

RYDER SYSTEM INC  
Form 10-Q  
July 27, 2016

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2016  
OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_  
Commission File Number: 1-4364

RYDER SYSTEM, INC.  
(Exact name of registrant as specified in its charter)

Florida 59-0739250  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

11690 N.W. 105th Street  
Miami, Florida 33178 (305) 500-3726  
(Address of principal executive offices, including zip code) (Registrant's telephone number, including area code)  
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES ☒ NO ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES ☐ NO ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐  
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) ☐  
YES ☐ NO ☒

The number of shares of Ryder System, Inc. Common Stock (\$0.50 par value per share) outstanding at June 30, 2016 was 53,478,452.

RYDER SYSTEM, INC.  
FORM 10-Q QUARTERLY REPORT  
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PART I. FINANCIAL INFORMATION  
ITEM 1. FINANCIAL STATEMENTS

RYDER SYSTEM, INC. AND SUBSIDIARIES  
CONSOLIDATED CONDENSED STATEMENTS OF EARNINGS  
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(In thousands, except per share amounts)			
Lease and rental revenues	\$798,387	779,046	\$1,566,141	1,508,070
Services revenue	785,791	737,170	1,544,918	1,430,874
Fuel services revenue	119,566	146,715	222,357	291,140
Total revenues	1,703,744	1,662,931	3,333,416	3,230,084
Cost of lease and rental	555,302	531,308	1,107,792	1,049,730
Cost of services	646,129	603,488	1,277,843	1,185,818
Cost of fuel services	115,478	142,176	214,379	278,465
Other operating expenses	27,796	29,582	57,947	61,955
Selling, general and administrative expenses	222,448	214,868	433,661	421,473
Gains on used vehicles, net	(12,000 )	(29,985 )	(31,129 )	(57,193 )
Interest expense	37,268	39,075	75,157	75,877
Miscellaneous income, net	(5,456 )	(1,028 )	(7,721 )	(3,665 )
	1,586,965	1,529,484	3,127,929	3,012,460
Earnings from continuing operations before income taxes	116,779	133,447	205,487	217,624
Provision for income taxes	42,737	47,530	75,260	78,381
Earnings from continuing operations	74,042	85,917	130,227	139,243
Loss from discontinued operations, net of tax	(292 )	(758 )	(683 )	(1,295 )
Net earnings	\$73,750	85,159	\$129,544	137,948
Earnings (loss) per common share — Basic				
Continuing operations	\$1.39	1.62	\$2.45	2.63
Discontinued operations	(0.01 )	(0.01 )	(0.01 )	(0.02 )
Net earnings	\$1.39	1.61	\$2.43	2.61
Earnings (loss) per common share — Diluted				
Continuing operations	\$1.38	1.61	\$2.43	2.61
Discontinued operations	(0.01 )	(0.01 )	(0.01 )	(0.03 )
Net earnings	\$1.38	1.59	\$2.42	2.59
Cash dividends declared per common share	\$0.41	0.37	\$0.82	0.74

See accompanying notes to consolidated condensed financial statements.

Note: EPS amounts may not be additive due to rounding



RYDER SYSTEM, INC. AND SUBSIDIARIES  
CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME  
(unaudited)

	Three months ended June 30, 2016      2015 (In thousands)		Six months ended June 30, 2016      2015	
Net earnings	\$73,750	85,159	\$129,544	137,948
Other comprehensive income (loss):				
Currency translation adjustment and other	(32,264 )	27,027	(18,578 )	(30,345 )
Amortization of pension and postretirement items	7,446	6,834	14,869	13,892
Income tax expense related to amortization of pension and postretirement items	(2,479 )	(2,366 )	(5,187 )	(4,814 )
Amortization of pension and postretirement items, net of tax	4,967	4,468	9,682	9,078
Change in net actuarial loss and prior service cost	(17,367 )	(8,526 )	(17,367 )	(8,526 )
Income tax benefit related to change in net actuarial loss and prior service cost	6,345	3,205	6,345	3,205
Change in net actuarial loss and prior service cost, net of taxes	(11,022 )	(5,321 )	(11,022 )	(5,321 )
Other comprehensive income (loss), net of taxes	(38,319 )	26,174	(19,918 )	(26,588 )
Comprehensive income	\$35,431	111,333	\$109,626	111,360
See accompanying notes to consolidated condensed financial statements.				

RYDER SYSTEM, INC. AND SUBSIDIARIES  
CONSOLIDATED CONDENSED BALANCE SHEETS  
(unaudited)

	June 30, 2016	December 31, 2015
	(Dollars in thousands, except per share amount)	
Assets:		
Current assets:		
Cash and cash equivalents	\$ 65,964	60,945
Receivables, net of allowance of \$16,138 and \$15,560, respectively	850,504	835,489
Inventories	66,553	63,725
Prepaid expenses and other current assets	143,227	138,143
Total current assets	1,126,248	1,098,302
Revenue earning equipment, net	8,300,108	8,184,735
Operating property and equipment, net of accumulated depreciation of \$1,105,458 and \$1,083,604, respectively	741,022	714,970
Goodwill	388,278	389,135
Intangible assets, net of accumulated amortization of \$48,691 and \$45,736, respectively	51,618	55,192
Direct financing leases and other assets	528,853	510,246
Total assets	\$ 11,136,127	10,952,580
Liabilities and shareholders' equity:		
Current liabilities:		
Short-term debt and current portion of long-term debt	\$ 1,047,208	634,530
Accounts payable	462,335	502,373
Accrued expenses and other current liabilities	508,517	543,352
Total current liabilities	2,018,060	1,680,255
Long-term debt	4,586,806	4,868,097
Other non-current liabilities	828,181	829,595
Deferred income taxes	1,655,982	1,587,522
Total liabilities	9,089,029	8,965,469
Shareholders' equity:		
Preferred stock, no par value per share — authorized, 3,800,917; none outstanding, June 30, 2016 or December 31, 2015	—	—
Common stock, \$0.50 par value per share — authorized, 400,000,000; outstanding, June 30, 2016 — 53,478,452; December 31, 2015 — 53,490,603	26,739	26,745
Additional paid-in capital	1,016,173	1,006,021
Retained earnings	1,736,839	1,667,080
Accumulated other comprehensive loss	(732,653)	(712,735)
Total shareholders' equity	2,047,098	1,987,111
Total liabilities and shareholders' equity	\$ 11,136,127	10,952,580
See accompanying notes to consolidated condensed financial statements.		

