ROYAL CARIBBEAN CRUISES LTD
Form 10-Q
August 02, 2016
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2016

OR

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

For the transition period from to

Commission File Number: 1-11884
ROYAL CARIBBEAN CRUISES LTD.
(Exact name of registrant as specified in its charter)

Republic of Liberia	98-0081645
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1050 Caribbean Way, Miami, Florida 33132
(Address of principal executive offices) (zip code)

(305) 539-6000
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter 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 ý No o

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No ý

There were 215,264,909 shares of common stock outstanding as of July 26, 2016.

Table of Contents

ROYAL CARIBBEAN CRUISES LTD.

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ROYAL CARIBBEAN CRUISES LTD.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(unaudited; in thousands, except per share data)

	Quarter Ended June 30,	
	2016	2015
Passenger ticket revenues	$1,516,530	$1,507,468
Onboard and other revenues	588,732	550,854
Total revenues	2,105,262	2,058,322
Cruise operating expenses:		
Commissions, transportation and other	334,568	355,835
Onboard and other	136,198	147,105
Payroll and related	230,433	218,570
Food	124,517	119,407
Fuel	176,649	202,565
Other operating	308,222	272,927
Total cruise operating expenses	1,310,587	1,316,409
Marketing, selling and administrative expenses	286,357	274,148
Depreciation and amortization expenses	221,620	206,468
Restructuring charges	4,425	—
Operating Income	282,273	261,297
Other income (expense):		
Interest income	5,683	2,772
Interest expense, net of interest capitalized	(78,747)	(76,620)
Other income (expense)	20,696	(2,482)
	(52,368)	(76,330)
Net Income	$229,905	$184,967
Earnings per Share:		
Basic	$1.07	$0.84
Diluted	$1.06	$0.84
Weighted-Average Shares Outstanding:		
Basic	215,265	219,913
Diluted	216,131	220,902
Comprehensive Income		
Net Income	$229,905	$184,967
Other comprehensive (loss) income:		
Foreign currency translation adjustments	(2,268)	11,741
Change in defined benefit plans	(3,585)	3,742
Gain on cash flow derivative hedges	156,351	202,473
Total other comprehensive income	150,498	217,956
Comprehensive Income	$380,403	$402,923

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

1

ROYAL CARIBBEAN CRUISES LTD.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(unaudited; in thousands, except per share data)

	Six Months Ended June 30,	
	2016	2015
Passenger ticket revenues	$2,894,697	$2,814,247
Onboard and other revenues	1,128,360	1,059,674
Total revenues	4,023,057	3,873,921
Cruise operating expenses:		
Commissions, transportation and other	659,458	680,253
Onboard and other	239,852	263,344
Payroll and related	457,874	430,161
Food	246,027	239,193
Fuel	352,511	407,841
Other operating	596,443	518,234
Total cruise operating expenses	2,552,165	2,539,026
Marketing, selling and administrative expenses	588,378	560,980
Depreciation and amortization expenses	432,384	406,936
Restructuring charges	4,730	—
Operating Income	445,400	366,979
Other income (expense):		
Interest income	8,403	6,509
Interest expense, net of interest capitalized	(144,193)	(146,779)
Other income (including a $21.7 million loss related to the 2016 elimination of the Pullmantur reporting lag)	19,435	3,488
	(116,355)	(136,782)
Net Income	$329,045	$230,197
Earnings per Share:		
Basic	$1.52	$1.05
Diluted	$1.52	$1.04
Weighted-Average Shares Outstanding:		
Basic	216,089	219,770
Diluted	217,040	220,886
Comprehensive Income		
Net Income	$329,045	$230,197
Other comprehensive income (loss):		
Foreign currency translation adjustments	4,380	(19,803)
Change in defined benefit plans	(7,097)	2,249
Gain (loss) on cash flow derivative hedges	159,088	(58,476)
Total other comprehensive income (loss)	156,371	(76,030)
Comprehensive Income	$485,416	$154,167

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

Table of Contents

ROYAL CARIBBEAN CRUISES LTD.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

	As of June 30, 2016 (unaudited)	December 31, 2015
Assets		
Current assets		
Cash and cash equivalents	$175,164	$121,565
Trade and other receivables, net	215,804	238,972
Inventories	112,380	121,332
Prepaid expenses and other assets	265,063	220,579
Derivative financial instruments	3,592	134,574
Assets held for sale	85,935	—
Total current assets	857,938	837,022
Property and equipment, net	20,185,878	18,777,778
Goodwill	288,399	286,764
Other assets	1,139,278	880,479
	$22,471,493	$20,782,043
Liabilities and Shareholders’ Equity		
Current liabilities		
Current portion of long-term debt	$895,411	$899,542
Accounts payable	319,606	302,072
Accrued interest	47,415	38,325
Accrued expenses and other liabilities	551,293	658,601
Derivative financial instruments	237,743	651,866
Customer deposits	2,222,196	1,742,286
Liabilities held for sale	99,967	—
Total current liabilities	4,373,631	4,292,692
Long-term debt	9,153,499	7,627,701
Other long-term liabilities	798,698	798,611
Commitments and contingencies (Note 7)		
Shareholders’ equity		
Preferred stock ($0.01 par value; 20,000,000 shares authorized; none outstanding)	—	—
Common stock ($0.01 par value; 500,000,000 shares authorized; 234,566,541 and 233,905,166 shares issued, June 30, 2016 and December 31, 2015, respectively)	2,346	2,339
Paid-in capital	3,306,685	3,297,619
Retained earnings	7,112,096	6,944,862
Accumulated other comprehensive loss	(1,172,062)	(1,328,433)
Treasury stock (19,312,522 and 15,911,971 common shares at cost, June 30, 2016 and December 31, 2015, respectively)	(1,103,400)	(853,348)
Total shareholders’ equity	8,145,665	8,063,039
	$22,471,493	$20,782,043

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

3

Table of Contents

ROYAL CARIBBEAN CRUISES LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, in thousands)

	Six Months Ended June 30,	
	2016	2015
Operating Activities		
Net income	$329,045	$230,197
Adjustments:		
Depreciation and amortization	432,384	406,936
Net deferred income tax expense	348	2,534
Loss on derivative instruments not designated as hedges	3,979	16,902
Changes in operating assets and liabilities:		
Decrease in trade and other receivables, net	33,929	54,272
Decrease (increase) in inventories	1,394	(17,523)
Increase in prepaid expenses and other assets	(47,056)	(58,722)
Increase in accounts payable	41,173	14,668
Increase in accrued interest	9,090	4,998
Increase (decrease) in accrued expenses and other liabilities	21,839	(39,474)
Increase in customer deposits	467,539	405,752
Dividends received from unconsolidated affiliates	23,878	3,981
Other, net	(46,630)	15,824
Net cash provided by operating activities	1,270,912	1,040,345
Investing Activities		
Purchases of property and equipment	(2,047,195)	(1,151,616)
Cash paid on settlement of derivative financial instruments	(161,307)	(118,521)
Investments in and loans to unconsolidated affiliates	—	(54,250)
Cash received on loans to unconsolidated affiliates	14,923	120,297
Other, net	(18,871)	(12,482)
Net cash used in investing activities	(2,212,450)	(1,216,572)
Financing Activities		
Debt proceeds	5,300,561	2,376,001
Debt issuance costs	(70,406)	(41,171)
Repayments of debt	(3,738,905)	(1,992,232)
Purchases of treasury stock	(250,051)	—
Dividends paid	(243,557)	(197,718)
Proceeds from exercise of common stock options	1,512	5,067
Other, net	1,309	1,156
Net cash provided by financing activities	1,000,463	151,103
Effect of exchange rate changes on cash	9,195	(4,757)
Net increase (decrease) in cash and cash equivalents	68,120	(29,881)
Cash and cash equivalents at beginning of period	121,565	189,241
Less: Cash and cash equivalents attributed to assets held for sale	(14,521)	—
Cash and cash equivalents at end of period	$175,164	$159,360
Supplemental Disclosure		
Cash paid during the period for:		
Interest, net of amount capitalized	$116,531	$120,089
Non-cash Investing Activities		
Notes receivable issued upon sale of property and equipment	$213,042	$—

