SABRE HOLDINGS CORP
Form 10-Q
August 05, 2005

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

ý **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the Quarterly Period Ended June 30, 2005.

OR

o **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 1-12175.

SABRE HOLDINGS CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**75-2662240**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3150 Sabre Drive, Southlake, Texas	**76092**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code **(682) 605-1000**

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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 periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

Indicate by checkmark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ý No o

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class A Common Stock, $.01 par value **131,116,780** as of July 29, 2005

INDEX

SABRE HOLDINGS CORPORATION

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SABRE HOLDINGS CORPORATION

CONSOLIDATED BALANCE SHEETS

(In thousands)

	June 30, 2005 (Unaudited)	December 31, 2004
Assets		
Current assets		
Cash	$ 47,427	$ 49,671
Marketable securities	756,613	787,353
Accounts receivable, net	431,341	349,621
Prepaid expenses	78,355	63,521
Deferred income taxes	31,105	23,349
Total current assets	1,344,841	1,273,515
Property and equipment		
Buildings and leasehold improvements	313,916	309,635
Furniture, fixtures and equipment	36,017	33,579
Computer equipment	118,586	120,515
Internally developed software	227,165	195,638
	695,684	659,367
Less accumulated depreciation and amortization	(299,578)	(272,026)
Total property and equipment	396,106	387,341
Deferred income taxes	7,665	9,955
Investments in joint ventures	158,125	176,249
Goodwill and intangible assets, net	1,015,231	988,600
Other assets, net	198,464	182,317
Total assets	$ 3,120,432	$ 3,017,977
Liabilities and stockholders equity		
Current liabilities		
Accounts payable	$ 146,681	$ 177,207
Net rate program related liabilities	148,594	58,313
Accrued compensation and related benefits	56,279	80,448
Accrued subscriber incentives	91,288	84,357
Deferred revenues	25,058	24,906
Other accrued liabilities	227,641	183,061
Total current liabilities	695,541	608,292
Pensions and other postretirement benefits	154,692	154,537
Other liabilities	22,164	23,101
Minority interests	11,456	5,143
Long-term capital lease obligation	162,322	161,114

Public and other notes payable		438,278		439,309
Commitments and contingencies				
Stockholders equity				
Preferred stock: $0.01 par value; 20,000 shares authorized; no shares issued				
Class A Common Stock: $0.01 par value; 250,000 shares authorized; 145,855 shares issued at June 30, 2005 and December 31, 2004		1,459		1,459
Additional paid-in capital		1,275,213		1,289,574
Retained earnings		722,398		644,360
Accumulated other comprehensive loss		(26,594)		(9,426)
Less treasury stock at cost: 14,770 and 12,913 shares, respectively		(336,497)		(299,486)
Total stockholders equity		1,635,979		1,626,481
Total liabilities and stockholders equity	$	3,120,432	$	3,017,977

See Notes to Consolidated Financial Statements.

SABRE HOLDINGS CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited) (In thousands, except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Revenues	**$ 619,255**	$ 550,903	**$ 1,201,143**	$ 1,090,656
Cost of revenues	**365,736**	307,777	**703,759**	619,292
Gross profit	**253,519**	243,126	**497,384**	471,364
Other operating expenses				
Selling, general and administrative	**163,620**	139,455	**328,263**	286,084
Amortization of intangible assets	**6,793**	15,228	**14,821**	27,349
Total other operating expenses	**170,413**	154,683	**343,084**	313,433
Operating income	**83,106**	88,443	**154,300**	157,931
Other income (expense)				
Interest income	**6,100**	3,306	**10,469**	6,541
Interest expense	**(8,388)**	(6,431)	**(16,002)**	(12,858)
Gain on sale of investment			**20,594**	
Loss on derivative instrument	**(9,994)**		**(9,994)**	
Other, net	**988**	6,057	**1,597**	6,485
Total other income (expense)	**(11,294)**	2,932	**6,664**	168
Income before provision for income taxes	**71,812**	91,375	**160,964**	158,099
Provision for income taxes	**27,925**	32,438	**59,396**	56,125
Net earnings	**$ 43,887**	$ 58,937	**$ 101,568**	$ 101,974
Earnings per common share				
Basic	$ 0.34	$ 0.43	$ 0.78	$ 0.74
Diluted	$ 0.34	$ 0.42	$ 0.78	$ 0.73

See Notes to Consolidated Financial Statements.