RYDER SYSTEM, INC. AND SUBSIDIARIES  
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS  
(unaudited)

	Six months ended June 30,	
	2016	2015
	(In thousands)	
Cash flows from operating activities from continuing operations:		
Net earnings	\$ 129,544	137,948
Less: Loss from discontinued operations, net of tax	(683 )	(1,295 )
Earnings from continuing operations	130,227	139,243
Depreciation expense	581,043	541,076
Gains on used vehicles, net	(31,129 )	(57,193 )
Share-based compensation expense	10,001	11,169
Amortization expense and other non-cash charges, net	31,407	28,329
Deferred income tax expense	67,031	67,592
Changes in operating assets and liabilities:		
Receivables	(39,071 )	(33,535 )
Inventories	(2,633 )	1,006
Prepaid expenses and other assets	(18,734 )	(25,555 )
Accounts payable	68,584	(30,439 )
Accrued expenses and other non-current liabilities	(34,054 )	17,005
Net cash provided by operating activities from continuing operations	762,672	658,698
Cash flows from financing activities:		
Net change in commercial paper borrowings and revolving credit facilities	162,105	34,750
Debt proceeds	298,254	930,090
Debt repaid	(328,416 )	(486,103 )
Dividends on common stock	(44,261 )	(39,690 )
Common stock issued	6,259	17,129
Common stock repurchased	(21,899 )	(6,141 )
Excess tax benefits from share-based compensation and other items	(1,710 )	710
Debt issuance costs	(933 )	(5,225 )
Net cash provided by financing activities	69,399	445,520
Cash flows from investing activities:		
Purchases of property and revenue earning equipment	(1,120,182 )	(1,329,218 )
Sales of revenue earning equipment	245,681	211,153
Sales of operating property and equipment	6,322	641
Collections on direct finance leases and other items	43,957	33,912
Changes in restricted cash	886	4,849
Net cash used in investing activities	(823,336 )	(1,078,663 )
Effect of exchange rate changes on cash	(3,415 )	(1,198 )
Increase in cash and cash equivalents from continuing operations	5,320	24,357
Decrease in cash and cash equivalents from discontinued operations	(301 )	(1,096 )

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Increase in cash and cash equivalents	5,019	23,261
Cash and cash equivalents at January 1	60,945	50,092
Cash and cash equivalents at June 30	\$65,964	73,353
See accompanying notes to consolidated condensed financial statements.		



RYDER SYSTEM, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS  
(unaudited)

1. GENERAL

Interim Financial Statements

The accompanying unaudited Consolidated Condensed Financial Statements include the accounts of Ryder System, Inc. (Ryder) and all entities in which Ryder has a controlling voting interest (subsidiaries) and variable interest entities (VIEs) required to be consolidated in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). The accompanying unaudited Consolidated Condensed Financial Statements have been prepared in accordance with the accounting policies described in our 2015 Annual Report on Form 10-K and should be read in conjunction with the Consolidated Financial Statements and notes thereto. The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included and the disclosures herein are adequate. The operating results for interim periods are unaudited and are not necessarily indicative of the results that can be expected for a full year.

Beginning in 2016, we reclassified the losses from fair value adjustments on our used vehicles from "Other operating expenses" to "Gains on used vehicles, net" within the Consolidated Condensed Statement of Earnings. Prior year amounts have been reclassified to conform to the current period presentation.

RYDER SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

## 2. RECENT ACCOUNTING PRONOUNCEMENTS

### Share-Based Payments

In March 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-09, Stock Compensation, which is intended to simplify several aspects of the accounting for share-based payment award transactions. The guidance will be effective January 1, 2017. We are in the process of evaluating the impacts of the adoption of this standard.

### Leases

In February 2016, the FASB issued ASU No. 2016-02, Leases, which sets out the principles for the recognition, measurement, presentation and disclosure of leases. The standard requires lessees to apply a dual approach, classifying leases as either finance or operating leases. This classification will determine whether the lease expense is recognized based on an effective interest method or on a straight-line basis over the term of the lease. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months regardless of their classification. Leases with a term of 12 months or less will be accounted for similar to existing guidance for operating leases. The new standard requires lessors to account for leases using an approach that is substantially equivalent to existing guidance for sales-type leases, direct financing leases and operating leases. The standard is effective January 1, 2019, with early adoption permitted. The standard is to be applied using a modified retrospective transition method. We are in the process of determining the effect on our consolidated financial position, results of operations and cash flows.

### Revenue Recognition

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which together with related, subsequently issued guidance, requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU is effective January 1, 2018, and will replace most existing revenue recognition guidance. The standard permits the use of either the modified retrospective or cumulative effect transition methods.

In connection with the FASB's recently issued guidance on leases, the standard requires the lease component of our full service lease product line to be accounted for under the lease accounting guidance and the maintenance and other elements of the product line to be accounted for under the new revenue guidance. Because of the interrelationship of these standards on our full service lease product line, we have not yet selected a transition method. We are in the process of determining the effect on our consolidated financial position, results of operations and cash flows.

### Presentation of Debt Issuance Costs

In April 2015, the FASB issued ASU No. 2015-03, Simplifying the Presentation of Debt Issuance Costs, which requires an entity to present debt issuance costs as a direct reduction from the carrying amount of the related debt liability on the balance sheet. We adopted this guidance on January 1, 2016 and reclassified \$15 million from other assets to long-term debt in our December 31, 2015 balance sheet. Other than the change in presentation within the Consolidated Condensed Balance Sheets, this accounting guidance did not impact our consolidated financial position,

results of operations or cash flows.

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

## 3. REVENUE EARNING EQUIPMENT

	June 30, 2016			December 31, 2015		
	Cost	Accumulated Depreciation	Net Book Value <sup>(1)</sup>	Cost	Accumulated Depreciation	Net Book Value <sup>(1)</sup>
(In thousands)						
Held for use:						
Full service lease	\$9,239,442	(2,838,897 )	6,400,545	\$8,839,941	(2,723,605 )	6,116,336
Commercial rental	2,589,646	(874,713 )	1,714,933	2,811,715	(907,412 )	1,904,303
Held for sale	576,449	(391,819 )	184,630	496,634	(332,538 )	164,096
Total	\$12,405,537	(4,105,429 )	8,300,108	\$12,148,290	(3,963,555 )	8,184,735

Revenue earning equipment, net includes vehicles acquired under capital leases of \$43.9 million, less accumulated (1)depreciation of \$21.1 million, at June 30, 2016, and \$47.5 million, less accumulated depreciation of \$22.2 million, at December 31, 2015.

We lease revenue earning equipment to customers for periods typically ranging from three to seven years for trucks and tractors and up to ten years for trailers. The majority of our leases are classified as operating leases. However, some of our revenue earning equipment leases are classified as direct financing leases and, to a lesser extent, sales-type leases. As of June 30, 2016 and December 31, 2015, the net investment in direct financing and sales-type leases was \$431 million and \$438 million, respectively. Our direct financing lease customers operate in a wide variety of industries, and we have no significant customer concentrations in any one industry. We assess credit risk for all of our customers including those who lease equipment under direct financing leases prior to signing a full service lease contract. For those customers who are designated as high risk, we typically require deposits to be paid in advance in order to mitigate our credit risk. Additionally, our receivables are collateralized by the vehicles which further mitigates our credit risk.

As of June 30, 2016 and December 31, 2015, the amount of direct financing lease receivables past due was not significant, and there were no impaired receivables. Accordingly, we do not believe there is a material risk of default with respect to the direct financing lease receivables.

Revenue earning equipment held for sale is stated at the lower of carrying amount or fair value less costs to sell. Losses on vehicles held for sale for which carrying values exceeded fair value are recognized at the time they arrive at our used truck centers and are presented within "Gains on used vehicles, net" in the Consolidated Condensed Statements of Earnings. For revenue earning equipment held for sale, we stratify our fleet by vehicle type (trucks, tractors and trailers), weight class, age and other relevant characteristics and create classes of similar assets for analysis purposes. For a certain population of our revenue earning equipment held for sale, fair value was determined based upon recent market prices obtained from our own sales experience for sales of each class of similar assets and vehicle condition. These vehicles held for sale were classified within Level 3 of the fair value hierarchy.

