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# Hertz Global Holdings, Inc. (HTZ)

Q3 2019 Earnings Call

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# MANAGEMENT DISCUSSION SECTION

**Operator**: Welcome to the Hertz Global Holdings Third Quarter 2019 Earnings Call. Currently, all lines are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. I would like to remind you that today's call is being recorded by the company.

I would now like to turn the call over to our host, Leslie Hunziker. Please go ahead, ma'am.

Leslie M. Hunziker
*Senior Vice President-Investor Relations, Corporate Communications & Corporate Social Responsibility, Hertz Global Holdings, Inc.*

Good morning, everyone. By now, you should have our press release and associated financial information. We've also provided slides to accompany our conference call that can be accessed on our website.

I want to remind you that certain statements made on this call contain forward-looking information. Forward-looking statements are not guarantees of performance, and by their nature, are subject to inherent uncertainties. Actual results may differ materially. Any forward-looking information relayed on this call speaks only as of this date and the company undertakes no obligation to update that information to reflect changed circumstances.

Additional information concerning these statements is contained in our earnings press release and in the risk factors and forward-looking statements section of our 2018 Form 10-K and our third quarter 2019 Form 10-Q when filed. Copies of these filings are or will be available from the SEC and on the Hertz's website.

Today, we'll use certain non-GAAP financial measures, all of which are reconciled with GAAP numbers in our press release, which is posted on our website. We believe that our profitability and performance is better demonstrated using these non-GAAP metrics.

Our call today focuses on Hertz Global Holdings, Inc., the publicly-traded company. Results for the Hertz Corporation are materially the same as Hertz Global Holdings.

On the call this morning, we have Kathy Marinello, our CEO; and Jamere Jackson, Hertz's Chief Financial Officer. I'll now turn the call over to Kathy.

## Kathryn V. Marinello

*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*

Thank you, Leslie, and good morning, everyone. In the third quarter, we delivered our ninth consecutive quarter of year-over-year top line improvement and our eighth consecutive quarter of earnings growth.

Worldwide adjusted corporate EBITDA was 12% higher in the latest three-month period. These strong results continue to reflect operational efficiencies, the successful execution of our strategies, early returns on foundational and growth investments and the valued 38,000 employees around the world deliver to their commitment to understanding the needs of our customers and to creating differentiated experiences for them. So let me start there.

The investments we've made over the last three years in enabling efficient personalized service, offering top rated vehicles and developing customer-centric technologies that enhance the travel experience are paying off. Last month, J.D. Power's named Hertz number one overall in its 2019 North America Rental Car Satisfaction Survey.

I want to personally thank everyone across the organization for their contribution to this accomplishment. Our employees are committed, caring and take great pride in making the Hertz experience number one for our customers.

In addition to being awarded best overall, Hertz also took the top spot in several key categories, including pickup process, return process, cost and fees and the reservation process. When it comes to reserving a vehicle, Hertz's enhanced digital app makes user experiences more personal and provides customizable content, a seamless checkout process and intuitive navigation. The app is helping to drive a 10% increase in Hertz's digital direct bookings year-to-date.

Everyone at Hertz, Dollar and Thrifty knows that putting the customer first is key to capturing demand and earning a higher price. In the recent third quarter, our U.S. Rental Car business generated 6% more revenue on 5% higher volume and a 1% increase in RPD, on top of a very strong growth in the prior year.

When it comes to revenue growth, by leveraging core strengths and looking at our business with an entrepreneurial mindset, we're not only improving the customer experience, we're finding new ways to capture incremental growth in adjacent markets like TNC and last mile delivery.

We're also creating incremental value with innovations like Hertz's Fast Lane biometrics technology, our easy-to-use online Car Sales portal and Donlen's DriverPoint Telematics platform. Through the combination of Donlen and Hertz's strength, we found increased advantages and opportunities for differentiation and expansion.

Donlen's proprietary Telematics and Analytics platform, its maintenance network and its large fleet management capabilities dovetail nicely with the operating, logistics, distribution and service strength of our rental car business. With Donlen, we've been connecting the TNC vehicles and the delivery trucks and vans we rent globally to facilitate driver maintenance alerts and encourage driver safety.

