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MANAGEMENT DISCUSSION SECTION

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

Neal H. Goldner, Vice President-Investor Relations

Thank you, Tanya. Good morning, everyone, and thank you for joining us. On the call with me are Ron Nelson, our Chairman and Chief Executive Officer; and David Wyshner, our Senior Executive Vice President and Chief Financial Officer.

Before we discuss our second quarter results, I would like to remind everyone that the company will be making statements about its future results and expectations, which constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act. Such statements are based on current expectations and the current economic environment, and are inherently subject to economic, competitive, and other uncertainties and contingencies beyond the control of management.

You should be cautioned that these statements are not guarantees of future performance. Actual results may differ from those expressed or implied in the forward-looking statements. Important assumptions and other important factors that could cause actual results to differ materially from those in the forward-looking statements are specified in our earnings release, which was issued last night, our Form 10-K, and other SEC filings.

If you did not receive a copy of our press release, it is available on our website at ir.avisbudgetgroup.com. We've provided slides to accompany this morning's conference call, which can be accessed on our website as well. Also, certain non-GAAP financial measures will be discussed in this call and these measures are reconciled to the GAAP numbers in our press release.

Now, I'd like to turn the call over to Avis Budget Group's Chairman and Chief Executive Officer, Ron Nelson.

Ronald L. Nelson, Chairman, President, Chief Executive Officer & COO

Thanks, Neal, and good morning. While our second quarter didn't come in exactly as we expected, our results do reflect progress on a number of important fronts; growing our revenues, controlling costs and delivering on our strategic initiatives.

In North America, car rental volume and pricing both increased as we continued to take price increases where and when we could. In Europe, we continued to grow our Budget brand at a rapid pace. Our performance excellence and customer led initiatives delivered significant benefits, strengthening our brands and our bottom line. We made substantial progress in the integration of Zipcar. We acquired Payless Car Rental in July, providing us with a meaningful position in the deep value segment of our industry. And last night, we announced a $200 million share repurchase authorization, providing us with an efficient avenue to return cash to our shareholders.

All of these along with a number of other important initiatives resulted in adjusted EBITDA of $272 million and earnings of $0.58 per share excluding items in the first half, making it one of our best first halves ever. Of course, we faced impossible year-over-year comparisons due to the low level of fleet costs in North America last year. And you can see this in how our results stacked up this quarter.

In fact, the normalization of residual values in North America had more of an impact in Q2 than we had expected. And when combined with a somewhat surprising soft operating environment in Australia, this had an impact on full-year guidance. To put a somewhat finer point on it, these two issues along with the continuing soft economy in Europe are the key near-term challenges that caused us to narrow our guidance to the lower half of the range.

We're nonetheless working hard to address these and at the same time looking to grow our earnings through higher pricing, particularly in North America. So let me spend some time on each of these topics beginning with fleet costs.

In each of 2011 and 2012, our industry benefited from anomalous and market-driven spikes in used car prices that drove temporary imbalances between the supply and demand of late model used cars. Our 2013 business plan assumed that such spikes would not recur and that our fleet costs would therefore normalize over the course of the year. The first quarter was consistent with those expectations, but we were surprised to see the market decline as much as it did in April and May before leveling off in June. This caused our North America per unit fleet costs to increase 60% in the second quarter, 10 points more than we had anticipated at the time of our last earnings call. This impacted our North American fleet costs by roughly $20 million in the second quarter.

We're actively working to mitigate the effects of changes in residual values. We are using our fleet optimization system to help us revise our tactical plans for which vehicles to sell, where and when. We're increasing our use of alternative distribution channels to optimize fleet costs. In particular, we've expanded our direct-to-consumer partnership with AutoNation to include New Jersey, Georgia and Illinois with additional states expected to be launched by the end of the year. We've expanded our pilot programs to sell cars directly to dealers with sales people now in Texas, Illinois and Florida and a new proprietary direct-to-dealer website.

We continued to increase our use of other online disposition channels to maximize residual values and most importantly, we continue to aggressively pursue price increases to mitigate the impact of higher fleet costs.

One of the highlights of the second quarter was the continuation of year-over-year price increases we saw in the first quarter. Realized pricing in North America increased almost to 0.5% despite the shift of some relatively high-priced Easter business into March this year. Pricing in the U.S. was up 2% in the quarter as a whole, and 3% for May and June combined, which obviously weren't impacted by the shift of Easter into Q1 this year.

We continued to be aggressive in our approach to pricing. We instituted price increases multiple times over the course of the second quarter to help offset the fleet costs headwinds we knew we would be facing. We also continued to benefit from our strategic initiatives to grow volume in the most profitable segments, with each of our key target segments growing faster than our overall volume growth. With respect to commercial pricing, we maintained a more aggressive stance in our contract negotiations and are seeing some early returns. Pricing trends for contract renewals improved from the first quarter to the second, with more contracts renewed at flat or increased pricing than we have experienced in a while.

Given the length of the commercial selling cycle, this initiative is going to take time, but we're not going to be satisfied until our pricing on renewals starts to rise. Frankly, after three years of declining renewal rates facilitated by lower fleet costs, this is an industry-wide issue as the impact of declining residual values affects all of us uniformly.

On the leisure side, our pricing in North America was up 4% in the second quarter, slightly more in the U.S. alone. Our focus on more profitable channels and transactions contributed to this number. I'll talk about how the year-over-year pricing increase we achieved in second quarter bodes well for the summer in a moment. Focusing on North America though, in addition to the positive pricing we achieved, our North America segment had other bright spots in the quarter. Overall revenue grew 9%, or 3% excluding Zipcar, with our strategic initiatives providing benefits.

