Company Report **Airlines** | **Turkey** | **4 February 2009**

Turkish Airlines

Strong growth with high cost efficiency

Resumption of coverage. Turkish Airlines, Turkey's national flag carrier, established in 1933 by the State with just five aircraft, today is a well-known brand name with a 127-strong fleet. It uses Istanbul Ataturk Airport as its main hub, conveniently bridging East and West, and flies to 145 destination points. Turkish Airlines currently trades at a 26% discount to the European median EV/EBITDAR of 3.8x and a 32% discount to P/BV of 0.5x. Based on a multi-stage DCF valuation and average EV/EBITDAR multiple of 3.0x (50%/50% weights), we derived a 12M target price of TRY 9.45. At a 2.8x EV/EBITDAR and 0.3x P/BV for 2009E, and given a 51% upside, we resume coverage with a Buy rating.

Still growing in a tough environment. In 2008, Turkish Airlines' RPK grew by 13% y-o-y to 34bn, while the total PAX increased by 15% y-o-y to 23mn compared to a 1.0% y-o-y decline in European airlines' PAX over Jan-Nov 08. The number of transit and business class passengers went up by 41% and 23% y-o-y, respectively, largely due to its Star Alliance membership. We forecast a 6% CAGR in PAX with an average load factor of 72.7% over 2009-2013, compared to management's 2009E guidance of 15% PAX growth and a 75% load factor.

Significant unit labour cost advantage over its international peers. At the current EUR 0.013 labour cost per ASK vs. the European peer average of EUR 0.018, Turkish Airlines should continue delivering superior profitability in the medium term. Turkey's cheap labour pool should help the company maintain this key advantage in the foreseeable future.

Strong and liquid balance sheet. With a net debt (including capitalized operating leases) of TRY 2.1bn (0.7x 08E BV, 1.7x 08E EBITDAR), Turkish Airlines is not burdened with heavy debt, which is a positive factor in tapping the credit markets. As such, we see it continuing its aggressive fleet expansion in 09+, with capex of TRY 745mn in 2009 (or 22% of equity).

Main downside risk: Deepening recession, both global and domestic. We are currently projecting an average annual real GDP growth rate of 2.5% for Turkey over 2009-2013 in our baseline scenario. Based on our load factor yield model, a 100bp decline in our 2009E load factor (71.3%) would lower Turkish Airlines' EBITDAR by 6%, and our TP by 11%.

	2006	2007	2008E	2009E	2010E
Sales (TRYmn)	4,051	4,773	6,066	6,324	6,803
EBITDAR (TRYmn)	618	1,096	1,262	1,303	1,165
EBIT (TRYmn)	86	546	720	641	463
Net income (TRYmn)	179	292	1,007	591	318
EPS reported (TRY)	1.02	1.67	5.75	3.38	1.82
DPS (TRY)	0.0	0.0	0.6	0.3	0.2
ROCE (%)	2.80	16.83	16.08	12.92	8.75
P/E (x)	6.1	3.7	1.1	1.8	3.4
P/CF (x)	2.1	1.7	0.8	1.1	1.4
P/BV (x)	0.7	0.6	0.4	0.3	0.3
EV/EBITDAR (x)	5.8	2.9	2.6	2.8	3.2
Net debt/Equity (%)	154.0	109.3	73.1	75.9	73.2
Div. yield (%)	0	0	9	5	3

Source: Turkish Airlines, UniCredit Research

Buy (prev. Cov. in Transition)

Price on 04 Feb 2009	**TRY 6.25**
Target price (prev. n.a.)	**TRY 9.45**
Upside to TP	51%
Cost of equity	18.7%
High/Low (12M)	7.90/3.82

INVESTMENT HIGHLIGHTS
- **One of the fastest growing airlines in Europe**
- **Unit cost advantage leading to higher margins**
- **Strong and liquid balance sheet**

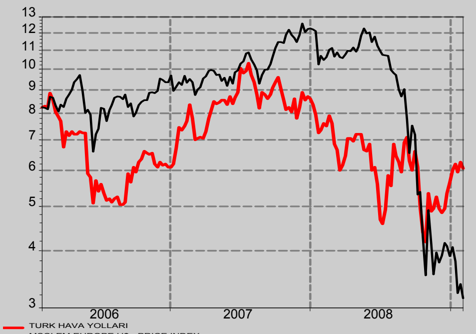
STOCK TRIGGERS
- **Strong air traffic data announcements**
- **Major changes in oil prices, in both directions**
- **Support from Turkey's tourism revenue growth**

STOCK DATA

Reuters/Bloomberg	THYAO.IS / THYAO TI
Average daily volume (mn)	15.6
Free float (%)	50.7
Market capitalization (TRYbn)	1.09
No. of shares (mn)	175.0
Shareholders	Privatization Administration 49%

UPCOMING EVENTS

Jan09 air traffic data	Feb 09
12M08 sales and earnings	Apr 09
1Q09 sales and earnings	Jun 09



Source: Thomson Datastream

STOCK PERFORMANCE (% CHG.)

	1M	3M	6M
Absolute	5.2	13.1	-6.2
rel. to MSCI EME	24.7	48.9	62.6
rel. to MSCI Turkey	10.5	26.4	33.4

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Frequently used abbreviations

ASK	Available seat kilometre
EBITDAR	Earnings before interest, taxes, depreciation, amortisation, rental expenses
EV	Enterprise value
LCC	Low-cost carrier
LF	Passenger load factor
PAX	Passenger
RPK	Revenue passenger kilometre

GENERAL NOTE

Turkish Airlines has posted its 2008 Air Traffic Results (ASK, RPK, LF, PAX, Cargo tons), whereas the latest announced Financial Results are for 9M08.

Highlights of the investment story

Turkish Airlines' passenger number grew by 15% y-o-y in 2008, whereas the European average declined by 1.0% during Jan-Nov 2008

- **Still growing in a tough environment:** Turkish Airlines' RPK (revenue passenger kilometres) grew by 13% y-o-y to 34bn in 2008, while total PAX (passengers) increased by 15% y-o-y to 23mn compared to a 1.0% y-o-y decline in the European airlines' number of passengers over Jan-Nov 08. The number of transit and business class passengers increased 41% and 23% y-o-y, respectively, largely, since April 2007, due to its Star Alliance membership. (The Star Alliance multiple-award-winning network was founded in 1997 as the first truly global airline alliance to offer passengers a worldwide reach and comfortable travelling.) We are forecasting a 6% CAGR in passenger number with an average load factor of 72.7% over 2009-2013, compared to management's 2009E guidance of a 75% load factor and 15% passenger growth.

Growth prospects are supported by the following:

– **Geographical advantage:** Since its major hub, Istanbul, is located within three hours' flying distance to 55 countries, the company easily serves as a transfer point between East and West, with its competitive medium-haul fleet.

– **A wide destination network:** Turkish Airlines offers one of the widest networks (142 cities in 70 countries), including all primary airports, especially in the CIS, Eastern Europe, Middle East and North Africa regions. Turkish Airlines provides mostly medium-haul flights, thanks to its geographical location, thus by offering higher frequency gains advantage over its long-haul-only competitors.

– **Star Alliance membership:** Higher brand awareness through Star Alliance membership contributes significantly to the growth in transit and business class passengers (41% and 23% y-o-y in 2008, respectively). In addition, inorganic growth opportunities are also being sought, e.g. recently the company acquired a 49% stake of Air Bosnia.

TURKISH AIRLINES' VS. EUROPEAN AVERAGE MAJOR AIR TRAFFIC FIGURES GROWTH

y-o-y growth (%)	Available Seat Km			Revenue Passengers Km			Passengers		
	2006	2007	2008*	2006	2007	2008*	2006	2007	2008*
Turkish Airlines	23.9	12.7	11.1	19.0	19.3	13.0	15.9	15.9	15.1
European Average	4.4	4.2	3.5	5.2	5.1	1.6	4.5	4.1	-1.0

*January-November figures

Source: Turkish Airlines, Association of European Airlines

Turkish Airlines' low unit labour cost and effective cost management in non-fuel expenses ensure higher margins

- **Cost efficiency is key profit driver:** The unit labour cost advantage and effective cost management have resulted in relatively low unit cost vs. the peers', thus enabling the company to offer competitive prices and still support faster growth without sacrificing margins.

The cost efficiency stems from the following factors:

– **Low labour cost:** Turkey's cheap labour pool ensures a sufficient workforce for Turkish Airlines to enjoy low unit labour cost vs. its peers (EUR 0,013 labour cost per ASK compared to the European peer average of EUR 0,018).

– **Effectively controlled other non-fuel costs:** Turkish Airlines managed to decrease its non-fuel cost per ASK (from EUR 0,046 in 2004 to EUR 0,040 in 9M08) with effective cost management strategies, such as the reduction of the number of employees per aircraft from 166 in 2002 to 133 in 9M08. In our view, the recent partnership in the ground-handling business further supports its cost management strategy.

– **Increasing fuel efficiency:** Average specific fuel consumption declined from 4.04 litres per 100 ASK in 2000 to 3.60 litres per 100 ASK in 2007 due to the better utilization of Turkish Airlines' younger fleet. The sharp decline in oil prices as of the last quarter of 2008 (the average Brent crude oil price was USD 100/bbl in 2008 vs. the current USD 40/bbl levels) is now working in favour of Turkish Airlines' non-hedge strategy.

OPERATING EFFICIENCY ITEMS (9M08)

EUR cent	Turkish Airlines	SAS Group	Austrian	Iberia	easyJet
Personnel cost per ASK	1.33	3.42	1.97	2.01	0.62

Source: Turkish Airlines

- **Strong and liquid balance sheet:** Turkish Airlines has a solid balance sheet with low gearing, which should be appraised especially during these turbulent times.

  – **Low gearing:** "(Net Debt + Capitalized Operating Lease) / Equity" ratio for 2009E stands at 0.8x, which, in our view, is a very valuable asset when most of the companies are afraid to face trouble in redeeming their loans in the current turmoil.

  – **Liquid balance sheet:** In our view, Turkish Airlines could easily secure its existing and potential credit lines to finance growth, as its "(Net Debt + Capitalized Operating Lease)/EBITDAR" ratio for 2009E stands at 2.0x, below the sector average (ca. 2.5x).

  – **High operating profit margins:** Despite heavy investments we expect Turkish Airlines to deliver a 10% EBIT margin in 2009 (vs. 2% of peers).

Main Risks

- **Worse-than-expected GDP growth, higher oil prices, and any potential tension between the company and the union are the main downside risks to our valuation.**

  – **Fuel price vs. yield:** Average Brent crude oil price at USD 55/bbl (vs. our USD 48/bbl estimate) in 2009 would yield a 12% decline in our 2009E EBITDAR. However, as long as the oil price increase is because of higher demand and recovery in the macro economic outlook, airlines can reflect this additional cost through fuel surcharges to ticket prices. In fact, a 10% increase in average yield would result in a much higher impact, namely a 45% jump in 2009E EBITDAR.

  – We would like to stress that Turkish Airlines should post one of the best performances in its history in 2008, with the oil prices skyrocketing, and demand remaining strong, and higher fuel surcharges leading to a higher revenue generation.

  – **Load factor:** A 100bp fall in the load factor, in addition to our conservative 250bp drop estimate for 2009 would lead to a 6% decrease in EBITDAR, thus, a 11% drop in the valuation.

  – **Trade union dispute**: We do not expect the dispute to end in a strike; however, if the dispute were to continue during the forthcoming collective bargaining negotiations, this may put pressure on the stock price.

(See our Sensitivity Analysis & Risks section for details)

Consensus' view

- **Consensus' view:** Our estimates for 2009, besides the net sales, are generally above consensus, which we attribute to the differing opinions of analysts regarding 2009 average fuel price expectations. Our lower-than-consensus net sales estimate is a result of our conservative yield and load factor assumptions.
  - We believe market players will start to appreciate Turkish Airlines' strong air traffic numbers more and more, if oil prices continue to stay at below USD 50/bbl levels for a while.

UNICREDIT VS. CONSENSUS ESTIMATES

		2008				2009	
TRYmn	**Consensus**	**UniCredit**	**Difference**		**Consensus**	**UniCredit**	**Difference**
Net Sales	6,166	6,066	-2%		6,428	6,324	-2%
EBIT	638	720	13%		480	641	34%
Net Income	757	1,007	33%		405	591	46%

Source: Bloomberg, UniCredit Research estimates

Valuation

Turkish Airlines is trading at very low multiples (2.8x EV/EBITDAR) and with our TRY 9.45 TP the stock is offering a significant 51% upside potential

- **At 2.8x 2009E EV/EBITDAR and 0.3x 2009E P/BV, we resume coverage of Turkish Airlines with a Buy rating, as our 12M TP implies a 55% upside from the current stock price. Based on a multi-stage DCF and average EV/EBITDAR multiple of 3.0x for airlines (50%/50% weights), we derived a 12M target price of TRY 9.45. Currently, Turkish Airlines is trading at a 26% discount to the European median EV/EBITDAR of 3.8x and at a 32% discount to the European median P/BV of 0.5x.** The major assumptions for our valuation are, as follows:
  - We divided our TRY-based multi-stage DCF model into three periods, where we assumed a 6% interim period growth followed by a 4% terminal growth rate. With our dynamic WACC, our DCF yields TRY 1,985mn fair value.
  - We also valued Turkish Airlines based on peer multiples by using a 3.0x EV/EBITDAR 2009E multiple, where our EV is adjusted for the remaining operational lease debt estimate (7.5x yearly rental expense). The multiple valuation yields TRY 1,327mn total market capitalization for the company.
  - We assigned equal weight to each method, thus arriving at a target MCAP of TRY 1,654mn for the stock. Our target price of TRY 9.45 per share offers 51% upside potential; hence, our Buy rating.

TURKISH AIRLINES' VALUATION SUMMARY

TRYmn		2006A	2007A	2008E	2009E	2010E	2011E
EBITDA		**444**	**930**	**1,112**	**1,076**	**927**	**918**
Tax (-)		11	112	252	148	80	81
Capital expenditure (-)		1,071	806	1,282	745	604	658
Changes in working capital (-)		-332	-150	-415	16	-64	-73
Free cash flow		**-306**	**162**	**-7**	**167**	**308**	**251**
Risk-free rate (%)				15.0	14.9	17.3	19.3
Equity risk premium (%)				5.5	5.5	5.5	5.5
Beta				1.0	1.0	1.0	1.0
Tax rate (%)				20.0	20.0	20.0	20.0
Cost of equity (%)				20.5	20.4	22.8	24.8
Cost of debt (%)				13.6	13.5	15.5	17.1
WACC (%)				18.1	17.9	20.3	22.1
Terminal growth rate (%)	4.0						
PV of total cash flows	2,508						
Net debt @ 9M08 results	926						
Implied target from DCF	1,985						
Implied target @ 3x EV/EBITDAR	1,327						
Implied target value	**1,654**						
Target price per share (TRY)	**9.45**						
Upside/(Downside) (%)	**51%**						
Recommendation	**BUY**						

Source: UniCredit Research estimates

VALUATION MULTIPLES OF THE EUROPEAN MAIN LINE CARRIERS

x	EV/Sales		EV/EBITDAR		EV/EBIT		EBIT Margin (%)		Price / Book Value		P/E	
	2008E	2009E	2008E	2009E	2008E	2009E	2008E	2009E	2008E	2009E	2008E	2009E
Air France / KLM	0.5	0.4	4.3	3.7	19.2	26.1	2.6	1.5	0.2	0.2	28.6	10.4
British Airways	0.6	0.5	6.2	4.7	91.9	27.5	0.6	1.8	0.5	0.5	-27.8	63.9
Lufthansa	0.4	0.4	3.9	3.7	9.7	16.3	4.4	2.2	0.7	0.7	10.9	13.3
Iberia	0.5	0.4	4.2	3.1	72.7	17.9	0.6	2.5	0.9	0.8	42.1	16.8
Turkish Airlines	0.5	0.6	2.5	2.8	4.4	4.4	11.9	10.1	0.4	0.3	1.1	1.8
Average	**0.5**	**0.4**	**4.4**	**3.8**	**16.9**	**21.1**	**3.0**	**1.9**	**0.5**	**0.5**	**14.3**	**21.0**

Source: UniCredit Research estimates

Sensitivity Analysis & Risks

A 14% increase in average fuel price would lower our 2009E EBITDAR by 12%...

