Sabre Q4 and Full Year 2018 Earnings Call Prepared Remarks

February 12, 2019

Slide 1 – Q4 and Full Year 2018 Earnings Report

Good morning and welcome to the Sabre fourth quarter and full year 2018 earnings conference call. Please note that today's call is being recorded and is also being broadcast live on the Sabre corporate website. This broadcast is the property of Sabre. Any redistribution, retransmission or rebroadcast of this call in any form without the express written consent of the company is strictly prohibited. I will now turn the call over to the Senior Vice President of Investor Relations and Corporate Communications, Mr. Barry Sievert. Go ahead sir.

Slide 2 – Forward-looking statements

Barry Sievert, SVP Investor Relations and Corporate Communications:

Thank you, and good morning everyone. Thanks for joining us for our fourth quarter and full year earnings call.

This morning we issued an earnings press release, which is available on our website at investors.sabre.com.

A slide presentation, which accompanies today's prepared remarks, is also available during this call on the Sabre IR web page. A replay of today's call will be available on our website later this morning.

Throughout today's call, we will be presenting certain non-GAAP financial measures, which have been adjusted to exclude certain items. All references during today's call to EBITDA, EBITDA Less Capitalized Software Development, Operating Income, EPS and Net Income have been adjusted for these items. The most directly comparable GAAP measures and reconciliations for non-GAAP measures are available in the earnings release and other documents posted on our website at investors.sabre.com.

We would like to advise you that our comments contain forward-looking statements. These statements include, among others, disclosure of our guidance, including revenue, EBITDA, EBITDA Less Capitalized Software Development, operating income, net income, EPS, cash flow and CapEx; our medium term outlook; our expected segment results; the amount and effects of changes in capitalization mix and depreciation and amortization, the effects of new or renewed agreements, products and implementations; our expectations of industry trends; and various other forward-looking statements regarding our business.

These statements involve risks and uncertainties that may cause actual results to differ materially from the statements made on today's conference call.

Information concerning the risks and uncertainties that could affect our financial results is contained in our SEC filings, including our 2017 Form 10-K and our third quarter 2018 Form 10-Q.

Slide 3 – Today's presenters

Participating with me on today's call are Sean Menke, our President and Chief Executive Officer, and Doug Barnett, Executive Vice President and Chief Financial Officer.

Sean will start us off and provide a review of our strategic and commercial performance and outlook. Doug will offer additional perspective on our financial results and forward outlook. We will then open the call to your questions. With that, I will turn the call over to Sean.

Slide 4 – 2018: Continued Progress

Sean Menke, President and CEO:

Good morning everyone and thank you for joining us today.

2018 demonstrates steady continued progress on a strong foundation. Our commitment and execution to the strategy we laid out at the beginning of 2018 resulted in solid financial and operational performance, with high-single digit revenue growth, a 10% increase in EPS and 22% growth in Free Cash Flow.

We augmented our leadership team with skilled technology executives, evolved our go-to-market strategy and made strong progress on our technology evolution. This, along with continued evidence of momentum behind our strategic and commercial initiatives gives me confidence in our 2019 expectations, including driving a 10% increase in Free Cash Flow, growth that is in line with our Investor Day guidance, but off a higher 2018 base.

Before we get into the details, I would like to acknowledge my team members around the world with a sincere thank you. Their collective hard work and effort over the past year have been a major contributor to the progress we have made and make me confident about the future. Now, let's look at our performance for 2018:

Slide 5 – FY 2018 Financial Highlights

In 2018, we delivered strong full-year results well ahead of our original expectations coming into the year.

Our solid full year revenue growth was driven by two main factors:

- Strong growth in Travel Network driven by a supportive bookings environment, the completion of the Flight Centre migration, increased share at global travel agencies and conversions, including CWT and other new agencies. The investments we have made in the new Sabre Red 360, the official name for our new Sabre Red Workspace, and the cloud-deployment of our shopping complex are clearly paying off. We gained 120 basis points of global booking share, leading to full year bookings growth of 6.4%, ahead of our expected 4% - 6% coming into the year. Additionally, average booking fee growth was higher than anticipated coming into the year.

- We expect continued solid growth in the mid-single digits at Travel Network in 2019, despite expected modest slowing in the global travel economy.