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

Table of Contents

ROYAL CARIBBEAN CRUISES LTD.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

As used in this Quarterly Report on Form 10-Q, the terms "Royal Caribbean," the "Company," "we," "our" and "us" refer to Royal Caribbean Cruises Ltd. and, depending on the context, Royal Caribbean Cruises Ltd.'s consolidated subsidiaries and/or affiliates. The terms "Royal Caribbean International," "Celebrity Cruises," "Pullmantur," "Azamara Club Cruises," "CDF Croisières de France" and "TUI Cruises" refer to our cruise brands. However, because TUI Cruises is an unconsolidated investment, our operating results and other disclosures herein do not include TUI Cruises unless otherwise specified. In accordance with cruise vacation industry practice, the term "berths" is determined based on double occupancy per cabin even though many cabins can accommodate three or more passengers. This report should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2015, including the audited consolidated financial statements and related notes included therein.

This Quarterly Report on Form 10-Q also includes trademarks, trade names and service marks of other companies. Use or display by us of other parties' trademarks, trade names or service marks is not intended to and does not imply a relationship with, or endorsement or sponsorship of us by, these other parties other than as described herein.

Note 1. General

Description of Business

We are a global cruise company. As of June 30, 2016, we owned Royal Caribbean International, Celebrity Cruises, Pullmantur, Azamara Club Cruises, CDF Croisières de France and a 50% joint venture interest in TUI Cruises.

Sale of Controlling Interest in Pullmantur

In July 2016, we sold 51% of our interest in Pullmantur and CDF Croisières de France. We retained a 49% interest in these businesses as well as full ownership of the vessels currently operated by the brands, which will be bareboat chartered to Pullmantur and CDF Croisières de France. We will also provide certain ship management services to these businesses. As a result of the sale of a majority interest in these businesses, we expect to recognize an immaterial gain and we will no longer consolidate these businesses in our consolidated financial statements. In addition, we also continue to retain full ownership of the aircraft, which were not impacted by this sales transaction. Our investment in these businesses will be accounted for under the equity method of accounting.

The sale did not represent a strategic shift that will have a major effect on our operations and financial results, as we continue to provide similar itineraries to and source passengers from the markets served by the Pullmantur and Croisières de France businesses. Therefore, the sale of these businesses did not meet the criteria for discontinued operations reporting. Due to the change in the nature of the cash flows to be generated by the Pullmantur vessels, we also reviewed the vessels for impairment. We determined that the undiscounted future cash flows of the vessels exceeded their carrying value; therefore, no impairment was required. Pullmantur and CDF Croisières de France met the accounting criteria to be classified as held for sale during the second quarter of 2016 and accordingly all assets and liabilities of these businesses have been reclassified to Assets held for sale and Liabilities held for sale as of June 30, 2016 on our consolidated balance sheets.

The major classes of assets and liabilities of Pullmantur and CDF Croisières de France included in our consolidated balance sheet as of June 30, 2016 were as follows (in thousands):

Assets	
Cash and cash equivalents	$14,521
Trade and other receivables, net	43,466
Inventories	6,943
Prepaid expenses and other assets	14,912
Property and equipment, net	4,436
Other assets	1,657
Total assets held for sale	$85,935
Liabilities	
Accounts payable	$27,691
Accrued expenses and other liabilities	42,873
Customer deposits	26,323
Other liabilities	3,080
Total liabilities held for sale	$99,967

Basis for Preparation of Consolidated Financial Statements

The unaudited consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). Estimates are required for the preparation of financial statements in accordance with these principles. Actual results could differ from these estimates. Refer to Note 2. Summary of Significant Accounting Policies in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2015 for a discussion of our significant accounting policies.

All significant intercompany accounts and transactions are eliminated in consolidation. We consolidate entities over which we have control, usually evidenced by a direct ownership interest of greater than 50%, and variable interest entities where we are determined to be the primary beneficiary. Refer to Note 5. Other Assets for further information regarding our variable interest entities. For affiliates we do not control but over which we have significant influence on financial and operating policies, usually evidenced by a direct ownership interest from 20% to 50%, the investment is accounted for using the equity method.

Prior to January 1, 2016, we consolidated the operating results of Pullmantur and CDF Croisières de France on a two-month reporting lag to allow for more timely preparation of our consolidated financial statements. Effective January 1, 2016, we eliminated the two-month reporting lag to reflect Pullmantur's and CDF Croisières de France's financial position, results of operations and cash flows concurrently and consistently with the fiscal calendar of the Company ("elimination of the Pullmantur reporting lag"). The elimination of the Pullmantur reporting lag represents a change in accounting principle which we believe to be preferable because it provides more current information to the users of our financial statements. A change in accounting principle requires retrospective application, if material. The impact of the elimination of the reporting lag was immaterial to prior periods and is expected to be immaterial for our fiscal year ended December 31, 2016. As a result, we have accounted for this change in accounting principle in our consolidated results for the first six months of 2016. Accordingly, the results of Pullmantur and CDF Croisières de France for November and December 2015, in addition to the six months ended June 30, 2016, are included in our statement of comprehensive income (loss) for the six months ended June 30, 2016. The effect of this change was a decrease to net income of $21.7 million and this amount is reported within Other income in our consolidated statements of comprehensive income (loss) for the six months ended June 30, 2016.

Table of Contents

Note 2. Summary of Significant Accounting Policies

Recent Accounting Pronouncements

In May 2014, amended GAAP guidance was issued to clarify the principles used to recognize revenue for all entities. The guidance is based on the principle that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard also requires more detailed disclosures and provides additional guidance for transactions that were not comprehensively addressed in the prior accounting guidance. Subsequent to the release of this guidance, amended GAAP guidance was issued to provide clarification and additional guidance related to revenue recognition. The revenue recognition guidance discussed above must be applied using one of two retrospective application methods and will be effective for our annual reporting period beginning after December 15, 2017, including interim periods therein. Early adoption is permitted for our annual reporting period beginning after December 15, 2016, including interim periods therein. We are currently evaluating the impact, if any, of the adoption of the revenue recognition guidance to our consolidated financial statements.

In August 2014, GAAP guidance was issued requiring management to evaluate, at each annual and interim reporting period, whether there are conditions or events that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date the financial statements are issued and provide related disclosures. This guidance will be effective for our annual reporting period ending after December 15, 2016 and for annual periods and interim periods thereafter. Early adoption is permitted. The adoption of this guidance is not expected to have an impact to our consolidated financial statements.

