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RYDER SYSTEM INC (R) Earnings Report: Q1 2016 Conference Call Transcript

The following RYDER SYSTEM INC conference call took place on April 26, 2016, 11:00 AM ET. This is a transcript of that earnings call:

Company Participants

- Bob Brunn; Ryder System Inc; Investor Relations
- Robert Sanchez; Ryder System Inc Chairman; President & CEO
- Art Garcia; Ryder System Inc; CFO
- Dennis Cooke; Ryder System Inc; President Global Fleet Management Solutions
- John Diez; Ryder System Inc; President of Dedicated Transportation Solutions

Other Participants

- David Ross; Stifel Nicolaus; Analyst
- Jeff Kauffman; Buckingham Research Group; Analyst
- Ben Hartford; Robert W. Baird & Company Inc.; Analyst
- Scott Group; Wolfe Research; Analyst
- John Barnes; RBC Capital Markets; Analyst
- Justin Long; Stephens Inc.; Analyst
- Art Hatfield; Raymond James & Associates Inc.; Analyst
- Matt Brooklier; Longbow Research; Analyst
- Todd Fowler; KeyBanc Capital Markets; Analyst
- Casey Deak; Wells Fargo Securities; Analyst
- Brian Ossenbeck; JPMorgan; Analyst

MANAGEMENT DISCUSSION SECTION

Operator:

Welcome to Ryder System Incorporated's first quarter 2016 earnings release conference call.

(Operator Instructions)

I would like to introduce Mr. Bob Brunn, Vice President, Corporate Strategy and Investor Relations for Ryder. Mr. Brunn, you may begin.

Bob Brunn (Investor Relations):

Thanks very much. Good morning. Welcome to Ryder's First Quarter 2016 earnings conference call.

I'd like to remind you that during this presentation you'll hear some forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are based on Management's current expectations and are subject to uncertainty and changes in circumstances.

Actual results may differ materially from these expectations due to changes in economic, business, competitive, market, political and regulatory factors. More detailed information about these factors is contained in this morning's Earnings Release and in Ryder's filings with the Securities and Exchange Commission.

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Presenting on today's call are Robert Sanchez, Chairman and Chief Executive Officer, and Art Garcia, Executive Vice President and Chief Financial Officer. Additionally Dennis Cooke, President of Global Fleet Management Solutions; John Diez, President of Dedicated Transportation Solutions; and Steve Sensing, President of Global Supply Chain Solutions are on the call today and available for questions following the presentation.

Before we get into our results, I'd like to remind everybody that Ryder will be holding our first Investor Day on Thursday, May 19 in New York from 8.30 a.m. to 1.30 p.m. The day will consist of presentations and Q&A with our CEO, CFO, Division Presidents and Chief Marketing Officer. We're also hosting a solutions showcase that will provide a more in depth look at some of the products and services driving our long term profitable growth strategy and a chance to interact with a broad group of Ryder officers and product leaders.

Please note that advance registration is required to attend and space is limited. If you're not already registered and are interested attending in person please send an e-mail to me or to ryderforinvestor@ryder.com. The event will also be webcast live and available for replay if you're unable to make it that day. Additional details about the Investor Day can be found on our IR website at investors.ryder.com.

With that, let me turn it over to Robert.

Robert Sanchez (President & CEO):

Good morning, everyone, and thanks for joining us. This morning we will recap our First Quarter 2016 results, review the Asset Management area, and discuss the current outlook for our business. Then we will open the call for questions. With that let's turn to an overview of our First Quarter results.

Comparable earnings per share from continuing operations were $1.12 for the First Quarter 2016 up 4% from the prior year. Comparable results were above our forecast range of $1.03 to $1.08 due to better than planned rental demand and used vehicle prices. First quarter comparable results exclude $0.07 of non-operating pension costs in 2016 and $0.06 in the prior year. 2015 comparable earnings also exclude $0.02 in professional fees.

Operating revenue, which excludes fuel and subcontracted transportation revenue, grew by 8% to a record $1.4 billion for the First Quarter and was higher in all business segments. Excluding the impact of foreign exchange, operating revenue grew by 9%. Total revenue increased by 4% and was impacted by lower fuel cost passed through to customers. Page 5 includes some additional financial information for the First Quarter.

The average number of diluted shares outstanding for the quarter increased to 53.4 million shares up from 53.1 million shares last year. We expect to begin repurchasing shares under our previously announced 2 million share anti-dilutive repurchase program in the second quarter -- earlier than previously anticipated.

The plan allows Management to purchase up to 1.5 million shares issued to employees after December 1, 2015 and another 500,000 shares from the former plan that were not repurchased prior to expiration. Excluding pension costs and other items, the comparable tax rate was 37.1%, consistent with the prior year. I'll turn now to Page 6 and discuss key trends we saw in the business segments during the quarter.