- **All other things being equal, a 14% increase in our average fuel price estimate lowers our 2009E EBITDAR by 12% and the target value by 17%.**

TURKISH AIRLINES: SENSITIVITY TO OIL PRICE ON 2009 NUMBERS

USD/bbl	Ch. %	EBIT	Ch. %	EBITDAR	Ch. %	Net Income	Ch. %	Valuation	Ch. %
30.0	-38	1,097	71	1,758	35	956	62	2,439	47
40.0	-17	849	32	1,511	16	758	28	2,020	22
48.4	0	641	0	1,303	0	591	0	1,654	0
55.0	14	478	-25	1,140	-12	461	-22	1,368	-17
65.0	34	231	-64	893	-31	263	-55	934	-44

Source: UniCredit Research estimates

...a jump in oil prices would lead to an increase in fuel surcharges

- **A 10% increase in our 2009E average yield will lead to a 45% jump in our EBITDAR estimate, thus more than enough to offset the rising oil costs' negative impact.**
  - It is worth mentioning that airlines reflect the increase in fuel expenses to customers through fuel surcharges (Turkish Airlines' target is to collect 50% of the total fuel expense). Thus, an increase in oil prices should result in a proportionate increase in yields.
  - We also performed a sensitivity analysis of our base yield assumptions. Holding all else constant, a 10% rise in our average yield estimate (in euro terms) will result in a 45% increase in our EBITDAR estimate and, hence, 67% increase in our valuation.

TURKISH AIRLINES: VALUATION SENSITIVITY TO OIL PRICE AND YIELDS

	Yield ch. (%)				
Oil Price (USD/bbl)	-10	-5	0	5	10
30.0	1,322	1,888	2,439	3,110	3,515
40.0	887	1,454	2,020	2,704	3,108
48.4	522	1,088	**1,654**	2,354	2,765
55.0	232	802	1,368	2,068	2,498
65.0	-253	367	934	1,634	2,066

Source: UniCredit Research estimates

Based on our load factor yield model, a 100bp decline in our 2009E-2013E average load factor (72.7%) would lower Turkish Airlines' EBITDAR by 6%

- **A 100bp drop in load factor would lower our 2009E EBITDAR by 6% and result in an 11% decline in our valuation. It is worth keeping in mind that our 71.3% load factor estimate for 2009 is already a conservative one, as we assumed a 250pp drop.**
  - In our view, in order to limit the negative impact of the slowdown in the sector, Turkish Airlines could take some precautions should the load factor drop below 71% levels. Capacity and flight frequency reductions, the closing of unprofitable routes are some of the precautions the company could consider.
  - In order to stimulate the demand in some routes, the company could start promotional campaigns (e.g. average ticket price reductions, special offers with discounts).

– The company might also consider strengthening its cooperation with Star Alliance members, by increasing the code share agreement on overlapping routes. This is by definition another means of capacity reduction, as the involved parties reduce their frequency offered on same routes and share the flight under two (or more) different flight codes. Thus, we expect the alliance members to lower their frequency on routes that could be affected by a severe downturn in the coming months.

TURKISH AIRLINES: LOAD FACTOR (LF) SENSITIVITY

LF (%)	Ch. (bp)	# of pax	Ch. %	EBIT (TRYmn)	Ch. %	EBITDAR (TRYmn)	Ch. %	Net Income (TRYmn)	Ch. %	Valuation (TRYmn)	Ch. %
69.3	-200	22.5	-3	475	-26	1,136	-13	458	-22	1,274	-23
70.3	-100	22.8	-1	558	-13	1,220	-6	525	-11	1,464	-11
71.3	0	23.1	0	641	0	1,303	0	591	0	1,654	0
72.3	100	23.5	1	724	13	1,386	6	658	11	1,844	11
73.3	200	23.8	3	807	26	1,469	13	724	22	2,034	23

Source: UniCredit Research estimates

Main Risks

The major risks to our valuation is worse-than-expected economic growth, higher oil prices and a dispute between the company and trade union regarding wage negotiations

- **Worse-than-expected GDP growth, higher oil prices, and any potential tension between the company and the trade union are the main downside risks to our valuation.**

– We are assuming a contraction in global airline traffic amid ongoing financial turbulence, which we have reflected in our model by lowering the load factor and decreasing the yields. Worse-than-forecast GDP growth will result in a further decline in passenger and cargo traffic and weaker yields, which are the major risks to our rating.

– Stagnant demand together with higher-than-expected oil prices will hurt the margins and our valuation, as it will not let the company reflect the oil price increase to customers. Based on our sensitivity analysis, a 14% increase in oil prices over our base case scenario (USD 48 per barrel in 2009E) would lower our valuation by 17%.

The trade union agreement due in 2009 could temporarily weigh on the shares

- **We do not expect a strike decision; however, a potential dispute during the collective bargaining negotiations could put pressure on the stock price.**

– The 22nd term of the Collective Bargaining negotiations for Turkish Airlines employees' wages, covering 2009-2010, is expected to start in March 2009. The previous negotiation process was a long and painful one, resulting in a strike decision after lengthy discussions, followed by an agreement so that the strike was averted.

– We attach a low probability to a potential strike in Turkish Airlines, as we believe that the Government may step in to solve the problem or even block the strike decision by arguing national security reasons. However, a long-lasting potential conflict between management and the union may weigh on the share price in the short term.

– In addition, we are assuming an average nominal wage increase corresponding with our estimate CPI + 200bp in our forecast period. A higher labour wage increase could create a downside risk to our valuation.

Key assumptions

ASK is the key driver in our forecast models

- **Baseline scenario: CAGR of 5% in Available Seat Kilometres (ASK), 6% in Revenue Passenger Kilometres (RPK) and 6% in total passengers during 2009E-2013E, all below their historical averages of a respective 12%, 13% and 14%, over 2002-2008.**

We forecast 5% CAGR in ASK over 2009-2013 vs. 12% achieved in 2002-2008

– ASK is the key metric in our model since most of our income and cost forecast items are related to ASK and the comparisons in the sector are mainly shown in terms of it (such as fuel expense per ASK, operating expense per ASK).

– Our 6% ASK growth for 2009E is based on capacity expansion announced so far, such as the new wet leased[1] B777s or the purchase of A321-200s. Going forward, our aircraft addition estimates are feasible considering management's fleet expansion plan for 2009-2023, targeting to become a carrier with 250 aircraft in 2023, to coincide with the 100th anniversary of the Turkish Republic in that year.

– We expect fleet and seat capacity to post CAGR of 3% and 4%, respectively, during 2009-2013, much lower than the realized figures of 12% and 13%, over 2002-2008. We assume ASK to grow slightly above our seat expansion assumption, since we believe that the effective utilization of the fleet with higher frequencies and widening destination network will also support the rise in ASK.

TURKISH AIRLINES: MAJOR AIR TRAFFIC DATA

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009E	2010E
Fleet size (YE) (#)	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**66**	**65**	**73**	**83**	**103**	**102**	**127**	**133**	**137**
y-o-y ch. (%)	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*-2*	*12*	*14*	*24*	*-1*	*25*	*5*	*3*
Total Seat Capacity (#)	**10,911**	**11,620**	**11,917**	**10,855**	**10,672**	**10,598**	**12,109**	**14,419**	**17,931**	**17,594**	**22,238**	**23,678**	**24,485**
y-o-y ch. (%)	*n.a.*	*6*	*3*	*-9*	*-2*	*-1*	*14*	*19*	*24*	*-2*	*26*	*6*	*3*
ASK (mn)	**21,416**	**23,101**	**26,001**	**24,890**	**24,071**	**24,040**	**26,482**	**29,805**	**36,934**	**41,625**	**46,319**	**49,184**	**51,525**
y-o-y ch. (%)	*n.a.*	*8*	*13*	*-4*	*-3*	*0*	*10*	*13*	*24*	*13*	*11*	*6*	*5*
Domestic	4,724	4,988	5,077	4,333	3,858	3,833	4,219	5,431	7,097	8,072	8,440	8,962	9,389
International	16,692	18,113	20,924	20,557	20,213	20,207	22,263	24,374	29,837	33,553	37,879	40,222	42,136
RPK (mn)	**13,814**	**13,903**	**17,396**	**15,679**	**16,594**	**16,113**	**18,594**	**21,333**	**25,379**	**30,250**	**34,168**	**35,052**	**37,235**
y-o-y ch. (%)	*n.a.*	*1*	*25*	*-10*	*6*	*-3*	*15*	*15*	*19*	*19*	*13*	*3*	*6*
Domestic	3,289	3,371	3,588	2,876	2,732	2,763	3,204	3,992	5,187	5,893	6,377	6,548	6,953
International	10,525	10,532	13,808	12,803	13,862	13,351	15,390	17,341	20,193	24,357	27,790	28,504	30,282
Load Factor (%)	**65**	**60**	**67**	**63**	**69**	**67**	**70**	**72**	**69**	**73**	**74**	**71**	**72**
Domestic	70	68	71	66	71	72	76	74	73	73	76	73	74
International	63	58	66	62	69	66	69	71	68	73	73	71	72
# of Passengers (mn)	**10.5**	**10.4**	**12.0**	**10.3**	**10.4**	**10.4**	**12.0**	**14.1**	**16.9**	**19.6**	**22.5**	**23.1**	**24.6**
y-o-y ch. (%)	*n.a.*	*-1*	*16*	*-15*	*1*	*0*	*15*	*18*	*20*	*16*	*15*	*3*	*6*
Domestic	6.0	6.1	6.5	5.2	5.0	5.0	5.8	7.2	8.9	9.9	11.0	11.3	12.0
International	4.5	4.3	5.5	5.1	5.4	5.4	6.2	7.0	8.1	9.7	11.5	11.9	12.6

Source: Turkish Airlines, UniCredit Research estimates

[1] **A wet lease is a leasing agreement whereby an airline (lessor) provides an aircraft, complete crew, maintenance and insurance to another airline (lessee), who pays by hours operated. The lessee provides fuel, covers airport fees, and any other duties, taxes, etc. The flight uses the flight number of the lessee.**

Domestic air traffic assumptions

We are expecting Turkish Airlines' domestic RPK to post CAGR of 6% in 2009-2013 vs. CAGR of 15% over 2002-2008

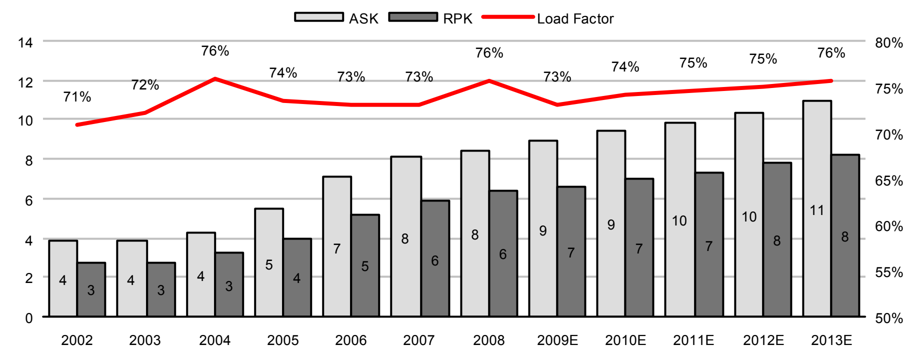
- **We have factored in a 250bp drop in domestic load factor to 73.1% in 2009 from 75.6% in 2008 and project a gradual recovery to 76% levels after 2013.**

  – Turkish Airlines' 75.6% load factor in domestic routes in 2008 is the second-highest figure ever achieved in the past decade. However, in line with our economic contraction estimate (1.0% y-o-y) for the Turkish economy and negative impact of newly established domestic routes, we are estimating a 250bp decline in the load factor in 2009.

  – Although our significant load factor decline forecast covers the domestic low-cost carrier (LCC) competition's negative impact, we believe that the competition may be limited and weaker than we assume. In our view, Turkish Airlines may offer competitive fares in domestic routes through promotions and discounts to keep stable passenger numbers. In addition, some local players may prefer to lease their aircraft during this financial turmoil, thus leaving the market to Turkish Airlines.

  – In line with our load factor estimates we are projecting domestic RPK to post 6% CAGR in 2009-2013 vs. the 15% CAGR achieved over 2002-2008.

TURKISH AIRLINES: MAJOR DOMESTIC TRAFFIC ASSUMPTIONS



Source: Turkish Airlines, UniCredit Research estimates

International air traffic assumptions

We assume the international load factor to decrease from 73.4% in 2008 to 71.3% in 2009, amid slowing global airline traffic

- **We expect Turkish Airlines to register a 6% CAGR in international RPK in 2009-2013 (vs. 12% over 2002-2008).**

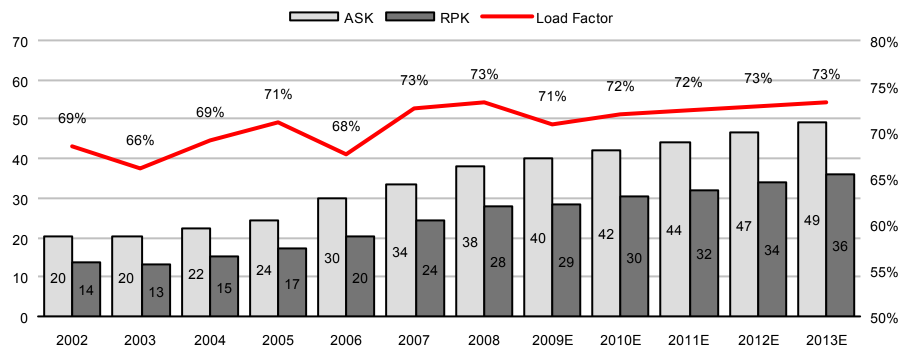
  – A 73.4% international load factor in 2008 is the highest figure recorded in the past decade and the sharp rise is largely attributable to increasing tourism activities, (the number of visitors increased by 13% y-o-y in Jan-Nov 2008 to 34mn, 70% of which prefer travelling by air), better integration with the global economy and the benefits of Star Alliance membership.

  – On the other hand, 2009 is expected to be a challenging year for airlines, including Turkish Airlines. In line with fleet expansion, the addition of new routes and increasing frequency in existing routes will lead to a rapid increase in ASK, which should also weigh on the international load factor. Thus, we assume the international load factor to decrease from 73.4% in 2008 to 71.3% in 2009, amid slowing global airline traffic.

– We believe that our assumption is conservative, since the company may reduce the capacity or stimulate the demand in order to stabilize the load factor at its 75% target level. Moreover, the share of business class passengers, highly correlated to the economic activity, is relatively small (high single digit) in Turkish Airlines compared to its peers. Thus, Turkish Airlines' international passenger base will be hit less compared to other main carriers.

– The average load factor for European airlines is 73.0% even in a challenging month like November 2008. Turkish Airlines has a good track record of increasing its load factor steadily to its European counterparts' level, and with the normalization in the sector we believe Turkish Airlines could easily achieve similar numbers to the European carriers, and beat our estimates.

TURKISH AIRLINES: MAJOR INTERNATIONAL TRAFFIC ASSUMPTIONS



Source: UniCredit Research estimates

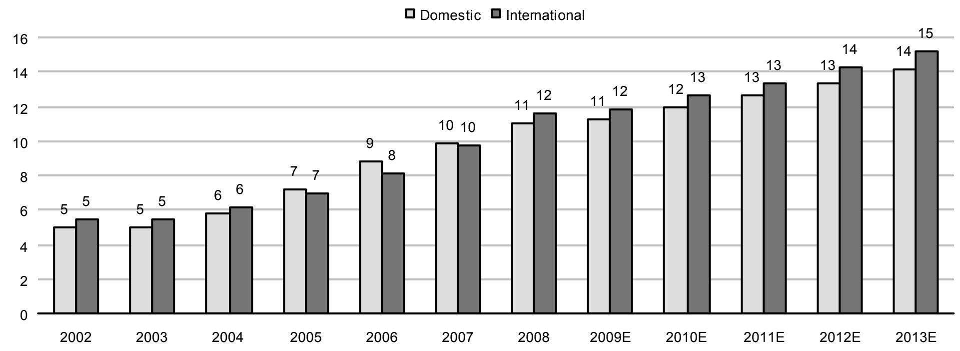
Passenger numbers

- **We are projecting a 6% CAGR in 2009-2013 in total passenger volume (vs. 14% CAGR over 2002-2008).**

– Turkish Airlines' domestic passenger number increased by 11% y-o-y to 11.0mn in 2008 while international passengers rose by 19% y-o-y to 11.5mn.

