transat

2005 Annual Report

Transat A.T. Inc.

Tour Operators
Distribution Networks
Air Transportation
Accommodation
Destination Services

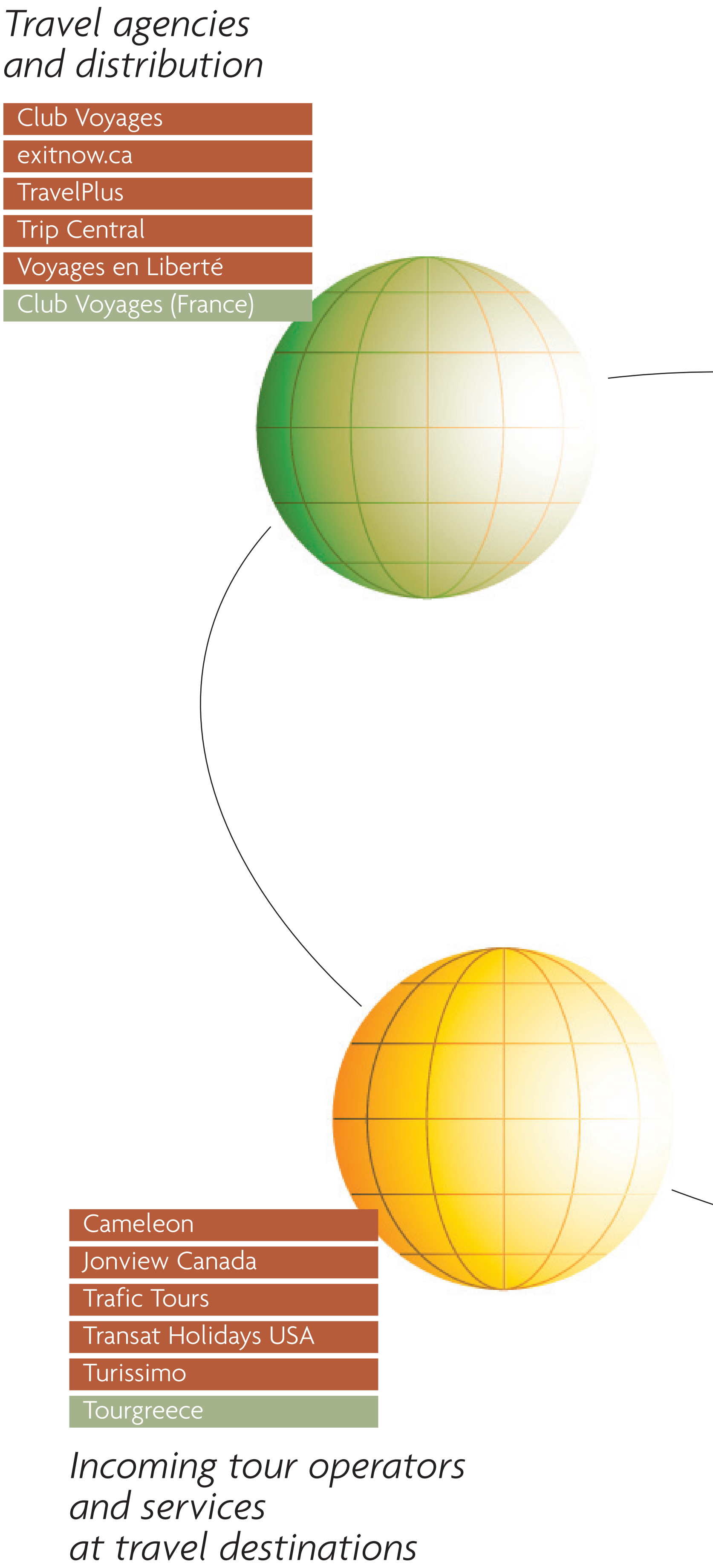
Highlights

- Transat A.T. Inc. recorded revenues of $2.4 billion and net earnings of $55.4 million in fiscal 2005, compared with $2.2 billion and $72.3 million respectively last year, amid exceptionally high fuel prices and intense competition.
- In Canada, we implemented a new product marketing strategy for our tour operator Nolitours with a view to increasing our market share and strengthening our margins, particularly in Ontario.
- We acquired a majority stake in Travel Superstore Inc. (Trip Central), based in Hamilton, Ontario. This company runs a travel agency network and operates the tripcentral.ca Web site.
- We renewed our agreement with Canadian airline WestJet until October 31, 2007, and sold our minority stake in Europe's Star Airlines.
- In Europe, we acquired outgoing French tour operator Bennett Voyages, which specializes in packages and tours to Scandinavia, the United Kingdom and Ireland. We also acquired 20 Carlson Wagonlit Travel agencies in France, in addition to a majority stake in Air Consultants Europe (ACE). Based in The Hague, ACE is Air Transat's sole commercial representative in Germany, the Netherlands and Belgium.
- As part of amendments to Transat's capital structure, the Company's common shares were replaced by two new classes of shares: Class A Variable Voting Shares (held by non-Canadians) and Class B Voting Shares (held by Canadians).
- We adopted a three-year strategic plan focused on growth and margin improvements.

[in thousands of dollars except amounts per share]	2005	2004
Revenues	2,364,481	2,199,822
Net income	55,416	72,320
Diluted earnings per share	1.33	1.76
Cash and cash equivalents	293,495	310,875
Cash flows relating to operating activities	63,785	185,100

Transat A.T. Inc. is an integrated company specializing in the organization, marketing and distribution of holiday travel. The core of its business consists of tour operators in North America and Europe. Transat is also involved in air transportation and value-added services at travel destinations. Finally, Transat has secured a dynamic presence in distribution through traditional and online travel agency networks.

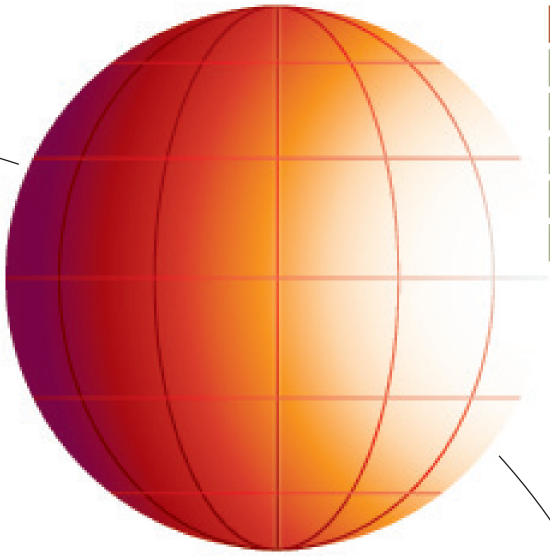
Above all, Transat has a dedicated team of thorough and efficient people who deliver quality vacation travel services at affordable prices to a broad clientele. Already recognized as a leader in Canada, Transat seeks to maintain its position as a major player in the holiday travel industry in North America and Europe by continuing to make travellers its number one priority.



Our organization

Outgoing tour operators

- Kilomètre Voyages
- Nolitours
- Rêvatours
- Vacances Transat
- Air Consultants Europe
- Bennett Voyages
- Brok'Air
- Look Voyages
- Vacances Transat (France)



Air transportation

- Air Transat
- Handlex

North America

Europe

Message to Shareholders

Jean-Marc Eustache

Chairman of the Board,
President and Chief Executive Officer

Poised for growth

International tourism continued to expand in 2005 following an excellent year in 2004. Despite the natural disasters and conflicts that made headlines, tourism continued its pattern of robust growth. Indeed, the future looks bright for businesses able to adapt to new market and industry trends.

In the tourism industry, company flexibility is quickly becoming a decisive factor. Although growth is relatively steady, the shift in travel destinations will inevitably gather pace. For many years, a handful of destination countries accounted for the lion's share of international tourism, stemming mainly from no more than a dozen issuing countries. This is no longer the case. Thanks to globalization, growth is increasingly driven by new issuing markets, especially in Asia and Latin America, as hundreds of destinations promising unique experiences compete head-to-head for tourist dollars.

Moreover, we have seen just how volatile the market can be. In 2003, the SARS crisis disrupted the summer season, particularly in Asia and Canada. On December 26, 2004, a tsunami swept the Indian Ocean. In summer 2005, a series of hurricanes struck the Caribbean and the Gulf of Mexico, and London was the site of terrorist attacks. In the fall, France was rocked by successive nights of rioting. These dramatic events posed significant challenges to the tourism industry, and not only because of their immediate consequences.

Lastly, 2005 will be remembered for the unprecedented surge in fuel prices. Although the impact on tourism demand cannot be quantified, spiralling fuel costs negatively affected the financial performance of many companies, including Transat.

→ Canada: a booming market

In Canada, we implemented a new strategy to enhance our market share and boost our margins, particularly in Ontario. This initiative led to changes in our distribution system and in product marketing activities at Nolitours (known until recently as World of Vacations/Nolitour), our tour operator subsidiary. We consequently revised our pricing approach, renegotiated agreements with travel agents and conducted a communications and marketing campaign to support the launch of the Nolitours brand as a symbol of quality at reasonable prices. At the same time, our Transat Holidays subsidiary, Canada's leading tour operator, is focusing on its product line, primarily package stays at exclusive hotels.

Given the challenges of Canada's geography and in recognition of the pivotal importance of fine tuning supply and demand, we opted to renew our agreement with WestJet until October 31, 2007; we have been leasing narrow-bodied aircraft from this carrier since 2003. This mutually beneficial partnership also serves the interest of our customers since it gives us the flexibility we need to offer competitively priced flights from some 15 Canadian cities.

For our wide-bodied requirements, we rely on the 14 Airbus jets operated by our subsidiary Air Transat. The late 2004 transfer of flights, facilities and operations from Montréal–Mirabel Airport to Montréal–Trudeau Airport in Dorval was carried out smoothly. In addition, thanks to assets such as its all-Airbus fleet, rigorous cost controls, high-quality product line and well-oiled organization, Air Transat is well positioned to fulfill its strategic role effectively, even in a turbulent environment.

While our operations focus on winter sun destinations, and therefore, mainly on vacation packages, we are also targeting tourist traffic between Canada and Europe in the summer months, when our customers are primarily seeking air carrier service. Once again, the summer season saw very intense competition, particularly in Ontario and on routes between Canada and the U.K. As a result, margins were down significantly. Market fragmentation in Ontario and the price war caused by oversupply prompted us to coordinate our efforts to achieve our high-priority goal of strengthening our presence in this market. Furthermore, we are striving to develop the summer package segment for European destinations, which remains less margin-sensitive.

We have acquired a majority ownership interest in Travel Superstore Inc., which is based in Hamilton, Ontario and operates travel agencies and the tripcentral.ca Web site. Travel Superstore has developed a new and dynamic marketing approach, combining the power of the Internet with a call centre and a travel advisor network. Expanding our distribution channels is part of Transat's vertical integration strategy and will provide us with additional tools to broaden our presence in Ontario.

We remain the largest incoming tour operator in Canada thanks to our subsidiary Jonview Canada, which has built an exceptional network of tourist industry partners for which it provides product distribution services abroad via outgoing tour operators. In this area, we have a solid presence in Europe and have begun positioning ourselves in the up-and-coming Latin American and Asian markets.

Synergies between our incoming and outgoing markets underpin our transatlantic platform, enabling us to serve a diversified customer base, maximize our capacity (particularly air traffic) and fully capitalize on market cycles. In this respect, Air Transat plays a pivotal role: in the summer months, it directly serves some 30 European destinations in nine countries, including several as a regular carrier.

Europe: Look Voyages on the right track

Every year, European travellers take approximately 400 million foreign trips. Although they often visit another European country, the popularity of the long-haul segment, which is of greater interest to us, is on the rise.

While it lags other regions in terms of market growth, continental Europe remains attractive due to its size and economic potential. Accordingly, Transat continues to strengthen its presence in Europe, as an outgoing tour operator via Vacances Transat (France), Look Voyages and, more recently, Bennett Voyages, as an incoming tour operator in Canada and Greece and as an air carrier on numerous transatlantic routes, particularly flights originating in France and the U.K. and serving several Canadian destinations.

In France, the turnaround of Look Voyages is proceeding according to the three-part plan we announced in July 2004. We have abandoned the air-only market—which explains the decline in our total air travellers—to focus on our specialty: holiday packages. In this respect, Look Voyages has built its offering around well-known products such as Clubs Lookéa. In addition, we are making greater use of Internet technologies to drive consumer and travel agency sales.

Our decision to sell our minority interest in Star Airlines generated a gain for shareholders. We have entered into business agreements with various carriers to meet our air transportation needs and will continue to do so as needed.

Concurrently, Transat acquired Bennett Voyages, an outgoing tour operator specialized in packages and tours to Scandinavia, the U.K. and Ireland. In early fiscal 2006, we also acquired 20 travel agencies of the Carlson Wagonlit Travel network. At the beginning of the year, we acquired a majority ownership interest in Air Consultants Europe, a company based in The Hague and Air Transat's exclusive business representative in Germany, the Netherlands and Belgium. These acquisitions have enhanced our European network in terms of supply and distribution capacity.

2005 results

Transat's revenues for the 2004-2005 winter season totalled $1.3 billion, up slightly compared with the previous year, while margins declined 17% to $80.0 million. Although travel volume was normal, our margins were slimmer due to the competitive pricing environment, particularly in Ontario, and higher fuel costs. Our summer revenues totalled $1.0 billion, yielding margins of $40.6 million, 40% lower than in 2004. In addition to the impact of fuel prices, our summer results were affected by heightened competition on routes between Canada and the U.K.

For the year as a whole, we posted total revenues of $2.4 billion and margins of $120.6 million. Net income stood at $55.4 million, or $1.43 per share, compared with $72.3 million ($2.07 per share) in 2004. Organizational changes, the reorganization of Air Transat's fleet and the cost reduction program implemented over the past few years significantly offset the negative impact of certain market conditions. Given the serious challenges we faced, we are relatively satisfied with our performance.

(from left to right)

H. Clifford Hatch Jr.
Lina De Cesare
Benoît Deschamps
Jean-Marc Eustache
Jean Guertin
Jacques Simoneau
John D. Thompson
Philippe Sureau
André Bisson, O.C.
Dennis Wood, O.C.
and
John P. Cashman
(not pictured)

Board of Directors

"At year-end, we finalized a three-year strategic plan that focuses on growth and profitability. We are increasingly turning to international tourism to enhance our development, particularly in North America and Europe."

New strategic plan

At year-end, we finalized a three-year strategic plan that focuses on growth and profitability. We are increasingly turning to international tourism to enhance our development, particularly in North America and Europe. To this end, we will be making additional acquisitions, while maintaining a brisk pace of internal growth. Our key strategic priorities are as follows:

- **In Canada, Transat is the leader in all regions except Ontario. We plan to bolster our presence in Ontario by adding new destinations and expanding our distribution network to become the market leader in all regions of the country.**

- **In Europe, Transat intends to grow its market share and continue its vertical integration in France and the U.K., building on its strong presence in these two high-potential markets. Transat will also continue its initiatives to expand into other European countries as a tour operator specializing in travel to Canada, among other destinations.**

- **Elsewhere, Transat will strive to invest in new markets and, in particular, to become a tour operator in the U.S., a strategic market it has been prospecting for some time. In addition, Transat will continue studying the possibility of penetrating other markets, such as Asia and Latin America.**

- **Transat wishes to step up development of destination services and to assume a portion of its accommodation needs in order to gain better control over capacity and product quality and to boost margins. In practical terms, this may mean pursuing stakes or acquisitions in the hotel industry. Markets in which Transat has already reached critical mass will be reviewed first.**

- **In light of rapid change in the distribution industry and travellers' expectations, and given the importance of organizational responsiveness and productivity, our strategic plan will include our ongoing technology and training initiatives and investments. To this end, Transat will strive to introduce cutting-edge solutions via agencies and direct sales in order to adapt to new markets and to continue efficiency enhancements.**

Transat estimates that implementing its strategic plan will require up to $300 million over three years, with funding from existing cash resources, future cash flows and external sources, as needed.

Capital structure: a transitional year

We maintained a solid financial position throughout 2005. Our net debt decreased by 24.8% and Transat currently enjoys an excellent financial position, with cash resources of $293.5 million as at October 31, 2005. Near year-end, following an in-depth analysis of our business environment and expected market conditions for 2006 and in response to the requirements associated with our three-year strategic plan, we informed our shareholders that we intend to maintain a $100 million reserve to meet our working capital and any unexpected needs. Moreover, the Board decided to fund a portion of the strategic plan's implementation costs out of existing cash resources, i.e., $85 million for 2006. After due consideration, we decided to buy back a substantial amount of shares, totalling $125 million, in December 2005 so that shareholders could reap the benefits of Transat's initiatives over the past few years. More information on this matter and our repurchase program in the normal course of business can be found in the Management's Discussion and Analysis.

During 2005, we amended Transat's capital structure by replacing common shares with two classes of shares: Class A Variable Voting Shares, owned by non-Canadians, carry one vote per share, unless the total number of such shares exceeds 25% of all outstanding voting shares, or 25% of the votes cast at a meeting; Class B Voting Shares, owned by Canadians, carry one vote per share at all times. This amendment was necessary because Transat holds 100% of air carrier Air Transat and must therefore comply with the *Canada Transportation Act*, which stipulates that all air carriers or the owners thereof be Canadian, i.e., no more than 25% of their voting shares may be owned or controlled by non-Canadians.

Poised for growth

As a result of current fuel prices and price volatility, in addition to fierce competition in Ontario for Caribbean and Mexican destinations and flights between Canada and the U.K., Transat anticipates that 2006 will be a difficult year with numerous challenges. Consolidated income is thus expected to be lower than in 2005. Moreover, in France, we still believe that Look Voyages will achieve profitability in late 2006.

Although this backdrop suggests that 2006 will be a tough year, tourism and international tourism, in particular, are faring very well and have shown resilience in the face of man-made and natural disturbances. Furthermore, the flurry of activity in certain markets is creating opportunities that the most adaptable companies will be able to capitalize on, with Transat foremost among them.

In 2005, we continued to seek the feedback of our employees, whose contribution is fundamental to our success. In a sector where human relationships are paramount, we consistently strive to foster the core values of efficiency, teamwork and customer satisfaction. With a keen awareness of our social responsibilities, we continue to provide financial and logistical support to educational and healthcare institutions, as well as cultural and international development organizations. Indeed, in early 2005, Transat and its staff made a significant donation to the Red Cross to help ease the hardships faced by tsunami victims in Indonesia and Sri Lanka. Air Transat and its staff also continued their partnership with the Children's Wish Foundation of Canada.

In December 2004, Lina De Cesare was appointed President, Tour Operators, and Philippe Sureau was appointed President, Distribution. In closing, I would like to congratulate François Laurin on his May 2005 appointment as Vice-President, Finance and Administration, and Chief Financial Officer. François' extensive knowledge of international markets, experience with public companies and financial management expertise are sure to be key factors in Transat's development and influence.

I would like to thank all Transat employees and all those who subscribe to our corporate values and vision. Thank you as well to our directors for their loyalty and invaluable contribution.

Jean-Marc Eustache

Chairman of the Board,
President and Chief Executive Officer
January 18, 2006

Management's Discussion and Analysis

This Management's Discussion and Analysis (MD&A) provides a review of Transat A.T. Inc.'s operations, performance and financial position for the year ended October 31, 2005, compared with October 31, 2004, and should be read in conjunction with the audited Consolidated Financial Statements and notes thereto beginning on page 49. The information contained herein is dated January 18, 2006. You will find more information about us on Transat's website at www.transat.com and on SEDAR at www.sedar.com, including the Certification Letters for fiscal 2005. These letters, signed by both the President/Chief Executive Officer and the Vice-President, Finance and Administration/Chief Financial Officer of the Corporation, attest to the effectiveness of disclosure controls and procedures.

We prepare our financial statements in accordance with Canadian generally accepted accounting principles (GAAP). We will occasionally refer to non-GAAP financial measures in this MD&A. These non-GAAP financial measures have no meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. They are furnished to provide additional information and should not be considered a substitute for measures of performance prepared in accordance with GAAP. All dollar figures are in Canadian dollars unless otherwise indicated. The terms "Transat," "we," "us," "our" and the "Corporation" mean Transat A.T. Inc. and its subsidiaries, unless otherwise indicated.

Caution regarding forward-looking statements

This MD&A also contains certain forward-looking statements with respect to the Corporation. These forward-looking statements, by their nature, necessarily involve risks and uncertainties that could cause actual results to differ materially from those contemplated by these forward-looking statements. We consider the assumptions on which these forward-looking statements are based to be reasonable, but caution the reader that these assumptions regarding future events, many of which are beyond our control, may ultimately prove to be incorrect since they are subject to risks and uncertainties that affect us. You will find elsewhere in this MD&A certain risks and uncertainties affecting us. The Corporation disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, other than as required by law.