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

The following table presents our assets held for sale that are measured at fair value on a nonrecurring basis and considered a Level 3 fair value measurement:

	June 30,		Total Losses <sup>(2)</sup>			
			Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015	2016	2015
	(In thousands)					
Assets held for sale:						
Revenue earning equipment <sup>(1)</sup> :						
Trucks	\$13,749	6,805	\$2,570	1,515	\$4,314	2,743
Tractors	51,795	7,389	9,206	1,081	14,088	1,908
Trailers	3,015	1,625	775	656	1,437	972
Total assets at fair value	\$68,559	15,819	\$12,551	3,252	\$19,839	5,623

(1) Assets held for sale in the above table only include the portion of revenue earning equipment held for sale where carrying value exceeded fair value.

(2) Total losses represent fair value adjustments for all vehicles reclassified to held for sale throughout the period for which fair value was less than carrying value.

For the three and six months ended June 30, 2016 and 2015, the components of gains on used vehicles, net were as follows:

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(In thousands)			
Gains on vehicle sales, net	\$(24,551)	(33,237)	\$(50,968)	(62,816)
Losses from fair value adjustments	12,551	3,252	19,839	5,623
Gains on used vehicles, net	\$(12,000)	(29,985)	\$(31,129)	(57,193)

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

## 4. GOODWILL

The carrying amount of goodwill attributable to each reportable business segment was as follows:

	Fleet Management Solutions	Dedicated Transportation Solutions	Supply Chain Solutions	Total
	(In thousands)			
Balance at January 1, 2016:				
Goodwill	\$231,358	40,808	146,190	418,356
Accumulated impairment losses	(10,322 )	—	(18,899 )	(29,221 )
	221,036	40,808	127,291	389,135
Foreign currency translation adjustments	(1,246 )	—	389	(857 )
Balance at June 30, 2016:				
Goodwill	230,112	40,808	146,579	417,499
Accumulated impairment losses	(10,322 )	—	(18,899 )	(29,221 )
	\$219,790	40,808	127,680	388,278

We assess goodwill for impairment on April 1st of each year or more often if deemed necessary. In the second quarter of 2016, we completed our annual goodwill impairment test. We performed quantitative assessments on two of our reporting units and determined there was no impairment. We performed qualitative assessments for three reporting units, which considered individual factors such as macroeconomic conditions, changes in our industry and the markets in which we operate as well as our historical and expected future financial performance. After performing the qualitative assessments, we concluded it was more likely than not that fair value is greater than the carrying value and determined there was no impairment.

## 5. ACCRUED EXPENSES AND OTHER LIABILITIES

	June 30, 2016			December 31, 2015		
	Accrued Expenses	Non-Current Liabilities	Total	Accrued Expenses	Non-Current Liabilities	Total
	(In thousands)					
Salaries and wages	\$87,558	—	87,558	\$99,032	—	99,032
Deferred compensation	2,725	42,378	45,103	2,252	41,691	43,943
Pension benefits	3,822	482,187	486,009	3,790	484,892	488,682
Other postretirement benefits	1,637	19,677	21,314	1,624	20,002	21,626
Other employee benefits	18,404	4,290	22,694	8,956	9,706	18,662
Insurance obligations <sup>(1)</sup>	139,959	218,058	358,017	157,014	213,256	370,270
Environmental liabilities	3,997	6,333	10,330	3,791	6,554	10,345
Operating taxes	97,187	—	97,187	101,649	—	101,649
Income taxes	448	24,110	24,558	3,378	22,366	25,744
Interest	31,369	—	31,369	31,218	—	31,218
Customer deposits	63,272	4,791	68,063	61,869	5,085	66,954
Deferred revenue	16,738	—	16,738	13,038	—	13,038

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Restructuring liabilities <sup>(2)</sup>	3,489	—	3,489	12,333	—	12,333
Other	37,912	26,357	64,269	43,408	26,043	69,451
Total	\$508,517	828,181	1,336,698	\$543,352	829,595	1,372,947

(1) Insurance obligations primarily represent claims for which we are self-insured.

The reduction in restructuring liabilities from December 31, 2015 principally represents cash payments for

(2) employee termination costs. The majority of the balance remaining in restructuring liabilities is expected to be paid by the end of 2016.

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

## 6. DEBT

	Weighted-Average Interest Rate				
	June 30, 2016	December 31, 2015	Maturities	June 30, 2016	December 31, 2015
	(In thousands)				
Short-term debt and current portion of long-term debt:					
Short-term debt	0.94%	2.26%		\$ 122,354	35,947
Current portion of long-term debt				924,854	598,583
Total short-term debt and current portion of long-term debt				1,047,208	634,530
Long-term debt:					
U.S. commercial paper <sup>(1)</sup>	0.71%	0.55%	2020	599,605	547,130
Global revolving credit facility	2.01%	2.31%	2020	53,037	25,291
Unsecured U.S. notes — Medium-term notes <sup>(4)</sup>	2.88%	2.84%	2016-2025	4,113,137	4,112,519
Unsecured U.S. obligations	1.86%	1.73%	2018	50,000	50,000
Unsecured foreign obligations	1.93%	1.92%	2016-2020	254,448	275,661
Asset-backed U.S. obligations <sup>(2)</sup>	1.78%	1.81%	2016-2022	407,217	434,001
Capital lease obligations	3.22%	3.31%	2016-2022	28,031	32,054
Total before fair market value adjustment				5,505,475	5,476,656
Fair market value adjustment on notes subject to hedging <sup>(3)</sup>				20,989	5,253
Debt issuance costs <sup>(4)</sup>				(14,804 )	(15,229 )
				5,511,660	5,466,680
Current portion of long-term debt				(924,854 )	(598,583 )
Long-term debt				4,586,806	4,868,097
Total debt				\$5,634,014	5,502,627

(1) Amounts are net of aggregate unamortized original issue discounts of \$7.2 million and \$7.7 million at June 30, 2016 and December 31, 2015, respectively.

(2) Asset-backed U.S. obligations are related to financing transactions involving revenue earning equipment.

(3) The notional amount of executed interest rate swaps designated as fair value hedges was \$825 million at June 30, 2016 and December 31, 2015.

(4) See Note 2, "Recent Accounting Pronouncements," for further discussion of the presentation of debt issuance costs.

We maintain a \$1.2 billion global revolving credit facility with a syndicate of twelve lending institutions led by Bank of America N.A., Bank of Tokyo-Mitsubishi UFJ, Ltd., BNP Paribas, Mizuho Corporate Bank, Ltd., Royal Bank of Canada, Lloyds Bank Plc, U.S. Bank National Association and Wells Fargo Bank, N.A. The facility matures in January 2020. The agreement provides for annual facility fees which range from 7.5 basis points to 25 basis points based on Ryder's long-term credit ratings. The annual facility fee is currently 10 basis points, which applies to the total facility size of \$1.2 billion.

The credit facility is used primarily to finance working capital but can also be used to issue up to \$75 million in letters of credit (there were no letters of credit outstanding against the facility at June 30, 2016). At our option, the interest rate on borrowings under the credit facility is based on LIBOR, prime, federal funds or local equivalent rates. The credit facility contains no provisions limiting its availability in the event of a material adverse change to Ryder's business operations; however, the credit facility does contain standard representations and warranties, events of



default, cross-default provisions and certain affirmative and negative covenants.

In order to maintain availability of funding, we must maintain a ratio of debt to consolidated net worth of less than or equal to 300%. Net worth, as defined in the credit facility, represents shareholders' equity excluding any accumulated other comprehensive income or loss associated with our pension and other postretirement plans. The ratio at June 30, 2016 was 214%. At June 30, 2016, there was \$424.7 million available under the credit facility.