Fleet Management Solutions' operating revenue, which excludes fuel grew 7% driven mainly by growth in full-service lease. Excluding the impact of foreign exchange, FMS operating revenue was up 8%. Full service lease revenue increased 8% due to fleet growth and higher rate on replacement vehicles reflecting the higher cost of new engine technology.

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The lease we grew organically by 6,500 vehicles year-over-year excluding the impact from the planned reduction of UK trailers. Sequentially the lease we'd increase by 1,700 vehicles excluding UK trailers. We continue to benefit from favorable outsourcing trends in our Sales and Marketing initiatives.

During the quarter, we were pleased to see that over 40% of our new lease sales came from customers new to outsourcing, up from about a 1/3 last year. Miles driven per vehicle per day on US lease power units were consistent with the prior year and continue to run at normal historical levels.

Contract maintenance revenue increased by 9%. The average contract maintenance fleet grew by 5,400 vehicles from the prior year and 2,700 units sequentially, reflecting a significant new customer win. Contract related maintenance revenue was up 21% from the prior year. Included in contract related maintenance are 7,100 vehicles serviced during quarter under On Demand maintenance agreements, an increase of 9% from the prior year.

Commercial rental revenue was flat for the quarter. Global rental demand was up by nearly 2% driven by higher truck demand partially offset by lower demand for tractors. Although higher than planned, rental demand was a driver of the product line's better than expected results, demand trends worsened through the quarter and April demand to date is lower than expected.

Global pricing was flat for the quarter due to higher pure rental rates offset by lower lease support rates. The average rental fleet grew by 2% from the prior year. The ending rental fleet was down by 5% or 2,000 vehicles sequentially from the Fourth Quarter consistent with our plan to position the rental fleet more conservatively for 2016 in light of softer expected demand conditions.

Rental utilization on power units was 70.4% down 300 basis points year-over-year but still at a solid level for the seasonally low First Quarter. Rental utilization was adversely impacted as we carried a higher fleet level than normal during the First Quarter in order to maintain sufficient capacity for the peak rental season given significantly lower rental capital spending for new vehicles this year.

Although better than forecast, used vehicle results were down year-over-year due to lower pricing on tractors. I'll discuss those results separately in a few minutes. Overall, FMS earnings decreased due to lower used vehicle results, higher insurance costs and the lack of an unusual fuel benefit realized in the prior year partially offset by higher full service lease results.

Earnings before tax and FMS decreased 8%. FMS earnings as a percent of operating revenue were 8.6%, down 140 basis points from the prior year. Of this 140 basis points decline, 130 basis points was due to used vehicle sales. I'll turn now to dedicated transportation solutions on Page 7.

Operating and total revenue growth were strong at 15% due to new business, higher volumes and increased pricing. DTS earnings increased 59% due to higher operating revenue and lower insurance cost. Segment earnings before taxes as a percent of operating revenue were 7.5% up 210 basis points from the prior year. I'll turn now to Supply Chain solutions on Page 8.

Operating revenue grew 9% or 11% excluding foreign exchange due to new business, increased volumes and higher pricing. Total revenue was up 5% as higher operating revenue was partially offset by lower third party purchased transportation cost and lower fuel cost passed through to customers. SCS earnings before tax were up 26% due to operating revenue growth. Segment earnings before tax as a percent of operating revenue were 6.1% for the quarter up 80 basis points from the prior year.

Page 9 shows the business segment view of the Income Statement I just discussed and is included here for your reference. At this point I'll turn the call over to our CFO, Art Garcia, to cover several items including capital spending.

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Art Garcia (CFO):

Thanks, Robert.

Turning to Page 10, gross Capital Expenditures for the quarter were around $500 million, down $55 million for the prior year. This decrease reflects lower planned rental capital spending.

We realized proceeds primarily from the sale of revenue earning equipment of $121 million, that's up $24 million from the prior year. The increase primarily reflects higher planned sales volumes and increased truck pricing partially offset by lower tractor pricing. Overall, used vehicle pricing exceeded our expectations. Robert will cover that area in more detail next.

First quarter net Capital Expenditures decreased by $179 million to $377 million. Turning to the next page, we generated cash from operating activities of $365 million for the quarter, up $81 million. The increase was driven primarily by higher cash based earnings and lower working capital needs. We generated $511 million of total cash during the year, up $114 million from the prior year reflecting higher operating cash and sales proceeds.

Cash payments for Capital Expenditures increased by $22 million to $575 million. Free Cash Flow for the quarter was negative $64 million, that's $92 million better then the prior year. Our full year Free Cash Flow forecast remains at a positive $100 million.

