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CAR - Q3 2019 Avis Budget Group Inc Earnings Call

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OVERVIEW:

Co. reported 3Q19 revenues of approx. $2.8b. Expects 2019 revenues to be $9.0-9.2b.

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PRESENTATION

Operator

Greetings and welcome to the Avis Budget Group Third Quarter 2019 Conference Call. (Operator Instructions) As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, David Calabria. Please go ahead, sir.

David T. Calabria - *Avis Budget Group, Inc. - Senior VP & CAO*

Good morning, everyone, and thank you for joining us. On the call with me are Larry De Shon, our Chief Executive Officer; and John North, our Chief Financial Officer.

Before we begin, I would like to remind everyone that we 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 and 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. We undertake no obligation to update or revise our 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, which are reconciled from the GAAP numbers in our press release and in our new investor presentation also 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.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Thank you, David, and good morning, everyone. Yesterday, we reported third quarter revenues of $2.8 billion driven by a 2% increase in rental days and a 20 basis point increase in vehicle utilization year-over-year.

Our Americas achieved record high revenue and adjusted EBITDA in the quarter, demonstrating the continued strength of the region. Our International team saw positive year-over-year pricing, excluding exchange rate effects, for the first time in 11 quarters. The average length of our rentals increased 1% from last year, lowering the frequency of vehicle cleaning and preparation, resulting in more profitable rentals.

And optimizing our fleet mix and pairing the right customer with the right car has also shown a positive impact on customer's rental experience, as seen through our record-high Net Promoter Scores throughout the world. We have now eclipsed more than 160,000 vehicles in our connected fleet, and we remain on track to connect more than 200,000 by the year-end.

We continue to launch locations for our mileage optimization initiative and have 14 cities active, with further locations targeted by the end of the year. This initiative allows us to balance mileage consumption and is yet another lever to lower fleet cost. Operationally, our focus on efficiency improved fleet utilization by 20 basis points. As we are driving efficiencies in the core business, we are simultaneously investing in mobility initiatives, unlocking incremental profit opportunities and enriching the Avis value proposition.

On the call this morning, I will provide an overview of the Americas and International segments, discuss ongoing progress with our innovation and mobility initiatives and provide an updated outlook for the remainder of the year.

The Americas segment delivered record earnings and the eighth consecutive quarter of adjusted EBITDA growth, totaling $321 million, up $8 million from prior year, excluding currency effects. Website revenue continues to be a focus area for us, where we saw online transactions up more than 3% in the quarter, the 28th consecutive month with an improvement.

Our local market strategy drove longer length of rental and increased revenue per transaction and provided solid returns, growing by 5% in rental days. The growth of our Zipcar Commuter business offers a monthly membership fee, which covers fuel, insurance and other costs, resulting in a lower revenue per day that provides higher utilization of vehicles in off-peak times with low mileage accretion at an attractive margin. Likewise, our Budget Truck package delivery business recognizes high utilization of our delivery vehicles for a longer duration, providing a greater revenue per rental. These business units capitalize on longer rentals, resulting in greater vehicle utilization and profitability.

Over the third quarter, fewer extreme weather events, recalls and vehicular accidents created excess fleet levels, which drove pressure on pricing in the quarter. However, in September, both industry-wide accelerated fleet dispositions and significantly fewer new vehicle purchases have helped to rightsize supply. These adjustments have delivered signs of positive pricing in the back half of October and beyond.

Instrumental to the overall performance in the Americas was a 9% reduction in per-unit fleet costs due to continued strength in the market for used vehicles, growth of our alternative disposition channels and our proprietary fleet management system that optimizes vehicle purchase and disposal decisions. Through the third quarter, we have already disposed of 85% of the fleet we expect to sell in 2019, with a record high of more than 70% in alternative disposition channels.

By leveraging our fleet connectivity, we can better manage vehicle usage, such as ensuring miles are distributed more evenly throughout the fleet. We also extend this technology to manage our ride-hail fleet vehicle mileage and reduce usage of vehicles that are accumulating miles too quickly to protect residual values. As a direct result, we are able to reduce fleet costs and deploy our right car, right customer rental experience for customers across all segments.

For the second quarter in a row, our ancillary revenue strategy drove higher sales due to more small business rentals and our revised rental sales agent incentive program. This program is a success for both our customers and our employees, as we are also seeing record Net Promoter Scores with this initiative.

On a constant currency basis, our International business achieved an adjusted EBITDA of $178 million, the same as prior year. We are proud of the team's results, considering the uncertainties surrounding Brexit, the weakness in intra-European travel and higher fleet costs due to the enactment of stricter vehicle regulations, such as WLTP. We continue to concentrate on maintaining and growing revenue per day to counter these impacts.

In the quarter, we achieved an increase in revenue per day, excluding exchange rate effects, our first positive increase in 11 quarters. Despite 7 European airlines halting operations and a recent bankruptcy in the travel and leisure market, the international team was able to mitigate lost volume while achieving a price increase.

