Transcription for PEGASUS AIRLINES

November 10th 2015

Corporate Participants

Serhan Ulga

Pegasus Airlines – Chief Financial Officer

Conference Call Participants

Cenk Orcan

HSBC

Muneeba Kayani

Morgan Stanley

Analyst/Participant Name

Company

Alper Paksoy

BNP Parisbas

Kerem Tezcan

Citi Group

Osman Memisoglu

Bank of America Merrill Lynch

Presentation

Operator

Welcome to Pegasus Airlines 2015 Q3 results webcast. At any time during this conference, you can press 01, the key for the question and answer session. I now hand over to Mr. Serhan Ulga, CFO. Sir, please go ahead.

Serhan Ulga

Good morning everyone. Ladies and gentlemen, welcome to our Q3 webcast.

Before I start with the presentation, I guess I want to just mention two housekeeping items. The first one is something that I think will make most of you very happy, that starting 2016 January, we are going to be publishing our Turkish results monthly. This will assist you with your numbers and models and everything.

The other reminder or housekeeping item is that we have an analysts meeting scheduled at our headquarters tomorrow at 09h30, which will be followed by a brief – not a brief but a visit to the Sabiha Gökçen Airport and have, of course, look at our operations. I think that will be a good opportunity to connect again.

Having said this, I think let's start with the key messages from management page. We just tried to highlight here the basic results as you see it from where we stand. It has been a good operating result for Q3. We were able to add nine new destinations. Now we are flying to more than 100 destinations in 40 countries.

One of the other important things that we wanted to share with you – I am sure there will be questions and we will talk about it more – is that we have seen the work in progress on the second runway project at Sabiha Gökçen, which is very good news and good developments. We have spent some time with the contractor and [airport of] Turkey's officials there and I will share our impressions on that one.

The basic has remained the same. Overall, no change in basic strength and design of the business for the end of the nine months. On the operational performance, I think the numbers, I don't want to spend time on it because I think we may deal with that more effectively on the Q&A session. The only thing that I am going to highlight here is the average stage length dropped slightly due to the portion of the domestic operation, that is into the Q3 compared to the same quarter in 2014 fiscal year.

On the revenue performance, the revenues went up from TL1.1 billion to TL1.3 billion on the back of an increase in production of more than 17% in seats, flying 10 more aircraft during the busy season, compared to the same quarter last year. What drove this increase in revenue, if you go to page 5, you are seeing that in domestic we have outgrown the market and we were able to increase the yield and yet keep the load factor flat on the back of a sizable growth in production. On the international scheduled operations, we outgrew the market by more than two times and again, with that, we were able to keep the load factor flattish and a slight drop in yields indicated on the right-hand side as well. Of course, especially on the scheduled international operations, the drop in the fuel cost helped us more then to offset the impact on the top-line for the overall performance.

On the fleet route and frequency update, this is just a repeated page. In fact, what we are documenting here is our fleet growth plan, which are under contract as of today, as of right now, so this does not potentially include other capacity we can find from the operational lease market. So the quick take-away is, based on the existing contracts, existing contractual obligations, we will be reaching 100 aircraft by the year 2020, so that would be one thing to mention, yet we still keep the flexibility of leveraging our old Boeing 737-800s in terms of disposing or selling in the market and also, by not exercising our options, we can keep this and significantly impact the growth of the fleet with those drivers. So there is the edge to keep the flexibility impact since when we started talking to you guys back in 2013.

I think the most exciting part here to me is the growth in the number of routes that I mentioned earlier. There are new routes in Q3 but there's more to come. We are foreseeing major frequency updates in European routes – Tel Aviv and Bahrain; new routes to be launched to Multan, Makhachkala, Sochi, also Baghdad, Erbil and Zaporishia, Ukraine, and there are other potential new routes that may be coming from Ankara to destinations that we always are willing to be, which is in sync with our strategy of growing north, east and south of Turkey, as we have always shared with you.