Page 12 addresses our debt to equity position. Total debt of $5.6 billion increased by $97 million from the prior year. Debt to equity at the end of the First Quarter decreased to 274% from 277% at the end of 2015 and is within our target range of 225% to 275%. We expect our balance sheet leverage to come down a bit more quickly than planned and as a result expect to resume anti-dilutive share repurchases in the Second Quarter.

Equity at the end of the quarter was just over $2 billion. That's up around $60 million from year-end 2015 primarily due to earnings, partially offset by dividends. Before I hand it back to Robert I want to highlight one reporting change we made starting this quarter. Gains on vehicle sales on the P&L are now being shown net of valuation adjustments that previously had been included in depreciation and reported in other operating expenses.

Valuation adjustments are made when a vehicle is moved to the used truck center if its book value is above recent sales prices, and therefore a loss is expected at the time of sale. Including this adjustment in the reported gains line provides a better picture of gains net of losses on vehicles to be sold. A table with quarterly history for the past five years under this approach is included on Page 19 in the appendix. At this point I'll hand the call back over to Robert to provide an Asset Management update.

Robert Sanchez (President & CEO):

Thanks, Art. Page 14 summarizes key results from our Asset Management area. Used vehicle inventory held for sale was 8,600 vehicles, up from 5,800 vehicles in the prior year and up sequentially by 600 vehicles. This is above the high end of our target range of 6,000 to 8,000 but consistent with our forecast.

Higher used vehicle inventory levels reflect our decision to downsize the rental fleet in order to position it more conservatively for 2016. We expect inventory levels to decline over the next few quarters and we should end 2016 closer to the bottom end of our target range. We sold 4,700 used vehicles during the quarter up 9% from the prior year and up 4% sequentially. Used vehicle pricing declined by somewhat less than we had initially forecast for the quarter.

Although pricing conditions are still relatively weak, the rate of price decline slowed as the quarter progressed. Proceeds from vehicles sold were down 8% for tractors and up 6% for trucks compared to the

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prior year. From a sequential standpoint, tractor pricing was unchanged and truck pricing was up 8% versus the Fourth Quarter of 2015.

As compared to peak prices realized in the Second Quarter of 2015, overall used vehicle prices for power units were down 5% as compared to our expectation of down 9%. This is driven primarily by used tractor pricing, which was down 12% from the Second Quarter peak partially offset by truck pricing which was up 2%.

The number of leased vehicles that were extended beyond their original lease term increased versus last year by around 400 units or 30% during the quarter, although still below recessionary levels. The increase was driven by activity with two specific customers.

The vehicles redeployed into other applications increased by almost 500 unit or 76%. This reflects our actions to put excess rental vehicles into lease contracts as we downsize the rental fleet. Early termination of lease vehicles decreased by 450 units this year, and weÕre below levels seen over the past six years. I'll turn now to Page 16 and cover our outlook for 2016.

During the first quarter we delivered profitable growth as strong performance in our contractual businesses and cost actions taken early in the year helped us offset a challenging environment in used vehicle sales and rental. We generated strong revenue growth in all business segments driven by growth in our contractual product lines. We're particularly encouraged by continued momentum in new sales contracts signed across all business segments.

In full service lease we grew the fleet by 1,700 vehicles sequentially and our full year plan remains at 3,500 vehicles. Our outlook anticipates slower fleet growth in the second half of the year due to new vehicle production declines at OEMs and generally soft rate conditions; however, this trend has not materialized yet, as we continue to see strong lease sales and strong new business pipeline during the quarter. We're also pleased that over 40% of our new lease trucks added during the quarter came from customers outsourcing for the first time.

In rental we reached our planned goal to downsize the fleet by 5% or 2,000 units by the end of the quarter. Although we saw better than expected rental demand during the First Quarter, April to date demand was lower than expected particularly with tractors. As a result we expect Second Quarter rental results to be below our initial forecast and are further reducing fleet size.

We now expect our full year average rental fleet to decline by 7% versus our prior forecast of 4%. This also -- we also expect rental pricing to be flat. We continue to focus on vehicle redeployment, especially into lease and dedicated as a strategy to deflate rental without needing to sell as many units.

In our asset light maintenance products we're pleased with the strong growth in contract maintenance and continued market interest in our On Demand maintenance service. We are emphasizing growth in these products as a way to drive revenue and earnings with no capital investment required.

In used vehicle sales pricing was stronger than we anticipated during quarter but market conditions remain soft. Based on recent activity including strong sales volumes in March and into April, we now expect used vehicle sales results to be slightly better than our original forecast for the balance of the year. We expect inventory levels to decline going forward and end the year at the lower end of our target range at around 6,500 vehicles.

