FEDEX CORP
Form 10-K/A
July 21, 2004

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

(Amendment No. 1)

(Mark One)

ý **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended May 31, 2004.

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from ___ to ___.

Commission file number 1-15829

FEDEX CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Delaware	**62-1721435**
(State or Other Jurisdiction of Incorporation or Organization)	*(I.R.S. Employer Identification No.)*
942 South Shady Grove Road, Memphis, Tennessee	**38120**
(Address of Principal Executive Offices)	*(ZIP Code)*

Registrant's telephone number, including area code: (901) 818-7500

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

Title of each class	Name of each exchange on which registered
Common Stock, par value $.10 per share	New York Stock Exchange

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ý

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

The aggregate market value of the common stock held by non-affiliates of the Registrant, computed by reference to the closing price as of the last business day of the Registrant's most recently completed second fiscal quarter, November 28, 2003, was approximately $20.2 billion. The Registrant has no non-voting stock.

As of July 12, 2004, 299,997,050 shares of the Registrant's common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive proxy statement to be delivered to stockholders in connection with the 2004 annual meeting of stockholders to be held on September 27, 2004 are incorporated by reference in response to Part III of this Report.

EXPLANATORY NOTE

FedEx Corporation ("FedEx") hereby amends its Annual Report on Form 10-K for the fiscal year ended May 31, 2004 (the "Form 10-K") (filed on July 16, 2004) as set forth in this Annual Report on Form 10-K/A (Amendment No. 1) (this "Form 10-K/A").

This Form 10-K/A includes an amendment to Item 8 of the Form 10-K. Specifically, in the table on page F-13 in Note 2: "Business Combinations" of the Notes to Consolidated Financial Statements, which presents the unaudited pro forma combined results of operations of FedEx and FedEx Kinko's Office & Print Services, Inc. ("FedEx Kinko's") as if FedEx's acquisition of FedEx Kinko's had occurred at the beginning of the fiscal year ended May 31, 2003, revenues, net income, basic earnings per common share and diluted earnings per common share for the fiscal year ended May 31, 2004 should have been shown as $26.056 billion, $836 million, $2.80 and $2.75, respectively.

No other changes are being made to the Form 10-K by means of this Form 10-K/A.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The following financial statements are filed with this Report:

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

The following exhibits are being filed or furnished with this Report:

Exhibit Number	Description of Exhibit
23	Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm.
31.1	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

FEDEX CORPORATION

Dated: July 21, 2004   By: /s/ JOHN L. MERINO

John L. Merino
Corporate Vice President and
Principal Accounting Officer

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
FedEx Corporation

We have audited the accompanying consolidated balance sheets of FedEx Corporation as of May 31, 2004 and 2003, and the related consolidated statements of income, changes in stockholders' investment and comprehensive income, and cash flows for each of the three years in the period ended May 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about 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. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of FedEx Corporation at May 31, 2004 and 2003, and the consolidated results of its operations and its cash flows for each of the three years in the period ended May 31, 2004, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 3 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, in 2002.

/s/ Ernst & Young LLP

Memphis, Tennessee
June 22, 2004

FEDEX CORPORATION
CONSOLIDATED BALANCE SHEETS
(IN MILLIONS)

ASSETS

	May 31, 2004	May 31, 2003
CURRENT ASSETS		
Cash and cash equivalents	$ 1,046	$ 538
Receivables, less allowances of $151 and $149	3,027	2,627
Spare parts, supplies and fuel, less allowances of $124 and $101	249	228
Deferred income taxes	489	416
Prepaid expenses and other	159	132
Total current assets	4,970	3,941
PROPERTY AND EQUIPMENT, AT COST		
Aircraft and related equipment	7,001	6,624
Package handling and ground support equipment and vehicles	5,296	5,013
Computer and electronic equipment	3,537	3,180
Other	4,477	4,200
	20,311	19,017
Less accumulated depreciation and amortization	11,274	10,317
Net property and equipment	9,037	8,700
OTHER LONG-TERM ASSETS		
Goodwill	2,802	1,063
Prepaid pension cost	1,127	1,269
Intangible and other assets	1,198	412
Total other long-term assets	5,127	2,744
	$ 19,134	$ 15,385

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

FEDEX CORPORATION
CONSOLIDATED BALANCE SHEETS
(IN MILLIONS, EXCEPT SHARE DATA)

LIABILITIES AND STOCKHOLDERS' INVESTMENT

	May 31, 2004	May 31, 2003
CURRENT LIABILITIES		
Current portion of long-term debt	$ 750	$ 308
Accrued salaries and employee benefits	1,062	724
Accounts payable	1,615	1,168
Accrued expenses	1,305	1,135
Total current liabilities	4,732	3,335
LONG-TERM DEBT, LESS CURRENT PORTION	2,837	1,709
OTHER LONG-TERM LIABILITIES		
Deferred income taxes	1,181	882
Pension, postretirement healthcare and other benefit obligations	768	657
Self-insurance accruals	591	536
Deferred lease obligations	503	466
Deferred gains, principally related to aircraft transactions	426	455
Other liabilities	60	57
Total other long-term liabilities	3,529	3,053
COMMITMENTS AND CONTINGENCIES		
COMMON STOCKHOLDERS' INVESTMENT		
Common stock, $0.10 par value; 800 million shares authorized; 300 million shares issued for 2004 and 299 million shares issued for 2003	30	30
Additional paid-in capital	1,079	1,088
Retained earnings	7,001	6,250
Accumulated other comprehensive loss	(46)	(30)
	8,064	7,338
Less deferred compensation and treasury stock, at cost	28	50
Total common stockholders' investment	8,036	7,288
	$ 19,134	$ 15,385

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

FEDEX CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(IN MILLIONS, EXCEPT PER SHARE AMOUNTS)

	Years ended May 31,		
	2004	**2003**	**2002**
REVENUES	$ 24,710	$ 22,487	$ 20,607
OPERATING EXPENSES:			
Salaries and employee benefits	10,728	9,778	9,099
Purchased transportation	2,407	2,155	1,825
Rentals and landing fees	1,918	1,803	1,780
Depreciation and amortization	1,375	1,351	1,364
Fuel	1,481	1,349	1,100
Maintenance and repairs	1,523	1,398	1,240
Business realignment costs	435		
Airline stabilization compensation			(119)
Other	3,403	3,182	2,997
	23,270	21,016	19,286
OPERATING INCOME	1,440	1,471	1,321
OTHER INCOME (EXPENSE):			
Interest expense	(136)	(124)	(144)
Interest income	20	6	5
Other, net	(5)	(15)	(22)
	(121)	(133)	(161)
INCOME BEFORE INCOME TAXES	1,319	1,338	1,160
PROVISION FOR INCOME TAXES	481	508	435
INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	838	830	725
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING FOR GOODWILL, NET OF TAX BENEFIT OF $10			(15)
NET INCOME	$ 838	$ 830	$ 710
BASIC EARNINGS PER COMMON SHARE:			
Income before cumulative effect of change in accounting principle	$ 2.80	$ 2.79	$ 2.43
Cumulative effect of change in accounting for goodwill			(0.05)
BASIC EARNINGS PER COMMON SHARE	$ 2.80	$ 2.79	$ 2.38

	Years ended May 31,		
DILUTED EARNINGS PER COMMON SHARE:			
Income before cumulative effect of change in accounting principle	$ 2.76	$ 2.74	$ 2.39
Cumulative effect of change in accounting for goodwill			(0.05)
DILUTED EARNINGS PER COMMON SHARE	$ 2.76	$ 2.74	$ 2.34

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

FEDEX CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN MILLIONS)

	Years ended May 31,		
	2004	**2003**	**2002**
OPERATING ACTIVITIES			
Net income	$ 838	$ 830	$ 710
Adjustments to reconcile net income to cash provided by operating activities:			
Depreciation and amortization	1,375	1,351	1,364
Provision for uncollectible accounts	106	105	110
Deferred income taxes and other noncash items	(8)	329	84
Cumulative effect of change in accounting principle			15
Tax benefit on the exercise of stock options	43	20	18
Changes in operating assets and liabilities, net of the effects of businesses acquired:			
Receivables	(307)	(197)	(88)
Other current assets	10	39	63
Pension assets and liabilities, net	155	(854)	(13)
Accounts payable and other operating liabilities	841	252	(37)
Other, net	(33)	(4)	2
Cash provided by operating activities	3,020	1,871	2,228
INVESTING ACTIVITIES			
Business acquisitions, net of cash acquired	(2,410)		(35)
Capital expenditures	(1,271)	(1,511)	(1,615)
Proceeds from asset dispositions	18	22	27
Other, net	1	(1)	11
Cash used in investing activities	(3,662)	(1,490)	(1,612)
FINANCING ACTIVITIES			
Principal payments on debt	(319)	(10)	(320)
Proceeds from debt issuances	1,599		
Proceeds from stock issuances	115	81	88
Dividends paid	(66)	(60)	
Purchase of treasury stock	(179)	(186)	(177)
Other, net		1	3
Cash provided by (used in) financing activities	1,150	(174)	(406)
CASH AND CASH EQUIVALENTS			
Net increase in cash and cash equivalents	508	207	210
Cash and cash equivalents at beginning of period	538	331	121
Cash and cash equivalents at end of period	$ 1,046	$ 538	$ 331

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

FEDEX CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' INVESTMENT AND COMPREHENSIVE INCOME
(IN MILLIONS, EXCEPT SHARE DATA)