In July 2015, amended GAAP guidance was issued to simplify the measurement of inventory for all entities. The amendments apply to all inventory that is measured using first-in, first-out or average cost. The guidance requires an entity to measure inventory at the lower of cost and net realizable value. The guidance must be applied prospectively and will be effective for our interim and annual reporting periods beginning after December 15, 2016. Early adoption is permitted as of the beginning of an interim or annual reporting period. The adoption of this guidance is not expected to have a material impact to our consolidated financial statements.

In November 2015, amended GAAP guidance was issued to simplify the presentation of deferred income taxes. The amendments require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position and eliminates the classification between current and noncurrent amounts. The guidance will be effective for financial statements issued for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. An entity can elect to adopt the amendments either prospectively or retrospectively. Early adoption is permitted as of the beginning of an interim or annual reporting period. The adoption of this guidance is not expected to have a material impact to our consolidated financial statements.

In January 2016, amended GAAP guidance was issued to address certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The amendments primarily impact the accounting for certain equity investments, the accounting for financial liabilities subject to the fair value option and the presentation and disclosure requirements for financial instruments. The guidance will be effective for financial statements issued for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. Early adoption is permitted for financial statements of fiscal years and interim periods that have not yet been issued or that have not yet been made available for issuance as of the beginning of the fiscal year of adoption. The adoption of this newly issued guidance is not expected to have a material impact to our consolidated financial statements.

In February 2016, amended GAAP guidance was issued to increase the transparency and comparability of lease accounting among organizations. For leases with a term greater than 12 months, the amendments require the lease rights and obligations arising from the leasing arrangements, including operating leases, to be recognized as assets and liabilities on the balance sheet. The amendments also expand the required disclosures surrounding leasing arrangements. The guidance must be applied using a retrospective application method and will be effective for financial statements issued for fiscal years beginning after December 15, 2018 and interim periods within those years. Early adoption is permitted. We are currently evaluating the impact of the adoption of this newly issued guidance to our consolidated financial statements.

In March 2016, amended GAAP guidance was issued addressing the effect of derivative contract novations on existing hedge accounting relationships. The amendments clarify that a change in the counterparty to a derivative instrument that has been designated as a hedging instrument does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria continue to be met. The guidance must be applied using a prospective or modified retrospective application method and will be effective for financial statements issued for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The adoption of this newly issued guidance is not expected to have a material impact to our consolidated financial statements.

Table of Contents

In March 2016, amended GAAP guidance was issued addressing contingent put and call options in debt instruments. The amendments clarify the requirements for assessing whether contingent call and put options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt hosts, or whether the embedded call and put options should be bifurcated from the related debt instrument and accounted for separately as a derivative. The guidance must be applied using a modified retrospective approach and will be effective for financial statements issued for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The adoption of this newly issued guidance is not expected to have an impact to our consolidated financial statements.

In March 2016, amended GAAP guidance was issued to simplify the transition to the equity method of accounting. The amendments eliminate the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations and retained earnings retroactively on a step-by step basis as if the equity method had been in effect during all previous periods that the investment had been held. The guidance must be applied prospectively and will be effective for financial statements issued for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. Early adoption is permitted. The adoption of this newly issued guidance is not expected to have a material impact to our consolidated financial statements, but could have an impact on our accounting for equity method investments in the future.

In March 2016, amended GAAP guidance was issued to simplify several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The guidance will be effective for annual periods beginning after December 15, 2016 and interim periods within those annual periods. Early adoption is permitted, including adoption in an interim period. The adoption of this newly issued guidance is not expected to have a material impact to our consolidated financial statements.

In June 2016, amended GAAP guidance was issued to address expected credit losses on financial instruments and other commitments. The amendment requires financial assets and net investment leases that are currently measured at amortized cost basis be presented at the net amount expected to be collected. The guidance must be applied using the modified-retrospective approach and will be effective for annual periods beginning after December 15, 2019 and interim periods within those annual periods. Early adoption is permitted beginning after December 15, 2018. The adoption of this newly issued guidance is not expected to have a material impact to our consolidated financial statements.

Other

Revenues and expenses include port costs that vary with guest head counts. The amounts of such port costs included in Passenger ticket revenues on a gross basis were $140.0 million and $141.7 million for the second quarters of 2016 and 2015, respectively, and $284.4 million and $268.8 million for the six months ended June 30, 2016 and 2015, respectively.

Reclassifications

On January 1, 2016, we adopted ASC 835, Presentation of Debt Issuance Costs ("ASC 835"), using the retrospective approach. Due to the adoption of ASC 835, $139.8 million of debt issuance costs have been reclassified in the consolidated balance sheet, as of December 31, 2015, from Other assets to either Current portion of long-term debt or Long-term debt in order to conform to the current year presentation.

For the six months ended June 30, 2015, $4.0 million has been reclassified in the consolidated statements of cash flows from Other, net to Dividends received from unconsolidated affiliates within Net cash provided by operating activities in order to conform to the current year presentation.

Table of Contents

Note 3. Earnings Per Share

A reconciliation between basic and diluted earnings per share is as follows (in thousands, except per share data):

	Quarter Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net income for basic and diluted earnings per share	$229,905	$184,967	$329,045	$230,197
Weighted-average common shares outstanding	215,265	219,913	216,089	219,770
Dilutive effect of stock options, performance share awards and restricted stock awards	866	989	951	1,116
Diluted weighted-average shares outstanding	216,131	220,902	217,040	220,886
Basic earnings per share	$1.07	$0.84	$1.52	$1.05
Diluted earnings per share	$1.06	$0.84	$1.52	$1.04

There were no antidilutive shares for the quarters and six month periods ended June 30, 2016 and June 30, 2015, respectively.

Note 4. Property and Equipment

In April 2016, we completed the previously announced sale of Splendour of the Seas to TUI Cruises for €188 million, or $213 million. Concurrent with the acquisition, TUI Cruises leased the ship to Thomson Cruises, an affiliate of TUI AG, our joint venture partner, who will operate the ship. The sale resulted in an immaterial gain.

In June 2016, we entered into an agreement to sell a ship to Thomson Cruises for $230.0 million in cash. The sale is scheduled to be completed in March 2017 in order to retain the future revenues to be generated for sailings through that date. We expect to recognize a gain on the sale, which we do not expect will have a material effect to our consolidated financial statements.

Note 5. Other Assets

A Variable Interest Entity (“VIE”) is an entity in which the equity investors have not provided enough equity to finance the entity’s activities or the equity investors: (1) cannot directly or indirectly make decisions about the entity’s activities through their voting rights or similar rights; (2) do not have the obligation to absorb the expected losses of the entity; (3) do not have the right to receive the expected residual returns of the entity; or (4) have voting rights that are not proportionate to their economic interests and the entity’s activities involve or are conducted on behalf of an investor with a disproportionately small voting interest.

We have determined that TUI Cruises GmbH, our 50%-owned joint venture, which operates the brand TUI Cruises, is a VIE. As of June 30, 2016, the net book value of our investment in TUI Cruises was approximately $514.9 million, consisting of $305.9 million in equity and a loan of $209.0 million. The loan is in connection with the sale of Splendour of the Seas, in the amount of the sales price, which was completed in April 2016 and is to be repaid to us over 10 years. The term loan is 50% guaranteed by TUI AG and is secured by a first priority mortgage on the ship. Interest accrues at the rate of 6.25% per annum. Refer to Note 4. Property and Equipment for further information. As of December 31, 2015, our equity investment in TUI Cruises was approximately $293.8 million. The majority of these amounts were included within Other assets in our consolidated balance sheets.