In Supply Chain we continue to expect mid single digits operating revenue growth based on strong sales activity. In dedicated we expect high single digit revenue growth for the year with the successful upselling of full service lease customers to dedicated continuing to be a key growth driver. Earnings comparisons in dedicated are expected to benefit from new sales and lower self-insurance expense.

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Our Second Quarter comparable EPS forecast is $1.50 to $1.55 versus our prior year of $1.65. This reflects weaker year-over-year performance in rental and used vehicle sales. Used vehicle sales comparison will be the most unfavorable in the Second Quarter as used vehicle pricing peaked in the Second Quarter of last year.

Due to ongoing uncertainty in rental and used vehicle sales, we're maintaining our full year EPS forecast range of $6.10 to $6.30, a flat to modest increase from the prior year. As the strength in our contractual businesses mitigates weakness with transactional products, we also plan to begin anti-dilutive share repurchase activity in the Second Quarter, earlier than previously expected.

That concludes our prepared remarks for this morning.

At this time, I'll turn it over to the operator to open up the line for questions.

In order to give everyone an opportunity, please limit yourself to one question and one related follow-up if clarification is needed. If you have additional questions, you're welcome to get back in the queue and we'll take as many calls as we can.

QUESTIONS & ANSWERS

Operator:

(Operator Instructions)

David Ross with Stifel Nicolaus.

Robert Sanchez (President & CEO):

Hello, David?

David Ross (Analyst - Stifel Nicolaus):

Hello?

Robert Sanchez (President & CEO):

Yes, we hear you David.

David Ross (Analyst - Stifel Nicolaus):

Oh, sorry. Used trucks. It seems like the trucks are outperforming the tractors in the used market. Is there a reason for why this is happening?

Robert Sanchez (President & CEO):

Well David, I think you've got to think back to some of the dynamics that we feel is driving the tractor pricing down. First and foremost there is some softness in general around tractor, you'll see it even in our rental fleet.

There's also the strong dollar really impacting some of the offshore sales that were happening across the industry, which now the dollar's coming down a little bit so that might turnaround but still that impacts tractors more that I think more tractors are being offshored. And then you had the issue around the 2011 and 2012 Navistars that came into the market. Those were primarily tractors also, which really created some pricing pressure and I think that's -- it's the combination of those things that's probably more heavily weighting the tractor issue than the straight truck issue.

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David Ross (Analyst - Stifel Nicolaus):

And are the new contracts that you're signing up for leasing more for trucks or more for tractors?

Robert Sanchez (President & CEO):

I don't know, Dennis, I think it's consistent with what we've done historically right?

Dennis Cooke (President Global Fleet Management Solutions):

There's no real trend for one being heavier than the other, its been consistent with what we've historically seen, David.

David Ross (Analyst - Stifel Nicolaus):

And last follow-up there, are there better returns on a tractor contract on average versus a truck contract?

Robert Sanchez (President & CEO):

We really target a similar return in terms of return on capital over our cost of capital really on both of them.

David Ross (Analyst - Stifel Nicolaus):

Excellent. Thanks.

Operator:

Jeff Kauffman with Buckingham Research.

Jeff Kauffman (Analyst - Buckingham Research Group):

Thank you. Good morning. I just wanted to focus a little bit more on the Supply Chain and dedicated divisions. That was really a nice surprise on the margins. You noticed or you noted improved customer wins and lower insurance costs.

I guess are you saying we're at a sustained level of profitability, and if I look at the jump in the improvement in earnings how much of this is more top line and operating driven versus lower insurance cost driven?

Art Garcia (CFO):

I think if you look at DTS , the year-over-year improves about half and half right? About half of it came from insurance and the other half I would say is operational, so if you look at 60% year-over-year earnings growth is not what we would expect for the full year, but we are expecting a pretty meaningful increase year-over-year in earnings overall and a top line growth of high single digits, again with the margins really expanding from last year pretty meaningfully.

Jeff Kauffman (Analyst - Buckingham Research Group):

Okay, and with respect to Supply Chain?

Robert Sanchez (President & CEO):

Supply Chain, I think what we said there is that what he's getting a benefit from is volumes and higher pricing and some of the new business. The pricing will catch its tail here in the next quarter and that's

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why we're going to see growth instead of at that 9%, probably looking at mid single digits but again still earnings expansion year-over-year is what we're expecting also.

Again remember if you just step back it's the contractual business. It's not just full service lease but dedicated and Supply Chain that we're really looking to help us offset the weakness in transactional and that's what we saw some of that materializing here in the First Quarter. Okay, guys, congratulations and thank you. Thanks, Jeff.