Financial highlights

Years ended October 31 [in thousands of dollars, except amounts per share]

	2005	2004	2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$ [restated]	$ [restated]		
Consolidated statements of income					
Revenues	**2,364,481**	2,199,822	2,096,649	**7.5**	4.9
Margin[1]	**120,631**	163,755	74,962	**(26.3)**	118.5
Gain on disposal of Anyway, net of related taxes of $18,775	**N/A**	N/A	53,101	**N/A**	N/A
Restructuring charge	**(934)**	11,350	47,972	**(108.2)**	(76.3)
Net income (loss) from continuing operations	**55,416**	72,320	(9,215)	**(23.4)**	884.8
Net income	**55,416**	72,320	44,868	**(23.4)**	61.2
Basic earnings (loss) per share (continuing operations)	**1.43**	2.07	(0.38)	**(30.9)**	644.7
Basic earnings per share	**1.43**	2.07	1.27	**(30.9)**	63.0
Diluted earnings (loss) per share (continuing operations)	**1.33**	1.76	(0.38)	**(24.4)**	563.2
Diluted earnings per share	**1.33**	1.76	1.27	**(24.4)**	38.6
Consolidated balance sheets					
Cash and cash equivalents	**293,495**	310,875	242,952	**(5.6)**	28.0
Cash and cash equivalents in trust or otherwise reserved	**182,268**	157,678	106,173	**15.6**	48.5
	475,763	468,553	349,125	**1.5**	34.2
Assets	**949,537**	838,389	714,757	**13.3**	17.3
Debt (short-term and long-term)	**106,769**	33,214	67,081	**221.5**	(50.5)
Total debt[1]	**463,382**	536,746	596,999	**(13.7)**	(10.1)
Net debt[1]	**169,887**	225,871	354,047	**(24.8)**	(36.2)
Consolidated statements of cash flows					
Operating activities (continuing operations)	**63,785**	185,100	71,697	**(65.5)**	158.2

1 NON-GAAP FINANCIAL MEASURES

The terms “margin,” “total debt” and “net debt” have no standard definition prescribed by Canadian GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. These terms are presented on a consistent basis from period to period. These terms are included because management uses them to measure Transat’s financial performance.

Margin is used by management to assess Transat’s ongoing and recurring operational performance. This term is represented by revenues less operating expenses in the Consolidated Statements of Income.

Total debt is used by management to assess Transat’s future liquidity requirements. It is represented by the combination of balance sheet debt (long-term debt, obligations under capital leases and debentures) and off-balance sheet arrangements presented on p. 36.

Net debt is used by management to assess Transat’s liquidity position. It is represented by total debt (as discussed above) less cash and cash equivalents that are not in trust or otherwise reserved.

This MD&A is divided into the following sections:

Overview

Describes the holiday travel industry in general as well as our business, vision, strategy and objectives, along with the performance drivers and resources required to successfully implement this strategy and achieve our objectives.

Consolidated operations

Provides information and analysis about our performance in 2005, compared with our 2005 objectives and with actual 2004 results.

Explains the sources and use of our funds in 2005, compared with 2004, and describes how we manage our financial position and capital resources.

Describes the normal course issuer bid launched in June 2004 and renewed in 2005 for a 12-month period, in addition to events subsequent to October 31, 2005 and recent appointments.

Discusses the financial instruments, transactions and balances with related parties and critical accounting estimates used by our Corporation, together with the changes made to our accounting policies in 2005 and the accounting changes that will be required in the future.

Provides an overview of the key risks and uncertainties that could affect us.

Provides a discussion of Transat's future prospects for fiscal 2006.

Overview

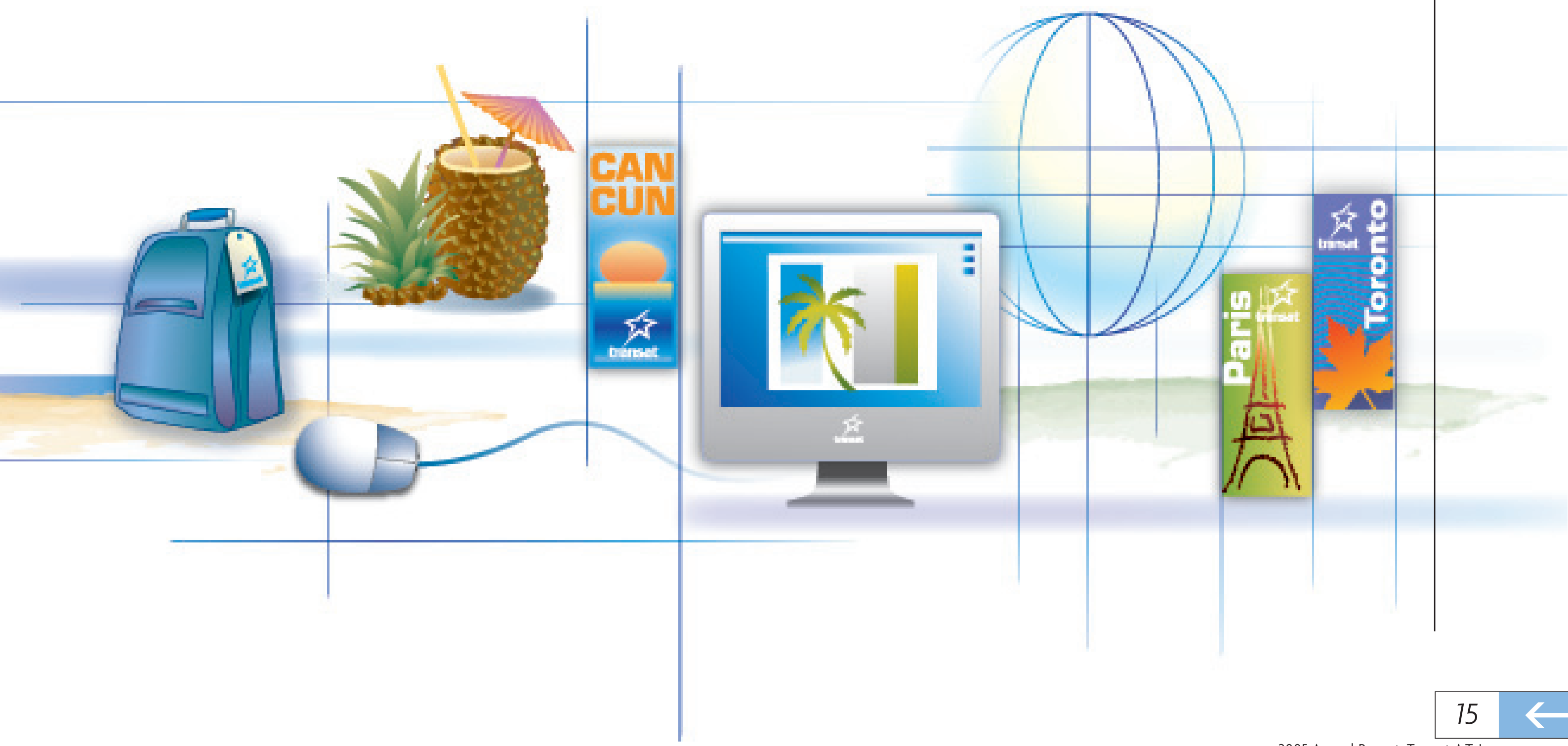
The holiday travel industry

The holiday travel industry is composed mainly of tour operators, travel agencies (traditional and online) and air carriers serving the holiday travel market through a combination of scheduled and charter air services. According to the World Tourism Organization, international tourist arrivals reached a record high of 763 million in 2004 and could reach one billion by 2010.

Tour operators specialized in outgoing services purchase the various components of a trip and sell them to the consumer via travel agencies, either as travel packages or separately. Some tour operators specialize as incoming tour operators, making arrangements for foreign tourists at their destinations or bundling certain services as packages to be sold on foreign markets.

Travel agencies are the intermediaries between tour operators and consumers. Travel agents meet with, advise and sell to consumers. Travel agencies sell holiday packages and plane tickets offered by tour operators, in addition to plane tickets sold directly by airline carriers and other travel products and services. Online travel agencies now offer a large range of travel products via transactional Internet Web sites. In both North America and Europe, online travel sales are now made up almost exclusively of air-only tickets, with only a small proportion made up of packages (including airline tickets and hotels). Sales of online packages, however, are expected to grow.

Air carriers provide services to travel agencies and tour operators. These carriers are known as "scheduled" when they sell services directly to the public and travel agencies, and as "charter" when they sell seats in blocks to tour operators.



Core business, vision and strategy

Core business – Transat is one of the largest fully integrated tour operators of international scope in North America. We conduct our activities in a single industry segment (holiday travel) and operate in two geographic business areas (North America and Europe). Transat's core business involves holiday packages and a combination of scheduled and charter flights. We operate as both an outgoing and incoming tour operator by bundling products and services bought in Canada and abroad and reselling them in Canada, France and elsewhere, mainly through travel agencies, some of which we own. We operate the leading airline company in Canada specializing in international charter services, with flights scheduled between Canada and thirteen countries. We also provide destination and hotel management services.

Vision – In light of the expanding international tourism market, our vision is to maximize shareholder value by penetrating new markets, increasing our market share and maximizing the benefits of vertical integration. We maintain a leadership position in the Canadian market, where we operate as an outgoing and incoming tour operator; we are also the country's largest charter airline. We also have a solid foundation in France as a vertically integrated outgoing tour operator. We have developed a number of solid brands and we offer a large number of international destinations in both Canada and France. Over time, we aim to expand our business in other countries where we believe there is high growth potential for an integrated player specializing in holiday travel, namely the U.S., the U.K. and other European countries.

Strategy – In late fiscal 2005, we completed a strategic three-year plan focused on growth and profitability. We anticipate that increased international tourism will speed our growth, particularly in North America and Europe. To this end, we will be making new acquisitions while pursuing a dynamic pace of internal growth.

Our key strategic focuses are as follows:

- **In Canada, Transat is the leader in all regions except Ontario. We plan to bolster our presence in Ontario by adding new destinations and expanding our distribution network to become the market leader in all regions of the country.**
- **In Europe, Transat intends to grow its market share and continue its vertical integration in France and the U.K., building on its strong presence in these two high-potential markets. Transat will also continue its initiatives to expand into other European countries as a tour operator specializing in travel to Canada, among other destinations.**
- **Elsewhere, Transat will strive to invest in new markets and, in particular, to become a tour operator in the U.S., a strategic market it has been analyzing for some time. In addition, Transat will continue studying the possibility of penetrating other markets, such as Asia and Latin America.**
- **Transat wishes to step up development of destination services and to assume a portion of its accommodation needs in order to gain better control over capacity and product quality and to boost margins. In practical terms, this may mean pursuing stakes or acquisitions in the hotel industry. Markets in which Transat has already reached critical mass will be reviewed first.**
- **In light of rapid change in the distribution industry and travellers' expectations, and given the importance of organizational responsiveness and productivity, our strategic plan will include our ongoing technology and training initiatives and investments. To this end, Transat will strive to introduce cutting-edge solutions via agencies and direct sales in order to adapt to new markets and to continue efficiency enhancements.**

Transat estimates that implementing its strategic plan will require up to $300 million over three years, with funding from existing cash resources, future cash flows and external sources, as needed.

2006 objectives

As part of its 2006-2008 strategic plan, Transat seeks to pursue growth by increasing its size and improving its profitability. The objective is to remain one of the top integrated tour operators worldwide. For fiscal 2006, our key development initiatives and related priorities will be as follows:

- **Increasing Transat's competitiveness in the Canadian and European markets.** We aim to refine our customer segmentation process and to ensure that our tour operators develop and implement separate customized marketing strategies, in line with the market. To this end, we will be upgrading our distribution system, which is based on three pillars: travel agencies; business-to-business (B2B) applications involving our tour operators and their retail network; and online business-to-consumer (B2C) distribution. Lastly, we will continue to integrate certain tour operators activities in both France and Canada, with a view to reducing costs, particularly via synergies.

- **Emphasizing vertical integration of destination services.** We intend to make additional investments in destination services through partnerships or acquisitions in the hotel and incoming tour operator sectors.

- **Achieving growth via new markets.** Transat is already a leading outgoing tour operator in Canada and France. To achieve further growth, we intend to become a leader, particularly in European and North American markets. In 2006, we will be examining other possibilities, including the U.K., which is already an important market for us, and we will complete a U.S. market analysis to ensure proper timing of our entry in that market.

- **Planning and implementing the next generation of information systems.** We will be drawing up a long-term plan with a view to implementing the next generation of information systems — the central component of tour operators' activities. These are expected to include a centralized seat inventory management system, which will be integrated into the operating systems of Air Transat A.T. Inc. ("Air Transat"). In addition, we aim to refine our preferred B2B applications and online sales systems (B2C), both in Canada and France. Lastly, we will be developing the information systems used by our Canadian incoming tour operator, particularly as regards multilingual capability and connectivity with customers and suppliers.

- **Continuing to build on our "new" base in France.** At Look Voyages, we aim to achieve profitability beginning in the second half of 2006. In light of our new emphasis on holiday packages, we will be redefining the "Clubs Lookéa" concept and drawing up a strategic plan accordingly. Although tour operator Vacances Transat (France) remains strongly focused on Canada, this subsidiary's growing diversification will enable us to pursue growth in continental Europe and the long-haul market while improving the targeting of our offer. In France, we will be mobilizing our entire team to build on the solid base we have already established.

- **Creating an environment to foster continuous knowledge acquisition, development and sharing.** We aim to use the best tools to identify, promote and attract talented people, thereby building a strong and diversified team capable of assuming responsibility for our ongoing viability. We will also be developing personal development initiatives for high-potential employees as part of an aggressive business succession plan.

Key performance drivers

The following key performance drivers are essential to the successful implementation of our strategy and to the achievement of our objectives.

Market share	To be the leader in Canada in all provinces and increase market share in Ontario, across the rest of the country and in Europe.
Revenue growth	To grow revenues by more than 5%, excluding acquisitions.
Margin	To generate margins higher than 5%.

Ability to deliver on our objectives

Our ability to deliver on our objectives is dependent on our financial and non-financial resources, both of which have contributed to the success of our strategies and the achievement of our objectives in the past.

Our financial resources include:

Cash	Our cash balances not held in trust or otherwise reserved, totalling $293.5 million as at October 31, 2005, are strong. Our continued focus on expense reductions is expected to maintain our cash balances at healthy levels, taking into consideration the expected use of cash balances as part of our issuer bids.

Our non-financial resources include:

Brand	We have taken all necessary steps, including the use of a new corporate logo and an integrated branding platform, to create a unique, strong and visible identity across our main business units with a view to maximizing customer awareness in both the B2C and B2B markets, fully leveraging the contribution of all business units and creating value.
Structure	Our vertically integrated structure enables us to ensure better quality control of our products and services.
Employees	In recent years, we have intensified our efforts to build a unified corporate culture based on a clear vision and shared values. As a result, our employees work together as a team and are committed to ensuring overall customer satisfaction and improving productivity. In addition, we believe we derive the benefits of strong leadership; indeed, our founders are still at the helm, bringing expertise and depth.
Relationship with suppliers	We have exclusive access to certain hotels in the Caribbean and the Gulf of Mexico. Our privileged relationships with many hotels in Europe, the Caribbean and the Gulf of Mexico date back almost 20 years.

Transat has the resources it needs to meet its 2006 objectives and to continue building on its long-term strategies.

Consolidated operations

Comparison of 2005 objectives with 2005 performance

In 2005, Transat set various objectives. Listed below are our 2005 objectives, compared with our 2005 performance. We will discuss these in more detail in our analysis of the 2005 fiscal year throughout this MD&A.

- **Returning Look Voyages to profitability in 2006.**
  We continued to implement the recovery initiatives begun in 2004 with a view to returning Look Voyages to profitability. The efforts of Transat's management and employees during fiscal 2004 and 2005 have paid off. We surpassed our objective of cutting Look Voyages' losses by one-half. We still believe we will be able to return this subsidiary to profitability beginning in the second half of 2006.

- **Continuing to execute the development plan in accordance with Transat's overall strategy.**
  In 2005, we made a number of acquisitions. In the outgoing tour operator sector, we acquired Air Consultants Europe and Bennett Voyages. In the incoming tour operator and destination services sectors, we acquired the assets of Turissimo Caribe & Excursiones C. Por A. Finally, in the distribution sector, we acquired a 50.1% stake in Travel Superstores Inc. (tripcentral.ca).

- **Fostering an enterprise culture in support of our long-term business model.**
  During the year, we developed a number of training programs to enhance our enterprise culture. These programs reflect our corporate values such as customer focus, teamwork and productivity. In addition, we drew up and implemented a succession plan and created a corporate Intranet.

- **Continuing to incorporate online technology within our business model.**
  During the year in Canada, we implemented a number of B2B platforms that should be operational in the first half of fiscal 2006. In Europe, our B2B platforms are already operational. In 2006, we will continue to develop our B2C platforms.

- **Continuing to focus on tour operators.**
  We revamped the product lines of our two main Canadian tour operators (Vacances Transat and Nolitours) to ensure full complementarity. In addition, we reviewed Nolitours' pricing policy and distribution approach in response to intense competition in certain market segments. These efforts included strengthening links with our partners and a marketing campaign. Finally, we pursued long-term planning initiatives for our aircraft fleet — a key factor for tour operators.

Acquisitions

During the year ended October 31, 2005, the Corporation made a number of business acquisitions, which were accounted for using the purchase method. The acquired companies' results were consolidated as of the respective acquisition dates.

On November 1, 2004, the Corporation acquired a 70% stake in Air Consultants Europe, a Netherlands-based outgoing tour operator, for a total consideration of €1.1 million ($1.6 million). A €1 million cash payment ($1.5 million) was made on the acquisition date, with the balance (€0.1 million) payable in two instalments until November 1, 2006. Moreover, under the Agreement, the Corporation has a call option related to the acquisition of the remaining shares; this option may be exercised at any time prior to October 31, 2007.

On May 1, 2005, the Corporation acquired a 50.1% stake in Travel Superstore Inc., a Canadian company operating a travel agency network, for a total cash consideration of $4.5 million. Moreover, under the Agreement, the Corporation has a call option related to the acquisition of the remaining shares; this option may be exercised prior to 2015.

On June 26, 2005, the Corporation acquired 100% of the outstanding shares of Bennett Voyages, a France-based outgoing tour operator, for a total consideration of €1.8 million ($2.6 million). A cash payment of €1.1 million ($1.6 million) was made on the acquisition date, with the balance (€0.7 million, or $1.0 million) payable in monthly instalments until December 31, 2006.

On August 1, 2005, the Corporation acquired the assets of Blenus Travel Service Ltd. and Fundy Travel Ltd. for a total consideration of $1.3 million. (Both of these Canadian companies operate travel agency networks.) A cash payment of $0.3 million was made on the acquisition date, with the balance ($1.0 million) payable over a five-year period without interest.

On October 31, 2005, the Corporation acquired the assets of Turissimo Caribe & Excursiones C. Por A., an incoming tour operator based in the Dominican Republic, for a cash consideration of US$1.2 million ($1.4 million).

As a result of these transactions, the goodwill on the balance sheet increased by $8.5 million. (See note 14 to the audited Consolidated Financial Statements.)

Geographic business areas

Revenues

Years ended October 31 [in thousands of dollars]

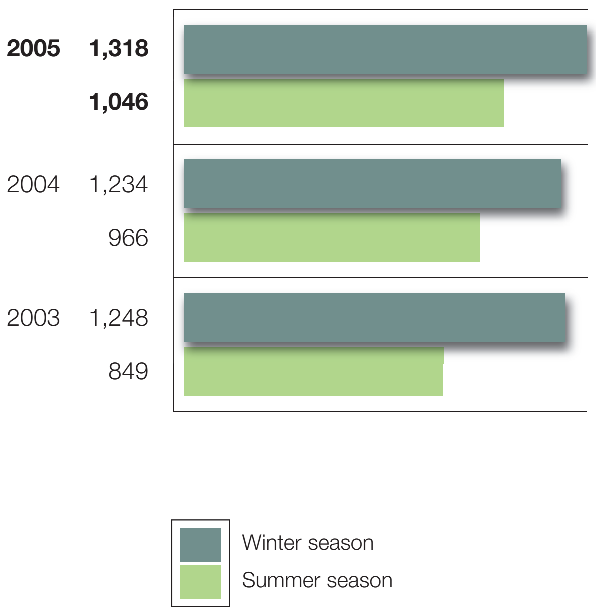
	2005	2004	2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$	$		
North America	**1,896,487**	1,673,530	1,525,846	**13.3**	9.7
Europe	**467,994**	526,292	570,803	**(11.1)**	(7.8)
Total	**2,364,481**	2,199,822	2,096,649	**7.5**	4.9

We derive our revenues from outgoing tour operators, air transportation, travel agencies and distribution, incoming tour operators and destination services.

