

## Class 8 Slides

# Hertz/Avis Budget/Dollar Thrifty

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Merger Antitrust Law

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Georgetown University Law Center

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# Hertz/Avis Budget/Dollar Thrifty



# 2010 Hertz/Dollar Thrifty deal

## ■ Hertz

- \$7.1 billion in revenues
- Hertz and Advantage brands
- Hertz: 8200 rental locations worldwide
  - Premium global rental car brand
  - Focus on corporate and high-end leisure
  - #1 in U.S. airport rentals (78 major airports)
- Advantage: 26 airports in the U.S.
  - “Flanker” brand to compete for price-conscious travelers at airports
  - Lower price proposition/fewer service attributes



# 2010 Hertz/Dollar Thrifty deal

## ■ Dollar Thrifty

- \$1.5 billion in revenues
- \$1.9 global enterprise value
- Dollar Rent A Car and Thrifty Car Rental brands
  - “Middle market” airport brands
- 1558 corporate and franchise locations worldwide
  - 298 corporate-owned
  - 1260 franchisee locations



# 2010 Hertz/Dollar Thrifty deal

- 2010 merger agreement
  - Signed on April 26, 2010
  - Hertz to buy Dollar Thrifty for \$41.00 per share (= \$1.3 equity value)
    - \$6.88 in special Dollar Thrifty dividend (= \$200 million)
    - \$25.92 to be paid by Hertz in cash (= \$756 million)
    - \$12.88 in Hertz stock (valued at the closing price on April 23, 2010) (= \$317 million)
      - DT shareholders will hold 5.5% of Hertz after closing
  - 19% deal premium to 30-day closing average
  - \$180 million in annual recurring synergies
    - Primarily in fleet, IT systems, and procurement savings



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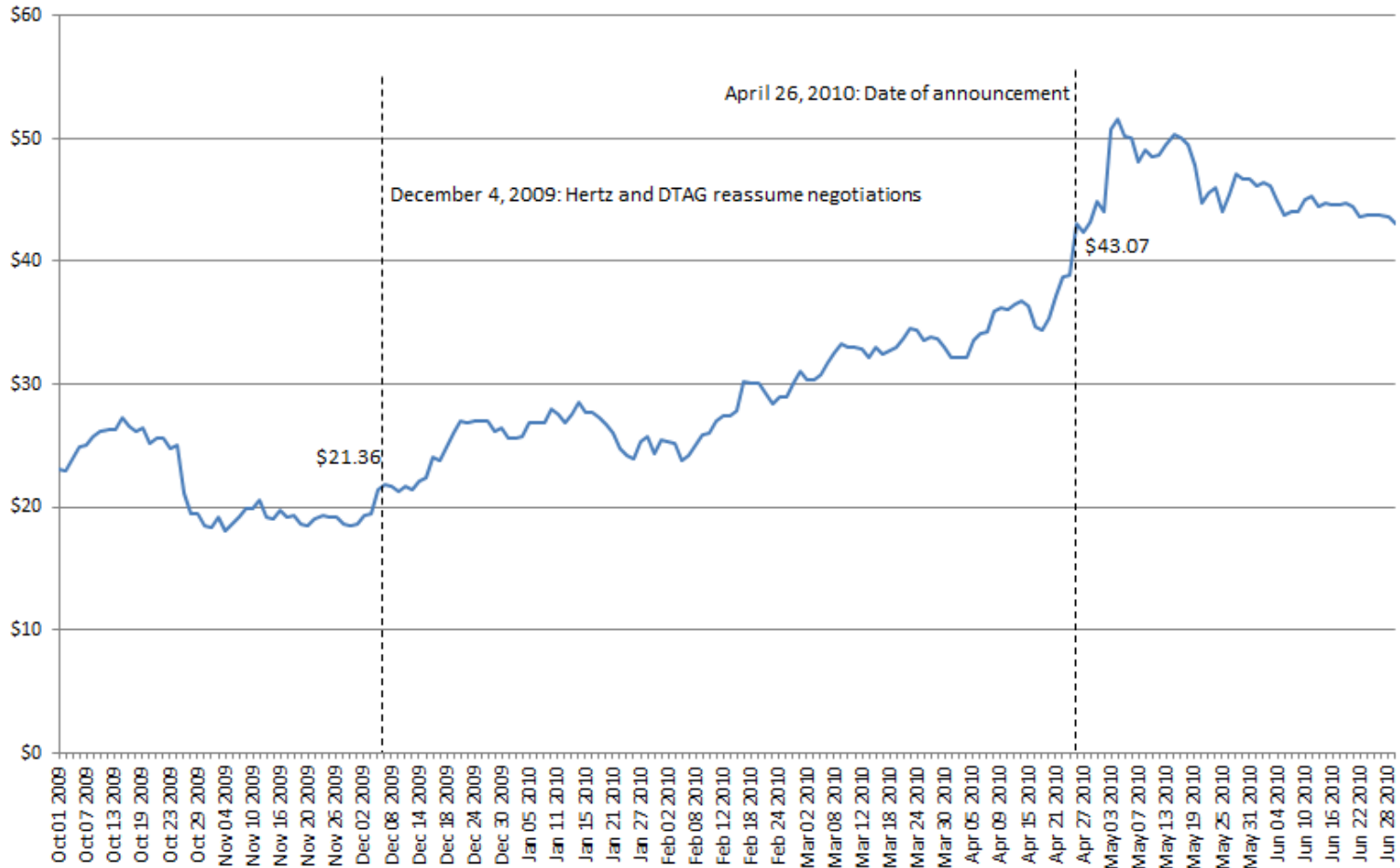
# 2010 Hertz/Dollar Thrifty deal