In addition, we and TUI AG, our joint venture partner, have each guaranteed the repayment of 50% of a bank loan. As of June 30, 2016, the outstanding principal amount of the loan was €126.9 million, or approximately $141.0 million based on the exchange rate at June 30, 2016. While this loan matures in May 2022, the lenders have agreed to release each shareholder's guarantee in 2018. The loan amortizes quarterly and is secured by first mortgages on the Mein Schiff 1 and Mein Schiff 2 vessels. Based on current facts and circumstances, we do not believe potential obligations under our guarantee of this bank loan are probable.

Our investment amount, outstanding term loan and the potential obligations under the bank loan guarantee are substantially our maximum exposure to loss in connection with our investment in TUI Cruises. We have determined that we are not the primary beneficiary of TUI Cruises. We believe that the power to direct the activities that most significantly impact TUI Cruises’ economic performance are shared between ourselves and TUI AG. All the significant operating and financial decisions of TUI Cruises require the consent of both parties, which we believe creates shared power over TUI Cruises. Accordingly, we do not consolidate this entity and account for this investment under the equity method of accounting.

As of June 30, 2016, TUI Cruises has three newbuild ships on order scheduled to be delivered in each of 2017, 2018 and 2019. TUI Cruises has in place agreements for the secured financing of each of the ships on order for up to 80% of the contract price. Finnvera, the official export credit agency of Finland, has agreed to guarantee to the lenders payment of 95% of each financing. The remaining portion of the contract price of the ships is expected to be funded through an existing €150.0 million bank facility and TUI Cruises’ cash flows from operations. The various ship construction and financing agreements include certain restrictions on each of our and TUI AG's ability to reduce our current ownership interest in TUI Cruises below 37.55% through 2021.

We have determined that Grand Bahama Shipyard Ltd. ("Grand Bahama"), a ship repair and maintenance facility in which we have a 40% noncontrolling interest, is a VIE. The facility serves cruise and cargo ships, oil and gas tankers and offshore units. We utilize this facility, among other ship repair facilities, for our regularly scheduled drydocks and certain emergency repairs as may be required. During the quarter and six months ended June 30, 2016, we made payments of $12.3 million and $33.4 million, respectively, to Grand Bahama for ship repair and maintenance services. We have determined that we are not the primary beneficiary of this facility as we do not have the power to direct the activities that most significantly impact the facility's economic performance. Accordingly, we do not consolidate this entity and we account for this investment under the equity method of accounting. As of June 30, 2016, the net book value of our investment in Grand Bahama was approximately $47.9 million, consisting of $24.1 million in equity and a loan of $23.8 million. As of December 31, 2015, the net book value of our investment in Grand Bahama was approximately $51.2 million, consisting of $12.6 million in equity and a loan of $38.6 million. These amounts represent our maximum exposure to loss related to our investment in Grand Bahama. Our debt agreement with Grand Bahama was amended during the quarter ended March 31, 2016 to extend the maturity by 10 years and increase the applicable interest rate to the lower of (i) LIBOR plus 3.50% and (ii) 5.5%. Interest payable on the loan is due on a semi-annual basis. We continue to classify the loan, as modified, as non-accrual status. The loan balance is included within Other assets in our consolidated balance sheets. During the quarter and six months ended June 30, 2016, we received principal payments of approximately $7.7 million and $14.8 million, respectively. We monitor credit risk associated with the loan through our participation on Grand Bahama's board of directors along with our review of Grand Bahama's financial statements and projected cash flows. Based on this review, we believe the risk of loss associated with the outstanding loan is not probable as of June 30, 2016.

We have determined that Skysea Holding International Ltd. ("Skysea Holding"), in which we have a 35% noncontrolling interest, is a VIE for which we are not the primary beneficiary, as we do not have the power to direct the activities that most significantly impact the entity's economic performance. Accordingly, we do not consolidate this entity and we account for this investment under the equity method of accounting. In December 2014, we and Ctrip.com International Ltd, which also owns 35% of Skysea Holding, each provided a debt facility to a wholly owned subsidiary of Skysea Holding in the amount of $80.0 million. Interest under these facilities, which mature in January 2030, initially accrues at a rate of 3.0% per annum with an increase of at least 0.5% every two years through maturity. The facilities, which are pari passu to each other, are each 100% guaranteed by Skysea Holding and are secured by first priority mortgages on the ship, Golden Era. As of June 30, 2016, the net book value of our investment in Skysea Holding and its subsidiaries was approximately $94.8 million, consisting of $13.6 million in equity and a loan of $81.2 million. As of December 31, 2015, the net book value of our investment in Skysea Holding and its subsidiaries was approximately $99.8 million, consisting of $17.3 million in equity and a loan of $82.4 million. The majority of these amounts were included within Other assets in our consolidated balance sheets and represent our maximum exposure to loss related to our investment in Skysea Holding.

Our share of income from investments accounted for under the equity method of accounting, including the entities discussed above, was $27.3 million and $14.7 million for the quarters ended June 30, 2016 and June 30, 2015, respectively, and $48.3 million and $23.8 million for the six months ended June 30, 2016 and June 30, 2015, respectively, and was recorded within Other income (expense). We received $23.1 million and $2.8 million of dividends from our equity method investees for the quarters ended June 30, 2016 and June 30, 2015, respectively, and $23.9 million and $4.0 million for the six months ended June 30, 2016 and June 30, 2015, respectively. We also provide ship management and procurement services to TUI Cruises GmbH and Skysea Holding and recorded $4.2 million and $5.9 million in revenues and $3.0 million and $6.4 million in expenses for these services during the quarters ended June 30, 2016 and June 30, 2015, respectively, and $8.6 million and $11.6 million in revenues and $6.5 million and $9.5 million in expenses for these services during the six months ended June 30, 2016 and June 30, 2015, respectively. These amounts were recorded within Onboard and other revenues and Other operating expenses, respectively.

Note 6. Long-Term Debt

In February 2016, we amended our unsecured term loans for Oasis of the Seas and Allure of the Seas to reduce the margins on those facilities and incorporate certain covenant improvements included in our more recent credit facilities. The interest rate on both the $420.0 million floating rate tranche of the Oasis of the Seas term loan and the $1.1 billion Allure of the Seas term loan was reduced from LIBOR plus 1.85% to LIBOR plus 1.65%. These amendments did not result in the extinguishment of debt.

In February 2016, we agreed with the lenders on our €365.0 million unsecured term loan due 2017 to convert €247.5 million, or $273.2 million, of the outstanding principal balance from Euro to US dollars. Interest on the new US dollar tranche accrues at a floating rate based on LIBOR plus the applicable margin. The balance of the facility of €117.5 million will remain outstanding in Euro and will continue to accrue interest at a floating rate based on EURIBOR, subject to a 0% floor, plus the applicable margin. The applicable margin varies with our debt rating and was 1.75% as of June 30, 2016. The amendment did not result in the extinguishment of debt.

In April 2016, we took delivery of Ovation of the Seas. To finance the purchase, we borrowed $841.8 million under a previously committed unsecured term loan which is 95% guaranteed by Euler Hermes Deutschland AG ("Hermes"), the official export credit agency of Germany. The loan amortizes semi-annually over 12 years and bears interest at LIBOR plus a margin of 1.00%, totaling 1.91% as of June 30, 2016. During 2015, we entered into forward-starting interest rate swap agreements which effectively converted $830.0 million of the loan from the floating rate available to us per the credit agreement to a fixed rate, including the applicable margin, of 3.16% effective from April 2016 through the maturity of the loan. See Note 10. Fair Value Measurements and Derivative Instruments for further information regarding these agreements.

