from the perspective of the airlines, we have plateauing business volumes, a lot of murkiness as it relates to blended travel. And then, of course, as you said, very strong outbound international travel, which is pulling from a potential domestic travel pool. So could you help frame or provide a little bit more color how we should think about seasonality given these moving parts here within the domestic U.S. for the second half?

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Sure. What we are seeing is close in reservations booked with an acceleration that we hadn't seen so far this year. As soon as the summer season started. I think when you look at last year, there was like more or less a straight-line level of demand going into the summer. We came off a huge Omicron bump and going into the summer, we didn't see that level of activity. This year, the peak seems elevated to me. It seems like there's more travel, and it seems like it will extend.

If you recall last year, there was during the course of the year. Kids were working for school remotely. They started to go the second half. I think it cut the summer period a bit shorter. Because people were excited to get the back-to-school stuff. I think that extends a little bit more this year. So we're seeing pretty significant demand going into the summer. And I think there was probably, if you want to call it out this way, there was probably some travel fatigue as you got into the fall. A whole lot of activity first and second quarter and then into the third in the early part of the third some travel fatigue. So we still see demand pretty strong.

And TSA activity right now is kind of plus 1 or give or take versus 2019. And our rentals are certainly higher than that. We have a lot of commercial business that has been coming in. People, commercial companies are getting back to travel. We've seen outsized demand in aerospace and defense, professional and financial service companies, tech. So we see domestic travel pretty good.

Operator

The final question we have comes from Ryan Brinkman from JP Morgan.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

Ryan Joseph Brinkman - *JPMorgan Chase & Co, Research Division - Senior Equity Research Analyst*

Relative to that $900 million deployed back into the vehicle programs in the first part of the year, of course, this is increasingly attractive with the rise in rates. What is the amount now that you are over collateralized or that you could withdraw from the programs and cash at any time. And I think you said before, you intend to be nimble with this going forward, given the changes in rates, your stock price or other opportunities. Could you, at the same time, maybe see yourself running with a structurally higher mix of equity in the fleet, such as your key private competitor has traditionally run with.

Are there advantages to that approach beyond obviously paying interest on less debt, such as maybe being able to negotiate better rates on the remaining debt or other benefits you can think of.

Brian J. Choi - *Avis Budget Group, Inc. - Executive Vice President & Chief Financial Officer*

Ryan, I'll take that. So in terms of the cash that we put into vehicle programs this year, all of that is available to be redeployed kind of almost at a moment's notice for this year, we're over-collateralized versus where we've historically been. And I think like without giving an exact number, the best way to look at this is look at what our vehicle debt is relative to our vehicle assets, and you've seen that tick down.

In terms of in terms of the benefits of having structurally more equity in the fleet, yes, that is -- there are benefits that come from that, but I feel like we're fairly a long ways away from becoming like any sort of investment grade. I don't think that that's kind of in the horizon for us. We feel that there is better use of our free cash flow at this time, especially given that we believe that our shares are undervalued at this time. And we're just taking a balanced approach to capital allocation, which we think is prudent in today's rate environment.

And then like you said, kind of parking excess free cash flow temporarily in vehicle programs. It preserves optionality. It's readily accessible when opportunities arise. But in the meantime, it lowers vehicle interest costs. So, as we said in the past, we won't be formulaic when it comes to capital deployment, we'll continue to be nimble with kind of timing and magnitude.

Ryan Joseph Brinkman - *JPMorgan Chase & Co, Research Division - Senior Equity Research Analyst*

Great. And then finally, I realize it is a diminishing number with less potential to benefit DPU going forward. But can you give us a sense as to how many fully depreciated vehicles might remain in stock. And are those vehicles primarily in the Americas segment? Or how should we think about that?

Brian J. Choi - *Avis Budget Group, Inc. - Executive Vice President & Chief Financial Officer*

We're not giving guidance around that or a specific number, but it's a de minimis amount at this point. And so we won't -- we're not forecasting benefits from that going forward, which is why we think that you'll see this convergence between straight line depth and kind of our reported net debt.

Operator

There are no further questions at this time. I would now like to turn the call back over to Joe Ferraro for closing comments. Please go ahead, sir.

Joseph A. Ferraro - *Avis Budget Group, Inc. - Chief Executive Officer & President*

Yes. Thank you. So to recap, we reported strong earnings driven by robust demand from our commercial and leisure travel in the Americas and seasonally increased demand from our international segment. More importantly, the summer is off to a great start. And we are ready for this new

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV

and peak period that we are undertaking now. I would like to once again say thank you to all our employees for their hard work and dedication for getting us ready for the strong season, and thank you all for your interest and time with our company.

Operator

Thank you, sir. Ladies and gentlemen, that then concludes today's conference. Thank you for joining us. You may now disconnect your lines.

DISCLAIMER

Refinitiv reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES REFINITIV OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2023, Refinitiv. All Rights Reserved.

©2023 Refinitiv. All rights reserved. Republication or redistribution of Refinitiv content, including by framing or similar means, is prohibited without the prior written consent of Refinitiv. 'Refinitiv' and the Refinitiv logo are registered trademarks of Refinitiv and its affiliated companies.

REFINITIV