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CARNIVAL CORP
Form 10-K/A
May 07, 2003

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K/A
AMENDMENT NO. 3

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the fiscal year ended November 30, 2002

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 1-9610

CARNIVAL CORPORATION
(Exact name of registrant as specified in its charter)

Republic of Panama
(State or other jurisdiction of
incorporation or organization)

59-1562976
(I.R.S. Employer
Identification No.)

3655 N.W. 87th Avenue, Miami, Florida
(Address of principal executive offices)

33178-2428
(Zip Code)

Registrant's telephone number, including area code (305) 599-2600

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Name of exchange on which registered |
|------------------------------------|---|
| Common Stock (\$0.01 par value) | New York Stock Exchange, Inc. |

Securities registered pursuant to Section 12(g) of the Act: None.

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

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The aggregate market value of the voting stock held by non-affiliates of the Registrant is approximately \$7.1 billion based upon the closing market price on February 10, 2003 of a share of common stock on the New York Stock Exchange as reported by the Wall Street Journal.

At February 10, 2003 the Registrant had outstanding 586,969,154 shares of its common stock, \$.01 par value.

PART IV

Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

(a) (1)(2) Financial Statements and Schedules

The financial statements shown in Exhibit 13 are amended in their entirety to comply with Securities and Exchange Commission Regulation G and to reclassify our segment information in Note 12 to the financial statements to conform to our fiscal 2003 presentation, and are incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CARNIVAL CORPORATION

| | | |
|----------------------------------|--|-------------|
| /s/ Micky Arison Micky Arison | Chairman of the Board of Directors and Chief Executive Officer | May 5, 2003 |
|----------------------------------|--|-------------|

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| | | |
|----------------------------------|--|-------------|
| /s/ Micky Arison Micky Arison | Chairman of the Board of Directors and Chief Executive Officer | May 5, 2003 |
|----------------------------------|--|-------------|

| | | |
|--|---|-------------|
| /s/ Howard S. Frank Howard S. Frank | Vice Chairman of the Board of Directors and Chief Operating Officer | May 5, 2003 |
|--|---|-------------|

| | | |
|--|--|-------------|
| /s/ Gerald R. Cahill Gerald R. Cahill | Senior Vice President-Finance and Chief Financial and Accounting Officer | May 5, 2003 |
|--|--|-------------|

| | | |
|--|----------|-------------|
| /s/ Richard G. Capen, Jr. Richard G. Capen, Jr. | Director | May 5, 2003 |
|--|----------|-------------|

| | | |
|-------------------------|----------|-------------|
| /s/ Robert H. Dickinson | Director | May 5, 2003 |
|-------------------------|----------|-------------|

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Robert H. Dickinson

| | | |
|--|----------|-------------|
| /s/ Arnold W. Donald Arnold W. Donald | Director | May 5, 2003 |
| ----- Pier Luigi Foschi | Director | May 5, 2003 |
| ----- Baroness Hogg | Director | May 5, 2003 |
| /s/ A. Kirk Lanterman A. Kirk Lanterman | Director | May 5, 2003 |
| /s/ Modesto A. Maidique Modesto A. Maidique | Director | May 5, 2003 |
| ----- Sir John Parker | Director | May 5, 2003 |
| ----- Peter Ratcliffe | Director | May 5, 2003 |
| /s/ Stuart Subotnick Stuart Subotnick | Director | May 5, 2003 |
| /s/ Uzi Zucker Uzi Zucker | Director | May 5, 2003 |

CERTIFICATIONS

I, Micky Arison, certify that:

1. I have reviewed this annual report on Form 10-K/A of Carnival Corporation;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
 - (a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

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(c) Presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors:

(a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 5, 2003

/s/ Micky Arison
Micky Arison
Chairman of the Board of Directors
and Chief Executive Officer

I, Howard S. Frank, certify that:

1. I have reviewed this annual report on Form 10-K/A of Carnival Corporation;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

(a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

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(b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

(c) Presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors:

(a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 5, 2003

/s/ Howard S. Frank
Howard S. Frank
Vice Chairman of the Board of
Directors and Chief
Operating Officer

I, Gerald R. Cahill, certify that:

1. I have reviewed this annual report on Form 10-K/A of Carnival Corporation;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

(a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated

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subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

(b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

(c) Presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors:

(a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 5, 2003

/s/ Gerald R. Cahill
Gerald R. Cahill
Senior Vice President-Finance
and Chief Financial and
Accounting Officer

EXHIBIT 13

CARNIVAL CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except earnings per share)

| | Years Ended November 30, | | |
|----------|--------------------------|-------------|-------------|
| | 2002 | 2001 | 2000 |
| Revenues | \$4,368,269 | \$4,535,751 | \$3,778,542 |

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| | | | |
|---|-------------|------------|------------|
| Costs and Expenses | | | |
| Operating | 2,311,919 | 2,468,730 | 2,058,342 |
| Selling and administrative | 611,948 | 618,664 | 487,403 |
| Depreciation and amortization | 382,343 | 372,224 | 287,667 |
| Impairment charge | 20,000 | 140,378 | |
| Loss (income) from affiliated operations, net | | 44,024 | (37,828) |
| | 3,326,210 | 3,644,020 | 2,795,584 |
| Operating Income | 1,042,059 | 891,731 | 982,958 |
| Nonoperating (Expense) Income | | | |
| Interest income | 32,140 | 34,255 | 16,506 |
| Interest expense, net of capitalized interest | (110,740) | (120,692) | (41,372) |
| Other (expense) income, net | (4,080) | 108,649 | 8,460 |
| | (82,680) | 22,212 | (16,406) |
| Income Before Income Taxes | 959,379 | 913,943 | 966,552 |
| Income Tax Benefit (Expense), Net | 56,562 | 12,257 | (1,094) |
| Net Income | \$1,015,941 | \$ 926,200 | \$ 965,458 |
| Earnings Per Share | | | |
| Basic | \$1.73 | \$1.58 | \$1.61 |
| Diluted | \$1.73 | \$1.58 | \$1.60 |

The accompanying notes are an integral part of these consolidated financial statements.

CARNIVAL CORPORATION
CONSOLIDATED BALANCE SHEETS
(in thousands, except par value)

| ASSETS | November 30, | |
|---------------------------------------|--------------|--------------|
| | 2002 | 2001 |
| Current Assets | | |
| Cash and cash equivalents | \$ 666,700 | \$ 1,421,300 |
| Short-term investments | 39,005 | 36,784 |
| Accounts receivable, net | 108,327 | 90,763 |
| Inventories | 91,310 | 91,996 |
| Prepaid expenses and other | 148,420 | 113,798 |
| Fair value of hedged firm commitments | 78,390 | 204,347 |
| Total current assets | 1,132,152 | 1,958,988 |
| Property and Equipment, Net | 10,115,404 | 8,390,230 |
| Goodwill | 681,056 | 651,814 |
| Other Assets | 297,175 | 188,915 |
| Fair Value of Hedged Firm Commitments | 109,061 | 373,605 |
| | \$12,334,848 | \$11,563,552 |

LIABILITIES AND SHAREHOLDERS' EQUITY

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| | | |
|---|--------------|--------------|
| Current Liabilities | | |
| Current portion of long-term debt | \$ 148,642 | \$ 21,764 |
| Accounts payable | 268,687 | 269,467 |
| Accrued liabilities | 290,391 | 298,032 |
| Customer deposits | 770,637 | 627,698 |
| Dividends payable | 61,612 | 61,548 |
| Fair value of derivative contracts | 79,837 | 201,731 |
| Total current liabilities | 1,619,806 | 1,480,240 |
| Long-Term Debt | 3,011,969 | 2,954,854 |
| Deferred Income and Other Long-Term Liabilities | 170,814 | 157,998 |
| Fair Value of Derivative Contracts | 114,356 | 379,683 |
| Commitments and Contingencies (Notes 7 and 8) | | |
| Shareholders' Equity | | |
| Common stock; \$.01 par value; 960,000 shares authorized; 586,788 shares issued and outstanding at 2002 (620,019 shares issued at 2001) | 5,868 | 6,200 |
| Additional paid-in capital | 1,089,125 | 1,805,248 |
| Retained earnings | 6,325,850 | 5,556,296 |
| Unearned stock compensation | (11,181) | (12,398) |
| Accumulated other comprehensive income (loss) | 8,241 | (36,932) |
| Treasury stock; 33,848 shares at cost | | (727,637) |
| Total shareholders' equity | 7,417,903 | 6,590,777 |
| | \$12,334,848 | \$11,563,552 |

The accompanying notes are an integral part of these consolidated financial statements

CARNIVAL CORPORATION CONSOLIDATED STATEMENTS OF CASH FLOWS (in thousands)

| | Years Ended November 30, | | |
|---|--------------------------|------------|------------|
| | 2002 | 2001 | 2000 |
| OPERATING ACTIVITIES | | | |
| Net income | \$ 1,015,941 | \$ 926,200 | \$ 965,458 |
| Adjustments to reconcile net income to net cash provided by operating activities | | | |
| Depreciation and amortization | 382,343 | 372,224 | 287,667 |
| Impairment charge | 20,000 | 140,378 | |
| Gain on sale of investments in affiliates, net | | (116,698) | |
| Loss (income) from affiliated operations and dividends received | | 56,910 | (21,362) |
| Accretion of original issue discount | 19,294 | 2,174 | 199 |
| Other | 14,664 | 19,025 | (14,888) |
| Changes in operating assets and liabilities, excluding businesses acquired and consolidated | | | |
| (Increase) decrease in | | | |
| Receivables | (5,452) | (7,134) | (15,132) |
| Inventories | 1,667 | 8,455 | (8,205) |
| Prepaid expenses and other | (80,593) | 43,691 | (21,972) |
| (Decrease) increase in | | | |
| Accounts payable | (12,011) | (63,227) | 58,133 |
| Accrued and other liabilities | (28,380) | (335) | (5,977) |

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| | | | |
|---|-------------|-------------|-------------|
| Customer deposits | 141,559 | (142,727) | 55,614 |
| Net cash provided by operating activities | 1,469,032 | 1,238,936 | 1,279,535 |
| INVESTING ACTIVITIES | | | |
| Additions to property and equipment, net | (1,986,482) | (826,568) | (1,003,348) |
| Proceeds from sale of investments in affiliates | | 531,225 | |
| Proceeds from sale of property and equipment | 4,071 | 15,000 | 51,350 |
| Acquisition of consolidated subsidiary, net | | | (383,640) |
| Sale (purchase) of short-term investments, net | 2,213 | (33,395) | 22,170 |
| Other, net | (39,855) | (28,178) | 21,441 |
| Net cash used in investing activities | (2,020,053) | (341,916) | (1,292,027) |
| FINANCING ACTIVITIES | | | |
| Proceeds from issuance of long-term debt | 231,940 | 2,574,281 | 1,020,091 |
| Purchase of treasury stock | | | (705,137) |
| Principal repayments of long-term debt | (189,678) | (1,971,026) | (388,429) |
| Dividends paid | (246,323) | (245,844) | (254,333) |
| Proceeds from issuance of common stock, net | 7,240 | 5,274 | 7,811 |
| Other, principally debt issuance costs | (1,544) | (25,531) | |
| Net cash (used in) provided by financing activities | (198,365) | 337,154 | (319,997) |
| Effect of exchange rate changes on cash and cash equivalents | (5,214) | (2,156) | |
| Net (decrease) increase in cash and cash equivalents | (754,600) | 1,232,018 | (332,489) |
| Cash and cash equivalents at beginning of year | 1,421,300 | 189,282 | 521,771 |
| Cash and cash equivalents at end of year | \$ 666,700 | \$1,421,300 | \$ 189,282 |

The accompanying notes are an integral part of these consolidated financial statements.