– In line with our RPK assumptions, we are forecasting 6% CAGR in 2009-2013 both for domestic passengers (vs. 14% CAGR over 2002-2008) and international passengers (vs. 13% CAGR over 2002-2008).

TURKISH AIRLINES: PASSENGER NUMBERS



Source: UniCredit Research estimates

Significant upside on conservative scenario

With lower fuel surcharges and the company's strategy to stimulate demand, we are assuming a 15% decline in average yield in euro terms in 2009, in our very conservative scenario

- **We are projecting a 15% decline in yield (passenger revenue / RPK) in euro terms as a result of lower fuel surcharges and strategy to stimulate demand. Although we expect a decline in yields in euro terms, we are calculating a 3% increase in TRY terms, due to currency depreciation.**

  – In our model, we first broke down sales into three main parts: **scheduled flights**, **non-scheduled flights** and **other revenues**. Furthermore, we separated scheduled flights into **domestic, international** and **cargo** and calculated the yields. We used RPK for passenger yields and the revenue per cargo tons carried assumptions for the cargo division. For international flights, we calculated the yields in EUR terms, as major destinations are countries in the eurozone and ticket prices are denominated in euro.

TURKISH AIRLINES YIELD PER RPK

Yield	2004	2005	2006	2007	2008E	2009E	2010E	2011E	2012E	2013E
in EUR terms	7.9	8.3	8.4	8.4	8.7	7.4	7.7	7.7	7.7	7.6
y-o-y ch. (%)	*n.a.*	*5*	*1*	*1*	*4*	*-15*	*4*	*0*	*0*	*-1*
in TRY terms	13.9	13.9	15.0	14.9	16.6	17.1	17.3	18.5	19.8	21.1
y-o-y ch. (%)	*n.a.*	*-1*	*8*	*0*	*11*	*3*	*1*	*7*	*7*	*6*

Source: UniCredit Research estimates

We are forecasting an average EUR¢ 7.8 yield in 2008-2013 vs. EUR¢ 8.2 achieved over 04-07

– Our expectation of an EUR¢ 8.7 average yield for 2008 would be the highest yield in the past five years, as a result of i) **elevated fuel surcharges** due to record high oil prices; ii) **better passenger/route mixture** (more contribution from higher priced routes); and iii) albeit still at a low level, **increasing share of business class passengers**.

– For 2009, we expect a 15% decline in average yield in euro terms (a 10% decline in international yields in EUR terms and 15% reduction in domestic yields in TRY terms) in our conservative scenario, which is based on the following:

Lower fuel surcharges: The fuel surcharges will follow the declining trend in oil prices, thus they will have a downward impact on yields this year.

- **Promotions to stimulate demand:** We do expect a subdued demand and we believe Turkish Airlines, like most of the global airlines, will reduce its average yields (both in international and domestic routes) in order to stimulate demand.

- **Anadolu Jet impact:** Anadolu Jet (Turkish Airlines' LCC brand) will also have a dilutive impact on domestic yields with lower fares compared to the main carrier.

– We believe that Turkish Airlines will attract demand as long as it keeps its euro-based ticket prices lower than the competitors' on similar routes. However, for some destination points the demand may diminish quickly if the company were to reflect the whole EUR/TRY depreciation on its ticket prices. Thus, we expect it to absorb some of the exchange rate impact, which could lead to a decline in euro-term yields.

– Please note that this is our conservative scenario, since we believe that major European main line carriers will not reduce their fares as much as we assume for Turkish Airlines.

– Although we forecast a decline in yields in euro terms, due to currency depreciation, we are expecting an increase in yields in TRY terms.

– For the domestic market, the competition with local LCCs, amid the slowing economy, will force Turkish Airlines to reduce its fares to more competitive levels. Thus, we forecast a significant reduction in domestic yields in 2009, a 15% decline in TRY terms.

Cargo revenues will be hit more with the slowing international trade, as we are expecting a currency neutral (i.e. in euro terms) 14% y-o-y drop in 2009

- **We forecast a 15% decline in cargo yields in euro terms in 2009, amid increased competition in a slowing world economy. We are projecting cargo revenues to post CAGR of 8% and to represent 6% of total sales during 2008-2013 (vs. CAGR of 7% and an average 8% of total sales over 2002-2007).**

– In addition to the cargo carried via passenger planes together with luggage, Turkish Airlines has a scheduled cargo service with four aircraft. Cargo revenues as a percentage of total revenues stood at 6% as of the 9M08 results.

– The year 2008 was a strong year, as the company registered 9% y-o-y growth in cargo tons carried, much higher than the GDP growth. On the other hand, 2009 will be a challenging year amid the slowdown in trade volumes; and in line with our economic contraction forecast we are expecting a 1.0% decline in cargo tons carried.

– Non-scheduled flights and other revenues constitute a small portion of the total revenues, a respective 1% and 5% of total sales. We have assumed it to stay at similar levels in our forecast period.

Based on our load factor and yield projections, we are projecting a 4% y-o-y growth in net sales in 2009E

- **We are projecting a 10% CAGR at the top line in 2008-2013 (vs. 20% achieved over 2004-2007).**

– We are expecting Turkish Airlines' net sales to increase by 27% y-o-y and reach TRY 6.1bn in 2008. However, based on our load factor and yield projections we are projecting 4% y-o-y growth in net sales in TRY terms in 2009 (a currency neutral, in euro terms, 14% decline).

– Faster EUR depreciation against the TRY, while the demand is still in place, would have a positive impact on the Turkish Airlines' numbers. According to our calculations, holding all else constant, a 10% further depreciation in TRY will lead to an 8% increase in net sales.

Fuel expense is by far the most important item in costs

Fuel expense as a percentage of total cost increased from 27% in 9M07 to 36% in 9M08

- **Turkish Airlines' fuel expenses increased significantly by 66% y-o-y in 9M08, much higher than the increase in consumption (10% y-o-y increase in ASK), due to higher oil prices in 2008**.

  – Fuel cost, now constituting 36% of total expenses in 9M08, is the major item in the cost structure of the company followed by personnel expenses at 22%.

TURKISH AIRLINES: TOTAL COST BREAKDOWN (TRYMN)

	9M07A	% total	9M08A	% total	07/08 y-o-y ch. %
Fuel	854	27	1.414	36	66
Personnel	762	24	855	22	12
Sales & Marketing	175	6	127	3	-28
Rents	130	4	99	3	-24
Maintenance	106	3	183	5	72
Depreciation	271	9	275	7	1
Landing	250	8	283	7	13
Ground Handling	178	6	198	5	12
Catering	153	5	188	5	23
Other	271	9	305	8	12
Total	**3.149**	**100**	**3.927**	**100**	**25**

Source: UniCredit Research estimates

The company recently announced its plan for hedging transactions. Thus, oil prices lower than the 2008 average (e.g. Brent crude USD 100/bbl) will be reflected positively at the bottom line through reduction in total fuel expense

- **We forecast a 37% y-o-y decline in fuel costs on the back of an estimated oil price per barrel of USD 48 in 2009.**

  – Historically, Turkish Airlines has not hedged its oil exposure. However, management recently announced that the company will start fuel hedging (up to 10% of total jet fuel consumption) in order to minimize fluctuations in oil prices.

  – It is worth emphasizing that non-hedging for the time being is working in favour of the company, thanks to the sharp weakening in the oil prices. The current prices are far below last year's peak numbers (e.g. the Brent crude 2008 average was USD 100/bbl). Please note that we forecast an increase in total fuel consumption with higher ASK and also depreciation of the TRY against the USD, both of which would give rise to fuel expenses. However, the positive effect of our declining oil price estimates would offset the negative impact of these factors.

  – We are projecting an average USD 48 for Brent crude in 2009. We expect the percentage of fuel expense, which is predicted to jump 34% in 2008, to decline to 21% in 2009, in line with our lower oil price expectation. This will boost the bottom line by TRY 604mn. In our conservative scenario (a 15% decline in yield in euro terms and a 250bp drop in load factor), the TRY 592mn net income expectation for 2009 will mainly stem from the significant drop in fuel expenses.

FUEL COSTS IN TURKISH AIRLINES

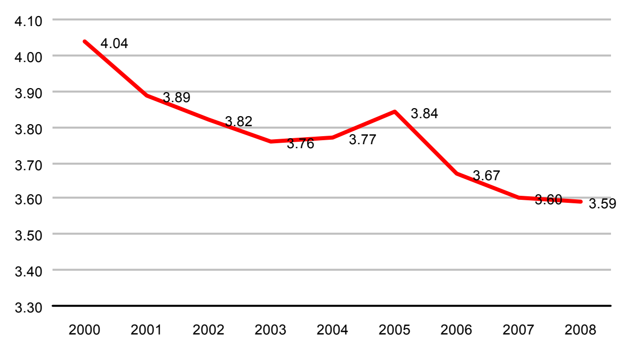
	2005	2006	2007	2008E	2009E	2010E
Fuel Costs (TRYmn)	**729**	**1,107**	**1,169**	**1,802**	**1,198**	**1,518**
Ch. %	41	52	6	54	-34	27
Change in ASK (%)	**13**	**24**	**13**	**11**	**6**	**5**
Oil Price (USD/bbl)	55	65	73	100	48	59
USD/TRY	**1.34**	**1.43**	**1.30**	**1.29**	**1.67**	**1.66**

Source: UniCredit Research estimates

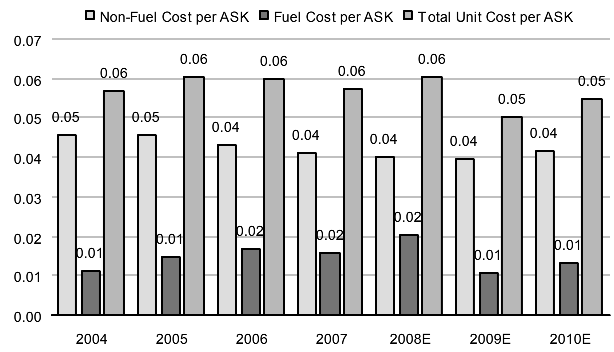
Management was successful in cutting the non-fuel costs while the relatively new fleet meant lower average specific fuel consumption

- **Non-fuel costs are forecast at an average EUR 0.041 per ASK over 2009-2013 (vs. EUR 0.044 over 2004-2007).**
  - The company was successful in keeping non-fuel costs steady in the past years with better cost management, which could be seen in the declining trend of non-fuel cost per ASK (EUR 0.046 in 2004 vs. EUR 0.040 in 9M08).
  - Though we expect this trend to continue, we assumed generally a constant per ASK ratio in USD terms for the other cost items, such as landing fee, handling and catering expenses.
  - We are expecting total non-fuel costs to post a 14% CAGR in 2009-2013 in TRY terms (vs. 13% over 2004-2007).
- **Average salaries to increase at our CPI estimate + 200bp**
  - For the second most important cost item, personnel expenses, we expect staff growth to rise parallel with our fleet expansion, while we assume average salaries to increase above our CPI estimates.
  - We are projecting monthly overhead costs (total labour cost per full-time employee per month) to register a 9% CAGR in 2009-2013 (vs. 9% CAGR in 2004-2007)

TURKISH AIRLINES: AVERAGE SPECIFIC FUEL CONSUMPTION



UNIT COST BREAKDOWN



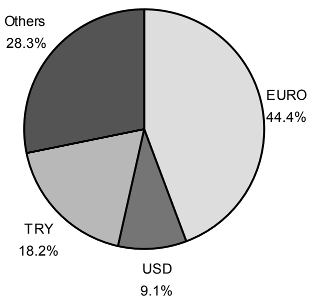
Source: Turkish Airlines, UniCredit Research estimates

Currency diversified revenue and expense structure is a partial cushion in time of volatility

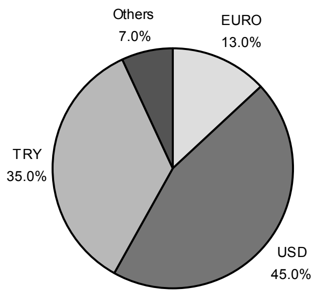
- **Other income and financial expenses are a major source of uncertainty**
  - The EUR is the major income currency with a 44% share in total revenues, while 45% of expenses are denominated in USD (mainly fuel expense), followed by 36% in TRY.
  - At first glance, it seems as if depreciation of the TRY is positive for Turkish Airlines in the short term by improving operating margins, since only 18% of the income is in TRY vs. 35% of the expenses.
  - However, Turkish Airlines “Financial Expenses” and “Net Other Income” lines in the income statement are also highly sensitive to currency movements. The company has a sizeable FX-denominated debt and a huge short FX position (TRY 1.3bn as of the end of 9M08), which will result in FX losses from a weaker TRY.

– On the other hand, Turkish Airlines is calculating the fair value of its planes, spare parts, simulators in USD terms, which more than offsets the short position's impact. Since the fair value of the fleet is too hard to estimate together with the change in exchange rate, the net impact of FX variations on the bottom line is very unpredictable. This is one of the reasons why the company's net other income/financial expense has been very volatile in the past.

TURKISH AIRLINES: INCOME BY CURRENCY (9M08)



EXPENSE BY CURRENCY (9M08)



Source: Turkish Airlines

TURKISH AIRLINES: NET OTHER INCOME AND FINANCIAL EXPENSE

	2004*	2005*	2006*	2007	9M08
Net Other Income (Loss) (TRYmn)	-18	177	163	261	203
Financial Expense (Gain) (TRYmn)	15	89	60	403	-141
USD/TRY (year-end)	1.34	1.34	1.41	1.16	1.23
EUR/TRY (year-end)	1.82	1.59	1.85	1.71	1.80

* FX loss/Income item adjusted with latest format

Source: Turkish Airlines, UniCredit Research estimates

– Based on the 9M08 results and company guidance, a 10% increase in EUR or USD decreases the net income by TRY 67mn (10%) and TRY 44mn (6%), respectively, due to higher FX losses on the balance sheet.

– However, Turkish Airlines also added a comment in the footnotes that a similar USD/TRY depreciation will raise the current value of the fleet, which will increase its 9M08 net income by TRY 242mn (36%). Thus, the overall effect of currency depreciation would have a positive contribution at the 9M08 bottom line.

– We note the TRY depreciated 23% against the major currencies in the last quarter of 2008 (USD/TRY was 1.23 at 30 September 08 vs. 1.51 at 31 December 08). Hence, we expect Turkish Airlines' bottom line to be boosted by the high "Net Other Income" and FX gain impact in the 2008 full-year results.

TURKISH AIRLINES: IMPACT OF TRY DEPRECIATION ON NET INCOME (2008)

+ %10 change in	USD/TRY	EUR/TRY
Due to FX position of balance sheet (TRYmn)	-44.3	-67.0
Due to revaluation of fleet (TRYmn)	242.5	n.a.

Source: Turkish Airlines

Natural hedge against currency volatility due to diversified revenue and expense generation

- We believe that Turkish Airlines has a natural hedge against the currency volatility, due to diversified revenue and expense generation. In addition, the short position in the balance sheet is covered through revaluation of the fleet.

- Overall, we assume a modest change in net other income/loss and financial expense items in our forecast period. However, we still note that major fluctuations in the currency may have a significant impact at the bottom line.

Dividend potential this year

Since the majority shareholder, the State, is looking for new funds to spend, we do not rule out a dividend this year

- **Since Turkish Airlines is now eligible to distribute dividends and has a pile of cash at hand, we are estimating a dividend distribution, albeit at a small amount, for the first time in the company's history.**

  - Turkish Airlines used to carry accumulated loss till the first half of this year, stemming from pre-2005 weak performance. However, the positive impact of tremendous growth both at the top and the bottom lines has wiped out this negative number. Hence, Turkish Airlines will be eligible to distribute a dividend this year based on Turkish regulations.