RYDER SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

Our global revolving credit facility enables us to refinance short-term obligations on a long-term basis. Short-term commercial paper obligations not expected to require the use of working capital are classified as long-term as we have both the intent and ability to refinance on a long-term basis. In addition, we have the intent and ability to refinance the current portion of certain long-term debt on a long-term basis. At June 30, 2016, we classified \$599.6 million of short-term commercial paper and \$351.9 million of current debt obligations as long-term. At December 31, 2015, we classified \$547.1 million of short-term commercial paper and \$300.0 million of current debt obligations as long-term.

In February 2016, we issued \$300 million of unsecured medium-term notes maturing in November 2021. The proceeds from these notes were used to pay off maturing debt and for general corporate purposes. If these notes are downgraded below investment grade following, and as a result of, a change in control, the note holders can require us to repurchase all or a portion of the notes at a purchase price equal to 101% of principal plus accrued and unpaid interest.

We have a trade receivables purchase and sale program, pursuant to which we sell certain of our domestic trade accounts receivable to a bankruptcy remote, consolidated subsidiary of Ryder, that in turn sells, on a revolving basis, an ownership interest in certain of these accounts receivable to committed purchasers. The subsidiary is considered a VIE and is consolidated based on our control of the entity's activities. We use this program to provide additional liquidity to fund our operations, particularly when it is cost effective to do so. The costs under the program may vary based on changes in interest rates. The available proceeds that may be received under the program are limited to \$175 million. If no event occurs which causes early termination, the 364-day program will expire on October 21, 2016. The program contains provisions restricting its availability in the event of a material adverse change to our business operations or the collectibility of the collateralized receivables. Sales of receivables under this program are accounted for as secured borrowings based on our continuing involvement in the transferred assets. No amounts were outstanding under the program at June 30, 2016 or December 31, 2015.

At June 30, 2016 and December 31, 2015, we had letters of credit and surety bonds outstanding totaling \$339.1 million and \$345.7 million, respectively, which primarily guarantee the payment of insurance claims.

The fair value of total debt (excluding capital lease and asset-backed U.S. obligations) at June 30, 2016 and December 31, 2015 was approximately \$5.31 billion and \$5.06 billion, respectively. For publicly-traded debt, estimates of fair value were based on market prices. For other debt, fair value was estimated based on a model-driven approach using rates currently available to us for debt with similar terms and remaining maturities. The fair value measurements of our publicly-traded debt and other debt were classified within Level 2 of the fair value hierarchy. The carrying amounts reported in the Consolidated Condensed Balance Sheets for "Cash and cash equivalents," "Receivables, net" and "Accounts payable" approximate fair value because of the immediate or short-term maturities of these financial instruments.

## 7. DERIVATIVES

From time to time, we enter into interest rate derivatives to manage our fixed and variable interest rate exposure and to better match the repricing of debt instruments to that of our portfolio of assets. We assess the risk that changes in interest rates will have either on the fair value of debt obligations or on the amount of future interest payments by monitoring changes in interest rate exposures and by evaluating hedging opportunities. We regularly monitor interest rate risk attributable to both our outstanding or forecasted debt obligations as well as any offsetting hedge positions. This risk management process involves the use of analytical techniques, including cash flow sensitivity analyses, to

estimate the expected impact of changes in interest rates on our future cash flows.

As of June 30, 2016, we had interest rate swaps outstanding which are designated as fair value hedges for certain debt obligations, with a total notional value of \$825 million and maturities through 2020. Interest rate swaps are measured at fair value on a recurring basis using Level 2 fair value inputs. The fair value of these interest rate swaps was approximately \$21.0 million as of June 30, 2016, and was presented in "Direct financing leases and other assets" in our Consolidated Condensed Balance Sheets. Changes in the fair value of our interest rate swaps were offset by changes in the fair value of the hedged debt instruments. Accordingly, there was no ineffectiveness related to the interest rate swaps.

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

## 8. SHARE REPURCHASE PROGRAMS

In December 2015, our Board of Directors authorized a share repurchase program intended to mitigate the dilutive impact of shares issued under our employee stock plans (the December 2015 program). Under the December 2015 program, management is authorized to repurchase (i) up to 1.5 million shares of common stock, the sum of which will not exceed the number of shares issued to employees under the Company's employee stock plans from December 1, 2015 to December 9, 2017, plus (ii) 0.5 million shares issued to employees that were not repurchased under the Company's previous share repurchase program. The December 2015 program limits aggregate share repurchases to no more than 2 million shares of Ryder common stock. Share repurchases of common stock are made periodically in open-market transactions and are subject to market conditions, legal requirements and other factors. Management may establish prearranged written plans for the Company under Rule 10b5-1 of the Securities Exchange Act of 1934 as part of the December 2015 program, which allow for share repurchases during Ryder's quarterly blackout periods as set forth in the trading plan.

During the six months ended June 30, 2016 and June 30, 2015, we repurchased 321,718 shares for \$21.9 million and 69,107 shares for \$6.1 million, respectively.

## 9. ACCUMULATED OTHER COMPREHENSIVE LOSS

The following summary sets forth the components of accumulated other comprehensive loss, net of tax:

	Currency Translation Adjustments and Other (In thousands)	Net Actuarial Loss <sup>(1)</sup>	Prior Service (Cost)/ Credit <sup>(1)</sup>	Accumulated Other Comprehensive Loss
December 31, 2015	\$(136,020)	(576,993)	) 278	(712,735 )
Amortization	—	9,754	(72)	) 9,682
Other current period change	(18,578 )	(5,597)	) (5,425)	(29,600 )
June 30, 2016	\$(154,598)	(572,836)	) (5,219)	(732,653 )

	Currency Translation Adjustments and Other (In thousands)	Net Actuarial Loss <sup>(1)</sup>	Prior Service Credit <sup>(1)</sup>	Accumulated Other Comprehensive Loss
December 31, 2014	\$(36,087)	(585,941)	) 1,758	(620,270 )
Amortization	—	9,790	(712)	) 9,078
Other current period change	(30,345 )	(5,321)	) —	(35,666 )
June 30, 2015	\$(66,432)	(581,472)	) 1,046	(646,858 )

(1) These amounts are included in the computation of net periodic benefit cost. See Note 12, "Employee Benefit Plans," for further information.

The loss from currency translation adjustments in the six months ended June 30, 2016 of \$18.6 million was primarily due to the weakening of the British Pound against the U.S. Dollar, partially offset by the strengthening of the Canadian Dollar against the U.S. Dollar. The loss from currency translation adjustments in the six months ended June 30, 2015 of \$30.3 million was due to the weakening of the Canadian Dollar and British Pound against the U.S. Dollar.

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

## 10. EARNINGS PER SHARE

The following table presents the calculation of basic and diluted earnings per common share from continuing operations:

	Three months ended June 30, 2016		Six months ended June 30, 2016	
	2015		2015	
	(In thousands, except per share amounts)			
Earnings per share — Basic:				
Earnings from continuing operations	\$74,042	85,917	\$130,227	139,243
Less: Earnings allocated to unvested stock	(235 )	(246 )	(398 )	(393 )
Earnings from continuing operations available to common shareholders — Basic	\$73,807	85,671	\$129,829	138,850
Weighted average common shares outstanding — Basic	53,057	52,827	53,067	52,712
Earnings from continuing operations per common share — Basic	\$1.39	1.62	\$2.45	2.63
Earnings per share — Diluted:				
Earnings from continuing operations	\$74,042	85,917	\$130,227	139,243
Less: Earnings allocated to unvested stock	(234 )	(244 )	(397 )	(390 )
Earnings from continuing operations available to common shareholders — Diluted	\$73,808	85,673	\$129,830	138,853
Weighted average common shares outstanding — Basic	53,057	52,827	53,067	52,712
Effect of dilutive equity awards	320	468	303	492
Weighted average common shares outstanding — Diluted	53,377	53,295	53,370	53,204
Earnings from continuing operations per common share — Diluted	\$1.38	1.61	\$2.43	2.61
Anti-dilutive equity awards not included above	669	363	928	273

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

## 11. SHARE-BASED COMPENSATION PLANS

Share-based incentive awards are provided to employees under the terms of various share-based compensation plans (collectively, the “Plans”). The Plans are administered by the Compensation Committee of the Board of Directors and principally include at-the-money stock option, unvested stock and cash awards. Unvested stock awards include grants of market-based, performance-based and time-vested restricted stock rights. Under the terms of our Plans, dividends may be paid on our unvested stock awards but are not paid unless the award vests. Upon vesting, the amount of the dividends paid is equal to the aggregate dividends declared on common shares during the period from the grant date of the award until the date the shares underlying the award are delivered.