Operator:

Thank you, the next question is from the line of Ben Hartford of Robert W. Baird.

Ben Hartford (Analyst - Robert W. Baird & Company Inc.):

Hello, Robert.

Robert Sanchez (President & CEO):

Hi, Ben.

Ben Hartford (Analyst - Robert W. Baird & Company Inc.):

A question on FMS margins, its gotten deeper into this year, trends have been a little bit more challenging, the outlook pressured. How do you feel about FMS margins and the ability to drive leverage. I know we've talked about that in the past, but given some of the puts and takes we've seen here year-to-date but still continued growth with some of these contractual products. How confident are you that we will see better peak margins in FMS going forward?

Robert Sanchez (President & CEO):

I'm still confident we'll get back to that 12 to13% range. Obviously with the headwind that we have particularly on the used truck side, right? Because used truck gains really put a lot of pressure on that metric, but as we get past this year and we start looking out into the next year or so I would expect us to really start moving back into that range of the 12 to13% and longer term, as we can really pick up some additional growth in the contractual businesses and the asset light business then even an opportunity to get above that.

Ben Hartford (Analyst - Robert W. Baird & Company Inc.):

And can you remind us in terms of the 2016 outlook what it assumed in terms of used truck pricing declines from the peak maybe at the mid point and what do you posting now?

Robert Sanchez (President & CEO):

We probably the most important metric is tractors. We were assuming tractors would be down 20% from the peak. We're probably looking at a number now more like 16 to17% down from the peak, so that's really the benefit that we're kind of baking into the balance of the year, again it being offset by some of the headwinds in rental. And trucks are going to be doing a little better too.

Operator:

Scott Group of Wolfe Research.

Scott Group (Analyst - Wolfe Research):

Hello, guys, good morning. Just to clarify that last point, so you're assuming another 4% or so drop in used

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truck pricing in the guidance from current levels?

Art Garcia (CFO):

Correct, yes, about 4%.

Scott Group (Analyst - Wolfe Research):

Okay, so I wanted to just focus on rental. Can you just talk maybe about what -- how much demand in your mind was up or down in the First Quarter and then kind of what you're seeing now in April, and can you just, is there any color you can give us on end markets that you're seeing?

Robert Sanchez (President & CEO):

I'll just give you a brief summary of First Quarter. Demand was actually up slightly, they were up 2%, and it's primarily trucks being up, tractors being down and it blends to a 2% up. It did deteriorate throughout the quarter and in April we've seen it now down certainly below what we had originally estimated and down below that, so we are trying to forecast out what that's going to be for the balance of the year, but we're looking at that right now and we built in some additional decline. I think we're looking at a percent, how much we looking at down, about 8%?

Art Garcia (CFO):

Yes.

Robert Sanchez (President & CEO):

We're looking at about 8% down in demand year-over-year, is what we've got built in.

Scott Group (Analyst - Wolfe Research):

Sorry, just to be clear 8% down in April or now 8% down for the full year?

Robert Sanchez (President & CEO):

I'm sorry 7% down for the full year, for the full year.

Scott Group (Analyst - Wolfe Research):

Okay. And do you have a, can you say what you're seeing for April?

Art Garcia (CFO):

Down 8%?

Robert Sanchez (President & CEO):

About 8% down.

Art Garcia (CFO):

For power.

Scott Group (Analyst - Wolfe Research):

Okay, perfect. Thank you, guys.

Robert Sanchez (President & CEO):

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Thank you.

Operator:

John Barnes with RBC Capital Markets.

John Barnes (Analyst - RBC Capital Markets):

Hello, just hate to keep beating on the used truck thing, but can you talk a little bit about your forecast in terms of unit sales, just given the environment right now and slowdown in cost and orders on the new equipment side, are you seeing slowdown in used equipment demand as well? Is that part of the forecast as well?

Robert Sanchez (President & CEO):

I'm sorry, I missed the first part of the question. Are you referring to used vehicle sales?

John Barnes (Analyst - RBC Capital Markets):

Yes, so you're forecasting down on proceeds. Can you talk a little bit about the unit sales? The forecast on the unit side. Are you seeing weakness on the unit side?

Robert Sanchez (President & CEO):

No, no our forecast is actually for proceeds. They will be down year-over-year but they're going to be better than our previous forecast, and we are seeing, we saw unit volumes really pick up throughout the first quarter so ended up March with pretty good volume. And you can see our volume year-over-year, our volumes were up total, was it, 9%.

John Barnes (Analyst - RBC Capital Markets):

And you expect that to continue, I guess is what I'm asking?

Robert Sanchez (President & CEO):

Yes.

John Barnes (Analyst - RBC Capital Markets):

The strength of Q1 you anticipate continuing?