We continue to grow our light commercial vehicle operations, which provides longer and less seasonal rental demand, growing volume nearly 10% from prior year. Commercial segment rental days showed positive year-over-year growth, with mid-market and small business accounts both up 9%. International made record strides, driving substantial improvements in Net Promoter Scores over prior year, exemplifying our continued focus on improving overall customer satisfaction.

With that, I'd like to update you on the progress we've made on our innovation initiatives around mobility. We continue to make strong progress on our goal of fully connected fleet through our partnerships with PowerFleet, formerly known as I.D. Systems; Continental; and our OEMs, including our most recent announcement that we'll be leveraging Ford's connected services across Europe. We are making progress every day with more than 160,000 vehicles currently connected and a line of sight to over 200,000 connected vehicles by the end of the year.

We continue to see benefits from our connected fleet, including well over $1 in incremental fuel recovery on each connected car rental, which more than pays for the cost of the technology. In addition, connectivity reduces the length of time to recover overdue vehicles; facilitates our mileage optimization initiatives; allows us to explore additional use cases, powered by self-service capabilities; and enhances our fleet management capabilities, supporting our new fleet models with ride-hail companies. It has been a multiyear journey for us to mature this concept to scale but the returns are there, and we see a path towards accelerating monetization in 2020.

We remain at the forefront of customer experience, powered by the Avis mobile app and its capabilities to allow customers to control their end-to-end rental experience. Initiatives like specialized Loss Damage Waiver pricing, pilot of e-Toll unlimited and the expansion of our new ancillary incentive plan continues to drive growth in revenue and customer experience. We have established new customer ancillary touch points to provide product and service offerings tailored to customer preferences, allowing us to sell beyond the counter. We continue to grow the number transactions on our mobile app, and preferred customers who use the app report significantly higher Net Promoter Scores than those who do not.

The third quarter was also our first quarter offering, Split My Bill, our split bill capability, and we are already seeing an increase of products being taken with our new functionality, like SiriusXM or Curbside Delivery. With the introduction of Split My Bill, our business travelers can go beyond the normal corporate rental to experience upgrades and additional services that travelers enjoy and want. We recognize that many travelers use business trips as an opportunity to explore new cities or meet up with family or friends in the area, and we are thrilled to offer a feature that will help them make the reconciliation of travel expenses cleaner and easier. Our mobile app experience gives customers more customization and more personalization of their trip than any other brand.

Previously, we discussed our partnership with Lyft. In the last quarter, we announced our partnership with Uber as well. Since then, we expanded our operations to new locations, and are now in 13 major cities. The fleet has grown approximately 60% in the quarter, and we continue to expect growth through the remainder of the year. We believe there are several benefits to the partnership that can improve our overall economic performance, such as extending the age of a portion of our fleet and derisking our fleet sales. The value we generate from these partnerships continues to show how car rental and ride-hail can operate in unison by providing mobility solutions to a wide array of intersecting customers.

We have begun to monetize the anonymous connected car data we collect from the fleet, leveraging one of the numerous benefits of having connected vehicles. Our partner, Otonomo, is one of the first to create a new marketplace for this information and has already gathered a growing number of customers. We look forward to new partnerships and new learnings from this relationship.

Our Zipcar Flex product in London continues to expand, as we are looking to grow the Flex offering to cover most of London, our largest Zipcar market globally. Zipcar Flex provides on-demand, one-way mobility throughout London as well as to and from Heathrow airport. We are seeing significant growth in this model and it is on course to exceed the objectives we have set for Flex.

To summarize, we continue to see real success in our multiyear mobility investments with the development of our technology and mobile apps, and our growth in our unique partnerships with other mobility leaders who are successfully leveraging our vehicles and fleet management capabilities to serve new use cases together.

With the summer behind us, we are proud of the record results the Americas achieved and how the international team has navigated through a difficult macroeconomic environment in Europe. Fleet costs were a benefit through September, resulting from strong residual values, although percentage improvements are not expected to be as great in the fourth quarter. Our use of alternative disposition channels will be key to unlocking continued incremental benefits.

In the International region, we are continuing to take steps to mitigate the effects of uncertainty in the market, but we are seeing encouraging trends in the back half of October, with pricing in the Americas and International starting to show strength. And October will also be our 29th consecutive month of increased dot-com bookings.

With that, I'd like to turn the call over to John to take you through the financial results.

John F. North - *Avis Budget Group, Inc. - Executive VP & CFO*

Thanks, Larry, and good morning, everyone. My comments today discussing changes in revenue per day, pricing and per-unit fleet costs will all refer to changes excluding exchange rate effects. My comments will also focus on our adjusted results, which are reconciled from our GAAP numbers in both our press release and investor presentation.

I'd like to start with an overview of the third quarter for the total company. As Larry mentioned, we had a strong quarter. We finished with a record revenue of approximately $2.8 billion, which is up $19 million from prior year on 2% higher volume, excluding a $44 million currency headwind.

Overall per-unit fleet costs were 6% lower, while vehicle interest expense increased by $5 million. This resulted in our adjusted EBITDA being $471 million for the quarter and $645 million through September. Excluding more than $23 million of currency exchange rate movements through the first 9 months, adjusted EBITDA was $668 million or a 5% improvement from prior year.