CARNIVAL CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(in thousands)

| | Compre- hensive income | Additional Common paid-in capital | Retained earnings | Unearned stock compen- sation | Accumulated other comprehensive income (loss) | Treasury stock | Tota shar hold equi |
|---|------------------------------|---|----------------------|--|--|-------------------|------------------------------|
| Balances at | | | | | | | |
| November 30, 1999 | \$6,170 | \$1,757,408 | \$4,176,498 | \$ (9,945) | \$ 1,116 | | \$5,931,2 |
| Comprehensive income: | | | | | | | |
| Net income | \$ 965,458 | | 965,458 | | | | 965,4 |
| Foreign currency translation adjustment | (73,943) | | | | (73,943) | | (73,9 |
| Unrealized losses on marketable securities, net | (2,232) | | | | (2,232) | | (2,2 |
| Total comprehensive income | \$ 889,283 | | | | | | |
| Cash dividends | | | (250,923) | | | | (250,9 |

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| | | | | | | | |
|---|---------|-------------|-------------|------------|----------|-----------|-----------|
| Issuance of stock under stock plans | 6 | 15,489 | | (5,977) | | | 9,5 |
| Amortization of unearned stock compensation | | | | 3,639 | | | 3,6 |
| Effect of conforming Costa's reporting period | | | | (7,010) | | | (7,0 |
| Purchase of treasury stock | | | | | | (705,137) | (705,1 |
| Balances at | | | | | | | |
| November 30, 2000 | 6,176 | 1,772,897 | 4,884,023 | (12,283) | (75,059) | (705,137) | 5,870,6 |
| Comprehensive income: | | | | | | | |
| Net income | \$ | 926,200 | 926,200 | | | | 926,2 |
| Foreign currency translation adjustment, net | 45,781 | | | | 45,781 | | 45,7 |
| Unrealized gains on marketable securities, net | 6,411 | | | | 6,411 | | 6,4 |
| Minimum pension liability adjustment | (5,521) | | | | (5,521) | | (5,5 |
| Changes related to cash flow derivative hedges, net | (4,330) | | | | (4,330) | | (4,3 |
| Transition adjustment for cash flow derivative hedges | (4,214) | | | | (4,214) | | (4,2 |
| Total comprehensive income | \$ | 964,327 | | | | | |
| Cash dividends | | | (246,021) | | | | (246,0 |
| Issuance of stock under stock plans | 24 | 32,351 | | (4,601) | | (22,500) | 5,2 |
| Amortization of unearned stock compensation | | | | 4,486 | | | 4,4 |
| Effect of conforming Airtours' reporting period | | | | (7,906) | | | (7,9 |
| Balances at | | | | | | | |
| November 30, 2001 | 6,200 | 1,805,248 | 5,556,296 | (12,398) | (36,932) | (727,637) | 6,590,7 |
| Comprehensive income: | | | | | | | |
| Net income | \$ | 1,015,941 | 1,015,941 | | | | 1,015,9 |
| Foreign currency translation adjustment | 51,294 | | | | 51,294 | | 51,2 |
| Minimum pension liability adjustment | (9,166) | | | | (9,166) | | (9,1 |
| Unrealized gains on marketable securities, net | 2,579 | | | | 2,579 | | 2,5 |
| Changes related to cash flow derivative hedges, net | 466 | | | | 466 | | 4 |
| Total comprehensive income | \$ | 1,061,114 | | | | | |
| Cash dividends | | | (246,387) | | | | (246,3 |
| Issuance of stock under stock plans | 6 | 11,176 | | (3,942) | | | 7,2 |
| Retirement of treasury stock | (338) | (727,299) | | | | 727,637 | |
| Amortization of unearned stock compensation | | | | 5,159 | | | 5,1 |
| Balances at November 30, 2002 | \$5,868 | \$1,089,125 | \$6,325,850 | \$(11,181) | \$ 8,241 | \$ | \$7,417,9 |

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The accompanying notes are an integral part of these consolidated financial statements.

CARNIVAL CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - General

Description of Business

Carnival Corporation is a Panamanian corporation and, together with its consolidated subsidiaries, is referred to collectively in these consolidated financial statements and elsewhere in this 2002 Annual Report as "our," "us" and "we." We are a global cruise vacation and leisure travel provider that operates six cruise lines under the brand names Carnival Cruise Lines ("CCL"), Costa Cruises ("Costa"), Cunard Line ("Cunard"), Holland America Line ("Holland America"), Seabourn Cruise Line ("Seabourn") and Windstar Cruises ("Windstar") and a tour business, Holland America Tours ("Tours"). CCL operates eighteen cruise ships with destinations primarily to the Caribbean, the Bahamas and the Mexican Riviera. Holland America operates eleven cruise ships with destinations primarily to Alaska, the Caribbean and Europe. Costa operates eight cruise ships with destinations primarily to Europe, the Caribbean and South America. Cunard operates two premium/luxury cruise ships and Seabourn and Windstar each operate three luxury cruise ships with destinations to the Caribbean, Europe, Central America, Tahiti and other worldwide destinations. Our current fleet of 45 ships has a passenger capacity of 67,282 lower berths. Tours is a leading cruise/tour operator in Alaska and the Canadian Yukon. Tours also markets sightseeing packages, both separately and as a part of our cruise/tour packages.

Preparation of Financial Statements

The preparation of our consolidated financial statements in accordance with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the amounts reported and disclosed in our financial statements. Actual results could differ from these estimates. All material intercompany accounts, transactions and unrealized profits and losses on transactions within our consolidated group and with affiliates are eliminated in consolidation.

NOTE 2 - Summary Of Significant Accounting Policies

Basis of Presentation

We consolidate subsidiaries over which we have control, as typically evidenced by a direct ownership interest of greater than 50%. For affiliates where significant influence over financial and operating policies exists, as typically evidenced by a direct ownership interest from 20% to 50%, the investment is accounted for using the equity method. See Note 5.

Prior to our acquisition of Costa in late fiscal 2000, we accounted for our 50% interest in Costa using the equity method and recorded our portion of Costa's operating results as earnings from affiliated operations on a two-month lag basis. As of November 30, 2000, we changed how we report Costa's operating results from a two-month lag basis to reporting on Costa's current month's results. Accordingly, our November 30, 2000 consolidated balance sheet included Costa's November 30, 2000 balance sheet. The impact

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of conforming Costa's reporting period on our fiscal 2000 revenues, operating income and net income was not material. Commencing in fiscal 2001, Costa's results of operations were also consolidated on a current month basis in the same manner as our other wholly-owned subsidiaries. See Note 17.

Cash and Cash Equivalents and Short-Term Investments

Cash and cash equivalents include investments with original maturities of three months or less are stated at cost. At November 30, 2002 and 2001, cash and cash equivalents included \$616 million and \$1.38 billion of investments, respectively, primarily comprised of strong investment grade asset-backed debt obligations and money market funds.

Short-term investments are comprised of marketable debt and equity securities which are categorized as available for sale and, accordingly, are stated at their fair values. Unrealized gains and losses are included as a component of accumulated other comprehensive income (loss) ("AOCI") within shareholders' equity until realized. The specific identification method is used to determine realized gains or losses.

Inventories

Inventories consist primarily of provisions, spare parts, supplies and fuel carried at the lower of cost or market. Cost is determined using the weighted average or first-in, first-out method.

Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization was computed using the straight-line method over our estimates of average useful lives and residual values, as a percentage of original cost, as follows:

| | Residual Values | Years |
|--|--------------------|--|
| Ships | 15% | 30 |
| Buildings and improvements | 0-10% | 5-40 |
| Transportation equipment and other | 0-25% | 2-20 |
| Leasehold improvements, including port facilities | | Shorter of lease term or related asset life |

We review our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of these assets may not be fully recoverable. The assessment of possible impairment is based on our ability to recover the carrying value of our asset based on our estimate of its undiscounted future cash flows. If these estimated undiscounted future cash flows are less than the carrying value of the asset, an impairment charge is recognized for the excess, if any, of the assets carrying value over its estimated fair value (see Notes 4 and 16).

Dry-dock costs are included in prepaid expenses and are amortized to operating expenses using the straight-line method generally over one year.

Ship improvement costs that we believe add value to our ships are capitalized to the ships, and depreciated over the improvements' estimated useful lives, while costs of repairs and maintenance are charged to expense

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as incurred. We capitalize interest on ships and other capital projects during their construction period. Upon the replacement or refurbishment of previously capitalized ship components, these assets' estimated cost and accumulated depreciation are written-off and any resulting gain or loss is recognized in our results of operations. No such material gains or losses were recognized in fiscal 2002, 2001 or 2000. See Note 3.

Gains or losses on the sale of property and equipment are classified as nonoperating other income or expense. In fiscal 2002, we realized an \$8 million loss on the sale of the former Nieuw Amsterdam.