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Deferred Compensation	Total
BALANCE AT MAY 31, 2001	$ 30	$ 1,120	$ 4,880	$ (56)	$ (53)	$ (21)	$ 5,900
Net income			710				710
Foreign currency translation adjustment, net of deferred taxes of $1				6			6
Minimum pension liability adjustment, net of deferred tax benefit of $2				(3)			(3)
Reclassification of deferred jet fuel hedging charges net of deferred tax benefit of $6				(9)			(9)
Adjustment for jet fuel hedging charges recognized in expense during period, net of deferred taxes of $6				9			9
Total comprehensive income							**713**
Purchase of treasury stock					(177)		(177)
Cash dividends declared ($0.05 per share)			(15)				(15)
Employee incentive plans and other (4,224,444 shares issued)		24	(110)		210	(12)	112
Amortization of deferred compensation						12	12
BALANCE AT MAY 31, 2002	30	1,144	5,465	(53)	(20)	(21)	6,545
Net income			830				830
Foreign currency translation adjustment, net of deferred taxes of $10				37			37
Minimum pension liability adjustment, net of deferred tax benefit of $7				(14)			(14)
Total comprehensive income							**853**
Purchase of treasury stock					(186)		(186)
Cash dividends declared ($0.15 per share)			(45)				(45)
Employee incentive plans and other (3,268,180 shares issued)		(56)			181	(16)	109
Amortization of deferred compensation						12	12
BALANCE AT MAY 31, 2003	30	1,088	6,250	(30)	(25)	(25)	7,288
Net income			838				838
Minimum pension liability adjustment, net of deferred tax benefit of $12				(16)			(16)
Total comprehensive income							**822**
Purchase of treasury stock					(179)		(179)
Cash dividends declared ($0.29 per share)			(87)				(87)
Employee incentive plans and other (4,013,182 shares issued)		(9)			204	(18)	177
Amortization of deferred compensation						15	15
BALANCE AT MAY 31, 2004	$ 30	$ 1,079	$ 7,001	$ (46)	$	$ (28)	$ 8,036

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

FEDEX CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1: Description of Business and Summary of Significant Accounting Policies

Description of Business. FedEx Corporation ("FedEx") provides a broad portfolio of transportation, e-commerce and business services with companies that operate independently and compete collectively under the respected FedEx brand. Our operations are primarily represented by Federal Express Corporation ("FedEx Express"), the world's largest express transportation company; FedEx Ground Package System, Inc. ("FedEx Ground"), North America's second largest provider of small-package ground delivery service; FedEx Freight Corporation ("FedEx Freight"), a leading U.S. provider of regional less-than-truckload ("LTL") freight services; and FedEx Kinko's Office and Print Services, Inc. ("FedEx Kinko's"), a leading provider of document solutions and business services. These businesses form the core of our reportable segments. Other business units in the FedEx portfolio are FedEx Trade Networks, Inc. ("FedEx Trade Networks"), a global trade services company; FedEx Supply Chain Services, Inc. ("FedEx Supply Chain Services"), a contract logistics provider; FedEx Custom Critical, Inc. ("FedEx Custom Critical"), a critical-shipment carrier; Caribbean Transportation Services, Inc. ("Caribbean Transportation Services"), a provider of airfreight forwarding services, and FedEx Corporate Services, Inc. ("FedEx Services"), a provider of customer-facing sales, marketing and information technology functions, primarily for FedEx Express and FedEx Ground.

The FedEx Kinko's segment was formed in the fourth quarter of 2004 as a result of our acquisition of FedEx Kinko's (formerly known as Kinko's, Inc.). As discussed in Note 2, we acquired FedEx Kinko's on February 12, 2004, and its results of operations have been included in our financial results from the date of acquisition.

Fiscal Years. Except as otherwise specified, references to years indicate our fiscal year ended May 31, 2004 or ended May 31 of the year referenced.

Principles of Consolidation. The consolidated financial statements include the accounts of FedEx and its subsidiaries, substantially all of which are wholly owned. All significant intercompany accounts and transactions have been eliminated.

Credit Risk. We routinely grant credit to many of our customers for transportation and business services without collateral. The risk of credit loss in our trade receivables is substantially mitigated by our credit evaluation process, short collection terms and sales to a large number of customers, as well as the low revenue per transaction for most of our services. Allowances for potential credit losses are determined based on historical experience, current evaluation of the composition of accounts receivable and expected credit trends. Historically, credit losses have been within management's expectations.

Revenue Recognition. Revenue is recognized upon delivery of shipments or the completion of the service for our office and print services, logistics and trade services businesses. For shipments in transit, revenue is recorded based on the percentage of service completed at the balance sheet date. Estimates for future billing adjustments to revenue and accounts receivable are recognized at the time of shipment for certain discounts, money-back service guarantees and billing corrections. Delivery costs are accrued as incurred.

Our contract logistics and global trade services businesses engage in certain transactions wherein they act as agents. Revenue from these transactions is recorded on a net basis.

Advertising. Advertising costs are expensed as incurred and are classified in other operating expenses. Advertising expenses were $284 million, $249 million and $226 million in 2004, 2003 and 2002, respectively.

Cash Equivalents. Cash equivalents in excess of current operating requirements are invested in short-term, interest-bearing instruments with maturities of three months or less at the date of purchase and are stated at cost, which approximates market value.

Spare Parts, Supplies and Fuel. Spare parts are stated principally at weighted-average cost. Supplies and fuel are stated principally at standard cost, which approximates actual cost on a first-in, first-out basis. Allowances for obsolescence are provided, over the estimated useful life of the related aircraft and engines, for spare parts expected to be on hand at the date the aircraft are retired from service, and for spare parts currently identified as excess or obsolete. These allowances are based on management estimates, which are subject to change.

Property and Equipment. Expenditures for major additions, improvements, flight equipment modifications and certain equipment overhaul costs are capitalized when such costs are determined to extend the useful life of the asset. Maintenance and repairs are charged to expense as incurred, except for certain aircraft-related costs on one of our aircraft fleet types, which are capitalized and amortized over their estimated service lives. We capitalize certain direct internal and external costs associated with the development of internal use software. The cost and accumulated depreciation of property and equipment disposed of are removed from the related accounts, and any gain or loss is reflected in the results of operations. Gains and losses on sales of property used in operations are classified with depreciation and amortization.

For financial reporting purposes, depreciation and amortization of property and equipment is provided on a straight-line basis over the asset's service life or related lease term as follows:

	Range
Wide-body aircraft and related equipment	15 to 25 years
Narrow-body and feeder aircraft and related equipment	5 to 15 years
Package handling and ground support equipment and vehicles	3 to 30 years
Computer and electronic equipment	3 to 10 years
Other	2 to 40 years

Substantially all property and equipment have no material residual values. The majority of aircraft costs are depreciated on a straight-line basis over 15 to 18 years, while vehicles are depreciated on a straight-line basis over five to ten years. We periodically evaluate the estimated service lives and residual values used to depreciate our aircraft and other equipment. This evaluation may result in changes in the estimated lives and residual values. The changes did not materially affect depreciation expense in any period presented. Depreciation expense, excluding gains and losses on sales of property and equipment used in operations, was $1.361 billion, $1.334 billion and $1.331 billion in 2004, 2003 and 2002, respectively. Depreciation and amortization expense includes amortization of assets under capital lease.

For income tax purposes, depreciation is generally computed using accelerated methods.

Capitalized Interest. Interest on funds used to finance the acquisition and modification of aircraft, construction of certain facilities and development of certain software up to the date the asset is ready for its intended use is capitalized and included in the cost of the asset. Capitalized interest was $11 million in 2004, $16 million in 2003 and $27 million in 2002.

Impairment of Long-Lived Assets. Long-lived assets are reviewed for impairment when circumstances indicate the carrying value of an asset may not be recoverable. For assets that are to be held and used, an impairment is recognized when the estimated undiscounted cash flows associated with the asset or group of assets is less than their carrying value. If impairment exists, an adjustment is made to write the asset down to its fair value, and a loss is recorded as the difference between the carrying value and fair value. Fair values are determined based on quoted market values, discounted cash flows or internal and external appraisals, as applicable. Assets to be disposed of are carried at the lower of carrying value or estimated net realizable value.

Pension and Postretirement Healthcare Plans. These defined benefit plans are measured as of the last day of our fiscal third quarter of each year using actuarial techniques that reflect estimates for mortality, turnover and expected retirement. In addition, management makes assumptions concerning future salary increases, future expected long-term returns on plan assets and future increases in healthcare costs. Discount rates are established as of the measurement date using theoretical bond models that select high-grade corporate bonds with maturities or coupons that correlate to the expected payouts of the applicable liabilities. Assets for funded plans are presented at fair value at the measurement date in the accompanying footnotes. A calculated-value method is employed for purposes of determining the expected return on the plan asset component of net periodic pension cost for our qualified U.S. pension plans. Generally, we do not fund defined benefit plans when such funding provides no current tax deduction.

Goodwill. Goodwill is recognized for the excess of the purchase price over the fair value of tangible and identifiable intangible net assets of businesses acquired. Goodwill is reviewed at least annually for impairment. Unless circumstances otherwise dictate, we perform our annual impairment testing in the fourth quarter.

Intangible Assets. Amortizable intangible assets include customer relationships, contract based, technology based and other. Amortizable intangible assets are amortized over periods ranging from 2 to 15 years, either on a straight-line basis or an accelerated basis using the pattern in which the economic benefits are consumed. Non-amortizing intangible assets include the Kinko's trade name. Non-amortizing intangibles are reviewed at least annually for impairment. Unless circumstances otherwise dictate, we perform our annual impairment testing in the fourth quarter.

Income Taxes. Deferred income taxes are provided for the tax effect of temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements. The liability method is used to account for income taxes, which requires deferred taxes to be recorded at the statutory rate to be in effect when the taxes are paid.

We have not recognized deferred taxes for U.S. federal income taxes on foreign subsidiaries' earnings that are deemed to be permanently reinvested and any related taxes associated with such earnings are not material. Pretax earnings of foreign operations for 2004 and 2003 were approximately $430 million and $140 million, respectively, which represent only a portion of total results associated with international shipments.