SABRE HOLDINGS CORPORATION

CONSOLIDATED CONDENSED STATEMENT OF STOCKHOLDERS EQUITY

SIX MONTHS ENDED JUNE 30, 2005

(Unaudited) (In thousands)

	Class A Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total
Balance at December 31, 2004	$ 1,459	$ 1,289,574	$ 644,360	$ (9,426)	$ (299,486)	$ 1,626,481
Issuance of class A common stock pursuant to:						
Stock option plans		(516)			2,206	1,690
Restricted stock plan		(18,744)			16,993	(1,751)
Employee stock purchase plan		(882)			4,777	3,895
Tax benefit from exercise of employee stock options		127				127
Dividends, $0.09 per common share			(23,530)			(23,530)
Purchases of treasury stock					(60,987)	(60,987)
Stock based compensation for employees		5,663				5,663
Comprehensive income:						
Net earnings			101,568			101,568
Unrealized loss on foreign currency forward and option contracts, net of deferred income taxes				(8,103)		(8,103)
Unrealized gain on investments, net of deferred income taxes				579		579
Unrealized foreign currency translation loss				(9,783)		(9,783)
Other				139		139
Total comprehensive income						84,400
Other		(9)				(9)
Balance at June 30, 2005	$ 1,459	$ 1,275,213	$ 722,398	$ (26,594)	$ (336,497)	$ 1,635,979

See Notes to Consolidated Financial Statements.

SABRE HOLDINGS CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited) (In thousands)

	Six Months Ended June 30, 2005	2004
Operating Activities		
Net earnings	$ 101,568	$ 101,974
Adjustments to reconcile net earnings to cash provided by operating activities:		
Depreciation and amortization	53,334	64,448
Stock-based compensation for employees	5,663	6,433
Allowance for doubtful accounts	687	9,790
Deferred income taxes	2,757	(3,180)
Loss on derivative instrument	9,994	
Joint venture equity loss	2,661	7,621
Gain on sale of investment	(20,594)	
Other	(2,231)	(4,431)
Changes in operating assets and liabilities:		
Accounts receivable	(78,409)	(34,482)
Prepaid expenses	(23,620)	5,328
Other assets	2,788	20,270
Accrued compensation and related benefits	(24,169)	(4,293)
Accounts payable and other accrued liabilities	30,936	73,065
Net rate program related liabilities	90,282	40,835
Pensions and other postretirement benefits	294	5,075
Other liabilities	2,434	(2,102)
Cash provided by operating activities	154,375	286,351
Investing Activities		
Additions to property and equipment	(40,609)	(35,908)
Purchases of marketable securities	(5,837,810)	(4,138,162)
Sales of marketable securities	5,869,207	4,030,234
Proceeds from sale of investment	26,013	
Loans and investments to joint venture partners	(12,538)	(32,934)
Acquisitions (net of cash acquired)	(66,773)	
Purchase of foreign currency options	(10,000)	
Other investing activities		(5,000)
Cash used for investing activities	(72,510)	(181,770)
Financing Activities		
Proceeds from issuance of common stock	3,834	10,802
Dividends paid	(23,530)	(20,906)
Purchases of treasury stock	(63,213)	(101,925)
Other financing activities, net	(1,200)	(1,712)
Cash used for financing activities	(84,109)	(113,741)
Decrease in cash	(2,244)	(9,160)
Cash at beginning of period	49,671	40,862
Cash at end of period	$ 47,427	$ 31,702

See Notes to Consolidated Financial Statements.

SABRE HOLDINGS CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. General Information

Sabre Holdings Corporation (Sabre Holdings) is a Delaware holding company. Sabre Inc. is the principal operating subsidiary and sole direct subsidiary of Sabre Holdings. Sabre Inc. or its direct or indirect subsidiaries conduct all of our businesses. In this Quarterly Report on Form 10-Q, references to the company , we , our , ours and us refer to Sabre Holdings and its consolidated subsidiaries unless otherwise stated or the context otherwise requires.

We are a world leader in travel commerce, marketing travel products and providing distribution and technology solutions for the travel industry. We operate in multiple travel distribution channels: the travel agency channel, the consumer-direct channel and the business-direct channel. Through our *Sabre*®[(1)] global distribution system (the *Sabre* system or *Sabre* GDS) subscribers can access information about, and can book reservations for, among other things, airline trips, hotel stays, car rentals, cruises and tour packages. Our *Sabre Travel Network*™ business operates the *Sabre* GDS and markets and distributes travel-related products and services through the travel agency and corporate channels. We engage in consumer-direct and business-direct travel marketing and distribution through our *Travelocity*® business. In addition, our *Sabre Airline Solutions*™ business is a leading provider of technology and services, including development and consulting services, to airlines and other travel providers.