Just to give you a flavor for the overall developments since the IPO, at the IPO time we had 29 domestic destinations and 41 international destinations. As of this presentation, we have 33 domestic destinations and 70 international destinations. We are talking about almost 30 international destinations that have been added for the past two years, slightly more than two years. I think for me that is a good accomplishment and most of these international destinations that have been added are bilaterally restricted destinations. So it shows that the trend is one direction, is unlocking more restricted routes in our goal.

On the numbers side, the EBITDAR analysis, our EBITDAR margin has gone up compared to last year same quarter, from 35% to 39%, which is very a handsome growth and a very handsome percentage. The main players, as you can see in our step-up analysis, is that the fuel cost significantly helped to achieve this EBITDAR level, perhaps even slightly more than our anticipation of what we thought it was going to be.

This was offset by overall a combined scheduled flight RASK, including, as I discussed, both load factors and slightly yields erosion in the internationals. The same context, escalation on TL costs and structural impacts have remained the same and on the FX and other, actually, it is mostly volume-driven, the increase also. Our growth helped us to go up on this EBITDAR level as well, which added a net TL55 million.

The structural impacts, as you have been hearing from me, is a change in fleet mix as part of this transition from going to Airbus fleet and a one-off payroll cost that we are maintaining at the eve of the deployment of the ramp handling at our base by the company, by us, as opposed to from our ground handling supplier or vendor. We will talk about this perhaps more but this one-off cost indicates the marginal cost that we have to sustain to make this ramp handling project viable and executable on 1 June 2016. When that time comes, this marginality is going to go away because, even though we are going to be introducing new payroll costs but we are going to be taking away ramp handling costs from the P&L. So there is going to be a shift in the line of the P&L for the most part, which we can talk about a little later.

The CASK performance has been stellar although we still are in the league of the top performers in the European LCCs. As we have tried to highlight this non-fuel CASK bridge, there are certain things which are not in our control – FX and, at least, matching of the Turkish-led inflation cost base in our Turkish lira franchise and cost base, then one-off ramp handing, as I just briefly discussed with you, and then the fleet structure and the other pieces.

Compared to that same quarter last year, we had this gas station subsidiary and in June a provisional update came in. This came in on the back of an announced agreement we had reached with the OEM, our engine OEM, CFM, which has provided us significant benefits in maintenance of overhauling of our 737-800 engines up to the year 2022. So that helped us, which reflects only the portion that is attributable to Q3.

So then the CASK, the non-fuel CASK went from 2.23 to 2.32 yet, on a controllable level, it actually went up just like 0.01€c. like-for-like. Overall it was a good cost management quarter, also on the CASK side, assisted by lower fuel costs than we anticipated.

On the balance sheet side, we have introduced a new KPI line, which I think makes sense on a rolling 12 month basis... You see that we are maintaining both healthy liquidity and leverage ratios on a cash/aircraft and adjusted net debt or EBITDAR basis and our accumulation in dollar, as the stronger currency on the balance sheet, has continued or is sustained at around 60% levels.

On the foreign currency exposure, I am very glad to report to you that, compared to the same quarter last year, our dollar earnings with the transition to dollar pricing of European routes out of Turkey, which started in July you would remember, has gone up from 19% in Q3 2014 to 35% in Q3 2015 on the revenue currency breakdown and the expense breakdown has been similar but, on a net cash flow position basis, it looks like nominally our euro long portion was enough to offset the dollar short portion on our cash flow basis. This is a good improvement overall on rolling out this natural hedges in our P&L, assisted by our pricing. Overall, I am very happy about this as I have to worry less about foreign currency hedging.