International inbound revenue increased 5%, small business revenue grew 6%, revenue from our higher margin specialty and premium vehicles increased more than 15%, and sales of ancillary products and services grow in line with volume. We also saw continued growth in our local market operations with both our Avis and Budget brands reporting good increases.

Local market revenue increased 6%, as we continued to focus on growing higher price to general use business. And our ability to form and maintain mutually beneficial relationships with travel and non-travel related marketing partners is becoming increasingly valuable to us. We announced the acquisition of Payless in July, giving us a recognized brand position in the faster growing deep value segment of the car rental market and enabling us to better distinguish and support Budget's mid-tier value brand positioning. The Payless acquisition is also expected to provide us with further flexibility to benefit from fleet management as this brand can prosper using vehicles that are slightly older than our core Avis and Budget fleet.

Overtime, we expect to be able to satisfy all of Payless' fleet needs by cascading vehicles from Avis and Budget, driving further efficiencies. When fully integrated, we expect to own Payless at slightly over three times EBITDA.

Moving to international, revenue in our international segment increased 5% in the quarter, and 3% in organic constant currency terms. Let me start with our Latin America/Asia Pacific region. Rental volume in Latin America/Asia Pacific increased 9% year-over-year, primarily due to the acquisition of Apex. Pricing in our Latin America/Asia Pacific region, however, was weak, with price declining 4% in the second quarter even excluding the effects of foreign exchange and the acquisition of Apex.

The weakness is primarily related to Australia where significant reductions in government spending and economic weakness notably in the mining sector have reduced demand causing industry-wide over fleeting during the usually softer trough winter months. We've seen significant rate reductions in the leisure market as competitors attempt to utilize their excess fleet.

We're hopeful that the Australian market will stabilize towards the end of the year and into early 2014 during the peak summer demand period there. In the meantime, we're taking steps to mitigate the impact including an increased focus on ancillary revenue growth along with stringent cost controls and fleet rationalization. What we're not going to do, however, is cede our strong position in this market despite the current pricing pressures.

Moving to EMEA. The economic environment in Europe remains tough, but we saw some encouraging signs in our results at least during the second quarter. Our volume increased year-over-year in France, Italy, Spain and the U.K., and our initiative to expand our presence in the value segment of the European market continued to bear fruit with Budget volumes up over 50% across Europe.

Avis volume also increased in the quarter, the first quarterly increase since 2011, with both commercial and leisure rental days increasing. The overall increase in Avis volume was about 0.5%, but excluding the impact of our decision to walk away from some unprofitable insurance replacement business, it was up 3%. Pricing in Europe declined slightly due solely to the faster growth of Budget as both the Avis and Budget brands reported positive year-over-year constant currency pricing in the quarter. These increases reflect our strategy of pricing to realize the appropriate positioning that our brands merit in the marketplace, as well as shrinking our book of low margin business, primarily in the U.K.

We took important steps in Europe during the quarter that we believe will enable us to hit our goal of generating an incremental $55 million to $75 million in annual synergies by 2015. These include significant progress in our initiative to dual brand locations in Spain and Germany, with remaining countries expected to be completed later this year. The continued successful push on ancillary sales, together with product introductions such as roadside safety net, and a new refueling service in France which is now being rolled out to all the other European countries, and a drive on improving vehicle utilization, partly by achieving a substantial reduction in out-of-service vehicles, resulting in more cars being available to rent without a commensurate increase in overall fleet.

Lastly, before turning to our outlook, I want to talk about the strides we made at Zipcar to capture the $50 million to $70 million in synergies we continue to believe are achievable within the next two years. We have increased Zipcar's North American fleet by 15%, enabling more members to get wheels when they want them. We are adding Zipcars to existing Avis Budget locations in our largest urban markets, increasing the number of places where Zipcars are available.

We continue to grow our membership base, which totaled more than 818,000 at quarter end, up 12% year-over-year. We started offering Zipcars at 19 airports since we closed the acquisition in March, with further expansion planned for this year.

We've taken steps to enable Zipcar to capture demand for other rental occasions such as multi-day and weekly rentals, enabling us to satisfy more of Zipsters' mobility needs, and we're about to begin testing one-way rentals, a benefit Zipcar currently doesn't offer its members.

Our efforts are having a positive impact as evidenced by the 10% year-over-year growth in revenue we experienced in the second quarter, the growth in membership and the improved member satisfaction scores. Meanwhile, we continue to make progress in reducing Zipcar's cost base and integrating our respective fleets, which David will discuss in a few minutes.

Moving beyond the second quarter, the headlines are residual values in North America stabilized over the course of July and actually ticked up a little heading into August. We expect volume trends to be positive in the second half of the year as our growth initiatives continue to deliver and airline capacity begins to increase.

We are seeing volume pressure from the effects of the sequester on government spending and from our decision to move away from certain opaque business, but gains in the other more profitable parts of our business are offsetting these challenges.

We recently signed an exclusive multi-year agreement with AARP, giving us the opportunity to promote Avis, Budget and Budget Truck to AARP's base of more than 37 million members, and we're already seeing some early benefits from this relationship.

We're continuing to push for pricing wherever we can. Average rate per day was up 1% in July, close to 1.5% in the U.S., and the reservations we're holding suggest August will be similar, which is encouraging. We'll maintain our focus on the fastest growing and most profitable segments, particularly international inbound, small-business, specialty and premium car classes, and general use, off-airport rentals. As a result, we currently expect that Q3 will be the third consecutive quarter in which we report year-over-year price increases in North America.

In our international segment, we continue to expect our rental volumes in Europe to increase this year, benefiting from the rapid growth of the Budget brand and the new corporate accounts we signed at Avis last year. In addition, we recently extended our longstanding arrangement with France's national railway operator, SNCF, for five additional years.