Why did Dollar Thrifty want to do this deal?

Why did Hertz want to do this deal?

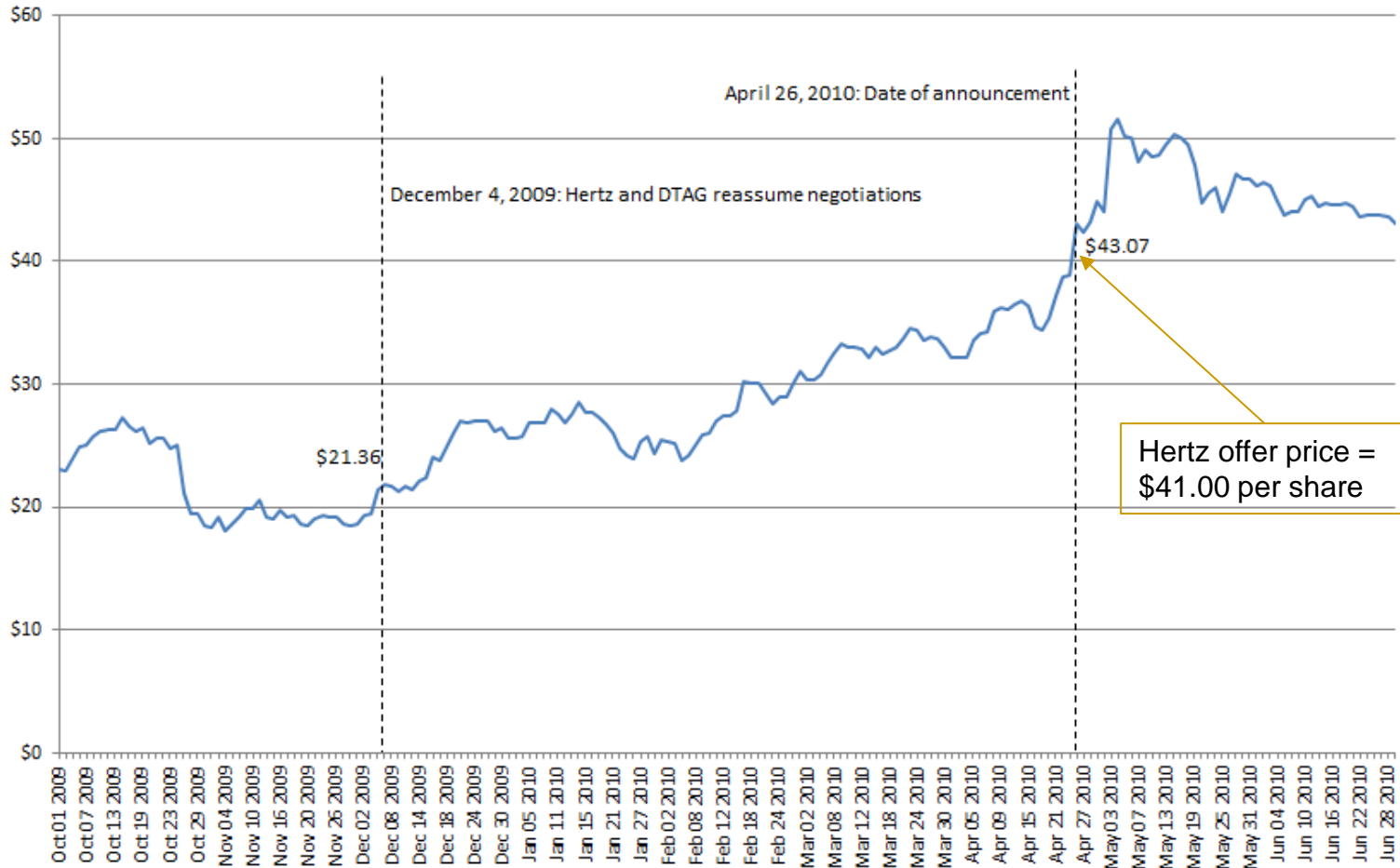
# Dollar Thrifty business rationale

**Dollar Thrifty Closing Prices**  
October 1, 2009 — June 29, 2010



# Dollar Thrifty business rationale

Dollar Thrifty Closing Prices  
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# Hertz business rationale



- Premium global brand competing with Avis, National
- Corporate, higher-end leisure, special occasions
- High service, higher-end fleet mix
- Making inroads in Off-Airport segment historically dominated by Enterprise



- Middle market airport brands competing with, but differentiated from Enterprise, Budget, Alamo
- Value proposition emphasizing lower price but consistently delivering essential services (speed, reliability)
- Consider dual brand operationally, but keep separate for marketing, positioning, e.g., separate websites



- Flanker airport brand to compete for economy leisure business against Payless, Fox, etc.
- Lower price proposition for price-focused leisure customers
- Reliable, clean cars, but fewer service attributes

# Hertz business rationale

## Significant Strategic & Financial Benefits

### Strategic Rationale

- Gain instant scale in middle tier sector with established brand and airport infrastructure
- Allows Hertz to pursue aggressive value strategy without risking dilution to Hertz brand
- Provides Hertz with multiple strategic options to address leisure business and compete with multi-brand peers in all three tiers of the market

### Significant Synergy Potential

- At least \$180 million of annual run-rate synergies expected
- Key areas of cost reduction / operational improvement include
  - Procurement: significant portion of Dollar Thrifty's spend is decentralized
  - IT: overlapping systems and future capital spend
  - Fleet: benefit from fleet sharing and reduced cap. cost
  - Public company costs

### Positive Financial Impact

- 20% equity used to maintain strong credit profile

(\$ in millions)