- Airline Solutions growth also came in stronger than expected, with over 5% full year passengers boarded growth on a consistent carrier basis. Our progress in driving stronger product health and customer relationships led to a higher rate of renewals and new implementations than we factored into our initial expectations coming into 2018.

- One thing that I believe was underappreciated by investors is the concentrated renewal cycle that Airline Solutions went through in 2017 and 2018. We successfully renewed 94% of our total contract value up for renewal over the period. After emerging from this heavy renewal cycle, we have 75% of total Airline Solutions revenue through 2023 under contract. And, I am thrilled to report that this morning, we announced we have agreed to extend and expand our long-term alliance with JetBlue, one of Airline Solutions' largest customers. In addition to a PSS renewal, JetBlue will upgrade to the Sabre Commercial Platform that was announced in the second-half of 2018.

- As has been announced in the market, we did have three losses of SabreSonic customers, Pakistan, Bangkok and Philippine Airlines, that will impact the Airline Solutions growth rate in 2019. But looking ahead at 2019 and the medium term, our number of contracts up for renewal is much lower, while we believe one of our competitors will face a much heavier renewal cycle. This gives us the opportunity to shift from playing defense to playing offense. With the introduction of our new innovations in the Sabre Commercial Platform, we are excited about our prospects for winning and reinvigorating strong growth in Airline Solutions going forward.

- Although Hospitality Solutions revenue growth was a bit lower than originally expected, the recurring SynXis Software and Services revenue growth was in the very high-single digits. Furthermore, Hospitality Solutions had its best sales year ever, with particular strength over the back half of the year, providing a healthy foundation for the years ahead. We expect 2019 to be a strong year for the core Hospitality business, with reported growth expected to be between 7% and 9%. We expect double digit growth from new and most of our existing customers, however, a few of our larger customers are in the process of being acquired by larger hoteliers, which we expect to dampen reported growth for the year.

And, in what I consider a key metric, Free Cash Flow, we delivered $441 million in 2018, up 22% year-over-year and well ahead of initial expectations. We expect continued strong growth of approximately 10% in Free Cash Flow in 2019 as we continue to gain scale in our investments.

Slide 6 – 2019 Expectations

In 2019, we expect continued solid growth in the metrics that are key to our investors, with expectations for mid-single digit revenue growth, and Free Cash Flow growth of about 10% to approximately $485 million. And as Doug will discuss in a moment, our underlying expectations for the business are largely consistent with the medium-term guidance we gave in March of 2018, off the higher base of our 2018 results.

We've made tremendous progress against our technology initiatives in 2018. In 2019, we expect total technology expense growth to begin to moderate. However, under new technology leadership, we are making great progress and refining our technology roadmap to help drive accelerated results. This progression in the business, particularly as it relates to the sequencing of our continued cloud migration and mainframe offload, and our transition to full adoption and maturity of agile development methods, is expected to drive a meaningful reduction in the percentage in technology spend that is capitalized in 2019.

There are four key points to keep in mind about this mix shift:

1. First, we are making great progress against our technology initiatives. Efficiencies we are gaining are allowing increased investment in the migration, platform development and innovation, even as our expectations for total technology spend growth over the medium term have been reduced from the 3%-4% discussed at last year's investor day, to expected 1% growth over the medium term going forward.

2. Second, this shift will have a significant impact on our near-term reported earnings as our P&L is temporarily burdened by both the increased portion of technology spend that is expensed in current periods, and the depreciation and amortization from previous capitalization.

3. Third, over the medium term, we expect this shift to a lower level of capitalization of total technology costs to remain relatively stable to 2019 levels. However, we expect depreciation and amortization to decline significantly over the next few years and for earnings to roughly normalize to previous expectations by 2021.

4. Fourth, our technology transformation is already driving greater efficiency, stability, security and flexibility. We expect that benefits will continue to accrue over the coming years, resulting in a further enhanced competitive position and efficiency that will allow us to rotate increasing investment into innovation to drive stronger growth in the years ahead.

Doug will provide more detail in a moment, but you need to remember this shift in capitalization mix itself has no impact on our expectations for total technology spend. And, importantly, it has zero impact on a key metric – Free Cash Flow.

Slide 7 – Hybrid cloud infrastructure footprint – 2018

As I mentioned, we are making great progress on our technology initiatives.

Our cloud migration is going well. We are already seeing significant benefits from the work that has been completed. We continue to expect to complete our transition to a cloud-first infrastructure by the end of 2023, with significant performance, stability and efficiency benefits that are expected to continue to accumulate as the transition work continues.