This arrangement gives us exclusive rights to co-market to SNCF customers at choice rental locations at rail stations throughout France. This is significant in as much as when the economy rebounds, domestic travel should increase, and rail represents not only an important mode of travel, but a very large customer base.

We're also seeing positive pricing trends across Europe in July and August, particularly in the southern holiday regions, which is also encouraging, as Europe generates most of its profit in the third quarter. As we noted in our earlier calls, our efforts to yield Budget up during the holiday period is positively impacting our realized pricing. But as we mentioned last quarter, our results in Europe this year will be muted to some extent by economic conditions, as well as by investments we're making in people, process, and technology in order to enhance our competitive position in the market.

In our Latin America/Asia Pacific region, we'll continue to expand Apex's footprint in the Australian market and will be developing franchise opportunities for Apex outside of its home region. We'll continue to add resources to accelerate our growth in China and roll out new initiatives to drive high margin international inbound and outbound revenue throughout the region, as well as manage costs to offset some of the soft pricing in Australia. All taken together, the important takeaway here is that our guidance continues to reflect year-over-year growth in the second half of the year, as we lap most of the remainder of 2012's timing benefit on fleet costs in Q3 and Q4 of this year.

Lastly, before I turn the call over to David, I want to discuss our new $200 million share repurchase authorization. We've long believed that our stock represents attractive value and we've demonstrated that over the past two years by repurchasing $270 million of our convertible debt, which reduced our diluted share count by more than 16 million shares or around 13%. We believe now is the right time to begin to return a portion of our strong annual free cash flow to shareholders in the form of a share repurchase program.

This decision reflects the confidence we have in our business and our long-term prospects, including our goal of achieving more than $1 billion of adjusted EBITDA by 2015, while also enabling us to maintain a prudent capital structure and the flexibility to execute on our strategic objectives. Going forward, the amount of shares we repurchase in a given period will continue to be evaluated against the needs of the business and other strategic opportunities.

We plan to continue to look for tuck-in acquisitions and investments that will improve our strategic position, and have meaningful synergy opportunities. Payless certainly fit those criteria and we'll continue to look for other opportunities, most likely among existing licensees to improve our long-term competitive position.

Given our cash commitments for this year however, I would not expect us to repurchase much more than $50 million of stock in calendar year 2013. I should also point out that we have not abandoned our target leverage ratio of 3 times to 4 times EBITDA, but we will seek to strike a balance between these three priorities for the deployment of free cash flow.

With that, I'll turn the call over to David.

David B. Wyshner, Chief Financial Officer and Senior Executive Vice President

Thanks, Ron, and good morning, everyone. Today, I'd like to discuss our second quarter results, fleet costs, our integration of Zipcar and some of our key technology initiatives as well as our balance sheet and outlook. My comments will focus on our results, excluding certain items. As Neal mentioned, these results are reconciled to our GAAP numbers in our press release and in the earnings call presentation on our website.

The second quarter marked our 12th consecutive quarter of year-over-year revenue growth, principally as a result of higher volume and improved year-over-year pricing in North America, as well as our first full quarter including Zipcar's results.

Adjusted EBITDA declined year-over-year primarily due to higher fleet costs in North America. Trailing 12 months adjusted EBITDA now stands at $727 million. For those analysts who calculate EBITDA before deferred financing fees and stock-based compensation, our trailing 12 months adjusted EBITDA would be $40 million higher or $767 million.

In our North America segment, revenue increased in the quarter due to the acquisition of Zipcar and continued organic growth, with volume increasing 2% and pricing up nearly 0.5%. Leisure pricing increased 4% in the quarter and leisure volume grew 2%, both excluding Zipcar.

The increase in realized leisure pricing was a result of our continued aggressive push to improve rates to offset fleet costs, as well as positive channel and fleet mix. We also saw solid demand in our commercial business in the quarter, with volume up three points, while pricing was down less than 1%.

Growth in higher price, small business rentals, continues to help offset declines in contracted commercial pricing. Adjusted EBITDA benefited from positive pricing, volume growth, significantly lower vehicle interest costs, and contributions from our performance excellence process improvement initiative, which continued to deliver solid results. But as anticipated, this was not enough to offset the significant year-over-year fleet costs increase we faced this quarter.

As a result, North America adjusted EBITDA decline 38% from the prior year. I'll come back to fleet costs in a moment.

In our international segment, revenue increased in the second quarter primarily due to higher rental volumes and ancillary revenues partially offset by a 2% decline in reported pricing. The October 2012 acquisition of Apex Car Rentals contributed $7 million to revenue in the quarter.

International adjusted EBITDA declined in Q2 due to inflationary increases in operating costs and higher commission expense in Europe. The combination of these two items offset the roughly $10 million of incremental synergies we realized in second quarter 2013, compared to second quarter 2012. In our Latin America/ Asia Pacific region cost savings throughout our operations, strong results in New Zealand and currency hedge gains offset the effects of weak demand in pricing in Australia.

Apex did not have a material impact on our adjusted EBITDA in the quarter. As Ron mentioned, the integration of Avis Europe continues to proceed well as we continue to reduce our European fixed cost base, streamlined operations and move more functions and position to our shared services center in Budapest. Headcount in our Budapest location has more than doubled since we acquired Avis Europe in 2011. With the new facility we moved to in April we have opportunities for additional growth there.

We believe that the work we're doing in our EMEA region is putting us in position to drive substantially higher profits once the economy there improves. Revenue in our Truck Rental segment declined $1 million as a 9% increase in pricing was offset by a 9% volume decline. The volume decline primarily reflected the intentional 7% year-over-year reduction in the size of our average truck rental fleet. As we reposition the business for long-term sustainable profitability. This strategic repositioning will impact reported results for this segment for the rest of 2013 as well as we plan to reduce our fleet from 25,000 trucks at the start of the year to approximately 20,000 by the end of 2013.