2. Summary of Significant Accounting Policies

Basis of Presentation The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, these financial statements contain all adjustments, consisting of normal recurring accruals, necessary to present fairly the financial position, results of operations and cash flows for the periods indicated. The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Operating results for the three and six months ended June 30, 2005 are not necessarily indicative of results that may be expected for any other interim period or for the year ended December 31, 2005. Our quarterly financial data should be read in conjunction with our consolidated financial statements for the year ended December 31, 2004 (including the notes thereto), set forth in Sabre Holdings Corporation s Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 11, 2005.

We consolidate all of our majority-owned subsidiaries and companies that are not variable interest entities over which we exercise control through majority voting rights. We would also consolidate all variable interest entities of which we are the primary beneficiary. However, no entities are currently consolidated due to us being the primary beneficiary through operating agreements, financing agreements, or other arrangements (including variable interests held in variable interest entities). In the third or fourth quarter of 2005, we expect to loan additional funds or may possibly choose to participate in future anticipated capital calls of Zuji Holdings Limited (Zuji), a joint venture in which we hold a 13% equity stake through direct and indirect ownership, and which we account for under the equity method. Without a pro rata contribution from the other equity holders, we could be required to consolidate Zuji under the guidance of the Financial Accounting Standards Board (FASB) Interpretation No. 46R, *Consolidation of Variable Interest Entities.* See *Management s Discussion and Analysis Business Trends Investments in Travelocity.*

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(1) Agent 59, Custom Trip, Direct Connect, Hotel Spotlight, GetThere, Internet View, Jurni, Jurni Network, JurniCruise, MySabre, Nexion, Sabre, Sabre Airline Solutions, Sabre Holdings, the Sabre Holdings logo, Sabre Travel Network, SabreSonic, SabreSurround, Showtickets.com, Site 59, Site59.com, SynXis, TotalTrip, Travelocity, Travelocity Business, and Travelocity.com are trademarks of affiliates of Sabre Holdings Corporation. All other trademarks are the property of their respective owners.

The consolidated financial statements include our accounts after elimination of all significant intercompany balances and transactions. We account for our interests in joint ventures and investments in common stock of other companies that we do not control but over which we exert significant influence using the equity method, with our share of their results classified as revenues. Investments in the common stock of other companies over which we do not exert significant influence are accounted for at cost. We periodically evaluate for impairment equity and debt in entities accounted for as cost investments by reviewing updated financial information provided by the investee, including valuation information from new financing transactions by the investee and information relating to competitors of investees when available. If we determine that a cost method investment is other than temporarily impaired, the carrying value of the investment is reduced to its estimated fair value. To date, write-downs of investments have been insignificant to our results of operations.

Reclassifications Certain reclassifications have been made to the 2004 financial statements to conform to the 2005 presentation. These reclassifications are not material, either individually or in the aggregate, to our financial statements.

Advertising Prior to 2005, certain advertising costs were deferred within the fiscal year to future interim periods where the benefit of that advertising extended beyond the quarter in which they occurred. Beginning in 2005 and all subsequent interim periods, advertising costs are expensed as incurred with no deferral within the fiscal year. Our current advertising strategy is to generate immediate interest in travel promotions and products where returns are more immediate than in the past when our strategy was developing overall brand awareness.

This timing change resulted in lower selling, general and administrative expenses for the three months ended June 30, 2005 of an estimated $2 million and higher net income of $1 million or $.01 per share. For the six months ended June 30, 2005, this timing change resulted in higher selling, general and administrative expenses of an estimated $6 million and lower net income of $4 million or $.03 per share. Due to this timing change, we expect to recognize lower advertising expenses in subsequent quarters of 2005 than in the comparable periods of the prior year, offset by any increases in advertising volume.

Had we employed the revised methodology in 2004, selling, general and administrative expenses would have been an estimated $2 million higher and net income an estimated $1 million, or $.01 per share lower for the three months ended June 30, 2004. For the six months ended June 30, 2004, selling, general and administrative expenses would have been an estimated $14 million higher and net income an estimated $9 million, or $.07 per share lower under the revised methodology.

Net Rate Program Related Liabilities To facilitate the provision of travel accommodations to travelers, we enter into agreements with travel suppliers for the right to market their products, services and other content offerings at pre-determined net rates. Net rate travel offerings can include air travel, hotel stays, and dynamically packaged combinations (via Travelocity *TotalTrip* and Last Minute Deals). We market those offerings to travelers at a price that includes an amount sufficient to pay the travel supplier for its charge for providing the travel accommodations, along with any applicable taxes we expect will be invoiced to us by the travel supplier on that charge, as well as additional amounts representing our service fees. For this type of business model, we require pre-payment by the traveler at the time of booking. The net rate program related liability included on our balance sheet represents the amounts we have collected from the customer that are payable to the travel supplier as well as the amount received from the customer for our service fees that will be recognized as revenue when the travel has been consumed.