  - We believe that Turkish Airlines is not a dividend play but a growth story and the company requires substantial funds to finance its fast growth, e.g. the financing need of new fleet expansion.

  - However, we believe management may consider distributing a dividend this year (though the amount would be limited due to long-term financing need concerns), since the major shareholder, the State, is looking for new funds to spend. Turkish Airlines is one of the few state enterprises that could still supply cash to the Turkish Treasury in this gloomy environment.

Investment thesis – growth, cost control, balance sheet management

Turkish Airlines' passenger number grew by 15% y-o-y in 2008, while the European average was a -1.0% decline during the Jan-Nov period

- **Turkish Airlines managed to grow its passenger's numbers by 14% CAGR to 22.5mn during 2002-2008 and posted a double-digit growth (15% y-o-y) even in 2008 while the sector faced a decline.**

  – Turkish Airlines' RPK increased by 13% y-o-y to 34.2bn while ASK expanded a lesser 11% y-o-y to 46.3bn in 2008, thus increasing the passenger load factor by 110bp to 73.8%. Turkish Airlines carried 22.5mn passengers, implying a 15% y-o-y increase.

  – This performance is very impressive when compared with the latest released air traffic data for European airlines, which on average passenger traffic volume declined by 1.0% y-o-y in January-November. Turkish Airlines' cargo-mail carried increased by 9% to 199,006 tons, which is also much higher than that of its European counterparts.

  – On a monthly basis, we started to see the negative impact of expansion in fleet size on the load factor, as the RPK increase lagged behind the pace in ASK. However, it is still positive to see limited impact of financial turbulence on the passenger numbers, as it increased by 14% y-o-y in December, supported by higher non-scheduled flights and increasing transit passengers for Hajj (pilgrimage to Mecca, Saudi Arabia) activities.

TURKISH AIRLINES' VS. EUROPEAN AVERAGE GROWTH

	2006	2007	2008*
Turkish Airlines ASK growth	23.9	12.7	11.1
European Average ASK growth	4.4	4.2	3.5
Turkish Airlines RPK growth	19.0	19.3	13.0
European Average RPK growth	5.2	5.1	1.6
Turkish Airlines PAX growth	15.9	15.9	15.1
European PAX growth	4.5	4.1	-1.0

*January-November data

Source: Turkish Airlines, Association of European Airlines

At least 25 wide-body and 50 narrow-body aircraft are expected to join the fleet between 2009 and 2023

- **Turkish Airlines recently announced its 2009-2023 fleet expansion plan, which covers 25 (plus 10 optional) wide-body and 50 (plus 20 optional) narrow-body aircraft, which should support growth.**

  – The company invited Airbus (320, 330 and 350 families) and Boeing (737NG, 777 and 787 families) to submit their offers for each class of aircraft.

TURKISH AIRLINES' FLEET EXPANSION PLAN 2009-2023

Type	Producer	Family	Min. (USDmn)	Max. (USDmn)
Narrow Body	Airbus	A320	73	81
Narrow Body	Boeing	B737NG	71	85
Wide Body	Airbus	A330	177	206
Wide Body	Airbus	A350	206	272
Wide Body	Boeing	B777	200	279
Wide Body	Boeing	B787	146	200

Type	Planned Order	Optional	Min. (USDmn)	Max. (USDmn)
Narrow Body	50	20	3,525	6,496
Wide Body	25	10	3,650	9,765
Total	**75**	**30**	**7,175**	**16,261**

Source: Turkish Airlines, Boeing, Airbus, UniCredit Research estimates

We do not expect any financing problem for the new fleet expansion plan

– This expansion plan is in line with the company's previous strategy to have 250 aircraft by the 100th anniversary of the Turkish Republic in 2023. Based on our rough calculations, we estimate the delivery size list price to range between USD 7bn and USD 16bn (assuming only the min. or max. price of aircraft to be paid in each class and options to be fully, or not at all, exercised).

– However, we expect the actual cost to be much lower than the list price, like before, due to huge discounts applied. We expect the discount rates to be much higher nowadays, since Turkish Airlines will have more bargaining power against the producers when most airlines are cancelling their existing orders.

– The expansion plan covers a long duration and the company expects the aircraft deliveries to start in the second half of 2010, when the current financial turmoil should subside, in our view. Thus, we do not anticipate the financing of the expansion plan to be a problem for the company and we expect Turkish Airlines to enjoy favourable financing terms again, as in the previous fleet renewal programmes.

TURKISH AIRLINES CAPEX ESTIMATES

USDmn	2006	2007	2008E	2009E	2010E
Investments, of which	**753**	**624**	**1,001**	**450**	**368**
in aircraft	689	570	912	410	335
in other tangible assets	60	50	79	36	29
in other intangible assets	3	4	10	4	3

Source: Turkish Airlines, UniCredit Research estimates

Turkey is located at a major crossroads, as Istanbul is easily accessible from 55 countries in three flight hours

- **Turkish Airlines has a major location advantage because of Turkey's and Istanbul's geographical position, as a transfer point between West and East while Istanbul is becoming a major hub with Star Alliance membership support.**

  – Istanbul is easily reachable from 55 countries in only three flight hours. This is why the company is positioning itself as a major player of transferring passengers between East and West. Accordingly, Turkish Airlines is offering one of the widest networks around this region, especially in the CIS, Eastern Europe and Middle East.

  – A less-than-three-hour flight with a short/medium-haul aircraft also allows the company to offer much higher frequency compared to its competitors, as the latter could offer a similar destination with a long-haul aircraft resulting in fewer frequency. Moreover, Turkish Airlines has one of the most modern and fuel efficient medium-haul fleet (i.e. 52 B737-800 and 39 A320/321 aircraft) resulting in cost advantage in ticket prices.

São Paulo (Brazil), Toronto (Canada) and Nairobi (Kenya) are some of the new long-haul routes…

- **Turkish Airlines continues to expand its destination network by adding new long- and medium-haul routes and we believe that the new destination routes could be value-added due to their unique characteristics**.

  – The São Paulo route would be the first direct flight to a South American destination from Turkey, and the Toronto route would be mainly frequented by Turks living in Canada.

  – Although the global passenger demand is decreasing, especially in the long-haul network, the demand for Turkish Airlines' existing long-haul routes also seems stable, as the company recently acquired three B777-300ER from Jet Airways through a wet lease agreement.

...while the company will strengthen its position in its core region by opening up Mashhad (Iran), Lviv (Ukraine) and Benghazi (Libya) routes

– Management has clearly expressed its target to become one of the top five carriers in Europe through expansion mainly in Europe, Central Asia and the Middle East, which will be supported by new destination announcements such as Göteborg in Sweden, Mashhad in Iran, Lviv in Ukraine and Benghazi in Libya.

Star Alliance membership supports the growth with increasing brand awareness

- **Star Alliance membership, which kicked off in April 2008, further supports Turkish Airlines' growth strategy by increasing brand awareness and supplying more transfer passengers from the member airlines.**

  – Star Alliance also gives a boost to the number of business class passengers, as Turkish Airlines' ticket prices are competitive compared to its peers. In fact, business class and transfer passenger numbers in international routes increased by 23.2% and 41.3%, respectively, in 2008.

  – Turkish Airlines' strategy, especially during these times, is to increase its customer base in business class service when ticket prices become more important in the decision process. The company's main strategy is to serve the highest quality at the most appropriate price and to create brand loyalty. This is why the company formed a joint venture in the catering business with Austrian DO&CO (Hold rating) to improve inflight service quality, and it heavily invested in upgrading the quality of seats in the fleet, especially in business class.

  – We believe the company's strategy to catch flyers who have not yet flown Turkish Airlines from other airlines, especially from Star Alliance members, could easily work in these tough days, since some competitors will reduce capacity by decreasing their frequency or even eliminating some of their routes.

The Air Bosnia acquisition is a small step now but clearly signals management's professional attitude

- **Inorganic growth is also on the table, as in late December last year Turkish Airlines signed an agreement with the Bosnian government for the acquisition of a 49% share in Air Bosnia.**

  – The company is expected to introduce new jet aircraft for Air Bosnia and make further investments to increase the operational efficiency of the company. Currently, with two passenger aircraft, around 67,500 passengers and 89 employees, Air Bosnia is too small in size and will have limited impact on Turkish Airlines' figures.

  – Nevertheless, we welcome this acquisition, as it will be i) a valuable experience for management for future acquisition projects; and ii) a long-term positive move, as Turkish Airlines will have a hub in one of the promising Eastern European markets.

  – It is highly likely that Turkish Airlines would also utilize some of its aircraft in the fleet in Bosnia, as it has been doing through its LCC brand, Anadolu Jet, in Turkey.

  – Though we do not expect any other major acquisition deals in the short term, it is positive to see that management is considering potential small targets for possible inorganic growth, provided that they acquire it at a bargain price.

  – Moreover, even though the majority share is still held by the Turkish State, taking risk through investing abroad, in our view, should be seen as a clear signal that Turkish Airlines is no longer managed like a state enterprise but with a commercial attitude.

Cost efficiency is the profit driver

Turkish Airlines enjoy having low labour cost due to a relatively cheap labour pool in Turkey

- **Operating efficiency in Turkish Airlines is higher compared to the European main carriers since the second-biggest cost item, personnel expense, is lower due to the cheap labour pool in Turkey.**
  - Low personnel cost per ASK enables Turkey's flag carrier to charge ticket prices similar to the European main carriers but enjoy higher margins.

OPERATING EFFICIENCY ITEMS (9M08)

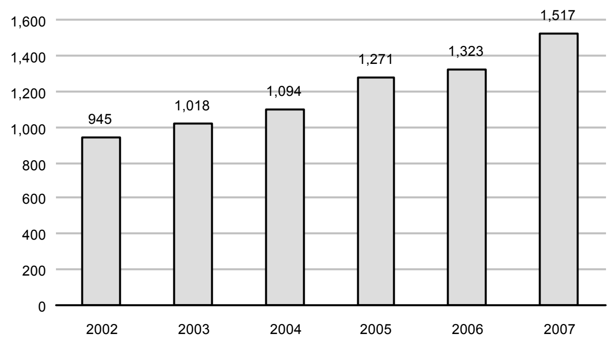
		Turkish Airlines	SAS Group	Austrian	Iberia	easyJet
Personnel cost per ASK	EUR cent	1.39	3.42	1.97	2.01	0.62

Source: Turkish Airlines

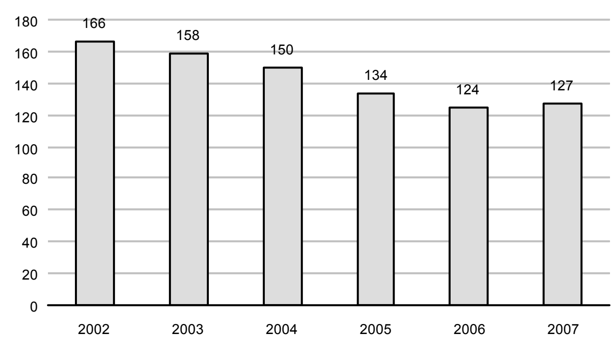
Employee efficiency has been increasing over the years

- **Turkish Airlines has improved its operational efficiency notably in the past five years, when employee per aircraft decreased from 166 in 2002 to 127 in 2007, passengers per employee almost doubled from 945 to 1,517 in the same period.**
  - We believe in the past Turkish Airlines' non-hedging policy forced management to implement new cost-cutting measures earlier, since the increasing oil prices had a much more direct impact on the company's financials.
  - Although operational efficiency improvements are likely to continue in this hostile economic environment, we project no change in employee per aircraft and a modest increase of 3% CAGR in passengers per employee during 2009-2013 (vs. 9% achieved in 2002-2009).

TURKISH AIRLINES: PASSENGER PER EMPLOYEE



EMPLOYEE PER AIRCRAFT



Source: Turkish Airlines

Newly established cooperation in ground-handling business with Havas is a long-term positive with potential cost-savings

- **Outsourcing non-core business to reduce non-fuel costs**
  - In 2006, Turkish Airlines established a joint venture with Austrian DO&CO in catering and in 2007 with Pratt&Whitney in the Maintenance, Repair and Overhaul business.
  - Recently, Turkish Airlines selected Havas (ground-handling subsidiary of airport operator TAV Havalimanları Holding) as the joint venture partner for its newly established ground-handling subsidiary, TGS Yer Isletmeleri. We believe this partnership will be beneficial and a cost saving in the medium to long term.

Please note that TAV, Havas' parent company, is the current operator of Istanbul Ataturk Airport (the major hub of Turkish Airlines), thus it already has notable knowledge and operates with lower costs.

– Meanwhile, the company is actively seeking to outsource other non-core activities, such as call centre operations, which will further reduce the headcount and staff expense in the long term.

Solid and liquid balance sheet

Net debt is expected to stabilize at 2.1% of EBITDAR over 2009-2013

- **Turkish Airlines' "(Net Debt + Capitalized Operating Lease) / Equity" ratio for 2009E stands at 0.8x, which, in our view, is a very valuable asset when most of the companies are feared to face trouble in redeeming their loans in the upcoming turbulent times.**

  – Like most of its global peers, Turkish Airlines was founded as "State Airlines Administration" in 1933 and the State is still the majority shareholder through the 49% share of the Privatization Administration. We believe the state shareholder structure (not state enterprise structure) should positively contribute to the company's credibility nowadays. That is, Turkish Airlines is one of the most attractive and secured airlines to debtors, because the company has full support from the Turkish Government in addition to its positive bottom-line performance.

  – Increasing equity value, combined with low and easily funded debt structure (debt is generally denominated in FX terms as significant revenue is generated outside Turkey), should be noteworthy and appraised amid a gloomy macro environment. This low indebtedness would also work in its favour, when the company starts negotiations to raise new debt for its fleet expansion project. Thus, we do not expect the company to face any problems in obtaining new credit lines or preserving the existing ones.

TURKISH AIRLINES' DEBT STRUCTURE

TRYmn	2006	2007	2008E	2009E	2010E
Total Cash	365	772	1,410	1,096	720
Total Debt	1,704	1,826	2,274	1,976	1,614
Net Debt	1,339	1,053	864	880	894
Capitalized operating lease	1,140	1,027	1,265	1,701	1,785
Net Debt + Capitalized operating lease	2,478	2,081	2,129	2,581	2,679
Net Debt + Capitalized operating lease / Equity	1.5	1.1	0.7	0.8	0.7
Net Debt + Capitalized operating lease / EBITDAR	4.0	1.9	1.7	2.0	2.3

Source: Turkish Airlines, UniCredit Research estimates

– Assuming a linear yearly distribution in maturity brackets, we expect the remaining debt due in the next two years to be around TRY 914mn, which is less than the current cash at hand.

– High liquidity is a plus: As of 9M08, Turkish Airlines' short-term debt (financial lease and other) stands at TRY 341mn on the balance sheet, while it reaches TRY 500mn when the off-balance sheet item of operational lease related debt is added. On the other hand, the company is sitting on a pile of cash (TRY 1,500mn), which is more than enough to cover its short-term debt.

TURKISH AIRLINES: FINANCIAL & OPERATIONAL LEASING DEBT STRUCTURE (9M08)

TRYmn	Financial	Operational	Total
Maturity structure*			
Not later than one year	302	158	**461**
Between 1-4 years	791	452	**1,243**
Over 4 years	1,293	525	**1,819**
Total	**2,387**	**1,135**	**3,522**
Rate structure			
Floating rate (4.27%)	1,047		
Fixed rate (5.00%)	1,340		
Total	**2,387**		
Currency structure**			
USD based (USD 873mn)	1,075		
EUR based (EUR 730mn)	1,312		
Total	**2,387**		

*Future interest expense deductions are distributed proportionally **FX values in brackets Source: Turkish Airlines

– Out of the total TRY 2,387mn financial leasing debt, 56% is at a fixed rate, while the remaining floats, denominated in USD and euro. Though there is a currency mismatch, due to high real interest rates paid for the Turkish lira, the company is enjoying higher interest income from its sizeable cash at hand versus the interest paid for the loans.