Truck rental adjusted EBITDA declined by $1 million in the quarter. As we discussed during our last earnings call, corporate and other expense increased as we reallocate certain existing corporate level costs that benefit multiple regions and segments. We still expect to see $4 million to $6 million in year-over-year increases in corporate and other expense in each of the remaining quarters of 2013.

Separately, our total SG&A costs increased as a percentage of revenue in the second quarter. This was primarily due to the inclusion of Zipcar, which has higher sales and marketing expenses than our traditional car rental operations and increased marketing commissions in Europe. The additional commissions in Europe, which were particularly pronounced in the second quarter shoulder period, are supporting both the growth of the Budget brand and our efforts to shift toward retail bookings and away from net rates.

Moving now to fleet costs, I provided some background during my webcast presentation last quarter on how changes in vehicle residual values can affect our earnings. I want to go over this example again. As we outline on slide 18 of today's deck, we typically sell our risk cars in the $16,000 range and for purposes of this discussion, assuming that projected residual values were to decline by 1%. This will reduce the value of a car at the time of sale by approximately $160.

To make the math easy, assume we hold a risk vehicle for 16 months. In that case, a one point change in residual value would impact the depreciation of that car by $10 per month over its life. Since our fleet of roughly 330,000 vehicles in North America is comprised of approximately 65% risk cars, we have 215,000 risk cars on average. On this base, a $10 change in monthly depreciation rates for risk cars would have a $2 million monthly impact or $25 million annual impact on our pre-tax earnings.

And when the one point change in residual values is not expected, such as in Q2, the near term impact is greater, since the $160 change in value is reflected sooner either in increased depreciation or loss on sale rather than being spread over the full 16 month life of the vehicle.

With all that being said, we continue to believe that by having approximately 35% of our fleet comprised of program cars, our exposure to changes in residual values is significantly less than that of our principal competitors in North America.

In Europe, residual values remain soft, but with the fleet there that now stands at more than 70% program cars. Our exposure to changes in the used car market is limited. At the same time we built a new direct-to-dealer online selling system for fleet dispositions in Europe, and are now selling most of our risk cars in Italy are online with good results. We plan to expand this model to other European countries to further optimize our fleet costs.

In North America, our negotiations for model year 2014 vehicles have been progressing reasonably well. We're seeing ample availability in both program and risk cars with no material change in risk car purchase prices or program car holding costs expected.

Turning to another increasingly important part of our business model, our Zipcar operation contributed $76 million of revenue, and $6 million of adjusted EBITDA in the second quarter and our integration work continues to progress well. Since the acquisition closed in March, we've been actively implementing the cost synergies we laid out. We've largely eliminated Zipcar's public company costs. We centralized fleet purchases here in New Jersey, which allowed Zipcar to benefit from Avis Budget substantial purchasing power.

We're now financing Zipcars at the lower interest rates associated with our vehicle backed financing facility. We've in-sourced most of Zipcar's routine maintenance work, largely eliminating the use of outsourced vendors, as our mechanics at existing locations can do this work much more economically. And as Ron noted we have substantially increased Zipcars fleet for the summer demand peak. We plan to continue to provide more services, cars, and location for Zipcar members to enjoy, encouraging increased usage while leveraging our existing infrastructure to drive synergies and growth.

While Zipcar was built on the notion of using technology to serve additional transportation services needs, we're aggressively using technology in new ways throughout our business. This includes both customer facing and non-customer facing opportunities. For example, we've added our Wizard – we've added in to our Wizard System a behind the scenes technology solution for our Avis Preferred Select & Go vehicle choice program, now operating nearly 50 airports in North America.

We are enhancing our mobile applications to improve usability and drive incremental sales of high-margin ancillary products and services. We're investing to further enhance the customer experience offered on our avis.com and budget.com websites throughout the world, which will help us increase conversion rates. Our Avis Preferred customers can now receive an e-mail upon landing that tells them what vehicle they've been assigned and exactly where it's parked. We have plans to extend this value-added service to Budget Fastbreak members in the near future.

We've launched customer relationship management systems that allow us to better identify, serve, and market to our customers, which we think we will improve customer retention and our share of wallet. We're actively using fleet optimization software that is helping us better plan and manage fleet purchases, fleet deployment and fleet dispositions.

We're building what we think will be the industry state-of-the-art yield management system, which we're already using to help automate price changes in select markets throughout the United States, which we think will provide annual benefits in the eight figure range by 2014. And we're looking at ways to combine the in-car technology solutions that powers Avis On Location rentals and automated processing of vehicle returns with Zipcar's in-car and customer facing systems in ways that will simplify fleet sharing and expand Zipcar's capabilities. These are important projects for us. We think they'll have a meaningful impact on how we attract and serve customers and on our bottom line. We'll be talking more about them in coming quarters.

Turning to the balance sheet, our liquidity position remains strong with $1.8 billion of available liquidity worldwide. We ended the quarter with $500 million of cash, no borrowings under our corporate revolver, and roughly $400 million of availability under that facility with unused capacity of $900 million under various vehicle back funding programs. Our ratio of net corporate debt to LTM adjusted EBTIDA at the end of the quarter was four times.

This figure includes the debt incurred to acquire Zipcar, but with minimal contribution to our LTM adjusted EBITDA from Zipcar since we've only owned it for one quarter. Pro forma for anticipated Zipcar synergies, our net leverage is 3.7 times. We took advantage of the strength in the credit markets in the first half of the year to strengthen our balance sheet and lower our interest costs.