8

2. Summary of Significant Accounting Policies

Earnings Per Share Basic earnings per share excludes any dilutive effect of stock awards or options. The number of shares used in the diluted earnings per share calculations includes the dilutive effect of any stock awards or options.

The following table reconciles weighted average shares used in computing basic and diluted earnings per common share (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	**2004**	**2005**	**2004**
Denominator for basic earnings per common share - weighted-average shares	129,286	137,397	129,767	138,309
Dilutive effect of stock awards and options	756	2,583	628	1,497
Denominator for diluted earnings per common share - adjusted weighted-average shares	130,042	139,980	130,395	139,806

Options to purchase approximately 21,216,956 and 20,029,511 weighted-average shares of our Class A Common Stock, par value $0.01 per share (Common Stock), were outstanding during the three and six month periods ending June 30, 2005, respectively, but were excluded from the computation of diluted earnings per share because the effect would be anti-dilutive. For the corresponding periods in 2004, anti-dilutive options to purchase approximately 13,512,386 and 15,628,627 weighted average shares of our Common Stock were excluded from the computation of diluted earnings per share. The increase in anti-dilutive weighted average shares from June 30, 2004 to June 30, 2005 is due primarily to a lower market price for shares of our Common Stock. The decrease in weighted average shares from June 30, 2004 to June 30, 2005 is due to our share repurchase programs.

Stock Awards and Options Currently, we account for stock awards and stock option grants using the intrinsic value method set forth in Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25), and related interpretations. Generally, no compensation expense is recognized for stock option grants to employees if the exercise price is at or above the fair market value of the underlying stock on the date of grant. Compensation expense relating to other stock awards is recognized over the period during which the employee renders service to us necessary to earn the award.

We have not made, and will not make, loans (including the acceptance of promissory notes) for the exercise of our stock options or the purchase of our Common Stock.

On December 16, 2004, the FASB issued Statement of Financial Accounting Standards No. 123 (Revised 2004), *Share-Based Payment* (FAS 123R), which is a revision of FASB Statement No. 123, *Accounting for Stock-Based Compensation* (FAS 123). FAS 123R supersedes APB 25 and amends FASB Statement No. 95, *Statement of Cash Flows.* Generally, the approach in FAS 123R is similar to the approach described in FAS 123. However, FAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized on the income statement based on their fair values. Pro forma footnote disclosure is no longer an alternative once the standard is required to be adopted.

We expect to adopt FAS 123R on January 1, 2006 and we intend to use the modified prospective method. We expect the adoption of FAS 123R to have a significant impact on our results of operations, although it will have no impact on our overall financial position. FAS 123R also requires that the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow, as required under the current guidance. We expect the impact of adoption of FAS 123R to be somewhat similar to that disclosed in our current pro forma disclosures, however, levels of share-based payments granted in the future could cause results to be different.

The following table summarizes the pro forma effect of stock-based compensation on our net earnings and net earnings per share for the three and six months ended June 30, 2005 and 2004, as if we had accounted for such compensation at fair value (in thousands, except per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Net earnings as reported	$ 43,887	$ 58,937	$ 101,568	$ 101,974
Add stock compensation expense determined under intrinsic value method, net of income taxes	1,874	1,889	3,552	3,972
Less total stock-based employee compensation expense determined under fair value based method for all awards, net of income taxes	(8,022)	(7,978)	(16,291)	(16,266)
Pro forma net earnings	$ 37,739	$ 52,848	$ 88,829	$ 89,680
Net earnings per common share, as reported:				
Basic	$ 0.34	$ 0.43	$ 0.78	$ 0.74
Diluted	$ 0.34	$ 0.42	$ 0.78	$ 0.73
Net earnings per common share, pro forma:				
Basic	$ 0.29	$ 0.38	$ 0.68	$ 0.65
Diluted	$ 0.29	$ 0.38	$ 0.68	$ 0.64

3. Significant Events

AOL Agreement - On January 21, 2004, we revised the terms of and extended our agreement with America Online (AOL) so that Travelocity would continue to be the exclusive reservations engine for AOL s internet properties through March 2006, with an optional year after that. Under the revised terms of the agreement, we benefit from more strategically aligned terms for placement within AOL s brands. Further, we are obligated for a payment of up to $13 million for 2005. In February of 2005, AOL agreed to revise the contract terms to incorporate a formula by which the anticipated $13 million payment may be reduced if AOL does not achieve certain revenue targets under the agreement. The revised terms also allow AOL to continue and expand in the travel search arena through its sites and partners. The anticipated payment, along with the unamortized portion of fixed payments previously paid under the original contract, is being expensed on a straight-line basis over the remaining term of the agreement. For 2005, this expense is expected to be approximately $23 million.