In April 2016, we entered into and drew in full on a credit agreement which provides an unsecured term loan in the amount of $200 million. The loan is due and payable at maturity in April 2017. Interest on the loan accrues at a floating rate based on LIBOR plus a margin of 1.30%, totaling 1.75% as of June 30, 2016. The proceeds from this loan were used to repay amounts outstanding under our unsecured revolving credit facilities.

Table of Contents

In May 2016, we took delivery of Harmony of the Seas. To finance the purchase, we borrowed an unsecured Euro-denominated term loan in the amount of €700.7 million, or $778.8 million based on the exchange rate at June 30, 2016, and an unsecured US dollar-denominated term loan in the amount of $226.1 million under previously committed credit agreements. Both of the facilities are 100% guaranteed by Compagnie Francaise d’Assurance pour le Commerce Extérieur (“COFACE”), the official export credit agency of France. The Euro-denominated term loan amortizes semi-annually over 12 years and bears interest at EURIBOR, subject to a 0% floor, plus the applicable margin of 1.15%, totaling 1.15% as of June 30, 2016. The US dollar-denominated term loan amortizes semi-annually over 12 years and bears interest at a fixed rate of 2.53%. During 2015, we entered into forward-starting interest rate swap agreements which effectively converted €693.4 million, or $770.7 million based on the exchange rate at June 30, 2016, of the Euro-denominated term loan from the floating rate per the credit agreement to a fixed rate, including the applicable margin, of 2.26% effective from May 2016 through the maturity of the loan. See Note 10. Fair Value Measurements and Derivative Instruments for further information regarding these agreements.

Note 7. Commitments and Contingencies

In June 2016, we entered into credit agreements for the unsecured financing of our two "Project Edge" ships for up to 80% of each ship’s contract price through facilities to be guaranteed 100% by COFACE. The ships are expected to enter service in the second half of 2018 and the first half of 2020, respectively. Under these financing arrangements, we have the right, but not the obligation, to satisfy the obligations to be incurred upon delivery and acceptance of each vessel under the shipbuilding contract by assuming, at delivery and acceptance, the debt indirectly incurred by the shipbuilder during the construction of each ship. The maximum loan amount under each facility is not to exceed the US dollar equivalent of €622.6 million and €652.6 million, or approximately $692.0 million and $725.4 million, respectively, based on the exchange rate at June 30, 2016, for the first "Project Edge" ship delivery and the second "Project Edge" ship delivery, respectively. The loans will amortize semi-annually and will mature 12 years following delivery of each ship. Interest on the loans will accrue at a fixed rate of 3.23%.

In May 2016, we signed a memorandum of understanding with STX France to build a fifth Oasis-class ship expected to be delivered in the first half of 2021, and two additional "Project Edge" ships expected to be delivered in the second half of each of 2021 and 2022. These orders are contingent upon completion of customary conditions, including documentation and financing.

As of June 30, 2016, the aggregate cost of our ships on firm order, not including the TUI Cruises' ships on order and those subject to conditions to effectiveness, was approximately $5.3 billion, of which we had deposited $151.5 million as of such date. Approximately 65.1% of the aggregate cost was exposed to fluctuations in the Euro exchange rate at June 30, 2016. Refer to Note 10. Fair Value Measurements and Derivative Instruments for further information.

In July 2016, we executed an agreement with Miami Dade County (“MDC”), which was subsequently assigned to Sumitomo Banking Corporation (“SMBC”), to lease land from MDC and construct a new cruise terminal at PortMiami in Miami, Florida. The terminal is expected to be approximately 170,000 square-feet and will serve as a homeport to the Royal Caribbean International brand. During the construction period, expected to be approximately 42 months, SMBC will fund the costs of the terminal’s construction and land lease. Upon completion of the terminal's construction, we will operate and lease the terminal from SMBC for a five-year term. We determined that the lease arrangement between SMBC and us should be accounted for as an operating lease upon completion of the terminal.
Litigation

In April 2015, the Alaska Department of Environmental Conservation issued Notices of Violation to Royal Caribbean International and Celebrity Cruises seeking monetary penalties for alleged violations of the Alaska Marine Visible Emission Standards that occurred over the past five years on certain of our vessels. We believe we have meritorious defenses to the allegations and we are cooperating with the state of Alaska. We do not believe that the ultimate outcome of these claims will have a material adverse impact on our financial condition or results of operations and cash flows.

We are routinely involved in other claims typical within the cruise vacation industry. The majority of these claims are covered by insurance. We believe the outcome of such claims, net of expected insurance recoveries, will not have a material adverse impact on our financial condition or results of operations and cash flows.

Other

If any person acquires ownership of more than 50% of our common stock or, subject to certain exceptions, during any 24-month period, a majority of the Board is no longer comprised of individuals who were members of the Board on the first day of such period, we may be obligated to prepay indebtedness outstanding under our credit facilities, which we may be unable to replace on similar terms. Our public debt securities also contain change of control provisions that would be triggered by a third-party acquisition of greater than 50% of our common stock coupled with a ratings downgrade. If this were to occur, it would have an adverse impact on our liquidity and operations.

Note 8. Shareholders' Equity

During the first and second quarters of 2016, we declared and paid a cash dividend on our common stock of $0.375 per share. During the first quarter of 2016, we also paid a cash dividend on our common stock of $0.375 per share which was declared during the fourth quarter of 2015.

During the first and second quarters of 2015, we declared and paid a cash dividend on our common stock of $0.30 per share. During the first quarter of 2015, we also paid a cash dividend on our common stock of $0.30 per share which was declared during the fourth quarter of 2014.

In October 2015, our board of directors authorized a common stock repurchase program for up to $500 million. The timing and number of shares purchased depend on a variety of factors including price and market conditions. During the first and second quarters of 2016, we purchased 2.8 million and 0.6 million shares, respectively, for a total of $200.0 million and $50.0 million, respectively, in open market transactions. These transactions were recorded within Treasury stock in our consolidated balance sheet. Following these repurchases, as well as the $200.0 million of stock repurchased during the fourth quarter of 2015, we have $50 million that remains available for future stock repurchase transactions under our Board approved program. Future stock repurchase transactions could include open market purchases or accelerated share repurchases. We expect to complete the program by the end of 2016.