– The company's "(Net Debt +Capitalized Operating Lease) / EBITDAR" ratio stands at 2.0x for 2009E**,** which is below the sector average (ca. 2.5x) and signals that Turkish Airlines is on the safe side in terms of financial strength.

The company – branding, market dominance

National flag carrier with a well-known brand name

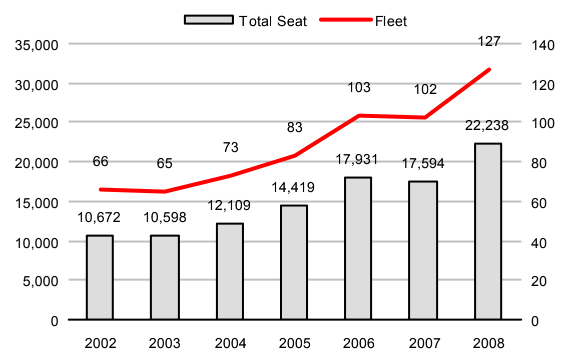
National flag carrier status is a plus for attracting Turks living abroad, which is also the reason for advantageous slots in major destination routes

- **Turkey's national flag carrier Turkish Airlines was established by the State in 1933 under the name "State Airlines Administration" in order to operate in passenger and cargo airline transportation.**
  - During the IPO in 1990 only a tiny amount (1.55%) went public, which was followed by two secondary public offerings in 2004 and 2006. The State was left with only 49% of shares (through the Privatization Administration) and Turkish Airlines adopted a private company structure. However, senior management is still appointed by the government.
  - Its long history as a state enterprise and national flag carrier status have provided great benefits to Turkish Airlines, especially getting the first-mover advantage in international slots. Some international slots to countries solely held by Turkish Airlines or at least the ones that have an advantageous hours' structure are occupied by the company.
  - Although Turkish Airlines has been competing with well-known brands on international flights for a long time, its market share always stayed strong thanks to loyal customers and its good reputation with Turkish nationals abroad.
  - The company has a 65% market share on the domestic market and 46% share in international flights as of 9M08 results.

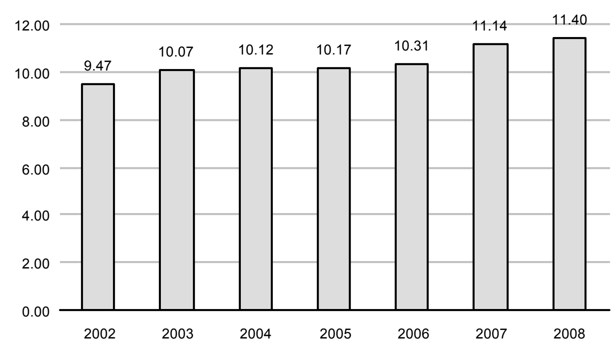
Seat capacity surged by 26% y-o-y to 22,238, as the total fleet increased from 102 in 2007 to 127 in 2008

- **Turkish Airlines, which had only five aircraft when it was founded, increased its fleet size steadily and now boasts the biggest fleet in Turkey, with 127 aircraft.**
  - With an average age of six years, the company has one of the youngest fleets in Europe. Total seat capacity increased to 22,238 in 2008, almost double the number in 2005, while it is better utilized by increasing the average daily flight utilization hours.

TURKISH AIRLINES: TOTAL SEAT CAPACITY & FLEET SIZE



AVERAGE DAILY FLIGHT UTILIZATION (HOURS)



Source: Turkish Airlines

TURKISH AIRLINES' FLEET (AS OF 31 DECEMBER 2008) (1)

	Type of aircraft	Seat capacity	Max Range (km)	# of aircraft	Owned	Financial Lease	Operational Lease
	A340	271	11,952	9	*7*	–	*2*
	A330	250	10,371	5	–	*5*	–
	A310 (2)	210	8,100	6	*5*	–	*1*
	A321	202	3,350	17	–	*12*	*5*
	B737-800(3)	165	4,755	53	–	*39*	*14*
	A320	150	3,350	22	–	*12*	*10*
	B737-400	150	3,350	9	–	–	*9*
	A319	124	3,350	4	–	–	*4*

* (1) excluding two wet lease B777-300ER (2) Including three cargo planes (3) Including one B737-700

Source: Turkish Airlines

Geographical hub advantage

Turkey is located at a major crossroads, as Istanbul is easily accessible from 55 countries in three flight hours

- **Turkish Airlines uses Istanbul Ataturk Airport as its main hub and flies to 145 destination points, 34 of which are domestic and 102 international in 70 countries.**

  – The company has a major advantage because of its geographical location, i.e. as a transfer point between West and East. As a matter of fact, Istanbul is easily accessible from 55 countries in only three flight hours.

  – As an example, rather than offering Dushanbe (Tajikistan)-London with a long-range plane, Turkish Airlines can offer Dushanbe-Istanbul and from Istanbul to any city in Europe including London with medium-haul aircraft, (e.g. cost-efficient B737-800). This is an advantage vs. its peers in terms of lower costs and, much more important, higher frequency.

  – In order to utilize more of its location advantage and position itself as a transfer point, Turkish Airlines is trying to widen its destination network by adding routes in its core operation area. We believe recently added Baghdad (Iraq) and upcoming routes such as Mashhad (Iran), Göteborg (Sweden) and Benghazi (Lebanon) will serve this purpose.

– According to company representatives, more than half of the passengers from/to North Europe, such as from Stockholm (Sweden), are transfer passengers (e.g. natives from countries around Turkey having emigrated to Sweden). The recently added Baghdad route is also a very profitable one, especially in terms of transfer passengers, since no other major airlines fly to this destination.

TURKISH AIRLINES' LONG-HAUL ROUTES

Source: Turkish Airlines *SkyLife Magazine*

TURKISH AIRLINES' LONG-HAUL ROUTES

Destination	Region	Distance (km)	Destination	Region	Distance (km)
Almaty	CIS	4,145	Shanghai	Far East	8,975
Astana	CIS	3,902	Singapore	Far East	9,172
Bishkek	CIS	4,072	Tokyo	Far East	10,149
Dushanbe	CIS	3,587	Muscat	Middle East	3,531
Tashkent	CIS	3,517	Sana'a	Middle East	3,550
Bangkok	Far East	7,819	Chicago	North America	9,204
Beijing	Far East	7,690	New York	North America	8,575
Hong Kong	Far East	9,078	Cape Town	South Africa	9,185
Karachi	Far East	4,210	Johannesburg	South Africa	7,920
Mumbai	Far East	5,014	Lagos	West Africa	4,852
New Delhi	Far East	4,841	Addis Ababa	East Africa	3,935
Osaka	Far East	10,536	São Paulo	South America	scheduled 2009
Seoul	Far East	8,708	Toronto	North America	scheduled 2009

Source: Turkish Airlines *SkyLife Magazine*

TURKISH AIRLINES' MEDIUM-HAUL ROUTES

Destination	Region	Distance (km)	Destination	Region	Distance (km)
Amsterdam	Europe	2,356	Riga	Europe	1,866
Athens	Europe	580	Rome	Europe	1,489
Baku	Europe	1,845	Rostov	Europe	1,379
Barcelona	Europe	2,278	Sarajevo	Europe	1,461
Basel	Europe	1,963	Simferopol	Europe	659
Batum	Europe	1,122	Skopje	Europe	704
Belgrade	Europe	893	Sofia	Europe	574
Berlin*	Europe	1,858	St. Petersburg	Europe	2,253
Birmingham	Europe	2,750	Stockholm	Europe	2,408
Brussels	Europe	2,228	Stuttgart	Europe	1,830
Bucharest	Europe	576	Tbilisi	Europe	1,439
Budapest	Europe	1,189	Tirana	Europe	872
Chisinau	Europe	724	Venice	Europe	1,510
Cologne	Europe	2,146	Vienna	Europe	1,356
Copenhagen	Europe	2,109	Warsaw	Europe	1,446
Dnepropetrovsk	Europe	1,009	Zagreb	Europe	1,198
Donetsk	Europe	1,150	Zurich	Europe	1,830
Dublin	Europe	3,033	Göteborg	Europe	scheduled 2009
Dusseldorf	Europe	2,182	Lviv	Europe	scheduled 2009
Ekaterinburg	Europe	3,035	Ashgabad	Far East	2,636
Frankfurt	Europe	1,909	Abu Dhabi	Middle East	3,246
Geneva	Europe	1,952	Aleppo	Middle East	993
Hamburg	Europe	2,180	Amman	Middle East	1,528
Hannover	Europe	2,061	Bahrain	Middle East	2,787
Helsinki	Europe	2,292	Baghdad	Middle East	1,890
Kazan	Europe	2,252	Beirut	Middle East	1,046
Kiev	Europe	1,109	Damascus	Middle East	1,193
Lefkoşa	Europe	837	Doha	Middle East	3,122
Lisbon	Europe	3,484	Dubai	Middle East	3,274
Ljubljana	Europe	1,337	Jeddah	Middle East	2,584
London*	Europe	2,580	Kuwait	Middle East	2,632
Lyon	Europe	2,147	Medina	Middle East	2,399
Madrid	Europe	2,821	Riyadh	Middle East	2,602
Manchester	Europe	2,785	Tabriz	Middle East	1,552
Milan	Europe	1,735	Tehran	Middle East	2,165
Minsk	Europe	1,561	Tel Aviv	Middle East	1,261
Moscow	Europe	1,932	Mashhad	Middle East	scheduled 2009
Munich	Europe	1,637	Algiers	North Africa	2,471
Nice	Europe	1,983	Cairo	North Africa	1,293
Nuremberg	Europe	1,733	Casablanca	North Africa	3,469
Odessa	Europe	663	Tripoli	North Africa	1,941
Oslo	Europe	2,734	Tunis	North Africa	1,796
Paris	Europe	2,358	Khartoum	East Africa	2,693
Prague	Europe	1,613	Nairobi	East Africa	scheduled 2009
Pristina	Europe	860			

* operates to/from two airports in Berlin and London

Source: Turkish Airlines' *SkyLife Magazine*

TURKISH AIRLINES' – DOMESTIC ROUTES

TURKISH AIRLINES*			
Destination	**Distance (km)**	**Destination**	**Distance (km)**
Adana	824	Mardin	1,140
Adıyaman	955	Merzifon	610
Ağrı	1,244	Muş	1,168
Ankara	419	Nevşehir	635
Antalya	535	Samsun	698
Batman	1,144	Sinop	543
Bodrum/Milas	526	Sivas	734
Dalaman	648	Şanlıurfa	1,072
Denizli	461	Trabzon	974
Diyarbakır	1,087	Van	1,304
Elazığ	961	Uşak	424
Erzincan	987	Çanakkale	267
Erzurum	1,091		
Eskişehir	305	*From İstanbul Sabiha Gokcen*	
Gaziantep	983	Ankara	393
Hatay	959	Antalya	489
İzmir	419	İzmir	431
Kahramanmaraş	874		
Kars	1,265	*From Ankara Esenboğa*	
Kayseri	696	Ağrı	911
Konya	530	Elazığ	596
Malatya	861	İstanbul	161

ANADOLU JET**			
Destination	**Distance**	**Destination**	**Distance**
Adana	402	İzmir	542
Adıyaman	542	Kahramanmaraş	447
Antalya	405	Kars	856
Batman	742	Malatya	494
Diyarbakır	670	Mardin	738
Erzincan	558	Muş	759
Erzurum	696	Samsun	325
Gaziantep	526	Şanlıurfa	592
Hatay	536	Trabzon	580
Hatay-Ercan	261	Van	907

*From Istanbul unless otherwise stated **From Ankara unless otherwise stated

Source: Turkish Airlines' *SkyLife Magazine*

Europe still constitutes the major portion of revenue generation while Middle East and African routes are growing at full speed

■ **European destinations constitute the major portion of scheduled services, with a 54% share, while the Middle East and African routes are the fastest growing ones.**

– After the first international flight to Athens, Turkish Airlines has been focusing mainly on European routes for a long time and grown strong in this region. The company preferred to fly first to European countries with large Turkish communities, which explains the vast destination routes to Germany.

– Later on, with the addition of long-haul aircraft and in line with its strategy to focus on transit flights with new narrow body aircraft, the company expanded its destination network especially in the CIS, Middle East and African countries. This is why the revenue generation from Middle East and African routes increased by 41% and 70% y-o-y, respectively, in 9M08 results. Going forward, we expect the share of European destinations to decrease while Middle East and African routes will increase at a fast pace.

TURKISH AIRLINES: BREAKDOWN OF SCHEDULED REVENUES BY GEOGRAPHY

TRYmn	2005	y-o-y %	2006	y-o-y %	2007	y-o-y %	9M08	y-o-y %
Europe	1,269	16	1,621	28	1,827	13	1,701	22
Far East	487	11	675	39	829	23	684	11
Middle East	282	13	350	24	445	27	435	41
North America	154	0	194	25	211	9	167	3
Africa	78	13	104	34	146	40	169	70
Total scheduled flight revenue	**2,269**	**13**	**2,944**	**30**	**3,458**	**17**	**3,156**	**22**

Source: Turkish Airlines

The workforce

Attractive corporate structure

■ **An adequate workforce is not a problem since Turkish Airlines has a long history of attracting new graduates through its appealing corporate structure.**

– The company offers a career in a globally operating firm with wide social benefits resulting in a higher number of new graduates applying for jobs. Experienced staff and facilities such as flight simulators enable the company to offer its staff in-house training, which ensures well-trained personnel from a high-quality labour base in Turkey. Thus, among a population of more than 70mn, we believe that Turkish Airlines will not face any problem in supplying a high-quality labour force to sustain its growth in the future.

TURKISH AIRLINES: BREAKDOWN OF STAFF (YE 2008)

Administrators	633
Pilots	1,512
Cabin Crew	3,088
IT Personnel	182
Officers abroad	1,128
Engineers, Lawyers, Doctors	103
Expert Dispatchers, Trainers	634
Technicians	72
Civil Servants	3,493
Others	727
TOTAL	**11,572**

Source: Turkish Airlines

Turkish Airlines Cargo

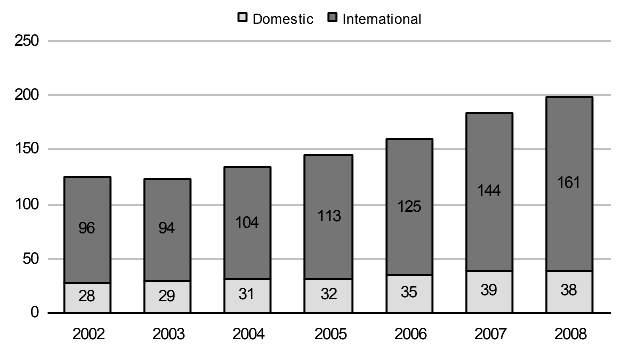
Its cargo fleet (three aircraft in 2008), will have a more positive contribution to the bottom line after the dust settles in the global economy

- **The Turkish Airlines cargo division has shown steady growth in the past five years, with Turkey's deeper integration with the global economy through rising export and import numbers.**

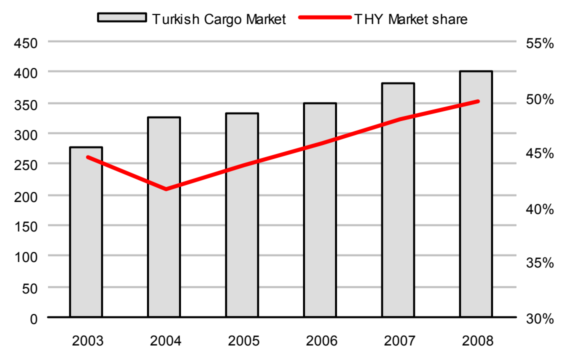
  – Total cargo carried increased by 11% CAGR in 2004-2007 while cargo revenues posted CAGR of 7% in the same period. Turkish Airlines also succeeded in increasing its 44% market share in 2003 to 49% at the end of 2008. The company served its customers via goods carried in the cargo compartment in passenger aircraft and with A310-304 cargo aircraft having 36 tons capacity. In order to utilize more from air cargo transportation, Turkish Airlines also converted some of its old aircraft for the purpose of scheduled cargo flights and increased its destination routes to those countries with which Turkey has strong economic ties.