In June, we refinanced our existing $900 million in term loan borrowings with $1 billion in new term loan borrowings, and lowered the interest rate on this debt by 75 basis points. We redeemed the entire $124 million balance of our 9 5/8% notes. We also redeemed the $100 million of our floating rate notes, due 2014. We recently amended our revolving credit facility expanding its – extending its maturity to 2018, increasing its size to $1.65 billion and lowering the interest rate by 75 basis points. We expect this transaction to save us more than $5 million annually. We feel that our floating rate interest exposure is manageable, and that the interest expense on our income statement still exaggerates what our debt would cost at current market rates. In particular, we have $950 million of corporate debt that has interest rates above 8% compared to the roughly 6% at which we could issue fixed rate term debt today.

Lastly, I'd like to spend a few minutes on our updated 2013 outlook. The changes to our projections reflect our updated fleet cost estimate, the positive pricing we realized in the second quarter and our expectation of positive pricing in North America in Q3, as well as the macro economic challenges we see in Europe and Australia. As we announced last night, we expect our 2013 revenues to be approximately $7.8 billion to $8 billion, a 6% to 9% increase compared to 2012. We expect North America per unit fleet costs to stabilize this year, at around $300 per month, an increase of approximately 25% versus 2012. We expect adjusted EBITDA, excluding items to be approximately $750 million to $800 million. We think our full year corporate interest expense will be approximately $230 million, a decline of $30 million compared to 2012, and $10 million lower than our prior forecast due to our favorable refinancing activities.

With non-vehicle depreciation and amortization expense of $130 million to $135 million excluding purchase accounting effects, we estimate that our 2013 pre-tax income will be $385 million to $440 million. We expect our effective tax rate in 2013 will be 37% to 38% and our diluted share count will be approximately 117 million to 118 million, including a modest benefit from share repurchases in the second half of this year.

Based on these expectations, we estimate that our 2013 diluted earnings per share excluding certain items will be approximately $2.05 to $2.35. We expect our capital expenditures to be around $160 million this year. We continue to expect our performance excellence initiative to provide more than $50 million in incremental benefits in 2013 compared to 2012. And finally, we expect our cash taxes to be approximately $60 million this year and for free cash flow to be in the $300 million range absent any significant timing differences.

As a reminder, $300 million of free cash flow this year in addition to the $518 million we generated in 2012 would mean that we are averaging around $3.50 of free cash flow per share over the two-year period. With that being said, our revised 2013 outlook is clearly somewhat lower than we would like and we are focused on implementing actions and seizing opportunities to finish the year strong. At the same time, we're working toward the intermediate term goal of $1 billion of adjusted EBITDA in 2015, excluding our expectations for Zipcar.

Our plan continues to be to combine regular organic growth in our business globally with meaningful incremental contributions from strategic initiatives and projects. These initiatives include fleet optimization, yield management, performance excellence, incremental synergies in Europe, and fleet maintenance and damage efficiencies, each of which has the potential to contribute tens of millions of dollars to our bottom line by 2015.

So to wrap up, while we are facing a combination of incremental fleet costs pressures and economic headwinds in various parts of the world, we're taking steps to mitigate as much of this as possible and remain enthusiastic about the positive volume and pricing trends we're seeing this summer and this year in North America and Europe.

We remain on track to achieve $300 million of free cash flow this year and anticipate using a portion of this to repurchase shares. And our goal of generating more than $1 billion of adjusted EBITDA by 2015 should translate into at least $500 million of annual free cash flow or more than $4 dollars per share.

With that, Ron and I would be happy to take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. At this time, we are ready for the question-and-answer session. [Operator Instructions] Our first question, John Healy with Northcoast Research, you may ask your question.

<Q – John Healy – Northcoast Research Partners LLC>: Thank you. I want to ask a little bit about fleet costs. Ron you mentioned that you're going to be at the $300 level in the U.S. this year and with your comments regarding negotiations and outlook for 2014, should we be thinking that the $300 number is probably a good number to use going forward as we think to next year? And with that you talked about – it seems like you're talking a little bit more progressively about using some alternative remarketing channels. Can you talk to what you think the type of savings you could get per car across the U.S. fleet if you kind of changed your remarketing strategies a little bit?

<A – Ron Nelson – Avis Budget Group, Inc.>: Yeah. Hi, John, I think the unknown in the $300 fleet cost is what happens in residual value market. I think on the cap cost front we're reasonably comfortable that absent some mix changes in terms of kinds of cars we buy that we're not going to see a lot difference in the acquisition costs. I think we'll see a little bit less of interest costs as the lower interest costs works its way through the fleet costs line. But in the end it all comes down to what happens to residual values, and while I think we've seen a stabilization of it coming into July and August, I don't think that you can take two months and then extend it to out over the course of the year. The usual things will tend to impact residual values, the off-lease vehicles, the SAAR and how many cars the car rental companies buy and in turn try to sell. So I think that's going to be the unknown and that will impact whether $300 is the right number or $295 or $305. So I think that's that aspect.

I think in terms of the alternative rental channels, we're clearly seeing some benefits from our joint venture with AutoNation. We're sharing effectively the spread between retail and wholesale margin and that's providing some incremental benefit. In terms of volumes it's still not a material number that's going to drive a big increase in volumes that will sell through that channel. And I think as I've explained you before, I mean we are selling 30% to 40% of our cars through online wholesale channels, which while it doesn't really generate a lot of incremental benefit over traditional auctions, what we are seeing pretty consistently is less time between last revenue and sales. So, you pick up a little bit of depreciation and you pick up interest in that.