Donlen's DriverPoint, Analytics and dashboards also help our rental car operations, better monitor vehicle usage and manage fleet utilization and maintenance requirements in real-time, and we're only just getting started. The potential for leveraging Donlen's systems capabilities is significantly expanding.

While technology and improved processes are helping to create new revenue opportunities and make the customer experience faster and easier, it's also allowing our employees to operate more efficiently without jeopardizing service. Enhancements to our customer relationship management tools are resolving issues and getting customers on their way faster.

Our recently launched cloud-based financial system has reduced manual activities, offering direct access to data and greater flexibility, which improves reporting execution and forecasting accuracy. And just last week, we cut over to our fleet management cloud solution in a small North American market the first module of our integrated platform. This more agile and streamlined system will allow for better lifecycle asset management, on-demand vehicle reporting and greater employee productivity.

Technology-enabled productivity, along with a companywide commitment to process excellence ensures we operate at a sustainably lower cost, while delivering the award-winning service to our customers, leaders across the organization are taking accountability for efficiencies and returns on incremental growth investment. We're making steady progress.

Year-to-date direct operating and SG&A expenses as a percent of revenue improved 140 basis points and there's still quite a bit of opportunity. Vehicle depreciation expense is also low year-over-year, somewhat due to strong market residual values in the US, but also driven by our strategic fleet buying and the benefits of having one of the leading car sales operations nationally. Jamere will give you more details on our recent performance.

Overall, it's clear our foundational strength of disciplined fleet and revenue management, operational excellence and brand marketing are effectively delivering consistent revenue and EBITDA growth. Having that strong foundation in place now affords us the ability to innovate and respond to new growth opportunities. Towards that end, we're already seeing strong year-over-year earnings contribution from ride-hailing, retail delivery and large corporate fleet management.

Additionally, the investments we've been making in the connected technology platform will further elevate and support the future of the business. There's a lot to be excited about with so many opportunities. As always, we'll be disciplined and thoughtful in our approach to creating value.

With that, I'll turn it over to Jamere.

## Jamere Jackson

*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*

Thank you, Kathy, and good morning, everyone. Overall, we had a solid third quarter, marked by year-over-year improvement in revenue, double-digit improvement in adjusted corporate EBITDA, and significant progress on our growth and productivity initiatives.

We are building a faster growing business, driven by improvements in our fleet, expanded product offerings, industry-leading customer service and brand building marketing. The growth initiatives, lower vehicle carrying costs and our laser focus on productivity are driving margin expansion and improved profitability. The improved operating capability of the company position us well as we look forward to 2020.

First, let me provide an overview of our total company results. Slide 6 shows our consolidated results on a US GAAP basis and our non-GAAP measures for the third quarter. Total revenue of $2.8 billion was up 3% on a reported basis and up 4% on a constant currency basis versus third quarter 2018, driven by exceptionally strong 6% growth in our U.S. RAC segment, partially offset by a 4 point drag due to foreign currency in our International RAC segment.

Our revenue results marked nine quarters of consecutive year-over-year quarterly growth for our business. GAAP net income for Hertz Global was $169 million during the quarter compared to $141 million in the third quarter of 2018, and net income per diluted share was $1.26 compared to $1.47.

The drag on net income per share is attributable to the equity rights offering, which increased the weighted average number of diluted shares outstanding from $96 million in the prior year to $134 million in the third quarter of 2019. We've included an appendix in the presentation, slide 15, that provides a reconciliation of our share counts for the third quarter 2019 and 2018.

On a non-GAAP basis, adjusted corporate EBITDA improved 12% to $392 million and our adjusted corporate EBITDA margin expanded by 110 basis points. The significant improvement in our results were driven by higher volume, increased pricing, lower vehicle depreciation expense in our RAC business, and the impact of our productivity initiatives, which caused our direct operating expenses and SG&A to remain flat, while revenue grew 4% on a constant currency basis.

Adjusted net income for the quarter was $214 million or $1.60 per share compared to $180 million or $1.88 per share in the prior year quarter. The drag on adjusted EPS is also attributable to the equity rights offering that I mentioned earlier.