Already in 2018, we:

- Signed strategic agreements with AWS and Microsoft Azure.
- Established cloud landing zones across North America, Europe and Asia-Pacific.
- Began consolidating smaller legacy data centers around the globe.
- Built automation tools for deploying cloud infrastructure.
- Increased the percentage of our total open systems footprint by 1.6 points. Over 89% of all processing power is now on open systems versus less than 11% on the mainframe.
- Within our open systems footprint, we migrated important open systems applications to the cloud that increased our open systems cloud footprint by 19 percentage points. Over 50% of our open systems processing power is now in the cloud.
- Two years ago, our shopping complex was entirely hosted in our Tulsa data center.

- We now have deployed our shopping complex to a multi-site configuration leveraging public and private cloud environments.
- And most recently, for a 24-hour period, we successfully completed a test to shift our shopping complex to operate entirely in the cloud.
- As a result of our initiatives, our hosting costs were 6% lower in 2018 than they otherwise would have been under our historical infrastructure, even as total compute volumes increased over 30%. In 2019, we expect continued growth in compute volumes, but even greater savings, with hosting costs 10% lower than they would have been under our historical infrastructure. As a reminder, we expect $100 million of annual cost benefit beginning in 2024, concurrent with the expiration of our DXC contract. And based on the progress I have described, we have even greater confidence in reaching that objective.
- Let me put in simple terms why we feel good about where our technology investment is going. If you look at our compute cost today, it's roughly half a billion dollars. About 40% of that is mainframe, even though the mainframe is only 11% of our total compute power.
- There is a clear path to cost savings, which is why we are so focused on accelerating the completion of our technology evolution.

Included among the list of applications that are now running in production in the cloud, are:

- Shopping and schedule updater.
- Sabre Red 360 for some of our largest customers,
- AirCentre and AirVision products, including Digital Experience and Check-in, Revenue Optimizer, Dynamic Availability, Planning and Scheduling and Distributed Availability, and
- All Hospitality solutions including the new SynXis Property Hub and SynXis Booking Engine.

In addition to cost benefits, shifting our applications and platform to the cloud brings processing closer to customers, reducing response times.

Cloud migration also increases our security and leading system stability. In 2018, we saw zero major stability incidents, compared to five in 2017. We also saw more than a 30% reduction across all other stability incidents and our average time to recovery was significantly reduced, which has also reduced our Service Level Agreement, or SLA, payments significantly.

Slide 8 – Hybrid cloud infrastructure footprint – 2019

We fully expect continued improvements in these metrics in 2019 and the years ahead as we continue to mature our global cloud footprint and get into some of the 'heavier lifting' of our mainframe offload efforts around ticketing, PNR and check-in.

With that, I'll turn the call over to Doug to get into more of the financial details and expectations going forward.

Slide 9 – Q4‘18 Financial highlights

Doug Barnett, Chief Financial Officer:

Turning to the Q4 results:

- Revenue growth was solid, up 5% year-over-year.
  Over the period, recurring revenue represented 93% of total revenue, versus 95% in the prior year.

- EBITDA grew 4%, reflecting revenue growth and lower Corporate costs, partially offset by increased Travel Network incentives,

- Operating income increased 2% year-over-year, which includes an $8 million increase in depreciation and amortization,

- Earnings per share increased 6%, driven by operating income growth and a lower tax rate due to the impact of U.S. tax reform,

And as expected, in the quarter, Free Cash Flow declined 26% to $110 million due to working capital timing. Full year Free Cash Flow of $441 million represents growth of 22%, and was more than $50 million above our initial expectations of approximately $390 million for the year.

Slide 10 – Q4 & FY’18 Travel Network

Looking a bit closer at Travel Network in Q4, total revenue growth of 7.5% supported an increase in operating income of 2% for the quarter.

Bookings grew 4% in the quarter, and average booking fee increased 3% in the quarter. About half of the average booking fee growth was driven by the net positive impact from customer pricing at specific carriers experimenting with different distribution strategies in Europe.

Travel Network operating margin decline of 130 basis points in the quarter was driven by:

- 3 points of margin decline from incentive fee growth, and
- Approximately 150 basis points of negative impact from higher technology operating expenses, all due to lower third-party service credits,
- Partially offset by a 2 point benefit from the increase in average booking fee and
- A 1 point benefit from headcount-related and other expense leverage from cost savings initiatives.