The following table provides information on share-based compensation expense and income tax benefits recognized during the periods:

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(In thousands)			
Stock option and stock purchase plans	\$1,904	1,956	\$3,777	4,257
Unvested stock	3,209	3,548	6,224	6,912
Share-based compensation expense	5,113	5,504	10,001	11,169
Income tax benefit	(1,715 )	(1,860 )	(3,370 )	(3,743 )
Share-based compensation expense, net of tax	\$3,398	3,644	\$6,631	7,426

The following table is a summary of compensation expense recognized for market-based cash awards in addition to the share-based compensation expense reported in the previous table:

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(In thousands)			
Cash awards	\$177	281	\$328	464

Total unrecognized pre-tax compensation expense related to all share-based compensation arrangements at June 30, 2016 was \$26.8 million and is expected to be recognized over a weighted-average period of 1.9 years.

The following table is a summary of the awards granted under the Plans during the periods presented:

	Six months ended June 30,	
	2016	2015
	(In thousands)	
Stock options	513	362
Market-based restricted stock rights	34	19
Performance-based restricted stock rights	45	42
Time-vested restricted stock rights	129	80

Total	721	503
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## RYDER SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)  
(unaudited)

## 12. EMPLOYEE BENEFIT PLANS

Components of net pension expense were as follows:

	Three months ended June 30, 2016		Six months ended June 30, 2015	
	2016	2015	2016	2015
	(In thousands)			
Pension Benefits				
Company-administered plans:				
Service cost	\$3,005	3,566	\$6,405	7,193
Interest cost	27,093	22,048	49,332	43,935
Expected return on plan assets	(22,667 )	(25,021 )	(45,752 )	(49,921 )
Amortization of:				
Net actuarial loss	8,600	7,664	16,565	15,472
Prior service cost/(credit)	2,740	(74 )	2,740	(150 )
	18,771	8,183	29,290	16,529
Union-administered plans	2,406	2,113	4,728	4,285
Net pension expense	\$21,177	10,296	\$34,018	20,814
Company-administered plans:				
U.S.	\$19,263	8,599	\$30,437	17,491
Non-U.S.	(492 )	(416 )	(1,147 )	(962 )
	18,771	8,183	29,290	16,529
Union-administered plans	2,406	2,113	4,728	4,285
Net pension expense	\$21,177	10,296	\$34,018	20,814

During the second quarter of 2016, we determined that certain pension benefit improvements made in 2009 had not been fully reflected in our projected benefit obligation. Because the amounts were not material to our consolidated financial statements in any individual prior period, and the cumulative amount is not material to 2016 results, we recognized a one-time, non-cash charge of \$7.7 million in "Selling, general and administrative expenses" and a \$12.8 million pre-tax increase to "Accumulated other comprehensive loss" in our second quarter 2016 consolidated condensed financial statements to correctly state the pension benefit obligation and account for these 2009 benefit improvements.

During the six months ended June 30, 2016 we contributed \$42.3 million to our pension plans. In 2016, we expect total contributions to our pension plans to be approximately \$80 million. We also maintain other postretirement benefit plans that are not reflected in the above table. The amount of postretirement benefit expense was not material for the three or six months ended June 30, 2016.

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

## 13. OTHER MATTERS

We are a party to various claims, complaints and proceedings arising in the ordinary course of our continuing business operations including but not limited to those relating to commercial and employment claims, environmental matters, risk management matters (e.g., vehicle liability, workers' compensation, etc.) and administrative assessments primarily associated with operating taxes. We have established loss provisions for matters in which losses are probable and can be reasonably estimated. For matters from continuing operations, we believe that the resolution of these claims, complaints and legal proceedings will not have a material effect on our consolidated condensed financial statements.

Our estimates regarding potential losses and materiality are based on our judgment and assessment of the claims utilizing currently available information. Although we will continue to reassess our reserves and estimates based on future developments, our objective assessment of the legal merits of such claims may not always be predictive of the outcome and actual results may vary from our current estimates.

Although we discontinued our South American operations in 2009, we continue to be party to various federal, state and local legal proceedings involving labor matters, tort claims and tax assessments. We have established loss provisions for any matters where we believe a loss is probable and can be reasonably estimated. Other than with respect to the matters discussed below, we believe that such losses will not have a material effect on our consolidated condensed financial statements.

In Brazil, we were assessed \$5 million in prior years for various federal income taxes and social contribution taxes for the 1997 and 1998 tax years. These federal tax assessments were overturned in the lower courts; however, there is a reasonable possibility that these rulings could be reversed and we would be required to pay the assessments. We believe it is more likely than not that our position will ultimately be sustained if appealed and no amounts have been reserved for these matters. We are entitled to indemnification for a portion of any resulting liability on these federal tax claims which, if honored, would reduce the amount of any potential loss.

## 14. SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental cash flow information was as follows:

	Six months ended June 30,	
	2016	2015
	(In thousands)	
Interest paid	\$71,141	69,681
Income taxes paid	10,233	9,970
Changes in accounts payable related to purchases of revenue earning equipment	(105,480)	124,766
Operating and revenue earning equipment acquired under capital leases	777	5,847

RYDER SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

15. SEGMENT REPORTING

Our primary measurement of segment financial performance, defined as “Earnings Before Tax” (EBT) from continuing operations, includes an allocation of Central Support Services (CSS) and excludes non-operating pension costs and professional fees. CSS represents those costs incurred to support all business segments, including human resources, finance, corporate services, public affairs, information technology, health and safety, legal, marketing and corporate communications. The objective of the EBT measurement is to provide clarity on the profitability of each segment and, ultimately, to hold leadership of each segment accountable for their allocated share of CSS costs. Certain costs are not attributable to any segment and remain unallocated in CSS, including costs for investor relations, public affairs and certain executive compensation.

Our Fleet Management Solutions (FMS) segment leases revenue earning equipment and provides fuel, maintenance and other ancillary services to the Dedicated Transportation Solutions (DTS) and Supply Chain Solutions (SCS) segments. Inter-segment revenue and EBT are accounted for at rates similar to those executed with third parties. EBT related to inter-segment equipment and services billed to customers (equipment contribution) are included in both FMS and the segment which served the customer and then eliminated (presented as “Eliminations”).

The following tables set forth financial information for each of our segments and provide a reconciliation between segment EBT and earnings from continuing operations before income taxes for the three and six months ended June 30, 2016 and 2015. Segment results are not necessarily indicative of the results of operations that would have occurred had each segment been an independent, stand-alone entity during the periods presented.