Now, let me provide some color on the quarter, starting with our U.S. RAC segment and I'll start with revenue. Our U.S. RAC business had total revenues of $2 billion, up 6% versus the prior year and a third quarter record for the segment. U.S. RAC segment saw strong volume growth with a 5% increase in transaction days and moderate pricing improvements with both time and mileage rate and total RPD up 1%.

The revenue results were driven by strong demand in retail, high-margin value-added services and rentals to Uber and Lyft drivers, which we call TNC rentals. Ex-TNC, U.S. RAC revenue grew 5%, driven by a 3% increase in transaction days and a 2% increase in RPD.

In the quarter, we saw strong revenue growth in Hertz, Dollar and Thrifty and both on and off airport. TNC, which is one of our key growth initiatives, was up 30% and contributed over a point of revenue growth for the segment. We continue to see robust demand, increased pricing and we're adding new locations and service offerings to capitalize on this important growth opportunity.

U.S. RAC adjusted EBITDA was $269 million or 29% improvement versus the prior year quarter. Our results were driven by the strong top line growth, a 5% decrease in monthly per unit vehicle depreciation and outstanding productivity. Our teams continue to execute on our growth initiatives, disciplined fleet management, service excellence, brand building marketing, and productivity, resulting in solid growth and profitability improvements in our U.S. RAC segment.

Now turning to fleet, monthly vehicle depreciation expense of $247 per unit for the quarter decreased 5% as a result of disciplined fleet acquisitions, residual value strength and solid execution on our disposition strategy.

Utilization in the quarter was impacted by securing cargo vans and trucks to support the fourth quarter holiday peak for package delivery and the growing industry demand for last mile delivery drivers. Last mile package delivery represents another important growth initiative for the company.

We've already partnered with nearly 650 delivery service providers, who are servicing retailers, e-tailers and end market consumers. In addition, we grew our fleet capacity to support the growth in our TNC business. Excluding TNC and delivery vehicles, fleet capacity was in line with the growth in core rental transaction days.

Moving to our fleet sales initiatives, overall, retail dispositions grew 9% for the quarter and thanks to our sales, grew 2%. Our retail channel is an important growth initiative that has given us a competitive advantage on the cost of cars and the opportunity to grow retail car sales beyond dispositions of our rental fleet. As such, we're continuing to invest in our world-class sales teams, adding new locations and adding capability to our web-based platform to drive revenue growth and profitability.

We've grown to 88 stores in the US and Canada with plans for additional openings by the end of the year. The strength of the Hertz brand, the mix and quality of the fleet, and the investments in the customer experience will drive strong results for us in 2020 and beyond.

Moving to our International RAC segment, total revenues for the third quarter were $702 million, down 4%, but were flat on a constant currency basis. Our business in Asia-Pacific continues to see solid growth in pricing growth, while our European business saw pricing improvements partially offset by weaker volume.

The implementation of new revenue and fleet management capabilities in our International segment is underway and we're investing in growth and service initiatives that will drive better results in International. The International RAC segment reported adjusted EBITDA of $115 million, down 18% versus the prior year. The adjusted EBITDA results were driven primarily by higher vehicle related costs and flat revenue.

I'd like to provide an update on some of our financing activities and free cash flow. On our last call, we mentioned that we completed our highly successful rights offering in July, raising $750 million, and in August, we issued $500 million of unsecured senior notes. The proceeds from those transactions were used to redeem $700 million of 2020 corporate debt maturities and refinance $500 million of 2021 maturities to 2026. As a result, we have no significant corporate debt maturities until June 2021.

Our corporate leverage, as measured by adjusted corporate EBITDA to net corporate debt, has declined 4 turns in the last 12 months to 5.1 times from 9.1 times. Our improved financial results and stronger balance sheet should enable us to lower both our vehicle and corporate financing costs in the future.

On the liquidity side, we ended the quarter with no drawings under our corporate senior revolving credit facility, with $860 million in corporate liquidity.

Now turning to cash flow, we expect continued improvement in overall cash flow through the remainder of the year as our fleet needs seasonally declined. We now expect full year 2019 adjusted free cash flow will be positive, driven primarily by the improvement in operating cash flow and favorable ABS fair market value marks on our US fleet, consistent with the strong residual value market this year.