  – Currently, Turkish Airlines had scheduled cargo flights to the cities in Turkey's major economic partners such as Frankfurt (Germany), Milan (Italy) or Moscow (Russia). We believe Turkish Airlines' cargo revenues will be hit by the slowing global economy in 2009, while we expect it to return to its high-growth path in the medium term, in line with the company's fast-growing dynamics and Turkey's further integration with the global economy.

TURKISH AIRLINES: CARGO CARRIED ('000 TONS)



TURKISH CARGO MARKET ('000 TONS)



Source: Turkish Airlines

Shareholder structure

SPO rumours from time to time may have a negative impact on the stock price...

- **Through the Privatization Administration's stake, the State is still the major shareholder of Turkish Airlines, with a 49% share.** The government also holds a golden share, which gives it enormous power over the approval of strategic decisions, such as the appointment of board members, changes in the Articles of Association, mergers and flight route planning.

  – There is a foreign ownership limitation in Turkish Airlines' Articles of Association: foreigners cannot own more than 40% of the total. If foreign investors were to buy the whole free float, they could exceed the limits, which will force management to take some actions to decrease its foreign ownership (e.g. a share buyback or raising the capital while limiting the rights issue of existing ones). We believe this limitation may cause ambiguity in the case of strong foreign interest.

– After the tiny amount of IPO proceeds back in 1990, the State decreased its stake in the company through two SPOs. During the previous SPO processes, transaction prices were calculated by taking the average of the past 10 days' closing prices prior to the SPO date, and generally around a 20% discount is applied to this calculated figure. Hence, because of the huge discount expectations and share overhang concerns, SPO announcements have negatively affected the stock price.

...while we find a short-to-medium term SPO highly unlikely

- **As long as the State holds a significant share, speculations will occasionally pop up that the State may sell its remaining shares through another SPO, which we find highly unlikely.**

– Due to the limited capital base in Turkey, foreign investors are holding 67% of the free float and are also the major buyers during IPOs and SPOs. In fact, during Turkish Airlines' SPO back in May 2006, when 28.75% of the shares were offered to the public, Templeton Funds purchased 80% of what was sold to foreign institutional investors (8.6% of the total capital) at a price of TRY 6.30 per share and placed themselves as the second-largest investor.

– Although foreign ownership of each stock is not disclosed by the authorities, taking into account the custodian data, we calculate that ca. 28% of Turkish Airlines are held by foreign investors. Thus, any potential Turkish Airlines SPO will lead to foreign ownership ratios that are prohibited in its Articles of Association.

– Based on Turkish Civil Aviation Law, the majority shareholder of all airlines operating on Turkish domestic routes should be of Turkish origin. Thus, the Turkish Civil Aviation Law should be amended first, which, in our view, is not an urgent issue before full accession into the EU.

– Second, many bilateral agreements between countries (e.g. regarding the designation of airlines for the operation of specified routes) require substantial ownership of the flag carrier (in Turkey's case Turkish Airlines) stay in local hands. Thus, in order to keep its flag carrier status, Turkish Airlines' majority of the shares should be owned by Turkish nationals.

– And finally, the Privatization Administration's current agenda is already full with urgent deals, such as electricity distribution tenders. Therefore, a Turkish Airlines SPO is not on the short-term agenda of the Privatization Administration, which the head of the Privatization Administration has already clearly stated.

– Nevertheless, although we do not expect an SPO in the short term, it is worth noting that occasional rumours could have a negative impact on the stock.

Major subsidiaries

With the Maintenance, Repair and Overhaul centre project, HABOM, THY Teknik should turn into a profit centre

- Turkish Airlines has one of the most developed technical service infrastructures in this region and in order to use this resource effectively a separate company called THY Teknik was formed on 23 May 2006.

– All related technical staff and equipment were transferred to this fully-owned subsidiary, which is the first step of Turkish Airlines' target to establish an international engine Maintenance, Repair and Overhaul (MRO) centre in İstanbul's second airport, Sabiha Gokcen, called HABOM.

– In January 2008, THY Teknik signed a joint venture agreement with Pratt & Whitney to build an aircraft engine overhaul centre in Istanbul, which will overhaul V2500 and CFM56® type engines. The centre is expected to generate revenue in 1H09 and overhaul up to 200 engines per year, which are considered to be fuel efficient new generation type engines that will face less frequent grounding in turbulent times.

– Turkish Airlines has also signed a Memorandum of Understanding with Goodrich Aerostructures to establish a JV for maintenance of Nacelle (covered housing, separate from the fuselage, which holds engines, fuel, or equipment) and a thrust reverser, and is looking for other potential partners for HABOM.

– The planned maintenance capacity of HABOM is expected to be 400 aircraft per year, most likely to serve Turkish Airlines' own growing fleet first, and is expected to generate USD 500mn in revenue by 2016. We have not included the HABOM project in our calculations, as the process has a long way to go. However, it will be clearly an additional value once fully operational.

THY DO&CO is expected to grow rapidly due to its geographical location advantage, while increasing Turkish Airlines' catering service quality

■ **Turkish Airlines formed a joint venture with Austrian catering firm DO&CO in order to enhance quality in catering services while reducing costs. The established joint venture THY DO&CO acquired all catering-related assets, personnel as well as a customer portfolio from USAS, Turkish Airlines' previous catering supplier.**

– Turkish Airlines is aiming to grow THY DO&CO as a separate business, supported by DO&CO's knowledge and efficient management and Istanbul's location as a natural hub. Star Alliance membership will have a positive impact in receiving new customers, as member airlines will likely act together with Turkish Airlines in Turkey.

– We believe that the catering business will be supportive of Turkish Airlines' bottom line in the future, both by lowering costs and increasing revenues from third parties. However, we have not attached any additional value in our calculations for the time being.

In addition to its main brand, Turkish Airlines are competing with domestic and international carriers with two LCC type sub-brands, Anadolu Jet and SunExpress

■ **To challenge LCC (low-cost carrier) and support growth, Turkish Airlines launched its own LCC for the domestic market and has also formed a joint venture with Lufthansa under the brand SunExpress for international competition.**

– Turkey's national flag carrier used to enjoy a dominant position in domestic scheduled flights prior to 2003, but started to face local LCC competition after market liberalization. Turkish Airlines doubled its number of domestic flight passengers in 2002-2007, while local LCCs grabbed a much higher portion of the strong growth in the domestic market, resulting in a drop in the company's overall market share in real terms.

– In order to challenge local LCCs more strongly, Turkish Airlines' LCC brand, Anadolu Jet, commenced its operations on 23 April 2008. Anadolu Jet is based in Ankara, the capital, and uses modified planes with a narrow seat distance, enabling much higher passenger capacity and offering limited in-flight service.

– Although constituting a small portion of the total fleet (8 out of 127 as of January 2009), Anadolu Jet supports the increase in domestic passengers, as Anadolu Jet's load factor, according to the company, is currently above 80% and it expectz to carry 2.5mn passengers in 2008.

- In addition to Anadolu Jet, Turkish Airlines has a joint venture called SunExpress to compete with other players via a different service structure. SunExpress, a joint venture with Lufthansa, operates mainly charter flights between Germany and Turkey. Based in Antalya and Izmir, the carrier has domestic and international flights from Istanbul's second airport, Sabiha Gokcen.

- Like its major domestic competitor, Pegasus Airlines, Turkish Airlines aims to grab a bigger portion from the flights out of Sabiha Gokcen, which is located on the Anatolian side of the city compared to Ataturk Airport on the European side. We believe Sabiha Gokcen Airport has long-term growth dynamics once its operating rights have been transferred to the private sector and it is classified as a LCC type of airport with some incentives offered by the State, such as lower landing fees.

- We assume limited cannibalization from the existing business of Turkish Airlines in the long term, since the services offered would be different for each brand.

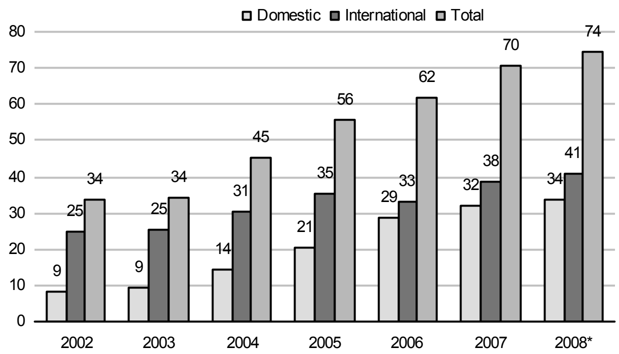
- We believe Turkish Airlines will focus more on first class passengers (both on international and domestic flights), while Anadolu Jet in Ankara and SunExpress in Istanbul will fiercely compete with both local and international carriers.

The sector – A fast growing market

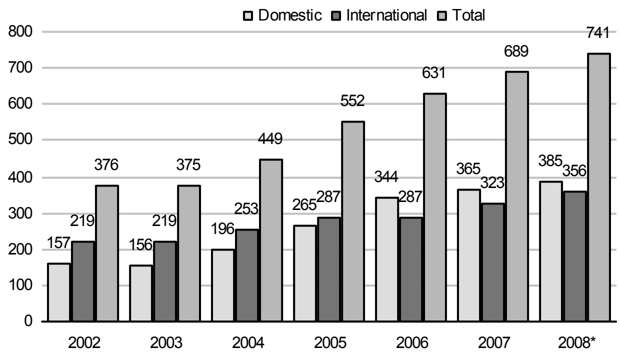
The Turkish airline sector has shown tremendous growth, as the total passenger number posted 14% CAGR in 2002-2008

- **The Turkish airline market has grown at a faster pace than the overall world market, with a 14% CAGR in passenger numbers during 2002-2007.**
  - This was supported by increasing tourism activities, integration with the global economy and the rising domestic GDP per capita in a country with a population of more than 70mn.
  - International passengers increased by 8% CAGR in this period, (tourists arrivals showed a similar rate of change), while domestic traffic has shown a tremendous growth of 30%, mainly after 2003, when the market was fully liberalized.

NUMBER OF PASSENGERS IN TURKEY (MN)



NUMBER OF FLIGHTS IN TURKEY ('000)

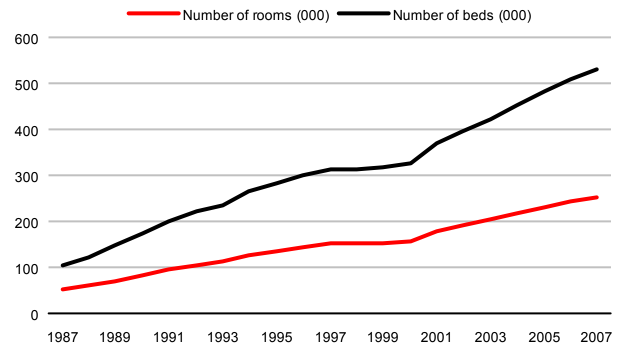


Source: SHGM

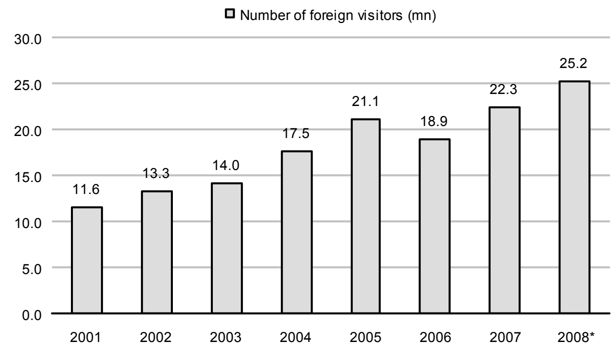
Tourism is the key supplier of Turkey's international passenger growth

- **Turkey has become one of the attractive touristy destination routes in the Mediterranean region, especially after the heavy infrastructure investments on modern accommodation facilities.**
  - Long ago, Turkey earmarked tourism as a strategic sector to be supported by incentives, because the tourism sector is a major export revenue generator and also a labour intensive service sector supporting the fight against unemployment. In line with this strategy, many infrastructure investment incentives were given to increase the number of accommodation facilities.
  - In fact, the total number of rooms and number of beds of the accommodation facilities with tourism operating licences has steadily increased in the past (8% CAGR in the past 20 years), higher than the average GDP growth. The positive development in the tourism infrastructure together with the governments' efforts to increase the brand awareness of the country's touristy destinations has boosted the number of tourists visiting Turkey.

ACCOMMODATION FACILITIES IN TURKEY



NUMBER OF FOREIGN VISITORS TO TURKEY (MN)



*2008 foreign visitors data only include January-November figures

Source: Ministry of Culture

- **Air travel is the most preferred means of transportation for tourist visits to Turkey, which mainly attracts people from Europe.**

  – According to the latest January-November 2008 figures, out of the 25.2mn tourists visiting Turkey, 71% prefer air transportation, whilst the second means of transportation is land transport with a 20% share. Thus, the number of tourist arrivals has a direct impact on international passenger numbers.

  – The number of tourist arrivals doubled between 2000 and 2007, reaching 23.3mn with a CAGR of 12%, and we are estimating this high growth to continue in the future with further investments in tourism accommodation facilities.

  – In terms of countries, Germany has the biggest stake with almost one-fifth of all tourist arrivals, as many Turks live there. Not only Turkish people coming to visit relatives in Turkey but also higher awareness of Turkish touristy regions in Germany are the reasons for this high share in total tourist numbers. Russia, on the other hand, has steadily been increasing its share in the past years (21% CAGR in 2001-2007).

  – The recent depreciation of the TRY against the EUR would position Turkey as a much more favourable holiday destination, which would be a catalyst for tourist arrivals in 2009.

TOP FIVE COUNTRIES IN TERMS OF TOURIST ARRIVALS IN TURKEY

‘000	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008***	% in total
Germany	2,884	3,482	3,332	3,984	4,244	3,601	3,979	4,250	16.8
Russia	757	947	1,281	1,605	1,865	1,801	2,405	2,830	11.2
UK	846	1,038	1,091	1,388	1,758	1,648	1,883	2,129	8.4
Bulgaria	540	834	1,007	1,310	1,622	1,084	1,129	1,135	4.5
Netherlands	633	873	940	1,191	1,254	969	1,025	1,112	4.4

*January-November figures

Source: Ministry of Culture

– Integration with Europe and increasing international trade activities especially with the EU also support the airline customer base. Turkey has made progress in recent years toward EU membership and the convergence story has resulted in an attractive investment outlook and strong foreign direct investment flow into the country in this period. This economic integration process is creating a basis for high-profile customers, who are less price-sensitive and demand a fast and high-quality service.

– Star Alliance membership confirms Turkish Airlines' safety and quality and supports the growth in premium-class passengers via increasing brand awareness and reaching a higher customer base. In fact, the company's transit and business class passenger numbers grew by 43% and 23% y-o-y respectively in 2008. Thanks to the geographical location advantage of Istanbul in the Star Alliance network and the exit of some players in some competitive routes, we expect transfer and premium class passenger numbers will continue increasing.