Year-to-date, net income and diluted earnings per share is up 5% and 12%, respectively, due to the strong earnings as well as the shares repurchased in the third quarter. We opportunistically took advantage of market volatility and repurchased approximately 2.1 million shares at an average price of $27.46.

Moving to the Americas. We had a record quarter with adjusted EBITDA 3% higher to $321 million. Revenues, excluding exchange rate effects, improved 1%. And rental days improved by more than 3% despite a softer pricing environment contributing to revenue per day being down 1.7%, excluding exchange rate effects from prior year.

However, the majority of our decline in revenue per day was driven by increasing our package delivery business in Budget Truck, the increase in our Zipcar Commuter product and the increase in ride-hail rental business, which are all utilization-accretive and profitable businesses. Each of these had a roughly 30 basis point impact to rate per item or over 90 basis points in total.

As Larry mentioned, the ancillary revenue increase was attributable to our increased focus on ancillary sales, paired with new product offerings as well as our revised rental sale agent incentive program. Our focus on ancillary products and providing customizable product offering packages helped drive revenue per day, showing that our customers prefer optionality and personalization to complete their rental experience. The e-Toll product that we have been testing in Texas has seen favorable responses since launch, and we look forward to rolling the product out to new markets before the end of the year.

Per-unit fleet costs decreased by 9% as we continue to utilize alternative disposition channels to take advantage of stable residual values. We continue to be focused on the growth of our alternative disposition channels, particularly our direct-to-consumer sales, which have grown 136%

in 2019 from the prior year. Third quarter U.S. risk vehicle dispositions grew 8% from prior year, topping 48,000 in the quarter, with a record 70% of the disposals occurring through alternative channels.

We now have 13 operating car sales locations, including our newest in Victorville, California, and we'll continue to benefit from the significant opportunity to improve fleet costs through further success in this initiative. Each vehicle we dispose through alternative channels saves us hundreds of dollars in disposal costs. And each vehicle we sell direct to consumer can generate more than $1,000 of additional benefit.

We believe our strategy to accelerate the de-fleeting process beat our competitors to market and helped us to take advantage of stable residual values over the summer. As a result, we have disposed of approximately 85% of the vehicles we had planned to sell in 2019. As we anticipated, vehicle interest continues to be a headwind, increasing due to rates by $5 million in the quarter. Although floating rates have come down, we expect vehicle interest to continue to be a headwind through the remainder due to our significant portion of fixed-rate debt.

In our International business, we continue to focus on revenue per day, which increased $0.05 from prior year, excluding exchange rate effects, our first positive increase in 11 quarters. Currency continues to be the largest impact on reported revenue, with $42 million in the quarter. However, excluding currency exchange rate effects, revenue was down less than 1%, even with the airline disruptions and travel agency bankruptcy Larry mentioned earlier.

Per-unit fleet costs were up 1% in the quarter driven by Brexit-related inflation in the U.K. and the Apex fleet refresh in Australia and New Zealand. Traditionally, the European market has had a higher program fleet mix that we have begun to shift toward a heavier risk-based fleet as we take advantage of select international markets with stronger used car demand.

Third quarter EBITDA of $178 million was consistent with prior year in constant currency, expanding margin to more than 19%, a 13 basis point improvement from prior year, in part due to our cost reduction program as well as acquisitions and divestitures in the last year. The commercial segment in Europe showed positive signs, with volume up nearly 10%.

Our adjusted free cash flow was $116 million inflow through September 30 compared to a $289 million inflow last year, as the timing benefiting vehicle programs we saw in the prior year-end reversed and a temporary investment in vehicle programs in the quarter caused vehicle programs to be approximately a $139 million outflow compared to a $3 million outflow in the prior year. We still anticipate cash flow to be within our guidance at year-end. Our financial position remains strong, with approximately $3.9 billion of available liquidity. This comprised ending the quarter with $615 million of cash, having $853 million of unused capacity in our revolving credit facility, plus an additional $2.4 billion of availability under our vehicle programs.

We remain committed to keeping our corporate net leverage ratio in the range of 3 to 4x, with a preference over time for being in the lower half of that range. In October, we redeemed $75 million of the $275 million notes outstanding in 2023 as we continue to execute our capital allocation plan accordingly. Ultimately, our net corporate leverage was 3.6x and remains within our targeted range. It is also approximately 2/10 lower than the 3.8x it was, both at the same time last year and last quarter.

During the quarter, we also repurchased $59 million of shares outstanding. We directed capital from our share buyback program to take advantage of what we thought was a depressed share price, returning more value to our shareholders. We will continue to take an aggressive approach to share repurchases whenever we view it as an attractive opportunity. Overall, we remain committed to allocate capital to drive the highest return possible.

In the third quarter, we had an effective tax rate of 42% in comparison to our prior year rate of 38% primarily due to foreign taxes on our international operations, state taxes and a onetime net tax effect from the sale of equity investment in our Chinese operation. We are implementing tax planning strategies that we believe will result in a lower effective tax rate, in line with the guidance we provided for 2019.