In the direct-to-dealer market, again we're continuing to move forward and expand that. We are seeing some incremental gains. I would put them at 2% to 5% kind of number on an apples-to-apples basis. So, I think that's those are sort of the elements of what's driving our alternative sale strategy.

<Q – John Healy – Northcoast Research Partners LLC>: Okay. Great. And David, I had a kind of housekeeping question for you. You guys have been very active with the taking advantage or refining a lot of the parts of your balance sheet. I know you mentioned for 2013 how you think about the interest expense level. Can you remind us kind of what you think maybe the tailwind might be in 2014 on the interest expense line as well?

<A – Dave Wyshner – Avis Budget Group, Inc.>: Sure. We – starting with the recent refinancing of our revolving credit facility, that's going to produce a $5 million annual impact. We only have five months for that this year. So that will produce some incremental benefit next year. And the same is true of the actions we took earlier in the year in terms of refinancing various pieces of our debt which are produced about $15 million of savings this year and were annualizing into a slightly greater number next year. So, we'll have a pickup there as well. And then the opportunity that that lies in front of us that at some point that I alluded to is refinancing the over 8% debt that we have on our balance sheet, it's not currently callable, but the premiums associated with retiring or refinancing that debt that do decline over time and we'll continue to look at that to see when there's a good opportunity.

<Q – John Healy – Northcoast Research Partners LLC>: All right. Thank you guys.

Operator: Our next question, Chris Agnew with MKM Partners. You may ask your question.

<Q – Chris Agnew – MKM Partners LLC>: Thanks very much. Good morning. Ron, you mentioned on the last quarter that the fleet levels were in line with demand. Now with pricing, and pricing was up 3% in May and June and you also mentioned today that pricing is lower in the third quarter sort of 1%, 1.5%. I'm assuming that means fleets have loosened in the interim and I also note that your fleet levels increased more than transaction days and there may be other things behind that. But, I guess my question is how, when and why did fleet solution and how long do you think it'll take the industry to adjust and what are you doing to adjust fleet bubbles? Thanks.

<A – Ron Nelson – Avis Budget Group, Inc.>: Well, I'm not sure, Chris, that we would characterize fleets at least during the third quarter as being loose. I mean we're seeing a lot of LOR restrictions across the industry, and I think if you look at the second quarter, you always expect fleets to be a little loose as people in fleet for the – or the summer months. The other thing that I think factors into it, in terms of premium vehicles and luxury vehicles, the issue really isn't utilization so much as it is RPU, and so what you're seeing is, is an increased mix of luxury premium vehicles in our fleet that that have lower utilization, but clearly have substantially higher RPUs. So it continues to get reflected in the revenue even though the utilization metric suffers a little bit.

I do want to clarify that pricing is up in July and August and I think in terms of the absolute water level of pricing in those months, it's significantly higher than obviously the water level of pricing in the second quarter on a sequential basis. So, getting gains in a period where you already have significant pricing, I think is generally what we would have expected.

Nonetheless, we continue to increase pricing. We don't think that pricing is at a level yet where it generates the return on capital that this business will have and so we continue to post price increases whenever and wherever we can.

<Q – Chris Agnew – MKM Partners LLC>: Great. Thank you. And then one more question and I know you touched on this through the presentation, but maybe just to recap what gives you confidence that fleet costs will stable or are stabilizing going forward? Thanks.

<A – Ron Nelson – Avis Budget Group, Inc.>: Well I think we know enough about where the 2014 model negotiations are to have a good, pretty good sense of where our acquisition costs are going to come out. And I think in terms of the 2013 cap costs, the manufacturers look at what's going on the residual values as well. And I think that – 2013 cap costs were probably a little higher than otherwise would have been the case as they look to capitalize on the value that was being generated by increased residual values. What's hard to predict is what other residual values of the cars that we're going to be selling in first, second, and third quarters of next year and that's why – I think we've gotten back to a more normalized rate. I think things have stabilized. I think the rationalization of fleets across the industry because of acquisitions has probably worked its way pretty well through. And so you're not going to have any sort of disproportionate sales month-to-month and quarter-to-quarter like we experienced in the second quarter. But ultimately it's hard to predict residual values with any precision that are going to affect that holding cost.

<A – Dave Wyshner – Avis Budget Group, Inc.>: One other element of that was on our experience in used car market. We saw what I would characterize as stability in June as that continued into July and the last 10 days of July may have even been a half tick upward. So we do feel that based on our own experience, we're seeing stability in the wholesale market.

<Q – Chris Agnew – MKM Partners LLC>: Correct. Thank you.

Operator: Our next question, Afua Ahwoi with Goldman Sachs. Your line is – you may ask your question.

<Q – Afua Ahwoi – Goldman Sachs & Co.>: Thank you. Two questions from me. First on – I just wanted a clarification on the reason for the tightening of the guidance range. In the release you mentioned the better pricing trends in North America offset by residuals in North America and weak economic conditions in Europe and Australia. But I gather from your comments and from even the second quarter that Europe is a little better. So I just wanted to make sure that are you saying that Europe is getting incrementally worse or is it just the sort of same level of weakness we've seen or are you even seeing signs of stabilization and an uptick?

And then the second part was on the volumes in North America, how much do you think the decision to walk away from some of the opaque channels cost that I think last quarter you said it was about a 300 basis point impact. Is that – is there a similar number you can give us for this quarter? Thank you.

<A – Dave Wyshner – Avis Budget Group, Inc.>: Good morning. Working backward the – we do continue to step away from opaques a bit and I think it – both in the first quarter and in the second quarter it helped our achieve pricing by close to a point, it's not 300 basis points, but close to a point.