Self-Insurance Accruals. We are primarily self-insured for workers' compensation claims, vehicle accidents and general liabilities, benefits paid under employee healthcare programs and long-term disability. Accruals are primarily based on the actuarially estimated, undiscounted cost of claims, which includes incurred-but-not-reported claims. Current workers' compensation claims, vehicle and general liability, employee healthcare claims and long-term disability are included in accrued expenses.

Deferred Lease Obligations. While certain aircraft, facility and retail location leases contain fluctuating or escalating payments, the related rent expense is recorded on a straight-line basis over the lease term. The deferred lease obligation is the net cumulative excess of rent expense over rent payments.

Deferred Gains. Gains on the sale and leaseback of aircraft and other property and equipment are deferred and amortized ratably over the life of the lease as a reduction of rent expense. Substantially all of these deferred gains were related to aircraft transactions.

Employees Under Collective Bargaining Arrangements. The pilots of FedEx Express, which represent a small number of FedEx Express total employees, are employed under a collective bargaining agreement. Negotiations with the pilots' union began in March 2004, as the current agreement became amendable on May 31, 2004. We will continue to operate under our current agreement while we negotiate with our pilots.

Stock Compensation. We apply Accounting Principles Board Opinion No. ("APB") 25, "Accounting for Stock Issued to Employees," and its related interpretations to measure compensation expense for stock-based compensation plans. We are required to disclose the pro forma effect of accounting for stock options using a valuation method under Statement of Financial Accounting Standards No. ("SFAS") 123, "Accounting for Stock-Based Compensation," for all options granted in 1996 and thereafter. We have currently not elected to adopt this accounting method because it requires the use of subjective valuation models, which we believe are not representative of the real value of the options to either FedEx or our employees. If compensation cost for stock-based compensation plans had been determined under SFAS 123, pro forma net income, stock option compensation expense, and basic and diluted earnings per common share, assuming all options granted in 1996 and thereafter were valued at fair value using the Black-Scholes method, would have been as follows (in millions, except per share amounts):

	Years ended May 31,		
	2004	**2003**	**2002**
Net income, as reported	$ 838	$ 830	$ 710
Add: Stock compensation included in reported net income, net of tax	10		
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of tax benefit	37	34	37
Pro forma net income	$ 811	$ 796	$ 673
Earnings per common share:			
Basic as reported	$ 2.80	$ 2.79	$ 2.38
Basic pro forma	$ 2.71	$ 2.67	$ 2.26
Diluted as reported	$ 2.76	$ 2.74	$ 2.34
Diluted pro forma	$ 2.68	$ 2.63	$ 2.22

See Note 9 for a discussion of the assumptions underlying the pro forma calculations above.

Foreign Currency Translation. Translation gains and losses of foreign operations that use local currencies as the functional currency are accumulated and reported, net of applicable deferred income taxes, as a component of accumulated other comprehensive loss within common stockholders' investment. Transaction gains and losses that arise from exchange rate fluctuations on transactions denominated in a currency other than the local currency are included in results of operations. Cumulative net foreign currency translation losses in accumulated other comprehensive loss were $13 million, $13 million and $50 million at May 31, 2004, 2003 and 2002, respectively.

Reclassifications. Certain reclassifications have been made to prior year financial statements to conform to the current year presentation.

Use of Estimates. The preparation of our consolidated financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, the reported amounts of revenues and expenses and the disclosure of contingent liabilities. Management makes its best estimate of the ultimate outcome for these items based on historical trends and other information available when the financial statements are prepared. Changes in estimates are recognized in accordance with the accounting rules for the estimate, which is typically in the period when new information becomes available to management. Areas where the nature of the estimate makes it reasonably possible that actual results could materially differ from amounts estimated include: self-insurance accruals; employee retirement plan obligations; income tax liabilities; accounts receivable allowances; obsolescence of spare parts; airline stabilization compensation; contingent liabilities; and impairment assessments on long-lived assets (including goodwill and indefinite lived intangible assets).

Note 2: Business Combinations

On February 12, 2004, we acquired FedEx Kinko's for approximately $2.4 billion in cash. We also assumed $39 million of capital lease obligations. FedEx Kinko's is a leading provider of document solutions and business services. Its network of worldwide locations offers access to color printing, finishing and presentation services, Internet access, videoconferencing, outsourcing, managed services, Web-based printing and document management solutions.

The allocation of the purchase price to the fair value of the assets acquired, liabilities assumed and goodwill, as well as the assignment of goodwill to our reportable segments, was based primarily on internal estimates of cash flows and independent appraisals. We used an independent appraisal firm to determine the fair value of certain assets and liabilities, primarily property and equipment and acquired intangible assets, including: the value of the Kinko's trade name, customer-related intangibles, technology assets and contract-based intangibles. While the purchase price allocation is substantially complete and we do not expect any material adjustments, we may make adjustments to the purchase price allocation if new data becomes available.

A significant amount of the purchase price was recorded as goodwill, as the acquisition expands our portfolio of business services, while providing a substantially enhanced capability to provide package-shipping services to small-and medium-sized business customers through FedEx Kinko's array of retail store locations. Because this was an acquisition of stock, goodwill is not deductible for tax purposes. Approximately $200 million of the $1.7 billion goodwill balance will be attributed to the FedEx Express segment ($130 million) and the FedEx Ground segment ($70 million) based on the expected increase in each segment's incremental fair value as a result of the acquisition.

Our balance sheet reflects the following allocation of the total purchase price of $2.4 billion (in millions):

Current assets, primarily accounts receivable and inventory	$	236
Property and equipment		328
Goodwill		1,739
Indefinite lived intangible asset (trade name)		567
Amortizable intangible assets		82
Other long-term assets		52
Total assets acquired		3,004
Current liabilities		(282)
Deferred income taxes		(266)
Long-term capital lease obligations and other long-term liabilities		(36)
Total liabilities assumed		(584)
Total purchase price	$	2,420

Indefinite lived intangible asset. This intangible asset represents the estimated fair value allocated to the Kinko's trade name. This intangible asset will not be amortized because it has an indefinite remaining useful life based on the length of time that the Kinko's name had been in use, the Kinko's brand awareness and market position and the plans for continued use of the Kinko's brand.

Amortizable intangible assets. These intangible assets represent the value associated with business expected to be generated from existing customer relationships and contracts as of the acquisition date. The value of these assets was primarily determined by measuring the present value of the projected future earnings attributable to these assets. Substantially all of these assets are being amortized on an accelerated basis over a weighted-average estimated useful life of approximately seven years. While the useful life of these customer-relationship assets is not limited by contract or any other economic, regulatory or other known factors, the useful life of seven years was determined at the acquisition date based on management's expectations of customer attrition patterns.

The following unaudited pro forma consolidated financial information presents the combined results of operations of FedEx and FedEx Kinko's as if the acquisition had occurred at the beginning of 2003. The unaudited pro forma results have been prepared for comparative purposes only. Adjustments were made to the combined results of operations, primarily related to higher depreciation and amortization expense resulting from higher property and equipment values and acquired intangible assets and additional interest expense resulting from acquisition debt. The accounting literature establishes firm guidelines around how this pro forma information is presented, which precludes the assumption of business synergies. Therefore, this unaudited pro forma information is not intended to represent, nor do we believe it is indicative of the consolidated results of operations of FedEx that would have been reported had the acquisition been completed as of the beginning of 2003. Furthermore, this pro forma information is not representative of the future consolidated results of operations of FedEx.

Pro forma unaudited results were as follows (in millions, except per share data):

	Years ended May 31,	
	2004[1]	2003
Revenues	$ 26,056	$ 24,427
Net income	836	841
Basic earnings per common share	2.80	2.82
Diluted earnings per common share	2.75	2.78

(1) Includes $27 million, net of tax, of nonrecurring expenses at FedEx Kinko's, primarily in anticipation of the acquisition. Also, includes $270 million, net of tax, of business realignment costs and a $37 million, net of tax, nonrecurring tax benefit at FedEx.

We paid a portion of the purchase price from available cash balances. To finance the remainder of the purchase price, we entered into a six-month credit facility for $2 billion. During February 2004, we issued commercial paper backed by unused commitments under this facility. In March 2004, we issued $1.6 billion of senior unsecured notes in three maturity tranches: one, three and five years at $600 million, $500 million and $500 million, respectively. Net proceeds from the borrowings were used to repay the commercial paper backed by the six-month credit facility. We canceled the six-month credit facility in March 2004. See Note 6 for further discussion.

On March 1, 2002, a subsidiary of FedEx Trade Networks acquired for cash certain assets of Fritz Companies, Inc. that provide essential customs clearance services exclusively for FedEx Express in three U.S. locations, at a cost of $36.5 million. The excess cost over the estimated fair value of the net assets acquired (approximately $35 million) was recorded as goodwill, which was entirely attributed to the FedEx Express segment. Goodwill for tax purposes associated with this transaction will be deductible over 15 years. Pro forma results including this acquisition would not differ materially from reported results.

These acquisitions were accounted for under the purchase method of accounting. The operating results of the acquired businesses are included in our consolidated results of operations from the date of acquisition.

Note 3: Goodwill and Intangibles

Effective June 1, 2001, we adopted SFAS 142, "Goodwill and Other Intangible Assets," which establishes new accounting and reporting requirements for goodwill and other intangible assets. Under SFAS 142, material amounts of recorded goodwill attributable to each of our reporting units were tested for impairment by comparing the fair value of each reporting unit with its carrying value (including attributable goodwill). Fair value was determined using a discounted cash flow methodology. Based on our initial impairment tests when the statement was adopted, we recognized an adjustment of $25 million ($15 million or $0.05 per share, net of tax) in 2002 to reduce the carrying value of certain goodwill. Under SFAS 142, the impairment adjustment recognized at adoption of the new rules was reflected as a cumulative effect of accounting change in our 2002 consolidated statement of income.