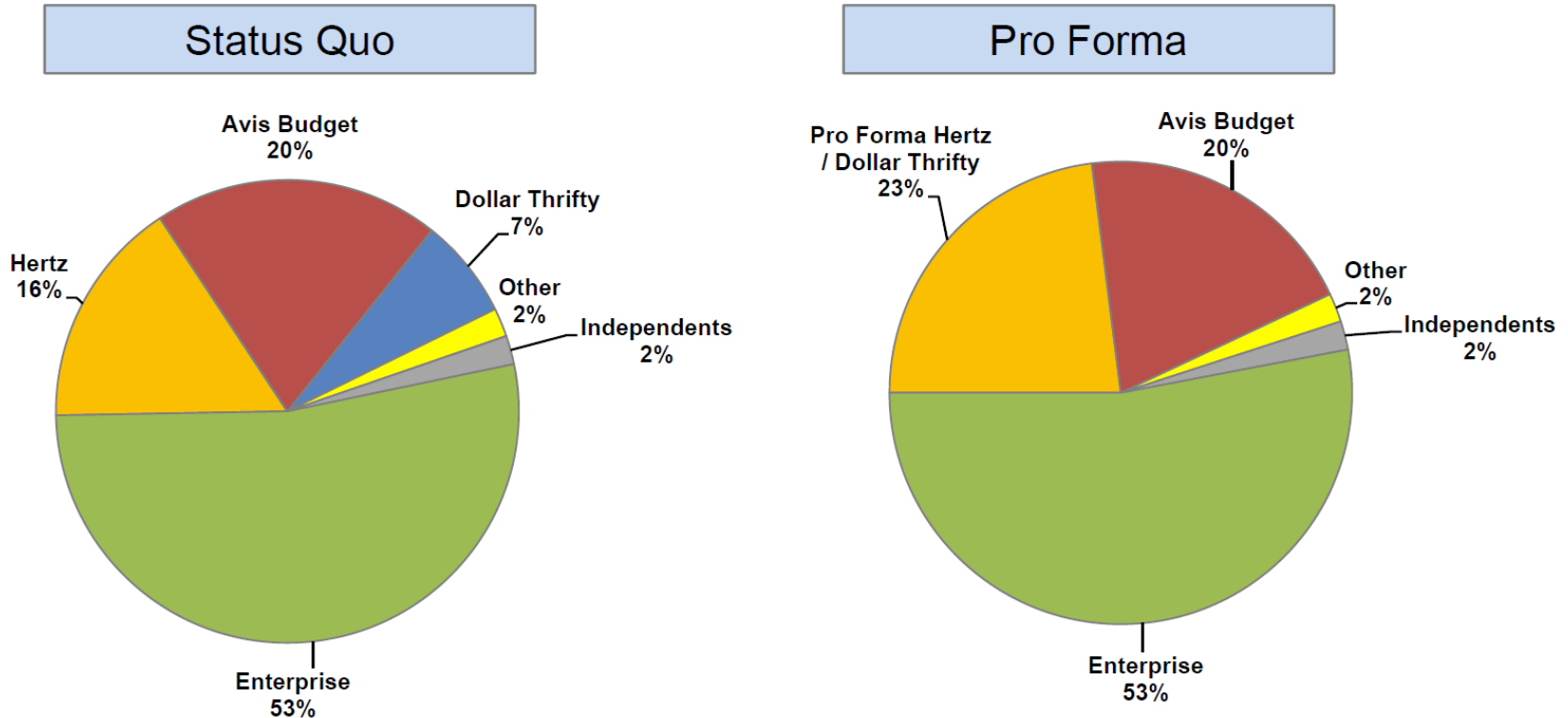
As of December 31, 2009

	Hertz Standalone	Hertz Pro Forma
Total Corp. Debt / Corp. EBITDA	4.8x	4.4x
Total Corp. Debt / Corp. EBITDA (w/ syn)		3.7x
Total Debt / Gross EBITDA	3.6x	3.4x
Total Debt / Gross EBITDA (w/ syn)		3.2x