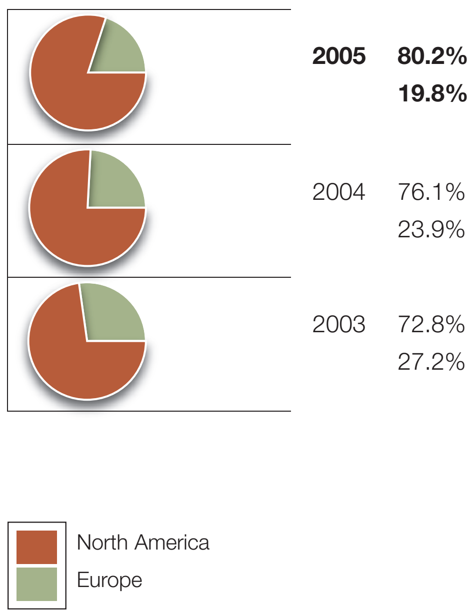
The overall increase was due to a 13.3% jump in revenues in North America, offset by an 11.1% decrease in revenues from our European operations. The terms “travellers” and “passengers” will be used throughout the MD&A to explain these increases and decreases. Basically, tour operators record round-trips in terms of travellers and airlines record flight segments in terms of passengers. The key factor driving higher revenues was the number of travellers, which increased by 8.6% compared with 2004. This in turn resulted from an 11.6% increase in the number of North American travellers, offsetting a 7.9% drop in Europe. The decrease in revenues from our European operations was also exacerbated by the dollar’s appreciation against the euro and by Look Voyages’ abandonment of its air-only operations in 2004.

We expect that the total number of travellers in 2006 will be similar to that of 2005. We also anticipate an increase in revenues compared with 2005.

Revenues by season
North America and Europe
(continuing operations)
[in millions of dollars]



Geographic segmentation
of revenues
(continuing operations)



Operating expenses

Years ended October 31 [in thousands of dollars]

	2005	2004	2003	As a % of revenues 2005	As a % of revenues 2004	As a % of revenues 2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$	$					
Direct costs	**1,168,612**	1,075,861	1,023,199	**49.4**	48.9	48.8	**8.6**	5.1
Salaries and employee benefits	**241,776**	227,626	228,320	**10.2**	10.4	10.9	**6.2**	(0.3)
Aircraft fuel	**199,376**	128,112	137,716	**8.4**	5.8	6.6	**55.6**	(7.0)
Commissions	**181,587**	179,873	171,791	**7.7**	8.2	8.2	**1.0**	4.7
Aircraft maintenance	**91,778**	88,684	112,960	**3.9**	4.0	5.4	**3.5**	(21.5)
Airport and navigation fees	**67,937**	59,379	60,382	**2.9**	2.7	2.9	**14.4**	(1.7)
Aircraft rent	**52,064**	59,640	67,988	**2.2**	2.7	3.2	**(12.7)**	(12.3)
Other	**240,720**	216,892	219,331	**10.2**	9.9	10.4	**11.0**	(1.1)
Total	**2,243,850**	2,036,067	2,021,687	**94.9**	92.6	96.4	**10.2**	0.7

Our operating expenses consist mainly of direct costs, salaries and employee benefits, aircraft fuel, commissions, aircraft maintenance, airport and navigation fees and aircraft rent.

The overall growth in our operating expenses was due to an 18.8% increase in North America, offset by a 13.5% decrease in our European operations. These fluctuations stemmed primarily from surging fuel prices, increased business activity in North America, reduced air-only activity in France and the euro's depreciation against the dollar.

Approximately 30% of our operating expenses are payable in U.S. dollars. We did not fully benefit from the rebounding Canadian dollar, however, due to our hedging program.

Direct costs include the costs of the various trip components sold to consumers via travel agencies and incurred by our tour operators. They also include hotel room costs and the costs of reserving blocks of seats or complete flights, mainly with third-party air carriers. In 2005, these costs represented 49.4% of our revenues, compared with 48.9% in 2004. The dollar-figure increases were due to increased business activity and higher per-seat and hotel room costs.

Salaries and employee benefits decreased as a percentage of revenues thanks to our cost controls and to the restructuring efforts undertaken in 2003, resulting in the termination of over 700 employees.

Aircraft fuel costs increased by 55.6%, or almost $71.3 million, during the year, due to higher fuel prices, which continued to surge all year.

Commissions include the fees paid by tour operators to travel agencies for serving as intermediaries between tour operators and consumers. The dollar-figure increase was due to increased business activity, offset in part by the decrease in commission rates.

Aircraft maintenance costs relate mainly to the engine and airframe overhaul expenses incurred by Air Transat. Our maintenance costs were up only slightly as a result of our increased business activity.

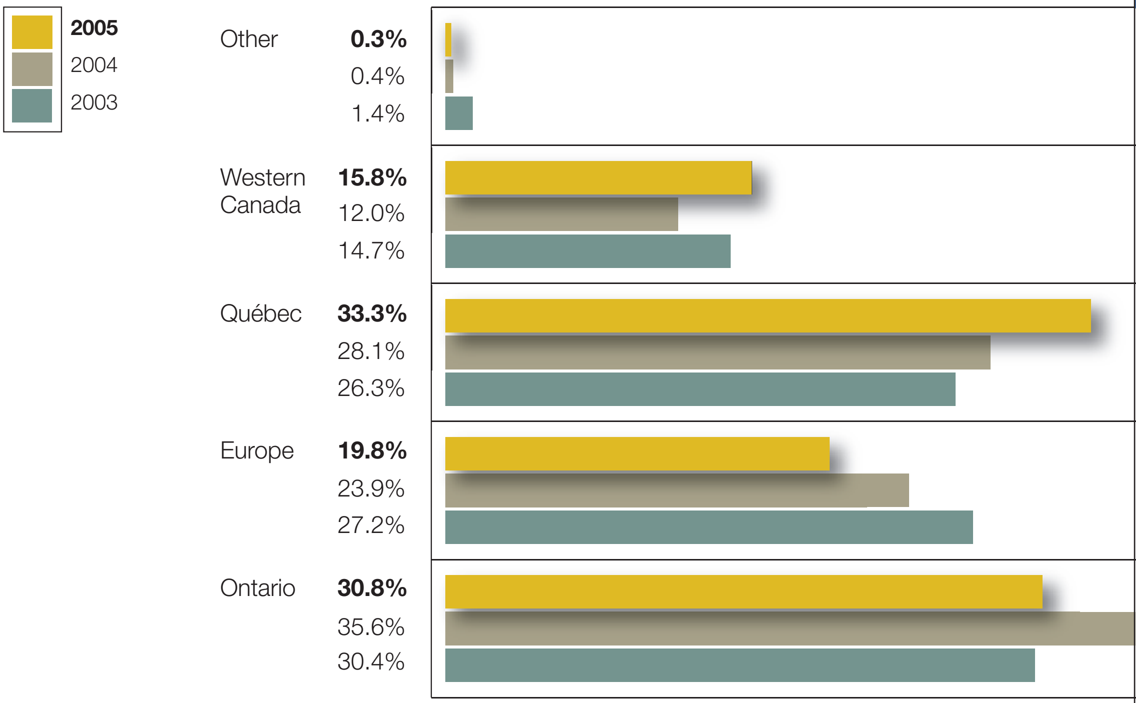
Airport and navigation fees relate mainly to fees charged by airports. The 14.4% increase resulted from the higher landing fees charged by several airports since fiscal 2004.

The decrease in aircraft rental costs was due to the adoption of Accounting Guideline 15 (AcG-15), *Consolidation of Variable Interest Entities*, which was issued by the Canadian Institute of Chartered Accountants (CICA) and which took effect on November 1, 2004. AcG-15's impact on aircraft leasing costs was offset in part by the delivery of new aircraft in fiscal 2004. (See *Changes to Accounting Policies* in the *Accounting* section of this MD&A.)

The increase in our other expenses was primarily due to increased business activity. In addition, our computer expenditures also rose during the year. In 2004, other expenses included a US$4.6 million ($6.2 million or $3.9 million after-tax) payment to the Corporation to settle a dispute with the U.S. government. The dispute related to fees paid pursuant to U.S. regulations that were subsequently deemed null and void by the U.S. courts.

Although we anticipate further savings as a result of our continuing restructuring and cost-control efforts, we expect that our overall operating expenses will rise as a result of increased business activity in 2006.

Sources of revenues
(continuing operations)



North America

Winter season

Years ended October 31 [in thousands of dollars]

	2005	2004	2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$	$		
Revenues	**1,111,924**	993,373	976,336	**11.9**	1.7
Operating expenses	**1,026,033**	884,185	921,857	**16.0**	(4.1)
Margin	**85,891**	109,188	54,479	**(21.3)**	100.4
Margin (%)	**7.7**	11.0	5.6	**(30.0)**	96.4

In North America, revenues increased by 11.9% during the 2005 winter season, compared with the same period in 2004. This increase was due to a 14.9% rise in the number of travellers, compared with the corresponding period in 2004, offset in part by competition-driven pricing pressure. Demand for Caribbean and Gulf of Mexico destinations was particularly strong; it was relatively stable for Florida.

The impact of higher fuel prices began putting pressure on our margins during the 2005 winter season. Margins decreased to 7.7%, compared with 11.0% during the 2004 winter season.

During the 2005 winter season, Air Transat served some 50 destinations in 19 countries, primarily southern or other sunshine destinations. During the summer months, Air Transat shifts most of its capacity to Europe, while maintaining some flights to southern destinations. In 2005, Air Transat offered direct flights to some 30 cities in nine European countries.

North America

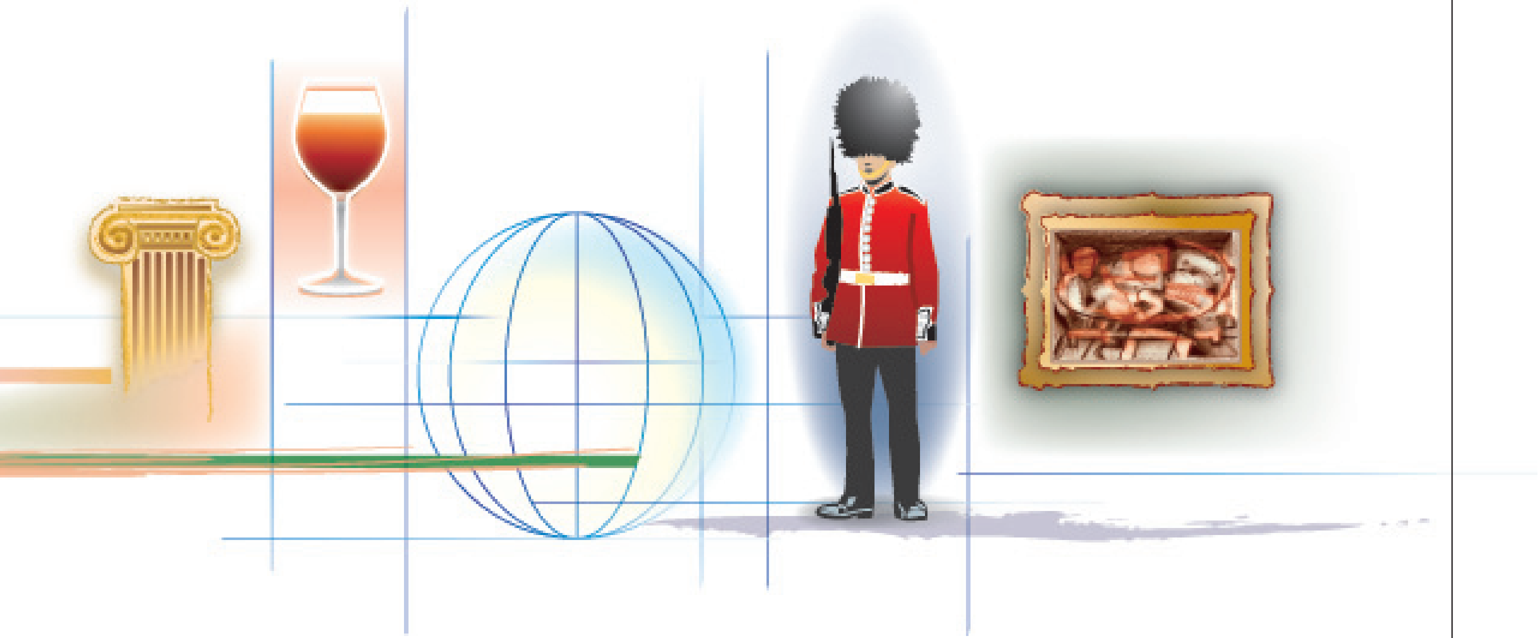
Summer season

Years ended October 31 [in thousands of dollars]

	2005	2004	2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$	$		
Revenues	**784,563**	680,157	549,510	**15.4**	23.8
Operating expenses	**750,778**	611,786	513,333	**22.7**	19.2
Margin	**33,785**	68,371	36,177	**(50.6)**	89.0
Margin (%)	**4.3**	10.1	6.6	**(57.4)**	53.0

During the 2005 summer season, revenues increased by 15.4% compared with the 2004 summer season, thanks mainly to a 10.3% increase in the number of travellers and to the excellent performance of our incoming tour operator Jonview Canada. Demand was significantly higher for European destinations, particularly in Greece, Italy and the U.K., where capacity was increased.

As in the 2005 winter season, margins were strongly impacted by higher fuel prices, which continued to surge throughout the 2005 summer season. For the summer season, our margins dropped from 10.1% in 2004 to 4.3% in 2005.



Europe

Winter season

Years ended October 31 [in thousands of dollars]

	2005	2004	2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$	$		
Revenues	**205,760**	240,051	271,562	**(14.3)**	(11.6)
Operating expenses	**211,614**	252,953	280,796	**(16.3)**	(9.9)
Margin	**(5,854)**	(12,902)	(9,234)	**54.6**	(39.7)
Margin (%)	**(2.8)**	(5.4)	(3.4)	**48.1**	(58.8)

Our European operations mainly consist of two outgoing tour operators, Vacances Transat (France) and Look Voyages.

As the market leader for Canadian destinations, Vacances Transat (France) has successfully implemented a long-standing strategy of specializing as a long-haul holiday tour operator, with a focus on travel package sales. It has reached a top-tier position in that market segment and is the leader for several Caribbean and Gulf of Mexico destinations.

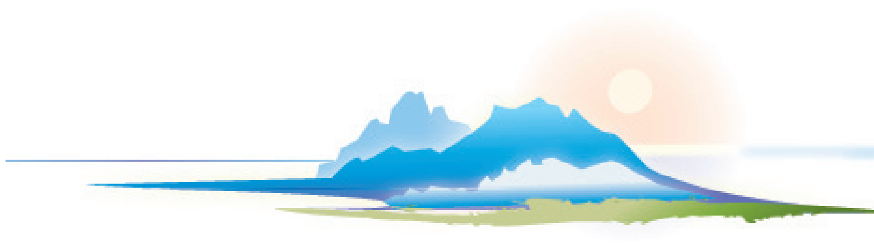
Look Voyages is solidly positioned in the French market and its flagship product, the Clubs Lookéa (with all-inclusive services, including French-language entertainment), continues to appeal to French travellers. The Lookéko product was launched a few years ago and is also very popular with Look Voyages clients.

In July 2004, we unveiled a plan to reposition Look Voyages and to pursue our efforts to bring it back to profitability. Please refer to “Restructuring charge” in this section of the MD&A for more information on this plan.

In Europe, revenues and expenses both decreased during the 2005 winter season, compared with the corresponding season of 2004. The drop in revenues was primarily due to the decrease in air-only passengers, which in turn stemmed from Transat’s decision to withdraw Look Voyages from this market segment. In addition, competitive pressures resulted in lower demand (compared with last year) for our products, including long-haul flights from Europe to Caribbean and Gulf of Mexico destinations (travel packages).

The restructuring plan we initiated in 2004 began paying off during the 2005 winter season, with the 5.4% negative margin in 2004 dropping to a 2.8% negative margin in 2005.

In Europe, the prospects for the 2006 winter season are encouraging. The current reservation trend is up slightly, compared with 2005. We anticipate an increase in long-haul flights from Europe to North American destinations and a decrease to Caribbean and Gulf of Mexico destinations.



Europe

Summer season

Years ended October 31 [in thousands of dollars]

	2005	2004	2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$	$		
Revenues	**262,234**	286,241	299,241	**(8.4)**	(4.3)
Operating expenses	**255,425**	287,143	305,701	**(11.0)**	(6.1)
Margin	**6,809**	(902)	(6,460)	**854.9**	86.0
Margin (%)	**2.6**	(0.3)	(2.2)	**966.7**	86.4

In Europe, our restructuring efforts (initiated in 2003) and acquisitions produced results.

The drop in revenues during the 2005 summer season, compared with that of 2004, was primarily due to lower demand for long-haul flights from Europe to Caribbean and Gulf of Mexico destinations. The number of travellers to these destinations was down nearly 2.4%, compared with 2004.

Although revenues were down for the 2005 summer season, margins exceeded the break-even point thanks to reduced losses at Look Voyages and the strong performance of our other European subsidiaries. However, the euro's depreciation against the dollar, compared with the 2004 summer season, had a negative impact on the profitability of our European operations.

While it is too early to draw any conclusions concerning the 2006 summer season in Europe, we anticipate an increase (compared with 2005) in the number of people travelling from France to Canadian destinations.

Other expenses/revenues

Amortization

Years ended October 31 [in thousands of dollars]

				% Increase (Decrease)	
	2005	2004	2003	**2005**	2004
	$	$	$		
Amortization	**37,558**	33,027	42,138	**13.7**	(21.6)

Amortization expense relates to capital assets and other assets, primarily long-term financing costs and development costs.

The amortization expense increased by more than 13%, due to the adoption of AcG-15 (effective November 1, 2004) and to acquisitions of capital assets during the year.

Restructuring charge (2004)

In July 2004, we unveiled a plan to reposition Look Voyages and to pursue our efforts to bring it back to profitability. The plan involved abandoning certain operations considered non-strategic, namely the marketing and sale of air-only tickets. The plan called for Look Voyages to boost its holiday package business and to step up its use of Web-based technologies with a view to stimulating sales to travel agents and the general public. In accordance with French labour regulations, we submitted our plan; negotiations subsequently led to a staff reduction of approximately 90 individuals. Implementation of this plan resulted in Transat recording an $11.4 million restructuring charge in the fourth quarter of 2004. This amount included $8.3 million in cash charges and $3.0 million in asset write-offs. In 2004, we forecast that the plan would reduce Look Voyages' losses by 50% in fiscal 2005. Today, we can confirm that this objective has been exceeded. Look Voyages is expected to return to profitability in late fiscal 2006.

In 2005, our review of the measures implemented during the year ended October 31, 2004 led to a $0.9 million reversal of the provision, primarily due to lower employee training and reclassification expenses (as required under French law), lower negotiation expenses related to the cancellation of contracts and earlier-than-expected employee departures.

The following table highlights our restructuring activities and the balance of the provision for the restructuring charge for the year ended October 31, 2005.

[in thousands of dollars]

	Balance as at October 31, 2004 $	Reversal of the provision $	Cumulative drawdowns (cash) $	Translation adjustment $	**Balance as at October 31, 2005 $**
Employee termination benefits	4,590	230	4,071	47	**242**
Contract termination costs	2,526	287	992	129	**1,118**
Other costs	1,115	417	393	69	**236**
Total	8,231	934	5,456	245	**1,596**

Restructuring charge (2003)

In 2003, we undertook to reduce our costs, while improving our operational efficiencies and ensuring that all products and services not generating targeted returns would be either remedied or eliminated. As part of these efforts, we drew up a restructuring program in the second quarter of fiscal 2003. This program included changes to our management structure, as well as a fundamental restructuring of our operations in France and Canada. The war in Iraq and SARS, both of which drove down demand, accelerated the need for such a program. These events also significantly affected our fleet composition.

The 2003 restructuring program is substantially completed. We expect that the final related expenditures will be carried out during fiscal 2008.

The following table highlights the restructuring activities and the balance of the 2003 restructuring provision for the year ended October 31, 2005.