Yahoo! Agreement - We have an agreement with Yahoo! whereby we are the exclusive air, car and hotel booking engine on Yahoo! Travel. That agreement was set to expire on December 31, 2005. In July 2005, we agreed with Yahoo! to extend our relationship through December 31, 2006. Travelocity will continue to be the exclusive provider of air, car, and hotel products to Yahoo! Travel. Our fees for 2006 will consist of a fixed payment of $26 million, which includes payments for purchased advertising and corporate services; plus we will pay a productivity component, whereby Yahoo! is paid a percentage of the transaction services revenue generated through the Yahoo! network. $10 million of the $26 million fixed fee could be less depending on revenue performance compared to 2005 levels, and a formula agreed to between us and Yahoo!. We believe this variability provides necessary downside protections into the contract extension to preserve the value of our investment in that partnership. The revised terms also allow Yahoo! to continue and expand in the travel search arena throughout the Yahoo! network. Pursuant to this agreement, Travelocity has decided to not participate in Yahoo! s Farechase metasearch model under either the Travelocity brand or the Yahoo! travel brand.

Gulf Air Joint Venture - On December 31, 2004, we entered into a joint venture with Gulf Air, a leading airline carrier in the Middle East, for which we will pay $31 million throughout 2005, $20 million of which has been paid as of June 30, 2005. The joint venture, Sabre Travel Network Middle East, is owned 60% by Sabre Travel Network and 40% by Gulf Air and will further extend our travel network products and services into the Middle East region. The joint venture will provide technology services, bookable travel products and distribution services for travel agencies, corporations and travel suppliers in the region. In addition, Sabre Airline Solutions entered into a five-year revised contract with Gulf Air to provide the *SabreSonic*™ suite of products for passenger management, as well as additional operational software and consulting services. The goodwill resulting from this transaction is not deductible for tax purposes. The results of the Gulf Air joint venture will be consolidated into our financial results. The following table summarizes the allocation of the purchase price and the amounts allocated to goodwill (in thousands):

Subscriber contracts (3 year useful life)	$	10,679
Net assets		517
Goodwill		20,008
Total	$	31,204

Acquisition of SynXis - On January 19, 2005, we completed the acquisition of SynXis Corporation (SynXis), a provider of the *SynXis*® reservation management, distribution and technology services for hotels, for approximately $41 million in cash including acquisition costs, of which $37 million has been paid as of June 30, 2005. This acquisition enables Sabre Travel Network to further build on our capabilities and offerings to hoteliers, to leverage new hotel content for all of our travel agents, and to extend reservation technology currently used at approximately 6,000 hotels, primarily in the United States and Europe. SynXis will continue to operate under the SynXis name as a wholly-owned subsidiary of Sabre Inc. The acquired goodwill is not deductible for tax purposes. Intangible assets subject to amortization will be amortized over their respective lives. The following table summarizes the allocation of the purchase price and the amounts allocated to goodwill (in thousands):

Assets acquired net of liabilities assumed	$	5,506
Purchased technology (5 year useful life)		3,900
Customer relationships (8 year useful life)		10,700
Tradenames		1,800
Goodwill		19,226
Total	$	41,132

Sale of Karavel Investment - On March 11, 2005, we sold our interest in Karavel SA, a French tour operator, to Opodo Limited. We received approximately $26 million (Euro 20 million) in cash proceeds in connection with the sale and recorded a $21 million gain in other income.

Cost Reductions - We incurred approximately $4 million in severance and related cost during 2004 for a workforce reduction of which approximately $1 million remains accrued for as of June 30, 2005. In June 2005, we announced a plan for a workforce reduction and accrued approximately $3 million for severance and related costs due to employees under the plan. We expect the majority of the amounts accrued under this plan will be paid out in the third quarter of 2005 and expect savings of $13 million to $16 million through 2006 and beyond.

4. Pension and Other Post Retirement Benefit Plans

The components of net periodic benefit cost of defined benefit pension plans and other defined benefit postretirement plans for the three and six months ended June 30, 2005 and 2004 are presented in the tables below (in thousands).