- Earnings accretive

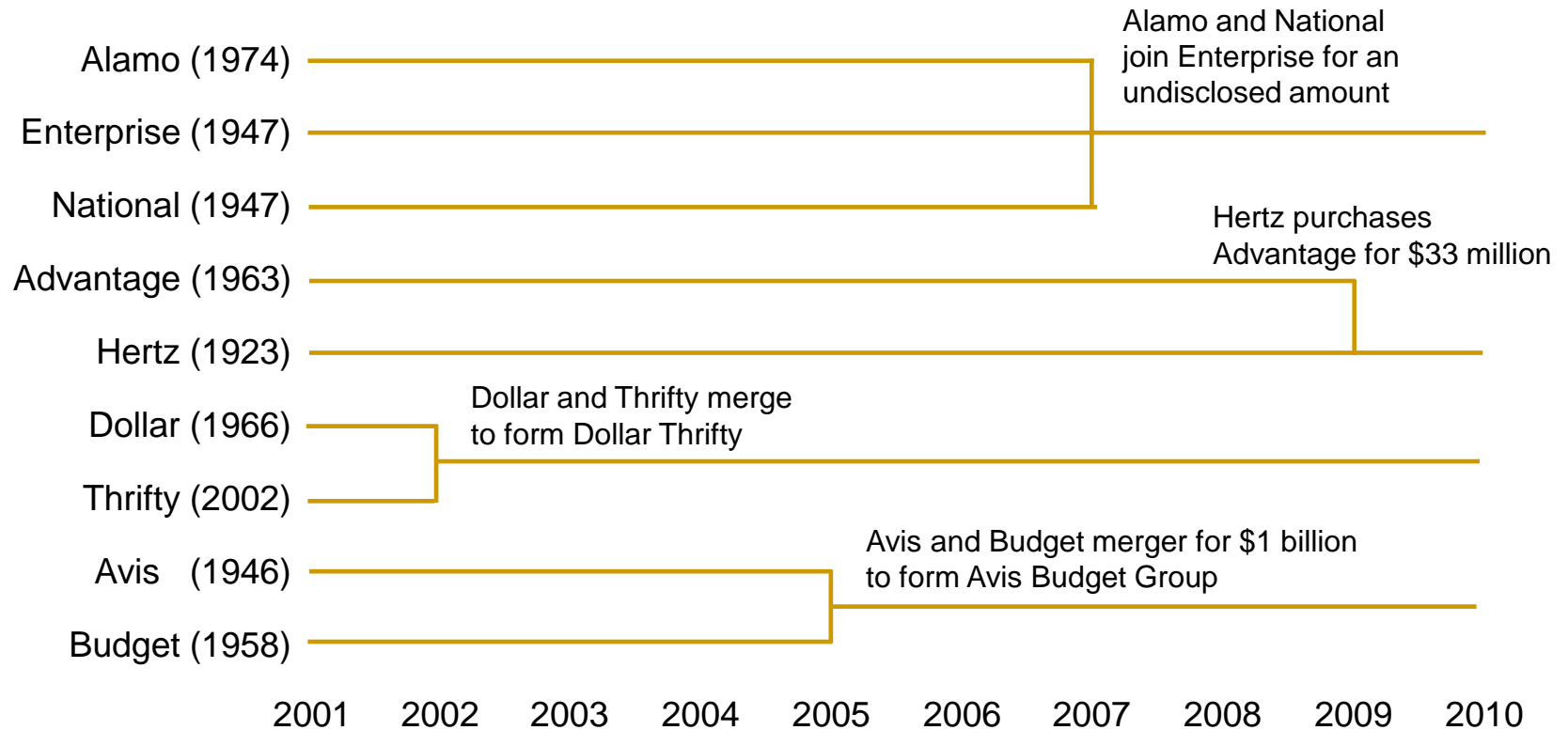
# Hertz business rationale

## Total U.S. Rental