Goodwill

Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets" requires companies to stop amortizing goodwill and requires an annual, or when events or circumstances dictate a more frequent, impairment review of goodwill. Accordingly, upon adoption of SFAS No. 142 on December 1, 2001, we ceased amortizing our goodwill, all of which has been allocated to our Costa, Cunard and Holland America reportable units, which are all part of our reportable cruise segment. We completed the transitional and annual impairment tests of these reporting units' existing goodwill as of December 1, 2001 and July 31, 2002, respectively, and determined that their goodwill was not impaired. There has been no change to our goodwill carrying amount since November 30, 2001, other than the change resulting from using a different foreign currency translation rate at November 30, 2002 compared to November 30, 2001. If goodwill amortization, including goodwill expensed as part of our loss or income from affiliated operations, had not been recorded for fiscal 2001 and 2000 our adjusted net income and adjusted basic and diluted earnings per share would have been as follows (in thousands, except per share amounts):

| | 2001 | 2000 |
|-----------------------------|-----------|-----------|
| Net income | \$926,200 | \$965,458 |
| Goodwill amortization | 25,480 | 23,046 |
| Adjusted net income | \$951,680 | \$988,504 |
| Adjusted earnings per share | | |
| Basic | \$1.63 | \$1.65 |
| Diluted | \$1.62 | \$1.64 |

The SFAS No. 142 goodwill impairment review consists of a two-step process of first determining the fair value of the reporting unit and comparing it to the carrying value of the net assets allocated to the reporting unit. Fair values of our reporting units were determined based on our estimates of comparable market price or discounted future cash flows. If this fair value exceeds the carrying value, which was the case for our reporting units, no further analysis or goodwill write-down is required. If the fair value of the reporting unit is less than the carrying value of the net assets, the implied fair value of the reporting unit is allocated to all the underlying assets and liabilities, including both recognized and unrecognized tangible and intangible assets, based on their fair value. If necessary, goodwill is then written-down to its implied fair value.

Prior to fiscal 2002, our goodwill was reviewed for impairment pursuant to the same policy as our other long-lived assets as discussed above (see Note 4) and our goodwill was amortized over 40 years using the straight-line method. In addition, accumulated goodwill amortization at November 30, 2001 was \$118 million.

Derivative Instruments and Hedging Activities

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We utilize derivative instruments, such as forward foreign currency contracts to limit our exposure to fluctuations in foreign currency exchange rates and interest rate swaps to manage our interest rate exposure and to achieve a desired proportion of variable and fixed rate debt (see Note 11).

Our most significant contracts to buy foreign currency are forward contracts entered into to fix the cost in United States ("U.S.") dollars of seven of our foreign currency denominated shipbuilding commitments (see Note 7). If our shipbuilding contract is denominated in the functional currency of the cruise line that is expected to be operating the ship, we have not entered into a forward foreign currency contract to hedge that commitment.

Effective December 1, 2000, we adopted SFAS No. 133, as amended, "Accounting for Derivative Instruments and Hedging Activities," which requires that all derivative instruments be recorded on our balance sheet at their fair values. Derivatives that are not hedges must be recorded at fair value and the changes in fair value must be immediately included in earnings. If a derivative is a fair value hedge, then changes in the fair value of the derivative are offset against the changes in the fair value of the underlying hedged firm commitment. If a derivative is a cash flow hedge, then changes in the fair value of the derivative are recognized as a component of AOCI until the underlying hedged item is recognized in earnings. The ineffective portion of a hedge derivative's change in fair value is immediately recognized in earnings. We formally document all relationships between hedging instruments and hedged items, as well as our risk management objectives and strategies for undertaking our hedge transactions. Upon adoption, we recorded an adjustment of \$4.2 million in AOCI to record the unrealized net losses from our cash flow hedges that existed on December 1, 2000.

The total \$187 million and \$578 million of current and long-term fair value of hedged firm commitment assets on our November 30, 2002 and 2001 balance sheets, respectively, includes \$178 million and \$567 million, respectively, of unrealized gains on our shipbuilding commitments denominated in foreign currencies because of the strengthening of the dollar compared to the euro. In addition, the total \$194 million and \$581 million of fair value of derivative contract liabilities on our November 30, 2002 and 2001 balance sheets, respectively, includes \$178 million and \$567 million of unrealized losses on our forward foreign currency contracts relating to those same shipbuilding commitments, which are used to fix the cost of our shipbuilding commitments in U.S. dollars, and effectively offsets the related hedged firm commitment assets.

We classify the fair value of our derivative contracts and the fair value of our offsetting hedged firm commitments as either current or long-term liabilities and assets depending on whether the maturity date of the derivative contract is within or beyond one year from our balance sheet dates, respectively. The cash flows from derivatives treated as hedges are classified in our statements of cash flows in the same category as the item being hedged.

Derivative gains and losses included in AOCI are reclassified into earnings at the same time the underlying hedged transaction is recorded in earnings. During fiscal 2002 and 2001, all net changes in the fair value of both our fair value hedges and the offsetting hedged firm commitments and our cash flow hedges were immaterial, as were any ineffective portions of these hedges. No fair value hedges or cash flow hedges were derecognized or discontinued in fiscal 2002 and 2001, and the amount of estimated unrealized net losses which are expected to be reclassified to earnings in the next twelve months is not material. At November 30, 2002 and 2001, AOCI included \$8 million and \$8.5 million of unrealized net losses, respectively, from cash flow hedge derivatives, which were substantially all variable to fixed

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interest rate swap agreements.

Finally, if any of the three shipyards with which we have contracted to build our ships is unable to perform, we would still be required to perform under our foreign currency forward contracts related to that shipyard's shipbuilding contracts. Accordingly, based upon the circumstances, we may have to discontinue the accounting for those forward contracts as hedges, if the shipyard cannot perform.

Prior to fiscal 2001, changes in the fair values of and any discounts or premiums on, our shipbuilding forward foreign currency contract hedges were recorded at maturity, which coincided with the dates when the related foreign currency payments were to be made, with any resulting gains or losses recorded as a decrease or increase, respectively, to the cost paid for our ships.

Revenue and Expense Recognition

Guest cruise deposits represent unearned revenues and are initially recorded as customer deposit liabilities on our balance sheet when received. Customer deposits are subsequently recognized as cruise revenues, together with revenues from onboard activities and all associated direct costs of a voyage, generally upon completion of voyages with durations of ten days or less and on a pro rata basis for voyages in excess of ten days. Future travel discount vouchers issued to guests are recorded as a reduction of revenues when such vouchers are utilized. Revenues and expenses from our tour and related services are recognized at the time the services are performed or expenses are incurred.

Advertising Costs

Substantially all of our advertising costs are charged to expense as incurred, except costs which result in tangible assets, such as brochures, which are recorded as prepaid expenses and charged to expense as consumed. Media production costs are also recorded as prepaid expenses and charged to expense upon the first airing of the advertisement. Advertising expenses totaled \$208 million, \$214 million and \$181 million in fiscal 2002, 2001 and 2000, respectively. At November 30, 2002 and 2001, the amount of advertising costs included in prepaid expenses was not material.

Foreign Currency Translations and Transactions

For our foreign subsidiaries and affiliates using the local currency as their functional currency, assets and liabilities are translated at exchange rates in effect at the balance sheet dates. Translation adjustments resulting from this process are reported in AOCI. Revenues and expenses of these foreign subsidiaries and affiliates are translated at weighted-average exchange rates for the period. Exchange gains and losses arising from transactions denominated in a currency other than the functional currency of the entity involved are immediately included in our earnings.

Earnings Per Share

Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during each period. Diluted earnings per share is computed by dividing net income by the weighted-average number of shares of common stock, common stock equivalents and other potentially dilutive securities outstanding during each period. See Note 14.

Stock-Based Compensation

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Pursuant to SFAS No. 123, "Accounting for Stock-Based Compensation," we elected to use the intrinsic value method of accounting for our employee and director stock-based compensation awards. Accordingly, we have not recognized compensation expense for our noncompensatory employee and director stock option awards. Our pro forma net income and earnings per share for fiscal 2002 and 2001, had we elected to adopt the fair value approach of SFAS No. 123, which charges earnings for the estimated fair value of stock options, would have been \$991 million and \$904 million and \$1.69 and \$1.54, respectively, and would not have been materially different from reported net income and earnings per share for fiscal 2000.

As determined below, the weighted-average fair values of options we granted during fiscal 2002, 2001 and 2000 were \$12.16, \$12.67 and \$13.31 per share, respectively, at the dates of grant. As recommended by SFAS No. 123, the fair values of options were estimated using the Black-Scholes option pricing model with the following weighted-average assumptions for fiscal 2002, 2001 and 2000, respectively; expected dividend yields of 1.23%, 1.16% and 1.17%; expected volatility of 48.0%, 50.0% and 28.9%; risk free interest rates of 4.3%, 4.5% and 6.4%; and expected option life of six years for all periods.

The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options that have no vesting or trading restrictions and are fully transferable. In addition, option-pricing models require the input of subjective assumptions, including expected stock price volatility. Because our options have characteristics different from those of traded options, the existing models do not necessarily provide a reliable single measure of the fair value of our options.

Concentrations of Credit Risk

As part of our ongoing control procedures, we monitor concentrations of credit risk associated with financial and other institutions with which we conduct significant business. Credit risk, including counterparty nonperformance under derivative instruments, contingent obligations and new ship progress payment guarantees, is considered minimal, as we primarily conduct business with large, well-established financial institutions who have long-term credit ratings of A or above and we seek to diversify our counterparties. In addition, we have established guidelines regarding credit ratings and investment maturities that we follow to maintain safety and liquidity. We do not anticipate nonperformance by any of our significant counterparties.

We also monitor the creditworthiness of our customers to which we grant credit terms in the normal course of our business. Concentrations of credit risk associated with these receivables are considered minimal primarily due to their short maturities. We have experienced only minimal credit losses on our trade receivables. We do not normally require collateral or other security to support normal credit sales. However, we do normally require collateral and/or guarantees to support notes receivable on significant asset sales and new ship progress payments to shipyards.

Reclassifications

Reclassifications have been made to prior year amounts to conform to the current year presentation.

NOTE 3 - Property and Equipment

Property and equipment consisted of the following (in thousands):

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| | November 30, | |
|--|--------------|--------------|
| | 2002 | 2001 |
| Ships | \$10,665,958 | \$ 8,892,412 |
| Ships under construction | 712,447 | 592,781 |
| | 11,378,405 | 9,485,193 |
| Land, buildings and improvements, and port facilities | 314,448 | 264,294 |
| Transportation equipment and other | 409,310 | 349,188 |
| Total property and equipment | 12,102,163 | 10,098,675 |
| Less accumulated depreciation and amortization | (1,986,759) | (1,708,445) |
| | \$10,115,404 | \$ 8,390,230 |

Capitalized interest, primarily on our ships under construction, amounted to \$39 million, \$29 million and \$41 million in fiscal 2002, 2001 and 2000, respectively. Ships under construction include progress payments for the construction of the ship, as well as design and engineering fees, capitalized interest, construction oversight costs and various owner supplied items. At November 30, 2002, two ships with an aggregate net book value of \$623 million were pledged as collateral pursuant to a \$119 million note and a \$463 million contingent obligation (see Notes 6 and 8).

Maintenance and repair expenses and dry-dock amortization were \$175 million, \$160 million and \$132 million in fiscal 2002, 2001 and 2000, respectively.