The carrying amount of goodwill attributable to each reportable operating segment and changes therein follows (in millions):

	May 31, 2003	Goodwill Acquired During the Year	May 31, 2004
FedEx Express segment	$ 397	$ 130[1]	$ 527
FedEx Ground segment		70[1]	70
FedEx Freight segment	666		666
FedEx Kinko's segment		1,539	1,539
	$ 1,063	$ 1,739	$ 2,802

(1) These amounts represent goodwill from the FedEx Kinko's acquisition that is attributable to the FedEx Express and FedEx Ground segments.

The components of our intangible assets were as follows (in millions):

	May 31, 2004		May 31, 2003	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortizable intangible assets				
Customer relationships	$ 72	$ (3)	$	$
Contract related	79	(43)	73	(37)
Technology related and other	45	(17)	40	(12)
Total	$ 196	$ (63)	$ 113	$ (49)
Non-amortizing intangible asset				
Trade name	$ 567	$	$	$

Amortization expense for intangible assets was $14 million in 2004, $13 million in 2003 and $14 million in 2002. Estimated amortization expense for the next five years is as follows (in millions):

2005	$ 24
2006	23
2007	21
2008	20
2009	17

Note 4: Business Realignment Costs

During 2004, voluntary early retirement incentives with enhanced pension and postretirement healthcare benefits were offered to certain groups of employees at FedEx Express who were age 50 or older. Voluntary cash severance incentives were also offered to eligible employees at FedEx Express. These programs, which commenced August 1, 2003 and expired during the second quarter, were limited to eligible U.S. salaried staff employees and managers. Approximately 3,600 employees accepted offers under these voluntary programs, which considerably exceeded our expectations. Costs were also incurred in 2004 for the elimination of certain management positions at FedEx Express and other business units based on the staff reductions from the voluntary programs and other cost reduction initiatives.

Costs for the benefits provided under the voluntary programs were recognized in the period that eligible employees accepted the offer. Other costs associated with business realignment activities were recognized in the period incurred. The savings from these initiatives will be reflected primarily in lower salaries and benefits costs.

The components of our business realignment costs and changes in the related accruals were as follows for the year ended May 31, 2004 (in millions):

	Voluntary Retirement	Voluntary Severance	Other[1]	Total
Beginning accrual balances	$	$	$	$
Charged to expense	202	158	75	435
Cash paid	(8)	(152)	(31)	(191)
Amounts charged to other assets/liabilities	(194)		(22)	(216)
Ending accrual balances	$	$ 6	$ 22	$ 28

(1) Other includes costs for management severance agreements, which are payable over future periods, including compensation related to the modification of previously granted stock options and incremental pension and healthcare benefits. Other also includes professional fees directly associated with the business realignment initiatives and relocation costs.

Amounts charged to other assets/liabilities relate primarily to incremental pension and healthcare benefits.

Note 5: Selected Current Liabilities

The components of selected current liability captions were as follows (in millions):

	May 31, 2004	May 31, 2003
Accrued Salaries and Employee Benefits		
Salaries	$ 163	$ 119
Employee benefits	496	227
Compensated absences	403	378
	$ 1,062	$ 724
Accrued Expenses		
Self-insurance accruals	$ 442	$ 401
Taxes other than income taxes	291	279
Other	572	455
	$ 1,305	$ 1,135

	May 31,	

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Note 6: Long-Term Debt and Other Financing Arrangements

The components of our long-term debt were as follows (in millions):

	May 31,	
	2004	2003
Unsecured debt	$ 2,855	$ 1,529
Capital lease obligations	534	422
Other debt, interest rates of 2.35% to 9.98% due through 2017	198	66
	3,587	2,017
Less current portion	750	308
	$ 2,837	$ 1,709

At May 31, 2004, we had two revolving bank credit facilities totaling $1 billion. One revolver provides for $750 million through September 28, 2006. The second is a 364-day facility providing for $250 million through September 24, 2004. Interest rates on borrowings under the agreements are generally determined by maturities selected and prevailing market conditions. Borrowings under the credit agreements will bear interest, at our option, at a rate per annum equal to either (a) the London Interbank Offered Rate ("LIBOR") plus a credit spread, or (b) the higher of the Federal Funds Effective Rate, as defined, plus $^1/_2$ of 1%, or the bank's Prime Rate. The revolving credit agreements contain certain covenants and restrictions, none of which are expected to significantly affect our operations or ability to pay dividends.

From time to time, we finance certain operating and investing activities, including acquisitions, through the issuance of commercial paper. Our commercial paper program is backed by unused commitments under our revolving credit agreements and reduces the amounts available under the agreements. As of May 31, 2004 and 2003, no commercial paper borrowings were outstanding and the entire $1 billion under the revolving credit agreements was available.

The components of unsecured debt (net of discounts) were as follows (in millions):

	May 31,	
	2004	2003
Senior unsecured debt		
Interest rate of three-month LIBOR (1.11% at May 31, 2004) plus 0.28%, due in 2005	$ 600	$
Interest rate of 7.80%, due in 2007	200	200
Interest rate of 2.65%, due in 2007	500	
Interest rate of 3.50%, due in 2009	499	
Interest rates of 6.63% to 7.25%, due through 2011	499	747
Interest rate of 9.65%, due in 2013	299	299
Interest rate of 7.60%, due in 2098	239	239
Medium term notes, interest rates of 8.00% to 10.57%, due through 2007	19	44
	$ 2,855	$ 1,529

To finance our acquisition of FedEx Kinko's, we entered into a six-month credit facility for $2 billion. During February 2004, we issued commercial paper backed by unused commitments under this facility. In March 2004, we issued $1.6 billion of senior unsecured notes in three maturity tranches: one, three and five years, at $600 million, $500 million and $500 million, respectively. Net proceeds from these borrowings were used to repay the commercial paper backed by the six-month credit facility. We canceled the six-month credit facility in March 2004.

In conjunction with the acquisition of FedEx Freight East in February 2001, debt of $240 million was assumed, a portion of which was refinanced subsequent to the acquisition. On April 5, 2002, we prepaid the remaining $101 million. Under the debt agreements, we incurred a prepayment penalty of $13 million, which was included in other non-operating expense in 2002.

Capital lease obligations include certain special facility revenue bonds that have been issued by municipalities primarily to finance the acquisition and construction of various airport facilities and equipment. These bonds require interest payments at least annually with principal payments due at the end of the related lease agreements. In addition, during 2004, FedEx Express amended two leases for MD11 aircraft and during 2003, FedEx Express amended four leases for MD11 aircraft, which commit FedEx Express to firm purchase obligations for two of these aircraft during both 2005 and 2006. These amended leases were accounted for as capital leases from the date of amendment.

Other long-term debt includes $133 million related to two leased MD11 aircraft that are consolidated under the provisions of Financial Accounting Standards Board Interpretation No. ("FIN") 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." The debt requires interest at LIBOR plus a margin and is due in installments through March 30, 2007. See Note 16 for further discussion.

We incur other commercial commitments in the normal course of business to support our operations. Letters of credit at May 31, 2004 were $498 million. The amount unused under our letter of credit facility totaled $114 million at May 31, 2004. This facility expires in May of 2006. These instruments are generally required under certain U.S. self-insurance programs and are used in the normal course of international operations. The underlying liabilities insured by these instruments are reflected in the balance sheet, where applicable. Therefore, no additional liability is reflected for the letters of credit.

Scheduled annual principal maturities of debt, exclusive of capital leases, for the five years subsequent to May 31, 2004, are as follows (in millions):

2005	$ 613
2006	265
2007	844
2008	
2009	499

Long-term debt, exclusive of capital leases, had carrying values of $3.0 billion and $1.6 billion at May 31, 2004 and 2003, respectively, compared with estimated fair values of approximately $3.2 billion and $1.9 billion at those respective dates. The estimated fair values were determined based on quoted market prices or on the current rates offered for debt with similar terms and maturities.

We have a $1.0 billion shelf registration statement with the SEC to provide flexibility and efficiency when obtaining financing. Under this shelf registration statement we may issue, in one or more offerings, either unsecured debt securities, common stock or a combination of such instruments. The entire $1 billion is available for future financings.

Note 7: Lease Commitments

We utilize certain aircraft, land, facilities, retail locations and equipment under capital and operating leases that expire at various dates through 2039. In addition, supplemental aircraft are leased under agreements that generally provide for cancelation upon 30 days' notice.

The components of property and equipment recorded under capital leases were as follows (in millions):

	May 31,	
	2004	2003
Aircraft	$ 344	$ 221
Package handling and ground support equipment and vehicles	207	207
Other, principally facilities	230	137
	781	565
Less accumulated amortization	390	268
	$ 391	$ 297

Rent expense under operating leases was as follows (in millions):

	For years ended May 31,		
	2004	2003	2002
Minimum rentals	$ 1,560	$ 1,522	$ 1,453
Contingent rentals	143	107	132
	$ 1,703	$ 1,629	$ 1,585

Contingent rentals are based on equipment usage.

A summary of future minimum lease payments under capital leases and noncancelable operating leases (principally aircraft, retail locations and facilities) with an initial or remaining term in excess of one year at May 31, 2004 is as follows (in millions):

	Capital Leases	Operating Leases
2005	$ 160	$ 1,707
2006	122	1,555
2007	22	1,436
2008	99	1,329
2009	11	1,169
Thereafter	225	7,820
	639	$ 15,016
Less amount representing interest	105	
Present value of net minimum lease payments	$ 534	

FedEx Express makes payments under certain leveraged operating leases that are sufficient to pay principal and interest on certain pass-through certificates. The pass-through certificates are not direct obligations of, or guaranteed by, FedEx or FedEx Express.

Note 8: Preferred Stock

Our Certificate of Incorporation authorizes the Board of Directors, at its discretion, to issue up to 4,000,000 shares of series preferred stock. The stock is issuable in series, which may vary as to certain rights and preferences, and has no par value. As of May 31, 2004, none of these shares had been issued.