Car Market Revenue Share 2009



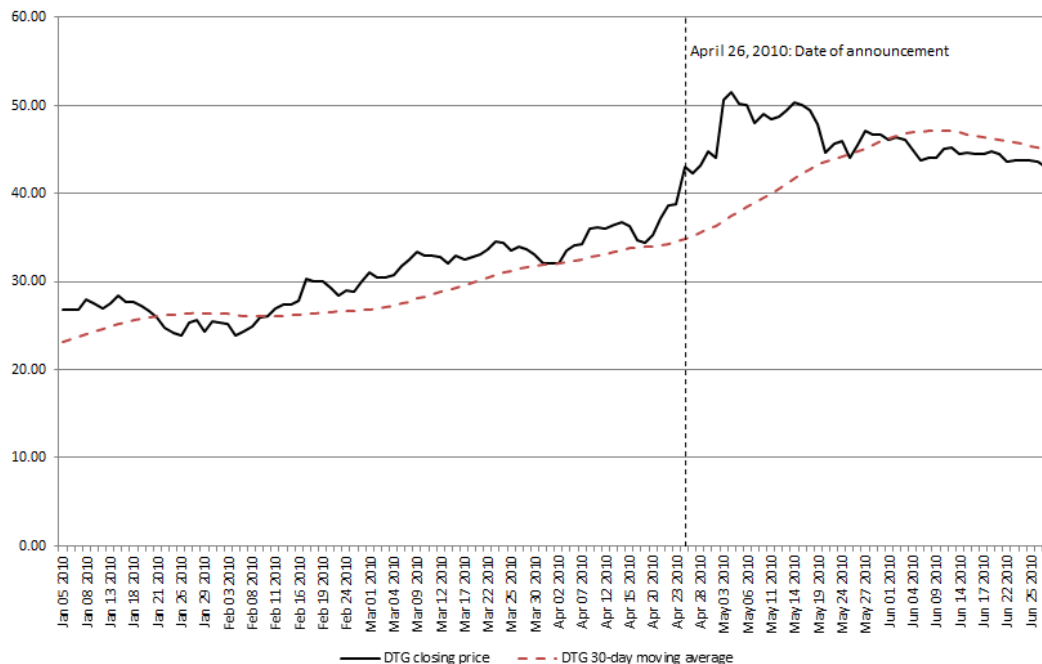
Source: Auto Rental News, 2010 Fact Book