[in thousands of dollars]

	Balance as at October 31, 2004 $	Cumulative drawdowns (cash) $	**Balance as at October 31, 2005 $**
Employee termination benefits	3,273	1,689	**1,584**
Contract termination costs	50	50	**—**
Other costs	393	393	**—**
Total	3,716	2,132	**1,584**

Interest

Years ended October 31 [in thousands of dollars]

	2005	2004	2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$ [restated]	$ [restated]		
Interest on long-term debt, obligations under capital leases and debentures	**10,815**	7,712	9,839	**40.2**	(21.6)
Other interest and financial expenses	**1,708**	1,907	3,071	**(10.4)**	(37.9)
Interest income	**(12,963)**	(11,307)	(9,530)	**14.6**	18.6

Interest on long-term debt, obligations under capital leases and debentures

Interest on long-term debt, obligations under capital leases and debentures increased in 2005, compared with 2004, due to the adoption of AcG-15. Under this Guideline, a portion of the off-balance sheet debt (approximately $92 million as at October 31, 2005) is reflected on our balance sheet, thereby increasing our balance sheet debt and our interest expense. In addition, we redeemed in advance $21.9 million in debentures on January 10, 2005, thereby incurring a $1.7 million non-cash charge reflecting the difference between the debentures' face value amount and their book value at that time, in addition to a $0.8 million interest penalty.

Other interest and financial expenses

Our other interest and financial expenses remained stable during the year, compared with the previous year.

We do not expect that these expenses will vary significantly in 2006, compared with 2005.

Interest income

The increase in interest income was due to higher average cash and cash equivalent balances during the year, as well as to higher interest rates. We expect that interest income will decrease in 2006, primarily due to lower-than-expected cash and cash equivalent balances (compared with 2005) resulting from the use of cash and cash equivalents as part of the issuer bid announced on November 14, 2005, and completed on January 3, 2006.

Foreign exchange gain (loss) on long-term monetary items

For fiscal 2005, the Corporation recorded a foreign exchange gain on long-term monetary items due to the Canadian dollar's continuing appreciation against the U.S. dollar during the year. A stronger Canadian dollar reduces the value of our long-term monetary assets and liabilities. The adoption of AcG-15 resulted in an increase in our U.S.-dollar-denominated balance sheet debt. The foreign exchange gain on long-term monetary items was primarily due to the positive impact of exchange rates on our debt levels. During the corresponding period in 2004, the foreign exchange loss was due to deposits we made related to engine and airframe overhaul expenses and paid to certain aircraft lessors in U.S. dollars.

Gain on disposal of investments

In June 2005, we signed an agreement that led to the sale of our 44.27% stake in Star Airlines S.A. (Star) for a total consideration of €4.5 million. This transaction resulted in a $5.7 million gain on disposal.

Share of net income (loss) of companies subject to significant influence

On January 31, 2004, we discontinued recording an interest in Star's results. This change adopted in 2004 was the main reason for the variance between fiscal 2005 and fiscal 2004. The corresponding period in 2004 included Star's first-quarter results, which showed a loss.

Income taxes

Our total income tax provision amounted to $36.3 million for the fiscal year ended October 31, 2005, compared with $45.0 million for fiscal 2004. Excluding the share of net income (loss) of companies subject to significant influence, the effective tax rates were 39.1% for the fiscal year ended October 31, 2005 and 38.1% for the preceding fiscal year.

The increase in our tax rate was due in part to the decision to write down $5.6 million in future tax assets. This amount had been recorded based on the deferrable tax losses generated by our French operations and incurred as at July 31, 2004. This writedown was recorded based on our analysis (from an accounting perspective) of whether our unused tax losses related to our French operations could be used to realize tax savings in the future. Excluding the writedown of future tax assets, however, our effective tax rate for fiscal 2005 and 2004 would have been 33.5% if we had recorded tax recoveries on losses generated by our French operations.

Net income

As a result of the items discussed in “Consolidated operations” of this MD&A, our net income was $55.4 million, or $1.43 per share, for fiscal 2005, compared with net income of $72.3 million, or $2.07 per share, for fiscal 2004. The weighted average number of outstanding shares used to compute per share amounts was 37,863,000 for the current year and 33,374,000 for 2004.

On a diluted per share basis, earnings per share for fiscal 2005 amounted to $1.33 per share, compared with $1.76 per share for fiscal 2004. The adjusted weighted average number of outstanding shares used to compute diluted earnings per share was 41,684,000 for the current year and 41,156,000 for 2004.

Excluding the restructuring charge, the gain on disposal of our investment in Star and the foreign exchange gain resulting from the adoption of AcG-15 requiring us to consolidate certain financial transactions, net earnings in 2005 were $46.8 million, or $1.14 per fully diluted share, compared with $83.7 million, or $2.04 per fully diluted share, in 2004. (See note 11 to the audited Consolidated Financial Statements.)

Selected quarterly unaudited financial information

[in thousands of dollars, except amounts per share]

	Q1		Q2		Q3		Q4	
	2005	2004	**2005**	2004	**2005**	2004	**2005**	2004
	$	$ [restated]	**$**	$ [restated]	**$**	$ [restated]	**$**	$ [restated]
Revenues	**588,740**	537,200	**728,944**	696,224	**552,897**	499,118	**493,900**	467,280
Margin	**13,833**	16,945	**66,204**	79,341	**17,214**	28,120	**23,380**	39,349
Net income (loss)	**(1,800)**	2,786	**38,400**	45,424	**794**	12,772	**18,022**	11,338
Earnings (loss) per share	**(0.08)**	0.06	**1.05**	1.35	**0.02**	0.36	**0.45**	0.31
Diluted earnings (loss) per share	**(0.08)**	0.06	**0.91**	1.10	**0.02**	0.31	**0.44**	0.27

Overall, revenues in 2005 were up compared with 2004, primarily due to an increase in the number of travellers and to the acquisitions made since the third quarter of fiscal 2004.

Our margins demonstrated significant fluctuations in fiscal 2005, compared with 2004. In general, they were under great pressure throughout the year from surging fuel prices and selling price competition.

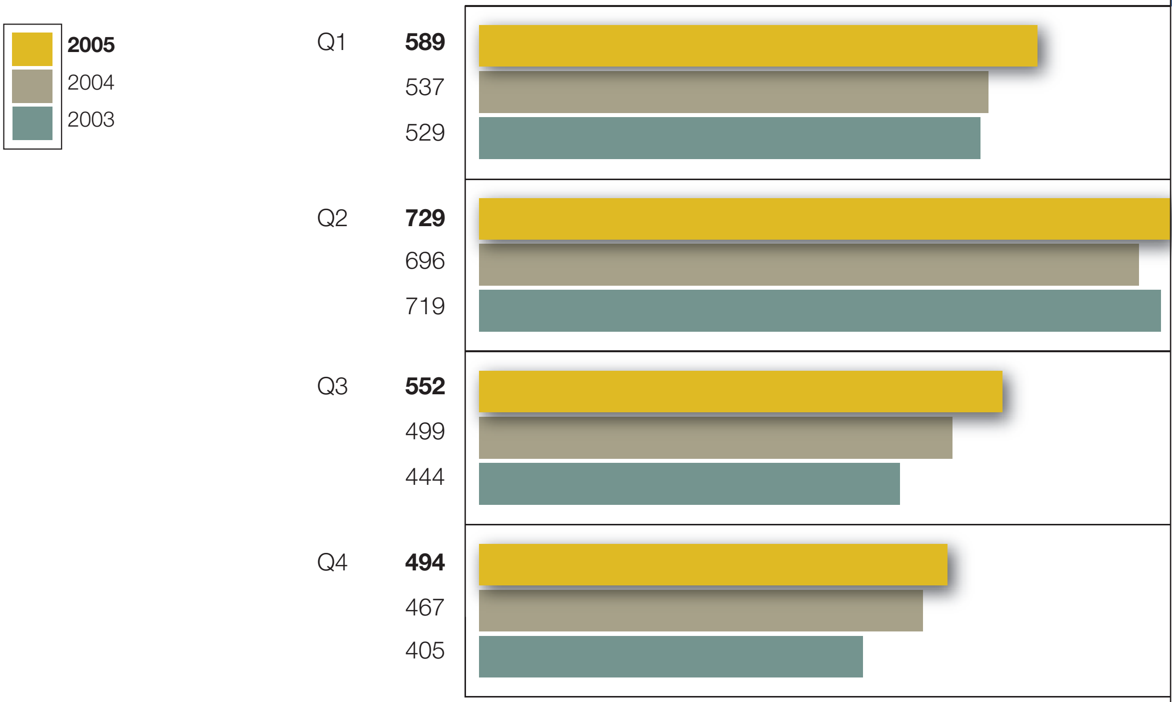
Fourth-quarter highlights

In the fourth quarter of fiscal 2005, we recorded revenues of $493.9 million, compared with $467.3 million for the same period in 2004, representing an increase of $26.6 million, or 5.7%. This was primarily due to increased business activity in North America and to the acquisitions made since 2004, offset in part by pricing pressures in Ontario and the U.K. and by the depreciating euro.

In addition, we generated a margin of $23.4 million, or 4.7%, during the fourth quarter of fiscal 2005, compared with $39.4 million, or 8.4%, in 2004. The increase in operating expenses stemmed from surging fuel prices and increased business activity.

Net income for the quarter stood at $18.0 million, or $0.44 per share on a fully diluted basis ($9.1 million, or $0.22 per share, excluding the after-tax effect of reversing certain restructuring charges, of the gain on disposal of our investment in Star and of the gain on foreign exchange resulting from the application of AcG-15 and requiring us to consolidate certain financial transactions). This compared with $11.3 million, or $0.27 per share on a fully diluted basis ($22.7 million, or $0.54 per share), excluding the after-tax restructuring charge.

Revenues by quarter
(continuing operations) [in millions of dollars]



Cash flows

Years ended October 31 [in thousands of dollars]

	2005	2004	2003	% Increase (Decrease) 2005	% Increase (Decrease) 2004
	$	$	$		
Cash flows relating to operating activities	**63,785**	185,100	71,697	**(65.5)**	158.2
Cash flows relating to investing activities	**(18,600)**	(32,970)	(4,275)	**43.6**	(671.2)
Cash flows relating to financing activities	**(37,975)**	(32,702)	(56,278)	**(16.1)**	41.9
Net change in cash and cash equivalents	**7,210**	119,428	11,144	**(94.0)**	971.7

The above table summarizes the cash flow activity and should be read in conjunction with the audited Consolidated Statements of Cash Flows.

As at October 31, 2005, cash and cash equivalents totalled $293.5 million, compared with $310.9 million in 2004. Cash and cash equivalents in trust or otherwise reserved amounted to $182.3 million at the end of fiscal 2005, compared with $157.7 million in 2004. Our balance sheet included $225.8 million in working capital, or a ratio of 1.6, compared with $204.3 million in 2004, or a ratio of 1.5. As regards our French operations, we also have access to unused lines of credit totalling €11.8 million ($16.7 million).

Total assets increased by $111.1 million, or 13.3%, rising from $838.4 million as at October 31, 2004 to $949.5 million. This increase was primarily due to the adoption of AcG-15, effective November 1, 2004. Shareholders' equity increased by $51.2 million, rising from $311.1 million as at October 31, 2004 to $362.3 million as at October 31, 2005, due mainly to the $55.4 million in net income generated in the current year.

Operating activities

During the year, cash flows of $63.8 million were generated from operating activities, a decrease of $121.3 million compared with 2004. This decrease was primarily due to the lower margins generated during the year, as well as to the decrease in the net change in working capital balances related to operations. In 2004, the net change in working capital balances related to operations was greater, primarily due to higher credit balances, charges payable and income tax payable, compared with 2003.

We expect to continue to generate positive cash flows from our operating activities in 2006.

Investing activities

During the year, cash flows used for investing activities decreased by $14.4 million to $18.6 million, compared with $33.0 million in 2004. This decrease was primarily due to cash inflows resulting from the disposal of property, plant and equipment and of our investment in Star.

In 2006, we expect that capital asset acquisitions will total between $35.0 million and $40.0 million.

Financing activities

During the year, cash flows of $38.0 million were used for financing activities, a $5.3 million increase compared with 2004. This increase was primarily due to the higher value of share redemptions during fiscal 2005 (compared with 2004), offset in part by lower repayments in regard to long-term debt capital lease obligations and debentures, compared with 2004.

On January 3, 2006, we completed our issuer bid (discussed elsewhere in this MD&A). Completion of this bid required an outlay of $125.0 million.

Off-balance sheet arrangements

In the normal course of business, Transat enters into arrangements and incurs obligations that will impact its future operations and liquidity. Some of these obligations are reflected as liabilities in the Consolidated Financial Statements at year-end. Total debt obligations amounted to $106.8 million as at October 31, 2005 (compared with $33.2 million in 2004). Obligations not reflected as liabilities are considered off-balance sheet arrangements. These contractual arrangements are entered into with non-consolidated entities and are made up of:

- Guarantees (see notes 9 and 20 to the audited Consolidated Financial Statements)
- Operating leases (see note 20 to the audited Consolidated Financial Statements)

The 2005 off-balance sheet debt that can be estimated was approximately $356.6 million as at October 31, 2005 (down from $503.5 million in 2004) and can be reconciled as follows:

[in thousands of dollars]

	2005	2004
	$	$
Guarantees		
Irrevocable letters of credit *[notes 8 and 20]*	**17,238**	17,663
Security contracts *[note 20]*	**1,260**	1,045
Operating leases		
Commitments under operating leases *[note 19]*	**338,115**	415,832
Guaranteed residual value	**—**	68,992
Total	**356,613**	503,532

Guarantees are required in the normal course of business in the travel industry to provide indemnifications to counterparties in transactions such as operating leases, irrevocable letters of credit and security contracts. Thus far, Transat has made no significant payments under such guarantees. Operating leases are entered into to enable us to lease certain items, rather than acquiring them. The adoption of AcG-15 on November 1, 2004, resulted in a $101.8 million decrease in our off-balance sheet debt.

We believe that we will be able to meet our obligations from existing funds, operating cash flows and borrowings under existing credit facilities.

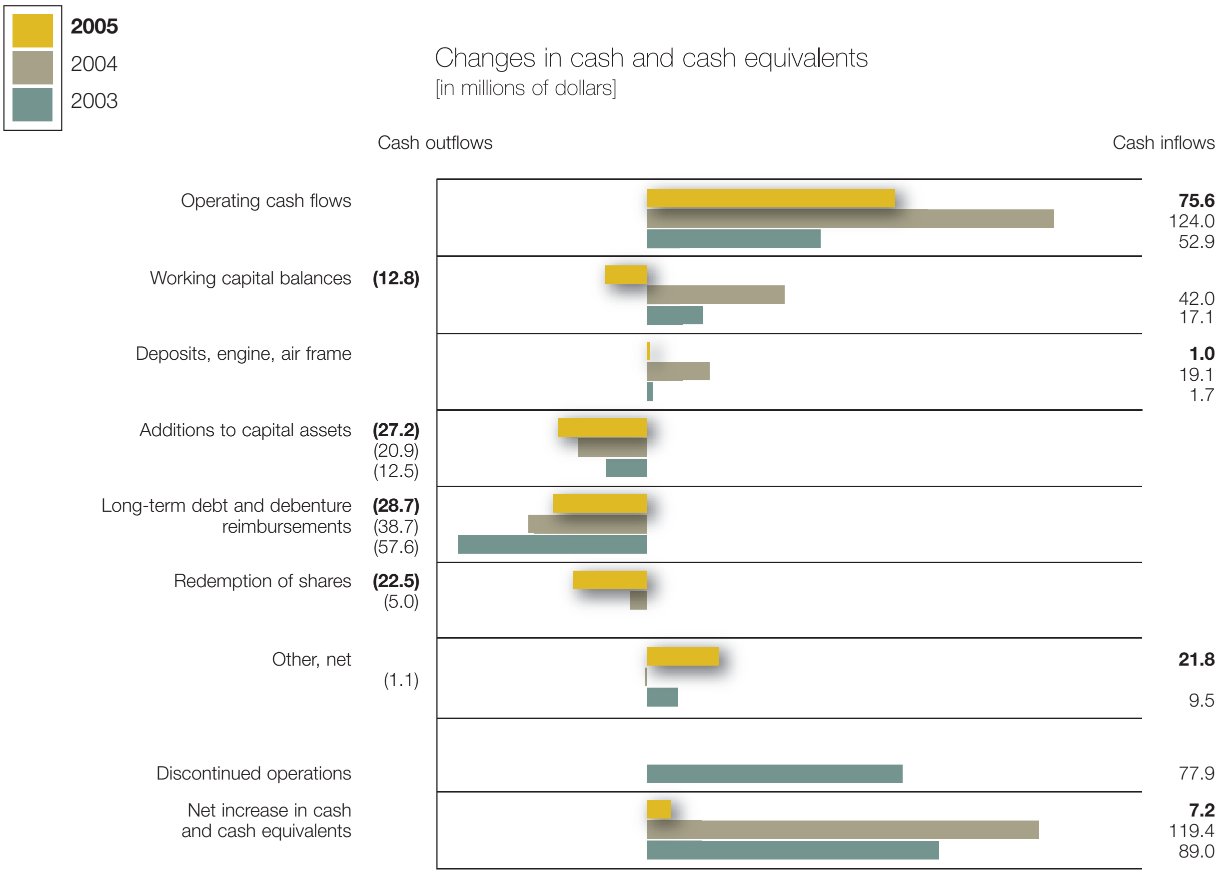
Contractual obligations

Payments due by period

Years ending October 31 [in thousands of dollars]

Contractual obligations	2006 $	2007 $	2008 $	2009 $	2010 $	2011 and thereafter $	Total $
Debentures	10,000	—	—	3,156	—	—	13,156
Obligations under capital leases	6,199	6,968	80,446	—	—	—	93,613
Operating leases (aircraft)	50,140	50,370	49,664	43,036	22,919	11,910	228,039
Operating leases (other)	18,464	13,294	10,169	7,479	4,535	56,135	110,076
Total	**84,803**	**70,632**	**140,279**	**53,671**	**27,454**	**68,045**	**444,884**

The above table summarizes the Corporation's obligations and commitments to make future payments under contracts, including obligations under capital leases, other leases and debentures. For further information, see notes 9, 10 and 19 to the audited Consolidated Financial Statements.



Other

Normal course issuer bid

On June 8, 2005, the Board of Directors of Transat filed a notice to extend the normal course issuer bid for a 12-month period; the bid was originally scheduled to expire on June 14, 2005. In the notice, the Corporation stated its intention to purchase for cancellation up to a maximum of 3,935,000 Class A Variable Voting Shares and Class B Voting Shares, representing 10% of the public float of Class A Variable Voting Shares and the Class B Voting Shares held by the public. As at June 3, 2005, there were 7,970,922 Class A Variable Voting Shares and 32,602,040 Class B Voting Shares issued and outstanding, of which 39,351,600 Class A Variable Voting Shares and Class B Voting Shares represent the public float.

This program is designed to allow the Corporation to purchase Class A Variable Voting Shares and Class B Voting Shares in the normal course of business, i.e., when the Corporation estimates that the Class A Variable Voting Shares and Class B Voting Shares are undervalued by the market

These purchases are to be made via the Toronto Stock Exchange in accordance with its policy on normal course issuer bids. The price the Corporation will pay for any Class A Variable Voting Shares and Class B Voting Shares will be the market price at the time of acquisition, plus brokerage fees. Purchases began on June 15, 2004 and will end no later than June 14, 2006.

During the year, 1,081,100 voting shares, made up of Class A Variable Voting Shares and Class B Voting Shares, were purchased for cancellation for a cash consideration of $22.5 million.

Subsequent events

On November 14, 2005, the Corporation announced an offer to purchase its Class A Variable Voting Shares and Class B Voting Shares for cancellation. A maximum of 7,142,857 shares, or approximately 18% of the 40,156,450 Class A Variable Voting Shares and Class B Voting Shares issued and outstanding, could have been purchased at a price of at least $17.50 per share but no more than $20.00 per share, for a maximum total consideration of $125.0 million. This offer expired on December 22, 2005.

In accordance with its offer, the Corporation redeemed, on January 3, 2006, a total of 6,443,299 voting shares, consisting of 1,780,797 Class A Variable Voting Shares and 4,662,502 Class B Voting Shares, for a cash consideration of $125.0 million.

On December 1, 2005, the Corporation acquired the assets of 20 travel agencies operating in France and belonging to the Carlson Wagonlit Travel network for a total cash consideration of €2.9 million ($4.0 million).

Appointments

In May 2005, François Laurin was appointed Vice-President, Finance and Administration and Chief Financial Officer. Both positions had previously been held by Nelson Gentiletti, who was named Executive Vice-President of Transat Tours Canada in August 2004.