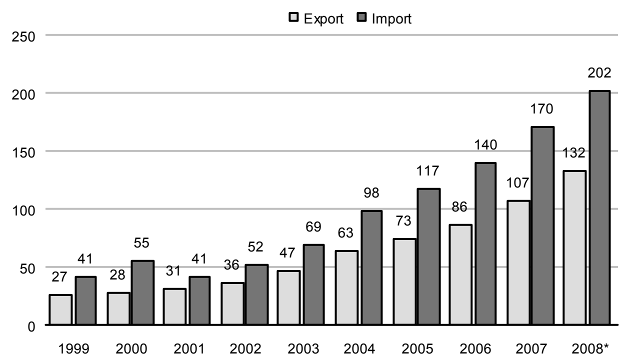
Increasing economic activity is also supporting a base for international passenger growth, especially the premium class

- **Increasing exports and imports as well as the jump in foreign direct investment are leading further growth in international passenger numbers.**

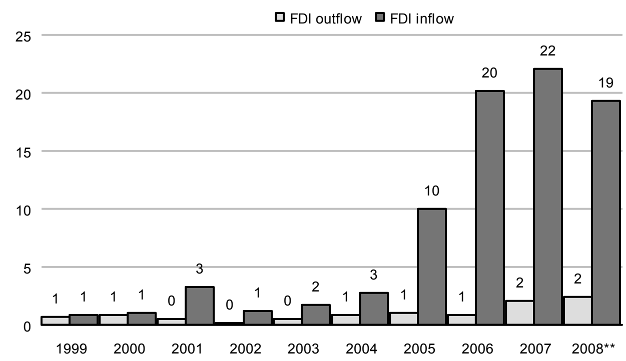
– The Turkish economy has been transforming itself as a more open and global economy, with increasing exports and imports. The stabilization in domestic politics, decline in long-time high inflation and increasing GDP have attracted more and more foreign direct investment to Turkey while Turkish companies have also started to look at opportunities abroad.

– We believe the positive developments for Turkey in the international trade and further integration with the global economy will support international passenger growth, especially those demanding premium service.

TURKEY'S INTERNATIONAL TRADE (USDBN)



FOREIGN DIRECT INVESTMENTS (USDBN)



Source: Central Bank of Turkey

Vast geography and rising disposable income supports the domestic airline traffic

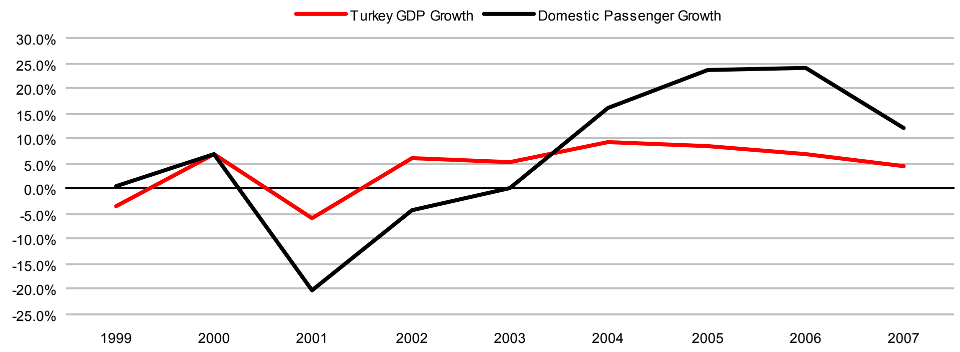
- **Because of Turkey's vast geography and rising population, there will always be demand for domestic flights.**

– Yet, the rise in disposable income and easy access to air transportation after the increase in the number of local players were the major drivers in domestic passenger growth. Thus, domestic passenger growth is highly correlated with Turkey's GDP. This trend could be easily seen from the Turkish Airlines' domestic passenger growth and GDP change.

- We believe that the Turkish domestic airline market, which posted 34% CAGR in 2003-2007, offers growth potential for all players, since travel by air is one of the most convenient means of transportation in Turkey's vast geographical area. Turkey is one of the largest countries in Europe in terms of geography with 781,000 sqkm and the distances between some major cities exceed 1,000 km (Please refer to the "Domestic Routes" table earlier in this report).

- Currently, transportation by intercity buses is still the major source of domestic travel, while the infrastructure for railways is not very well developed. If you look at the journey duration to some cities from Istanbul by bus or train, air travel is obviously the most time-efficient transportation method.

TURKEY'S GDP CHANGE VS. TURKISH AIRLINES DOMESTIC PASSENGER CHANGE



Source: Turkstat, Turkish Airlines

Legal infrastructure

SHGM under the Ministry of Transport is the top governing body in Turkish aviation while DHMI is responsible for the management of airports

- **The Ministry of Transport is the main body responsible for the regulation, licensing and certification of air transport in Turkey.**

  - The Ministry of Transport sets up the general policies and requirements for aircraft and crew, regulates the tariffs to be charged for air transport services, such as licensing fees and flight routes to be followed by the airlines.

  - The ministry exercises its authority through the Directorate General of Civil Aviation (SHGM in short in Turkish). SHGM, which was founded as The Civil Aviation Department in 1954, performs its duties in accordance with Law No. 5431, governing the organizations and duties of the Ministry of Transport. This includes air space and navigation coordination, certification and licensing of personnel and aircraft, control and inspection of navigation activities as well as implementation of international treaties.

  - The management of the airports and provision of the air traffic service in Turkey is performed by another state enterprise called General Directorate of State Airports Authority (DHMI in Turkish). DHMI performs its activities in accordance with three laws, one of which is Law No. 2920, the Civil Aviation Code. Law No. 2677 relates to the execution of functions and services at commercial airports, ports and border posts and Law No. 3832 to Defence and the Security of certain bodies and organisations.

  - The supervision of ground-handling services and execution of air traffic control services are also duties of DHMI. This is why TAV Havalimanları, the operator of Istanbul Ataturk Airport, governs the passenger side while DHMI is in control of air traffic.

A well-developed infrastructure network

Major airports were recently constructed, thus brand-new, and operated by the private sector

- **Build-Own-Transfer model was the key in the development of Turkey's infrastructure in air traffic.**

  – Turkey has sped up the private sector participation in the airport operating side, with the Build-Own-Transfer models. In the past 10 years, each major airports' operating rights are transferred to the private sector for specified durations via tenders, thus most are modernized and brand-new in terms of infrastructure.

  – Excluding the military and private purpose airports, there are 44 airports in Turkey in varying sizes and with a varying legal structure. Some airports are open to both the domestic and international carriers while others are restricted to domestic carriers only.

Domestic competition is getting tougher

The liberalization in 2003 paved the way for a fiercer domestic competition in Turkey

- **With the abolishment of Turkish Airlines' monopoly in the domestic scheduled services and the introduction of incentives to promote air traffic, domestic aviation traffic has started to face stiff competition.**

  – Domestic carriers, besides Turkish Airlines, only served as non-scheduled airlines prior to 2003. The introduction of a scheduled service to other carriers has led to a decline in average ticket prices and easy access to aviation, thus supporting the growth.

  – Currently there are 17 airlines serving scheduled/non-scheduled passenger or cargo services in Turkey. Out of seven scheduled service suppliers besides Turkish Airlines, four – Pegasus, Atlas Jet, Onur Air and SunExpress (the Turkish Airlines subsidiary) – are the most well-known in the market.

  – The domestic players mainly position themselves as an LCC and their operations are highly correlated with tourism activities, as they offer significant non-scheduled international flights to Turkey's tourism destinations. Hence, local players benefit more during tourism booms, while they may prefer to lease their fleet in other countries during turbulent times on the domestic market.

LOCAL CARRIERS IN TURKEY – DOMESTIC & INTERNATIONAL NETWORK

Name	Service (scheduled & non-scheduled)
Turkish Airlines	passenger, mail and cargo
Onur Air	passenger, mail and cargo
Atlasjet	passenger and cargo
Pegasus	passenger and cargo
SunExpress	passenger and cargo
SIK-AY	passenger and cargo
KTHY	passenger and cargo
MNG Hava Yolları ve Tasımacılık	cargo
Kuzu Hava Yolları Kargo Tasımacılık	cargo
ACT Hava Yolları	cargo
Hurkus Hava Yolu Tasımacılık	cargo
Inter Ekspres	cargo
Turıstık Hava Tasımacılık	cargo
Saga Hava Tasımacılık	cargo
IHY Izmır Hava Yolları	cargo
Tunca Havacılık	cargo
AYF Hava Tasımacılık	cargo

Source: SHGM

Financials

CONSOLIDATED INCOME STATEMENT (IFRS)

TRYmn	2006	2007	2008E	2009E	2010E
Scheduled flights	3,812	4,522	5,685	5,998	6,452
International	2,644	3,155	4,043	4,511	4,766
Domestic	852	1,048	1,270	1,108	1,295
Total cargo	316	318	372	378	391
Non-scheduled flights	38	56	85	72	77
Other revenues& discounts	202	195	296	255	274
Net sales	**4,051**	**4,773**	**6,066**	**6,324**	**6,803**
Fuel expenses	1,107	1,169	1,802	1,198	1,518
Personnel expenses	591	736	855	983	1,115
Landing&overflight expenses	333	332	407	563	591
Depreciation expenses	325	347	347	389	415
Handling expenses	194	224	285	391	411
Maintenance expenses	234	175	263	360	378
Passenger service&catering expenses	178	211	270	371	389
Operating lease expenses	174	166	150	227	238
Other	118	94	107	147	152
Cost of sales	**3,253**	**3,454**	**4,486**	**4,628**	**5,207**
Gross profit	**799**	**1,319**	**1,580**	**1,696**	**1,596**
Commission and promotion expenses	261	219	182	250	260
Other expenses	451	554	678	805	873
Operating expenses	**712**	**773**	**860**	**1,055**	**1,132**
EBIT	**86**	**546**	**720**	**641**	**463**
Net other income	163	261	211	43	36
Total financial expenses	-60	-403	328	55	-102
Minority interest	0	0	0	0	0
Profit Before Tax	**189**	**404**	**1,259**	**739**	**398**
Tax	-11	-112	-252	-148	-80
Net Profit	**179**	**292**	**1,007**	**591**	**318**
Depreciation on fixed and intangible assets	338	365	369	411	439
Severance Allowance	20	19	23	24	24
EBITDA	**444**	**930**	**1,112**	**1,076**	**927**
Operating lease expenses	174	166	150	227	238
EBITDAR	**618**	**1,096**	**1,262**	**1,303**	**1,165**
as a percentage of net sales (%)	15	23	21	21	17

Source: Turkish Airlines, UniCredit Research estimates

CONSOLIDATED BALANCE SHEET (IFRS)

TRYmn	2006	2007	2008E	2009E	2010E
Cash and liquid assets	365	772	1,410	1,096	720
Inventories	136	114	108	124	140
Accounts receivable	249	246	421	457	491
Other current assets	311	356	213	240	258
Total current assets	**1,061**	**1,488**	**2,153**	**1,917**	**1,609**
Fixed assets	3,086	3,234	4,457	4,945	5,279
Financial Assets	33	41	44	46	49
Other non-current assets	247	148	183	171	184
Total non-current assets	**3,374**	**3,434**	**4,701**	**5,181**	**5,531**
Total assets	**4,435**	**4,922**	**6,854**	**7,098**	**7,140**
Short-term debt	224	230	320	260	242
Accounts payable	318	365	419	426	479
Other current liabilities	527	522	805	831	888
Total current liabilities	**1,069**	**1,116**	**1,544**	**1,517**	**1,609**
Long-term debt	1,480	1,596	1,955	1,716	1,372
Other non-current liabilities	276	306	444	463	498
Total non-current liabilities	**1,757**	**1,901**	**2,399**	**2,179**	**1,870**
Minority interest	0	0	0	0	0
Total shareholders' equity	**1,610**	**1,904**	**2,911**	**3,402**	**3,661**
Total liabilities and equity	**4,435**	**4,922**	**6,854**	**7,098**	**7,140**
Total cash	365	772	1,410	1,096	720
Total debt on balance sheet	1,704	1,826	2,274	1,976	1,614
Capitalized operating leases*	1,140	1,027	1,265	1,701	1,785
Total debt (including operating leases)	**2,843**	**2,853**	**3,539**	**3,677**	**3,399**
Net debt (including operating leases)	**2,478**	**2,081**	**2,129**	**2,581**	**2,679**
Net debt /Equity (%)	**153.96**	**109.27**	**73.14**	**75.87**	**73.20**
Capital expenditures	**1,071**	**806**	**1,282**	**745**	**604**

* 7.5x operating leases expenses (aircraft)

Source: Turkish Airlines, UniCredit Research estimates

CASH FLOW STATEMENT (IFRS)

TRYmn	2006	2007	2008E	2009E	2010E
Profit before tax	189	404	1,259	739	398
Depreciation	338	365	369	411	439
Changes in working capital	210	113	415	-16	64
Other	-76	-95	-421	-279	-132
Operating cash flow	**661**	**787**	**1,622**	**855**	**768**
Capex	-1,071	-806	-1,282	-745	-604
Other	0	0	0	0	0
Investing cash flow	**-1,071**	**-806**	**-1,282**	**-745**	**-604**
Change in debt	-528	-211	298	-525	-600
Dividends	0	0	0	101	59
Other	0	1	0	0	0
Financing cash flow	**-528**	**-210**	**298**	**-424**	**-541**

Source: Turkish Airlines, UniCredit Research estimates

Appendix 1 – European Main Carriers

KEY FIGURES

Company	Turkish Airlines	Air France KLM	AUA	British Airways	Iberia	Lufthansa	Air Berlin	easyJet	Ryanair
Currency	TRY	EUR	EUR	GBp	EUR	EUR	EUR	GBp	EUR
Price (03 Feb 09)	6.05	7.36	4.14	120.80	1.84	10.13	4.40	277.75	3.24
Rating	Buy	Sell	Hold	Sell	no Rating	Buy	Hold	Hold	Sell
Financial Year	31.12.	31.03.	31.12.	31.03.	31.12.	31.12.	31.12.	30.09.	31.03.
Reuters	THYAO.IS	AIRF.PA	AUAV.VI	BAY.L	IBLA.MC	LHAG.DE	AB1 DE	EZJ.L	RYA.I
# of shares (mn)	175.00	294.91	88.1	1152.50	961.5	457.92	65.72	419.40	1479.13
Market cap (mn)	1,058.8	2,209.3	364.9	1,393.6	1,769.2	4,636.6	289.2	1,176.0	4,791.8
EV (mn)									
2005	2,395.2	13,340.7	2,609.7	7,546.6	3,183.1	10,299.2	1,228.0	1,462.0	6,150.0
2006	3,537.1	14,653.7	2,349.7	7,283.6	4,978.1	12,327.2	1,583.0	2,310.0	8,293.7
2007	3,139.6	16,786.7	2,062.7	7,508.9	4,756.1	13,063.2	3,506.0	2,739.0	7,205.6
2008E	3,187.9	12,496.4	1,374.7	5,052.9	2,544.1	10,743.7	3,601.9	1,898.1	5,673.6
2009E	3,639.6	9,807.3	1,074.7	4,397.6	2,414.1	8,824.6	3,305.2	1,820.1	5,766.6
2010E	3,738.1	9,578.3	1,044.7	4,423.6	2,236.1	8,862.6	3,230.9	1,934.6	5,706.1
Sales (mn)									
2005	3,107.1	21,448.0	2,393.0	8,515.0	4,946.0	18,065.0	1,215.3	1,341.4	1,692.5
2006	4,051.3	23,073.0	2,593.0	8,492.0	5,188.0	19,849.0	1,575.4	1,619.7	2,236.9
2007	4,772.6	24,114.0	2,469.0	8,753.0	5,304.0	22,420.0	2,536.5	1,797.2	2,713.8
2008E	6,065.9	24,822.4	2,460.0	9,110.0	5,428.0	25,108.1	3,402.0	2,362.8	2,962.2
2009E	6,324.1	25,375.5	2,415.0	8,955.0	5,380.0	24,694.9	3,482.0	2,581.0	3,412.1
2010E	6,803.0	26,380.0	2,470.0	9,375.0	5,475.0	24,986.5	3,594.0	2,862.0	3,914.5
EBITDAR (mn)									
2005	514.0	3,229.0	304.0	1,562.0	699.9	2,262.0	153.2	206.5	546.8
2006	618.1	3,622.0	277.0	1,416.0	790.6	2,349.0	255.5	278.5	673.4
2007	1,096.2	3,622.0	373.0	1,658.0	932.0	3,136.0	379.1	298.2	785.7
2008E	1,262.3	2,902.0	262.5	809.0	602.0	2,738.0	487.0	248.6	345.1
2009E	1,302.7	2,651.0	295.5	940.0	790.0	2,385.0	496.0	188.5	701.1
2010E	1,164.8	2,881.0	330.5	1,090.0	842.0	2,555.0	524.0	316.0	836.8
Group net result (mn)									
2005	138.2	913.0	-131.0	451.0	396.0	453.0	-115.9	59.0	306.7
2006	178.8	891.0	-130.1	290.0	57.0	803.0	50.0	94.1	435.6
2007	291.9	748.0	2.6	682.0	327.0	1,655.0	21.0	152.3	390.7
2008E	1,006.8	165.0	-196.5	-92.0	42.0	612.0	-24.0	83.2	-70.0
2009E	591.2	264.0	-52.5	30.0	105.0	366.0	15.0	29.2	322.0
2010E	318.1	402.0	21.1	140.0	198.0	458.0	40.0	113.6	423.0
EPS									
2005	0.79	3.47	-4.05	40.40	0.41	0.99	-11.59	0.15	0.20
2006	1.02	3.35	-3.55	25.50	0.06	1.75	0.84	0.23	0.28
2007	1.67	2.58	0.03	59.00	0.34	3.61	0.32	0.37	0.26
2008E	5.75	0.56	-2.23	-7.97	0.04	1.34	-0.37	0.20	-0.05
2009E	3.38	0.90	-0.60	2.60	0.11	0.80	0.23	0.07	0.22
2010E	1.82	1.36	0.24	12.14	0.21	1.00	0.61	0.27	0.29
Book value per share									
2005	7.13	29.09	16.59	166.71	1.84	8.96	19.72	2.16	1.30
2006	9.20	30.77	9.34	194.42	1.85	9.40	7.50	2.42	1.64
2007	10.88	34.52	9.36	258.17	2.12	13.70	9.03	2.77	1.65
2008E	16.63	37.19	6.35	250.08	2.14	14.24	8.68	3.05	1.67
2009E	19.44	37.55	5.95	252.85	2.22	14.70	8.90	3.12	1.88
2010E	20.92	38.16	6.12	264.99	2.49	15.15	9.51	3.39	2.16