<Q – Afua Ahwoi – Goldman Sachs & Co.>: That question was actually on the – I think last quarter you said the impact to volumes from walking away from the opaque was – I thought you said it was 300 basis points. I was wondering if you could give us a similar number for this quarter?

<A – Dave Wyshner – Avis Budget Group, Inc.>: We will get that. I don't have it in front of me, but clearly our opaques were down double digits and I think the impact would be certainly at least a point – closer to 2 points in the second quarter. With respect to the change or the revision of our guidance and what's driving that, Europe is clearly playing a part and what we're seeing there is, stability but at what we would characterize as fairly depressed levels economically. And you can see that in GDP figures and unemployment rates and so forth and we certainly see it in our business and the demand that's there particularly on the commercial side of the business. We feel that our own results are better than the market as a whole for the reasons that Ron outlined. We've been able to win some significant commercial accounts, we're growing the Budget brand, nicely and seizing additional business in the value portion of that market, and those activities are allowing us to produce and report volume numbers that are stronger than we think the underlying demand is in Europe. So we are looking at both our – the actions we're taking as well as the underlying macro trends when we think about Europe.

<Q – Afua Ahwoi – Goldman Sachs & Co.>: So, sorry, just to clarify, so has Europe gotten – the macro trend has that gotten incrementally worse from what you see and your initiatives are offsetting that or it's still the same level as what you're seeing?

<A – Dave Wyshner – Avis Budget Group, Inc.>: I think the only way to think about it is that we fail to see any improvement in the underlying macroeconomic trends over the course of this year.

<Q – Afua Ahwoi – Goldman Sachs & Co.>: Got it. Thank you.

Operator: Our next question, Adam Jonas with Morgan Stanley. You may ask your question.

<Q – Adam Jonas – Morgan Stanley & Co. LLC>: Hey, everybody. First question on pricing and your outlook, you cited better-than-expected pricing in the quarter and your fleet costs are rising more than expected. So, in your revised guidance for the full-year, do you at least embed some better pricing assumption for you versus your prior guidance and if so how much?

<A – Dave Wyshner – Avis Budget Group, Inc.>: Hi, Adam. We have assumed modestly better pricing consistent – with respect to the third quarter, consistent with the comments that Ron made about in July and August and I think that probably translates into a point of pricing for the third quarter. For the fourth quarter, we're still hesitant to be as aggressive as that. So, we built in a little bit for that but not a lot at this point. So, I think there could be some upside in the fourth quarter compared to our outlook on pricing, but at this point, we look forward to be flat to maybe upper fraction of a point.

<Q – Adam Jonas – Morgan Stanley & Co. LLC>: In the fourth quarter?

<A – Dave Wyshner – Avis Budget Group, Inc.>: In Q4, right.

<Q – Adam Jonas – Morgan Stanley & Co. LLC>: Thank you. And just a follow-up on pricing. You've commented kind of before about how the competitive dynamic was working with you leading price increases and I think for a large part of the last 12 months, Enterprise seemed to be the fast follower and then Hertz perhaps a more sluggish follower given some unique expansion of their business and digestion of that. Any change in the nuance of that. Have you seen maybe Hertz following or Enterprise following Hertz or kind of how is that change versus that previous dance?

<A – Ron Nelson – Avis Budget Group, Inc.>: Yeah. Adam, I don't think much has changed. I still think we see somewhat the similar trends. I think the following by our competitors is choppy. I think we probably do see a little more consistency out of the Enterprise complex of brands than we do out of Hertz, but I think the fair answer is it hasn't changed much over the course of this year in terms of people being followers. Nonetheless, I will point out that we are undaunted in moving forward. We are continuing to post price increases. We're continuing to go after commercial rate increases, and I don't think this is about driving as much profit as we can out of these rentals. This is really about getting the return on capital in our industry up to rates where we think a business that uses a much capital as we do should have. And so, we're going to continue to push and particularly as we move into the third quarter and into the fourth quarter.

<Q – Adam Jonas – Morgan Stanley & Co. LLC>: That's great, Ron. Thank you. And just one – I just want to clarify one earlier question on the fleet costs. Just to clarify, it wasn't quite clear. In your revised depreciation guidance, was that just based on the current level or the 2Q level of residuals kind of holding for the rest of the year or did you anticipate any further weakness from that end of 2Q level? Thank you.

<A – Ron Nelson – Avis Budget Group, Inc.>: Yeah, we made some assumptions about Q4. As you know the market does traditionally weaken as the rental car industry de-fleets over the course of the fourth quarter. So, we...

<Q – Adam Jonas – Morgan Stanley & Co. LLC>: But nothing beyond seasonal factors? Just – you only took in a normal seasonal pattern or anything a bit more draconian than that?

<A – Ron Nelson – Avis Budget Group, Inc.>: I think we've taken a normal seasonal pattern based upon experience that we're currently seeing over the course of the second and third quarter.

<Q – Adam Jonas – Morgan Stanley & Co. LLC>: Great. Thank you very much.

<A – Ron Nelson – Avis Budget Group, Inc.>: Sure.

Operator: Our next question, Brian Johnson with Barclays. You may ask you question.

<Q – Brian Johnson – Barclays Capital, Inc.>: Yes. Good morning, Dave and Ron. Just want to drill, continue the line of questioning around pricing. You talked on the last call about changing the sales force incentives, changing the retention metrics and not necessarily being willing to be the stalking horse in large corporate bids. With corporate continuing down, one, I imagine most of the corporate rentals were under older contracts coming into the quarter. Can you give us any sense of how those discussions went with large corporate buyers? When is even really the season for rolling over those contracts, is it winter, is it generally 4Q? And just in general, the reaction and progress you're getting on aligning the prices large corporate guys pay with the value you're providing?