Financial instruments

In the normal course of business, the Corporation is exposed to risks related to certain exchange rate and fuel price fluctuations. These risks are managed by entering into various financial instruments. Management is responsible for determining acceptable levels of risk and only uses financial instruments to hedge existing commitments or obligations, not to realize a profit on trading activities.

Credit risk related to financial instruments

The theoretical risk to which we are exposed in relation to financial instruments is limited to the replacement cost of contracts at market rates in the event of counterparty default. Management is of the opinion that the credit risk related to financial instruments is adequately managed because we only enter into agreements with large financial institutions and multinational companies with appropriate credit ratings.

Management of fuel price and foreign exchange rate risks

We entered into fuel purchasing contracts to manage fuel price fluctuation risks. To manage foreign exchange risks, we also entered into foreign exchange forward contracts expiring in less than one year for the purchase and sale of foreign currencies.

Credit risk

We believe we are not exposed to significant concentrations of credit risk. Cash and cash equivalents are invested on a diversified basis in investment grade corporations. Accounts receivable generally arise from the sale of vacation packages to individuals through retail travel agencies and the sale of seats to tour operators, which are dispersed over a wide geographic area.

Fair value of financial instruments presented on the balance sheets

Due to their short-term nature, the carrying amount of current financial assets and liabilities reflected on the consolidated balance sheets approximates their fair value.

Due to their specific nature, the carrying value of obligations under capital leases presented in the consolidated balance sheets approximates their fair value.

The fair value of the debentures could not be determined with sufficient reliability due to their specific nature.

Note 21 to the audited Consolidated Financial Statements for the year ended October 31, 2005 (included in this 2005 Annual Report) contains additional information on financial instruments.

Related parties

In the normal course of business, we enter into transactions with related companies. These transactions are measured at the exchange amount, which corresponds to the amount of consideration determined and agreed to by the related parties.

As a result of the disposal of our investment in Star, we have no material transactions or balances with related parties.

Critical accounting estimates

Preparing financial statements in accordance with GAAP requires management to make certain estimates. We periodically review these estimates, which are based on historical experience, changes in the business environment and other factors that management considers reasonable under the circumstances. Our estimates involve judgements we make based on the information available to us. Actual results may differ materially from these estimates.

In the discussion below, we have identified a number of critical accounting estimates that required us to make assumptions about matters that were highly uncertain at the time the estimates were made. Our results, financial position and cash flows might have been substantially different if we had used different estimates in the current period or if these estimates were likely to change in the future.

This discussion addresses only those estimates that we consider important based on the degree of uncertainty and the likelihood of a material impact if we had used different estimates. There are many other areas in which we use estimates about uncertain matters.

Aircraft maintenance/Provision for engine and airframe overhaul

We provide for aircraft engine and airframe overhaul expenses based on an estimate of expected future costs until the expiry of the leases for these aircraft, or on an estimate of their remaining useful lives if they are owned. These expenses are amortized over the total number of engine cycles and the total number of months anticipated over the same periods. They are charged to income based on the number of engine cycles or the number of months recorded during the year, via amortization of the capitalized overhaul costs or via a provision for future costs, as the case may be. Any changes in demand for air travel or in the economy as a whole, or any additional actions by management, could alter the factors used to estimate this provision. This may result in charges that could materially affect our results, financial position and cash flows. In general, the main assumptions used to calculate this provision would have to be reduced by approximately 15%, resulting in additional charges that could have a material impact on our results, financial position and cash flows.

Goodwill

We record material balance sheet amounts relating to goodwill based on historical costs. To determine possible goodwill impairment, we are required to review goodwill annually, or more often if events or changes in circumstances so warrant. Our review is based on an asset's ability to generate future cash flows. We carry out an analysis by estimating the discounted future cash flows attributable to each asset; this analysis requires us to make a variety of judgements concerning our future operations. The cash flow forecasts used to determine asset values may change in the future due to market conditions, competition and other factors. Any changes may result in non-cash charges that could materially affect our results and financial position. In general, the main assumptions would have to be reduced by 30%-70% (depending on the operating unit), resulting in a significant loss in value for the operating unit and a material impact on our results and financial position. However, reducing these assumptions would only result in a non-cash charge and would not affect our cash flows.

Property, plant and equipment

Property, plant and equipment on the balance sheet includes material amounts based on historical costs. These assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Our review is based on an asset's ability to generate future cash flows. We carry out an analysis by estimating the net undiscounted future cash flows attributable to each asset; this review requires us to make a variety of judgements concerning our future operations. The cash flow forecasts used to determine asset values may change in the future due to market conditions or other factors. Any changes may result in non-cash charges that could materially affect our results and financial position. In general, the main assumptions would have to be reduced by 60%, resulting in a loss in value and a material impact on our results and financial position. However, reducing these assumptions would not result in cash outlays and would not affect our cash flows.

Accounting changes

During fiscal 2005, we adopted CICA Accounting Guideline 15 (AcG-15), *Consolidation of Variable Interest Entities*, together with the amendments set out in CICA Handbook Section 3861, "Financial Instruments – Disclosure and Presentation."

Effective November 1, 2004, we adopted AcG-15 retroactively, without restatement of prior periods. This new Guideline clarifies the application of consolidation principles to certain entities that are subject to control on a basis other than ownership of voting interests. AcG-15 provides guidance for determining when an enterprise should include a variable interest entity's assets, liabilities and operating results in its Consolidated Financial Statements. As a general rule set out in AcG-15, an enterprise should consolidate a variable interest entity when that enterprise has a variable interest, or a combination of variable interests, that will absorb a majority of the entity's expected losses (if they occur), receive a majority of the entity's expected residual returns (if they occur), or both (the "primary beneficiary").

We have conducted a number of aircraft financing transactions whereby we guaranteed a portion of the residual value at the end of the lease term involving special purpose entities. These entities are considered variable interest entities and we are considered the primary beneficiary. The application of AcG-15 (effective November 1, 2004) resulted in a $12.2 million increase in retained earnings; a $116.0 million increase in property, plant and equipment; and a $103.9 million increase in liabilities, including $101.8 million (US$83.4 million) for obligations under capital leases. Although the application of AcG-15 had no impact on our cash flows, net earnings decreased by $2.0 million and basic earnings per share decreased by $0.05 for the year ended October 31, 2005.

On November 1, 2004, we retroactively adopted the amendments set out in Section 3861, with restatement of prior periods. Under these amendments, certain obligations that must or could be settled by one of the issuer's equity instruments should be presented as liabilities. Previously, the liability and equity components of these obligations were recorded separately. In accordance with these amendments, the balance sheet dated October 31, 2004 was restated to reflect an amount of $2.4 million (pertaining to the equity component of a debenture and originally presented under shareholders' equity), which was reclassified under debentures as a long-term liability. Although the application of these amendments had no impact on retained earnings as at November 1, 2003, net earnings and interest on the equity component of debentures (as presented in the Consolidated Statement of Retained Earnings) for the year ended October 31, 2004 was reduced by $0.1 million. The application of these amendments had no impact on basic earnings per share for these same periods or on cash flows. The application of these amendments had no significant impact on the results for the year ended October 31, 2005.

Future accounting changes

On January 27, 2005, the CICA issued three new accounting standards: Section 1530 ("Comprehensive Income"), Section 3855 ("Financial Instruments – Recognition and Measurement") and Section 3865 ("Hedges"). We will be adopting these standards effective November 1, 2006. We are currently assessing the impact of these new standards on our Consolidated Financial Statements upon initial adoption on November 1, 2006.

Comprehensive income

This new standard describes how comprehensive income (and its components) should be presented. Comprehensive income corresponds to the variation in an enterprise's net assets resulting from transactions, events and circumstances from non-shareholder sources. The main components include unrealized currency translation adjustments arising from a self-sustained foreign operation and fair value adjustments of the effective component of cash flow hedging instruments.

Financial Instruments – Recognition and Measurement

This new standard establishes the timing and method of accounting for financial instruments in the balance sheet. In some cases, fair value may be used; in other cases, a method based on the historical cost may apply. This standard also describes how gains and losses on financial instruments should be presented.

Hedges

Hedge accounting is discretionary. This standard makes it possible for entities to apply accounting treatments other than those set out in Section 3855 ("Financial Instruments – Recognition and Measurement") to eligible transactions that the entities choose to designate (for accounting purposes) as components of a hedging relationship. This new standard adds to Accounting Guideline 13 (AcG-13), *Hedging Relationships*, and Section 1650 ("Foreign Currency Translation") by specifying how hedge accounting may be applied and the related disclosure requirements.

Risks and uncertainties

Economic and general factors

Economic factors such as a significant downturn in the economy, a recession or a decline in the employment rate in North America, Europe or key international markets could have a negative impact on our business and operating results by affecting demand for our products and services. Our operating results could also be adversely affected by more general factors, including the following: extreme weather conditions; war, political instability or terrorism, or any threat thereof; epidemics or disease outbreaks; consumer preferences and spending patterns; consumer perceptions of airline safety; demographic trends; disruptions to air traffic control systems; and costs of safety, security and environmental measures. Furthermore, our revenues are sensitive to events affecting domestic and international air travel as well as the level of car rentals and hotel and cruise reservations.

Competition

We face many competitors in the holiday travel industry. Some of them are larger, with strong brand name recognition and an established presence in specific business areas, substantial financial resources and preferred relationships with travel suppliers. We also face competition from travel suppliers selling directly to travellers at preferential prices. These competitive pressures could adversely impact our revenues and margins since we would likely have to match competitors' prices.

Fluctuations in currency exchange rates and interest rates

We are exposed, by reason of our many arrangements with foreign-based suppliers, to fluctuations in exchange rates between the U.S. dollar, the Canadian dollar and the euro. These fluctuations could increase our costs of operations. Changes in interest rates could also impact our interest income from our cash and cash equivalents and interest expense from variable-rate debt instruments, in turn affecting our earnings. We currently purchase derivative financial instruments to hedge against exchange-rate fluctuations affecting our obligations under capital leases and our off-balance sheet aircraft financing arrangements.

Fuel costs and supply

In particular, Transat is exposed to fluctuations in fuel costs. Due to competitive pressures in the industry, there can be no assurance that we would be able to pass along any increase in fuel prices to our customers by increasing fares, or that any fare increase would offset higher fuel costs, which could in turn adversely impact our business, financial position or operating results. We currently purchase futures contracts to hedge against fuel cost fluctuations. Furthermore, if there were a reduction in the supply of fuel, our operations could be adversely impacted.

Changing industry dynamics: new distribution methods

The widespread popularity of the Internet has resulted in travellers being able to access information about travel products and services and to purchase such products and services directly from suppliers, thereby bypassing not only vacation providers such as Transat, but also retail travel agents through whom we generate a substantial portion of our revenues. To remain competitive, we developed and launched an online booking service (www.exitnow.ca) in Canada several years ago enabling consumers to purchase travel products on line.

In addition, the recent erosion of commissions paid to travel distributors by travel suppliers, particularly airlines, has weakened the financial position of many travel agents. Because we currently rely to some extent on retail travel agencies for access to travellers and revenues, any consumer shift away from travel agencies and toward direct purchases from travel suppliers could have an impact on our operations.

Reliance on contracting travel suppliers

Despite being well positioned due to our vertical integration, we are reliant on travel suppliers to sell our products and services. Furthermore, we are increasingly dependent on non-group airlines to transport our passengers to their vacation destinations. In general, our travel suppliers can terminate or modify existing agreements with us at relatively short notice. The inability to replace these agreements with similar suppliers or to renegotiate agreements at reduced rates could have an adverse effect on our results. Furthermore, any decline in the quality of travel products and services provided by these suppliers, or any perception by travellers of such a decline, could adversely affect our reputation. Any loss of contracts, changes to our pricing agreements, access restrictions to travel suppliers' products and services or negative shifts in public opinion concerning certain travel suppliers and resulting in lower demand for their products and services could have a significant effect on our results.

Dependence on technology

Our business depends on our ability to access information, manage reservation systems (including handling high telephone call volumes on a daily basis) and distribute our products to retail travel agents and other travel intermediaries. To this end, we rely on a variety of information and telecommunications technologies. Rapid changes in these technologies could require higher-than-anticipated capital expenditures to improve or upgrade the level of customer service; this could impact our operating results. In addition, any systems failures or outages could adversely affect our business, customer relationships and operating results.

Dependence on customer deposits and advance payments

Transat derives significant interest income from customer deposits and advance payments. In accordance with our investment policy, we are required to invest these deposits and advance payments exclusively in investment-grade securities. Any failure of these investment securities to perform at historical levels could reduce our interest income.

Negative working capital

Our activities generate customer deposits and advance payments. In the event that the flow of advance payments diminished and Transat were required to find alternative sources of capital, there could be no assurance that such sources would be available at terms and conditions acceptable to us. This could have a significant effect on our business.

Fluctuations in financial results

The travel industry in general and our operations in particular are seasonal. As a result, our quarterly operating results are subject to fluctuations. In our view, quarter-to-quarter comparisons of our operating results are not necessarily meaningful and should not be relied on as indicators of future performance. Furthermore, due to the economic and general factors described above, our operating results in future periods could fall short of the expectations of securities analysts and investors, thus affecting the market price of our shares.

Government regulation and taxation

Transat's future results may vary depending on the steps taken by governmental authorities with jurisdiction over our operations. These steps include the granting and timing of certain governmental approvals or licenses; the adoption of regulations impacting customer service standards (such as new passenger security standards); the adoption of more stringent noise restrictions or curfews; and the adoption of provincial regulations impacting the operations of retail and wholesale travel agencies. In addition, the adoption of new regulatory frameworks (or amendments thereto) or tax policy changes could affect our operations, particularly as regards hotel taxes, car rental taxes, airline excise taxes and airport taxes and fees.

Future capital requirements

Transat may need to raise additional funds in the future to capitalize on growth opportunities or in response to competitive pressures. There can be no assurance that additional financing will be available on terms and conditions acceptable to us. This could adversely affect our business.

Interruption of operations

If our operations are interrupted for any reason (including aircraft unavailability due to mechanical factors), the loss of associated revenues could have an impact on our business, financial position and operating results.

Insurance coverage

In the wake of the terrorist attacks of September 11, 2001, the airline insurance market gave notice that it intended to cancel all aircraft third-party liability coverage for risks associated with war and terrorist acts. Although this notice was subsequently rescinded, the limit on third-party civil liability coverage for bodily injury and property damage was reduced to US$50 million per incident.

Since no commercial market was immediately available to provide airlines with third-party civil liability coverage against war and terrorist acts in excess of US$50 million, it was necessary for individual governments to cover locally-based airlines against this risk until commercial insurance became available at commercially reasonable terms. Both France and Canada covered their air carriers accordingly.

Over the last three and a half years, a commercial market has become available to cover these risks. However, the reasonableness of the terms has been a subject of some discussion, and some market participants are not licensed to transact business in Canada. The Canadian government continues to cover its air carriers, prompted by the licensing situation and by the U.S. government's decision to continue protecting its own carriers against such risks. However, there can be no assurance that the Canadian government will not rescind its coverage, particularly if the U.S. government changes its position.

Casualty losses

We believe that we and our suppliers have adequate liability insurance to cover risks arising in the normal course of business, including claims for serious injury or death arising from accidents involving aircraft or other vehicles carrying our customers. Although we have never faced a liability claim for which we did not have adequate insurance coverage, there can be no assurance that our coverage will be sufficient to cover larger claims or that the insurer concerned will be solvent at the time of any covered loss. In addition, there can be no assurance that we will be able to obtain coverage at acceptable levels and cost in the future. These uncertainties could adversely affect our business and operations.

Slot and gate availability

Access to landing and departure runway slots, airport gates and facilities is critical to our operations and future growth strategy. The availability or cost of these facilities in the future could have a negative effect on our operations.

Aircraft lease obligations

Transat has significant non-cancellable lease obligations relating to its aircraft fleet. If revenues from aircraft operations were to decrease, the payments to be made under our existing lease agreements could have a substantial impact on our operations.

Key personnel

Our future success depends on our ability to attract and retain qualified personnel. The loss of key individuals could adversely affect our business and operating results.

Uncertainty of future collective bargaining agreements

Our operations could be adversely affected in the event of an inability to reach an agreement with a labour union representing our employees, including pilots.

Outlook

Our efforts over the next three years will be focused primarily on driving growth (both from within and via acquisitions), improving our margins and penetrating new markets. We expect to invest nearly $300 million over three years to carry out our development plan.

In North America, the winter season reservation trend is similar to that of last year, despite Hurricane Wilma's impact on the Cancun region and related consumer perceptions. We expect our margins to come under pressure, primarily due to higher fuel prices and increased capacity in certain markets, particularly Ontario.

In Europe, the trend for winter season reservations is higher, compared with 2005.

As a result, we expect that overall margins will be lower in the first half of 2006, compared with the corresponding period in 2005.

North America

[revenues in thousands of dollars]

	2005	2004	2003
Outgoing tour operators and air transportation			
Tour operators under the **Transat Tours Canada*** banner and the airline company **Air Transat**			
** Transat Holidays and Nolitours*			
Revenues ($)	**1,777,000**	1,570,000	1,433,000
Employees	**2,616**	2,500	2,608
Passengers[1]	**2,504,000**	2,394,500	2,571,000
Travellers[2]	**1,140,000**	1,017,500	905,000
Rêvatours			
Revenues ($)	**19,600**	19,000	14,000
Employees	**27**	26	25
Travellers	**7,000**	7,000	5,000
Américanada			
Revenues ($)	**—**	—	20,000
Employees	**—**	—	—
Travel agencies and distribution			
Consultour/Transat Distribution Canada**			
*** Club Voyages, exitnow.ca, TravelPlus and Voyages en Liberté*			
Revenues ($) (commissions and franchise)	**19,500**	19,600	18,100
Outlets owned	**21**	22	27
Employees	**210**	203	225
Outlets franchised	**190**	173	182
Trip Central			
Revenues ($) (commissions)	**2,800**	—	—
Employees	**103**	—	—
Outlets	**16**	—	—
Other airline services			
Handlex			
Revenues ($)	**37,000**	29,000	25,000
Employees	**1,024**	857	861
Incoming tour operators and services at travel destinations			
Jonview Canada***			
**** DMC Transat and Kilomètre Voyages*			
Revenues ($)	**117,300**	108,000	98,000
Employees	**169**	156	159
Travellers	**223,000**	206,000	196,000
Transat Holidays USA			
Revenues ($)	**4,400**	5,300	6,100
Employees	**19**	18	19

Europe

[revenues in thousands of dollars]

	2005	2004	2003
Outgoing tour operators			
Vacances Transat (France)			
Revenues (€)	**128,000**	133,000	102,000
Employees	**187**	177	160
Travellers	**91,000**	95,000	77,000
Look Voyages			
Revenues (€)	**132,000**	179,000	235,000
Employees	**275**	319	409
Passengers	**65,000**	465,000	740,000
Travellers	**129,000**	145,000	140,000
Brok'Air			
Revenues (€)	**24,000**	24,000	26,000
Employees	**18**	14	14
Bennett Voyages			
Revenues (€)	**7,100**	—	—
Employees	**26**	—	—
Travellers	**6,000**	—	—
Travel agencies and distribution			
Club Voyages (France)			
Revenues (€) (commissions)	**8,800**	8,700	8,600
Employees	**170**	167	178
Outlets	**52**	59	63
Anyway			
Revenus (€) (commissions)	**—**	—	8,300
Employees	**—**	—	—
Incoming tour operators and services at travel destinations			
Tourgreece			
Revenues (€)	**19,000**	10,400	—
Employees	**27**	20	—
Travellers	**65,000**	46,000	—
Air Consultants Europe			
Revenues (€) (commissions)	**2,600**	—	—
Employees	**21**	—	—
Travellers	**51,000**	—	—

Transat owns a 100% stake in its subsidiaries listed above with the exception of:
Air Consultants Europe (70.0%)
Jonview Canada (80.07%)
Tourgreece (90.0%)
Trip Central (50.1%).

[1] Airlines record flight segments in terms of passengers.
[2] Tour operators record round-trip travellers.

Management's report and Auditors' report

The consolidated financial statements are the responsibility of management and have been approved by the Board of Directors. Management's responsibility in this respect includes the selection of appropriate accounting principles as well as the exercise of sound judgment in establishing reasonable and fair estimates in accordance with Canadian generally accepted accounting principles which are adequate in the circumstances. The financial information presented throughout this annual report is consistent with that appearing in the financial statements.

The Corporation and its affiliated companies have set up accounting and internal control systems designed to provide reasonable assurance that the Corporation's assets are safeguarded against loss or unauthorized use and that its books of account may be relied upon for the preparation of financial statements.