Our free cash flow was affected by higher cash tax payments in the quarter due to accelerated state income tax payments and impacts associated with tax reform. We anticipate a temporary increase in cash tax payments in future years as a result of the timing differences due to the repeal of like-kind exchange until cumulative accelerated depreciation deductions match the ongoing level of fleet additions.

As we enter the fourth quarter, we have narrowed and changed the ranges of our 2019 guidance based on our expectations for the remainder of the year. We expect to generate between $9 billion and $9.2 billion of revenue, which has been impacted by $175 million currency exchange headwind; and for adjusted EBITDA to be between $750 million and $800 million, including $14 million in unanticipated currency headwinds. Please see our earnings release for definitions and the full list of assumptions.

As we look to the future, we remain focused on further developing and leveraging our family of brands across our global footprint to provide value to our customers and to create value for our shareholders. Our ambitious track record is focused on the future state of the company, industry and the numerous opportunities we have in front of us to continue our rich history as a mobility leader.

In summary, the Americas had record third quarter results. And although the international market remains competitive, we are seeing signs of pricing improvements while continuing to get more efficient and target strategic growth opportunities. Underpinning all of this, we are investing in new technologies, mobility solutions and ways to continue to delight our customers.

And with that, Larry and I'd be happy to take some questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question today is coming from John Healy from Northcoast Research.

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

Wanted to ask you guys just to dive in a little bit more into the expectations for the Americas as it relates to fourth quarter pricing. I know you guys are still saying 0 to 1% for the year. But given some of the items that you called out, with the mobility in the truck business, should we expect those types of headwinds to persist? I'm sure it's good business, but should we expect those headwinds to kind of weigh RPD down for the next few quarters? And if that's the case, is the math of kind of low to mid-single digit kind of traditional RPD what you're expecting for the fourth quarter to kind of get to that range? I just was hoping to just kind of see if that math framework seemed reasonable.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

This is Larry. So what I would say is that, yes, as we continue to grow the package delivery business and as we continue to grow our Zipcar Commuter business as well as, obviously, we're going to be growing our car hail business, all very profitable businesses. They are utilization-accretive. They're the right decision to make, but they will have a drag ongoing on rate per day.

And I would say, as we turn the corner into the fourth quarter, without giving specifics on exact numbers, we're pretty pleased with how we're seeing bookings right now come through. October started off a little lower on pricing than what we wanted. But as the fleets tightened down in the industry coming out of the summer, then we saw that change in the back half of October.

As we take a look at bookings coming through for the remainder of the year, particularly around the holidays, both volume and rate look pretty good. So I think just you have to kind of work through the balance of those. But to your point that we will have a drag on RPD on these products that we are working very hard to expand, once again for the right decisions, for the right profitability decisions.

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

Understood. Makes sense. And then just a follow-up question. Was hoping to see if there was any sort of qualitative update you guys could give us about the CEO succession planning and kind of where you guys are at with that opportunity.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes, sure. What I'd say is the Board is performing a very diligent and deliberate search to find the very best candidates they can to make sure we stay on course to continue our leadership position in mobility. The good news is we have a very strong strategy in place. And fortunately, we have a very strong, great management team that's out there executing every single day, and none of that will change. So we'll update everyone as soon as decisions have been made, but the process just continues on.

Operator

Our next question is coming from Brian Johnson from Barclays.

Brian Arthur Johnson - *Barclays Bank PLC, Research Division - MD & Senior Equity Analyst*

Hopefully we'll have you on the call for at least a couple more, Larry, but if not, pleasure to have worked with you.

I want to drill down on the 2 key financial drivers in the Americas and maybe try to get some waterfall-like color on each fleet cost as well as pricing. So in fleet costs, could you maybe separate out the positive impact in terms of dollars per month from the retail and alternative disposal channel from what appeared to be some negative headwinds in the auction lanes?

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Brian -- and by the way, this is my last call, so there won't be any more calls for me after this. But let me just talk a little bit about fleet costs. Obviously, we've had a number of initiatives in this area. So if you put just residual value strength aside for a second, just take a look at the initiatives that we've had in place. We've been working a number of initiatives that really first start with data analytics, and we have enhanced and strengthened the data analytics team.

We've got a lot of data scientists who are really using data to really understand how we're buying fleet, makes and models, trim levels, colors; where we end fleet; where we run the vehicles; where we de-fleet; what time of the year we de-fleet them; how many miles we de-fleet them with. Not every car is the same as the next.

And so through that data analytics capability, and we are looking at tons of data, both internal trends as well external data, to really get a good handle over how we acquire and how we dispose of the fleet. Then you couple that with the fact that we're growing our alternative channels.

Our alternative channels are up 8 points, so we're up to 70% now that are sold through the alternative channels. So just in that area alone, we still have a lot of head -- a lot of runway to go to continue growing that number. But what's even more important is the mix of alternative channels that we can continue to grow as well.

So our direct-to-consumer is up quite a bit in the quarter, but we have a long runway to go. I think we're up 136% in the number of cars that were sold direct to consumers in the quarter, but we have a lot of cars yet to move into that channel. And so we're up to 13 retail locations, and we're continuing to improve our Ultimate Test Drive, which is our online platform selling cars. And -- but we're going to continue to grow that channel.

