



Transcription for PEGASUS AIRLINES

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Corporate Participants

Mehmet Nane (Translated)

Pegasus Airlines – Chief Executive Officer

Serhan Ulga (Translated)

Pegasus Airlines – Chief Financial Officer

Conference Call Participants

Alper Paksoy (Translated)

Teb Yatirim

Gorkem Görker

Yapi Kredi Yatirim

Osman Memişođlu

Bank of America

Kerem Tezcan

Citigroup

Baris Ince

Garanti Yatirim

Nida Iqbal

Morgan Stanley



Presentation

Operator

Distinguished participants, we would like to welcome you to the teleconference where we will share with you the financial results for 2016. Speakers today, we have Mr Mehmet Nane the CEO and Mr Serhan Ulga, CFO. I would like to now turn it over to Mehmet Nane.

Mehmet Nane

Hello, good morning to all. I will try and summarise the year very briefly, because this year it was really a very busy year, maybe the first of its kind for a period of 93 years. We had the attack in Sultan Ahmed and then the embargo by Russia and then we had the Ankara attacks, and all of these, of course, reached a peak with the coup attempt of 15th July, and then there was the military operations and, of course, things quickly escalated. All of these, of course, because of the developments in Turkey, affected our foreign guests. According to announcements by the Ministry of Tourism, if we do a year-on-year comparison with 2015, there have been about 10 million passenger decrease and also a decrease in revenues. This affected the tourism sector and naturally us as operators in the transportation sector. Of course, this was not the end of the world. We had to learn to live with it and we sat down and we thought about and we launched an initiative called [inaudible] and Serhan will be sharing this with you. We aimed to bring down our costs and we tried to, effectively, manage our capacity and we also did try to ensure a good cash management. As you will see in our results, thanks to these measures, as the Pegasus family, we closed the year 2016 in the best possible way, and this, of course, gives us hope for 2017 and beyond.

This was a short introduction. Mr Serhan Ulga, our CFO will be going through the presentation and sharing with you the figures. I would like to apologise, we have an annual meeting that I have to attend, so I will have to leave at quarter-past, so I apologise for having to leave this conference.

Serhan Ulga



Hello. I think you have all seen the numbers, but I will go over them briefly and then I will try and answer your questions. On slide five, you see a general comparison with 2016 and 2015. What quickly strikes our attention is, of course, the increase in the number of passengers by 8%, and the load factor has remained stable in spite of all of what has happened. Then in ancillary revenue per passenger, there has been about a €0.50 increase per passenger. These are very positive movements. In addition to this, if we carry on, if we look at the total revenue. In total revenues, the most important point is, of course, the volume impacts, the effective volume growth, and this is, of course, very significant. Then there is a devaluation of the Turkish lira and the increase in international and increasing, of course, FX impact. This has also carried our revenues forward. If we look at growth and market dynamics, we see that we grow much faster than the market, and if we look at the domestic lines, the market has grown at 5.8%, but we were able to grow almost twofold of that. In Sabiha Gökçen, of course, our market share is at around 60% and for two years it has been stable. In international lines, Turkey is contracting by 16%, but we have recorded a growth of 4% and from Sabiha Gökçen, we ensure and provide 70% of the international capacity.

If we look at the detail of domestic lines, again, there has been a passenger growth of 10.7%, as we have said, and we did share with you before that on the domestic side, we have quite a good performance. On international lines, the opposite situation is apparent. In international lines, maybe even more apparent is a drop in the yield of about 15.7%, and unfortunately there is a non-fare security perception and we feel as if we haven't done much in that area to counter that, so we plan to bring down our prices and become more competitive.

Now, looking at the fleet development. On the fleet side, the situation is, again, similar to what we have explained. As we have said, we are currently taking steps in the framework of 3c's, and we continue to work in the field of aircraft. We have signed a contract for the sale of three aircraft and I think there will be an additional sale of seven aircraft. We have made some strides in this. If we look at network and frequency development in 2016, there has been a significant growth, but there were some lines that came into play for 2017, Diyarbakır-Ercan etc and SAW and Grozny. There are some activities on the pipeline and we are receiving the permits. Armenia is one destination I can account [most there], Abu Dhabi from Istanbul and from Turkmenistan we are working on several cities as destinations. In Russia, Samara, [Svetlograd] and Volgograd are some of our destinations that we are currently working on. Next year, hopefully, we will increase a range of passengers with new destinations.