Taking a closer look at incentive fee growth in the quarter:

- About half of the increase was from new commercial deals and agency conversions, and
- Half was due to normal incentive growth consistent with historic growth in the low-to-mid single digits, including the impact of agency consolidation.

For the full year, Travel Network revenue increased 10% to reach $2.8 billion.

Full year operating margin of 26.9% was a bit below the prior year, reflecting incentive growth and lower third-party service credits. As previously mentioned, we expect incentive fee growth to revert to historical, normal growth rates in the low-to-mid single digits beginning in the second quarter of 2019.

Slide 11 – Total bookings

Total bookings increased more than 4% in the quarter, a bit of a slowdown versus prior quarters as we started to anniversary the positive year-over-year impact of the Flight Centre migration. Our geographic mix and strong share gain, driven by increased share at large travel management companies, including the implementation of our strategic agreement with CWT, and other new agency conversions more than offset the deceleration in overall market growth driven by macro-economic factors impacting EMEA and Latin America.

Within our total bookings, air bookings grew 5% and lodging, ground and sea bookings grew 1%. Within Lodging, ground and sea, higher value hotel bookings grew double digits, partially offset by a decline in lower margin rail bookings.

Full year bookings growth of over 6% was driven by a supportive macro environment and global share gain.

Slide 12 – Total Q4 & FY'18 bookings growth by region

Q4 bookings growth was supported by an increase of 9% in Asia-Pacific, driven by agency conversions and solid market growth. This was a bit slower than previous quarters as we started to anniversary the positive year-over-year impact of the Flight Centre migration.

Bookings increased 6% in North America, driven by increased share at large, global travel management companies, including our expanded strategic agreement with CWT. EMEA bookings grew faster than the market at 2%. Bookings declined in Latin America due to unfavorable macro-economic factors in the region.

In total, global booking share increased 110 basis points in the fourth quarter to 37.1%. Full year global share reached 37.5%, an increase of 120 basis points.

Slide 13 – Q4 & FY'18 Airline Solutions

At Airline Solutions, revenue declined as expected due to the negative impact related to the adoption of ASC 606. The net impact of adopting ASC 606 drove a $7 million decrease in revenue in the quarter, net of upfront revenue recognition from new license fee implementations and renewals. Excluding this impact, revenue increased 2% in the quarter.

SabreSonic revenue declined 1% in the quarter, with the completion of the SabreSonic implementation at LATAM in Q2 and consistent carrier growth offset by a modest decline in SabreSonic PB rate.

AirVision and AirCentre declined mid-single digits in the quarter due to the impact of ASC 606, and professional services revenue increased in the quarter.

The decline in Airline Solutions' operating income includes the negative impact of:

- ASC 606, and
- lower third-party service credits.

Excluding the impacts of ASC 606 and lower third-party service credits, operating margin declined 100 basis points in the quarter.

Full year Airline Solutions revenue growth of 1% exceeded our expectations coming into the year for revenue to decline mid-single digits. We more than offset large headwinds from the Southwest Airlines de-migration in mid-2017 and ASC 606 adoption with organic growth, new implementations and renewals. Excluding the impacts of Southwest Airlines and ASC 606, full year revenue increased more than 5%.

As expected, the full year Airline Solutions operating income and margin decline includes the negative impacts of:

- the Southwest de-migration,
- ASC 606,and
- the decrease in third-party service credits.

Excluding the impacts of ASC 606 and the decline in third-party service credits, operating income growth was 10%, and operating margin increased 90 basis points.

Slide 14 – Total passengers boarded

Passengers boarded increased more than 6% in the quarter. On a consistent carrier basis, passengers boarded increased 3%, a deceleration versus historic growth rates due to a year-over-year decline at a large carrier in Asia-Pacific. If this particular carrier had continued to grow at first half growth rates, total PB growth would have been 10% and PB growth on a consistent carrier basis would have been 7% in the quarter.

Full year passengers boarded increased 8% excluding the impact of Southwest Airlines, reflecting 5% consistent carrier growth and the completion of the SabreSonic implementation at LATAM in Q2.

Slide 15 – Q4 & FY'18 Hospitality Solutions

At Hospitality Solutions, Q4 SynXis software and services revenue increased 8%, while digital marketing services revenue declined $2 million in the quarter, driving overall revenue growth of 4%.