Pension Benefits	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
Components of net periodic benefit cost:	**2005**	**2004**	**2005**	**2004**
Service cost	$ 1,465	$ 982	$ 3,019	$ 2,286
Interest cost	5,356	3,220	10,807	8,223
Expected return on plan assets	(6,033)	(3,378)	(12,009)	(8,986)
Amortization of transition asset	(3)	(3)	(6)	(8)
Amortization of prior service cost	54	(8)	69	36
Amortization of actuarial loss	1,065	699	2,378	1,405
Net periodic benefit cost	$ 1,904	$ 1,512	$ 4,258	$ 2,956

Other Benefits	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
Components of net periodic benefit cost:	**2005**	**2004**	**2005**	**2004**
Service cost	$ 54	$ 788	$ 623	$ 1,583
Interest cost	180	1,859	2,162	3,730
Amortization of transition asset	4	3	8	7
Amortization of prior service cost	56	78	(3,077)	159
Amortization of actuarial loss	218	679	1,591	1,375
Net periodic benefit cost	$ 512	$ 3,407	$ 1,307	$ 6,854

There were no contributions to fund our various defined benefit pension plans during the six months ended June 30, 2005. During the three months ended June 30, 2004, $5 million was contributed to fund our defined benefit pension plans. We are evaluating making contributions during the remainder of 2005. Annual contributions to our defined benefit pension plans are based on several factors that may vary from year to year, therefore, past contributions are not always indicative of future contributions.

On January 21, 2005, the final regulations implementing the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 were issued. We have considered the effects of the regulations and we do not expect them to have a significant impact on our financial condition or results of operations.

5. Income Taxes

The provision for income taxes relating to continuing operations differs from amounts computed at the statutory federal income tax rate as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Income tax provision at statutory federal income tax rate	$ 25,134	$ 31,982	$ 56,337	$ 55,335
State income taxes, net of federal benefit	1,435	420	3,186	2,200
Other, net	1,356	36	(127)	(1,410)
Total provision for income taxes	$ 27,925	$ 32,438	$ 59,396	$ 56,125

6. Derivatives

In order to hedge our operational exposure to foreign currency movements, we are a party to certain foreign currency forward and option contracts. We have designated these instruments as cash flow hedges. Amounts reclassified from other comprehensive income to earnings due to the settlement of forward and option contracts were $2 million during both the three months ended June 30, 2005 and 2004 and $4 million and $6 million for the six months ended June 30, 2005 and 2004, respectively. No hedging ineffectiveness was recorded in earnings relating to the forwards or options during the six months ended June 30, 2005 and 2004. The estimated fair values of the foreign currency forward and option contracts were a liability of $1 million at June 30, 2005 and an asset of $12 million at December 31, 2004. These foreign currency forward and option contracts were recorded in other accrued liabilities at June 30, 2005 and prepaid assets at December 31, 2004 on the Consolidated Balance Sheet.

We are also a party to certain interest rate swap contracts. We have designated the swaps as fair value hedges of our public notes payable and capital lease obligation. No hedging ineffectiveness was recorded in earnings relating to our interest rate swaps during the six months ended June 30, 2005 or 2004. The estimated fair values of the interest rate swaps were a net asset of $10 million at June 30, 2005 and a net asset of $9 million at December 31, 2004, the values of which are included in other assets on the Consolidated Balance Sheet.

In order to offset our currency exposure in relation to the acquisition of lastminute.com, in May 2005, we purchased an option to acquire British Pounds Sterling (GBP) and Euros (EUR) at a fixed rate at or near the closing of the transaction for $10 million. Due to the strengthening of the U.S. Dollar against these currencies, the value of the option has declined to less than $1 million at June 30, 2005 and is included as a prepaid asset on the Consolidated Balance Sheet. We recorded a loss on this option of $10 million to the Consolidated Statement of Income during the quarter ended June 30, 2005. This option does not qualify for hedge accounting and therefore is marked to market each reporting period to the income statement.

Shortly after completion of the lastminute.com shareholder vote on June 29, 2005, when the outlook for completion of the acquisition became more certain, we entered into forward contracts to purchase £578 million and 115 million Euros to lock in the U.S. Dollar price of the acquisition of lastminute.com. As of June 30, 2005, £190 million and 85 million Euros of these forward contracts had been entered into. These forward contracts do not qualify for hedge accounting and therefore are marked to market each reporting period to the income statement. We recorded a loss of less than $1 million for the instruments outstanding for the quarter ended June 30, 2005. The fair value of these forwards is recorded in other accrued liabilities.