So to wrap up, I recently celebrated my one year anniversary as the CFO at Hertz and I could not be more excited about the opportunity to help create a faster growing, higher-margin business. We still have work to do. We've made tremendous progress in growing the top line and driving margin expansion through productivity improvement. The growth initiatives are delivering and we're winning in [ph] new (00:15:55) marketplace as evidenced by the recent J.D. Power rankings.

And as we move forward into 2020, we will have a keen focus on four key areas: number one, growing the top line with investments in our brand, fleet, products and services; two, driving margin expansion through productivity initiatives; three, disciplined fleet management to drive asset utilizations; and four, innovation that will enable growth, expansion into new markets and further improvements in cost and productivity.

We believe these are the right catalysts to drive improved shareholder returns and I look forward to updating you on our future progress in our – in future quarters.

With that, I'll turn it back over to the operator for questions. Operator?

# QUESTION AND ANSWER SECTION

**Operator**: Ladies and gentlemen, we'll now begin the question-and-answer session of today's conference. [Operator Instructions] Our first question will come from the line of Chris Woronka of Deutsche Bank. Please go ahead.

Chris Woronka
*Analyst, Deutsche Bank Securities, Inc.*
Q

Hey. Good morning, everyone, and congratulations on another very solid quarter. Wanted to ask a little bit about the ramp up of the, I guess, last mile delivery service. And I guess what kind of inning do you think that's in for you guys as a company, and could that expand beyond some of the local delivery? Kind of how much of an investment are you willing to make in that?

Kathryn V. Marinello
*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*
A

Well, we see it as a really significant opportunity and it dovetails nicely with the abilities we have in our corporate fleet management along with what we can do from a direct-to-consumer rental perspective. So we have thousands of locations around the country. We have a really great fleet management company. And we've signed hundreds of contracts with the Amazon DSP providers and that, frankly, we can't get enough vans. We fleeted up towards the end of the third quarter for this business. We continue to get great demand. We get good margins from it. And we just think it's a natural adjunct to what we've been doing in our TNC space as well as corporate fleet management, leveraging great assets in the rental car space.

Chris Woronka
*Analyst, Deutsche Bank Securities, Inc.*
Q

Okay, very good. And then maybe on the retail strategy, obviously, it's paid a lot of dividends for you so far. Kind of along the same lines, how do you kind of maybe internally underwrite the growth there? How much of that do you want the total business to become? I guess trying to think about it in the context of sizable raw fleet and you mentioned doing things beyond just reselling your core rental cars.

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**Kathryn V. Marinello**
*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*
A

I think if you look at how mobility is changing, and I think mobility is a little overused, but the demand on vehicles, particularly for last mile delivery and the distribution assets that we have, the retail car sales assets that we have, the corporate fleet business that we have, and thousands of locations that [ph] we kind of (00:19:21) think about 90% of the time within 15 minutes can reach a consumer, there's enormous upside for us to move into outside of the traditional – be at the airports growth. So I think we've got a lot of leverage still in our Hertz Local Edition and we've begun to expand what we do out of those locations.

So I think that could be a business double its current size with expanding more around deliveries and more affordable opportunities for TNC drivers. So I think we look at – if you look at the growth we've have already experienced in the TNC space, which was really incredibly rapid, because I think we've got a great product, we've got great process around it and it delivers good margins, we're seeing the same kind of opportunities in the last mile delivery space.

So I think we've just started and it's very early innings in both of those spaces. So I'd like to see more diversity and we're moving towards that and making investments towards that from our large corporate fleet business, our ride-hailing business, our last mile delivery in addition to our traditional consumer rental car business.

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**Jamere Jackson**
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*
A

Yeah. And specifically as it relates to retail car sales, I mean we've been very vocal about the fact that we are a top 10 used car dealer. If you're looking at it on a standalone basis, we've built tremendous capability inside the organization. We have a world class sales team. We're investing in our web-based capabilities. And if you look at the growth that we've had in locations, in same-store sales growth, we do think there's opportunity for us to grow beyond just the dispositions of our rental fleet. And it is something that as we look at our strategic plan over the next few years or so that we'll be exploring in more detail.