Going into the next slide, we have discussed with you here the hedge and the implications of hedging activities, which are, as you know, an important subject for all of us and all of you guys. Just to report to you that there has not been any fuel hedging activities since last webcast and there has been a very nominal non-euro, like [GBP/CHF], hedging at a very marginal level. Overall, the hedge cover ratio for 2015 Q4 was 45%. On a 12 month rolling basis, we are at 28% level into 2016. I will leave you with the sensitivity numbers based on Q3 2015, to give you a flavour for how directionally it moves, how P&L moves, given the change in either the euro or dollar versus Turkish lira and the jet fuel, which has obvious implications in the P&L.

The final page, the outlook has actually stayed the same but I want to comment on this just to give you a little more background and a little deeper clarity on what we are trying to say here... We just kind of went through this. As you know, the expected increase, we are still, in fact, around the upper end of the range here in the capacity increase. Utilization is flat. On load factor and yield, the guidance is the same. The guidance is still directionally on track. However, on the market outlook, we are seeing [some deterioration] that is taking place, slightly more than we are anticipating. Winter is looking a little more challenging compared to the same time last year, earlier, but on the other hand, if you look at the charts, we have been helped by the fuel prices, similar to our competitors but more than we anticipated, as I indicated before, which also assisted us in maintaining a higher EBITDAR margin in Q3 and overall for the first 9 months.

On the ancillary revenue, the target still remains the same but bear in mind that the Turkish lira valuation or devaluation may have a slight impact on this €10 per pax revenue because a considerable close to 40% of our revenue is coming from domestic operations, which is priced in TL. Capex and cash flow guidance is pretty much the same. That leaves us with in this environment similar overall guidance that we have left you with the previous webcast.

With that, I end my comments and presentation so we can go to Q&A. I am sure there will be a lively discussion there.

Question and Answer Session

Operator

Ladies and gentlemen, if you wish to ask a question, please press 01 on your telephone keypad. Please click your handset before you ask your question. Thank you for holding until we have the first question. We have a question from Cenk Orcan, HSBC. Please go ahead.

Cenk Orcan

Hello. This is Cenk from HSBC. Good morning – one question regarding your full year guidance EBITDAR margin. You had a strong Q3 with a 34% surge in EBITDAR and you have not changed your guidance. I was wondering if you are still being conservative here. Is it more likely that you approach this EBITDAR margin ... from the upper end or do you expect a tough Q4 by not changing your guidance? I also want to confirm that – so if I missed that in your talk, did you say there has been no hedge component to your reported fuel cost in Q3?

Serhan Ulga

Cenk, thank you. First of all, our guidance has remained the same, as you have indicated. In a sense, we said similar things in different words. We have lived through October and we are looking into December. As I said, our guidance is directionally on track.

However, we are seeing more challenges going ahead of us into the winter season but on the other side we are also seeing what I call positive help coming from fuel pricing levels. Therefore, when we add them all up and being able to deliver [what we should be going to] deliver, we have [inaudible] being tracked as well, the two risks. If you look at the first 9 months, the guidance is right on track and I think the ups and downs coming from the [first line] and also the second coming from the fuel, the CASK line, guidance would remain in the existing frame for 2015. I hope that answers the question.

The other piece you asked about is the amount of – the hedging that went into the fuel line. I don't have it in front of me but I will again talk to you in just a few minutes. You can keep in mind the majority of the FX – sorry, the fuel hedging for us goes down below the line. It's what is called an ineffective hedging because it has – due to the nature of the product that we have used and therefore we cannot take a comparable P&L line, like fuel expense, but we take again the financial expense line...

Cenk Orcan

Okay, thank you very much.

Operator

We have a question from Muneeba Kayani from Morgan Stanley. Please go ahead.

Muneeba Kayani

Hi. This is Muneeba. Thanks for the call. Again on guidance, so you have maintained your CASK guidance of 2-3% increase for the full year. Given the 9 month trends, why have you maintained that guidance?

The second question is on fuel hedging. So your hedging has come down this year. What's your policy and how should we be thinking about hedging going forward?