Robert Sanchez (President & CEO):

Yes, we do. We do expect that to continue. We're seeing it continue in April. I'll give you, I can tell you that.

John Barnes (Analyst - RBC Capital Markets):

Okay, very good, and then can you just talk a little bit about, you know, right now in this kind of environment where maybe it's a little bit more sluggish just what you're seeing from a sales channel perspective? I mean have you seen the sales pipeline as robust as it was in Q3 and Q4? Have you seen it moderate a little bit and have you seen any other factors that might have changed there, size of the lease deals being looked at in terms of units or is it taking longer to close a transaction, has there been any change there reflective of maybe a little bit more challenging environment?

Robert Sanchez (President & CEO):

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Yes, we're seeing a very strong pipeline really across all three segments, in terms of the volume of activity I'd say it hasn't really slowed down. I think there's probably been a little bit of a shift if you think about FSL, maybe some of the smaller deals are taking a little bit longer, but they're being offset by larger deals especially some of these new to outsourcing type customers. So all-in all I'd tell you the activity is strong across the three segments.

John Barnes (Analyst - RBC Capital Markets):

Very good, and nice quarter guys, thank you.

Robert Sanchez (President & CEO):

Thank you.

Operator:

Justin Long with Stephens.

Justin Long (Analyst - Stephens Inc.):

Thanks and good morning.

Robert Sanchez (President & CEO):

Good morning, Justin.

Justin Long (Analyst - Stephens Inc.):

So I wanted to ask what you would view as a worse case scenario for rental demand, and maybe one way to think about it would be that if you're assuming rental demand is down 7% this year what type of incremental decline in demand would get you to a recession scenario for that business?

Robert Sanchez (President & CEO):

That's the crystal ball question that's tough to answer. If you look back at what happened in 2009, 2009 was down 14%, so if you had a recurrence of a 2009 type scenario we would be down double what we're forecasting. Right now based on what we're seeing and where we think things are coming in, we're forecasting to 7% but that gives you an idea of what it could be.

I think the important thing to us is to be quickly right sizing the fleet, and if you think about we're down 2,000 units in the First Quarter, we're down 3,700 units already from the peak of the Third Quarter, so we're going to continue to bring that fleet down. By the end of the year, we'll be down another 1,500 units, and we should be at our target rate though in terms of the number of units in rental by end of the Second Quarter beginning of Third Quarter, so we're really trying to track demand as tightly as we can with the vehicles that we have in the fleet.

Justin Long (Analyst - Stephens Inc.):

That's really helpful and maybe to follow-up on that last point so for the full year, you said you expect to take the average rental fleet down 7%. I don't want to be pessimistic but let's just say rental demand is worse than your forecast. What's your flexibility to quickly react and maybe adjust the fleet down even more than that.

Robert Sanchez (President & CEO):

Well we're going to continue to really rely on redeployments into lease. We're up to 300 to 400 a month

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that we're doing and we're going to keep that ramped up, especially on tractors. I should step back, this is primarily a tractor issue right now so really stay focused on redeploying into lease.

It's helping our lease sales and we think that can continue going forward. So if you think about 300 to 400 a month going forward there's certainly capacity to keep bringing it down. Let me hand it over to Dennis to give you a little more color.

Dennis Cooke (President Global Fleet Management Solutions):

Justin, I just wanted to add that 2009 was down 14%, 2012 demand was down 1%. So we're somewhere in the middle and really we're positioned to handle either scenario, and that's what we want to make sure that we're prepared for. So if we got to deplete more, as Robert said, we're ready and if not, then we'll adjust and handle the demand by moving units that are coming off of lease that still have some life in them. We'll move that into the rental fleet if we need to.

Justin Long (Analyst - Stephens Inc.):

Sounds great. Thanks a lot for the time.

Operator:

Thank you, the next question is from Art Hatfield of Raymond James.

Art Hatfield (Analyst - Raymond James & Associates Inc.):

Hello, thanks for taking my questions this morning and good morning. Back to used trucks just real quick to get a good understanding, you mentioned it's 8,600 units held for sale. Typically in the past when you got above that 8,000 number you'd go to the wholesale market. I haven't heard you say that you're going to do that.

One, could you address that and also, is that group of assets kind of unusually skewed towards tractors at the moment?

Robert Sanchez (President & CEO):

Let me answer. You have 50 questions there. Once you get over 8,600, you're right, we do a little more wholesale. We did do in the quarter globally I think it was 65% retail, and in the US we're about 72% to 73%, so we have done a little bit more.