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**Chris Woronka**
*Analyst, Deutsche Bank Securities, Inc.*
Q

[ph] Right. (00:21:20)

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**Chris Woronka**
*Analyst, Deutsche Bank Securities, Inc.*
Q

Yeah. I think we've got early innings there and we've developed great online capabilities and payment capabilities, so there's a lot of opportunity in that space alone. I think 88 locations, we've clearly done a decent job of expanding quickly just based on our own volumes, but there's a lot more cars out there to sell.

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**Operator**: Brian Johnson, Barclays. Please go ahead.

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**Brian A. Johnson**
*Analyst, Barclays Capital, Inc.*
Q

Thank you. I want to drill down into some of the cost lines. Let's start with SG&A, in particular. If I look at the two segments, it was basically flat year-over-year despite rising revenues. Corporate came down as well. I forget how much of that is adjusted out. So can you kind of – you talked about some of the cost controls yet investing in service. Could you give us a feel for trajectory of SG&A over the next couple of years, given your initiatives? As well as within that, how much of the IT spend is still in the adjusted numbers and then in the overall numbers?

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### Jamere Jackson
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*

A

Yeah. So from an SG&A standpoint, it's part of our overall productivity initiatives. We are running the productivity play inside the company with real intensity and you saw that this quarter, as we look at DOE and SG&A combined, it's literally flat year-over-year, while our revenue was growing 4% on a constant currency basis.

As we've said before on previous calls, we see opportunities really across the organization, everything from the way that we're staffing certain functions to opportunities in procurement, to opportunities in working with third-party vendors, and we're making tremendous progress there. As we look at our plans over the next two to three years or so, what I'll say to you is our commitment is to grow DOE and SG&A at a slower rate than the top line, and that should give us nice operating leverage as we move forward.

As it relates to the technology investments, we've made really good progress, as Kathy alluded to on the call this morning. We still have some investments to make on our integrated platform. But what you'll see going forward is that the things that we're working on from a productivity standpoint will essentially be the bill payers for the investments that we are making. That's a much healthier place for us to be as a company.

So we feel good about where we are. It is another leg to the stool that we've added to drive our results and you're seeing it as we get operating leverage this quarter and in future quarters as well.

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### Kathryn V. Marinello
*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*

A

Yeah. I think one of the benefits of the technology upgrades has been, we have been looking at the process before we put it on the new technology. And as a result, our operations leaders have really done a great job building great new process into the new technology. And I think if you look at what we've been able to accomplish despite waiting for some of these improvements to come in, winning the J.D. Power Award is a significant evidence of we're getting the process right, regardless of the technology investments.

So I think as we just launched the fleet module of our integrated platform, they're already seeing great opportunities in fleet management, maintenance, and just how to get the cars quicker to the customers as they come in. So we're pretty excited about the future productivity as we – every time we get a new module and most of it has been helping us in our top line, now we're starting to see technology coming in that'll help us in our productivity.

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### Brian A. Johnson
*Analyst, Barclays Capital, Inc.*

Q

And follow-up on the fleet cost side, if auction values, which is, of course, the measure [ph] we see (00:25:14) publicly, [ph] whether it'd (00:25:14) be flat or down 1%, where would your fleet costs go? I guess underneath that, as we'll see in the Q, how much gain on sales were there? And then, how much of sort of just mild inflation in used car can you continue to offset for your channel strategy?

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Jamere Jackson
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*

A

Yeah. So as you know, that's a little nuanced when you look at sort of what happens with auction value. Sometimes that does not necessarily reflect what we're actually experiencing in our fleet. The good news with what we've done with our disposition strategy is we've actually moved the lion's share of our disposition strategy through either direct to dealer or, as I mentioned earlier, to retail car sales. And that actually gives us a significant advantage versus what you see in auctions.

What I'll say to you is that the initiatives that we've put in place around building a better fleet, all taken into account, not only the demand that we see in the rental car business but it also takes in account what we expect to see in residual values and how we expect the disposition cars either through the TNC fleet or through auction or through direct to dealer or through retail. And so all of those things will be the drivers for what we ultimately see in terms of the financial results on our business.