<A – Ron Nelson – Avis Budget Group, Inc.>: I think in terms of very large corporate customers, Brian, there haven't been that many RFPs over the course of the quarter. And I think that there's actually been a couple where we know there's not any service issues, where we've been stalking horses and we've actually – I mean certainly we'll bid, but we're not going to bid in order to just get the business and serve as a stalking house for the incumbent, particularly if there aren't any services issues that are associated with the account.

The majority of our renewals, just because of the sheer volume and size, we've been in mid-market area, and I think that's where we've seen the most significant types of benefit. It's – this has been three to four months, so you can't extrapolate and expect to see all of the benefit rolling through your commercial pricing. But I do think we're encouraged that we are getting some traction with this and our sales people have really gotten the message that it's time to hold firm and try to get rate increases.

I think the other thing that you need to sort of keep in the back of your mind is that there's a fair amount of flipping that goes on in the mid-market accounts. And when the first quarter flipping was stunted, because leisure pricing was up so significant, my recollection is we were up 8% or 9% across the board, we were up 4% in the second quarter, so that, at the margin, that probably allowed flipping to increase a little bit depending on where your rate was on your mid-market contract. So I think that the modest decline in commercial pricing that we saw was more influenced by the flipping mix than it was by anything else.

<Q – Brian Johnson – Barclays Capital, Inc.>: Could you just maybe explain the flipping effect? Is it when leisure price is less than the corporate price?

<A – Ron Nelson – Avis Budget Group, Inc.>: Well, everybody has different pricing all across the board, and so they always have the right to flip into a leisure rate. So if leisure rates are lower than your commercial contracted rate then accounts tend to flip into the lower rate. So, it just depends on what your rate is and whether or not they can flip. When prices are up 8% or 9% in the quarter, my guess is that flipping doesn't look terribly attractive, but on a year-over-year basis when they're only up 4%, there is probably some segment of accounts where flipping does look attractive.

<Q – Brian Johnson – Barclays Capital, Inc.>: And secondly, since my understanding is the pricing algorithms take the fleeted location and try to, or in a metro area, and try to optimize the yield. Did you ever have to manually intervene in order to delete fleet or move fleet around in order to preserve a pricing level? And if not you, are you in general seeing your competitors being relatively nimble about adjusting fleet sizes to allow their programs to clear the inventory at a good rate?

<A – Ron Nelson – Avis Budget Group, Inc.>: Brian, we do that every week. I mean, we move the fleet in and out and in between locations based upon the reservation, build demand, competitive fleets that we see out there. So that is an everyday occurrence. What I think would be fair to say is that you tend to see less of it in the second quarter because, while you might move fleet from one location that's over fleeted to another location that's got demand, you're not taking the fleet out because you need it for the third quarter.

As I said, our experience thus far this summer is that across the country, there are LOR restrictions from all our competitors. And so I think that we would probably say that fleets are right sized with respect to demand and are deriving the amount of pricing that those fleet levels command and the competitive market obviously commands.

<Q – Brian Johnson – Barclays Capital, Inc.>: Thanks.

<A – Ron Nelson – Avis Budget Group, Inc.>: Yep.

Operator: Our final question comes from Fred Lowrance with Avondale Partners. You may ask your question.

<Q – Fred Lowrance – Avondale Partners LLC>: Hey, guys. Thank you and good morning. Just want to touch on the fleet costs side of things quickly before the call ends. Obviously, you're going with AutoNation now to sell you cars to retail. Just wondering if you could give us a little bit of background on why you choose to go with a third party instead of doing that yourself. And then if you could sort of quantify what you think the – if you were to completely build out a retail channel yourself, what you think the difference in economics is between selling your cars yourself at retail versus having AutoNation do it for you and obviously splitting some of the economics with them? Thanks.

<A – Ron Nelson – Avis Budget Group, Inc.>: Well, I think Fred, the quick answer to that is that we didn't want to replicate the infrastructure in terms of the services that you have to provide to be in the used car business. And a fast and efficient way to get into the retail market and understand what was going on was with somebody that has largely national footprint. AutoNation is in 37 states I believe. So there's an opportunity to rollout more significantly than we have and drive volumes. And I think in those states where they're not, then we'll look for other partners and over the course of the years, we just think that this is a better way in terms of return on capital, of garnering some of the spread between wholesale and retail. So what was the second part of your question, I'm...

<Q – Fred Lowrance – Avondale Partners LLC>: It was just if you had a sense for, you know what the economics are that you're getting on an AutoNation sale, just wondering you know the difference between...

<A – Ron Nelson – Avis Budget Group, Inc.>: Yeah, the average spread between wholesale and retail varies all over the lot. But I think if we used a number of somewhere around $1,600 to $1,700 as the spread and assume that it's roughly 50/50, 40/60 kind of spread or kind of split between us and AutoNation, you're not going to be too far off.

<Q – Fred Lowrance – Avondale Partners LLC>: Okay. Thank you.

Operator: For closing remarks, the call is being turned back over to Mr. Ronald Nelson. Please go ahead, sir.

Ronald L. Nelson, Chairman, President, Chief Executive Officer & COO

So just in closing what I'd like to do is reiterate what I believe are the key points from today's call. Pricing and volume trends we are seeing across North America and Europe this summer are encouraging. We're continuing to push for pricing wherever we can and whenever we can to offset higher fleet costs, and our integration of Zipcar is proceeding well. We do remain optimistic about the opportunities that lie ahead of us over the next few years and has not been diminished and the share repurchase program we announced last night is a testament to that optimism, as well as those opportunities in our current position. We have an active investor calendar over the remainder of the quarter, we hope to see many of you during our travels and with that, I want to thank you for your time and your interest in our company.

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