So when you look at what you get for the car, it's hard to kind of dice out, well, how much of the gain on sale, for example, was due to this versus this. But the residual value market through the summer continued to be strong.

And as you go into the fourth quarter, I think what you're seeing this fourth quarter is kind of the normal downtick that you would see in pricing that we didn't really see the last couple of years. A couple of years ago, we had the hurricanes. Last year, we had I think it was really kind of started with the threat of tariffs. And we had some other events that caused residual values to be stronger in the fourth quarter than what you'd normally anticipate.

I think this year, we're kind of back to a normal downtick, but nothing to be concerned about. In fact, we've already sold over 85% of our fleet that we need to sell for this year, so we can be pretty choosy and picky as we go into the fourth quarter about what we sell and where we sell it. So there's just been -- these last few years just a great deal of science and data and analytics that have gone into our purchasing and disposal decisions that are just helping us maximize these opportunities.

Brian Arthur Johnson - *Barclays Bank PLC, Research Division - MD & Senior Equity Analyst*

Okay. But in terms of the year-over-year change in monthly depreciation and, well, down $3 despite some potential weakening in the residual markets. You can't -- excuse me, down $30. You can't really break it out of $10 of optimization, $10 of channel, however it is. And are you even tracking that internally, just to judge how your -- efforts you're doing in taking out the noise of the outside market?

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes. We're tracking it internally. I don't want to go through it on this call. But of course, as we take a look at how we're performing in each of the initiatives that I walked us -- that I just walked you through, we are kind of tracking those metrics as close as we possibly can. But once again, we're really pretty excited in this area, and we just think that there's more opportunity there than what we've been able to harvest so far.

Brian Arthur Johnson - *Barclays Bank PLC, Research Division - MD & Senior Equity Analyst*

Okay. And second place to try to get color on is within the Americas RPD. Is there any way you could break out the impact of, for example, you're beginning to grow with TNC fleets, shifts in mix and channel from just pricing pressures due to what sounded like due to lack of recalls? Recalls are sometimes bad. Well, seems like recalls are always bad. If they happen, they're bad. If they don't happen, they're bad, but the impact of that on pricing.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes. I think, as we said, that if you take a look at the 3 businesses that we're talking about that we've been growing that impact RPD, so the ride-hail business that we continue to grow, that had about 30 basis points impact; the package delivery business that we continue to grow, that's had about a 30% basis impact; and then also the commuter product and Zipcar, also around 30 basis points. So over 90 basis points of the drop were due to kind of those 3 products that we've been working pretty hard to continue to grow.

Operator

(Operator Instructions) Our next question is coming from Adam Jonas from Morgan Stanley.

Adam Michael Jonas - *Morgan Stanley, Research Division - MD*

I do have one question, one follow-up. Larry, first, I want to kind of offer thanks and farewell, given it's your last call. I think you've done some really very innovative and even some extraordinary things during a challenging -- during some challenges to your business. And I just want to say well done, and good luck to your next endeavor.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Thanks, Adam, appreciate that.

Adam Michael Jonas - *Morgan Stanley, Research Division - MD*

And yes, I know -- and we've had disagreements and things, but I think you -- we've always handled -- you've always been really, really classy and very enlightening, so I want to thank you for that.

All right. So how -- out of the 450, I guess, on average, over the year, I guess you have 450,000 cars in the North American fleet, give or take. Roughly, what percentage -- or maybe the individual unit count, what percentage are pure electric vehicles?

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes. We don't really...

Adam Michael Jonas - *Morgan Stanley, Research Division - MD*

I know it's low, and everyone's is low. I was just curious if you had a number.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes. We don't really run electric vehicles at this point in the U.S. We do internationally, but in the U.S. fleet, no, we do not. If we have any -- we basically have some hybrid vehicles, but we do not have any pure electric vehicles.

Adam Michael Jonas - *Morgan Stanley, Research Division - MD*

Yes. Okay. And you're not the only ones, I'm not just calling you out on that. I was just curious if there was -- if there's anything. My follow-up, Larry, is does Enterprise, to your knowledge, rent to TNC companies right now? And I'm just curious why not? Because I -- I'm not aware if they -- I don't think they do. But I think they tried it once and then pulled out, and I'm just kind of curious what do you know they don't kind of thing.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Not to my knowledge. You'd have to ask them if they're renting any to them. I mean not to my knowledge they are. But I think the way I would answer that question is, as we've worked through the partnership with Lyft and now with Uber, we've approached it very differently, I think, than maybe others have in the past. Number one, we rent only by the week, and we rent only connected vehicles. So we manage the fleet, we manage the usage of the fleet and we manage the miles on the fleet. And if we see anything in those areas that we don't like, then we don't re-rent at the end of the week. So our biggest exposure to any one driver is 1 week.

So -- and what we -- what I can say is as we -- we still have very -- only about 4,000 cars in the fleet at this point, but we're going to probably be about 5,500 cars by the end of the year. And we'll continue to grow that next year. What I can say, as we watch the results of this, that there's really been nothing that's been too surprising for us. And so far, we like what we see.