Table of Contents

Note 9. Changes in Accumulated Other Comprehensive Income (Loss)

The following table presents the changes in accumulated other comprehensive income (loss) by component for the six months ended June 30, 2016 and 2015 (in thousands):

	Accumulated Other Comprehensive Income (Loss) for the Six Months Ended June 30, 2016				Accumulated Other Comprehensive Income (Loss) for the Six Months Ended June 30, 2015			
	Changes related to cash flow derivative hedges	Changes in defined benefit plans	Foreign currency translation adjustments	Accumulated other comprehensive loss	Changes related to cash flow derivative hedges	Changes in defined benefit plans	Foreign currency translation adjustments	Accumulated other comprehensive loss
Accumulated comprehensive loss at beginning of the year	$(1,232,073)	$(26,447)	$(69,913)	$(1,328,433)	$(826,026)	$(31,207)	$(39,761)	$(896,994)
Other comprehensive (loss) income before reclassifications	(24,062)	(8,184)	4,380	(27,866)	(183,646)	1,249	(19,803)	(202,200)
Amounts reclassified from accumulated other comprehensive loss	183,150	1,087	—	184,237	125,170	1,000	—	126,170
Net current-period other comprehensive income (loss)	159,088	(7,097)	4,380	156,371	(58,476)	2,249	(19,803)	(76,030)
Ending balance	$(1,072,985)	$(33,544)	$(65,533)	$(1,172,062)	$(884,502)	$(28,958)	$(59,564)	$(973,024)

The following table presents reclassifications out of accumulated other comprehensive income (loss) for the quarters and six months ended June 30, 2016 and 2015 (in thousands):

Details About Accumulated Other Comprehensive Income (Loss) Components	Amount of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income (Loss) into Income				Affected Line Item in Statements of Comprehensive Income (Loss)
	Quarter Ended June 30, 2016	Quarter Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	
Loss on cash flow derivative hedges:					
Interest rate swaps	$(10,938)	$(9,962)	$(20,066)	$(16,748)	Interest expense, net of interest capitalized
Foreign currency forward contracts	(1,980)	(685)	(2,698)	(1,402)	Depreciation and amortization expenses
Foreign currency forward contracts	(12,830)	(239)	(6,742)	(477)	Other income (expense)

Foreign currency forward contracts	(207)	—	(207)	—	Other operating
Foreign currency collar options	(601)	(435)	(1,204)	(435)	Depreciation and amortization expenses
Fuel swaps	13,933	—	6,597	—	Other income (expense)
Fuel swaps	(68,129)	(52,416)	(158,830)	(106,108)	Fuel
	(80,752)	(63,737)	(183,150)	(125,170)	
Amortization of defined benefit plans:					
Actuarial loss	(285)	(354)	(1,087)	(707)	Payroll and related
Prior service costs	—	(84)	—	(293)	Payroll and related
	(285)	(438)	(1,087)	(1,000)	
Total reclassifications for the period	$(81,037)	$(64,175)	$(184,237)	$(126,170)	

Table of Contents

Note 10. Fair Value Measurements and Derivative Instruments

Fair Value Measurements

The estimated fair value of our financial instruments that are not measured at fair value, categorized based upon the fair value hierarchy, are as follows (in thousands):

	Fair Value Measurements at June 30, 2016 Using					Fair Value Measurements at December 31, 2015 Using				
Description	Total Carrying Amount	Total Fair Value	Level 1(1)	Level 2(2)	Level 3(3)	Total Carrying Amount	Total Fair Value	Level 1(1)	Level 2(2)	Level
Assets:										
Cash and cash equivalents(4)	$175,164	$175,164	$175,164	$—	$—	$121,565	$121,565	$121,565	$—	$—
Cash attributed to assets held for sale(4)	$14,521	14,521	14,521	—	—	—	—	—	—	—
Total Assets	$189,685	$189,685	$189,685	$—	$—	$121,565	$121,565	$121,565	$—	$—
Liabilities:										
Long-term debt (including current portion of long-term debt)(5)	$10,004,487	$10,526,958	$1,202,286	$9,324,672	$—	$8,478,473	$8,895,009	$1,536,629	$7,358,380	$—
Total Liabilities	$10,004,487	$10,526,958	$1,202,286	$9,324,672	$—	$8,478,473	$8,895,009	$1,536,629	$7,358,380	$—

(1) Inputs based on quoted prices (unadjusted) in active markets for identical assets or liabilities that we have the ability to access. Valuation of these items does not entail a significant amount of judgment.
(2) Inputs other than quoted prices included within Level 1 that are observable for the liability, either directly or indirectly. For unsecured revolving credit facilities and unsecured term loans, fair value is determined utilizing the income valuation approach. This valuation model takes into account the contract terms of our debt such as the debt maturity and the interest rate on the debt. The valuation model also takes into account the creditworthiness of the Company.
(3) Inputs that are unobservable. The Company did not use any Level 3 inputs as of June 30, 2016 and December 31, 2015.
(4) Consists of cash and marketable securities with original maturities of less than 90 days.
(5) Consists of unsecured revolving credit facilities, senior notes, senior debentures and term loans. Does not include our capital lease obligations.

Other Financial Instruments

The carrying amounts of accounts receivable, accounts payable, accrued interest and accrued expenses approximate fair value at June 30, 2016 and December 31, 2015.

15

Table of Contents

Assets and liabilities that are recorded at fair value have been categorized based upon the fair value hierarchy. The following table presents information about the Company's financial instruments recorded at fair value on a recurring basis (in thousands):

	Fair Value Measurements at June 30, 2016 Using				Fair Value Measurements at December 31, 2015 Using			
Description	Total	Level 1(1)	Level 2(2)	Level 3(3)	Total	Level 1(1)	Level 2(2)	Level 3(3)
Assets:								
Derivative financial instruments(4)	$41,633	$ —	$41,633	$ —	$134,574	$ —	$134,574	$ —
Investments(5)	$3,697	3,697	—	—	$3,965	3,965	—	—
Total Assets	$45,330	$ 3,697	$41,633	$ —	$138,539	$ 3,965	$134,574	$ —
Liabilities:								
Derivative financial instruments(6)	$614,150	$ —	$614,150	$ —	$1,044,292	$ —	$1,044,292	$ —
Total Liabilities	$614,150	$ —	$614,150	$ —	$1,044,292	$ —	$1,044,292	$ —

(1) Inputs based on quoted prices (unadjusted) in active markets for identical assets or liabilities that we have the ability to access. Valuation of these items does not entail a significant amount of judgment.
(2) Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. For foreign currency forward contracts, interest rate swaps, cross currency swaps and fuel swaps, fair value is derived using valuation models that utilize the income valuation approach. These valuation models take into account the contract terms, such as maturity, as well as other inputs, such as foreign exchange rates and curves, fuel types, fuel curves and interest rate yield curves. Fair value for foreign currency collar options is determined by using standard option pricing models with inputs based on the options' contract terms, such as exercise price and maturity, and readily available public market data, such as foreign exchange curves, foreign exchange volatility levels and discount rates. All derivative instrument fair values take into account the creditworthiness of the counterparty and the Company.
(3) Inputs that are unobservable. The Company did not use any Level 3 inputs as of June 30, 2016 and December 31, 2015.
(4) Consists of foreign currency forward contracts, interest rate swaps and fuel swaps. Please refer to the "Fair Value of Derivative Instruments" table for breakdown by instrument type.
(5) Consists of exchange-traded equity securities and mutual funds reported within Other assets in our consolidated balance sheets.
(6) Consists of foreign currency forward contracts, interest rate swaps and fuel swaps. Please refer to the "Fair Value of Derivative Instruments" table for breakdown by instrument type.

The reported fair values are based on a variety of factors and assumptions. Accordingly, the fair values may not represent actual values of the financial instruments that could have been realized as of June 30, 2016 or December 31, 2015, or that will be realized in the future, and do not include expenses that could be incurred in an actual sale or settlement.

We have master International Swaps and Derivatives Association ("ISDA") agreements in place with our derivative instrument counterparties. These ISDA agreements provide for final close out netting with our counterparties for all positions in the case of default or termination of the ISDA agreement. We have determined that our ISDA agreements provide us with rights of setoff on the fair value of derivative instruments in a gain position and those in a loss position with the same counterparty. We have elected not to offset such derivative instrument fair values in our consolidated balance sheets.