I'm sorry – I have a third question as well. At Sabiha Airport, with capacity constraint at this point before the second runway opens and you will be adding more fleet, how do you expect to manage that and what market share do you expect to have there next year? Thank you.

Serhan Ulga

I may have not kept track of all the questions but I will try to answer as I remember them, so please help me in reminding me what you were asking. The reason we kept the CASK guidance is basically there is still the volatility that exists in dollar/Turkish lira world and also potential disruption costs that may continue to exist in the operation as we are going through this phase.

I want to also address Cenk's comment about how much hedging expense to fuel line in Q3 2015. It is TL27 million. For the 9 months, it is TL77 million, Cenk. So that FX seems to be the reason why there is so much volatility. We would say we were a little shy of changing the CASK guidance. Also adding on to that is the operational disruption that takes place and may take place at Sabiha Gökçen as the growth continues at the airport, the existing infrastructure. That was why.

The hedge policy question, I can answer it like this. As we have moved our P&L structure more dollar pricing ... and that helps us quite a bit in our dollar exposure... On the fuel side, the levels we are at right now, as I keep saying, the fuel price is not set on a level where it is consistently going to increase little by little. There is still a lot of volatility in the fuel prices. It changes week over week and there seems to be quite a lot of different stories going around the world in terms of growth, production or supply and other constraints.

So we will reconsider this hedging, continue to maintain 30% hedging or not, in our December board meeting and I will have a clearer answer for you on this going forward but currently where we stand, we are ... maintaining our 30% levels which we made or we may revise this policy based on the decision that will be taken at the board level in mid-December.

On the capacity issue, there have been meetings and constant development taking place, most of the development being the second runway under construction. There seems to be a lot of visibility and effort going into this existing progress, so that is very encouraging on 2016. This is not going to happen in 2015 but for 2016. Then also the management has been meeting with the civil aviation, the airport air traffic control and others, all related people, other players are meeting as well and there have been a lot of talk.

There have been a lot of recommendations made to the government authorities which will potentially help and I cannot tell you because it's up to the ATC and the civil aviation authorities to implement some of those recommendations. I cannot tell you how much of relief it is going to bring but yet there is still capacity left and we will for sure be there to fill that capacity. As the time passes, as the recommendations become more operational, we will share those with you first thing and it will give us a better feel as to how the operation will evolve in 2016 as well.

Muneeba Kayani

Thank you. You have answered all my questions. One last bit was on market shares – what is it now and how do you see it next year?

Serhan Ulga

Our market share domestic is 28%. Are you talking about Turkish market share or are you talking about market share at Sabiha Gökçen?

Muneeba Kayani

Sabiha Gökçen please.

Serhan Ulga

It's about 65% and we should be around the same, perhaps slightly higher, going into next year.

Muneeba Kayani

Thank you.

Operator

We have a question from Alper Paksoy, BNP Paribas. Please go ahead.

Alper Paksoy

Hi, Serhan. Thanks very much for the presentation and the information. I have a question about the ramp handling take-over process as I presume related with that was a 19% QoQ increase in number of staff. I was curious if this staff started towards the end of the quarter, beginning of the quarter. In other words, how much of the staff costs you are having in your P&L really includes the increase in staff and to get an overall picture, going into Q4, would you increase then labour costs? Would the increase in labour costs be less than or more than the decrease in handling costs? How would the total look like overall adjusted or an adjusted for this? Would there be a cost increase and how much specifically in Q4 because of this change?

The second question, if I may, is regarding the construction for the new runway at Sabiha Gökçen. When do you expect the construction to start because, from what I read, there were some legal challenges to the contract for the new runway? Have these been fully resolved and now there is a set starting date for the construction so that the new runway can be completed by mid-2017 as you mentioned?