Hospitality Solutions operating margins expanded 30 basis points in the quarter due to the mix-shift toward higher margin recurring revenue and cost reduction initiatives, partially offset by a 10% increase in D&A.

Full year SynXis software and services revenue increased 11%, and although digital marketing services revenue declined, the mix shift toward higher margin recurring revenue and cost reduction initiatives drove 33% growth in full year operating income.

Slide 16 – Q4’18 Technology expenditures

In Q4 2018, total technology spend was $243 million. As a reminder, this includes the costs that we incur, whether capitalized or expensed, for hosting, third-party software and R&D.

Total technology spend was up 3% in the quarter. This increase was due to $10 million lower third-party hosting service provider credits in Q4 2018 versus 2017.

The amount of total technology expense running through our income statement in Q4’18 went up by $2 million, or 1%. Remember, this refers to our total technology spend less capitalized software development, plus amortization of previous capitalization.

Although total technology expense running through our P&L increased only modestly at the total Sabre level in the quarter, more pressure was felt in the individual business unit segments with a substantial offset at the Corporate line due to investment project mix.

Slide 17 – FY‘18 Technology expenditures

For the full year, total technology spend increased 6%.

As a reminder, our third-party hosting service provider credits, which are related to hitting volume minimums, stepped down from $58 million in 2017 to approximately $15 million in 2018 and go away in 2019. Therefore, about 75% of the year-over-year increase in total technology spend was due to these lower service credits. These service provider credits impact both EBITDA and Free Cash Flow. Excluding the decline in third-party service credits, total technology spend increased 2%, much lower than revenue growth of 7.5%.

As we have mentioned on previous earnings calls, the costs supporting our cloud migration are not capitalized. This, along with a shift in development mix, resulted in a 260 basis point decline in capitalization mix for the full year, and year-over-year, there was a $9 million decline in capitalized software development. Although neutral to Free Cash Flow, this shift impacts operating income and EBITDA and is what we have been discussing all year, referred to as the CapEx/OpEx rotation.

Finally, the increase in amortization of previous capitalization resulted in a $36 million headwind to 2018 operating income. This of course is neutral to both EBITDA and Free Cash Flow.

Excluding the third-party hosting service provider credits, the decline in capitalization mix, and the increase in amortization, full year operating margin would have increased 100 basis points from 18% in 2017 to 19% in 2018.

Slide 18 – Q4 & FY’18 Net debt, leverage and cash flow

Full year Free Cash Flow generation of $441 million was ahead of expectations and represents growth of 22% year-over-year.

Our cash flow supported the continued strengthening of our balance sheet, with leverage declining to 2.6 times as of year end.

We repurchased 1.1 million shares under our share repurchase authorization in 2018 for approximately $26 million in aggregate. Including dividends, we returned $180 million to shareholders in 2018.

We have $365 million remaining under our share repurchase authorization. As we have said, we expect to repurchase enough shares to offset dilution from equity plans, while maintaining flexibility to be opportunistic beyond that.

Slide 19 – FY 2019 Guidance before impact of lower capitalization mix and increased depreciation & amortization

Let's level set and review the medium-term guidance provided at our Investor Day in March last year:

- Mid-to-high single digit revenue growth, with Travel Network and Airline Solutions growing in line with or above global travel growth, or about mid-single digits, and double-digit growth in Hospitality solutions,
- Relatively stable operating margin,
- 10% EPS growth over the medium term, with mid-to-high single digit EPS growth specifically in 2019, and
- Free Cash Flow growth of 10%.

So how are we tracking against that in 2019? Largely in line with expectations, excluding the impact of the lower capitalization mix and an increase in depreciation and amortization that I will explain shortly.

Off a higher base year than we anticipated last March given our strong 2018 performance, in 2019, before these impacts, we expect:

- Total Sabre revenue growth of 4% to 6%, to $4.005 billion to $4.085 billion,
- EBITDA growth of 2% to 6% to $1.150 billion, to $1.190 billion,
- Operating income growth of 2% to 8%, to $715 million to $755 million,
- Net income growth of 1% to 10%, to $430 million to $470 million,
- EPS growth of 1% to 10%, to $1.56 to $1.70, and
- Free Cash Flow growth of 10% to approximately $485 million.