We're integrated into the Lyft app, so the driver experience is good. We're getting a good selection of drivers coming through. So -- and we have the flexibility to change the arrangements around the deal. So if it looks like pricing needs to be improved, we have the flexibility to do that within the contract. So, so far, so good, and nothing that we're seeing in there that really tells us that we shouldn't continue to pursue this product.

Adam Michael Jonas - *Morgan Stanley, Research Division - MD*

Thanks, Larry, good luck.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Thanks, Adam.

Operator

Our next question today is coming from Ryan Brinkman from JPMorgan.

Ryan J. Brinkman - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

Can you just help further unpack the drivers of the 2% lower revenue per day in the Americas segment? How much was due to, I guess, underlying or pure pricing relative to how much was due to the ancillary revenue or changes in to the Budget package delivery or Zipcar Commuter?

And then as you think of the diverse of the underlying pricing, the demand environment, industry-wide utilization, et cetera, how do you see these factors tracking going forward relative to in 3Q?

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes. So once again, we did have some pricing weakness just in the regular business in the quarter. But as I said that we've kind of turned the corner on that now that we're into the fourth quarter. Volume's looking good, and pricing has improved and is looking much stronger, and looks like it'll be positive for the quarter. So that's one piece.

And then the other pieces are the pieces I just talked about. So they've had almost 1 point impact on price. And we will continue to grow in those 3 areas as we go forward. Now at some point, we'll overlap a lot of the growth and so over time that will continue -- that will start to kind of moderate. But for a while, we are in a trajectory of growth in those 3 areas. We'll probably continue to feel that impact going forward.

But I would say that the pricing on just the core rental car business in the quarter, there was probably a bit too much fleet. We just didn't see the tightness in the quarter that we had hoped to see. But then I think it was due to the fact that recalls for -- at least, for us, were down over 70% in the third quarter this year versus last year. The number of weather events that occur in the quarter that causes cars to be sucked up just did not happen this year versus last year. And so -- and in fact, insurance claims as well are just down when you take a look year-over-year. So the number of cars that are probably going into the replacement business is down. It's certainly down for us.

So I think those are kind of the key movements that were happening in the second quarter. And then as you turn into the third quarter, a lot of that has kind of gone away as fleets have tightened down, and we're starting to see kind of more the normal length of rental restrictions by the industry being put in place kind of city by city.

Ryan J. Brinkman - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

Okay. That's helpful. And then, lastly, can you just sort of help us dimension what the trend in fleet costs could be in 2020, in the event that used car prices track sequentially flat from here? And maybe that's not your assumption, but just would be great if you could try to separate the tailwind to 2019 earnings from maybe the lower normal course perspective rate of depreciation that should continue at this level of car prices versus, separately, the sort of more onetime gains you could have recorded from unexpectedly higher disposal prices.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes. I won't really comment on 2020 fleet costs at this point because we're not really ready to yet from the perspective of the buy. But I will point out the fact that what we will continue to see is the further development of our alternative channels, so we're at 70% now. That will continue to grow next year. Our direct to consumer, where we see our largest benefit, will continue to grow as our -- as the locations that we're selling cars through continue to mature, and as we open new locations next year. So we have a lot of runway still ahead of us as it relates to the data science behind the decisions, behind the buy and behind the sell as well as the methods in which we're selling. We are still -- we have a lot of maturity left to go in those areas. And so I will -- I would say we continue to see benefits coming from those as we go through 2020.

Right now, as far as residual values for next year, we're still looking at the data. And a lot of data hasn't really come out yet about expectations, external data around expectations for 2020. We're obviously modeling our own trends of how we've been performing, and we continue to perform very, very well in this area. So we'll balance all those as we get closer to the end of the year, and as we put our budget to bed. But it's -- overall, it's probably just a bit too soon to talk about overall fleet costs for next year.

Operator

Your next question is coming from Michael Millman from Millman Research Associates.

Michael Millman - *Millman Research Associates - Research Analyst*

I don't think you've talked very much about the corporate market. So what are you seeing in the corporate market? What did you see in the corporate market in the third quarter? And what's your expectation? Also, what tax rate should be, which should we be assuming for next year? And sort of related to that is were we, The Street, just simply weigh off on the third quarter to start with, and that was exacerbated by the weakness?

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Sure, Michael. I'll take the first one, then John can take the second question. So good news on corporate market is that we're now back into a volume growth period of time here. So we've had now a number of months where we've been able to improve volume on our corporate business in the U.S. And corporate volume in EMEA has been extremely strong. It was up 10 points this past quarter.

So we've kind of turned the corner on volume. Now we just have to work on rate. And so rate continues to be under pressure. The small business kind of moves along with the leisure rate. So as fleets tighten up, and we get leisure rate improvements, we'll see improvements in small business rate per day.

The mid-market and large commercials continues to be extremely competitive when those get renewed. So I'm hoping, at some point, we can turn the corner on pricing on those contracts. But the good news is that we're seeing commercial volumes strengthen, and we're seeing volume improvements kind of month after month now in both regions.