The reason we haven't ratcheted that up more is that we know what the fleet is coming in for the balance of the year and we believe we can handle that through enough retail and still get the fleet down to the low end of the target range by the end of the year. If we don't see that materializing we will obviously do more wholesaling, but we are trying to get as much money as we can for those vehicles.

In terms of the mix of tractors to straight trucks, I believe that there is probably more tractors than straight trucks, but I don't know the exact percentages. Do you have those, Dennis?

Dennis Cooke (President Global Fleet Management Solutions):

I will get the percentage right now.

Art Hatfield (Analyst - Raymond James & Associates Inc.):

And Dennis while you look that up if I can ask a follow-up, Robert. You've said, and I can't recall you mentioning it today, but in the past you've talked about historically these used truck cycles, these down cycles, lasting anywhere from four to eight quarters, I think if I recall correctly. Anything that you're

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seeing now that would indicate a different scenario, a more lengthy type of down cycle than we've seen in the past?

Robert Sanchez (President & CEO):

Yes, typically it's been four to six and considering we saw a bit of a leveling off here in the first quarter I would say probably not.

It's probably looking more like a four to six quarter event because who knows, anything could happen next quarter, but we're into our -- now we're into our Third Quarter of a slowing used truck market, and if it starts to level off a little bit we could be out of this in the four to six quarters that you normally see.

Dennis Cooke (President Global Fleet Management Solutions):

And Art following up for the quarter, 30% of the units sold were tractors, 50% were trucks and 20% trailers, and historically actually tractors were slightly higher percent on a volume basis, they were pretty much even year-over-year.

Art Hatfield (Analyst - Raymond James & Associates Inc.):

Great, thanks. That's a big help. Thank you.

Operator:

Matt Brooklier of Longbow Research.

Matt Brooklier (Analyst - Longbow Research):

Hello, thanks, good morning. Did you guys provide the number in terms of how many vehicles were serviced at On Demand maintenance and if you didn't, could you? And have your thoughts changed at all? I guess where did that come in relative to your expectations, and then have your thoughts changed at all in terms of On Demand's contribution to 2016 earnings?

Robert Sanchez (President & CEO):

No, it's in line with our expectations. I think as we mentioned in the Fourth Quarter, I think what we did learn I think in the third and Fourth Quarter is that it's taking us a little bit longer to get the vehicles into the shop once we have these signed contracts, but what came in the First Quarter really is in line with what we had built into the plan, and Dennis do you have something else?

Dennis Cooke (President Global Fleet Management Solutions):

Yes, I would just add that it's not only the sales of On Demand, it's we're talking to more customers and then we're able to oftentimes sell them up to other asset light contract maintenance products, and we found that to be very helpful.

Matt Brooklier (Analyst - Longbow Research):

And then just my second question, central support, the services, the overhead there, that was I think down on a year-over-year basis. I'm just curious to hear what drove that and if that's sustainable for the rest of the year.

Art Garcia (CFO):

Yes, I think overall we're expecting that number to trend up a little bit maybe from where we were in Q1, but generally to reflect some of the cost actions we've taken over the past few months.

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Matt Brooklier (Analyst - Longbow Research):

Okay, great thank you.

Operator:

Thank you, next question is from Todd Fowler of KeyBanc Capital Markets.

Todd Fowler (Analyst - KeyBanc Capital Markets):

Great thanks, good morning. Robert, I just wanted to make sure I understood some of the comments on the dedicated performance here in the quarter. It was obviously a good margin for the First Quarter and some improvement year-over-year, and I think that there were comments about part of that was from insurance. Was that related to good weather or was that something unusual on the insurance side? And I'm trying to get a sense of the sustainability of dedicated margins as you move through 2016?

Robert Sanchez (President & CEO):

Yes, that was a result of self-insurance activity. Some of that coming from prior year development.

Art Garcia (CFO):

Plus it's a comparisons to the prior year we had, we had some adverse development last year. We didn't really see those headwinds this year.

Todd Fowler (Analyst - KeyBanc Capital Markets):

Okay, so when I think about dedicated margins moving off of the First Quarter, should they continue to improve from these levels with some seasonality or is this kind of the run rate that they should be for the full year?

John Diez (President of Dedicated Transportation Solutions):

Todd, it's John Diez here. Typically, you do expect some up lift when you move from Q1 into Q2 and Q3 which are typically our stronger quarters, so we do expect that to continue in 2016 as we look forward.

Todd Fowler (Analyst - KeyBanc Capital Markets):

Okay, and then just for a follow-up, I might have missed this but did you give a number for gross CapEx and net CapEx for 2016? Did that change from the initial guidance?

Art Garcia (CFO):

No, we didn't change. We're sticking with the original forecast.

Todd Fowler (Analyst - KeyBanc Capital Markets):

Okay, thank you very much.