Coming to the market, we are presenting to you the figures in all of its frankness, and we have listed all the figures. I am not going to go over these figures. Here, we have hit the targets in EBITDAR, and



yes, we have reached some 550 million and there are various important factors that have played an important role here. Of course, there has been the contraction in various lines and then there are some parts that have compensated this. There has been a drop of about \$100 in the fuel cost. This has made a positive contribution, and there have been some structural changes, which have also had an impact.

For non-fuel cost per available seat, non-fuel CASK development. Here, again, we have the familiar actors. What is important here is that when you look at production of course, the most important effect comes from a low CASK production per aircraft and the capacity cuts at Sabiha Gökçen airspace has had an impact here, and the operational at least has increased. I am sure you have seen these factors before, and we're going to talk about our estimations and target for 2017.

In the balance sheet structure, of course, our cash is going down, and we continue to make investments in aircrafts. This is the main reason for this drop, and we will be making the payment for these incoming aircraft, so we continue with our aircraft investments, because as an operation, we produce positive cash. Most of the cash is being kept in hard currency, especially in US dollars. Our strategy has remained the same.

If we look at our foreign currency exposure, we don't see significant changes here. As you see in the income statement, dollar has, of course, gone up, and in expenditures, dollar has a continuing effect. It doesn't make sense to buy dollars, and so we would like to take certain measures which will be more economical. As we have explained, the dollar denominated flight tickets, we used to convert these into dollars, and for ticket and for non-ticket items now, what we do is we convert them to dollars. This is the situation and then we put these amounts in our cash deposit. We have the non-discretion standard structure for the fuel hedge and half of that is being done through purchase and then we secure the rest. For fuel, we haven't had an initiative for extra hedging, so this is the hedge operation we have. About our management action plan, about 3c, we had presented to you the roadmap and there hasn't been a significant change in these. In many processes, we have moved forward, and we have agreed with [everyone] on various issues, and we have agreed on the new neo engine, and we have signed a final sales contract for three aircraft. Again, we have in the pipeline the possible sale of seven more aircraft. Hopefully, we are going to conclude these operations. And about the human resources structure, we have taken some steps forward, and now we are doing some fine-tuning, and we don't expect a lot of change in that.



About the pricing of ancillary products, we will have a more dynamic approach to this, and hopefully we will aim at a higher level. Also, the speed taxiway construction is expected to be completed in 2017 summer season. This will also contribute to capacity. We also revisit existing contracts with suppliers, and we have concentrated more on digital marketing, and we continue with optimisation in fuel consumption. There is no new news on that.

For the cash position, as I said, it is important to manage capacity and introduce cash and, of course, the sales of aircraft will be an important step towards that direction and we will have more effective aircraft operation at lower cost. As we have said, we have the sales and lease operation that is underway. We have some eight aircraft engines and hopefully that will also be concluded.

Yes, we can now move to the target stage. Yes, we can easily say that we have kept our promise and you can even see that especially in the category of passenger growth, we have exceeded our targets and we have kept to all of the other categories and we have kept our promise.

I would like to now turn it over to Mehmet and then we can have your questions.

Mehmet Nane

If we look at 2017, we will hopefully be very active in 2017. We would like to... we have an estimate of 5-7% passenger growth. Hopefully, there will be more passengers coming from Russia. That will hopefully contribute to domestic lines, and we expect our capacity increase to be between 6-8%. In block hours, we continue to be stable at a level of 12, and in domestic and international load factors, we expect an increase of maybe 1-2%. Capacity utilisation here will be of more importance, and that will, of course, be reflected upon other categories. In domestic yield, we have a certain level and in international yield, if we can reach the 2016 levels, we believe that that will be deemed as success for 2017. The ancillary per passenger stood at €10.13 in 2016. We would like to carry this to the €11 mark. The total CASK, keeping the total CASK at certain levels is important for us, and if we look at non-fuel CASK, we ended 2016 at €2.81. We would like to bring that by €0.10 further and pull it down to €2.70 levels, and hopefully the measures that we have taken in 2016 will contribute to this. For EBITDAR, hopefully in 2017, we will carry this 1 percentage point upwards and move towards 16% in 2017.