NOTE 4 - Impairment Charge

During fiscal 2002 and 2001 we reviewed our long-lived assets and goodwill for which there were indications of possible impairment or as required annually pursuant to SFAS No. 142. As a result of these reviews, in fiscal 2002 we reduced the carrying value of one of our ships by recording an impairment charge of \$20 million. In fiscal 2001, we recorded an impairment charge of \$140 million, which consisted principally of a \$71 million reduction in the carrying value of ships, a \$36 million write-off of Seabourn goodwill, a \$15 million write-down of a Holland America note receivable and a \$11 million loss on the sale of the Seabourn Goddess I and II. The impaired ships' and note receivable fair values were based on third party appraisals, negotiations with unrelated third parties or other available evidence, and the fair value of the impaired goodwill was based on our estimates of discounted future cash flows.

NOTE 5 - Investments In and Advances To Affiliates

On June 1, 2001, we sold our investment in Airtours plc, which resulted in a nonoperating net gain of \$101 million and net cash proceeds of \$492 million. Cumulative foreign currency translation losses of \$59 million were reclassified from AOCI and included in determining this 2001 net gain. We also recorded a direct charge of \$8 million to our retained earnings in fiscal 2001, which represented our share of Airtours' losses for April and May 2001, since Airtours results were reported on a two-month lag.

In fiscal 2001, we sold our interest in CRC Holdings, Inc. ("CRC") to an unrelated third party, which resulted in a nonoperating net gain of \$16 million and net cash proceeds of \$39 million. One of the members of our Board of Directors was a principal shareholder in CRC.

Dividends received from affiliates were \$13 million and \$16 million in fiscal 2001 and 2000, respectively, which reduced the carrying value of our investments in affiliates in accordance with the equity method of

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accounting.

Income statement and segment information for fiscal 2000 for our affiliated companies accounted for using the equity method, including Airtours and Costa, was as follows: revenues - \$6.7 billion, gross margin - \$1.3 billion, operating income - \$5 million, depreciation and amortization - \$152 million, net income - \$20 million and capital expenditures - \$650 million. Since we sold our interest in Airtours and CRC during fiscal 2001, no data has been presented for fiscal 2002 and 2001.

NOTE 6 - Long-Term Debt

Long-term debt consisted of the following (in thousands):

| | November 30, | |
|--|--------------|-------------|
| | 2002 (a) | 2001 (a) |
| Euro floating rate note, collateralized by one Costa ship, bearing interest at euribor plus 0.5% (4.0% and 4.8% at November 30, 2002 and 2001, respectively), due through 2008 | \$ 118,727 | \$ 125,770 |
| Unsecured fixed rate notes, bearing interest at rates ranging from 6.15% to 7.7%, due through 2028(b) | 848,900 | 848,779 |
| Unsecured floating rate euro notes, bearing interest at rates ranging from euribor plus 0.35% to euribor plus 0.53% (3.6% to 4.0% and 3.9% to 4.9% at November 30, 2002 and 2001, respectively), due 2005 and 2006 | 680,377 | 604,068 |
| Unsecured fixed rate euro notes, bearing interest at 5.57%, due in 2006 | 297,195 | 266,223 |
| Unsecured \$1.4 billion revolving credit facility, bearing interest at libor plus 0.17% (1.6% at November 30, 2002), due in 2006 | 50,000 | |
| Other | 44,468 | 29,833 |
| Unsecured 2% convertible notes, due in 2021 | 600,000 | 600,000 |
| Unsecured zero-coupon convertible notes, net of discount, with a face value of \$1.05 billion, due in 2021 | 520,944 | 501,945 |
| | 3,160,611 | 2,976,618 |
| Less portion due within one year | (148,642) | (21,764) |
| | \$3,011,969 | \$2,954,854 |

(a) All borrowings are in U.S. dollars unless otherwise noted. Euro denominated notes have been translated to U.S. dollars at the period end exchange rates. At November 30, 2002 and 2001, 65% and 66% of our debt was U.S. dollar denominated and 35% and 34% was euro denominated, respectively.

(b) These notes are not redeemable prior to maturity.

Our unsecured 2% convertible notes ("2% Notes") and our zero-coupon convertible notes ("Zero-Coupon Notes") are convertible into 15.3 million shares and 17.4 million shares, respectively, of our common stock. Our 2% Notes are convertible at a conversion price of \$39.14 per share, subject to adjustment, during any fiscal quarter for which the closing price of our common stock is greater than \$43.05 per share for a defined duration of time. Our Zero-Coupon Notes have a 3.75% yield to maturity and are convertible during any fiscal quarter for which the closing price of our common stock reaches certain targeted levels for a defined duration of time.

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These levels commenced at a low of \$31.94 per share for the first quarter of fiscal 2002 and increase at an annual rate of 3.75% thereafter, until maturity. The conditions for conversion of our 2% Notes or Zero-Coupon Notes were not met during fiscal 2002 and 2001.

Subsequent to April 14, 2008, we may redeem all or a portion of our 2% Notes at their face value plus any unpaid accrued interest, and subsequent to October 23, 2008, we may redeem all or a portion of our Zero-Coupon Notes at their accreted value.

In addition, on April 15 of 2005, 2008 and 2011 our 2% Noteholders and on October 24 of 2006, 2008, 2011 and 2016 our Zero-Coupon Noteholders may require us to repurchase all or a portion of the outstanding 2% Notes at their face value plus any unpaid accrued interest and the Zero-Coupon Notes at their accreted value.

Upon conversion, redemption or repurchase of our 2% Notes and Zero-Coupon Notes we may choose to deliver common stock, cash or a combination of cash and common stock with a total value equal to the value of the consideration otherwise deliverable. If our 2% Notes and Zero-Coupon Notes were to be put back to us, we expect to settle them for cash and, accordingly, they are not included in our diluted earnings per share common stock calculations. However, no assurance can be given that we will have sufficient liquidity to make such cash payments. See Note 14.

In May 2001, Costa entered into a five-year 257.5 million euro (255.6 million U.S. dollars at the November 30, 2002 exchange rate) unsecured floating rate euro denominated revolving credit facility, of which \$145 million was available at November 30, 2002.

Our \$1.4 billion unsecured multi-currency revolving credit facility matures in June 2006. This facility currently bears interest at *libor/euribor* plus 17 basis points ("BPS"), which interest rate spread over *libor/euribor* will vary based on changes to our senior unsecured debt ratings, and provides for an undrawn facility fee of eight BPS. Our commercial paper program is supported by this revolving credit facility and, accordingly, any amounts outstanding under our commercial paper program, none at November 30, 2002 and 2001, reduce the aggregate amount available under this facility. At November 30, 2002, \$1.35 billion of this facility was available. This facility and other of our loan agreements contain covenants that require us, among other things, to maintain a minimum debt service coverage and limits our debt to tangible capital ratio and the amount of our secured indebtedness. In addition, our ability to draw upon the then available portion of our \$1.4 billion credit facility could be terminated and we could also be required to repay the amounts outstanding under our one collateralized and three unsecured euro notes, which amounted to \$722 million at November 30, 2002, if our business suffers a material adverse change. At November 30, 2002, we were in compliance with all of our debt covenants.

At November 30, 2002, the scheduled annual maturities of our long-term debt was as follows (in thousands):

| Fiscal | |
|------------|---------------|
| 2003 | \$ 148,642 |
| 2004 | 127,985 |
| 2005 | 907,648 (a) |
| 2006 | 1,387,209 (a) |
| 2007 | 22,833 |
| Thereafter | 566,294 |

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\$3,160,611

- (a) Includes \$600 million of our 2% Notes in 2005 and \$521 million of our Zero-Coupon Notes in 2006 based on the date of the noteholders first put option.

Debt issuance costs are generally amortized to interest expense using the straight-line method over the term of the notes or to the noteholders first put option date, whichever is earlier. In addition, all loan issue discounts are amortized to interest expense using the effective interest method over the term of the notes.

NOTE 7 - Commitments

Ship Commitments

A description of our ships under contract for construction at November 30, 2002 was as follows (in millions, except passenger capacity data):

| Ship | Expected Service Date(1) | Shipyard | Passenger Capacity(2) | Estimated Total Cost(3) |
|-----------------------|--------------------------------|---------------------------------|--------------------------|-------------------------------|
| CCL | | | | |
| Carnival Glory | 7/03 | Fincantieri | 2,974 | \$ 510 |
| Carnival Miracle | 3/04 | Masa-Yards (4) | 2,124 | 375 |
| Carnival Valor | 11/04 | Fincantieri(4) | 2,974 | 510 |
| Newbuild | 1/06 | Fincantieri | 2,974 | 460 |
| Total CCL | | | 11,046 | 1,855 |
| Holland America | | | | |
| Oosterdam | 7/03 | Fincantieri(4) | 1,848 | 410 |
| Westerdam | 5/04 | Fincantieri(4) | 1,848 | 410 |
| Newbuild | 11/05 | Fincantieri(4) | 1,848 | 410 |
| Newbuild | 6/06 | Fincantieri | 1,848 | 390 |
| Total Holland America | | | 7,392 | 1,620 |
| Costa | | | | |
| Costa Mediterranea | 6/03 | Masa-Yards (5) | 2,114 | 360 |
| Costa Fortuna | 12/03 | Fincantieri(5) | 2,720 | 440 |
| Costa Magica | 11/04 | Fincantieri(5) | 2,720 | 460 |
| Total Costa | | | 7,554 | 1,260 |
| Cunard | | | | |
| Queen Mary 2 | 1/04 | Chantiers de l'Atlantique(4) | 2,620 | 780 |
| Newbuild | 2/05 | Fincantieri(4) | 1,968 | 410 |
| Total Cunard | | | 4,588 | 1,190 |
| Total | | | 30,580 | \$5,925 |

- (1) The expected service date is the date the ship is currently expected to begin its first revenue generating cruise.
- (2) In accordance with cruise industry practice, passenger capacity is calculated based on two passengers per cabin even though some cabins can accommodate three or more passengers.
- (3) Estimated total cost of the completed ship includes the contract price with the shipyard, design and engineering fees, capitalized interest, construction oversight costs and various owner supplied items.
- (4) These construction contracts are denominated in euros and have been fixed into U.S. dollars through the utilization of forward foreign currency contracts. The \$178 million of unrealized losses from these forward contracts has been recorded as fair value of derivative contract

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liabilities on our November 30, 2002 balance sheet and are also included in the above estimated total cost of these construction contracts.

- (5) These construction contracts are denominated in euros, which is Costa's functional currency. The estimated total costs have been translated into U.S. dollars using the November 30, 2002 exchange rate.

In connection with our ships under contract for construction, we have paid approximately \$712 million through November 30, 2002 and anticipate paying the remaining estimated total cost as follows (in millions):

| Fiscal | |
|--------|---------|
| 2003 | \$1,630 |
| 2004 | 2,110 |
| 2005 | 1,140 |
| 2006 | 330 |
| | \$5,210 |

Proposed Dual-Listed Company Transaction with P&O Princess Cruises plc ("P&O Princess")

After a series of preconditional offers made to the shareholders of P&O Princess by us, commencing in December 2001, on January 8, 2003 we entered into an agreement with P&O Princess, the world's third largest cruise company, providing for a combination of both companies (the "Combined Group") under a dual-listed company ("DLC") structure.