So, the strategy that we have in place is geared towards managing the entire lifecycle of the car and we do that with the notion of maximizing residual values really wherever we are in the cycle.

**Operator**: Michael Millman, Millman Research. Please go ahead.

Michael Millman
*Analyst, Millman Research*

Q

Thank you. You didn't talk about pricing. Avis the other day talked about how pricing seemed to at the end of October take a jump up and the fourth quarter looked very strong. And they also mentioned that for the first time in 11 quarters, there was a price increase internationally. And so I was wondering if you were seeing those, and to what extent, you're seeing those things?

Jamere Jackson
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*

A

We were pretty pleased with our results in the US from a pricing standpoint. As I said in my prepared comments that excluding TNC, we actually saw price up 2%, which was pretty strong given the environment that we're in. I would also say that as I look at the early results coming back from our October results here, pricing looks fairly strong during the month of October. I think fleets are tightening as we typically see in the fourth quarter of the year and we expect to see some pretty good yielding opportunities out there.

And then in terms of the International market, what we also saw is we saw pricing in both Europe and APAC. APAC is actually seeing volume growth and pricing, which is a big contributor to our results. The volumes scenario in Europe has been a little bit softer, just given some of the market dynamics and the macro dynamics there. But, overall, we are seeing some improvement in the International markets in pricing.

What we've said inside the company is that driving price is our number one priority. It's the most efficient way for us to build both the top line and the margin at the same time. We've invested in very sophisticated revenue management capabilities. We talked about the investments that we made in AI and machine-learning and predictive analytics. Those things are paying huge dividends for us in the US and we're starting to implement those capabilities outside the US as well. And we like the things that we've done with the fleet and those things are helping us to drive price inside the business.

Michael Millman
*Analyst, Millman Research*

Q

When do think that you'll be operating sort of on a normal basis, where most of the major improvements already incorporated? So it's next 12 months or is it continue sort of forever, it's the way of modern operations?

Kathryn V. Marinello
*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*

A

I think it's evidence of our winning the J.D. Power Award for the best service in the rental cars space that we exceeded, I would say, there's some industry positive in that. We had a 2% ex-TNC price growth on top of volume. I think given we've had eight consecutive quarters of EBITDA growth and expansion and nine of top line growth, we're doing it the right way.

We're delivering productivity and improved DOE and SG&A as a percent of revenue. Our fleet expense is down to, I would say, industry best averages and we continue to have all the foundations in place to drive that.

So, I think every company is constantly – it's not a destination. You constantly are expanding your margins, improving your process, innovating to create new opportunities. I think one of the things we've been able to do is consistently put in foundational capabilities that drive growth or EBITDA growth the right way through top line growth with controlled expenses.

At the same time, we've been investing and upgrading in our technology so we can manage and take advantage of things like connected cars and telematics. We've expanded into new opportunities like TNC and last mile delivery. And so I think we've got all of the gears hitting high-speed, full speed ahead, but again we're disciplined. And that's why we've been able to drive consistent EBITDA growth over eight quarters.

**Operator**: Adam Jonas, Morgan Stanley. Please go ahead.

Adam Michael Jonas
*Analyst, Morgan Stanley & Co. LLC*

Q

Thanks, everybody. Just one question and one follow-up. The first is can you confirm that you don't – how many electric vehicles, I mean, pure battery EVs, are in the US fleet right now?

Kathryn V. Marinello
*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*

A

Candidly, we don't have – I don't have the exact number, but it is not significant and that there's two issues with it.

Adam Michael Jonas
*Analyst, Morgan Stanley & Co. LLC*

Q

Yeah.

Kathryn V. Marinello
*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*

A

The ones we have, customers don't want to drive because they are concerned where do they plug them and to charge them. Generally speaking, people are going to a place they don't have a car, they're not familiar with and so they're not really comfortable looking at electric vehicles.

However, to your question, we're very interested around when we get into last mile delivery, from an economics and an environmental perspective, we are in discussions with one of the OEMs on electric vehicles and how we can get more electric vans for our DSP drivers. So I think that scenario where we expect to grow the fleet is just really tough. Consumers are afraid to rent electric cars in places they're not familiar with.