The Board of Directors is responsible for the consolidated financial statements through its Audit Committee. The Audit Committee reviews the annual consolidated financial statements and recommends their approval to the Board of Directors. The Audit Committee is also responsible for analyzing, on an ongoing basis, the results of the audits by the external auditors of the accounting methods and policies used as well as of the internal control systems set up by the Corporation. These financial statements have been audited by Ernst & Young LLP, the external auditors. Their report on the consolidated financial statements appears opposite.

Jean-Marc Eustache
Chairman of the Board,
President and
Chief Executive Officer

François Laurin
Vice-President, Finance
and Administration
and Chief Financial Officer

To the Shareholders of Transat A.T. Inc.

We have audited the consolidated balance sheets of Transat A.T. Inc. as at October 31, 2005 and 2004 and the consolidated statements of income, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at October 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Ernst & Young LLP
Chartered Accountants

Montréal, Canada
December 16, 2005
[Except as to note 23 (a) which is as of
January 3, 2006]

Consolidated Balance Sheets

As at October 31
[In thousands of dollars]

	2005 $	2004 $ [restated – note 3]
ASSETS		
Current assets		
Cash and cash equivalents	**293,495**	310,875
Cash and cash equivalents in trust or otherwise reserved *[note 4]*	**182,268**	157,678
Accounts receivable	**69,611**	72,745
Future income tax assets	**70**	586
Inventories	**7,524**	4,053
Prepaid expenses	**40,576**	39,729
Current portion of deposits	**29,259**	28,830
Total current assets	**622,803**	614,496
Deposits *[note 5]*	**24,127**	22,111
Future income tax assets *[note 16]*	**5,106**	10,656
Property, plant and equipment *[notes 6 and 15]*	**195,131**	93,128
Goodwill	**93,741**	86,966
Other assets *[note 7]*	**8,629**	11,032
	949,537	838,389
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	**193,277**	202,337
Income taxes payable	**4,763**	29,455
Customer deposits and deferred income	**182,752**	158,396
Debentures *[note 10]*	**10,000**	20,058
Current portion of obligations under capital leases	**6,199**	—
Total current liabilities	**396,991**	410,246
Obligations under capital leases *[note 9]*	**87,414**	—
Debentures *[note 10]*	**3,156**	13,156
Provision for engine and airframe overhaul in excess of deposits	**63,809**	62,818
Non-controlling interest and other liabilities	**30,833**	24,036
Future income tax liabilities *[note 16]*	**5,051**	17,027
	587,254	527,283
Shareholders' equity		
Share capital *[note 11]*	**179,438**	120,306
Convertible debentures *[note 12]*	**—**	51,092
Retained earnings	**183,718**	135,322
Contributed surplus	**531**	118
Warrants *[notes 10 and 11]*	**1,187**	3,994
Deferred translation adjustments	**(2,591)**	274
	362,283	311,106
	949,537	838,389

Commitments and contingencies *[note 19]*

See accompanying notes to consolidated financial statements.

On behalf of the Board:
Jean-Marc Eustache, Director
André Bisson, O.C., Director

Consolidated Statements of Income

Years ended October 31

[In thousands of dollars, except per share amounts]

	2005 $	2004 $ [restated – note 3]
Revenues	**2,364,481**	2,199,822
Operating expenses		
Direct costs	**1,168,612**	1,075,861
Salaries and employee benefits	**241,776**	227,626
Aircraft fuel	**199,376**	128,112
Commissions	**181,587**	179,873
Aircraft maintenance	**91,778**	88,684
Airport and navigation fees	**67,937**	59,379
Aircraft rent	**52,064**	59,640
Other	**240,720**	216,892
	2,243,850	2,036,067
	120,631	163,755
Amortization *[note 13]*	**37,558**	33,027
Restructuring charge *[note 15]*	**(934)**	11,350
Interest on long-term debt, obligations under capital leases and debentures	**10,815**	7,712
Other interest and financial expenses	**1,708**	1,907
Interest income	**(12,963)**	(11,307)
Foreign exchange loss (gain) on long-term monetary items	**(2,309)**	1,474
Gain on disposal of investment *[note 7]*	**(5,747)**	—
Share of net loss (income) of companies subject to significant influence	**(461)**	1,509
	27,667	45,672
Income before the following items	**92,964**	118,083
Income taxes (recovery) *[note 16]*		
Current	**48,705**	34,057
Future	**(12,403)**	10,953
	36,302	45,010
Income before non-controlling interest in subsidiaries' results	**56,662**	73,073
Non-controlling interest in subsidiaries' results	**(1,246)**	(753)
Net income for the year	**55,416**	72,320
Basic earnings per share *[note 11]*	**1.43**	2.07
Diluted earnings per share *[note 11]*	**1.33**	1.76

Consolidated Statements of Retained Earnings

Years ended October 31

[In thousands of dollars]

	2005 $	2004 $ [restated – note 3]
Retained earnings, beginning of year, as previously reported	**135,322**	70,336
Change in accounting policy *[note 3]*	**12,151**	—
Retained earnings, beginning of year	**147,473**	70,336
Net income for the year	**55,416**	72,320
Premium paid on redemption of shares *[note 11]*	**(17,731)**	(4,161)
Interest on equity component of debentures, net of related income taxes of $648 [$1,446 in 2004]	**(1,440)**	(3,173)
Retained earnings, end of year	**183,718**	135,322

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Years ended October 31
[In thousands of dollars]

	2005 $	2004 $ [restated – note 3]
OPERATING ACTIVITIES		
Net income	**55,416**	72,320
Operating items not involving an outlay (receipt) of cash		
Amortization	**37,558**	33,027
Write-off of property, plant and equipment and other assets *[note 15]*	**—**	3,031
Foreign exchange loss (gain) on long-term monetary items	**(2,309)**	1,474
Gain on disposal of investment	**(5,747)**	—
Share of net loss (income) of companies subject to significant influence	**(461)**	1,509
Non-controlling interest in subsidiaries' results	**1,246**	753
Future income taxes	**(12,403)**	10,953
Interest on debentures	**1,807**	827
Compensation expense related to stock option plan	**507**	145
Operating cash flow	**75,614**	124,039
Net change in non-cash working capital balances related to operations	**(12,820)**	41,991
Net change in deposits, expenses and provision for engine and airframe overhaul	**991**	19,070
Cash flows relating to operating activities	**63,785**	185,100
INVESTING ACTIVITIES		
Increase in deposits	**(11,069)**	(12,720)
Repayment of deposits	**8,601**	4,264
Additions to property, plant and equipment	**(27,213)**	(20,902)
Disposal of property, plant and equipment	**5,001**	—
Net change in other assets	**(1,254)**	3,143
Proceeds from disposal of investment	**6,900**	—
Cash and cash equivalents from acquired companies	**9,637**	5,905
Consideration paid for acquired companies	**(9,203)**	(12,660)
Cash flows relating to investing activities	**(18,600)**	(32,970)
FINANCING ACTIVITIES		
Repayment of other long-term debt and obligations under capital leases	**(6,766)**	(36,172)
Interest paid on convertible debentures	**(2,868)**	(4,600)
Proceeds from issuance of shares	**9,988**	9,718
Redemption of shares	**(22,545)**	(4,961)
Proceeds from issuance of a debenture	**—**	3,156
Repayment of debentures	**(21,900)**	(2,500)
Net change in other liabilities	**6,116**	2,657
Cash flows relating to financing activities	**(37,975)**	(32,702)
Net change in cash and cash equivalents	**7,210**	119,428
Cash and cash equivalents, beginning of year	**468,553**	349,125
Cash and cash equivalents, end of year	**475,763**	468,553
Supplementary information		
Income taxes paid	**72,486**	4,739
Interest paid	**6,226**	10,423

See accompanying notes to consolidated financial statements.

1 INCORPORATION AND NATURE OF BUSINESS

Transat A.T. Inc. [the "Corporation"], incorporated under the *Canada Business Corporations Act*, is an integrated company specializing in the organization, marketing and distribution of holiday travel. The core of its business consists of tour operators based in Canada and Europe. The Corporation is also involved in air transportation and value-added services at travel destinations. Finally, the Corporation has secured a dynamic presence in distribution through travel agency networks.

2 SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of the Corporation have been prepared by management in accordance with Canadian generally accepted accounting principles. The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized below.

Basis of consolidation
The consolidated financial statements include the accounts of the Corporation and its subsidiaries.

Cash equivalents
Cash equivalents consist primarily of term deposits, bankers' acceptances and commercial paper that are readily convertible into known amounts of cash with initial maturities of less than three months. These investments are recorded at cost plus accrued interest and their carrying value approximates their fair market value.

Inventories
Inventories are valued at the lower of cost, determined according to the first-in, first-out method, and replacement cost.

Property, plant and equipment
Property, plant and equipment are recorded at cost and are amortized, taking into account their residual value, on a straight-line basis over their estimated useful life as follows:

Property under capital leases	
Aircraft	5 to 6 years
Owned property, plant and equipment	
Hangar and administrative buildings	35 years
Improvements to aircraft under operating leases	Lease term
Aircraft equipment	5 to 10 years
Computer hardware and software	3 to 7 years
Aircraft engines	Cycles used
Office furniture and equipment	4 to 10 years
Leasehold improvements and other	Lease term
Rotable aircraft spare parts	Use

Goodwill
Goodwill represents the excess of the purchase price over the fair value of net assets acquired. Goodwill is tested for impairment annually or more often if events or changes in circumstances indicate that it might be impaired. The impairment test consists of a comparison of the fair value of the reporting unit to which goodwill is assigned with its carrying amount. Any impairment loss in the carrying amount compared with the fair value is charged to income in the year in which the loss is recognized. The Corporation uses the discounted cash flow method to assess the fair value of its reporting units.

Other assets
Other assets consist in particular of development costs and long-term investments.

Development costs are amortized over periods not exceeding five years. Long-term investments over which the Corporation has the ability to exercise significant influence are accounted for using the equity method.

Impairment of long-lived assets
Long-lived assets, excluding goodwill, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment is assessed by comparing the carrying amount of an asset with its expected future net undiscounted cash flows from use together with its residual value [net recoverable value]. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the net recoverable value.

Deposits, expenses and provision for engine and airframe overhaul
The Corporation provides for engine and airframe overhaul expenses for its aircraft based on an estimate of all such future expenses until the expiry of the leases for these aircraft, or for their estimated useful life anticipated for the Corporation while held, amortized over the total number of engine cycles and the total number of months anticipated for the airframe over the same periods.

These expenses are charged to income according to the number of cycles used or over the completed fiscal months, by a provision for future costs or the amortization of the capitalized overhaul costs, as the case may be. Actual results could differ from those estimates and differences could be significant.

The Corporation makes deposits representing a portion of engine and airframe overhaul expenses to certain aircraft lessors. These deposits are usually recoverable upon presentation of claims for eligible overhaul expenses. Amounts so claimed are included in assets as "Accounts receivable." The excess of the provision for future overhaul expenses over deposits made and unclaimed is included in liabilities as "Provision for engine and airframe overhaul in excess of deposits." The unamortized balance related to engine and airframe overhaul expenses is included, if any, in assets as "Deposits."

Foreign currency translation

(a) Self-sustaining foreign operations
The Corporation translates the accounts of its self-sustaining foreign subsidiaries using the current rate method. All assets and liabilities of self-sustaining foreign operations are translated at the exchange rates in effect at year-end. Revenues and expenses are translated at average rates of exchange during the period. Net gains or losses resulting from the translation of assets and liabilities are shown in shareholders' equity.

(b) Accounts and transactions in foreign currencies
The accounts and transactions of the Corporation denominated in foreign currencies are translated using the temporal method. Under this method, monetary items on the balance sheet are translated at the exchange rates in effect at year-end, while non-monetary items are translated at the historical rates of exchange. Revenues and expenses are translated at the rates of exchange on the transaction date or at the average exchange rates for the period. Gains or losses resulting from the translation are included in the consolidated statement of income.

Stock-based compensation plans
The Corporation accounts for its stock option plan for directors, executives and employees, for stock option awards granted after October 31, 2003, using the fair value method. The fair value of stock options at the grant date is determined using an option pricing model. Compensation expense is recognized in income over the vesting period of the stock options.

Prior to November 1, 2003, the Corporation accounted for its stock option plan for directors, executives and employees as capital transactions. Accordingly, the issuance of options did not give rise to compensation expenses. The Corporation disclosed the impact of applying the fair value-based method on pro forma net income and pro forma earnings per share by way of a note to the consolidated financial statements for the awards granted during 2003.

The Corporation's contributions to the stock ownership incentive and capital accumulation plan for officers and the permanent stock ownership incentive plan for senior executives are recognized in income when the shares are awarded. No compensation expense is recognized for the other plans when the shares are issued to directors, executives and employees. Any consideration paid by directors, executives and employees upon purchasing shares is credited to share capital.

A description of the stock-based compensation plans offered by the Corporation is included in note 11.

Revenues
The Corporation recognizes revenues once all the significant risks and rewards of the service have been transferred to the customer. As a result, revenues earned from passenger transportation are recorded upon each return flight. Revenues of tour operators and the related costs are recorded at the time of the departure of the passengers. Commission revenues of travel agencies are recorded at the time of reservation. Amounts received for services not yet rendered are included in current liabilities as "Customer deposits and deferred income."

Financial instruments
The Corporation uses foreign exchange forward contracts to hedge against future currency exchange rate variations related to aircraft operating and capital lease payments, receipts of revenue from certain tour operators and disbursements pertaining to certain operating expenses in other currencies. The gains or losses on contracts designated as hedges resulting from exchange rate variations are recorded in income when the related hedging transactions are realized. The gains or losses on contracts not designated as hedges or that cease being designated as such are recognized at their fair value on the balance sheet and any subsequent change in fair value is recognized in the statement of income.

To protect itself against variations in fuel costs, the Corporation has entered into fuel price hedging contracts. The gains or losses resulting from designated hedge contracts are recorded in fuel costs as purchases of fuel are made.

It is the Corporation's policy not to speculate on financial instruments; thus, these instruments are normally designated as hedges and maintained until maturity according to the primary objective of hedging risks.

Income taxes
The Corporation provides for income taxes using the liability method. Under this method, future income tax assets and liabilities are calculated based on differences between the carrying value and tax bases of assets and liabilities and measured using substantively enacted tax rates and laws expected to be in effect when the differences reverse. A valuation allowance has been recorded to the extent that it is more likely than not that future income tax assets will not be realized.

Employee future benefits
The Corporation offers defined benefit plans to certain members of senior management. The cost of pension benefits earned by employees is determined from actuarial calculations using the projected benefit method prorated on services and management's most likely estimate of expected plan investment performance, salary escalation and the retirement age of employees. Plan obligations are discounted using current market interest rates and are included in "Other liabilities."

Earnings per share
Earnings per share are calculated based on the weighted average number of Class A Variable Voting Shares and Class B Voting Shares outstanding during the year. Diluted earnings per share are calculated using the treasury stock method and take into account all the elements that have a dilutive effect.

3 CHANGES IN ACCOUNTING POLICIES

Consolidation of variable interest entities

On November 1, 2004, the Corporation retroactively adopted, without restatement of prior periods, Accounting Guideline 15, “Consolidation of Variable Interest Entities” [“AcG-15”], issued by the Canadian Institute of Chartered Accountants [“CICA”]. This new Guideline presents clarification on the application of consolidation principles to certain entities that are subject to control on a basis other than ownership of voting interests. AcG-15 provides guidance for determining when an enterprise includes the assets, liabilities and results of activities of a variable interest entity in its consolidated financial statements. As a general rule set out in AcG-15, an enterprise should consolidate a variable interest entity when that enterprise has a variable interest, or combination of variable interests, that will absorb a majority of the entity’s expected losses if they occur, receive a majority of the entity’s expected residual returns if they occur, or both (the “primary beneficiary”).

The Corporation has conducted certain aircraft financing transactions whereby it guaranteed a portion of the residual value at the end of the lease term involving special purpose entities. These entities are considered variable interest entities and the Corporation is considered to be the primary beneficiary thereof. The adoption of AcG-15 resulted in a $12,151 increase in the Corporation’s retained earnings as at November 1, 2004, a $116,009 net increase in property, plant and equipment, and a $103,858 increase in liabilities, including $101,773 [US$83,372] for obligations under capital leases. The adoption of this Guideline had no impact on the Corporation’s cash flows. However, it resulted in a decline of $2,034 in net income for the year ended October 31, 2005 and $0.05 in basic earnings per share.

Debentures

On November 1, 2004, the Corporation retroactively adopted, with restatement of prior periods, the changes contained in CICA Handbook Section 3861, “Financial Instruments – Disclosure and Presentation.” These changes require that certain obligations that must or could be settled with the issuer’s own equity instruments be presented as liabilities. Previously, the liability and equity components related to these obligations had to be accounted for separately. The adoption of these changes resulted in the reclassification on the balance sheet as at October 31, 2004, of $2,422 of the equity component of a debenture, presented in shareholders’ equity, and now presented under debentures in long-term liabilities. The adoption of these changes had no impact on retained earnings as at November 1, 2003, but resulted in a $131 decline in net income and interest expense related to the equity component of debentures, presented in the consolidated statement of retained earnings for the year ended October 31, 2004. These changes had no impact on basic earnings per share or on cash flows for the year ended October 31, 2004. The adoption of these changes had no material effect on the results for the year ended October 31, 2005.

Stock-based compensation and other stock-based payments

On November 1, 2003, the Corporation adopted prospectively the amended CICA Handbook Section 3870, “Stock-Based Compensation and Other Stock-Based Payments.” The amendments require that the fair value-based method be applied to awards granted to employees and that a compensation charge be accounted for. Enterprises are required to account for the effect of such awards in their financial statements for fiscal years beginning on or after January 1, 2004. Retroactive, with or without restating prior periods, or prospective application is allowed. However, prospective application is only available to enterprises that elect to apply the fair value-based method of accounting for fiscal years beginning before January 1, 2004. The adoption of these amendments resulted in a reduction in net income for the year ended October 31, 2004 of $145 and a decrease in basic earnings per share of $0.01.

Hedging relationships

On November 1, 2003, the Corporation adopted CICA Accounting Guideline 13, “Hedging Relationships” [“AcG-13”]. AcG-13 addresses the identification, designation, documentation and effectiveness of hedging relationships for hedge accounting purposes. In addition, it deals with the discontinuance of hedge accounting and establishes conditions for applying hedge accounting. Under the new Guideline, an enterprise is required to document its hedging relationships and explicitly demonstrate that the hedges are sufficiently effective in order to continue accrual accounting for positions hedged with derivatives. In accordance with the Guideline, gains and losses related to derivatives designated as eligible for hedge accounting are booked in the statement of income in the same period as for the hedged item. Derivatives that are no longer eligible for hedge accounting are recorded at their fair value on the balance sheet and any subsequent changes in fair value are recorded in the statement of income. The adoption of this Guideline had no impact on the Corporation’s results, financial position or cash flows.

4 CASH AND CASH EQUIVALENTS IN TRUST OR OTHERWISE RESERVED

As at October 31, 2005, cash and cash equivalents in trust or otherwise reserved included $140,675 [$118,146 as at October 31, 2004] in funds received from customers for services not yet rendered and $41,593 [$39,532 as at October 31, 2004] was pledged as collateral security against letters of credit and foreign exchange forward contracts *[note 18]*.

For its Canadian operations, the Corporation has a revolving credit facility renewable annually amounting to $60,000. Under the terms and conditions of the agreement, funds may be drawn by issuing letters of credit. As at October 31, 2005, letters of credit had been issued for a total of $39,613 [$28,679 as at October 31, 2004], thereby reducing the undrawn balance of the revolving term credit facility by the same amount.