If the DLC transaction is completed, it would create a combination of the two companies through a number of contracts and certain amendments to our Articles of Incorporation and By-Laws and to P&O Princess' Memorandum and Articles of Association. The two companies would retain their separate legal identities and each company's shares would continue to be publicly traded on the New York Stock Exchange for us and the London Stock Exchange for P&O Princess. However, both companies would operate as if they were a single economic enterprise. The contracts governing the DLC structure would provide that the boards of directors of the two companies would be identical, the companies would be managed by a unified senior management team and that, as far as possible, P&O Princess' and our shareholders would be placed in substantially the same economic position as if they held shares in a single enterprise which owned all of the assets of both companies. The net effect of the DLC transaction would be that our existing shareholders would own an economic interest equal to approximately 74% of the Combined Group and the existing shareholders of P&O Princess would own an economic interest equal to approximately 26% of the Combined Group. Also in connection with the DLC transaction, we will be making a Partial Share Offer ("PSO") for 20% of P&O Princess' shares, which will enable P&O Princess shareholders to exchange P&O Princess shares for our shares on the basis of 0.3004 of our shares for each P&O Princess share up to, in aggregate, a maximum of 20% of P&O Princess issued share capital. If the maximum number of P&O Princess' shares are exchanged under the PSO, holders of our shares, including our new shareholders who exchanged their P&O Princess shares for our shares under the PSO, would own an economic interest equal to approximately 79% of the Combined Group and holders of P&O Princess shares would own an economic interest equal to approximately 21% of the Combined Group. The PSO is conditional on, among other things, the closing of the DLC transaction. Upon completion of the DLC transaction, P&O Princess will reorganize and consolidate its share capital so that one share of P&O Princess will have the same economic and voting interest as one of our shares.

The completion of the DLC transaction between P&O Princess and us is subject to approval by P&O Princess' shareholders and our shareholders. No

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assurance can be given that the DLC transaction will be completed and, if it is completed, when completion will take place. If the DLC transaction is not completed by September 30, 2003, either party can terminate the agreement if it is not in material breach of its obligations. We have incurred \$30 million of transaction costs as of November 30, 2002, and continue to incur costs, which have been or will be deferred in connection with the DLC transaction. In the event a transaction with P&O Princess is not consummated, we would be required to write off the above \$30 million plus all costs incurred and deferred subsequent to November 30, 2002, resulting in an estimated total write-off of approximately \$45 million to \$50 million. If the DLC transaction or another transaction with P&O Princess is completed by us, these deferred costs, together with any additional direct costs, which may be incurred, would be capitalized as part of the transaction.

If our agreement with P&O Princess is terminated under certain circumstances, we would be required to pay P&O Princess a break fee of \$49 million. These circumstances include, among other things, our board of directors withdrawing or adversely modifying its recommendation to shareholders to approve the DLC transaction, our board of directors recommending an alternative acquisition proposal to shareholders, or our shareholders failing to approve the DLC transaction if a third-party acquisition proposal exists at the time of our meeting or if we breach our exclusivity covenant and a third party acquisition proposal with respect to us is completed prior to July 2004. Similarly, P&O Princess would be obligated to pay us a break fee of \$49 million upon the occurrence of reciprocal circumstances.

If the DLC transaction is completed, we expect to account for it as an acquisition of P&O Princess by us, which will be accounted for using the purchase method.

Operating Leases

Rent expense under our operating leases, primarily for office and warehouse space, was \$15 million, \$13 million and \$10 million in fiscal 2002, 2001 and 2000, respectively. At November 30, 2002, minimum annual rentals for our operating leases, with initial or remaining terms in excess of one year, were as follows (in thousands):

| Fiscal | |
|------------|----------|
| 2003 | \$10,700 |
| 2004 | 9,300 |
| 2005 | 9,100 |
| 2006 | 9,100 |
| 2007 | 6,000 |
| Thereafter | 25,300 |
| | \$69,500 |

Port Facilities and Other

At November 30, 2002, we had commitments through 2027, with initial or remaining terms in excess of one year, to pay minimum amounts for our annual usage of port facilities and other contractual commitments as follows (in thousands):

| Fiscal | |
|--------|-----------|
| 2003 | \$ 52,100 |
| 2004 | 38,800 |
| 2005 | 25,300 |

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| | |
|------------|-----------|
| 2006 | 25,800 |
| 2007 | 27,100 |
| Thereafter | 179,600 |
| | \$348,700 |

Travel Vouchers

Pursuant to CCL's and Holland America's settlement of litigation, travel vouchers with face values of \$10 to \$55 were required to be issued to qualified past passengers. As of November 30, 2002, approximately \$123 million of these travel vouchers are available to be used for future travel prior to their expiration, principally in fiscal 2005.

NOTE 8 - Contingencies

Litigation

Several actions (collectively, the "ADA Complaints") have been filed against Costa, Cunard and Tours alleging that they violated the Americans with Disabilities Act by failing to make certain cruise ships accessible to individuals with disabilities. The plaintiffs seek injunctive relief to require modifications to certain vessels to increase accessibility to disabled passengers and fees and costs. Costa and the plaintiffs have agreed to settle this action, subject to court approval. Cunard and Tours are in ongoing settlement negotiations with the plaintiffs.

Three actions (collectively, the "Facsimile Complaints") were filed against us on behalf of purported classes of persons who received unsolicited advertisements via facsimile, alleging that we and other defendants distributed unsolicited advertisements via facsimile in contravention of the U.S. Telephone Consumer Protection Act. The plaintiffs seek to enjoin the sending of unsolicited facsimile advertisements and statutory damages. The advertisements referred to in the Facsimile Complaints were not sent by us, but rather were distributed by a professional faxing company at the behest of travel agencies that referenced a CCL product. We do not advertise directly to the traveling public through the use of facsimile transmission.

The ultimate outcome of the pending ADA and Facsimile Complaints cannot be determined at this time. We believe that we have meritorious defenses to these claims and, accordingly, we intend to vigorously defend against these actions.

Several actions filed in the U.S. District Court for the Southern District of Florida against us and four of our executive officers on behalf of a purported class of persons who purchased our common stock were consolidated into one action in Florida (the "Stock Purchaser Complaint"). The plaintiffs have claimed that statements we made in public filings violated federal securities laws and seek unspecified compensatory damages and attorney and expert fees and costs. Recently, a magistrate judge recommended that our motion to dismiss the Stock Purchaser Complaint be granted and that the plaintiffs' amended complaint be dismissed without prejudice. However, because it was dismissed without prejudice, the plaintiffs may file a new amended complaint. Nevertheless, the parties have entered into a memorandum of understanding settling the case pending confirmatory discovery and judicial approval. A substantial portion of the \$3.4 million settlement amount, which includes plaintiff's attorneys fees, will be covered by insurance.

In February 2001, Holland America Line-USA, Inc. ("HAL-USA"), our wholly-owned subsidiary, received a grand jury subpoena requesting that it

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produce documents and records relating to the air emissions from Holland America ships in Alaska. HAL-USA responded to the subpoena. The ultimate outcome of this matter cannot be determined at this time.

On August 17, 2002, an incident occurred in Juneau, Alaska onboard Holland America's Ryndam involving a wastewater discharge from the ship. As a result of this incident, various Ryndam ship officers have received grand jury subpoenas from the Office of the U.S. Attorney in Anchorage, Alaska requesting that they appear before a grand jury. One of the subpoenas also requests the production of Holland America documents, which Holland America is producing. If the investigation results in charges being filed, a judgment could include, among other forms of relief, fines and debarment from federal contracting, which would prohibit operations in Glacier Bay National Park and Preserve during the period of debarment. The State of Alaska is separately investigating this incident. The ultimate outcome of these matters cannot be determined at this time.

Costa has instituted arbitration proceedings in Italy to confirm the validity of its decision not to deliver its ship, the Costa Classica, to the shipyard of Cammell Laird Holdings PLC ("Cammell Laird") under a 79 million euro denominated contract for the conversion and lengthening of the ship. Costa has also given notice of termination of the contract. It is now expected that the arbitration tribunal's decision will be made in mid-2004 at the earliest. In the event that an award is given in favor of Cammell Laird, the amount of damages, which Costa will have to pay, if any, is not currently determinable. The ultimate outcome of this matter cannot be determined at this time.

In the normal course of our business, various other claims and lawsuits have been filed or are pending against us. Most of these claims and lawsuits are covered by insurance. We are not able to estimate the impact or the ultimate outcome of any such actions, which are not covered by insurance.

Contingent Obligations

At November 30, 2002, we had contingent obligations totaling \$1.05 billion to participants in lease out and lease back type transactions for three of our ships. At the inception of the leases, the entire amount of the contingent obligations was paid by us to major financial institutions to enable them to directly pay these obligations. Accordingly, these obligations were considered extinguished, and neither funds nor the contingent obligations have been included on our balance sheets. We would only be required to make any payments under these lease contingent obligations in the remote event of nonperformance by these financial institutions, all of which have long-term credit ratings of AAA or AA. In addition, we obtained a direct guarantee from another AAA rated financial institution for \$285 million of the above noted contingent obligations, thereby reducing even the remote exposure to this portion of the contingent obligations. If the major financial institutions' credit ratings fall below AA-, we would be required to move a majority of the funds from these financial institutions to other highly-rated financial institutions. If our credit rating falls below BBB, we would be required to provide a standby letter of credit for \$91 million, or alternatively provide mortgages in the aggregate amount of \$91 million on two of our ships.

In the unlikely event that we were to terminate the three lease agreements early or default on our obligations, we would, as of November 30, 2002 have to pay a total of \$180 million in stipulated damages. As of November 30, 2002, \$148 million of standby letters of credit have been issued by a major financial institution in order to provide further security for the payment of these contingent stipulated damages. An additional \$40

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million of standby letters of credit would be required to be issued if our three credit ratings fall below A-/A3. Between 2017 and 2022, we have the right to exercise options that would terminate these transactions at no cost to us. We entered into these three transactions in order to receive \$67 million, which was recorded as deferred income on our balance sheets and is being amortized to nonoperating income through 2022. In the event we were to default under our \$1.4 billion revolving credit facility, we would be required to post cash collateral to support the stipulated damages standby letters of credit.

NOTE 9 - Income and Other Taxes

We believe that substantially all of our income, with the exception of our U.S. source income from the transportation, hotel and tour businesses of Tours, is exempt from U.S. federal income taxes. If we were found not to qualify for exemption pursuant to applicable income tax treaties or under the Internal Revenue Code or if the income tax treaties or Internal Revenue Code were to be changed in a manner adverse to us, a portion of our income would become subject to taxation by the U.S. at higher than normal corporate tax rates.