Source: Company data, UniCredit Research estimates

EUROPEAN MAIN CARRIERS: MARGINS (%)

Company	Air France KLM	AUA	British Airways	Iberia	Lufthansa	Turkish Airlines	Air Berlin	easyJet	Ryanair
ROCE									
2005	4.9	-3.5	6.2	2.4	6.6	3.5	-1.2	3.6	14.3
2006	6.3	-3.3	4.9	0.8	7.8	2.8	6.9	5.5	17.3
2007	4.1	1.0	9.0	3.9	9.9	16.8	-2.2	9.2	14.8
2008E	4.1	n.a.	1.6	0.6	0.0	16.1	1.7	3.4	1.4
2009E	1.8	n.a.	1.0	2.5	0.0	12.9	2.6	0.8	8.3
2010E	2.7	0.1	2.6	4.4	0.0	8.7	3.6	4.8	9.6
EBITDAR margin									
2005	15.1	12.7	18.3	14.2	12.5	16.5	12.6	15.4	32.3
2006	15.7	10.7	16.7	15.2	11.8	15.3	16.2	17.2	30.1
2007	15.0	15.1	18.9	17.6	14.0	23.0	14.9	16.6	29.1
2008E	11.7	10.7	8.9	11.1	10.9	20.8	14.3	10.5	11.6
2009E	10.4	12.2	10.5	14.7	9.7	20.6	14.2	7.3	20.5
2010E	10.9	13.4	11.6	15.4	10.2	17.1	14.6	11.0	21.4
EBITDA margin									
2005	12.1	9.9	17.0	5.9	11.7	13.3	4.7	6.2	29.5
2006	13.1	7.9	15.7	6.6	11.1	11.0	8.1	9.0	27.5
2007	12.5	12.0	18.2	9.4	13.1	19.5	4.5	11.5	26.1
2008E	9.3	7.7	8.1	5.4	9.9	18.3	3.7	5.8	8.9
2009E	8.1	9.5	9.7	6.8	8.7	17.0	4.5	2.8	17.8
2010E	8.7	11.4	10.8	8.3	9.4	13.6	5.3	6.8	18.7
EBIT margin									
2005	4.3	-4.2	8.6	2.3	5.7	3.0	-0.5	4.9	22.2
2006	5.2	-3.4	7.3	2.2	5.8	2.1	4.1	7.3	21.1
2007	3.7	1.1	10.3	5.4	7.7	11.4	0.8	9.6	20.2
2008E	2.6	-4.3	0.6	0.6	4.4	11.9	0.7	3.9	2.2
2009E	1.5	-2.1	1.8	2.5	2.2	10.1	1.5	0.8	11.4
2010E	2.1	1.8	3.1	4.5	2.9	6.8	2.3	4.7	12.7
EBT margin									
2005	5.5	-9.6	7.3	3.1	5.1	5.9	-5.8	6.2	20.0
2006	4.9	-5.3	7.2	3.2	5.3	4.7	2.9	8.0	20.2
2007	4.7	-0.4	10.1	5.9	7.2	8.5	-0.5	11.2	19.8
2008E	2.5	-6.7	-0.4	1.0	3.3	20.7	-0.6	4.7	-2.9
2009E	1.4	-3.3	0.9	3.3	1.9	11.7	0.5	1.5	10.5
2010E	2.1	1.1	2.2	5.3	2.4	5.8	1.5	5.3	12.0
Net margin									
2005	4.3	-5.5	5.3	8.0	2.5	4.4	-9.5	4.4	18.1
2006	3.9	-5.0	3.4	1.1	4.0	4.4	3.2	5.8	19.5
2007	3.1	0.1	7.8	6.2	7.4	6.1	0.8	8.5	17.7
2008E	0.7	-8.0	-1.0	0.8	2.4	16.6	-0.7	3.5	-2.4
2009E	1.0	-2.2	0.3	2.0	1.5	9.3	0.4	1.1	9.4
2010E	1.5	0.9	1.5	3.6	1.8	4.7	1.1	4.0	10.8

Source: Company data, UniCredit Research estimates

EUROPEAN MAIN CARRIERS: VALUATION MULTIPLES (X)

Company	Air France KLM	AUA	British Airways	Iberia	Lufthansa	Turkish Airlines	Air Berlin	easyJet	Ryanair
EV/Sales									
2005	0.62	1.09	0.89	0.68	0.51	0.77	1.01	1.09	3.63
2006	0.64	0.91	0.86	1.00	0.61	0.87	1.00	1.43	3.75
2007	0.70	0.84	0.86	0.93	0.57	0.66	1.38	1.52	1.65
2008E	0.50	0.56	0.55	0.47	0.43	0.53	1.06	0.80	1.92
2009E	0.39	0.45	0.49	0.45	0.36	0.58	0.95	0.71	1.69
2010E	0.36	0.42	0.47	0.41	0.35	0.55	0.90	0.68	1.46
EV/EBITDAR									
2005	4.1	8.6	4.8	4.8	4.8	4.7	8.0	7.1	11.2
2006	4.0	8.5	5.8	6.6	5.1	5.7	6.2	8.3	12.5
2007	4.6	5.5	4.5	5.3	4.1	2.9	9.2	9.2	5.7
2008E	4.3	5.2	6.2	4.2	3.9	2.5	7.4	7.6	16.4
2009E	3.7	3.6	4.7	3.1	3.7	2.8	6.7	9.7	8.2
2010E	3.3	3.2	4.1	2.7	3.5	3.2	6.2	6.1	6.8
EV/EBITDA									
2005	5.2	11.0	5.2	11.5	4.7	5.8	21.5	17.7	12.3
2006	4.8	11.5	5.4	15.2	5.5	8.0	12.3	15.8	13.6
2007	5.6	7.0	4.7	9.9	4.4	3.4	30.4	13.3	6.3
2008E	5.4	7.2	6.8	8.7	4.3	2.9	28.6	13.8	21.4
2009E	4.8	4.7	5.1	6.6	4.1	3.4	21.2	25.1	9.5
2010E	4.2	3.7	4.4	4.9	3.8	4.0	16.8	9.9	7.8
EV/EBIT									
2005	14.5	-26.2	10.3	29.2	9.8	25.6		22.1	16.4
2006	11.2	-26.5	11.7	44.7	10.5	40.9	24.7	19.6	17.8
2007	19.1	79.5	8.4	17.5	7.4	5.7	163.1	15.9	8.2
2008E	19.2	-13.1	91.9	72.7	9.7	4.4	150.1	20.9	88.7
2009E	26.1	-21.3	27.5	17.9	16.3	5.7	63.6	93.5	14.8
2010E	17.4	23.2	15.0	9.2	12.4	8.1	38.5	14.3	11.5
P/E									
2005	4.0	neg.	7.0	6.0	11.0	7.7	0.0	17.8	19.8
2006	7.0	neg.	15.1	21.6	8.8	5.9	14.9	18.6	19.0
2007	12.6	neg.	7.6	9.0	5.7	3.6	46.9	16.9	8.6
2008E	28.6	neg.	-27.8	42.1	10.9	1.1	-17.0	17.0	-68.5
2009E	10.4	neg.	63.9	16.8	13.3	1.8	19.3	39.9	14.9
2010E	6.9	17.3	13.7	8.9	10.6	3.3	7.2	10.3	0.0
P/CF									
2005	1.4	0.8	2.7	3.4	2.9	2.4	0.0	13.9	14.1
2006	2.2	0.7	12.8	8.9	4.3	2.0	6.5	14.3	14.3
2007	4.5	1.3	9.2	5.3	6.2	1.6	8.5	13.4	6.4
2008E	2.6	2.5	4.2	8.0	4.1	0.8	5.2	0.0	0.0
2009E	1.4	2.7	2.5	5.3	2.7	1.1	2.4	0.0	0.0
2010E	1.3	1.8	2.4	3.6	2.5	1.4	2.0	0.0	0.0
P/Book value									
2005	0.48	0.20	1.69	1.30	1.22	0.85	0.00	1.22	3.05
2006	0.70	0.40	1.99	1.40	1.63	0.66	1.66	1.78	3.27
2007	0.91	0.40	1.73	1.40	1.50	0.56	1.66	2.17	1.77
2008E	0.20	0.65	0.89	0.86	1.02	0.36	0.51	1.11	1.94
2009E	0.20	0.70	0.48	0.83	0.69	0.31	0.49	0.89	1.72
2010E	0.19	0.68	0.46	0.74	0.67	0.29	0.46	0.82	1.50

Source: Company data, UniCredit Research estimates

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POTENTIAL CONFLICTS OF INTERESTS

A&D Pharma Holdings N.V. 4; AmRest 3, 4; Asseco Poland 4; Asseco Slovakia 2, 3; Bank Handlowy 3; Bank of Georgia 2; Bulgarian American Credit Bank 4; CA Immo International 3; Central Cooperative Bank 1a; CEZ 3, 4; Cinema City International 3; Cyfrowy Polsat SA 2, 3; Dom Development 3; ECM 3; Emperia Holding 3; Empik 3; Erste Bank 3; Eurocash 3; Getin Holding 4; GTC 3; Immoeast 3; ING Bank Slaski SA 2, 3; KGHM SA 3; Komercni Banka 3; LC Corp. 3; Lotos 3; Multimedia 3; New World Resources N.V. 2, 3; Noble Bank SA 3; OMV 3; Orco Property Group 3; OTP 2; PBG S.A. 2; Pegas Nonwovens S.A. 3; Philip Morris CR 3; PKN 3; PKO BP 3; Polskie Górnictwo Naftowe 3; Raiffeisen International 3; Ronson Europe N.V. 3; Sava Re 2, 4; Strabag SE 2, 3; Telefonica O2 CR 3; Telekomunikacja Polska SA 3; Tofas Fabrika 4; Trakcja Polska 2; TVN 3; Unipetrol 3; Vienna Insurance Group 3; Vimetco 1a; Warimpex 3; Wienerberger 3; Zakladny Azotowe Pulawy 3; Zaklady Metali Lekkich Kety SA 1a; Zentiva 3

Aareal Bank 2, 3; adidas 4; ADLER Real Estate 3; Air Liquide 3; Alcatel-Lucent 3; Allgeier Holding 4; Allianz 1b, 3, 6a; AMB Generali Holding 3; Aragon 3; BASF SE 2; Bertrandt 3; BMW 2, 3, 4; Carrefour 3; Crédit Suisse 2; Daimler 2, 3, 4; DEPFA BANK plc 2, 3; Deutsche Bank 1a, 3; Deutsche Telekom 2, 3; DIC Asset 3; E.ON 2, 3; EADS 3; ENEL 3, 6a, 7; EPCOS 4; Escada 2; FJA 4; France Telecom 3; Fresenius Pref. 2; Fresenius SE 2; Grammer 3; Graphit Kropfmühl 3, 4; HeidelbergCement 1a; hotel.de 1a, 3; Hypo Real Estate Group 2, 3; IDS Scheer 3; itelligence 3; Koenig & Bauer 2, 3, 4, 6a; LEONI 4; MPC Capital 2, 4; Nokia 3; Nordex AG 1a; Novartis 2; POLIS Immobilien 3; Postbank 2, 3, 4; Premiere 2, 4; PROCON MultiMedia AG 3, 5; Qimonda 2; Rhön-Klinikum 3; RWE 2; SAP 4; Schmack Biogas 2, 3, 4; SGL Group 6a; Sixt 3; SoftM 3; STMicroelectronics 3; Teles 3; TUI 4; UBS 2, 4; Vizrt 3; Volkswagen 1a, 2, 3; WashTec 4

A2A 3; Acotel 3, 5; ACTELIOS 3, 5, 7; Aicon 7; ALLEANZA 1a, 3; Ansaldo STS 7; Astaldi 3, 5; Autogrill 7; BANCA GENERALI 1a; Banca Monte dei Paschi di Siena 3; BANCA POPOLARE DI MILANO 3; Banco Popolare 3; Bialetti 5, 7; BREMBO 7; BULGARI 3; CAD IT 3, 5; Cairo Communication 1a; Damiani 3, 5; De' Longhi 7; Digital Multimedia Technologies 3, 5; EDISON 7; ELICA 3, 5, 7; ENEL 3, 6a, 7; ENI 3; Erg 3, 4, 7; ERG Renew 3, 4, 7; Fastweb 7; Fiat 3, 7; Finmeccanica 2, 3, 7; Fondiaria-SAI 1a; Generali 1a, 3; GEOX 3; Hera 4, 7; IFIL 6a; IMA 3, 5; IMPREGILO 7; Indesit Company 7; Intesa Sanpaolo 3; IT HOLDING 3, 5, 7; ITALCEMENTI 3, 6a; LUXOTTICA GROUP 3; Mediaset 3; MEDIOLANUM 3; Pirelli 3, 6a, 7; Poltrona Frau 1a, 3, 5, 7; Prima Industrie 2, 4, 7; Prysmian 3; REPLY 3, 5; Safilo Group 7; SAIPEM 3; SARAS 7; Seat Pagine Gialle 3; Snam Rete Gas 3; SNIA Group 7; SOGEFI 3, 5; STEFANEL 7; STMicroelectronics 3; Telecom Italia 3, 6a; TELECOM ITALIA MEDIA 6a; TENARIS 3; Terna 3; TISCALI 3; UBI Banca 3; UNIPOL 3

A-TEC Industries 4; Andritz 3; AT&S 2; Austrian Airlines 1a, 3; Bwin 3; BWT 3; C-Quadrat Investment 3; CA Immo 1a, 3, 4; CA Immo International 3; Century Casinos 3; conwert 3; CWT 3; DO & CO 3; Erste Bank 3; EVN 3; Immoeast 3; Mayr-Melnhof 3; OMV 3; Österreichische Post 3; Palfinger 3; Polytec Holding 3; Raiffeisen International 3; RHI 3; SBO 2, 3; Semperit 3; Strabag SE 2, 3; Telekom Austria 3; Verbund 3, 4; Vienna Insurance Group 3; Vienna Int. Airport 3; voestalpine 3; Warimpex 3; Wienerberger 3; Wolford 3; Zumtobel 3

Acron 4; Caspian Services 1a; Highland Gold 2; Lukoil 3; Norilsk Nickel 3; Rambler 3; RBC 1a; Steppe Cement 3; SurgutNG 3; Tatneft 3; Urals Energy 3, 4; Vimpelcom 2

Tofas Fabrika 4

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