Taking a closer look at the segment level:

- At Travel Network, we expect full year 2019 revenue growth of 4% to 6%, driven by bookings growth of the same amount. Although we expect recent booking fee trends to continue through Q1, we expect full year booking fee to be roughly flat as we fully anniversary both the favorable mix impact of the Flight Centre conversion and favorable pricing at specific carriers in EMEA beginning in Q2. We expect incentive fee growth to normalize to historical growth rates in the low-to-mid single digits beginning in Q2.

- At Airline Solutions, as you know and has been announced, growth in 2019 will be impacted by the attrition of certain PSS customers. The de-migration of Pakistan, Bangkok and Philippine Airlines is expected to reduce our full year 2019 revenue growth by approximately $30 million, and because of this, we expect full year revenue growth of 1% to 3%. Excluding the impact of customer attrition, expected revenue growth would have been 5% to 7%, in line with or better than Investor Day expectations. As Sean mentioned, we have successfully navigated a very significant renewal cycle with our existing Airline Solutions customers, which gives us confidence in 2019 and the medium term.

- At Hospitality Solutions, we expect 7% to 9% revenue growth for full year 2019. Hospitality Solutions had its strongest sales year ever in 2018. However, the impact of customer consolidation in the Hospitality space is expected to reduce our full year 2019 revenue by $10 million as the acquired brands are migrated onto the larger hoteliers' existing technology platforms. Excluding this impact, the core business is expected to grow 11% to 13%, in line with Investor Day expectations.

So, as we look at 2019, we believe our business is solid and in line with our prior guidance.

Slide 20 – Estimated impact of certain items on 2019 expectations

Now, I want to take a moment to explain two items that will impact our reported 2019 earnings.

First, we are taking significant steps in our technology evolution in 2019 and as a result, expect the capitalized portion of our total technology spend to be lower.

- As we have stated on the past several earnings calls, the costs supporting our cloud migration are not capitalized under GAAP. This, combined with the acceleration of our mainframe offload and our transition to full adoption and maturity of agile development methods, is expected to reduce the percentage of technology spend that is capitalized in 2019 with an equal and offsetting increase in the percent of technology spend that is expensed as incurred.

- The important thing is to remember this change in capitalization mix has no impact to Free Cash Flow. Additionally, it has no impact on total technology spend dollars, which we expect to grow in line with our previous expectations of 3% to 4%, slower than revenue, in 2019 as we continue to gain scale. One percentage point of this cost growth is driven by the contractual decline in third-party hosting service provider credits from $15 million in 2018 to zero in 2019. We are committed to continuing to report and provide clarity into our total technology spend, just like we have these past two quarters.

- The capitalization mix of our total technology spend in 2018 was 26%, and we expect the capitalization mix to decrease to approximately 9-10% in 2019. We estimate that this will result in approximately $175 million more of our technology spend being expensed immediately, with a corresponding $175 million reduction in CapEx. This capitalization mix change is expected to reduce our full year 2019 EPS by $0.51.

Second, as we accelerate our technology evolution, more products have been placed into service than anticipated in the medium-term guidance we issued last March. We now expect a $25 million increase related to the accelerated frequency of products placed into service as new leadership and methods have increased our innovation velocity versus our previous expectations for 2019. This is expected to result in an EPS reduction of $0.07 versus our previous 2019 expectations.

So, in total, the impact of the capitalization mix change and increased D&A are expected to reduce our full year EPS by $0.58 versus our 2019 expectations from a year ago. To reiterate, there is no impact to Free Cash Flow.

The estimated quarterly impact of these items in 2019 is included in the appendix of today's presentation, which is available on our website.

Slide 21 – Adjusted EBITDA Less Capitalized Software Development

Because of this reduction in capitalization mix, and in order to have a comparable earnings measure year-over-year, we are introducing a new metric: EBITDA Less Capitalized Software Development.

We believe EBITDA Less Capitalized Software Development is a useful metric to analyze the underlying operational performance of our business because it reflects total development spend as does not benefit from the amount that is capitalized. It normalizes for the impact of changes in capitalization mix across periods for better comparability. We will provide this metric in our quarterly reporting in 2019.

Slide 22 – FY 2019 Guidance

As I just explained, in 2019, we estimate the change in capitalization mix and increase in depreciation and amortization will negatively impact our reported results as follows:

- Lower EBITDA by $175 million,
- Lower CapEx also by $175 million,
- Lower Operating income by $200 million, and
- Lower EPS by $0.58.