7. Business Segments

We are a world leader in travel commerce, marketing travel products and providing distribution and technology solutions for the travel industry. We operate in multiple travel distribution channels: the travel agency channel, the consumer-direct channel and the corporate or business-direct channel. Through our *Sabre* GDS subscribers can access information about, and can book reservations for, among other things, airline trips, hotel stays, car rentals, cruises and tour packages. Our Sabre Travel Network business operates the *Sabre* GDS and markets and distributes travel-related products and services through the travel agency and corporate channels. We engage in consumer-direct and business-direct travel marketing and distribution through our Travelocity business. In addition, our Sabre Airline Solutions business is a leading provider of technology and services, including development and consulting services, to airlines and other travel providers.

Our reportable segments are strategic business segments that offer different products and services and are managed separately because each business requires different market strategies. The accounting policies of the segments are the same as those used in our consolidated results. We account for significant intersegment transactions as if the transactions were to third parties, that is, at estimated current market prices. The majority of the intersegment revenues and cost of revenues are between Travelocity and Sabre Travel Network, consisting mainly of incentives paid by Sabre Travel Network to Travelocity for transactions processed through the *Sabre* GDS, data processing fees paid by Travelocity to Sabre Travel Network for transactions processed through the *Sabre* GDS, transaction fees paid by Travelocity to Sabre Travel Network for transactions facilitated through the *Sabre* GDS in which the travel supplier pays Travelocity directly, and fees paid by Sabre Travel Network to Travelocity for corporate trips booked through the *Travelocity*® online booking technology. In addition, Sabre Airline Solutions pays fees to Travelocity for airline trips booked through the *Travelocity* online booking technology. Personnel and related costs for the corporate headquarters, certain legal and professional fees, and other corporate charges are allocated to the segments through a management fee based on the relative size of the segments and usage of corporate resources or services. Depreciation expense on the corporate headquarters buildings and related facilities costs are allocated to the segments through a facility fee based on headcount. Benefits expense, including pension expense, postretirement benefits, medical insurance and workers compensation are allocated to the segments based on headcount.

Selected information for our three reportable segments for the three and six months ended June 30, 2005 and 2004 follows (in thousands). This presentation is consistent with the manner in which our management assesses the operating performance of our business segments.

	Three Months Ended June 30, 2005	Three Months Ended June 30, 2004	Six Months Ended June 30, 2005	Six Months Ended June 30, 2004
Revenues from external customers, excluding adjusting items:				
Sabre Travel Network	$ 416,619	$ 393,477	$ 830,321	$ 797,049
Travelocity	134,485	97,474	243,866	180,981
Sabre Airline Solutions	66,844	60,511	129,617	120,247
Total	$ 617,948	$ 551,462	$ 1,203,804	$ 1,098,277
Intersegment revenues:				
Sabre Travel Network	$ 8,939	$ 7,688	$ 14,895	$ 15,227
Travelocity	39,655	34,850	81,468	69,584
Total	$ 48,594	$ 42,538	$ 96,363	$ 84,811
Equity in net income/(loss) of equity method investees:				
Sabre Travel Network	$ 3,383	$ 6,222	$ 3,532	$ 5,947
Travelocity	(2,076)	(6,781)	(6,193)	(13,568)
Total	$ 1,307	$ (559)	$ (2,661)	$ (7,621)
Consolidated revenues:				
Sabre Travel Network	$ 428,941	$ 407,387	$ 848,748	$ 818,223
Travelocity	172,064	125,543	319,141	236,997
Sabre Airline Solutions	66,844	60,511	129,617	120,247
Elimination of intersegment revenues	(48,594)	(42,538)	(96,363)	(84,811)
Total	$ 619,255	$ 550,903	$ 1,201,143	$ 1,090,656