Some of our subsidiaries, including Costa and Tours, are subject to foreign and/or U.S. income taxes. In fiscal 2002, we recognized a net \$57 million income tax benefit primarily due to a new Italian investment incentive law, which allowed Costa to receive a \$51 million income tax benefit based on contractual expenditures during 2002 on the construction of new ships. At November 30, 2002, Costa had a remaining net deferred tax asset of approximately \$45 million relating to the tax benefit of the net operating loss carryforwards arising from this incentive law, which expire in 2007. In fiscal 2001, we recognized a \$9 million income tax benefit from Costa primarily due to changes in Italian tax law.

We do not expect to incur income taxes on future distributions of undistributed earnings of foreign subsidiaries and, accordingly, no deferred income taxes have been provided for the distribution of these earnings.

In addition to or in place of income taxes, virtually all jurisdictions where our ships call, impose taxes based on passenger counts, ship tonnage or some other measure. These taxes, other than those directly charged to and collected from passengers by us, are recorded as operating expenses in the accompanying statements of operations.

NOTE 10 - Shareholders' Equity

Our Articles of Incorporation authorize our Board of Directors, at their discretion, to issue up to 40 million shares of our preferred stock. At November 30, 2002 and 2001, no preferred stock had been issued.

In February 2000, our Board of Directors authorized the repurchase of up to \$1 billion of our common stock. As of November 30, 2001, we had repurchased 33.1 million shares of our common stock at a cost of \$705 million pursuant to this authorization. In addition in 2001, we received 761,000 shares of our common stock from our chief executive officer valued at its quoted market price of \$23 million, which we recorded as treasury stock, in payment of the exercise price for two million shares of our common stock issued to him pursuant to a stock option plan (see Note 13). In fiscal 2002, we retired all of our treasury stock.

At November 30, 2002, there were 77.5 million shares of our common stock reserved for issuance pursuant to our convertible notes and our stock option, employee stock purchase, restricted stock and dividend reinvestment plans. During fiscal 2002, 2001 and 2000 we declared cash dividends

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aggregating \$0.42 per share for each year.

At November 30, 2002 and 2001, AOCI included cumulative foreign currency translation adjustments which increased shareholders' equity by \$29 million and decreased shareholders' equity by \$22 million, respectively.

NOTE 11 - Financial Instruments

We estimated the fair value of our financial instruments through the use of public market prices, quotes from financial institutions and other available information. Considerable judgment is required in interpreting data to develop estimates of fair value and, accordingly, amounts are not necessarily indicative of the amounts that we could realize in a current market exchange. Our financial instruments are not held for trading or other speculative purposes.

Cash and Cash Equivalents

The carrying amounts of our cash and cash equivalents approximate their fair values due to their short maturities.

Other Assets

At November 30, 2002 and 2001, long-term other assets included marketable securities held in rabbi trusts for certain of our nonqualified benefit plans and notes and other receivables, principally collateralized by a ship, the former Nieuw Amsterdam. These assets had carrying and fair values of \$173 million at November 30, 2002 and \$143 million at November 30, 2001. Fair values were based on public market prices, estimated discounted future cash flows or estimated fair value of collateral.

Long-Term Debt

At November 30, 2002 and 2001, the fair value of our long-term debt, including the current portion, was \$3.33 billion and \$2.95 billion, respectively, which was \$166 million greater than and \$26 million less than its carrying value on those respective dates. The net difference between the fair value of our long-term debt and its carrying value was due primarily to our issuance of debt obligations at fixed interest rates that are below or above market interest rates in existence at the measurement dates. The fair values of our unsecured fixed rate notes, convertible notes and unsecured 5.57% euro notes were based on their public market prices. The fair values of our other long-term debt were estimated based on appropriate market interest rates being applied to this debt.

Foreign Currency Contracts

We have forward foreign currency contracts, designated as foreign currency fair value hedges, for seven of our euro denominated shipbuilding contracts (see Note 7). At November 30, 2002 and 2001, the fair value of these forward contracts was an unrealized loss of \$178 million and \$567 million, respectively. These forward contracts mature through 2005. The fair values of our forward contracts were estimated based on prices quoted by financial institutions for these instruments.

Interest Rate Swaps

We have interest rate swap agreements designated as fair value hedges whereby we receive fixed interest rate payments in exchange for making variable interest rate payments. At November 30, 2002 and 2001, these interest rate swap agreements effectively changed \$225 million of fixed rate debt with a weighted-average fixed interest rate of 6.8% to Libor-based

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floating rate debt.

In addition, we also have interest rate swap agreements designated as cash flow hedges whereby we receive variable interest rate payments in exchange for making fixed interest rate payments. At November 30, 2002 and 2001, these interest rate swap agreements effectively changed \$468 million and \$637 million, respectively, of euribor floating rate debt to fixed rate debt with a weighted-average fixed interest rate of 5.5% and 5.3%, respectively.

These interest rate swap agreements mature through 2006. At November 30, 2002 and 2001, the fair value of our interest rate swaps was a net unrealized loss of \$0.1 million and \$3.3 million, respectively. The fair values of our interest rate swap agreements were estimated based on appropriate market interest rates being applied to these instruments.

NOTE 12 - Segment Information

Our cruise segment included six cruise brands (five, excluding Costa, prior to fiscal 2001), which have been aggregated as a single reportable segment based on the similarity of their economic and other characteristics. Cruise revenues are comprised of sales of passenger cruise tickets, which includes accommodations, meals and most onboard activities, in some cases the sale of air transportation to and from our cruise ships, and the sale of certain onboard activities and other services. The tour segment represents the transportation, hotel and tour operations of Tours.

The significant accounting policies of the segments are the same as those described in Note 2 - "Summary of Significant Accounting Policies." Cruise revenues included intersegment revenues, which primarily represent billings to the tour segment for the cruise portion of a tour when a cruise is sold as a part of a tour package. In addition, cruise and tour operating expenses included a cost allocation of certain corporate and other expenses. Information for the cruise and tour segments for fiscal 2002, 2001 and 2000 was as follows (in thousands)

| | Revenues | Operating income (loss) | Depreciation and amortization | Capital expenditures | Total assets |
|------------------------------|-------------|-------------------------------|-------------------------------------|-------------------------|-----------------|
| 2002 | | | | | |
| Cruise (b) | \$4,229,124 | \$1,055,460 (a) | \$ 370,998 | \$ 1,949,680 | \$12,120,443 |
| Tour | 175,831 | (13,401) | 11,345 | 36,802 | 214,405 (c) |
| Intersegment elimination | (36,686) | | | | |
| | \$4,368,269 | \$1,042,059 | \$ 382,343 | \$ 1,986,482 | \$12,334,848 |
| 2001 | | | | | |
| Cruise (b) | \$4,357,942 | \$ 946,112 (a) | \$ 360,750 | \$ 801,460 | \$11,375,256 |
| Tour | 229,483 | (10,357) (a) | 11,474 | 25,108 | 188,296 (c) |
| Affiliated operations (d) | | (44,024) | | | |
| Intersegment elimination | (51,674) | | | | |
| | \$4,535,751 | \$ 891,731 | \$ 372,224 | \$ 826,568 | \$11,563,552 |
| 2000 | | | | | |
| Cruise (b) | \$3,578,372 | \$ 937,466 | \$ 276,842 | \$ 973,219 | \$ 9,194,207 |
| Tour | 259,662 | 7,664 | 10,825 | 30,129 | 199,722 (c) |
| Affiliated | | | | | |

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| | | |
|--------------|-------------|---|
| operations | 37,828 (b) | 437,391 |
| Intersegment | | |
| elimination | (59,492) | |
| | \$3,778,542 | \$ 982,958 \$ 287,667 \$1,003,348 \$ 9,831,320 |

- (a) Cruise operating income included impairment charges of \$20 million in 2002 and \$134 million in 2001 and Tour operating loss included \$6 million in 2001 (see Note 4).
- (b) In 2002 and 2001, the cruise segment information included Costa. At November 30, 2000, Costa's total assets were included in the cruise segment, but its 2000 results of operations were included in the affiliated operations segment (See Notes 2 and 17). In addition, in 2003 we commenced allocating all corporate expenses to our cruise segment. Accordingly, the presentations for fiscal 2002, 2001 and 2000 have been reclassified to allocate, the previously unallocated, 2002, 2001 and 2000 corporate expenses to our cruise segment.
- (c) Tour assets primarily included hotels in Alaska and the Canadian Yukon, luxury dayboats offering tours to the glaciers of Alaska and the Yukon River, motor coaches used for sightseeing and charters in the states of Washington and Alaska, British Columbia, Canada and the Canadian Yukon and private, domed rail cars, which are run on the Alaska Railroad between Anchorage and Fairbanks.
- (d) On June 1, 2001, we sold our investment in Airtours. Accordingly, we did not record any equity in the earnings or losses from the affiliated operations of Airtours after our quarter ended May 31, 2001.

See Note 5 for affiliated operations segment information, which were not included in our consolidated operations.

Foreign revenues for our cruise brands, excluding Costa in 2000, represent sales generated from outside the U.S. primarily by foreign tour operators and foreign travel agencies. The majority of these foreign revenues are from Italy, Canada, United Kingdom, France, Germany and Spain. Substantially all of our long-lived assets are located outside of the U.S. and consist principally of our goodwill, ships and ships under construction.