Our 2019 guidance inclusive of the shift in capitalization mix and increased depreciation and amortization expense, which is how we expect to talk about our 2019 financial results, is the following:

- Revenue, EBITDA Less Capitalized Software Development and Free Cash Flow are consistent with my previous comments, as the capitalization mix change and increased D&A have no impact on these metrics,
- EBITDA of $975 million to $1.015 billion,
- Operating income of $515 million to $555 million,
- Net income of $270 million to $310 million, and
- EPS of $0.98 to $1.12.

This guidance incorporates expectations for approximately $460 million of depreciation and amortization, $170 million in interest expense, a tax rate of approximately 20%, flat share count at 278 million shares and total CapEx of $130 million to $150 million in 2019.

Slide 23 – Normalization by 2021: Lower capitalization mix and D&A impact expected to normalize by 2021

What does this mean for the medium term from 2019 through 2022? For the core business, nothing has changed. Our revenue growth expectations are the same, and our expectations for Free Cash Flow are the same or better.

There is obviously a near term P&L impact from the shift to less capitalization and increased expensed R&D over the period, but this effect is transitory as D&A from previous capitalization quickly burns down. We expect our capitalization mix to remain relatively consistent with 2019 levels over the medium term and expect Depreciation and Amortization to decline by $150 million between 2019 and 2022, helping to drive a full recovery of Operating Income and EPS to previously expected levels by 2021. We currently expect D&A to total approximately $460 million, $420 million, $340 million and

$310 million for each year from 2019 through 2022.

Slide 24 – Updated medium term outlook

Looking at a consolidated view of our updated medium-term guidance metrics compared with what we said last March at our Investor Day, we continue to expect a mid-to-high single digit revenue CAGR over the 2019 through 2022 medium term period.

Our cloud migration, mainframe offload and rapid adoption of agile development methods are expected to deliver significant efficiencies and lower our compute costs. As a result of the benefits we expect from these efforts and the work being done in 2019, we now expect even better efficiencies than at Investor Day last year, although from the 2019 base. We now expect total technology spend growth of 1% over the medium term. This is better than our previous expectations for medium-term total technology spend growth of 3% to 4%.

The amount of technology expense hitting the income statement, which includes amortization of previous capitalization, was 27% of revenue in 2018. We expect this to step up to about 31% in 2019 and then rapidly decline to the low 20%'s over the medium term.

You can see this reflected in our expectations for EBITDA Less Capitalized Software Development growth, which we expect to accelerate to high single-digit CAGR over the medium term.

Our previous expectations were for roughly stable operating margins and for operating income to grow relatively in line with revenue growth over the medium term. Although we expect operating margin to dip in 2019, from this base, we expect operating margin to expand significantly over the medium term off the new 2019 base as we gain leverage in total technology spend and depreciation and amortization declines. By 2021, we expect full operating margin recovery to our previous Investor Day expectations, with continued margin expansion into 2022. Accordingly, we now expect 20% - 25% compound annual growth in operating income from 2019 through 2022.

Moving down the income statement, as mentioned, we also expect full EPS recovery by 2021. This incorporates expectations for 25% - 30% medium-term EPS growth off the lower 2019 base.

Getting to the metric that I think matters most: we now expect low double-digit growth in Free Cash Flow off of a 2019 base of approximately $485 million. This reflects solid revenue growth and the leverage we are gaining in total technology spend. This is better than previous Investor Day expectations for 10% growth.

As a reminder, we expect to become a full U.S. cash tax payer in 2020, resulting in approximately $40 to $50 million of additional cash taxes over 2019 and, as a result, we expect more modest growth in Free Cash Flow in 2020. In terms of the Tax Receivable Agreement, or TRA, we now expect to put it behind us a year earlier than expected at Investor Day. Due to changes driven by US tax reform, we expect to pay out the remaining balance under the TRA in 2020. Back to you, Sean.

Slide 25 – Thank you

<u>Sean Menke, President and CEO:</u>

Strong full year results prove we're progressing well against our strategy. Continued evidence of momentum behind our strategic and commercial initiatives gives me confidence in our 2019 and medium-term expectations.

I look forward to continuing to share our progress over the quarters to come.

I want to once again thank you for joining our call today and for your continued interest in Sabre. With that I will ask the operator to open the call for your questions.