John F. North - *Avis Budget Group, Inc. - Executive VP & CFO*

Michael, this is John. As it pertains to taxes, I think, without getting too esoteric on the call, the short answer is there's often fluctuation from quarter-to-quarter. If you look at our guidance for the full year, which is in the press release, you can see that we expect the tax rate to come down from the sort of 40 percentage rate you saw in the third quarter. And that should help you in terms of what we think the full year is going to look like, which is basically unchanged.

And we mentioned in the prepared section that we're going to take some actions in the fourth quarter that we think are going to -- they're going to result in a lower tax rate in that quarter and help take the year kind of down into the range we expect. In terms of 2020, I think you can expect something similar at this point, based on what you're seeing for the full year '19. And we'll continue to update you on our outlook and try to refine that, particularly on a quarter-to-quarter basis as we get into early next year and have a bit more visibility there.

Operator

Our next question is coming from Chris Woronka from Deutsche Bank.

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

Larry, congratulations on a really good run at the company and best of luck in the future.

First question was just on the truck rentals. I know that was an area that I think a lot of years ago was kind of left for dead, and now there's a new delivery opportunity. Does that make you want to expand your fleet there? And maybe just a quick overview of the economics of how that might play out if you decided to do that.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes, we -- Chris, thank you. This is Larry. We went through a kind of a rightsizing initiative with Budget Truck and really kind of changed the areas that we were focusing on. So we brought down some segments that weren't just as profitable as we had hoped them to be. We reduced our truck fleet to accommodate for that, and we really started focusing on more of a round-trip model, more around local rentals and a lot more around package delivery.

And we've been then growing the fleet in accordance with the appropriate fleet for that kind of business. So we're seeing a lot more cargo vans and things like that, as you would expect as package delivery business, as that segment continues to grow.

So we've spent a few years kind of just really digging deep into Budget Truck and understanding where we think the profitability opportunities really are there, and getting the fleet mix and number of vehicles correct. And then from there, as we grow the package delivery business, we'll grow the fleet and the type of fleet accordingly with it. And those are longer length rentals, and so they impact the rate per day, but they're much more profitable rentals.

So I think the decisions that the truck team has taken to really rightsize that business has been the right ones to do. And I'm pretty proud of how they've really reengineered that business. So we'll continue down that path and grow appropriately to make sure we keep the utilization of our fleet up, and that we buy the right mix of fleet and we go after the right mix of the segments of that business.

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

Okay. Very good. And the follow-up is kind of thinking about the numerous investments in technology you've made over the years, and I know some of them are more kind of tangible and visible than others. But as we look out, and without asking for a specific number, but is there a point where kind of that DOE line inflects and you actually get -- this becomes a less labor-intensive business and you actually get savings there kind of irrespective of whatever volume pricing might be?

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Yes. What I would say is, over these last few years, we've been investing in modernizing all of our core systems in the business, so we had to start there. So if you want to really be able to offer new use cases and connect in a seamless way with partners in the future in mobility, we really had to modernize all of our core systems. So we did that.

We've modernized our rental reservation systems, our revenue management systems, our fleet systems, our websites, our mobile apps, our HR systems, and then mobile and now we're modernizing our accounting systems. And then we started investing in other technologies around replatforming the Zipcar and also connected car fleet, and now we're building our next-generation platform to be able to manage mobility in a different way and to be able to manage connected fleet data in a different way.

And so when you get into connected car and you start looking at the benefits, and we've been seeing these in Kansas City as we've been running the mobility lab. And you start to see the benefits of data and how data can instruct you to manage the fleet in a different way and more efficient way that you could never possibly do without the data and just depending on people to execute, so we're now starting to see the benefits of that.

We're seeing the benefits come through in gas collection as we continue to increase the penetration of gas that's being recorded. Gas profits are being recorded as it relates to the connected car transaction. And just how you manage your fleet and how your employees work with the fleet through data is very different than what we've been able to do without connected fleet.

And then as you take a look at new use cases, where connected car can allow a more seamless interaction with consumers to where you can really start driving more self-service, which we've been piloting on the rental side and take out some of the costs that's in between the customer and the car, that's the opportunity going forward as well.

So the technology kind of building up and modernizing the whole -- all of the systems to be able to be ready for a kind of a new world of mobility and connecting the fleet allows us to really look at the opportunities around how we deliver the product to the customer in a lower cost way. And we're starting to see those benefits come through.

Operator

Our next question is coming from Derek Glynn from Consumer Edge Research.

Derek J. Glynn - *Consumer Edge Research, LLC - Analyst*

Just on international, how are you thinking about that price and volume trade-off? And then can you provide some more color on what you're seeing from a competitive standpoint there, particularly from some of the third-tier players?

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Sure, Derek. This is Larry. What I would say on international is that we've gone down a path now of modernizing our volume growth a little bit and really trying to push for rate. It's extremely competitive market place. This summer was really competitive. It's under a lot of economic pressures. The Brexit delay continues to weigh heavy on the region.