# Consolidation in the rental car industry



# Dollar Thrifty preannouncement run-up

**Dollar Thrifty Closing Prices**  
January 4, 2010 — June 29, 2010



**Closing Price Changes**  
(compared to prior months)

	1-month	2-months	3-months
DTG	12.3%	36.9%	56.7%
DJIA	2.9%	9.0%	10.1%

# The deal price

## ■ Payments to Dollar Thrifty shareholders

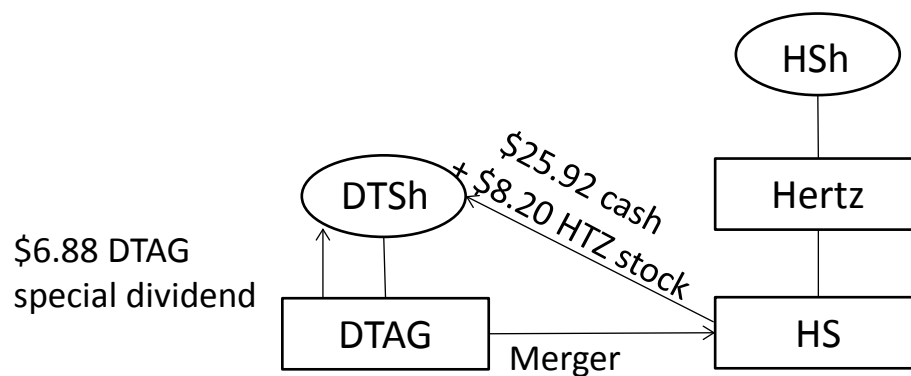
\$6.88	Dollar Thrifty special cash dividend
\$25.92	Cash paid by Hertz
\$8.20	0.6366 Hertz shares, valued on the closing price on April 23, 2010 (the closing on the last business day before the announcement on April 26, 2010)
\$41.00	Total consideration

## ■ Some implications

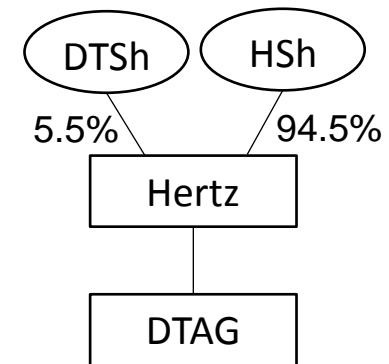
- Special DTAG cash dividend = \$200 million →
  - ~29m DTAG shares
  - DTAG would receive \$953m in cash
  - Hertz would only pay \$753 m in case
  - Total deal value to DTAG shareholders = \$1.2 billion

# Hertz/DTAG Reverse Triangular Merger

Before:



After:



where DTAG Dollar Thrifty Automotive Group (target firm)  
 DTSh TS DTAG's premerger shareholders  
 Hertz Acquiring firm  
 HSh Hertz premerger shareholders  
 HS Hertz acquisition subsidiary

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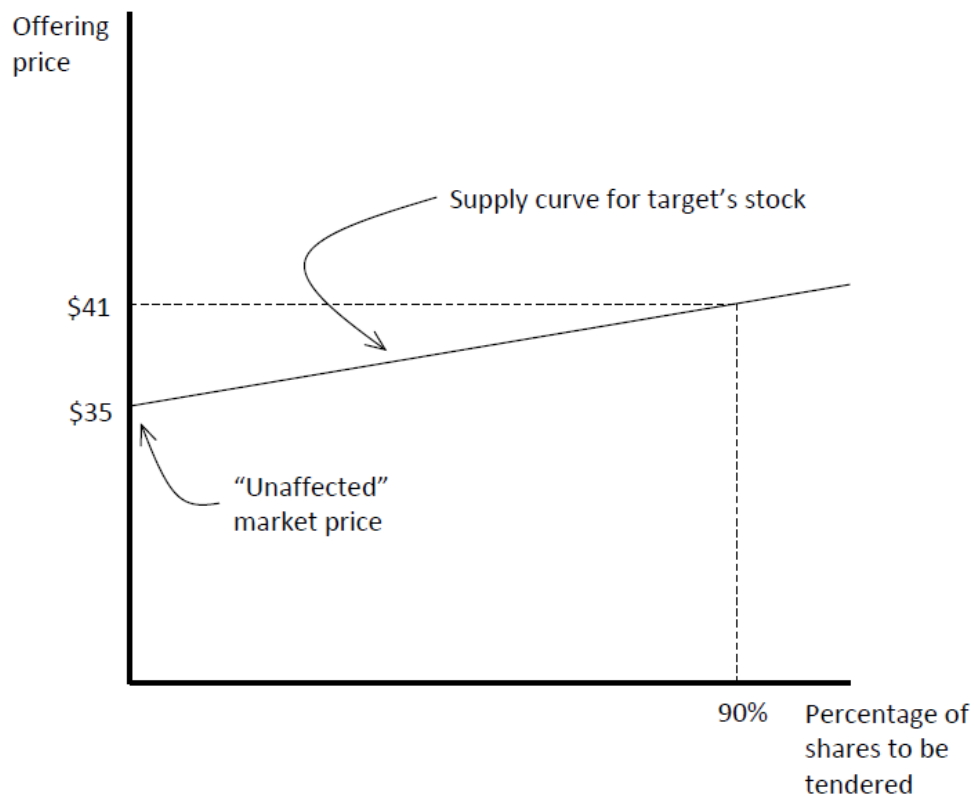
# Deal premium