5 DEPOSITS

	2005 **$**	2004 $
Deposits on leased aircraft and engines	**10,125**	10,473
Deposits with suppliers	**43,261**	40,468
	53,386	50,941
Less current portion	**29,259**	28,830
	24,127	22,111

6 PROPERTY, PLANT AND EQUIPMENT

	2005		2004	
	Cost **$**	**Accumulated amortization** **$**	Cost $	Accumulated amortization $
Property under capital leases				
Aircraft	**150,937**	**47,579**	—	—
	150,937	**47,579**	—	—
Owned property, plant and equipment				
Hangar and administrative buildings	**844**	**339**	7,640	2,302
Improvements to aircraft under operating leases	**23,643**	**10,015**	19,214	6,108
Aircraft equipment	**35,669**	**29,079**	33,750	26,160
Computer hardware and software	**87,106**	**63,436**	70,633	50,082
Aircraft engines	**20,358**	**6,482**	20,358	5,151
Office furniture and equipment	**24,531**	**18,439**	20,855	16,096
Leasehold improvements and other	**21,432**	**11,674**	18,367	10,411
Rotable aircraft spare parts	**25,118**	**7,464**	24,139	5,518
	238,701	**146,928**	214,956	121,828
	389,638	**194,507**	214,956	121,828
Accumulated amortization	**194,507**		121,828	
Net book value	**195,131**		93,128	

7 OTHER ASSETS

	2005 $	2004 $
Deferred costs, unamortized balance	**4,380**	6,220
Investments in companies subject to significant influence and other investments	**1,071**	2,186
Miscellaneous	**3,178**	2,626
	8,629	11,032

On February 1, 2004, the Corporation ceased being able to exercise significant influence over Star Airlines S.A. ["Star"]. As a result, the investment in Star has been carried at its carrying value as of that date. In addition, accumulated dividends received by the Corporation subsequent to February 1, 2004 that exceed the Corporation's share of the earnings previously realized by Star were applied against its carrying value. During the year ended October 31, 2004, the Corporation received a dividend amounting to €880 [$1,416] of which €694 [$1,116] was recorded in income and €186 [$300] was applied against the investment in Star. Previously, the investment was accounted for using the equity method.

On June 6, 2005, the Corporation sold its 44.27% ownership interest in Star for a cash consideration of €4,500 [$6,900], subject to approval by authorities in France. On August 5, 2005, the French authorities approved the transaction and, as a result, the Corporation accounted for a $5,747 gain on that date.

8 BANK LOANS

Operating lines of credit totalling €11,800 [$16,702] [€8,665 [$13,485] in 2004] have been authorized for certain French subsidiaries. These operating lines of credit are renewable annually and were unused as at October 31, 2005 and 2004. For the year ended October 31, 2004, operating lines of credit bore interest at an average rate of 2.8%.

For its European operations, the Corporation has guarantee facilities renewable annually amounting to €17,793 [$25,184] [€14,756 [$22,965] in 2004]. As at October 31, 2005, letters of guarantee had been issued totalling €11,906 [$16,851] [€11,192 [$17,418] in 2004].

9 OBLIGATIONS UNDER CAPITAL LEASES

	2005 $	2004 $
Obligations totalling US$57,828 related to aircraft, maturing in 2008	**68,243**	—
Obligations totalling US$20,311 related to an aircraft, maturing in 2007	**23,969**	—
Other	**1,401**	—
	93,613	—
Less current portion	**6,199**	—
	87,414	—

Obligations under capital leases related to aircraft were determined using the LIBOR rate plus 2.1% to 3.7%.

Future minimum lease payments total $109,052, including interest amounting to $15,439, and are as follows for the next three years: 2006 – $13,590; 2007 – $33,308 and 2008 – $62,154.

10 DEBENTURES

(a) The $10,000 debenture of the subsidiary Transat Tours Canada Inc. ["Transat Tours"] bears interest at 17.5% and matures on November 1, 2005. The debenture is repayable at the option of Transat Tours at a price such that the holder earns a compound annual return of 20.5% from its issuance on November 1, 1995, taking into consideration annual interest already paid and recorded at a rate of 17.5%. The debenture, if not redeemed, is convertible into 25% of the common shares of Transat Tours.

The debenture is collateralized by certain intercorporate guarantees and by a movable hypothec on the shares of a number of the Corporation's subsidiaries and on all of the tangible assets of the subsidiary Air Transat A.T. Inc. ["Air Transat"] and of Transat Tours. Should the Corporation be subject to a takeover bid, the lender has the option to acquire all of the outstanding shares of Transat Tours at a price determined under an agreed formula.

On November 1, 2005, Transat Tours redeemed the $10,000 debenture.

(b) In September 2001, a subsidiary of the Corporation issued a debenture in the amount of $2,500 bearing interest at a rate of 8.25%. The debenture was repayable in one instalment in September 2009 in cash or shares of the Corporation at the Corporation's option. The debenture was also repayable in advance at the subsidiary's option as of September 2004 in return for a premium whereby the holder would earn a return of 11.25% from its issuance, taking into consideration annual interest already paid and recorded at a rate of 8.25%. On September 8, 2004, the subsidiary redeemed the debenture in advance in accordance with the terms thereof.

(c) On January 10, 2002, the Corporation and Air Transat issued debentures to certain shareholders and executives of the Corporation in the amount of $21,865, bearing interest at a rate of 6% and maturing in January 2009. The debentures are redeemable in advance as of January 2005 in return for payment of a penalty equal to three months' interest. The Corporation and Air Transat must also pay the holders a premium at maturity, upon advance redemption or at conversion, such that the holders would earn a compound annual return of 15%, taking into consideration interest already paid at a rate of 6%.

In the course of this financing, the Corporation issued 1,421,225 warrants entitling the holders to subscribe to the same number of Class B Voting Shares of the Corporation at an exercise price of $6.75 each. These warrants expire on January 10, 2007.

On January 10, 2005, the Corporation redeemed these debentures with a nominal value of $21,865 in advance. The early redemption resulted in a total payment of $30,009, including accrued interest amounting to $7,324 and an $820 penalty, which was recorded at redemption. Furthermore, this early redemption resulted in an additional non-cash charge at the redemption date of $1,644 corresponding to the difference between the nominal value of the debentures and their carrying amount at that time.

(d) On April 6, 2004, a subsidiary of the Corporation issued a debenture in the amount of $3,156, bearing interest at a rate of 6%. The debenture is repayable in one instalment in September 2009 in cash or shares of the Corporation at the Corporation's option. The debenture is also redeemable in advance at the subsidiary's option as of April 2007 in return for a premium whereby the holder would earn a return of 9% from its issuance, taking into consideration annual interest already paid and recorded at the rate of 6%.

11 SHARE CAPITAL

Authorized

Class A Variable Voting Shares

An unlimited number of Class A Variable Voting Shares ["Class A Shares"], participating, which may be owned or controlled by non-Canadians as defined by the *Canada Transportation Act* ["CTA"], carrying one vote per Class A Share unless (i) the number of issued and outstanding Class A Shares exceeds 25% of the total number of all issued and outstanding voting shares (or any higher percentage that the Governor in Council may specify pursuant to the CTA); or (ii) the total number of votes cast by or on behalf of holders of Class A Shares at any meeting exceeds 25% (or any higher percentage that the Governor in Council may specify pursuant to the CTA) of the total number of votes that may be cast at such meeting.

If either of the above-noted thresholds is surpassed, the vote attached to each Class A Share will decrease automatically, without further act or formality. Under the circumstance described in subparagraph (i) above, the Class A Shares as a class cannot carry more than 25% (or any higher percentage that the Governor in Council may specify pursuant to the CTA) of the aggregate votes attached to all issued and outstanding voting shares of the Corporation. Under the circumstance described in subparagraph (ii) above, the Class A Shares as a class cannot, for a given shareholders' meeting, carry more than 25% (or any higher percentage that the Governor in Council may specify pursuant to the CTA) of the total number of votes that can be exercised at the said meeting.

Each issued and outstanding Class A Share shall be automatically converted into one Class B Voting Share without any further act on the part of the Corporation or of the holder if (i) the Class A Share is or becomes owned and controlled by a Canadian as defined by the CTA; or (ii) the provisions contained in the CTA relating to foreign ownership restrictions are repealed and not replaced with other similar provisions.

Class B Voting Shares
An unlimited number of Class B Voting Shares ["Class B Shares"], participating, which may be owned and controlled by Canadians as defined by the CTA only and shall confer the right to one vote per Class B Share at all meetings of shareholders of the Corporation.

Each issued and outstanding Class B Share shall be converted into one Class A Share automatically without any further act on the part of the Corporation or the holder if the Class B Share is or becomes owned or controlled by a non-Canadian as defined by the CTA.

Preferred shares
An unlimited number of preferred shares, non-voting, issuable in series, each series bearing the number of shares, designation, rights, privileges, restrictions and conditions as determined by the Board of Directors.

Issued and outstanding
On March 4, 2005, the Corporation's common shares were restructured into two classes of shares: Class A Shares and Class B Shares. Each issued and outstanding share that was not owned or controlled by a Canadian as defined by the CTA was converted into one Class A Share of the share capital of the Corporation and cancelled. Each issued and outstanding share owned and controlled by a Canadian as defined by the CTA was converted into one Class B Share of the share capital of the Corporation and cancelled. Immediately following the conversion, the number of Class A Shares and Class B Shares amounted to 7,818,212 and 27,228,227 respectively. The unissued common shares of the Corporation were cancelled and the Class A Shares and Class B Shares were substituted for the exercise of all rights to subscribe, purchase or convert the common shares thus cancelled.

The changes affecting the Class A Shares and the Class B Shares were as follows:

	Number of shares	$
Balance as at October 31, 2003	32,863,553	111,247
Issued from treasury	44,047	602
Exercise of options	1,231,541	8,817
Conversion of warrants	44,200	427
Conversion of debentures	1,484	13
Repurchase and cancellation of shares	(230,000)	(800)
Balance as at October 31, 2004	33,954,825	120,306
Issued from treasury	23,102	477
Exercise of options	456,992	3,074
Conversion of warrants	967,550	9,338
Conversion of debentures	5,835,081	51,057
Repurchase and cancellation of shares	(1,081,100)	(4,814)
Balance as at October 31, 2005	**40,156,450**	**179,438**

As at October 31, 2005, the number of Class A Shares and Class B Shares amounted to 7,598,306 and 32,558,144 respectively.

Normal course issuer bid

On June 13, 2005, the Corporation renewed its normal course issuer bid, which began on June 15, 2004, for a 12-month period. With this renewal, the Corporation intends to purchase for cancellation up to a maximum of 3,935,000 Class A Shares and Class B Shares, representing less than 10% of the issued and outstanding Class A Shares and Class B Shares at the offer date [1,662,847 common shares representing 5% of the issued and outstanding common shares as at June 15, 2004]. Shares are purchased at market prices plus brokerage fees.

In accordance with its normal course issuer bid, the Corporation redeemed, during the year ended October 31, 2005, a total of 1,081,100 voting shares, consisting of Class A Shares and Class B Shares, for a cash consideration of $22,545 [230,000 common shares for a cash consideration of $4,961 in 2004].

Subscription rights plan

At the annual meeting held on April 27, 2005, the shareholders ratified the renewal, by the Corporation, of a shareholders' subscription rights plan ["rights plan"]. The rights plan entitles holders of Class A and Class B Shares to acquire, under certain conditions, additional shares at a price equal to 50% of their market value at the time the rights are exercised. The rights plan is designed to give the Board of Directors time to consider offers, thus allowing shareholders to receive full and fair value for their shares. The rights plan will terminate at the annual shareholders' meeting in 2008, unless it is terminated earlier by the Corporation's Board of Directors.

Share purchase plan

A share purchase plan is available to eligible employees of the Corporation and its subsidiaries. Under the plan, as at October 31, 2005, the Corporation was authorized to issue up to 649,875 Class B Shares. The plan allows each eligible employee to purchase shares for a subscription limit up to 10% of his or her annual salary in effect at the time of the subscription. The purchase price of the shares under the plan is equal to the weighted average price of the Class B Shares during the five trading days prior to the issue of the shares, less 10%.

During the year, the Corporation issued 23,102 Class B Shares [44,047 common shares in 2004] for a total of $477 [$602 in 2004] under the share purchase plan.

Stock ownership incentive and capital accumulation plan

Subject to participation in the share purchase plan offered to all eligible employees of the Corporation, the Corporation attributes annually to each eligible officer a number of Class B Shares, the aggregate subscription price of which is equal to an amount ranging from 25% to 50% of the maximum percentage of salary contributed, which may not exceed 4% thereof. Shares so attributed by the Corporation will vest gradually to the eligible officer, subject to the eligible officer's retaining, during the first six months of the vesting period, all the shares subscribed for under the Corporation's share purchase plan.

Permanent stock ownership incentive plan

Subject to participation in the share purchase plan offered to all eligible employees of the Corporation, the Corporation attributes annually to each eligible senior executive a number of Class B Shares, the aggregate subscription price of which is equal to the maximum percentage of salary contributed, which may not exceed 10% thereof. Shares so attributed by the Corporation will vest gradually to the eligible senior executive, subject to the senior executive's retaining, during the vesting period, all the shares subscribed for under the Corporation's share purchase plan.

Stock option plan

Options are granted under a stock option plan for directors, executives and employees. Under the plan, as at October 31, 2005, the Corporation may grant 1,034,296 additional Class A or Class B Shares to eligible persons at a share price equal to the weighted average price of the shares during the five trading days prior to the granting of the options. Options granted may be exercised during a ten-year period subject to a maximum of one-third during the first two years after the grant date, an additional third in the third year and a final third after the start of the fourth year. The tables below summarize all outstanding options:

	2005		2004	
	Number of options	**Weighted average price $**	Number of options	Weighted average price $
Beginning of the year	**1,125,678**	**7.69**	2,281,666	6.75
Granted	**127,383**	**22.27**	171,500	16.06
Exercised	**(456,992)**	**6.52**	(1,231,541)	7.14
Cancelled	**—**	**—**	(95,947)	7.33
End of the year	**796,069**	**10.69**	1,125,678	7.69
Options exercisable at the end of the year	**369,947**	**10.19**	455,461	9.20

2005

	Outstanding options			**Exercisable Options**	
Range of exercise prices $	**Number of outstanding options as at October 31, 2005**	**Weighted average remaining life**	**Weighted average price $**	**Number of options exercisable as at October 31, 2005**	**Weighted average price $**
3.00 to 4.50	261,783	7.5 years	3.81	54,727	3.82
4.51 to 6.00	3,333	7.0 years	5.80	3,333	5.80
6.01 to 7.50	81,039	5.9 years	6.89	81,039	6.89
7.51 to 9.00	30,706	4.5 years	7.97	30,706	7.27
9.01 to 11.50	133,865	5.4 years	9.81	118,865	9.85
15.68 to 22.34	285,343	9.0 years	18.85	81,277	19.29
	796,069		10.69	369,947	10.19

Compensation expense related to stock option plan

During the year ended October 31, 2005, the Corporation granted 127,383 [171,500 in 2004] stock options to certain key employees and to its directors. The average fair value of each option granted was estimated on the date of grant using the Black-Scholes option pricing model. The assumptions used and the weighted average fair value of the options on the date of grant are as follows:

	2005	2004
Risk-free interest rate	**4.12%**	4.82%
Expected life	**6 years**	6 years
Expected volatility	**54.7%**	56%
Dividend yield	**—**	—
Weighted average grant-date fair value	**$22.27**	$8.99

During the year ended October 31, 2005, the Corporation recorded a compensation expense of $507 [$145 in 2004], of which $95 [$27 in 2004] was recorded in share capital subsequent to the exercise of options.

Pro forma disclosure of fair value of stock options

Prior to November 1, 2003, the Corporation accounted for options granted under its stock option plan as capital transactions. The following table shows what the impact on the financial statements would have been had the Corporation recorded the options granted between November 1, 2002 and October 31, 2003 using the fair value method. The pro forma figures do not take into account stock options granted prior to November 1, 2002.

	2005 **$**	2004 $ [restated – note 3]
Net income	**55,416**	72,320
Adjustment – stock-based compensation	**(292)**	(291)
Pro forma net income	**55,124**	72,029
Pro forma basic earnings per share	**1.42**	2.06
Pro forma diluted earnings per share	**1.33**	1.75

The assumptions used and the weighted average fair value of the options on the date of grant for the year ended October 31, 2003 are as follows:

Risk-free interest rate	4.73%
Expected life	6 years
Expected volatility	55%
Dividend yield	—
Weighted average grant-date fair value	$2.09

Warrants

On January 10, 2002, the Corporation granted 1,421,225 warrants *[note 10 (c)]*. As at October 31, 2005, the balance of the warrants amounted to 409,475 [1,377,025 as at October 31, 2004] and 967,550 warrants were exercised during the year [44,200 in 2004].

Basic earnings per share and diluted earnings per share were computed as follows:

[In thousands, except per share amounts]	**2005** **$**	2004 $ [restated – note 3]
NUMERATOR		
Net income	**55,416**	72,320
Interest on convertible debentures	**(1,440)**	(3,173)
Income attributable to voting shareholders	**53,976**	69,147
Interest on convertible debentures	**1,440**	3,173
Interest on debentures that may be settled in voting shares	**129**	95
Income used to calculate diluted earnings per share	**55,545**	72,415
DENOMINATOR		
Weighted average number of outstanding shares	**37,863**	33,374
Effect of dilutive securities		
Convertible debentures	**2,668**	5,841
Debentures that may be settled in voting shares	**135**	211
Stock options	**612**	918
Warrants	**406**	812
Adjusted weighted average number of outstanding shares used in computing diluted earnings per share	**41,684**	41,156
Basic earnings per share	**1.43**	2.07
Diluted earnings per share	**1.33**	1.76

12 CONVERTIBLE DEBENTURES

On February 19, 2002, the Corporation issued $51,105 of convertible unsecured subordinated debentures maturing on March 1, 2007. The debentures bore interest at 9%, payable semi-annually in cash or in common shares of the Corporation, at its option. The debentures were convertible into common shares of the Corporation, at a conversion price of $8.75 per share, at the holder's option at any time. During the year ended October 31, 2004, debentures totalling $13 were converted into 1,484 common shares of the Corporation.

On or after March 1, 2005 and prior to March 1, 2006, the debentures were redeemable at par by the Corporation provided its common shares were traded at a price of $10.94 or more for 20 consecutive trading days before the notice of redemption. After March 1, 2006, the debentures were redeemable at par. The Corporation had the option to repay the debentures, in whole or in part, in cash or by delivering a number of common shares obtained by dividing the principal amount of the debentures by 95% of the market price of the Corporation's shares at the redemption date or at maturity.

The Corporation, under its normal course issuer bid that started on June 15, 2004 *[see note 11]*, was entitled to repurchase and cancel up to a maximum of $2,555 in convertible subordinated unsecured debentures of the Corporation, representing approximately 5% of such floating debentures at the offer date. The debentures could be repurchased at market prices plus brokerage fees. The Company did not repurchase any convertible debentures in connection with its normal course issuer bid.

On March 24, 2005, the Corporation sent a redemption notice to the holders of its convertible unsecured subordinated debentures. Under the notice, on April 25, 2005, the Corporation redeemed, at their nominal value, $35 of such debentures, representing all outstanding debentures as at that date. During the year ended October 31, 2005, but prior to the redemption date, a total of $51,057 in convertible debentures was converted into 5,835,081 shares, consisting of Class A Shares and Class B Shares.

13 AMORTIZATION

	2005 **$**	2004 $
Property, plant and equipment	**36,991**	30,312
Other assets	**567**	2,715
	37,558	33,027

14 BUSINESS ACQUISITIONS

During the years ended October 31, 2004 and 2005, the Corporation acquired several businesses. These acquisitions were recorded using the purchase method. The results of these businesses were included in the Corporation's results as of their respective dates of acquisition.

On November 1, 2004, the Corporation acquired a 70% ownership interest in Air Consultants Europe ["ACE"], a Dutch outgoing tour operator, for a total consideration of €1,050 [$1,634]. A cash consideration of €950 [$1,473] was paid on the date of acquisition. The balance of €100 is payable in two staggered instalments through November 1, 2006. As a result of this acquisition, goodwill increased by $1,579.

On May 1, 2005, the Corporation acquired a 50.1% ownership interest in Travel Superstore Inc., a Canadian company operating a travel agency network, for a cash consideration of $4,478. As a result of this acquisition, goodwill increased by $2,799.

On June 26, 2005, the Corporation acquired all of the outstanding shares of Bennett Voyages, a French outgoing tour operator, for a total consideration of €1,773 [$2,629]. A cash consideration of €1,075 [$1,594] was paid on the date of acquisition. The balance of €698 [$1,035] is payable in staggered monthly instalments through December 31, 2006. As a result of this acquisition, goodwill increased by $1,971.

14 *BUSINESS ACQUISITIONS* [Cont'd]

On August 1, 2005, the Corporation acquired the assets of Blenus Travel Service Limited and Fundy Travel Limited, both Canadian companies operating a travel agency network, for a total consideration of $1,259. On the date of acquisition, a cash consideration of $260 was paid and the balance of $999 is payable over a five-year period without interest. As a result of this acquisition, goodwill increased by $1,117.

On October 31, 2005, the Corporation acquired the assets of Turissimo Caribe & Excursiones C. Por A., an incoming tour operator in the Dominican Republic, for a cash consideration of US$1,185 [$1,398]. As a result of this acquisition, goodwill increased by $1,075.