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

	FMS	DTS	SCS	Eliminations	Total
	(In thousands)				
For the three months ended June 30, 2016					
Revenue from external customers	\$1,043,430	258,262	402,052	—	1,703,744
Inter-segment revenue	108,083	—	—	(108,083)	—
Total revenue	\$1,151,513	258,262	402,052	(108,083)	1,703,744
Segment EBT	\$111,184	16,472	28,371	(12,766)	143,261
Unallocated CSS					(11,215)
Non-operating pension costs					(7,617)
Pension-related charge <sup>(1)</sup>					(7,650)
Earnings from continuing operations before income taxes					\$116,779
Segment capital expenditures paid <sup>(2)</sup>	\$502,040	363	37,139	—	539,542
Unallocated CSS					5,609
Capital expenditures paid					\$545,151
For the three months ended June 30, 2015					
Revenue from external customers	\$1,042,476	223,514	396,941	—	1,662,931
Inter-segment revenue	106,873	—	—	(106,873)	—
Total revenue	\$1,149,349	223,514	396,941	(106,873)	1,662,931
Segment EBT	\$122,452	12,435	27,699	(11,588)	150,998
Unallocated CSS					(10,924)
Non-operating pension costs					(4,688)
Professional fees <sup>(3)</sup>					(1,939)
Earnings from continuing operations before income taxes					\$133,447
Segment capital expenditures paid	\$761,542	646	3,570	—	765,758
Unallocated CSS					10,218
Capital expenditures paid					\$775,976

During the second quarter of 2016, we determined that certain pension benefit improvements made in 2009 were (1) not fully reflected in our projected benefit obligation. We recognized a charge of \$7.7 million related to these benefit improvements.

(2) Excludes revenue earning equipment acquired under capital leases.

(3) Charges related to professional fees associated with cost savings initiatives.

## RYDER SYSTEM, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS — (Continued)

(unaudited)

	FMS	DTS	SCS	Eliminations	Total
	(In thousands)				
For the six months ended June 30, 2016					
Revenue from external customers	\$2,039,545	503,104	790,767	—	3,333,416
Inter-segment revenue	209,896	—	—	(209,896)	—
Total revenue	\$2,249,441	503,104	790,767	(209,896)	3,333,416
Segment EBT	\$194,105	30,740	48,167	(24,510)	248,502
Unallocated CSS					(20,880)
Non-operating pension costs					(14,485)
Pension-related charge <sup>(1)</sup>					(7,650)
Earnings from continuing operations before income taxes					\$205,487
Segment capital expenditures paid <sup>(2)</sup>	\$1,062,325	880	44,462	—	1,107,667
Unallocated CSS					12,515
Capital expenditures paid					\$1,120,182
For the six months ended June 30, 2015					
Revenue from external customers	\$2,025,916	436,173	767,995	—	3,230,084
Inter-segment revenue	210,583	—	—	(210,583)	—
Total revenue	\$2,236,499	436,173	767,995	(210,583)	3,230,084
Segment EBT	\$212,170	21,405	43,388	(23,122)	253,841
Unallocated CSS					(22,866)
Non-operating pension costs					(9,571)
Professional fees <sup>(3)</sup>					(3,780)
Earnings from continuing operations before income taxes					\$217,624
Segment capital expenditures paid <sup>(2)</sup>	\$1,300,285	1,355	9,557	—	1,311,197
Unallocated CSS					18,021
Capital expenditures paid					\$1,329,218

During the second quarter of 2016, we determined that certain pension benefit improvements made in 2009 were (1) not fully reflected in our projected benefit obligation. We recognized a charge of \$7.7 million related to these benefit improvements.

(2) Excludes revenue earning equipment acquired under capital leases.

(3) Charges related to professional fees associated with cost savings initiatives.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION  
AND RESULTS OF OPERATIONS

OVERVIEW

The following discussion should be read in conjunction with the unaudited Consolidated Condensed Financial Statements and notes thereto included under Item 1. In addition, reference should be made to our audited Consolidated Financial Statements and notes thereto and related Management's Discussion and Analysis of Financial Condition and Results of Operations included in the 2015 Annual Report on Form 10-K.

Ryder System, Inc. (Ryder) is a global leader in transportation and supply chain management solutions. We report our financial performance based on three segments: (1) FMS, which provides full service leasing, commercial rental, contract maintenance, and contract-related maintenance of trucks, tractors and trailers to customers principally in the U.S., Canada and the U.K.; (2) DTS, which provides vehicles and drivers as part of a dedicated transportation solution in the U.S.; and (3) SCS, which provides comprehensive supply chain solutions including distribution and transportation services in North America and Asia. Dedicated transportation services provided as part of an integrated, multi-service, supply chain solution to SCS customers are reported in the SCS business segment.

We operate in highly competitive markets. Our customers select us based on numerous factors including service quality, price, technology and service offerings. As an alternative to using our services, customers may choose to provide these services for themselves, or may choose to obtain similar or alternative services from other third-party vendors. Our customer base includes enterprises operating in a variety of industries including automotive, industrial, food and beverage service, consumer packaged goods (CPG), transportation and warehousing, technology and healthcare, retail, housing, business and personal services, and paper and publishing.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)

Operating results were as follows:

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
	2016	2015	2016	2015	Three Months	Six Months
(In thousands, except per share amounts)						
Total revenue	\$ 1,703,744	1,662,931	\$ 3,333,416	3,230,084	2 %	3 %
Operating revenue <sup>(1)</sup>	1,449,713	1,392,618	2,855,726	2,692,904	4 %	6 %
EBT	\$ 116,779	133,447	\$ 205,487	217,624	(12)%	(6 )%
Comparable EBT <sup>(2)</sup>	132,046	140,074	227,622	230,975	(6 )%	(1 )%
Earnings from continuing operations	74,042	85,917	130,227	139,243	(14)%	(6 )%
Comparable earnings from continuing operations <sup>(2)</sup>	83,307	87,952	143,481	145,231	(5 )%	(1 )%
Net earnings	73,750	85,159	129,544	137,948	(13)%	(6 )%
Earnings per common share (EPS) — Diluted						
Continuing operations	\$ 1.38	1.61	\$ 2.43	2.61	(14)%	(7 )%
Comparable <sup>(2)</sup>	1.56	1.65	2.68	2.72	(5 )%	(1 )%
Net earnings	1.38	1.59	2.42	2.59	(13)%	(7 )%

(1) Non-GAAP financial measure. Refer to the “Non-GAAP Financial Measures” section for a reconciliation of total revenue to operating revenue and the reasons why management believes this measure is important to investors.

Non-GAAP financial measures. Refer to the “Non-GAAP Financial Measures” section for a reconciliation of EBT, (2) net earnings and earnings per diluted common share to the comparable measures and the reasons why management believes these measures are important to investors.

Total revenue increased 2% to \$1.70 billion and operating revenue increased 4% to \$1.45 billion in the second quarter of 2016. For the first half of 2016, total revenue increased 3% to \$3.33 billion and operating revenue increased 6% to \$2.86 billion. These increases reflect higher revenue across all business segments, partially offset by negative impacts from foreign exchange. Increased total revenue was also partially offset by lower fuel costs passed through to customers.