- Why did Hertz pay a deal premium?
  1. Upward-sloping demand curve for DTAG stock
  2. Bargaining game over the synergies gain



# Deal premium

- Why did Hertz pay a deal premium?
  1. Upward-sloping demand curve for DTAG stock



# Deal premium

## ■ Why did Hertz pay a deal premium?

### 2. Bargaining game over the synergies gain—Hertz

- Total value to Hertz ( $V_t$ ) is equal to the going concern value of DTAG ( $V_{DTAG}$ ) plus any synergy gains ( $V_s$ ) resulting from the transaction

$$V_t = V_{DTAG} + V_s$$

- Hertz set the going concern value  $V_{DTAG}$  of DTAG at \$932 million (after dividend)
- Hertz claimed an expected annually recurring synergy gain of \$180 million ( $A$ )
  - The present discounted value  $V_s$  of an annual recurring cash payment in perpetuity (that is, a perpetual annuity) discounted at rate  $r$  (say, 7%) is:

$$V_s = \frac{A}{r} = \frac{\$180 \text{ million}}{0.07} = \$2.57 \text{ billion}$$

- But say that Hertz values synergies only over a 10-year period. Then:

$$V_s = A \left[ \frac{1 - (1+r)^{-n}}{r} \right] = \$180 \text{ million} \left[ \frac{1 - (1+0.07)^{-10}}{0.07} \right] = \$1.26 \text{ billion}$$

# Deal premium

- Why did Hertz pay a deal premium?

- 2. Bargaining game over the synergies gain—Hertz

- So Hertz expects that the total value  $V_t$  of Dollar Thrifty postmerger will be:

$$\begin{aligned}V_t &= V_c + V_g \\ &= \$932 \text{ million} + \$1.26 \text{ billion} \\ &= \$2.17 \text{ billion}\end{aligned}$$

- But Hertz shareholders will own only 94.5% of the combined company
        - The original Hertz shareholders will not own the whole company because their interest is being diluted by the Hertz stock going to the DTAG shareholders
        - The original Hertz shareholders would hold only 94.5% of the Hertz stock postmerger, so that would get only that portion of  $V_t$  (= \$2.075 billion)

So Hertz shareholders should be willing to pay a maximum of \$2.075 billion for the deal (or about \$71 per DTAG share)

# Deal premium

- Why did Hertz pay a deal premium?
  2. Bargaining game over the synergies gain—DTAG
    - DTAG shareholders will not accept anything lower than their current stock price
    - BUT they can also bargain for some of the gain resulting from the deal, since unless they agree to the deal Hertz shareholders will receive no gain
    - At \$41 per share under Hertz's terms, DTAG shareholders receive a significant deal premium over the unaffected price:

	Closing price	Ex dividend (= \$6.88)	Deal premium
Mar. 23, 2010	34.60	27.72	18.5%
Feb. 23, 2010	28.37	21.49	90.8%
Jan. 22, 2010	24.29	17.41	135.5%

- So this looks like a good deal to the DTAG shareholders
- Also looks like a good deal to the Hertz shareholders
  - Willing to pay up to \$71 per share, but paid only \$41 per share