Revenue information by geographic area for fiscal 2002, 2001 and 2000 was as follows (in thousands):

| | 2002 | 2001 | 2000 |
|---------|--------------|--------------|-------------|
| U.S. | \$ 3,292,533 | \$ 3,489,913 | \$3,180,667 |
| Foreign | 1,075,736 | 1,045,838 | 597,875 |
| | \$ 4,368,269 | \$ 4,535,751 | \$3,778,542 |

NOTE 13 - Benefit Plans

Stock Option Plans

We have stock option plans primarily for supervisory and management level employees and members of our Board of Directors. The plans are administered by a committee of three of our directors (the "Committee") which determines who is eligible to participate, the number of shares for which options are to be granted and the amounts that may be exercised within a specified term. The option exercise price is generally set by the Committee at 100% of the fair market value of the common stock on the date the option is granted. Substantially all options granted during fiscal 2002, 2001 and 2000 were granted at an exercise price per share equal to the fair market value of our common stock on the date of grant. Employee options

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generally have vested evenly over five years and have a ten year term and director options granted prior to fiscal 2001 have vested immediately and have a five or ten year term. Director options granted subsequent to fiscal 2000 will vest evenly over five years and have a ten year term. At November 30, 2002, options for 40.7 million shares were available for future grants under the above plans. A summary of the activity and status of our stock option plans was as follows:

| | Weighted | | | Number of Options | | |
|----------------------|------------------------|---------|---------|--------------------------|-------------|-----------|
| | Average Exercise Price | | | Years Ended November 30, | | |
| | 2002 | 2001 | 2000 | 2002 | 2001 | 2000 |
| Outstanding options- | | | | | | |
| beginning of year | \$28.95 | \$26.80 | \$22.70 | 12,774,293 | 8,840,793 | 6,517,168 |
| Options granted | \$26.54 | \$26.44 | \$35.92 | 33,000 | 6,580,250 | 2,910,575 |
| Options exercised | \$14.35 | \$11.70 | \$13.43 | (404,615) | (2,218,075) | (244,850) |
| Options canceled | \$32.80 | \$35.15 | \$35.91 | (573,720) | (428,675) | (342,100) |
| Outstanding options- | | | | | | |
| end of year | \$29.26 | \$28.95 | \$26.80 | 11,828,958 | 12,774,293 | 8,840,793 |
| Options exercisable- | | | | | | |
| end of year | \$28.71 | \$25.96 | \$15.82 | 4,775,894 | 2,972,498 | 4,042,452 |

Information with respect to outstanding and exercisable stock options at November 30, 2002 was as follows:

| Exercise Price Range | Options Outstanding | | | Options Exercisable | |
|----------------------|---------------------|---|---------------------------------|---------------------|---------------------------------|
| | Shares | Weighted Average Remaining Life (Years) | Weighted Average Exercise Price | Shares | Weighted Average Exercise Price |
| \$ 1.94-\$ 2.25 | 32,980 | (a) | \$ 2.06 | 32,980 | \$ 2.06 |
| \$ 6.94-\$10.31 | 17,300 | 0.7 | \$ 9.76 | 17,300 | \$ 9.76 |
| \$10.59-\$15.00 | 666,050 | 2.3 | \$11.32 | 666,050 | \$11.32 |
| \$16.28-\$22.57 | 3,901,084 | 8.1 | \$21.66 | 1,236,830 | \$20.75 |
| \$24.63-\$27.78 | 1,182,894 | 6.3 | \$26.24 | 667,294 | \$26.35 |
| \$28.21-\$34.88 | 3,070,500 | 8.1 | \$30.05 | 673,100 | \$30.47 |
| \$36.72-\$41.34 | 102,000 | 5.8 | \$38.09 | 77,200 | \$38.05 |
| \$43.56-\$48.56 | 2,856,150 | 6.7 | \$44.36 | 1,405,140 | \$44.57 |
| Total | 11,828,958 | 7.2 | \$29.26 | 4,775,894 | \$28.71 |

| Contractual Cash Obligations (a) | Payments Due by Fiscal | | | | | | |
|----------------------------------|------------------------|-------------|-------------|-------------|------------|--------|------------|
| | Total | 2003 | 2004 | 2005 | 2006 | 2007 | Thereafter |
| Shipbuilding | \$5,210,000 | \$1,630,000 | \$2,110,000 | \$1,140,000 | \$ 330,000 | \$ | \$ |
| Long-term debt | 3,160,611 | 148,642 | 127,985 | 907,648 | 1,387,209 | 22,833 | 566,2 |
| Port and other commitments | 348,700 | 52,100 | 38,800 | 25,300 | 25,800 | 27,100 | 179,6 |
| Operating leases | 69,500 | 10,700 | 9,300 | 9,100 | 9,100 | 6,000 | 25,3 |

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Total contractual

| | | | | | | | |
|------------------|-------------|-------------|-------------|-------------|-------------|-----------|---------|
| cash obligations | \$8,788,811 | \$1,841,442 | \$2,286,085 | \$2,082,048 | \$1,752,109 | \$ 55,933 | \$771,1 |
|------------------|-------------|-------------|-------------|-------------|-------------|-----------|---------|

(a) See Notes 6 and 7 in the accompanying financial statements for additional information regarding our debt and these commitments.

In addition, see Note 7, "Contingent Obligations" and Note 6, "Proposed Dual-Listed Company Transaction with P&O Princess" and "Travel Vouchers" in the accompanying financial statements for a discussion of our contingent obligations related to our three lease-type ship transactions and our DLC transaction and travel voucher commitments, respectively.

At November 30, 2002, we had liquidity of \$2.2 billion, which consisted of \$706 million of cash, cash equivalents and short-term investments and \$1.5 billion available for borrowing under our revolving credit facilities obtained through a group of banks, which have strong credit ratings. Our revolving credit facilities mature in 2006. A key to our access to liquidity is the maintenance of our strong credit ratings. The proposed combination with P&O Princess under a DLC structure, if completed, may result in our debt being downgraded from our current ratings. A downgrade would increase our cost-of-borrowing, although we believe our senior unsecured debt will retain a strong investment grade rating.

We believe that our existing liquidity, together with our forecasted cash flow from future operations, will be sufficient to fund most of our capital projects, debt service requirements, dividend payments and working capital needs. Our forecasted cash flow from future operations, as well as our credit ratings, may be adversely affected by various factors, including, but not limited to, declines in customer demand, increased competition and overcapacity, the deterioration in general economic and business conditions, the international political and economic climate, accidents and other incidents at sea, adverse publicity and increases in fuel prices, as well as other factors noted under "Cautionary Note Concerning Factors That May Affect Future Results." To the extent that we are required, or choose, to fund future cash requirements, including our future shipbuilding commitments, from sources other than as discussed above, we believe that we will be able to secure such financing from banks or through the offering of debt and/or equity securities in the public or private markets. No assurance can be given that our future operating cash flow will be sufficient to fund future obligations or that we will be able to obtain additional financing, if necessary.

Although no assurance can be given, we expect to complete our DLC transaction with P&O Princess in the second quarter of fiscal 2003. As a result of the DLC transaction, the Combined Group's outstanding long-term debt will be approximately \$5.7 billion and its shipbuilding commitments for 18 new cruise ships and two river boats will be approximately \$7.0 billion, which is a substantial increase over our existing obligations and commitments. However, we believe that the Combined Group's liquidity, including cash and committed financings, and cash flows from future operations will be sufficient to fund the expected capital projects, debt service requirements, dividend payments, working capital and other firm commitments through at least the next twelve months.

Off-Balance Sheet Arrangements

We are not a party to any off-balance sheet arrangements, including guarantee contracts, retained or contingent interests, certain derivative

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instruments and variable interest entities, that either have, or are reasonably likely to have, a current or future material effect on our financial statements.

Other Matter

Market Risks

We are principally exposed to market risks from fluctuations in foreign currency exchange rates, bunker fuel prices and interest rates. We seek to minimize foreign currency and interest rate risks through our normal operating and financing activities, including netting certain exposures to take advantage of any natural offsets, through our long-term investment and debt portfolio strategies and, when considered appropriate, through the use of derivative financial instruments. The financial impacts of these hedging instruments are offset by corresponding changes in the underlying exposures being hedged. Our policy is to not use financial instruments for trading or other speculative purposes.

Exposure to Foreign Currency Exchange Rates

Our primary foreign currency exchange risk was related to our outstanding commitments under ship construction contracts denominated in a currency other than the functional currency of the cruise brand that is expected to be operating the ship. These non-functional currency commitments are affected by fluctuations in the value of the functional currency as compared to the currency in which the shipbuilding contract is denominated. Foreign currency forward contracts are generally used to manage this risk (see Notes 2 and 11 in the accompanying financial statements). Accordingly, increases and decreases in the fair value of these foreign currency forward contracts offset changes in the fair value of the hedged non-functional foreign currency denominated ship construction commitments, thus resulting in the elimination of such risk.

We have forward foreign currency contracts for seven of our euro denominated shipbuilding contracts (see Note 7 in the accompanying financial statement). At November 30, 2002, the fair value of these forward contracts was an unrealized loss of \$178 million which is recorded, along with an offsetting \$178 million fair value asset related to our shipbuilding firm commitments, on our accompanying 2002 balance sheet. These foreign currency forward contracts mature through 2005. Based upon a 10% strengthening or weakening of the U.S. dollar compared to the euro as of November 30, 2002, assuming no changes in comparative interest rates, the estimated fair value of these contracts would decrease or increase by \$235 million, which would be offset by a decrease or increase of \$235 million in the U.S. dollar value of the related foreign currency ship construction commitments resulting in no net dollar impact to us.

The cost of shipbuilding orders, which we may place in the future may be affected by foreign currency exchange rate fluctuations. Should the U.S. dollar weaken relative to the euro, future orders for new ship construction in European shipyards may be at higher prices relative to the U.S. dollar.

Additionally, our investments in foreign subsidiaries subjects us to foreign currency exchange rate risk. We consider our investments in foreign subsidiaries to be denominated in relatively stable currencies and/or of a long-term nature and, accordingly, do not typically manage our related foreign currency exchange rate risk through the use of derivative financial instruments. However, when we paid the Costa acquisition price, we utilized debt denominated in euros, the functional currency of Costa, to reduce a portion of this risk.

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Finally, we sell cruises and incur cruise expenses in foreign currencies which subjects us to foreign currency exchange risk. The primary currencies for which we have exchange rate exposure are the U.S. dollar versus both the euro and the UK Sterling. We do not expect that the impact of fluctuations in the foreign currency exchange rate on our foreign currency denominated cruise revenues and expenses to materially affect our results of operations due primarily to the natural hedges, which are expected to exist within our operations, including interest expense on euro denominated borrowings, and the relative stability of the foreign currencies. However, we will continue to monitor such items to determine if any actions, such as the issuance of additional foreign currency denominated debt or use of other financial instruments, would be warranted to reduce such risk.

Exposure to Bunker Fuel Prices

Cruise ship operating expenses are impacted by changes in bunker fuel prices. Bunker fuel consumed over the past three fiscal years ranged from approximately 4.2% in fiscal 2002 to 4.0% in fiscal 2001 and 2000 of our gross cruise revenues. We have typically not used financial instruments to hedge our exposure to the bunker fuel price market risk.

Based upon a 10% hypothetical increase or decrease in the November 30, 2002 bunker fuel price, we estimate that our fiscal 2003 bunker fuel cost would increase or decrease by approximately \$19 million compared to fiscal 2002. See "Outlook For Fiscal 2003."

Exposure to Interest Rates

In order to limit our exposure to interest rate fluctuations, we have entered into a substantial number of fixed rate debt instruments. We continuously evaluate our debt portfolio, including interest rate swap agreements, and make periodic adjustments to the mix of floating rate and fixed rate debt based on our view of interest rate movements. Accordingly in 2001, we entered into fixed to variable interest rate swap agreements, which lowered our fiscal 2002 and 2001 interest costs and are also expected to lower our fiscal 2003 interest costs. At November 30, 2002, 81% of the interest cost on our debt was effectively fixed and 19% was variable.