FMS total revenue in the second quarter was consistent with the prior year as higher operating revenue was partially offset by lower fuel prices passed through to customers and a negative impact from foreign exchange. FMS total revenue in the first half of 2016 increased as higher operating revenue was partially offset by lower fuel prices passed through to customers and a negative impact from foreign exchange. FMS operating revenue growth in both periods was due to growth in the full service lease fleet and higher prices on replacement vehicles, partially offset by lower demand in the commercial rental product line. The increase in DTS and SCS total revenue was driven by operating revenue growth, partially offset by lower fuel costs passed through to customers in the second quarter and first half of 2016. Increased subcontracted transportation also contributed to DTS total revenue growth, while lower subcontracted transportation partially offset total revenue growth in SCS. DTS and SCS operating revenue growth was due to new business, increased volumes and higher pricing in the second quarter and first half of 2016.

EBT decreased 12% in the second quarter of 2016 to \$116.8 million and 6% in the first half of 2016, reflecting lower commercial rental and used vehicle results, partially offset by higher full service lease results, lower insurance costs in DTS and increased pricing, new business and increased volumes in DTS and SCS. The 2016 EBT decrease also

reflects a \$7.7 million pension-related charge related to certain 2009 pension benefit improvements that were not fully reflected in our pension benefit obligation. EBT was negatively impacted by foreign exchange in the second quarter and first half of 2016 by 100 basis points.



## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)

## CONSOLIDATED RESULTS

## Lease and Rental

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
	2016	2015	2016	2015	Three Months	Six Months
	(Dollars in thousands)					
Lease and rental revenues	\$798,387	779,046	\$1,566,141	1,508,070	2 %	4 %
Cost of lease and rental	555,302	531,308	1,107,792	1,049,730	5 %	6 %
Gross margin	243,085	247,738	458,349	458,340	(2)%	— %
Gross margin %	30	% 32	% 29	% 30	%	

Lease and rental revenues represent full service lease and commercial rental product offerings within our FMS segment. Revenues increased 2% in the second quarter of 2016 and 4% in the first half of 2016 primarily driven by a 5% larger average full service lease fleet and higher prices on replacement vehicles, partially offset by lower commercial rental revenue reflecting lower demand. Foreign exchange negatively impacted revenue growth by 100 basis points.

Cost of lease and rental represents the direct costs related to lease and rental revenues. These costs consist of depreciation of revenue earning equipment, maintenance costs (primarily repair parts and labor), and other costs such as licenses, insurance and operating taxes. Cost of lease and rental excludes interest costs from vehicle financing. Cost of lease and rental increased 5% in the second quarter and 6% in the first half of 2016 primarily due to higher depreciation and maintenance costs from a larger average lease fleet, partially offset by lower depreciation on a smaller average rental fleet (7% lower in the second quarter and 2% lower in the first half of 2016). Cost of lease and rental benefited by approximately \$9 million in the second quarter of 2016 and by \$17 million in the first half of 2016 due to changes in estimated residual values effective January 1, 2016. Foreign exchange also reduced cost of lease and rental by 100 basis points.

Lease and rental gross margin decreased 2% in the second quarter and remained consistent with the first half of 2015. Lease and rental gross margin as a percentage of revenue decreased to 30% in the second quarter and 29% in the first half of 2016. The decrease in gross margin dollars in the second quarter of 2016 was due to lower commercial rental demand, partially offset by higher prices on replacement vehicles and lease fleet growth as well as benefits from improved residual values. The decrease in gross margin as a percentage of revenue in the second quarter and first half of 2016 reflects lower commercial rental fleet utilization, partially offset by benefits from improved residual values.

## Services

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
	2016	2015	2016	2015	Three Months	Six Months
	(Dollars in thousands)					
Services revenue	\$785,791	737,170	\$1,544,918	1,430,874	7 %	8 %
Cost of services	646,129	603,488	1,277,843	1,185,818	7 %	8 %
Gross margin	139,662	133,682	267,075	245,056	4 %	9 %
Gross margin %	18	% 18	% 17	% 17	%	

Services revenue represents all the revenues associated with our DTS and SCS segments as well as contract maintenance, contract-related maintenance and fleet support services associated with our FMS segment. Services revenue increased 7% in the second quarter and 8% in the first half of 2016 due to new business, increased volumes and higher pricing in the SCS and DTS segments. The contract-related maintenance and contract maintenance product lines benefited from growth in fleet size, and contract-related maintenance revenue also increased from higher volumes. These increases were partially offset by lower fuel prices passed through to our DTS and SCS customers. Foreign exchange also negatively impacted revenue growth by 100 basis points.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)

Cost of services represents the direct costs related to services revenue and is primarily comprised of salaries and employee-related costs, subcontracted transportation (purchased transportation from third parties) and maintenance costs. Cost of services increased 7% in the second quarter of 2016 and 8% in the first half of 2016 due to higher volumes, partially offset by lower fuel costs and lower insurance costs. Foreign exchange reduced cost of services by 100 basis points.

Services gross margin increased 4% in the second quarter and 9% in the first half of 2016. Services gross margin as a percentage of revenue in second quarter of 2016 and first half of 2016 were consistent with prior periods. The increase in gross margin dollars reflects higher pricing in our DTS and SCS segments. Gross margin dollars also benefited from new business and higher volumes in our SCS and DTS segments, growth in full service lease fleet size and higher volumes in the contract-related business and growth in the contract maintenance fleet.

## Fuel

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
	2016	2015	2016	2015	Three Months	Six Months
	(Dollars in thousands)					
Fuel services revenue	\$ 119,566	146,715	\$ 222,357	291,140	(19)%	(24)%
Cost of fuel services	115,478	142,176	214,379	278,465	(19)%	(23)%
Gross margin	4,088	4,539	7,978	12,675	(10)%	(37)%
Gross margin %	3	% 3	% 4	% 4	%	

Fuel services revenue represents fuel services provided to our FMS customers. Fuel services revenue decreased 19% in the second quarter of 2016 and 24% in the first half of 2016 due to lower fuel prices passed through to customers.

Cost of fuel services includes the direct costs associated with providing our customers with fuel. These costs include fuel, salaries and employee-related costs of fuel island attendants and depreciation of our fueling facilities and equipment. Cost of fuel services decreased 19% in the second quarter and 23% in the first half of 2016 as a result of lower fuel prices.

Fuel services gross margin decreased 10% in the second quarter and 37% in the first half of 2016. Fuel services gross margin as a percentage of revenue remained at 3% in the second quarter and 4% in the first half of 2016 compared to the same periods of 2015. Fuel is largely a pass-through to customers for which we realize minimal changes in margin during periods of steady market fuel prices. However, fuel services margin is impacted by sudden increases or decreases in market fuel prices during a short period of time as customer pricing for fuel is established based on trailing market fuel costs. Fuel services gross margin was favorably impacted by rapid decreases in the market fuel prices during the first quarter of 2015.

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
	2016	2015	2016	2015	Three Months	Six Months
	(In thousands)					
Other operating expenses	\$ 27,796	29,582	\$ 57,947	61,955	(6)%	(6)%

Other operating expenses include costs related to our owned and leased facilities within the FMS segment, such as facility depreciation, rent, purchased insurance, utilities and taxes. These facilities are utilized to provide maintenance

to our lease, rental, contract maintenance and fleet support services customers. Other operating expenses decreased 6% in the second quarter and first half of 2016 largely due to lower utility costs for FMS facilities.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
	2016	2015	2016	2015	Three Month	Six Months
(Dollars in thousands)						
Selling, general and administrative expenses (SG&A)	\$222,448	214,868	\$433,661	421,473	4 %	3 %
Percentage of total revenue	13	% 13	% 13	% 13	%	
Percentage of operating revenue	15	% 15	% 15	% 16	%	

SG&A expenses increased 4% in the second quarter of 2016 compared with the year-earlier period and increased 3% in the first half of 2016. The increase in the second quarter and first half of 2016 is primarily due to increased pension expenses, partially offset by lower professional fees, compensation-related expenses and foreign exchange. Foreign exchange reduced the growth in SG&A expenses by 100 basis points. Pension expense, which primarily impacts SG&A expenses, increased \$10.9 million in the second quarter of 2016 and \$13.2 million in the first half of 2016 due to a one-time charge of \$7.7 million related to pension benefit improvements made in 2009 that were not fully reflected in our pension benefit obligation, as well as the impact of a lower asset return assumption and a higher discount rate.