# Deal premium

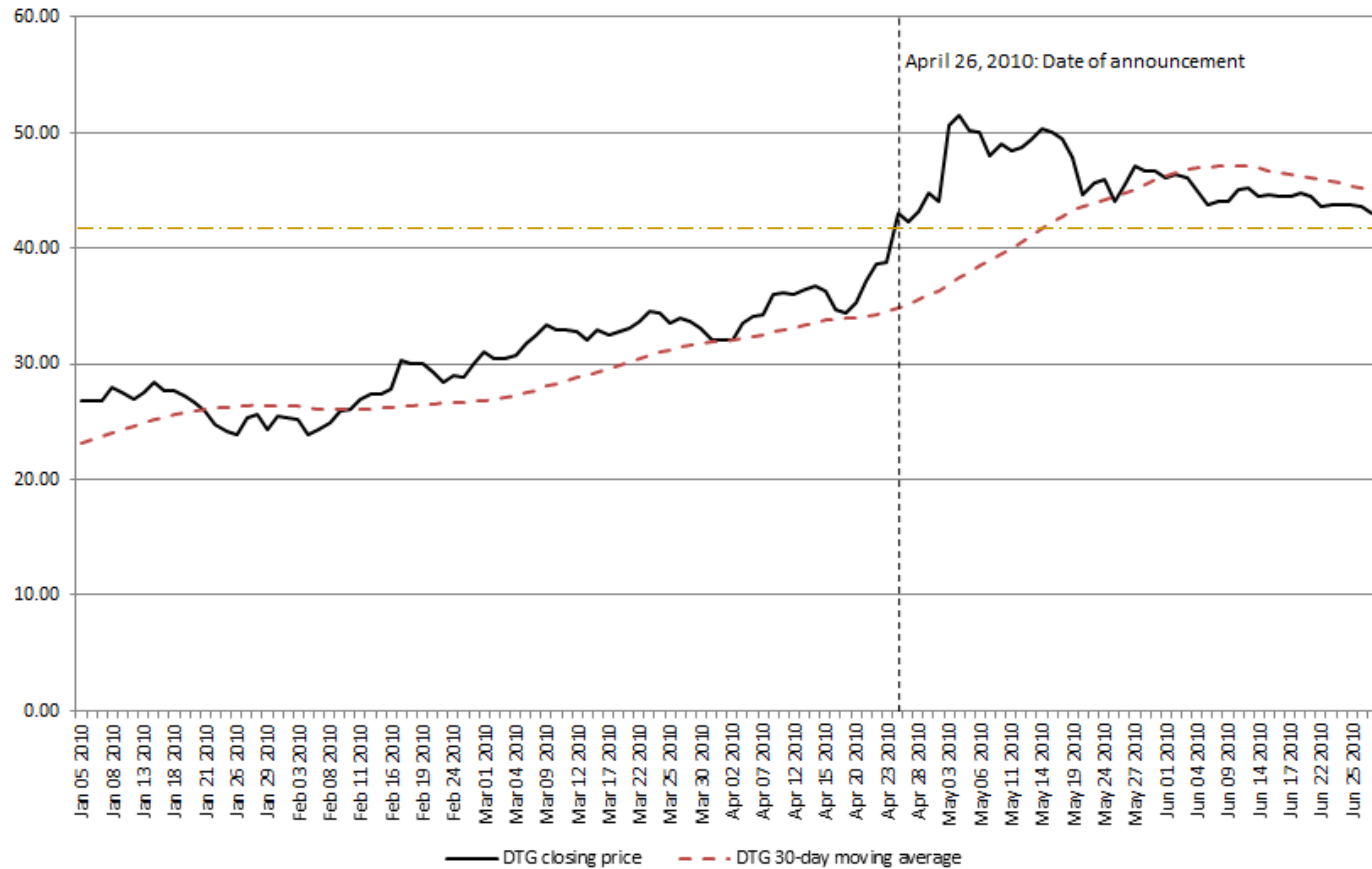
- Why did Hertz pay a deal premium?
  2. Bargaining game over the synergies gain
    - Division of the synergy gains

		Surplus gain
Hertz reservation price	\$71	\$40
Deal price	\$41	
DTAG reservation price	\$32	\$9

- *Query:* Why did DTAG accept so low a share of the synergies gain?

# Market reaction

**Dollar Thrifty Closing Prices**  
January 4, 2010 — June 29, 2010



# Market reaction