At November 30, 2002, our long-term debt had a carrying value of \$3.16 billion. At November 30, 2002, our swap agreements effectively changed \$225 million of fixed rate debt with a weighted-average fixed interest rate of 6.8% to Libor-based floating rate debt. In addition, interest rate swaps at November 30, 2002, effectively changed \$468 million of euribor floating rate debt to fixed rate debt with a weighted-average fixed interest rate of 5.5%. These interest rate swaps mature through 2006. The fair value of our debt and swaps at November 30, 2002 was \$3.33 billion. Based upon a hypothetical 10% decrease or increase in the November 30, 2002 market interest rates, the fair value of our debt and swaps would increase or decrease by \$55 million. In addition, based upon a hypothetical 10% decrease or increase in our November 30, 2002 common stock price, the fair value of our convertible notes would increase or decrease by approximately \$26 million.

These hypothetical amounts are determined by considering the impact of the hypothetical interest rates and common stock price on our existing debt and interest rate swaps. This analysis does not consider the effects of the changes in the level of overall economic activity that could exist in such environments or any relationships which may exist between interest rate and stock price movements. Furthermore, since substantially all of our fixed rate debt cannot currently be called or prepaid and a majority of our variable rate debt is subject to interest rate swaps which effectively fix the interest rate in the short-term, it is unlikely we would be able to take

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any significant steps in the short-term to mitigate our exposure in the event of a significant decrease in market interest rates.

Selected Financial Data

The selected consolidated financial data presented below for fiscal 1998 through 2002 and as of the end of each such fiscal year, are derived from our audited financial statements and should be read in conjunction with those financial statements and the related notes.

| | Years Ended November 30, | | | | |
|---|--------------------------|----------------|-------------|-------------|-------------|
| | 2002 | 2001 | 2000 | 1999 | 1998 |
| (in thousands, except per share data and percentages) | | | | | |
| Statement of Operations and Other Data (a) | | | | | |
| Revenues | \$4,368,269 | \$4,535,751 | \$3,778,542 | \$3,497,470 | \$3,009,306 |
| Operating income | \$1,042,059 | \$ 891,731 | \$ 982,958 | \$1,019,699 | \$ 896,524 |
| Net income (b) | \$1,015,941 (c) | \$ 926,200 (c) | \$ 965,458 | \$1,027,240 | \$ 835,885 |
| Earnings per share (b) | | | | | |
| Basic | \$ 1.73 | \$ 1.58 | \$ 1.61 | \$ 1.68 | \$ 1.40 (d) |
| Diluted | \$ 1.73 | \$ 1.58 | \$ 1.60 | \$ 1.66 | \$ 1.40 (d) |
| Dividends declared per share | \$.420 | \$.420 | \$.420 | \$.375 | \$.315 (d) |
| Cash from operations | \$1,469,032 | \$1,238,936 | \$1,279,535 | \$1,329,724 | \$1,091,840 |
| Capital expenditures | \$1,986,482 | \$ 826,568 | \$1,003,348 | \$ 872,984 | \$1,150,413 |
| Available lower berth days (e) | 21,436 | 20,685 | 15,888 | 14,336 | 12,237 |
| Passengers carried | 3,549 | 3,385 | 2,669 | 2,366 | 2,045 |
| Occupancy percentages (f) | 105.2% | 104.7% | 105.4% | 104.3% | 106.3% |

| | As of November 30, | | | | |
|---|--------------------|------------------|-------------|-------------|-------------|
| | 2002 (a) | 2001 (a) | 2000 (a) | 1999 | 1998 |
| (in thousands, except percentages) | | | | | |
| Balance Sheet and Other Data | | | | | |
| Total assets | \$12,334,848 (g) | \$11,563,552 (g) | \$9,831,320 | \$8,286,355 | \$7,179,323 |
| Long-term debt, excluding current portion | \$ 3,011,969 | \$ 2,954,854 | \$2,099,077 | \$ 867,515 | \$1,563,014 |
| Total shareholders' equity | \$ 7,417,903 | \$ 6,590,777 | \$5,870,617 | \$5,931,247 | \$4,285,476 |
| Debt to capital(h) | 29.9% | 31.1% | 28.6% | 15.3% | 27.6% |

(a) From June 1997 through September 28, 2000, we owned 50% of Costa. On September 29, 2000, we completed the acquisition of the remaining 50% interest in Costa. We accounted for this transaction using the purchase accounting method. Prior to the fiscal 2000 acquisition, we accounted for our 50% interest in Costa using the equity method. Commencing in fiscal 2001, Costa's results of operations have been consolidated in the same manner as our other wholly-owned subsidiaries. Our November 30,

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2000 and subsequent consolidated balance sheets include Costa's balance sheet. All statistical information prior to 2001 does not include Costa. See Notes 5 and 17 in the accompanying financial statements.

- (b) Effective December 1, 2001, we adopted SFAS No. 142, which requires us to stop amortizing goodwill and requires an annual, or when events or circumstances dictate a more frequent, impairment review of goodwill. Accordingly, as of December 1, 2001, we no longer amortize our goodwill. If goodwill had not been recorded for periods prior to December 1, 2001, our adjusted net income and adjusted basic and diluted earnings per share would have been as follows (dollars in thousands, except per share data):

| | Years Ended November 30, | | | |
|-----------------------------|--------------------------|-----------|-------------|-----------|
| | 2001 | 2000 | 1999 | 1998 |
| Net income | \$926,200 | \$965,458 | \$1,027,240 | \$835,885 |
| Goodwill amortization | 25,480 | 23,046 | 20,666 | 17,074 |
| Adjusted net income | \$951,680 | \$988,504 | \$1,047,906 | \$852,959 |
| Adjusted earnings per share | | | | |
| Basic | \$1.63 | \$1.65 | \$1.71 | \$1.43 |
| Diluted | \$1.62 | \$1.64 | \$1.70 | \$1.43 |

- (c) Our net income for fiscal 2002 and 2001 includes an impairment charge of \$20 million and \$140 million, respectively, and fiscal 2001 includes a nonoperating net gain of \$101 million from the sale of our investment in Airtours. In addition, fiscal 2002 includes a \$51 million income tax benefit as a result of a new Italian investment incentive, which allows Costa to receive an income tax benefit based on contractual expenditures during 2002 on construction of new ships. See Notes 4, 5 and 9 in the accompanying financial statements.
- (d) The 1998 per share amounts have been adjusted to reflect a two-for-one stock split effective June 12, 1998.
- (e) Represents the total annual passenger capacity, assuming two passengers per cabin, that our ships offered for sale, which is computed by multiplying passenger capacity by ship operating days.
- (f) In accordance with cruise industry practice, occupancy percentage is calculated based upon two passengers per cabin even though some cabins can accommodate three or more passengers. The percentages in excess of 100% indicate that more than two passengers occupied some cabins.
- (g) Effective December 1, 2000, we adopted SFAS No. 133, which requires that all derivative instruments be recorded on our balance sheet. Total 2002 and 2001 assets include \$178 million and \$567 million, respectively, which represents the fair value of hedged firm commitments. See Note 2 in the accompanying financial statements.
- (h) Represents the percentage of total debt to the sum of total debt and shareholders' equity.

Market Price for Common Stock

Our common stock is traded on the New York Stock Exchange under the symbol CCL. Our intra-day high and low common stock sales prices for the periods indicated were as follows:

| | High | Low |
|----------------|---------|---------|
| Fiscal 2002: | | |
| First Quarter | \$28.62 | \$25.05 |
| Second Quarter | \$34.64 | \$27.40 |
| Third Quarter | \$30.90 | \$22.81 |
| Fourth Quarter | \$29.78 | \$22.07 |

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Fiscal 2001:

| | | |
|----------------|---------|---------|
| First Quarter | \$34.94 | \$21.94 |
| Second Quarter | \$33.40 | \$23.60 |
| Third Quarter | \$33.74 | \$25.89 |
| Fourth Quarter | \$31.47 | \$16.95 |

As of January 29, 2003, there were approximately 4,556 holders of record of our common stock. The Republic of Panama does not currently have tax treaties with any other country. Under current law, we believe that distributions to our shareholders, other than residents of Panama or other business entities conducting business in Panama, are not subject to taxation under the laws of the Republic of Panama. Dividends that we pay to U.S. citizens, residents, corporations and to foreign corporations doing business in the U.S., to the extent treated as "effectively connected" income, will be taxable as ordinary income for U.S. federal income tax purposes to the extent of our current or accumulated earnings and profits, but generally will not qualify for any dividends-received deduction.

Selected Quarterly Financial Data (Unaudited)

Quarterly financial results for fiscal 2002 were as follows:

| | Quarters Ended | | | |
|---------------------------------|---------------------------------------|------------|----------------|----------------|
| | February 28 | May 31 | August 31 | November 30 |
| | (in thousands, except per share data) | | | |
| Revenues | \$ 905,776 | \$ 989,157 | \$1,437,655 | \$1,035,681 |
| Gross profit | \$ 387,611 | \$ 455,702 | \$ 755,412 | \$ 457,625 |
| Operating income | \$ 145,812 | \$ 220,411 | \$ 488,424 (a) | \$ 187,412 (a) |
| Net income | \$ 129,640 | \$ 194,201 | \$ 500,764 | \$ 191,336 |
| Earnings per share | | | | |
| Basic | \$.22 | \$.33 | \$.85 | \$.33 |
| Diluted | \$.22 | \$.33 | \$.85 | \$.33 |
| Dividends declared per share | \$.105 | \$.105 | \$.105 | \$.105 |

(a) Includes a \$17 million and a \$34 million income tax benefit in the August 31 and November 30 quarters, respectively, from Costa, resulting from a new Italian investment incentive law. In addition, the August 31 quarter includes a \$20 million impairment charge.

Quarterly financial results for fiscal 2001 were as follows:

| | Quarters Ended | | | |
|---------------------------------|---------------------------------------|----------------|----------------|---------------|
| | February 28 | May 31 | August 31 | November 30 |
| | (in thousands, except per share data) | | | |
| Revenues | \$1,007,606 | \$1,079,125 | \$1,489,918 | \$959,102 |
| Gross profit | \$ 407,486 | \$ 477,791 | \$ 770,540 | \$411,204 |
| Operating income | \$ 138,941 | \$ 207,907 | \$ 425,346 | \$119,537 |
| Net income | \$ 127,950 (a) | \$ 186,963 (b) | \$ 494,975 (c) | \$116,312 (d) |
| Earnings per share | | | | |
| Basic | \$.22 | \$.32 | \$.84 | \$.20 |
| Diluted | \$.22 | \$.32 | \$.84 | \$.20 |
| Dividends declared per share | \$.105 | \$.105 | \$.105 | \$.105 |