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
	2016	2015	2016	2015	Three Months	Six Months
(Dollars in thousands)						
Gains on used vehicles, net	\$12,000	29,985	\$31,129	57,193	(60)%	(46)%

Gains on used vehicles, net includes gains from sales of used vehicles as well as the costs associated with used vehicles such as write-downs of vehicles to fair market values. Gains on used vehicles, net decreased to \$12 million in the second quarter of 2016 and \$31 million in the first half of 2016 due to higher fair market value write-downs and lower gains on the sale of used vehicles. Write-downs increased \$9.3 million in the second quarter and \$14.2 million in the first half of 2016 due to an increase in the used vehicle inventory and lower pricing. Global average proceeds per unit in the second quarter decreased from the prior year reflecting a 15% decrease in tractor proceeds per unit and a 4% decrease in truck proceeds per unit. Global proceeds per unit in the first half of 2016 decreased from the prior year reflecting a 12% decrease in tractor proceeds per unit, partially offset by a 1% increase in truck proceeds per unit in the first half of 2016.

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
	2016	2015	2016	2015	Three Month	Six Months
(Dollars in thousands)						
Interest expense	\$37,268	39,075	\$75,157	75,877	(5)%	(1)%
Effective interest rate	2.7	% 3.1	% 2.7	% 3.1	%	

Interest expense decreased 5% to \$37.3 million in the second quarter of 2016 and 1% to \$75.2 million in the first half of 2016 reflecting a lower effective interest rate, partially offset by higher average outstanding debt. The increase in average outstanding debt reflects planned higher vehicle capital spending. The lower effective interest rate in 2016

reflects the replacement of higher interest rate debt with debt issuances at lower rates.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)

Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
2016	2015	2016	2015	Three Months	Six Months

(Dollars in thousands)

Miscellaneous income, net \$5,456 1,028 \$7,721 3,665 431% 111 %

Miscellaneous income, net consists of investment income on securities used to fund certain benefit plans, interest income, gains from sales of operating property, foreign currency transaction gains and other non-operating items. The increase in the second quarter and first half of 2016 is primarily driven by increased gains from sales of operating property and equipment.

Three months ended June 30,		Six months ended June 30,		Change 2016/2015	
2016	2015	2016	2015	Three Months	Six Months

(Dollars in thousands)

Provision for income taxes \$42,737 47,530 \$75,260 78,381 (10)% (4 )%

Effective tax rate from continuing operations 36.6 % 35.6 % 36.6 % 36.0 %

Provision for income taxes decreased 10% in the second quarter of 2016 and 4% in the first half of 2016. The decrease in the provision for income taxes reflects lower taxable earnings, partially offset by a higher effective income tax rate. Our effective income tax rate from continuing operations increased to 36.6% in both the second quarter and first half of 2016. The effective tax rates in the prior year benefited from enacted tax law changes in multiple jurisdictions, which decreased the provision for income taxes by \$1.9 million in the prior year.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - (Continued)

## OPERATING RESULTS BY SEGMENT

	Three months ended June 30,		Six months ended June 30,		Change 2016/2015			
	2016	2015	2016	2015	Three Months	Six Months		
	(Dollars in thousands)							
Revenue:								
Fleet Management Solutions	\$1,151,513	1,149,349	\$2,249,441	2,236,499	—	%	1	%
Dedicated Transportation Solutions	258,262	223,514	503,104	436,173	16		15	
Supply Chain Solutions	402,052	396,941	790,767	767,995	1		3	
Eliminations	(108,083 )	(106,873 )	(209,896 )	(210,583 )	1		—	
Total	\$1,703,744	1,662,931	\$3,333,416	3,230,084	2	%	3	%
Operating Revenue: <sup>(1)</sup>								
Fleet Management Solutions	\$995,238	959,050	\$1,957,562	1,858,237	4	%	5	%
Dedicated Transportation Solutions	194,292	176,805	384,565	342,635	10		12	
Supply Chain Solutions	331,558	320,053	653,974	615,494	4		6	
Eliminations	(71,375 )	(63,290 )	(140,375 )	(123,462 )	13		14	
Total	\$1,449,713	1,392,618	\$2,855,726	2,692,904	4	%	6	%
EBT:								
Fleet Management Solutions	\$111,184	122,452	\$194,105	212,170	(9 )	%	(9 )	%
Dedicated Transportation Solutions	16,472	12,435	30,740	21,405	32		44	
Supply Chain Solutions	28,371	27,699	48,167	43,388	2		11	
Eliminations	(12,766 )	(11,588 )	(24,510 )	(23,122 )	10		6	
	143,261	150,998	248,502	253,841	(5 )		(2 )	
Unallocated Central Support Services	(11,215 )	(10,924 )	(20,880 )	(22,866 )	3		(9 )	
Non-operating pension costs	(7,617 )	(4,688 )	(14,485 )	(9,571 )	62		51	
Other items	(7,650 )	(1,939 )	(7,650 )	(3,780 )	NM		NM	
Earnings from continuing operations before income taxes	\$116,779	133,447	\$205,487	217,624	(12)%		(6 )%	

Non-GAAP financial measures. Refer to the "Non-GAAP Financial Measures" section for a reconciliation of total revenue to operating revenue and the reasons why management believes these measure are important to investors.

(1) The reconciliations for each segment's total revenue to operating revenue are set forth in this "Operating Results by Segment" section on pages 27 (FMS), 30 (DTS) and 31 (SCS).

As part of management's evaluation of segment operating performance, we define the primary measurement of our segment financial performance as "Earnings Before Taxes" (EBT) from continuing operations, which includes an allocation of Central Support Services (CSS), and excludes non-operating pension costs and other items discussed in Note 15, "Segment Reporting," in the Notes to Consolidated Condensed Financial Statements. CSS represents those costs incurred to support all segments, including human resources, finance, corporate services and public affairs, information technology, health and safety, legal, marketing and corporate communications.

The objective of the EBT measurement is to provide clarity on the profitability of each segment and, ultimately, to hold leadership of each segment accountable for their allocated share of CSS costs. Segment results are not necessarily indicative of the results of operations that would have occurred had each segment been an independent, stand-alone entity during the periods presented. Certain costs are not attributable to any segment and remain unallocated in CSS, including costs for investor relations, public affairs and certain executive compensation.



Inter-segment revenue and EBT are accounted for at rates similar to those executed with third parties. EBT related to inter-segment equipment and services billed to customers (equipment contribution) are included in FMS, DTS and SCS and then eliminated (presented as “Eliminations” in the table above). Prior year amounts have been revised to conform to the current period presentation.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION  
AND RESULTS OF OPERATIONS - (Continued)

The following table sets forth equipment contribution included in EBT for our DTS and SCS segments:

Three months		Six months		Change 2016/2015	
ended June		ended June			
30,		30,			
2016	2015	2016	2015	Three	Six
				Months	Months
(Dollars in thousands)					

Equipment Contribution:

Dedicated Transportation Solutions \$8,449 8,020 \$