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Adam Michael Jonas
*Analyst, Morgan Stanley & Co. LLC*
Q

That makes a lot of sense, Kathy. Thanks for that, and just one follow-up. What can you tell us about the credit quality or just anything regarding the creditworthiness or financial wherewithal of the typical TNC driver, because some investors are out there thinking, if you're already in the gig economy and you don't have your own ride, it might skew more distress. And I'm just wondering what you can tell us about that. Thanks.

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Kathryn V. Marinello
*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*
A

Well, I think it's actually a better solution to some of the things these people might be getting into making a big investment in a car and then finding out that they don't have the chops or they're not – where they are, they're not able to generate the revenue. I think as you know, it's a really tough part for these drivers. You've got to put in a lot of hours. There is an expense around the car. I think we're a perfect solution where it's a great way to enter in. And plus, if you look at the low cost of the car, the maintenance that we provide, I think all in, we're a much more cost-effective solution for drivers than them going out on their own and dealing with their wrong car purchase, car sales and car maintenance.

So, I think if anything, we help that environment and we improve the likelihood of success of these drivers. I mean when I – on occasion, if I'm in an Uber, I ask them questions and they right away know Hertz and what we're doing and they think it's a really big help to get people started in this industry.

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**Operator**: Ryan Brinkman, JPMorgan. Please go ahead.

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Ryan Brinkman
*Analyst, JPMorgan Securities LLC*
Q

Great. Thanks for taking my question. Can you help us to maybe just think about how much of the benefit to lower per unit fleet cost in 2019 is, on the one hand, a function of lower prospective rates of depreciation that should be sustainable? Should residuals play out as you now expect or, I don't know, maybe stems from your disposition strategy, which can continue to help more versus how much maybe stems on the other hand from like a one-time benefit to gain on sale from unexpectedly higher auction prices that wouldn't be expected to continue even if the used car prices do continue at this level?

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Jamere Jackson
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*
A

As we've talked about, as it relates to depreciation overall, it's really nuanced. I mean, obviously, all of the things that we're doing inside the company, as it relates to disciplined fleet management, making sure that we have the right number of cars, making sure that we buy cars that not only our consumers want to rent but with an eye towards what are the residual values in the back end, the disposition strategy that we have moving vehicles through alternative channels, those are all things that are really, really important to making sure that we get the best outcome on depreciation. And obviously, the strength in residual values in the marketplace sort of help that. So, in any cycle, in any environment, we need to have that base level of capabilities to make sure that you maximize your outcomes on depreciation.

So while we are helped, obviously, by a strong residual value market, the fact that we're executing really well in terms of procurement, disposition and making sure that we buy the right fleet that has demand when it comes out of the rental market is important.

So, again, I think the most important thing that we've done is we've done our acquisition of the fleet with an eye towards the lifecycle of the vehicle. And some vehicles we're buying, we have an eye towards putting them into the TNC fleet, which helps us bend the depreciation curve in the latter months. And all of those things working together help us drive the best possible outcomes on vehicle depreciation, and our teams are executing well.

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Kathryn V. Marinello
*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*
A

And we have an amazing group of people and vehicle acquisitions. And every year, we actually get like-for-life vehicles at a lower cost, even though we have seen residual values up based on how we buy, we tend to get a price decrease every year. And the vehicles are of better quality with more of the things that consumers want in their cars when they're renting a car as well as when they're buying them.

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Ryan Brinkman
*Analyst, JPMorgan Securities LLC*
Q

Okay. Thanks. That's helpful color. And then, just lastly, I'm curious to if you have any thoughts on the impact to the industry from – in Europe, the transition next year to a more stringent grams of $CO_2$ per kilometer standard. Some observers expect this to increase the prices of new vehicles in Europe or restrict the types that can be sold. Just curious if you thought that that is something that might have potentially an impact.