Note 9: Common Stockholders' Investment

TREASURY SHARES

The following table summarizes information about treasury share repurchases for the years ended May 31:

	2004		2003		2002	
	Shares	Average Price Per Share	Shares	Average Price Per Share	Shares	Average Price Per Share
Repurchased	2,625,000	$ 68.14	3,275,000	$ 56.66	3,350,000	$ 52.70

These repurchases were done under share repurchase programs aggregating 15 million shares. A total of 5.75 million shares remain under existing share repurchase authorizations. At May 31, 2004 and 2003, respectively, 4,760 and 406,304 shares remained outstanding in treasury.

STOCK COMPENSATION PLANS

Fixed Stock Option Plans. Under the provisions of our stock incentive plans, key employees and non-employee directors may be granted options to purchase shares of common stock at a price not less than its fair market value at the date of grant. Options granted have a maximum term of 10 years. Vesting requirements are determined at the discretion of the Compensation Committee of our Board of Directors. Option-vesting periods range from one to four years with more than 80% of stock option grants vesting ratably over 4 years. At May 31, 2004, there were 4,140,440 shares available for future grants under these plans.

The weighted-average fair value of these grants, calculated using the Black-Scholes valuation method under the assumptions indicated below, was $18.02, $17.12 and $12.39 per option in 2004, 2003 and 2002, respectively.

We are required to disclose the pro forma effect of accounting for stock options using such a valuation method for all options granted in 1996 and thereafter (see Note 1). We use the Black-Scholes option-pricing model to calculate the fair value of options for our pro forma disclosures. The key assumptions for this valuation method include the expected life of the option, stock price volatility, risk-free interest rate, dividend yield, forfeiture rate and exercise price. Many of these assumptions are judgmental and highly sensitive in the determination of pro forma compensation expense. Following is a table of the key weighted-average assumptions used in the option valuation calculations for the options granted in the years ended May 31, 2004, 2003 and 2002, and a discussion of our methodology for developing each of the assumptions used in the valuation model:

	May 31,		
	2004	**2003**	**2002**
Expected lives	4 years	4 years	4 years
Expected volatility	32%	35%	30%
Risk-free interest rate	2.118%	4.017%	4.777%
Dividend yield	0.3102%	0.3785%	0%

Expected Lives. This is the period of time over which the options granted are expected to remain outstanding. Generally, options granted have a maximum term of ten years. We examine actual stock option exercises to determine the expected life of the options. An increase in the expected term will increase compensation expense.

Expected Volatility. Actual changes in the market value of our stock are used to calculate the volatility assumption. We calculate daily market value changes from the date of grant over a past period equal to the expected life of the options to determine volatility. An increase in the expected volatility will increase compensation expense.

Risk-Free Interest Rate. This is the U.S. Treasury Strip rate posted at the date of grant having a term equal to the expected life of the option. An increase in the risk-free interest rate will increase compensation expense.

Dividend Yield. This is the annual rate of dividends per share over the exercise price of the option. In July 2002, we paid the first dividend in the history of the company. Therefore, the fair value of options prior to 2003 is not affected by the dividend yield. An increase in the dividend yield will decrease compensation expense.

Forfeiture Rate. This is the estimated percentage of options granted that are expected to be forfeited or canceled before becoming fully vested. This percentage is derived from historical experience. An increase in the forfeiture rate will decrease compensation expense. Our forfeiture rate is approximately 8%.

The following table summarizes information about our fixed stock option plans for the years ended May 31:

	2004		2003		2002	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of year	17,315,116	$ 38.88	17,306,014	$ 34.32	17,498,558	$ 30.24
Granted	3,937,628	64.96	3,261,800	53.22	4,023,098	40.66
Exercised	(3,724,605)	31.05	(2,951,154)	27.73	(3,875,767)	22.34
Forfeited	(178,832)	46.71	(301,544)	40.47	(339,875)	35.06
Outstanding at end of year	17,349,307	46.39	17,315,116	38.88	17,306,014	34.32
Exercisable at end of year	8,747,523	38.28	8,829,515	33.58	8,050,362	29.98

The following table summarizes information about fixed stock options outstanding at May 31, 2004:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$14.59 - $21.89	970,670	1.9 years	$ 19.15	970,670	$ 19.15
21.97 - 32.95	2,500,525	3.7 years	29.71	2,437,553	29.86
33.02 - 49.52	5,635,270	6.6 years	39.58	3,248,939	39.49
49.71 - 73.67	8,242,842	8.0 years	59.31	2,090,361	55.09
14.59 - 73.67	17,349,307	6.6 years	46.39	8,747,523	38.28

Total equity compensation shares outstanding or available for grant represented approximately 7.1% and 7.3% of total outstanding common and equity compensation shares and equity compensation shares available for grant at May 31, 2004 and May 31, 2003, respectively.

Stock Options Expensed. Under our business realignment programs discussed in Note 4, we recognized approximately $16 million of expense ($10 million, net of tax) during 2004 related to the modification of previously granted stock options. We calculated this expense using the Black-Scholes method.

Restricted Stock Plans. Under the terms of our restricted stock plans, shares of common stock are awarded to key employees. All restrictions on the shares expire ratably over a four-year period. Shares are valued at the market price at the date of award. Compensation related to these plans is recorded as a reduction of common stockholders' investment and is amortized to expense as restrictions on such shares expire.

The following table summarizes information about restricted stock awards for the years ended May 31:

	2004		2003		2002	
	Shares	Weighted-Average Fair Value	Shares	Weighted-Average Fair Value	Shares	Weighted-Average Fair Value
Awarded	282,423	$ 67.11	343,500	$ 47.56	329,500	$ 43.01
Forfeited	10,000	43.41	17,438	48.01	12,000	49.79

At May 31, 2004, there were 747,553 shares available for future awards under these plans. Annual compensation cost for the restricted stock plans was approximately $14 million for 2004, and $12 million for 2003 and 2002.

Note 10: Computation of Earnings Per Share

The calculation of basic earnings per common share and diluted earnings per common share for the years ended May 31 was as follows (in millions, except per share amounts):

	2004	2003	2002
Net income applicable to common stockholders	$ 838	$ 830	$ 710
Weighted-average shares of common stock outstanding	299	298	298
Common equivalent shares:			
Assumed exercise of outstanding dilutive options	19	15	16
Less shares repurchased from proceeds of assumed exercise of options	(14)	(10)	(11)
Weighted-average common and common equivalent shares outstanding	304	303	303
Basic earnings per common share	$ 2.80	$ 2.79	$ 2.38
Diluted earnings per common share	$ 2.76	$ 2.74	$ 2.34

Note 11: Income Taxes

The components of the provision for income taxes for the years ended May 31 were as follows (in millions):

	2004	2003	2002
Current provision			
Domestic:			
Federal	$ 371	$ 112	$ 255
State and local	54	28	39
Foreign	85	39	41
	510	179	335
Deferred (benefit) provision			
Domestic:			
Federal	(22)	304	99
State and local	(7)	25	3
Foreign			(2)
	(29)	329	100
	$ 481	$ 508	$ 435

A reconciliation of the statutory federal income tax rate to the effective income tax rate for the years ended May 31 was as follows:

	2004	2003	2002
Statutory U.S. income tax rate	35.0%	35.0%	35.0%
Increase resulting from:			
State and local income taxes, net of federal benefit	2.3	2.6	2.4
Other, net	(0.8)	0.4	0.1
Effective tax rate	36.5%	38.0%	37.5%

The lower effective tax rate in 2004 was primarily attributable to the favorable decision in our U.S. tax case described below, stronger than anticipated international results and the results of tax audits during 2004. Our stronger than anticipated international results, along with other factors, increased our ability to credit income taxes paid to foreign governments on foreign income against U.S. income taxes paid on the same income, thereby mitigating our exposure to double taxation. The 38.0% effective tax rate in 2003 was higher than the 2002 rate primarily due to lower state taxes in 2002.

The significant components of deferred tax assets and liabilities as of May 31 were as follows (in millions):

	2004		2003	
	Deferred Tax Assets	Deferred Tax Liabilities	Deferred Tax Assets	Deferred Tax Liabilities
Property, equipment, leases and intangibles	$ 310	$ 1,372	$ 303	$ 946
Employee benefits	386	406	270	407
Self-insurance accruals	297		259	
Other	277	179	261	207
Net operating loss/credit carryforwards	32		15	
Valuation allowance	(37)		(14)	
	$ 1,265	$ 1,957	$ 1,094	$ 1,560

In 2004, the net deferred tax liability of $692 million is classified in the balance sheet as a current deferred tax asset of $489 million and a non-current deferred tax liability of $1.181 billion. In 2003, the net deferred tax liability of $466 million is classified in the balance sheet as a current deferred tax asset of $416 million and a non-current deferred tax liability of $882 million.

The valuation allowance primarily represents amounts reserved for operating loss and tax credit carryforwards, which expire over varying periods starting in 2005. As a result of this and other factors, we believe that a substantial portion of these deferred tax assets may not be realized. The net increase in the valuation allowance of $23 million was principally due to net operating loss/credit carryforwards obtained upon the acquisition of FedEx Kinko's during the third quarter of 2004 that are not expected to be realized.

In August 2003, we received a favorable ruling from the U.S. District Court in Memphis over the tax treatment of jet engine maintenance costs. The Court held that these costs were ordinary and necessary business expenses and properly deductible by us. In connection with an Internal Revenue Service ("IRS") audit for the tax years 1993 and 1994, the IRS had proposed adjustments characterizing routine jet engine maintenance costs as capital expenditures that must be recovered over seven years, rather than as expenses that are deducted immediately, as has been our practice. After settlement discussions failed to resolve this matter, in 2001 we paid $70 million in tax and interest and filed suit in Federal District Court for a complete refund of the amounts paid plus interest. Although the IRS has continued to assert its position in audits for the years 1995 through 2000 with respect to maintenance costs for jet engines and rotable aircraft parts, we believe this ruling should also apply to future tax years.