Operator:

Thank you, next question is from Casey Deak of Wells Fargo .

Casey Deak (Analyst - Wells Fargo Securities):

Thank you, good morning, guys.

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Robert Sanchez (President & CEO):

Good morning.

Casey Deak (Analyst - Wells Fargo Securities):

Wanted to ask on, you saw good result, early terminations remain pretty low relative to history. How is the customer base performing on the rental side, those lease customers, how much of the weakness year-over-year in rental is a product of lease customers not absorbing that capacity?

Robert Sanchez (President & CEO):

Well there is, some of that weaknesses that we're seeing especially around tractors is coming from lease customers who have fleeted up and are not needing as much additional capacity if you will as they did a year ago. So we're really seeing it across the lease customers and also other rental customers maybe more like companies that are in the carrier business, where we're seeing them have less demand for rental vehicles.

Casey Deak (Analyst - Wells Fargo Securities):

And how does that kind of parlay into your outlook? What are you expecting for the rest of the year from your lease customers as far as renting an extra truck, does that deteriorate or would you expect it to be more they would go to a redeployment and a lease vehicle versus trying to get that capacity?

Robert Sanchez (President & CEO):

I mean that's all built into our 7% down that we've got in the forecast, so we're really seeing -- but I think your point is it's not just coming from pure rental customers. It's also coming from lease customers who are renting less now. That could change, as you know the dynamics between freight volumes and capacity can change pretty quickly, but right now it's definitely soft.

Casey Deak (Analyst - Wells Fargo Securities):

Okay I appreciate the time. Thanks, Robert.

Operator:

Thank you, next question is from Brian Ossenbeck with JP Morgan.

Brian Ossenbeck (Analyst - JPMorgan):

Good morning, thanks for taking my question.

Robert Sanchez (President & CEO):

Good morning, Brian.

Brian Ossenbeck (Analyst - JPMorgan):

Just had a question about the new customer percentages with a fair amount in full service lease. So want to get your thoughts on that, what drove it and if that's something that you would expect to continue in the future? And when these customers come in are they more amenable to using some of the other services quicker, or do you think this is kind of a slower to get a higher number, but maybe a little bit slower conversion when it comes to up selling and cross selling (Inaudible)?

Robert Sanchez (President & CEO):

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I'm sorry, I missed the last part of the question.

Brian Ossenbeck (Analyst - JPMorgan):

I was just wondering how quickly you can cross-sell or upsell the new customer base which was a bigger percentage of your full service add this quarter.

Robert Sanchez (President & CEO):

Yes, no look, that's been our focus for the last several years is really how do we get that large market segment that hasn't outsourced yet to outsource, so for us its been very encouraging that the number's moved from 1/3 to 40%. We really -- one quarter doesn't make a trend but we would really like to see that number sustain and continue to move up from that level.

We've got a lot of focus around it. Dennis and his team -- around getting after the large market that's still, you know, is buying their own trucks and doing their own maintenance, so 40% of the growth, 40% plus is a new milestone for us so we're happy for that.

We also as you know, Dennis and the team really rolled out two and a half years ago this total cost of ownership tool that the salesforce has been using, and I think that's had a lot to do with some of the success that we're seeing there. Obviously along with the secular trends that are out there making it more difficult for them to do their own maintenance and buy their own trucks, but as an example over the last two years the team has done over 10,000 TCOs analysis with prospects, so that starts to chip away over time as customers really begin to see how much they can save by outsourcing versus doing things on their own. So when I think we're beginning to see some of the benefits of that and some of the fruits of that labor.

Brian Ossenbeck (Analyst - JPMorgan):

Okay, and then just a follow-up on that, do you think the 40% would be sustainable if the freight market were to remain softer and pricing wasn't as tight and pricing wasn't as high, or do you think that would just basically extend what you see as a longer secular trend? Thanks.

Robert Sanchez (President & CEO):

You know look, I don't have a crystal ball on that, but I would expect it to be sustainable because the market is so large, and even in a down market somebody is buying a truck and if we can save them money, that should be attractive for them, so it's really us knocking on enough doors and getting in front of enough people and fleets to be able to keep that number moving in the right direction.

Brian Ossenbeck (Analyst - JPMorgan):

Okay, thanks for taking my questions.

Robert Sanchez (President & CEO):

Thank you, Brian.

Operator:

Thank you. At this time there are no additional questions. I'd like to turn the call back over to Mr. Robert Sanchez for closing remarks.

Robert Sanchez (President & CEO):

Okay, well thank you, everyone. Great questions and look forward to seeing all of you over the next

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several weeks and certainly at our Investor Day, thank you.

Operator:

Thank you, and that concludes today's Conference Call.

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