On April 8, 2004, the Corporation acquired the balance of the outstanding shares [50%] of the Canadian incoming tour operator Jonview Corporation ["Jonview"] for a total consideration of $12,771, including acquisition costs of $113. A cash amount of $9,593 was paid at the closing of the transaction and the balance of $3,065 will be paid in cash in three instalments through September 2006. The minority shareholder's portion was financed, in part, by the issuance of a debenture *[see note 10 (d)]*. Prior to April 8, 2004, the results were recorded on a proportionate consolidation basis. Subsequent to these transactions, the Corporation now holds an 80.1% interest in Jonview. As a result of this acquisition, goodwill increased by $11,956.

On June 10, 2004, the Corporation acquired an additional 50% interest in Tourgreece S.A. ["Tourgreece"], an incoming tour operator in Greece, for a total cash consideration of €1,797 [$2,954], including acquisition costs of €219 [$354]. The acquisition was accounted for as a step acquisition using the purchase method. As a result of the acquisition of the Corporation's interests in Tourgreece, goodwill increased by $6,996. Prior to June 10, 2004, the results were recorded using the equity method. Subsequent to this transaction, the Corporation now holds a 90% interest in Tourgreece. Under the agreement, the Corporation has a call option to acquire the balance of shares at any time prior to 2011.

The Corporation's share in business acquisitions is summarized as follows:

	2005 $	2004 $
Assets acquired		
Cash and cash equivalents	**7,025**	3,764
Other current assets	**14,912**	2,598
Property, plant and equipment	**699**	841
Goodwill	**8,541**	15,294
	31,177	22,497
Liabilities assumed		
Current liabilities	**19,523**	6,564
Long-term debt	**256**	208
	19,779	6,772
Net assets acquired at fair value	**11,398**	15,725

2004 restructuring program

During the year ended October 31, 2004, the Corporation recorded a restructuring charge totalling $11,350 related to its restructuring program, which aimed to change the management structure and reposition the Corporation's subsidiary Look Voyages S.A.

The amount recorded included a cash charge of $8,319 and a write-off of property, plant and equipment and other assets of $3,031. The cash charge consisted mainly of employee termination benefits and contract termination costs.

In 2005, the execution of the restructuring initiatives approved during the year ended October 31, 2004 resulted in a reversal of $934. This reversal was mostly due to lower reallocation and employee training fees, as required by French authorities, lower than expected negotiation fees on the cancellation of contracts and earlier than expected departures of certain employees.

The following table highlights the activity and balance of the 2004 restructuring provision for the years ended October 31, 2004 and 2005.

	Employee termination benefits $	Contract termination costs $	Write-off of property, plant and equipment and other assets $	Other costs $	Total $
Amount incurred during the year ended October 31, 2004	4,590	2,526	3,031	1,203	11,350
Cumulative drawdowns:					
Cash	—	—	—	88	88
Non-cash	—	—	3,031	—	3,031
Balance as at October 31, 2004	4,590	2,526	—	1,115	8,231
Cash drawdowns	**4,071**	**992**	**—**	**393**	**5,456**
Provision reversal	**230**	**287**	**—**	**417**	**934**
Translation adjustment	**47**	**129**	**—**	**69**	**245**
Balance as at October 31, 2005	**242**	**1,118**	**—**	**236**	**1,596**

2003 restructuring program

During the year ended October 31, 2003, the Corporation recorded a restructuring charge totalling $47,972 before income taxes. This program included a change in the management structure and a reorganization that affected both the nature and focus of its operations in France and Canada.

The amount recorded included a cash charge of $13,489 and a write-off of property, plant and equipment and other assets totalling $34,483. The cash charge consisted mainly of employment termination benefits and contract termination costs.

The write-off of property, plant and equipment and other assets arose primarily from the gradual phase-out of the six Lockheed L-1011-500 aircraft of the Corporation through April 30, 2004. This amount included $21,462 in the form of a write-off for the three aircraft that ceased operations in September 2003, as well as $12,253 for an impairment write-down corresponding to the excess of the carrying amount, at the time recoverability is assessed, over the fair value of long-lived assets calculated using the estimated future cash flows directly related to the three remaining aircraft phased out by April 30, 2004.

The following table highlights the activity and balance of the 2003 restructuring provision for the years ended October 31, 2004 and 2005.

	Employee termination benefits $	Contract termination costs $	Other costs $	Total $
Balance as at October 31, 2003	5,614	50	440	6,104
Cash drawdowns	2,341	—	47	2,388
Balance as at October 31, 2004	3,273	50	393	3,716
Cash drawdowns	**1,689**	**50**	**393**	**2,132**
Balance as at October 31, 2005	**1,584**	**—**	**—**	**1,584**

16 INCOME TAXES

Income taxes as presented differ from the amount calculated by applying the statutory income tax rates to income before income taxes and non-controlling interest in subsidiaries' results.

The reasons for this difference and the effect on income tax expense are detailed as follows:

	2005 $	**2005** %	2004 $	2004 %
Income taxes at the statutory rate	**30,802**	**33.1**	37,947	32.1
Change in income taxes arising from the following:				
Non-deductible items	**900**	**1.0**	898	0.8
Recognition of previously unrecorded tax benefits	**(2,269)**	**(2.4)**	(598)	(0.5)
Unrecorded tax benefits	**1,165**	**1.3**	6,887	5.8
Valuation allowance	**5,591**	**6.0**	—	—
Other	**113**	**0.1**	(124)	(0.1)
	36,302	**39.1**	45,010	38.1

The tax effects of temporary differences giving rise to future income tax assets and liabilities are as follows:

	2005 $	2004 $
Future income taxes		
Net operating loss carry-forwards and other tax deductions	**20,574**	25,896
Carrying amount of capital assets over tax basis	**(25,089)**	(16,848)
Non-deductible reserves and provisions	**27,317**	5,324
Other	**(1,007)**	(550)
Total future income taxes	**21,795**	13,822
Valuation allowance	**(21,670)**	(19,607)
Net future income tax assets (liabilities)	**125**	(5,785)
Current future income tax assets	**70**	586
Long-term future income tax assets	**5,106**	10,656
Long-term future income tax liabilities	**(5,051)**	(17,027)
Net future income tax assets (liabilities)	**125**	(5,785)

Non-capital losses carried forward and other temporary differences, which are available to reduce future taxable income of certain subsidiaries in Europe, for which no related income tax benefits have been recognized, amounted to €40,545 [$57,388] as at October 31, 2005 [€32,401 [$50,425] as at October 31, 2004]; these losses and differences have no expiry date.

Undistributed earnings of the Corporation's foreign subsidiaries are considered to be indefinitely reinvested and, accordingly, no provision for income taxes has been provided thereon. Upon distribution of these earnings in the form of dividends or otherwise, the Corporation may be subject to withholding taxes.

During the year ended October 31, 2004, the Corporation recognized a tax savings totalling $1,420 as a reduction of goodwill. This savings was not recognized when the purchase price of an acquisition was allocated.

17 RELATED PARTY TRANSACTIONS AND BALANCES

In the normal course of its operations, the Corporation enters into transactions with related companies. These transactions are measured at the exchange amount, which is the amount of consideration determined and agreed to by the related parties. Significant transactions between related companies are as follows:

	2005 **$**	2004 $
Revenues from companies subject to significant influence	**3,002**	3,897
Operating expenses incurred from companies subject to significant influence	**3,996**	90,691

Operating expenses consist primarily of the purchase of airplane seats.

The balances receivable from and payable to related companies included in accounts receivable and accounts payable and accrued liabilities are as follows:

	2005 **$**	2004 $
Accounts receivable from companies subject to significant influence	**240**	984
Accounts payable and accrued liabilities due to companies subject to significant influence	**202**	782

18 EMPLOYEE FUTURE BENEFITS

As at October 31, 2005, accrued benefit obligations and the actuarial deficit amounted to $11,739 [$5,348 as at October 31, 2004]. For the year ended October 31, 2005, the pension expense totalled $2,400 [$811 for the year ended October 31, 2004]. The Corporation issued a letter of credit to the trustee in the amount of $11,090 in order to guarantee its benefit obligations *[note 4]*.

19 COMMITMENTS AND CONTINGENCIES

(a) The Corporation's commitments under operating leases relating to aircraft, buildings, automotive equipment, telephone systems, maintenance contracts and office premises amounted to $338,115, broken down as follows: $99,150, US$195,669 and €5,692.

The annual instalments to be made under these leases during the next five years are as follows:

	$
2006	68,604
2007	63,664
2008	59,833
2009	50,515
2010	27,454

(b) In 2009, the minority shareholder in Jonview's parent company may require the Corporation to buy the shares of Jonview's parent company which it holds at a price equal to the fair market value. The price paid may be settled, at the Corporation's option, in cash or by a share issue.

(c) The minority shareholder of ACE could require, between now and 2007, that the Corporation acquires the shares of ACE that it holds according to a predetermined pricing formula calling for a cash settlement.

(d) The minority shareholders of Travel Superstore Inc. could require, between 2011 and 2015, that the Corporation acquires the shares of Travel Superstore Inc. that they hold at a price equal to their fair market value and payable in cash.

(e) In the normal course of its operations, the Corporation is exposed to various claims and legal proceedings. These disputes often involve numerous uncertainties and the outcome of the individual cases is unpredictable. According to management, these claims and proceedings are adequately provided for or covered by insurance policies and their settlement should not have a significant negative impact on the Corporation's financial position.

20 GUARANTEES

In the normal course of business, the Corporation has entered into agreements that contain features which meet the definition of a guarantee. These agreements provide indemnification and guarantees to counter-parties in transactions such as operating leases, irrevocable letters of credit and security contracts.

These agreements may require the Corporation to compensate the counterparties for costs and losses incurred as a result of various events, including breaches of representations and warranties, loss of or damages to property and claims that may arise while providing services and environmental liabilities.

Notes 4, 8, 9, 10 and 19 to the financial statements provide information relating to some of these agreements. The following constitutes additional disclosure.

Operating leases
The Corporation's subsidiaries have general indemnity clauses in many of their airport and other real estate leases whereby they, as lessee, indemnify the lessor against liabilities related to the use of the leased property. These leases mature at various dates through 2034. The nature of the agreements varies based on the contracts and therefore prevents the Corporation from estimating the total potential amount its subsidiaries would have to pay to lessors. Historically, the Corporation's subsidiaries have not made any significant payments under such agreements and have liability insurance protecting them for the obligations undertaken.

Irrevocable letters of credit
The Corporation has entered into irrevocable letters of credit with some of its suppliers. The Corporation guarantees the payment of certain tourist services such as hotel rooms whether it sells the services or not. These agreements, which are entered into for significant blocks of tourist services, typically cover a one-year period and are renewable. The Corporation has also issued letters of credit to provincial regulatory agencies in Ontario and British Columbia guaranteeing amounts to the Corporation's clients for the performance of its obligations. In addition to the letters of credit and security contracts mentioned in notes 4 and 8, the other offered guarantees totalled $387 as at October 31, 2005. Historically, the Corporation has not made any significant payments under such letters of credit.

Security contracts
The Corporation has entered into security contracts whereby it has guaranteed a prescribed amount to its clients at the request of regulatory agencies for the performance of the obligations included in mandates by its clients during the term of the licenses granted to the Corporation for its travel agent and wholesaler activities in the province of Québec. These agreements typically cover a one-year period and are renewable annually. As at October 31, 2005, the amount guaranteed totalled $1,260. Historically, the Corporation has not made any significant payments under such agreements.

As at October 31, 2005, no amounts have been accrued with respect to the above-mentioned agreements.

21 FINANCIAL INSTRUMENTS

In the normal course of its operations, the Corporation is exposed to risks related to exchange rate variations for certain currencies and fuel cost variations. The Corporation manages these risks by entering into various financial instruments. The Corporation's management is responsible for determining the acceptable level of risk and only uses financial instruments to hedge existing commitments or obligations and not to realize a profit on trading operations.

Credit risk related to financial instruments

The theoretical risk to which the Corporation is exposed in relation to financial instruments is limited to the replacement cost of contracts at market rates in effect in the event of default by one of the parties. Management is of the opinion that the credit risk related to financial instruments is well controlled because the Corporation only enters into agreements with large financial institutions and multinational companies.

Management of fuel price and foreign exchange

The Corporation has entered into fuel purchasing contracts to manage fuel price fluctuation risks. As at October 31, 2005, 39% of the estimated requirements for fiscal 2006 were covered by fuel purchasing contracts [9% of the requirements for fiscal 2005 were covered as at October 31, 2004].

The Corporation has entered into foreign exchange forward contracts, expiring in less than one year, for the purchase and sale of foreign currencies to manage foreign exchange risks. As at October 31, 2005, the face value of these contracts to purchase foreign currencies amounted to $427,085 [$334,754 as at October 31, 2004].

The fair value of financial instruments generally reflects the estimated amounts that the Corporation would receive from settlements of favourable contracts or that it would be required to pay to cancel unfavourable contracts at year-end. These estimated fair values are based on the rates obtained from large financial institutions and multinational companies. As at October 31, 2005 and 2004, the fair values in the event of a settlement are as follows:

	2005		2004	
	Favourable $	**Unfavourable $**	Favourable $	Unfavourable $
Foreign exchange forward contracts	**1,095**	**9,400**	122	29,764
Fuel purchase contracts	**1,791**	**2,972**	4,640	—
	2,886	**12,372**	4,762	29,764

Credit risk

The Corporation believes it is not exposed to a significant concentration of credit risk. Cash and cash equivalents are invested on a diversified basis in corporations benefiting from an excellent credit rating. Accounts receivable generally arise from the sale of vacation packages to individuals through retail travel agencies and the sale of seats to tour operators which are dispersed over a wide geographic area. As at October 31, 2005 and 2004, no debtor represented more than 10% of the total accounts receivable.

Fair value of financial instruments presented on the balance sheets

Due to the short-term nature of current financial assets and liabilities reflected on the consolidated balance sheets, their carrying amount approximates their fair value.

Due to the nature of obligations under capital leases presented in the consolidated balance sheets, their carrying amount approximates their fair value.

The fair value of the debentures could not be determined with sufficient reliability due to their specific nature.

22 SEGMENT DISCLOSURE

The Corporation has determined that it conducts its activities in a single industry segment, namely holiday travel. Therefore, the statements of income include all the required information. With respect to geographic areas, the Corporation operates mainly in North America and in Europe. Geographic intersegment sales are accounted for at prices that take into account market conditions and other considerations.

	North America $	Europe $	Total $
2005			
Revenues from third parties	**1,896,487**	**467,994**	**2,364,481**
Operating expenses	**1,776,811**	**467,039**	**2,243,850**
	119,676	**955**	**120,631**
Amortization	**34,200**	**3,358**	**37,558**
Restructuring charge	**—**	**(934)**	**(934)**
Additions to property, plant and equipment	**26,042**	**1,171**	**27,213**
Property, plant and equipment and goodwill	**234,882**	**53,990**	**288,872**
2004			
Revenues from third parties	1,673,530	526,292	2,199,822
Operating expenses	1,495,971	540,096	2,036,067
	177,559	(13,804)	163,755
Amortization	28,585	4,442	33,027
Restructuring charge	—	11,350	11,350
Additions to property, plant and equipment	19,819	1,083	20,902
Property, plant and equipment and goodwill	127,485	52,609	180,094

23 SUBSEQUENT EVENTS

(a) On November 14, 2005, the Corporation announced an issuer bid to repurchase and cancel Class A Shares and Class B Shares. A maximum of 7,142,857 shares, or approximately 18% of the Corporation's 40,156,450 issued and outstanding Class A Shares and Class B Shares could have been repurchased at a price of not less than $17.50 per share and not more than $20.00 per share, for a total of $125,000. The bid was expiring on December 22, 2005.

In accordance with its issuer bid, the Corporation redeemed, on January 3, 2006, a total of 6,443,299 voting shares, consisting of 1,780,797 Class A Shares and 4,662,502 Class B Shares, for a cash consideration of $125,000.

(b) On December 1, 2005, the Corporation completed the acquisition of the assets of 20 Carlson Wagonlit Travel agencies in France, for a cash consideration of €2,900 [$3,990].

24 COMPARATIVE FIGURES

Certain comparative figures were reclassified to conform to the presentation adopted in the current year.

Supplementary Financial Data

[In thousands of dollars, except per share data]

Consolidated statements of income
Revenues
Operating expenses
Expenses and other income
Amortization
Restructuring charge
Interest on long-term debt, obligations under capital leases and debentures
Other interest and financial expenses
Interest income
Foreign exchange (gain) loss on long-term monetary items
Gain on disposal of investments
Share of net (income) loss of companies subject to significant influence
Income (loss) before the following items
Income taxes (recovery)
Non-controlling interest in subsidiaries' results
Income (loss) before goodwill charges
Goodwill charges
Income (loss) from continuing operations for the year
Income (loss) from discontinued operations for the year
Net income (loss) for the year
Basic earnings (loss) per share
Before goodwill charges
Continuing operations
Discontinued operations
Diluted earnings (loss) per share [1]
Before goodwill charges
Continuing operations
Discontinued operations
Cash flows from:
Operating activities (continuing operations)
Investing activities (continuing operations)
Financing activities (continuing operations)
Net change in cash and cash equivalents from continuing operations
Net change in cash and cash equivalents from discontinued operations
Net change in cash and cash equivalents
Cash and cash equivalents, end of year
Operating cash flow
Total assets
Long-term debt and obligations under capital leases (including current portion)
Debentures
Shareholders' equity
Debt ratio [2]
Book value per share
Return on weighted average shareholders' equity
Shareholding statistics (in thousands)
Outstanding shares at year-end
Weighted average number of outstanding shares (before dilution)
Weighted average number of outstanding shares (after dilution) [1]

[1] See note 11 to audited consolidated financial statements.
[2] Represents liabilities over liabilities plus shareholders' equity.

	2005	2004	2003	2002	2001
	2,364,481	2,199,822	2,096,649	2,073,508	2,121,886
	2,243,850	2,036,067	2,021,687	1,999,360	2,063,863
	120,631	163,755	74,962	74,148	58,023
	37,558	33,027	42,138	43,189	49,659
	(934)	11,350	47,972	—	116,972
	10,815	7,712	9,839	12,491	11,310
	1,708	1,907	3,071	4,563	3,762
	(12,963)	(11,307)	(9,530)	(5,628)	(10,043)
	(2,309)	1,474	(3,873)	(984)	2,303
	(5,747)	—	—	—	—
	(461)	1,509	(673)	(919)	(939)
	27,667	45,672	88,944	52,712	173,024
	92,964	118,083	(13,982)	21,436	(115,001)
	36,302	45,010	(5,533)	9,649	(19,909)
	(1,246)	(753)	(766)	(182)	(117)
	55,416	72,320	(9,215)	11,605	(95,209)
	—	—	—	—	4,442
	55,416	72,320	(9,215)	11,605	(99,651)
	—	—	54,083	(1,853)	—
	55,416	72,320	44,868	9,752	(99,651)
	1.43	2.07	(0.38)	0.30	(2.95)
	1.43	2.07	(0.38)	0.30	(3.09)
	—	—	1.65	(0.06)	—
	1.43	2.07	1.27	0.24	(3.09)
	1.33	1.76	(0.38)	0.30	(2.95)
	1.33	1.76	(0.38)	0.30	(3.09)
	—	—	1.65	(0.06)	—
	1.33	1.76	1.27	0.24	(3.09)
	63,785	185,100	71,697	183,234	(12,001)
	(18,600)	(32,970)	(4,275)	(25,864)	(59,441)
	(37,975)	(32,702)	(56,278)	17,700	8,660
	7,210	119,428	11,144	175,070	(62,782)
	—	—	77,858	434	—
	7,210	119,428	89,002	175,504	(62,782)
	475,763	468,553	349,125	260,123	84,619
	75,614	124,039	52,795	73,942	59,357
	949,537	838,389	714,757	773,468	626,442
	93,613	—	35,350	82,702	147,496
	13,156	33,214	31,731	30,907	12,500
	362,383	311,106	239,596	192,062	130,617
	0.62	0.63	0.66	0.75	0.79
	9.02	9.16	7.29	5.92	4.04
	16.03%	25.11%	19.32%	4.76%	(55.34%)
	40,156	33,955	32,864	32,460	32,324
	37,863	33,374	32,796	32,418	32,248
	41,684	41,156	32,796	32,497	32,248

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the Vice-President, Finance and Administration
and Chief Financial Officer.

*Vous pouvez obtenir un exemplaire
de ce rapport annuel en français
en écrivant au vice-président,
finances et administration
et chef de la direction financière.*

Stock Exchange
The shares of the Corporation
are listed on the Toronto Stock Exchange
under the ticker symbols
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*The annual meeting of shareholders
will be held on March 15, 2006,
10:00 a.m. at:*

*International Civil Aviation Organization
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