As a result of this ruling, we recognized a one-time benefit in 2004 of $26 million, net of tax, primarily related to the reduction of accruals related to this matter and the recognition of interest earned on the amount we paid in 2001. These adjustments affected both net interest expense ($30 million pre-tax) and income tax expense ($7 million). Future periods are not expected to be materially affected by the resolution of this matter. On November 19, 2003, the IRS appealed this ruling to the Sixth Circuit Court of Appeals. All briefs have been filed in the case. We believe the District Court's ruling will be upheld on appeal.

Note 12: Employee Benefit Plans

Pension Plans. We sponsor defined benefit pension plans covering a majority of our employees. The largest plan covers certain U.S. employees age 21 and over, with at least one year of service. Eligible employees as of May 31, 2003 were given the opportunity to make a one-time election to accrue future pension benefits under either a new cash balance formula which we call the Portable Pension Account or a traditional pension benefit formula. Benefits provided under the traditional formula are based on average earnings and years of service. Under the Portable Pension Account, the retirement benefit is expressed as a dollar amount in a notional account that grows with annual credits based on pay, age, and years of credited service, and interest on the notional account balance. In either case, employees retained all benefits previously accrued under the traditional pension benefit formula and continue to receive the benefit of future salary increases on benefits accrued as of May 31, 2003. Eligible employees hired after May 31, 2003 receive benefits exclusively under the Portable Pension Account.

Plan funding is actuarially determined and is subject to certain tax law limitations. International defined benefit pension plans provide benefits primarily based on final earnings and years of service and are funded in accordance with local laws and income tax regulations. Substantially all plan assets are actively managed. The weighted-average asset allocation for our primary pension plan at February 29, 2004 was as follows:

	Actual	Target
Domestic equities	54%	53%
International equities	19	17
Private equities	3	5
Long duration fixed income securities	16	15
Other fixed income securities	8	10
	100%	100%

The investment strategy for pension plan assets is to utilize a diversified mix of global public and private equity portfolios, together with public and private fixed income portfolios, to earn a long-term investment return that meets our pension plan obligations. Active management strategies are utilized within the plan in an effort to realize investment returns in excess of market indices.

Our pension cost is materially affected by the discount rate used to measure pension obligations, the level of plan assets available to fund those obligations at the measurement date and the expected long-term rate of return on plan assets. Due to a lower discount rate, a lower expected long-term rate of return and a reduction in the value of plan assets as a result of investment losses at the measurement date for 2004 pension expense (February 28, 2003), our total net pension cost for 2004 increased by approximately $115 million.

An increase in pension cost of approximately $30 million is expected for 2005 based primarily on a continuing decline in the discount rate (to 6.78%). Management reviews the assumptions used to measure pension costs (including the discount rate and the expected long-term rate of return on pension assets) on an annual basis. Economic and market conditions at the measurement date impact these assumptions from year to year and it is reasonably possible that material changes in pension cost may continue to be experienced in the future.

Establishing the expected future rate of investment return on our pension assets is a judgmental matter. Management considers the following factors in determining this assumption:

- the duration of our pension plan liabilities, which drives the investment strategy we can employ with our pension plan assets.

- the types of investment classes in which we invest our pension plan assets and the expected compound return we can reasonably expect those investment classes to earn over the next 10- to 15-year time period (or such other time period that may be appropriate).

- the investment returns we can reasonably expect our active investment management program to achieve in excess of the returns we could expect if investments were made strictly in indexed funds.

We review the expected long-term rate of return on an annual basis and revise it as appropriate. Also, we periodically commission detailed asset/liability studies performed by third-party professional investment advisors and actuaries. These studies project our estimated future pension payments and evaluate the efficiency of the allocation of our pension plan assets into various investment categories. These studies also generate probability-adjusted expected future returns on those assets. The study performed for 2003 supported the reasonableness of our 10.10% return assumption used for 2003 based on our liability duration and market conditions at the time we set this assumption (in 2002). We performed a more recent asset/liability study for 2004, which supported a long-term return on assets of 9.10%. The results of this study were reaffirmed for 2005 by our third-party professional investment advisors and actuaries.

Postretirement Healthcare Plans. Certain of our subsidiaries offer medical, dental and vision coverage to eligible U.S. retirees and their eligible dependents. U.S. employees covered by the principal plan become eligible for these benefits at age 55 and older, if they have permanent, continuous service of at least 10 years after attainment of age 45 if hired prior to January 1, 1988, or at least 20 years after attainment of age 35 if hired on or after January 1, 1988.

The following table provides a reconciliation of the changes in the pension and postretirement healthcare plans' benefit obligations and fair value of assets over the two-year period ended May 31, 2004 and a statement of the funded status as of May 31, 2004 and 2003 (in millions):

	Pension Plans		Postretirement Healthcare Plans	
	2004	**2003**	**2004**	**2003**
Changes in Projected Benefit Obligation ("PBO")				
Projected benefit obligation at the beginning of year	$ 7,117	$ 6,227	$ 382	$ 329
Service cost	376	374	35	27
Interest cost	490	438	25	25
Actuarial loss	661	164	36	23
Benefits paid	(136)	(103)	(23)	(21)
Special termination benefits(1)	158		38	
Amendments, benefit enhancements and other	17	17	3	(1)
Projected benefit obligation at the end of year	$ 8,683	$ 7,117	$ 496	$ 382
Accumulated Benefit Obligation ("ABO")	$ 7,427	$ 6,009		
Change in Plan Assets				
Fair value of plan assets at beginning of year	$ 5,825	$ 5,510	$	$
Actual return (loss) on plan assets	1,751	(663)		
Company contributions	335	1,072	16	18
Benefits paid	(136)	(103)	(23)	(21)
Other	8	9	7	3
Fair value of plan assets at end of year	$ 7,783	$ 5,825	$	$
Funded Status of the Plans	$ (900)	$ (1,292)	$ (496)	$ (382)
Unrecognized actuarial loss (gain)	1,694	2,247	(1)	(38)
Unamortized prior service cost (benefit)	118	123	1	(1)
Unrecognized transition amount	(5)	(7)		
Prepaid (accrued) benefit cost	$ 907	$ 1,071	$ (496)	$ (421)
Amount Recognized in the Balance Sheet at May 31:				
Prepaid benefit cost	$ 1,127	$ 1,269	$	$
Accrued benefit liability	(220)	(198)	(496)	(421)
Minimum pension liability	(67)	(42)		
Accumulated other comprehensive income(2)	54	26		
Intangible asset	13	16		
Prepaid (accrued) benefit cost	$ 907	$ 1,071	$ (496)	$ (421)

(1) The special termination benefits reflected in the table above related primarily to early retirement incentives offered to certain groups of our employees at FedEx Express during 2004 (see Note 4 for more information).

(2) The minimum pension liability component of Accumulated Other Comprehensive Income is shown in the Statement of Changes in Stockholders' Investment and Comprehensive Income, net of deferred taxes.

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Our pension plans included the following components at May 31, 2004 and 2003 (in millions):

	U.S. Plans							
	Qualified		Nonqualified		International Plans		Total	
	2004	2003	2004	2003	2004	2003	2004	2003
ABO	$ 7,069	$ 5,725	$ 166	$ 130	$ 192	$ 154	$ 7,427	$ 6,009
PBO	$ 8,274	$ 6,793	$ 179	$ 144	$ 230	$ 180	$ 8,683	$ 7,117
Fair Value of Plan Assets	7,678	5,747			105	78	7,783	5,825
Funded Status	$ (596)	$ (1,046)	$ (179)	$ (144)	$ (125)	$ (102)	$ (900)	$ (1,292)
Unrecognized actuarial loss	1,621	2,208	32	5	41	34	1,694	2,247
Unamortized prior service cost	95	105	20	18	3		118	123
Unrecognized transition amount	(7)	(8)			2	1	(5)	(7)
Prepaid (accrued) benefit cost	$ 1,113	$ 1,259	$ (127)	$ (121)	$ (79)	$ (67)	$ 907	$ 1,071

The projected benefit obligation ("PBO") is the actuarial present value of benefits attributable to employee service rendered to date, including the effects of estimated future pay increases. The accumulated benefit obligation ("ABO") also reflects the actuarial present value of benefits attributable to employee service rendered to date, but does not include the effects of estimated future pay increases. Therefore, the ABO as compared to plan assets is an indication of the assets currently available to fund vested and nonvested benefits accrued through May 31.

The measure of whether a pension plan is underfunded for financial accounting purposes is based on a comparison of the ABO to the fair value of plan assets and amounts accrued for such benefits in the balance sheet. In order to eliminate the need to recognize an additional minimum pension liability (generally required when the ABO exceeds the fair value of plan assets at the measurement date), we made $1.1 billion of tax-deductible contributions to our qualified U.S. pension plans in 2003. In 2004, we made $320 million in tax-deductible contributions. No contributions for 2004 or 2003 were legally required and none are expected to be required in 2005. Based on the substantial improvement in the funded status of our qualified plans, we do not currently expect to contribute any funds to our qualified defined benefit plans in 2005.

We have certain nonqualified defined benefit pension plans that are not funded because such funding would be deemed current compensation to plan participants. Primarily related to those plans and certain international plans, we have ABOs aggregating approximately $356 million at May 31, 2004 and $284 million at May 31, 2003, with assets of $105 million at May 31, 2004 and $78 million at May 31, 2003. Plans with this funded status resulted in the recognition of a minimum pension liability in our balance sheets. This minimum liability was $67 million at May 31, 2004 and $42 million at May 31, 2003.