As of June 30, 2016 and December 31, 2015, no cash collateral was received or pledged under our ISDA agreements. See Credit Related Contingent Features for further discussion on contingent collateral requirements for our derivative instruments.

Table of Contents

The following table presents information about the Company's offsetting of financial assets under master netting agreements with derivative counterparties:

	Gross Amounts not Offset in the Consolidated Balance Sheet that are Subject to Master Netting Agreements							
	As of June 30, 2016				As of December 31, 2015			
(In thousands)	Gross Amount of Derivative Assets Presented in the Consolidated Balance Sheet	Gross Amount of Eligible Offsetting Recognized Derivative Liabilities	Cash Collateral Received	Net Amount of Derivative Assets	Gross Amount of Derivative Assets Presented in the Consolidated Balance Sheet	Gross Amount of Eligible Offsetting Recognized Derivative Assets	Cash Collateral Received	Net Amount of Derivative Assets
Derivatives subject to master netting agreements	$41,633	$(41,633)	$ —	$ —	$134,574	$(129,815)	$ —	$ 4,759
Total	$41,633	$(41,633)	$ —	$ —	$134,574	$(129,815)	$ —	$ 4,759

The following table presents information about the Company's offsetting of financial liabilities under master netting agreements with derivative counterparties:

	Gross Amounts not Offset in the Consolidated Balance Sheet that are Subject to Master Netting Agreements							
	As of June 30, 2016				As of December 31, 2015			
(In thousands)	Gross Amount of Derivative Liabilities Presented in the Consolidated Balance Sheet	Gross Amount of Eligible Offsetting Recognized Derivative Assets	Cash Collateral Pledged	Net Amount of Derivative Liabilities	Gross Amount of Derivative Liabilities Presented in the Consolidated Balance Sheet	Gross Amount of Eligible Offsetting Recognized Derivative Liabilities	Cash Collateral Pledged	Net Amount of Derivative Liabilities
Derivatives subject to master netting agreements	$(614,150)	$ 41,633	$ —	$(572,517)	$(1,044,292)	$ 129,815	$ —	$(914,477)
Total	$(614,150)	$ 41,633	$ —	$(572,517)	$(1,044,292)	$ 129,815	$ —	$(914,477)

Concentrations of Credit Risk

We monitor our credit risk associated with financial and other institutions with which we conduct significant business and, to minimize these risks, we select counterparties with credit risks acceptable to us and we seek to limit our exposure to an individual counterparty. Credit risk, including but not limited to counterparty nonperformance under derivative instruments, our credit facilities and new ship progress payment guarantees, is not considered significant, as we primarily conduct business with large, well-established financial institutions, insurance companies and export credit agencies many of which we have long-term relationships with and which have credit risks acceptable to us or where the credit risk is spread out among a large number of counterparties. As of June 30, 2016, we did not have any exposure under our derivative instruments. As of December 31, 2015, we had counterparty credit risk exposure under our derivative instruments of approximately $4.8 million, which was limited to the cost of replacing the contracts in the event of non-performance by the counterparties to the contracts, the majority of which are currently our lending banks. We do not anticipate nonperformance by any of our significant counterparties. In addition, we have established guidelines we follow regarding credit ratings and instrument maturities to maintain safety and liquidity. We do not normally require collateral or other security to support credit relationships; however, in certain circumstances this option is available to us.

Derivative Instruments

We are exposed to market risk attributable to changes in interest rates, foreign currency exchange rates and fuel prices. We manage these risks through a combination of our normal operating and financing activities and through the use of derivative financial instruments pursuant to our hedging practices and policies. The financial impact of these hedging instruments is primarily offset by corresponding changes in the underlying exposures being hedged. We achieve this by closely matching the notional amount, term and conditions of the derivative instrument with the underlying risk being hedged. Although certain of our derivative financial instruments do not qualify or are not accounted for under hedge accounting, we do not hold or issue derivative financial instruments for trading or other speculative purposes. We monitor our derivative positions using techniques including market valuations and sensitivity analyses.

We enter into various forward, swap and option contracts to manage our interest rate exposure and to limit our exposure to fluctuations in foreign currency exchange rates and fuel prices. These instruments are recorded on the balance sheet at their fair value and the vast majority are designated as hedges. We also use non-derivative financial instruments designated as hedges of our net investment in our foreign operations and investments.

At inception of the hedge relationship, a derivative instrument that hedges the exposure to changes in the fair value of a firm commitment or a recognized asset or liability is designated as a fair value hedge. A derivative instrument that hedges a forecasted transaction or the variability of cash flows related to a recognized asset or liability is designated as a cash flow hedge.

Changes in the fair value of derivatives that are designated as fair value hedges are offset against changes in the fair value of the underlying hedged assets, liabilities or firm commitments. Gains and losses on derivatives that are designated as cash flow hedges are recorded as a component of Accumulated other comprehensive loss until the underlying hedged transactions are recognized in earnings. The foreign currency transaction gain or loss of our non-derivative financial instruments and the changes in the fair value of derivatives designated as hedges of our net investment in foreign operations and investments are recognized as a component of Accumulated other comprehensive loss along with the associated foreign currency translation adjustment of the foreign operation.

On an ongoing basis, we assess whether derivatives used in hedging transactions are “highly effective” in offsetting changes in the fair value or cash flow of hedged items. We use the long-haul method to assess hedge effectiveness using regression analysis for each hedge relationship under our interest rate, foreign currency and fuel hedging programs. We apply the same methodology on a consistent basis for assessing hedge effectiveness to all hedges within each hedging program (i.e. interest rate, foreign currency and fuel). We perform regression analyses over an observation period of up to three years, utilizing market data relevant to the hedge horizon of each hedge relationship. High effectiveness is achieved when a statistically valid relationship reflects a high degree of offset and correlation between the changes in the fair values of the derivative instrument and the hedged item. The determination of ineffectiveness is based on the amount of dollar offset between the change in fair value of the derivative instrument and the change in fair value of the hedged item at the end of the reporting period. If it is determined that a derivative is not highly effective as a hedge or hedge accounting is discontinued, any change in fair value of the derivative since the last date at which it was determined to be effective is recognized in earnings. In addition, the ineffective portion of our highly effective hedges is immediately recognized in earnings and reported in Other income (expense) in our consolidated statements of comprehensive income (loss).

Cash flows from derivative instruments that are designated as fair value or cash flow hedges are classified in the same category as the cash flows from the underlying hedged items. In the event that hedge accounting is discontinued, cash flows subsequent to the date of discontinuance are classified within investing activities. Cash flows from derivative instruments not designated as hedging instruments are classified as investing activities.

We consider the classification of the underlying hedged item’s cash flows in determining the classification for the designated derivative instrument’s cash flows. We classify derivative instrument cash flows from hedges of benchmark interest rate or hedges of fuel expense as operating activities due to the nature of the hedged item. Likewise, we classify derivative instrument cash flows from hedges of foreign currency risk on our newbuild ship payments as investing activities and derivative instrument cash flows from hedges of foreign currency risk on debt payments as financing activities.