Yes, we can now start taking your questions. Our moderator will be assisting us.

Question and Answer Session

Operator

[Operator instructions]

Alper Paksoy, Teb Yatirim, for the first question.

Alper Paksoy

I have several questions regarding the presentation and the results. First of all, you said you signed the contract for the sales of three aircraft. What will be the cash inflow from these and you said there will be some additional sales; if this is three plus up the sale of seven aircraft, what are you going to use this cash for? Also, all of these were probably aircraft that you owned or you were doing a financial lease of, so can you confirm that? How much of the debt do you have fixed and variable interest rates?

Mehmet Nane

Yes, we cannot share with you the information as to how much cash we are going to receive from the sales of aircraft, but we will be sharing these with you at a later stage, but I can say the following the cash that will come from the sales of these aircraft will contribute to the PDP and to the PDP of the aircraft that will be incoming, so for the pre-payment, so it will not respond to any operational need, but we continue with the investment, so it will help support our investments. Yes, we were doing financial lease of these aircrafts, so they are on our balance sheets and at the end of the lease period, they are turned over to your ownership. As of the end of the year, we have 25 financial lease



aircraft, so five of these have been fixed with [IRS] but the rest are based on variable interest rates at very minimal margins. I don't know if I have been able to answer your questions. Thank you.

Operator

Our next question, Gorkem Görker, Yapi Kredi Investment.

Gorkem Görker

I would like to ask about growth in 2017. Can you tell us more about the breakdown between domestic and international, and also when we make our estimates we now have some 80 aircraft, but based on what you're saying, 10 of these will be sold, but we see an increase in capacity, so how many aircraft will there be in the fleet in 2017 on average? Also, what is the CapEx that you plan?

Mehmet Nane

Now, Gorkem, our strategy is as follows. In the summer months, April through September, we aim to grow our capacity, so our end of year figures will not reflect the real production, but in 2016, between April-October, we have flown 73 aircraft, but that will increase; that will go up to 76, so there will be a 5% increase in the most important six-month period of the year. The rest, the maintenance and entry and exit of aircraft are usually carried out outside of this peak window. About the growth of 2017, I couldn't quite understand your question, because the FX that you see in financials will probably stay the same, a few percentage points may move towards the international destinations that will be launched, so there may be a change in the capacity, but when you look at the CapEx investment, it's around TL 600 million based on the FX rate of today, so that is the total CapEx investment, and more than half of that will go under aircraft CapEx.

Gorkem Görker

Additional question: we have reduced the human resources; can we take that as a trend for 2017?



Mehmet Nane

Yes.

Operator

Next question, Osman Memiřođlu, Bank of America.

Osman Memiřođlu

My first question is about... is 20 the rate for now or is it a target, because it was quite low in the beginning of the year? In your forecast for 2017, it seems as if capacity increase will be 6-8%, but you are moving upwards in the load factor, so does that mean kilometres will be increasing? Could you elaborate on that?

Mehmet Nane

The hedge issue, Osman, is, yes, 20% and 30% of that is rolling, so when a new destination opens, that is also added in the pipeline, so we have to meet a target of 30% hedged, that is our target, and that is the process that we are currently in, and this is what the story of 20% signifies. Yes, as it stands, but the 20% means that... 20% of the production for the next month and that is the story that you're asking about. What was the other question?

Gorkem Gorker

About the number of passengers and it seems as if the load factor is going down.



Mehmet Nane

But there is a [inaudible] that isn't present in this equation and we haven't written that down. Maybe that is the reason. Thank you.

Operator

[Operator instructions]

Kerem Tezcan from Citigroup.

Kerem Tezcan

We are in mid-March, in forward bookings, do you believe that there will be a development where you can push your target for passengers more than the 5-7% mark? Are these conservative expectations or is this where it stands and do you expect to be in this bracket until the year-end?

Mehmet Nane

What you said second holds true, especially the domestic developments supports what you said last, and forward booking usually picks up towards the last weeks, so that's what usually happens.