Net periodic benefit cost for the three years ended May 31 was as follows (in millions):

	Pension Plans			Postretirement Healthcare Plans		
	2004	2003	2002	2004	2003	2002
Service cost	$ 376	$ 374	$ 348	$ 35	$ 27	$ 27
Interest cost	490	438	409	25	25	25
Expected return on plan assets	(597)	(594)	(621)			
Net amortization and deferral	74	10	13		(2)	(2)
	$ 343	$ 228	$ 149	$ 60	$ 50	$ 50

Weighted-average actuarial assumptions for our primary U.S. plans, which comprise substantially all of our projected benefit obligations, were as follows:

	Pension Plans			Postretirement Healthcare Plans		
	2004	2003	2002	2004	2003	2002
Discount rate	6.78%	6.99%	7.11%	6.57%	6.75%	7.30%
Rate of increase in future compensation levels	3.15	3.15	3.25			
Expected long-term rate of return on assets	9.10*	10.10	10.90			

* For 2005, the expected long-term rate of return on plan assets will continue to be 9.10%.

The expected long-term rate of return assumptions for each asset class are selected based on historical relationships between the assets classes and the economic and capital market environments, updated for current conditions.

Benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows for the years ending May 31 (in millions):

	Pension Benefits
2005	$ 216
2006	219
2007	257
2008	283
2009	319
2010-2014	2,389

These estimates are based on assumptions about future events. Actual benefit payments may vary significantly from these estimates.

Future medical benefit costs are estimated to increase at an annual rate of 14% during 2005, decreasing to an annual growth rate of 5% in 2019 and thereafter. Future dental benefit costs are estimated to increase at an annual rate of 7% during 2005, decreasing to an annual growth rate of 5% in 2013 and thereafter. Our postretirement healthcare cost is capped at 150% of the 1993 employer cost and, therefore, is not subject to medical and dental trends after the capped cost is attained. Therefore, a 1% change in these annual trend rates would not have a significant impact on the accumulated postretirement benefit obligation at May 31, 2004, or 2004 benefit expense.

Defined Contribution Plans. Profit sharing and other defined contribution plans are in place covering a majority of U.S. employees. Profit sharing plans provide for discretionary employer contributions, which are determined annually by our Board of Directors. Other plans provide matching funds based on employee contributions to 401(k) plans. Expense under these plans was $89 million in 2004, $82 million in 2003 and $75 million in 2002.

Note 13: Business Segment Information

Our operations for the periods presented are primarily represented by FedEx Express, FedEx Ground, FedEx Freight and FedEx Kinko's. These businesses form the core of our reportable segments. Other business units in the FedEx portfolio are FedEx Trade Networks, FedEx Supply Chain Services, FedEx Custom Critical and Caribbean Transportation Services. Management evaluates segment financial performance based on operating income.

In 2004, we changed the reporting and responsibility relationships of our smaller business units so that they now report directly to a core segment. Prior year amounts have been reclassified to conform to the new segment presentation. As a result, our reportable segments included the following businesses for the periods presented:

FedEx Express Segment	FedEx Express FedEx Trade Networks
FedEx Ground Segment	FedEx Ground FedEx Supply Chain Services
FedEx Freight Segment	FedEx Freight FedEx Custom Critical Caribbean Transportation Services
FedEx Kinko's Segment	FedEx Kinko's

The following table provides a reconciliation of reportable segment revenues, depreciation and amortization, operating income (loss) and segment assets to consolidated financial statement totals for the years ended or as of May 31 (in millions):

	FedEx Express Segment	FedEx Ground Segment	FedEx Freight Segment	FedEx Kinko's Segment(1)	Other and Eliminations(2)	Consolidated Total
Revenues						
2004	$ 17,497	$ 3,910	$ 2,689	$ 521	$ 93	$ 24,710
2003	16,467	3,581	2,443		(4)	22,487
2002	15,438	2,918	2,253		(2)	20,607
Depreciation and amortization						
2004	$ 810	$ 154	$ 92	$ 33	$ 286	$ 1,375
2003	818	155	88		290	1,351
2002	819	136	91		318	1,364
Operating income (loss)(3)						
2004	$ 629	$ 522	$ 244	$ 39	$ 6	$ 1,440
2003	783	494	193		1	1,471
2002	801	337	185		(2)	1,321
Segment assets(4)						
2004	$ 12,443	$ 2,248	$ 1,924	$ 2,903	$ (384)	$ 19,134
2003	11,188	1,846	1,825		526	15,385
2002	10,151	1,480	1,786		395	13,812

(1) Includes the operations of FedEx Kinko's from the formation of the FedEx Kinko's segment on March 1, 2004.

(2) Includes the results of operations of FedEx Kinko's from February 12, 2004 (date of acquisition) through February 29, 2004 (approximately $100 million of revenue and $6 million of operating income).

(3) Includes business realignment costs of $428 million in the FedEx Express segment, $1 million in the FedEx Ground segment and $6 million in Other and Eliminations.

(4) Segment assets include intercompany receivables.

The following table provides a reconciliation of reportable segment capital expenditures to consolidated totals for the years ended May 31 (in millions):

	FedEx Express Segment	FedEx Ground Segment	FedEx Freight Segment	FedEx Kinko's Segment	Other	Consolidated Total
2004	$ 592	$ 314	$ 130	$ 36	$ 199	$ 1,271
2003	917	252	139		203	1,511
2002	1,069	214	86		246	1,615

The following table presents revenue by service type and geographic information for the years ended or as of May 31 (in millions):

	2004	2003	2002
REVENUE BY SERVICE TYPE			
FedEx Express segment:			
Package:			
U.S. overnight box	$ 5,558	$ 5,432	$ 5,338
U.S. overnight envelope	1,700	1,715	1,755
U.S. deferred	2,592	2,510	2,383
Total domestic package revenue	9,850	9,657	9,476
International priority	5,131	4,367	3,834
Total package revenue	14,981	14,024	13,310
Freight:			
U.S.	1,609	1,564	1,273
International	393	400	384
Total freight revenue	2,002	1,964	1,657
Other	514	479	471
Total FedEx Express segment	17,497	16,467	15,438
FedEx Ground segment	3,910	3,581	2,918
FedEx Freight segment	2,689	2,443	2,253
FedEx Kinko's segment(1)	521		
Other and Eliminations(2)	93	(4)	(2)
	$ 24,710	$ 22,487	$ 20,607
GEOGRAPHICAL INFORMATION(3)			
Revenues:			
U.S.	$ 18,643	$ 17,277	$ 15,968
International	6,067	5,210	4,639
	$ 24,710	$ 22,487	$ 20,607
Non-current assets:			
U.S.	$ 12,644	$ 9,908	$ 8,627
International	1,520	1,536	1,520
	$ 14,164	$ 11,444	$ 10,147

(1) Includes the operations of FedEx Kinko's from the formation of the FedEx Kinko's segment on March 1, 2004.

(2) Includes the results of operations of FedEx Kinko's from February 12, 2004 (date of acquisition) through February 29, 2004 (approximately $100 million of revenue).

(3) International revenue includes shipments that either originate in or are destined to locations outside the United States. Non-current assets include property and equipment, goodwill and other long-term assets. Flight equipment is allocated between geographic areas based on usage.

Note 14: Supplemental Cash Flow Information

Cash paid for interest expense and income taxes for the years ended May 31 was as follows (in millions):

	2004	2003	2002
Interest (net of capitalized interest)	$ 151	$ 125	$ 146
Income taxes	364	53	312

FedEx Express amended two leases in 2004 and four leases in 2003 for MD11 aircraft, which required FedEx Express to record $110 million in 2004 and $221 million in 2003, in both fixed assets and long-term liabilities.

FedEx Express consolidated an entity that owns two MD11 aircraft under the provisions of FIN 46. The consolidation of this entity on September 1, 2003 resulted in an increase in our fixed assets and long-term liabilities of approximately $140 million. See Note 16.

Note 15: Guarantees and Indemnifications

We adopted FIN 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others," during 2003, which required the prospective recognition and measurement of certain guarantees and indemnifications. Accordingly, any contractual guarantees or indemnifications we have issued or modified subsequent to December 31, 2002 are subject to evaluation. If required, a liability for the fair value of the obligation undertaken will be recognized.

Substantially all of our guarantees and indemnifications were entered into prior to December 31, 2002 and have not been modified since then. Therefore, no amounts have been recognized in our financial statements for the underlying fair value of these obligations. With the exception of residual value guarantees in certain operating leases, a maximum obligation is generally not specified in our guarantees and indemnifications. As a result, the overall maximum potential amount of the obligation under such guarantees and indemnifications cannot be reasonably estimated. Historically, we have not been required to make significant payments under our guarantee or indemnification obligations.

Operating Leases. We have guarantees under certain operating leases, amounting to $43 million as of May 31, 2004, for the residual values of vehicles and facilities at the end of the respective operating lease periods. Under these leases, if the fair market value of the leased asset at the end of the lease term is less than an agreed-upon value as set forth in the related operating lease agreement, we will be responsible to the lessor for the amount of such deficiency. Based upon our expectation that none of these leased assets will have a residual value at the end of the lease term that is materially less than the value specified in the related operating lease agreement, we do not believe it is probable that we will be required to fund any amounts under the terms of these guarantee arrangements. Accordingly, no accruals have been recognized for these guarantees.

Certain of our operating leases contain other indemnification obligations to the lessor, which are considered ordinary and customary (e.g., use and environmental indemnifications). The terms of these obligations range in duration and often are not limited. Such indemnification obligations continue until and, in many cases, after expiration of the respective lease.

Other Contracts. In conjunction with certain transactions, primarily sales or purchases of operating assets or services in the ordinary course of business, we sometimes provide routine indemnifications (e.g., environmental, tax and software infringement), the terms of which range in duration and often are not limited.

Intra-company Guarantees. FedEx's publicly held debt (approximately $2.3 billion) is guaranteed by our subsidiaries. The guarantees are full and unconditional, joint and several and any subsidiaries that are not guarantors are minor as defined by Securities and Exchange Commission regulations. FedEx, as the parent company issuer of this debt, has no independent assets or operations. There are no significant restrictions on our ability or the ability of any guarantor to obtain funds from its subsidiaries by such means as a dividend or loan.