Interest Rate Risk

Our exposure to market risk for changes in interest rates relates to our long-term debt obligations including future interest payments. At June 30, 2016 and December 31, 2015, approximately 40.0% and 31.2%, respectively, of our long-term debt was effectively fixed. We use interest rate swap agreements to modify our exposure to interest rate movements and to manage our interest expense.

Table of Contents

Market risk associated with our long-term fixed rate debt is the potential increase in fair value resulting from a decrease in interest rates. We use interest rate swap agreements that effectively convert a portion of our fixed-rate debt to a floating-rate basis to manage this risk. At June 30, 2016 and December 31, 2015, we maintained interest rate swap agreements on the following fixed-rate debt instruments:

Debt Instrument	Swap Notional as of June 30, 2016 (in thousands)	Maturity	Debt Fixed Rate	Swap Floating Rate: LIBOR plus	All-in Swap Floating Rate as of June 30, 2016
Oasis of the Seas term loan	$ 192,500	October 2021	5.41%	3.87%	4.78%
Unsecured senior notes	650,000	November 2022	5.25%	3.63%	4.26%
	$ 842,500				

These interest rate swap agreements are accounted for as fair value hedges.

Market risk associated with our long-term floating rate debt is the potential increase in interest expense from an increase in interest rates. We use interest rate swap agreements that effectively convert a portion of our floating-rate debt to a fixed-rate basis to manage this risk. At June 30, 2016 and December 31, 2015, we maintained interest rate swap agreements on the following floating-rate debt instruments:

Debt Instrument	Swap Notional as of June 30, 2016 (in thousands)	Maturity	Debt Floating Rate		All-in Swap Fixed Rate
Celebrity Reflection term loan	$463,604	October 2024	LIBOR plus	0.40%	2.85%
Quantum of the Seas term loan	643,125	October 2026	LIBOR plus	1.30%	3.74%
Anthem of the Seas term loan	664,583	April 2027	LIBOR plus	1.30%	3.86%
Ovation of the Seas term loan	830,000	April 2028	LIBOR plus	1.00%	3.16%
Harmony of the Seas term loan (1)	770,714	May 2028	EURIBOR plus	1.15%	2.26%
	$3,372,026				

(1) Interest rate swap agreements hedging the Euro-denominated term loan for Harmony of the Seas include swap EURIBOR zero-floors matching the hedged debt EURIBOR zero-floor. Amount presented is based on the exchange rate as of June 30, 2016.

These interest rate swap agreements are accounted for as cash flow hedges.

The notional amount of interest rate swap agreements related to outstanding debt and on our current unfunded financing arrangements as of June 30, 2016 and December 31, 2015 was $4.2 billion and $4.3 billion, respectively.

Foreign Currency Exchange Rate Risk

Derivative Instruments

Our primary exposure to foreign currency exchange rate risk relates to our ship construction contracts denominated in Euros, our foreign currency denominated debt and our international business operations. We enter into foreign currency forward contracts, collar options and cross currency swap agreements to manage portions of the exposure to movements in foreign currency exchange rates. As of June 30, 2016, the aggregate cost of our ships on firm order, not including the TUI Cruises' ships on order and those subject to conditions to effectiveness, was approximately $5.3 billion, of which we had deposited $151.5 million as of such date. At June 30, 2016 and December 31, 2015, approximately 65.1% and 58.2%, respectively, of the aggregate cost of the ships under construction was exposed to fluctuations in the Euro exchange rate. The majority of our foreign currency forward contracts, collar options and cross currency swap agreements are accounted for as cash flow, fair value or net investment hedges depending on the designation of the related hedge.

On a regular basis, we enter into foreign currency forward contracts and, from time to time, we utilize cross-currency swap agreements to minimize the volatility resulting from the remeasurement of net monetary assets and liabilities denominated in a currency other than our functional currency or the functional currencies of our foreign subsidiaries. During the second quarter of 2016, we maintained an average of approximately $532.6 million of these foreign currency forward contracts. These instruments are not designated as hedging instruments. Changes in the fair value of the foreign currency forward contracts resulted in a (loss) gain, of approximately $(24.7) million and $11.2 million during the quarters ended June 30, 2016 and June 30, 2015, respectively, and approximately $(9.3) million and $(16.9) million, during the six months ended June 30, 2016

Table of Contents

and June 30, 2015, respectively, that were recognized in earnings within Other income (expense) in our consolidated statements of comprehensive income (loss).

The notional amount of outstanding foreign exchange contracts including our forward contracts as of June 30, 2016 and December 31, 2015 was $1.0 billion and $2.4 billion, respectively.

Non-Derivative Instruments

We also address the exposure of our investments in foreign operations by denominating a portion of our debt in our subsidiaries' and investments' functional currencies and designating it as a hedge of these subsidiaries and investments. We had designated debt as a hedge of our net investments in TUI Cruises of approximately €260.8 million, or approximately $289.9 million, as of June 30, 2016.

Fuel Price Risk

Our exposure to market risk for changes in fuel prices relates primarily to the consumption of fuel on our ships. We use fuel swap agreements to mitigate the financial impact of fluctuations in fuel prices.

Our fuel swap agreements are accounted for as cash flow hedges. At June 30, 2016, we have hedged the variability in future cash flows for certain forecasted fuel transactions occurring through 2020. As of June 30, 2016 and December 31, 2015, we had the following outstanding fuel swap agreements:

	Fuel Swap Agreements	
	As of June 30, 2016	As of December 31, 2015
	(metric tons)	
2016	456,000	930,000
2017	854,000	854,000
2018	583,000	583,000
2019	458,000	231,000
2020	232,000	—

	Fuel Swap Agreements	
	As of June 30, 2016	As of December 31, 2015
	(% hedged)	
Projected fuel purchases:		
2016	64 %	65 %
2017	60 %	59 %
2018	40 %	40 %
2019	30 %	15 %
2020	15 %	—

At June 30, 2016 and December 31, 2015, $219.4 million and $321.0 million, respectively, of estimated unrealized net loss associated with our cash flow hedges pertaining to fuel swap agreements were expected to be reclassified to earnings from Accumulated other comprehensive loss within the next twelve months. Reclassification is expected to occur as the result of fuel consumption associated with our hedged forecasted fuel purchases.

Table of Contents

The fair value and line item caption of derivative instruments recorded within our consolidated balance sheets were as follows:

	Fair Value of Derivative Instruments					
	Asset Derivatives			Liability Derivatives		
	Balance Sheet Location	As of June 30, 2016 Fair Value	As of December 31, 2015 Fair Value	Balance Sheet Location	As of June 30, 2016 Fair Value	As of December 31, 2015 Fair Value
(In thousands)						
Derivatives designated as hedging instruments under ASC 815-20[1]						
Interest rate swaps	Other assets	$23,032	$ —	Other long-term liabilities	$164,060	$ 67,371
Foreign currency forward contracts	Derivative financial instruments	—	93,996	Derivative financial instruments	9,548	320,873
Foreign currency forward contracts	Other assets	—	—	Other long-term liabilities	17,488	—
Fuel swaps	Derivative financial instruments	—	—	Derivative financial instruments	211,973	307,475
Fuel swaps	Other assets	15,009	—	Other long-term liabilities	194,859	325,055
Total derivatives designated as hedging instruments under 815-20		38,041	93,996		597,928	1,020,774
Derivatives not designated as hedging instruments under ASC 815-20						
Foreign currency forward contracts	Derivative financial instruments	$—	$ 32,339	Derivative financial instruments	$—	$ —