A summary of the adjusting items and reconciliation to consolidated operating income is set forth below (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Segment operating income (loss) excluding adjusting items:				
Sabre Travel Network	$ 71,536	$ 89,308	$ 152,824	$ 173,794
Travelocity	6,544	9,643	(5,236)	8,178
Sabre Airline Solutions	11,660	5,593	21,570	4,971
Net corporate allocations	321	(41)	334	629
Total	$ 90,061	$ 104,503	$ 169,492	$ 187,572
Impact of adjusting items on operating income (increase) / decrease:				
Sabre Travel Network:				
Intangibles amortization	$ 4,402	$ 7,349	$ 9,611	$ 11,517
Total Sabre Travel Network	$ 4,402	$ 7,349	$ 9,611	$ 11,517
Travelocity:				
Intangibles amortization	$ 1,614	$ 7,390	$ 3,617	$ 14,852
Stock compensation	376	1,318	831	3,255
Total Travelocity	$ 1,990	$ 8,708	$ 4,448	$ 18,107
Sabre Airline Solutions:				
Intangibles amortization	$ 563	$	$ 1,133	$
Total Sabre Airline Solutions	$ 563	$	$ 1,133	$
Corporate:				
Stock compensation		3		17
Total Corporate	$	$ 3	$	$ 17
Total operating income adjusting items	$ 6,955	$ 16,060	$ 15,192	$ 29,641
Consolidated operating income (loss):				
Sabre Travel Network	$ 67,134	$ 81,959	$ 143,213	$ 162,277
Travelocity	4,554	935	(9,684)	(9,929)
Sabre Airline Solutions	11,097	5,593	20,437	4,971
Net corporate allocations	321	(44)	334	612
Total	$ 83,106	$ 88,443	$ 154,300	$ 157,931

Segment operating income for Travelocity for 2005 includes the impact of changes in the timing of recognizing advertising expenses within the fiscal year. See Note 2.

8. Supplemental Guarantor/Non-Guarantor Financial Information

Certain obligations of Sabre Holdings have been solely guaranteed by its 100% owned operating subsidiary, Sabre Inc. There are currently no restrictions on Sabre Holdings ability to obtain funds from Sabre Inc. in the form of a dividend or loan other than typical dividend requirements under Delaware law. Additionally, there are no significant restrictions on Sabre Inc. s ability to obtain funds from its direct or indirect subsidiaries other than those that would exist under state or foreign law. Sabre Inc. is the sole direct subsidiary of Sabre Holdings. All other subsidiaries are direct or indirect subsidiaries of Sabre Inc. These other subsidiaries are all included in the non-guarantor financial statements. The following financial information presents condensed consolidating balance sheets, statements of income and statements of cash flows for Sabre Holdings, Sabre Inc. and non-guarantor subsidiaries. The information has been presented as if Sabre Holdings accounted for its ownership of Sabre Inc., and Sabre Inc. accounted for its ownership of the non-guarantor subsidiaries, using the equity method of accounting. Certain reclassifications have been made to the 2004 financial statements to conform to the 2005 presentation. These reclassifications are not material, either individually or in the aggregate, to our financial statements.

Sabre Inc. conducts the domestic operations of both the Sabre Travel Network and Sabre Airline Solutions segments. The operations of the Travelocity segment, the principal international operations of the Sabre Travel Network segment as well as the principal international operations of Sabre Airline Solutions, are conducted by the non-guarantor subsidiaries.

Sabre Inc. and certain non-guarantor subsidiaries are parties to various intercompany agreements that affect the amount of operating expenses reported in the following condensed consolidating statements of income. Among other things, fees are paid by Sabre Inc. to a non-guarantor subsidiary relating to the use of trademarks, tradenames, etc. owned by a non-guarantor subsidiary; incentive and marketing payments are made by Sabre Inc. to non-guarantor subsidiaries relating to the use and distribution of the *Sabre* system; and payments are made by non-guarantor subsidiaries to Sabre Inc. for access to the *Sabre* system under the terms of these agreements. During the six months ended June 30, 2005 and 2004, Sabre Inc. recognized operating expenses in connection with these agreements totaling approximately $165 million and $120 million, respectively. These amounts, and the corresponding amounts recognized by the non-guarantor subsidiaries are eliminated in consolidation.

UNAUDITED CONSOLIDATING CONDENSED BALANCE SHEETS

JUNE 30, 2005

(in thousands)

	Sabre Holdings	Sabre Incorporated	Non-Guarantor Subsidiaries	Eliminations	Sabre Consolidated
Assets					
Current Assets					
Cash and marketable securities	$	$ 747,509	$ 56,531	$	$ 804,040
Accounts receivable, net		289,677	141,664		431,341
Intercompany accounts receivable (payable)		(267,289)	267,289		
Other current assets		33,837	75,623		109,460
Total current assets		803,734	541,107		1,344,841
Property and equipment, net		342,635	53,471		396,106
Investment in subsidiaries	751,829	1,460,105		(2,211,934)	
Intercompany notes	1,303,205	(1,303,205)			
Investment in joint ventures		4,171	153,954		158,125
Goodwill and intangible assets, net		11,768	1,003,463		1,015,231
Other assets, net	14,904	119,254	71,971		206,129
Total assets	$ 2,069,938	$ 1,438,462	$ 1,823,966	$ (2,211,934)	$ 3,120,432