Special facility revenue bonds have been issued by certain municipalities primarily to finance the acquisition and construction of various airport facilities and equipment. In certain cases, the bond proceeds were loaned to FedEx Express and are included in long-term debt and, in other cases, the facilities were leased to us and are accounted for as either capital leases or operating leases. Approximately $800 million in principal of these bonds (with total future principal and interest payments of approximately $1.5 billion as of May 31, 2004) is unconditionally guaranteed by FedEx Express. Of the $800 million bond principal, $45 million was in long-term debt and $204 million was in capital lease obligations at May 31, 2004 and the remainder was in operating leases.

Note 16: Variable Interest Entities

FedEx Express entered into a lease in July 2001 for two MD11 aircraft. These assets are held by a separate entity, which was established and is owned by independent third parties who provide financing through debt and equity participation. The original cost of the assets under the lease was approximately $150 million.

This lease contains residual value guarantees that obligate FedEx Express, not the third-party owners, to absorb the majority of the losses, if any, of the entity. The lease also provides FedEx Express with the right to receive any residual returns of the entity if they occur. At May 31, 2004, the residual value guarantee associated with this lease, which represents the maximum exposure to loss, was $89 million. FIN 46 required us to consolidate the separate entity that owns the two MD11 aircraft. Since the entity was created before February 1, 2003, we measured the assets and liabilities at their carrying amounts (the amounts at which they would have been recorded in the consolidated financial statements if FIN 46 had been effective at the inception of the lease). As a result of this consolidation, the accompanying May 31, 2004 balance sheet includes an additional $126 million of fixed assets and $133 million of long-term liabilities.

Note 17: Commitments

Annual purchase commitments under various contracts as of May 31, 2004 were as follows (in millions):

	Aircraft	Aircraft-Related[1]	Other[2]	Total
2005	$ 22	$ 170	$ 409	$ 601
2006		136	119	255
2007	111	97	44	252
2008	131	67	14	212
2009	567	63	13	643
Thereafter	1,141	119	179	1,439

(1) Primarily aircraft modifications.

(2) Primarily vehicles, facilities, computers, printing and other equipment and advertising and promotions contracts.

The amounts reflected in the table above for purchase commitments represent noncancelable agreements to purchase goods or services. Such contracts include those for certain purchases of aircraft, aircraft modifications, vehicles, facilities, computers, printing and other equipment and advertising and promotions contracts. Open purchase orders that are cancelable are not considered unconditional purchase obligations for financial reporting purposes.

FedEx Express is committed to purchase two A310s, seven ATRs and ten Airbus A380s (a new high-capacity, long-range aircraft). The A310s and ATRs are expected to be delivered in 2005. FedEx Express expects to take delivery of three of the ten A380 aircraft in each of 2009, 2010 and 2011 and the remaining one in 2012. Deposits and progress payments of $25 million have been made toward these purchases and other planned aircraft-related transactions. In addition, we have committed to modify our DC10 aircraft for passenger-to-freighter and two-man cockpit configurations. Payments related to these activities are included in the table above. Aircraft and aircraft-related contracts are subject to price escalations.

Note 18: Legal Proceedings

Operations in 2002 were significantly affected by the terrorist attacks on September 11, 2001. During 2002, we recognized a total of $119 million of compensation under the Air Transportation Safety and System Stabilization Act (the "Act"), of which $101 million had been received as of May 31, 2004. The amounts recognized were for our estimate of losses we incurred as a result of the mandatory grounding of our aircraft and for incremental losses incurred through December 31, 2001. All amounts recognized were reflected as reduction of operating expense under the caption "Airline stabilization compensation."

In the fourth quarter of 2003, the Department of Transportation ("DOT") asserted that we were overpaid by $31.6 million and has demanded repayment. We have filed requests for administrative and judicial review. We received an opinion from the District of Columbia U.S. Court of Appeals stating that most of the determinations that we requested were not yet ripe for decision and the Court will not rule prior to final determination by the DOT and exhaustion of administrative remedies.

Pursuant to the Federal Aviation Administration reauthorization enacted during the third quarter of 2004, the General Accounting Office submitted a report to Congress on June 4, 2004, on the criteria and procedures used by the Secretary of Transportation under the Act. Issuance of the report frees the DOT to make a final determination on our claim and also reinforces the Congressional directive to the DOT to refer any remaining disputed claims to an administrative law judge upon an affected claimant's request.

We agreed to mediation with the DOT, but it did not result in a resolution of the dispute. We will continue to pursue our claim for compensation under the Act.

We believe that we have complied with all aspects of the Act, that it is probable we will ultimately collect the remaining $18 million receivable and that we will not be required to pay any portion of the DOT's $31.6 million demand. We cannot be assured of the ultimate outcome; however, it is reasonably possible that a material reduction to the $119 million of compensation we have previously recognized under the Act could occur. Based on the DOT's assertion, the range for potential loss on this matter is zero to $49.6 million.

We are a defendant in a number of lawsuits filed in California state courts containing various class-action allegations under California's wage and hour laws. The plaintiffs in these lawsuits generally are hourly employees of FedEx operating companies who allege, among other things, that they were forced to work "off the clock" and were not provided work breaks. The plaintiffs generally seek unspecified monetary damages, injunctive relief, or both. To date, only one of these cases has been certified as a class action. We believe that the claims in these cases are without merit. We have denied any liability with respect to these claims and intend to vigorously defend ourselves in these cases. In the opinion of management, the aggregate liability, if any, with respect to these claims will not materially adversely affect our financial position, results of operations or cash flows.

Also, see Note 11 for discussion of other legal proceedings. FedEx and its subsidiaries are subject to other legal proceedings that arise in the ordinary course of their business. In the opinion of management, the aggregate liability, if any, with respect to these other actions will not materially adversely affect our financial position, results of operations or cash flows.

Note 19: Related Party Transactions

In November 1999, FedEx entered into a multi-year naming rights agreement with the National Football League Washington Redskins professional football team. Under this agreement, FedEx has certain marketing rights, including the right to name the Redskins' stadium "FedExField." In August 2003, Frederick W. Smith, Chairman, President and Chief Executive Officer of FedEx, personally acquired an approximate 10% ownership interest in the Washington Redskins and joined its board of directors.

Mr. Smith's son-in-law is a 50% owner of a company that provides insurance brokerage and consulting services in connection with certain insurance and legal services plan benefits offered by FedEx to certain of its employees. Mr. Smith's son-in-law's company is paid commissions and fees directly by the benefit providers and not FedEx. During fiscal 2004, such commissions and fees totaled approximately $497,000

A member of our Board of Directors, J.R. Hyde, III, and his wife together own approximately 13% of HOOPS, L.P. ("HOOPS"), the owner of the NBA Memphis Grizzlies professional basketball team. Mr. Hyde, through one of his companies, also is the general partner of the minority limited partner of HOOPS. During 2002, FedEx entered into a multi-year, $90 million naming rights agreement with HOOPS that will be amortized to expense over the life of the agreement. Under this agreement, FedEx has certain marketing rights, including the right to name the new arena where the Grizzlies will play. Pursuant to a separate agreement with HOOPS, the City of Memphis and Shelby County, FedEx has agreed to pay $2.5 million a year for the balance of the 25-year term of the agreement if HOOPS terminates its lease for the new arena after 17 years. FedEx also purchased $2 million of municipal bonds issued by the Memphis and Shelby County Sports Authority, the proceeds of which are to be used to finance a portion of the construction costs of the new arena.

On March 26, 2004, FedEx purchased an aggregate of 94 acres of real estate in Olive Branch, Mississippi for $4.7 million. FedEx proposes to construct a FedEx Ground hub on this site, which is just south of Memphis. The 94-acre site is divided into three parcels, two of which were owned by entities in which Mr. Hyde has a 50% ownership interest. These two parcels total approximately 3.4 acres. An independent appraisal of the property determined its fair market value to be not less than the negotiated purchase price.

Note 20: Summary of Quarterly Operating Results (Unaudited)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(in millions, except per share amounts)			
2004[(1)]				
Revenues	$ 5,687	$ 5,920	$ 6,062	$ 7,041
Operating income	200[(2)]	183[(4)]	372	685
Net income	128[(2)(3)]	91[(4)]	207	412[(5)]
Basic earnings per common share[(6)]	0.43[(2)(3)]	0.31[(4)]	0.69	1.38[(5)]
Diluted earnings per common share	0.42[(2)(3)]	0.30[(4)]	0.68	1.36[(5)]
2003				
Revenues	$ 5,445	$ 5,667	$ 5,545	$ 5,830
Operating income	283	427	269	492
Net income	158	245	147	280
Basic earnings per common share[(6)]	0.53	0.82	0.49	0.94
Diluted earnings per common share	0.52	0.81	0.49	0.92

(1) Includes FedEx Kinko's from February 12, 2004 (date of acquisition). See Note 2.

(2) Includes $132 million ($82 million, net of tax, $0.28 per share, or $0.27 per diluted share) of business realignment costs described in Note 4.

(3) Includes $26 million, net of tax ($0.09 per share or $0.08 per diluted share) related to a favorable ruling on an IRS case described in Note 11.

(4) Includes $283 million ($175 million, net of tax, $0.59 per share, or $0.57 per diluted share) of business realignment costs described in Note 4.

(5) Includes a $12 million ($0.04 per share and per diluted share) nonrecurring benefit related to the reduction of our effective tax rate. See Note 11.

(6) The sum of the quarterly earnings per share may not equal annual amounts due to differences in the weighted-average number of shares outstanding during the respective periods.

EXHIBIT INDEX

Exhibit Number	Description of Exhibit
23	Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm.
31.1	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

QuickLinks