So what we've really been working on is how do we turn the corner on this rate per day issue that we've been having the last -- as we said earlier, in the last 11 quarters, and start to turn that positive, which we were able to do during the third quarter. Now we've been very picky about the volume that we've taken. And we've actually -- part of our volume issue in third quarter was self-inflicted, where we actually got out of some low-yielding business that we decided just wasn't in our best interest to continue to pursue.

So as we worked our way out of that, that did impact volume in the third quarter, but that's done now. And we hope to kind of grow the 2 in balance a little bit better and balanced than what we have been in the past. So investments in DFP and other things like that help us to look at that differently, to help us to find us those opportunities. And based on how reservations are looking so far for this quarter, I'm pretty pleased with what we're seeing so far on the rate side for the international team.

But the competitive set is difficult. There are still a lot of third-tier players that are in the marketplace, and those don't seem to be going away anytime soon. So we just have to kind of find our way to manage through it. Thank god we've got very good partnership relationships, long-standing partnerships with our airlines and very good relationships with our corporate accounts, so we continue to work that business and continue to grow that business. So we just have to keep really focused on striking that right balance and not getting too far out ahead of volume and end up losing it out on price. That's not what we're there for. We really want to grow the price side of the business and have the right balance going forward.

Derek J. Glynn - *Consumer Edge Research, LLC - Analyst*

Okay, got it. That's helpful. And in the script, I think you mentioned shifting to a higher risk-based fleet in certain international markets. Are OEMs less willing to do program vehicles there? Or are you trying to be more opportunistic with respect to used values? Just any additional comments there will be helpful.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Just as we've learned how to manage a greater risk fleet, I think that we have opportunities internationally, like we have in North America. Now will we ever be a risk fleet size in international that we are in North America? I don't think so because the OEMs -- the balance of what they sell is not that. So but there are opportunities to grow our risk fleet, but we're doing it very specifically in markets where we feel like we've got the capabilities to remarket the cars, and where we feel like the remarketing -- the marketplace for residual values are in the right place.

So we're growing it slowly. We will increase our risk fleet for 2020 over 2019. We grew '19 over '18. So each year, we will just kind of methodically keep working our way up, but we want to make sure that we've got the right capability and the bandwidth, the right methods to remarket our vehicles. So we will continue to increase that, but once again, it won't be the scale as it is in the U.S. because the OEMs just don't sell that number of risk cars to the industry.

Derek J. Glynn - *Consumer Edge Research, LLC - Analyst*

Larry, I wish you the best of luck as well.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Thank you very much.

Operator

Our next question is from John Healy from Northcoast Research.

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

Larry, I just wanted to ask a follow-up question regarding just the calendar for the holidays this year. Just as you look at the late Thanksgiving and I think Christmas falling in the middle of the week, does that typically help the business? Or does that hurt the business? Just any color there.

And then, again, it's been a pleasure working with you the last few years, and I wish you all the best, sir.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Thanks, John. Yes, it's interesting, the calendar of the holidays. It's amazing how -- what it really changes is the booking pattern. So Christmas is just 1 day later this year. It kind of still falls in the middle of the week. But just that 1 day shift does change, a, how the bookings come through, and then the behavior of consumers around where they put their holidays. So there will be an opportunity for hopefully a kind of a Christmas Eve, a kind of a week before Christmas Eve leading over through Christmas. And you hope that there's the Christmas Eve that leads over New Year's.

I think, though, when you take a look at it shifting a day, that you'll see more of the vacations move to the back half of December than to the week prior to Christmas, which will put some of that rental activity into January as it checks in versus checking in, in December. And so that you have to really watch.

So what we do when these days shift like this is we go back to the -- we go back to the year where the day fell the same day of the week, and then we kind of model how those booking trends occurred coming into it, and then how the activity actually occurred through the holiday as you go from Christmas into New Year's. And then we try to apply those trends and any other changes that we think may have happened since the holiday fell in that period of time.

So there is a lot of kind of science that goes into it and trending models that go into it. But 1 day shift can actually change very significantly the booking patterns of how people book their holidays over the Christmas period. So we're watching that very closely, and as we are in international as well.

Operator

Thank you. We've reached the end of our question-and-answer session. I'd like to turn the floor back over to Larry for any further or closing comments.

Larry D. De Shon - *Avis Budget Group, Inc. - CEO, President, COO & Director*

Thank you very much. So just to summarize, we had a pretty strong third quarter with record earnings in the Americas and positive price in the international region. Year-to-date, we've generated $645 million in adjusted EBITDA, approximately 1% higher than prior year despite the numerous challenges we've faced in the international region. And the strategic focus on ancillary revenues and a shift in rentals to our direct website channel will continue to provide positive returns in the Americas.

So we've made significant progress on key strategic initiatives like our partnerships, connected car and direct-to-consumer sales in the third quarter. And we'll remain focused on improving our profitability as we go through the balance of the year and next year.

So for those of you that I don't talk to between now and end of the year, I'll stay on here until the end of the year. But if I don't catch up with you, thank you very much. It's been great working with you. And we'll see you, hopefully, again. Thanks, guys. Have a good day.

Operator

Thank you. That does conclude today's teleconference. You may disconnect your line at this time, and have a wonderful day. We thank you for your participation today.