Operator

Our next question, [inaudible].



Speaker

I would like to ask about domestic yield and international yield. When we look at the realisations, it seems as if your target for 2017 is a bit optimistic. Could you comment on this?

Mehmet Nane

Yes, the fourth quarters are always one of the lowest for any airline company, so Q4 cannot be an indicator for the whole of 2017. I don't think there is anything I can say further to this.

Speaker

So that cannot be seen as a factor that will spread out. If we look at the seasonality, my friends, the first three months usually are lower months and then there is an upward trend that starts, and then in Q2/Q3, this usually is sustained and as of October, there is a downward trend usually, and this period when... and in November and December, there will be a low point and then there will be a movement, so November and December are the two worst months of the year. My question really is about air travel demand and it is expected to be at a lower level in 2017, so an aggressive pricing policy is questionable. Are you going to continue to have an aggressive policy for 2017? In passenger growth you expect a 5-7% growth, so I wanted to ask if you can have a more aggressive pricing policy to increase the number of passengers just to measure your strategy.

Mehmet Nane

Hopefully, if you come and sit on this seat, you can apply these strategies, but this is how our strategy stands at the moment.



Operator

Osman Memiřođlu, Bank of America Merrill Lynch.

Osman Memiřođlu

On the lease side in costs, do we have the LIBOR effect on operating these, because there is a significant increase on the dollar side?

Mehmet Nane

In operating leases, no, those are monthly payments. When we are concluding them, this could be the situation for maybe three, four aircraft, but for the majority, there is no such effect, no.

Osman Memiřođlu

On the financial side, majority of the leases are dollar denominated, yes?

Mehmet Nane

No, most of them are in Euros is the answer.

Operator

Next question, Baris Ince, Garanti Yatirim.



Baris Ince

A short while ago, an announcement made about some changes in the Sabiha Gökçen terminal, I think there will be a new boarding hall etc. When will this construction be completed and how much is it going to ease the capacity situation in Sabiha Gökçen?

Mehmet Nane

Now, the reason for building this boarding hall is for the second apron that will be built. This one runway is fully utilising the existing terminal. When there will be two runways in 2019 then it will be necessary to have another terminal and it is not foreseen for the existing terminal to be extended, so there are plans to build a second terminal, but there have been no tenders. You may remember that three, four months ago, our Minister of Defence said Sabiha Gökçen will be sold and they expect revenue, but what he meant was that the second... he was talking about the tender process for the second terminal. If we have any documents, any information as regards this, and if it is going to be a public tender, because sometimes they're targeted tenders, then of course we will carry out visibility studies and we will pass on information to you, but we don't have any information. There's no work on this currently. Thank you.

Operator

[Operator instructions]

We have a question from Nida Iqbal, Morgan Stanley. Madame, please go ahead.

Nida Iqbal

But if you can comment on how competition is looking year-to-date and then secondly in terms of your 2017 CASK guidance, which is basically roughly flat in 2016, do you think this is conservative, i.e.



could CASK be lower than this? Thirdly, why did ancillary revenue per passenger decline in the fourth quarter year-on-year? Thank you.

Mehmet Nane

Three questions were asked, I don't know if everybody could hear. One was about competition, I think, if I didn't misunderstand, whether there is a newcomer in competition, at the moment it will be difficult to say yes to this question. I don't think there are any initiatives here. In the fourth quarter, but I think there was a question about the drop in ancillary income, which has to do with the domestic destinations and foreign exchange, and whether unit costs are conservative or if they can be even lower. Maybe they can be a little lower, but we have to manage it, as we carry on. So there may be a marginal downside movement, but we don't have reason to be more optimistic at the moment. I don't know if this has been the answer to your question.

Unfortunately, I will have to leave for the annual pilots meeting.

Operator

We have no further questions and I would like to turn it over to you once again.

Mehmet Nane

I thank you very much to each and every one of you for taking part on behalf of our team and CFO team. Hopefully, we believe wholeheartedly that 2017 is going to be a better year than 2016 and thanks to the measures that we employ we will have a much better time in 2017, a very bright future awaits us, so please have confidence in us. Thank you.