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Jamere Jackson
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*
A

Yeah, the regulatory environment is getting tougher there. And we are starting to feel the impact of some of that in some of our vehicle cost today. I think the industry will be disciplined in terms of how we think about procuring vehicles and the price that we need to get moving forward to able to make the business be profitable but there is no question that it is a tougher regulatory environment there and the entire industry's faced with it and I think we're all focused on dealing with it in a very disciplined way moving forward

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Ryan Brinkman
*Analyst, JPMorgan Securities LLC*
Q

Yeah. Seems like there could to be some potential offsets if new vehicles cost more that could provide upward pressure on used vehicle, you're in 1% on the total revenue. Just curious if there is – if it's primarily a headwind or there could potentially be tailwinds also, or it makes vehicles more affordable, people need the rent them instead of own, et cetera. I'm not sure.

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Jamere Jackson
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*
A

So, clearly, the puts and takes, and some of the dynamics that you alluded to certainly point out that there may be some opportunities. We'll just have to see. I mean these things take time to sort of work their way through the system, and you have to understand what consumer behavior is actually going to be. But what I can tell you is that the market tends to be pretty resilient and consumers in the industry sort of adapt to the regulatory environment, and you see things sort of normalizes as you move forward in time. But in the short-term a lots of things that are happening from a regulatory standpoint that we have to consider as we move forward in our business.

**Operator**: We have a question from the line of Yilma Abebe of JPMorgan Please go ahead

Yilma Abebe
*Analyst, JPMorgan Securities LLC*
Q

Thank you. A couple of questions for me. I guess, firstly, as you look into [ph] medium term (00:39:12) and near term here, what's your leverage target? And I guess as you move forward, what's the right leverage level for the business? Especially in the context of potential macro slowdown, would you expect to go into some sort of a recessionary environment with much lower leverage than you have right now? And what's the corporate ratings category in that sort of a scenario? That's the first question.

The second question is related to sort of the free cash flow, the sustained free cash flow earnings power of the business. In your 2019 expectations, how much of a one-time expenses are embedded in there that are expected to drop off in 2020 and beyond?

Jamere Jackson
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*
A

Yeah. So on the first question as it relates to leverage, we're comfortable running the business in the 3 times area. That gives us tremendous financial firepower to grow the business in a disciplined way and also make really smart investment decisions going forward. So, we're comfortable running the business in that area.

The second thing that I will say as it relates to free cash flow is our free cash flow is a fully loaded number that does include the investments. We'll start to see some of those investments that we're making, particularly in some of the technology things, sort of roll off and the free cash flow earnings power of the business actually starts to accelerate as we move through 2020.

But, however, what I'll say to you is that the most important thing and the most efficient way for us to grow our earnings and our cash flow is to do exactly the things that we've been doing, which is grow the top line in a disciplined way, manage our operating expenses and our SG&A to grow slower than revenue and to drive productivity improvements really across the business. And those will be the big drivers that drive our free cash flow capabilities going forward.

So – and I like the capabilities that we've built in the company. We are strengthening the balance sheet with some of the actions that we've taken this year. Those things are going to help us lower our borrowing cost both on cars and corporate debt in the future. And those things will give us the ability to drive meaningful free cash flow improvement as we move forward.

Yilma Abebe
*Analyst, JPMorgan Securities LLC*
Q

Thank you. And then, I guess, maybe a quick follow-up. In the 2019 expectations, are you able to share a number in terms of one-time expenses that are embedded in that expectation?

Jamere Jackson
*Executive Vice President and Chief Financial Officer, Hertz Global Holdings, Inc.*
A

So we haven't broken out sort of what the one timers are in the expectation. So what I'll say is that we have a scenario where we'll get the free cash flow positive this year. We've talked about the investments that we're making in technology, some of which are actually being offset by the productivity improvements. And then, as we move into next year, the opportunity for us to lower the amount of things that we're doing from a development standpoint on technology and drive additional productivity will give us a much more positive free cash flow scenario in 2020.

**Operator**: And ladies and gentlemen in the panel, there are no further questions in queue at this time.

## Kathryn V. Marinello

*President, Chief Executive Officer & Director, Hertz Global Holdings, Inc.*

Thank you for joining the call today and have a great day.

**Operator**: Ladies and gentlemen, that does conclude our conference call for today. On behalf of today's panel, we'd like to thank you for your participation in today's Hertz Global Holdings Teleconference call. Thank you for using our service. Have a wonderful day. You may now disconnect.