The third question, again if I may, on the hedging loss, you have mentioned in the presentation that for Q4 the hedging price is $887 per ton. That is quite above the 500 level we are seeing in the Mediterranean market for jet fuel at this time. I presume this is from 2014. You have already written off the chooser part in your P&L I presume in Q1 and then Q3. So is this hedge cost for Q4 after the hedging losses you have recognized because it looks quite high to me given the current price of $500 per ton and all the losses you have recognized in financial expenses? Thanks very much.

Serhan Ulga

Okay, Alper. If I remember correctly, I will start from the first one. When we had first discussed this ramp handling issue, I had told you that there will be a transition from all third party vendors to all company process and I also discussed with you that the first year or two, there would be a learning curve and probably on a net-net basis we may have higher handling costs but in the form of payroll line and from the payroll line when the transition takes place but, as the growth continues, as is the case in our case, our fixed costs ... paid to people that are handling our operation, it will be accreted to the bottom-line at the latest the second to third year after its full deployment. The amounts, you have been seeing that we have been highlighting as ramp handling costs are marginal employee costs and other overheads that is incurred in order to be able to resolve this operation effectively in 2016 when the time comes. It is scheduled for 1 June.

So you will continue to see what you are looking at roughly right now, in Q3 roughly about 650-700 people, marginal addition to the workforce, will go up to 1,000 plus levels when it is fully deployed. Until then, until 1 June, when we actually cease partially getting invoices from ÇELEBİ, then these payroll expenses will basically be replacing handling invoices. Therefore, I call it marginal today but when these guys are fully operational and are handling our own entire operation at Sabiha Gökçen hub, which is a big portion of our operation, then the ramp handling costs at Sabiha Gökçen is going to go away. It will be replaced by the employee costs. There will be a shift in the lines in the P&L.

So let's say until June 1, you would see this as a one-off cost because we will continue to add new people, train them, have their uniforms, other related expenses that are going to be incurred. It is kind of like launching or start-up costs for this operation. When it becomes fully – they take over the operation, then it's not going to be marginal because then they are going to be replacing the invoices so to speak on the handling side.

So this is the way it's going to progress. The staff increase has already started. As you know, we have been disclosing this to you in the past quarters as well. We are reviewing numbers and I don't have a full 2016 number in front of me that I can share with you right now but this is the way it is going to progress.

On the new runway, actually, I have personally gone to the contracting site and met with the guy who is in charge of the contract and also the chief engineer at the [State Airport] of Turkey, who is actually very engaged, he is a knowledgeable guy and all the people we have met were very enthusiastic people. Our understanding is that they may even actually turn around their part of the process even earlier than mid-2017.

The second and the third phase now, from what we now, has been lumped into one phase, the second phase, second part let's say of the project. It is going to be put up for bidding as well in a month or two at the latest. These guys are not going to be doing the second phase. These guys are construction people, they are moving earth, levelling ground, doing other exploratory things that I'm not too much familiar with but, anyhow, the second bidding is going to involve laying the runway and doing all the [signal aviation] stuff. The expense, you can imagine that these two separate parties work in tandem and roll this out as anticipated. I think from what it looks like, mid-2017 is a very reachable target, which makes us very happy from that perspective. So we are in touch with guys and monitoring their progress.

On the hedge loss, I am not sure if I honestly understand the question you have raised. What has happened since year-end, the outstanding exposure, both on the small amount of swaps on the fuel and a bigger amount of the chooser forward contracts we have, as they mature over the course of time, are being evaluated at quarter-end market rates compared to the contractual rates.

So the difference, as long as they are outstanding and have not settled, we continue to add more if the remaining quantity times the difference in market price and the contract price exceeds the reserve that we have put aside in the previous quarter or the previous year-end, whatever, so to the extent that this multiplication works and produces a positive number, we add more expense to the financial ... and to the fuel expense as well but, to the extent that – and this has not happened since then – to the extent that prices go up and the remaining [balance] due a less amount of total exposure, then we decrease by writing an income, by creating income in the financial income line and over in the swap on the fuel line to reduce this calculation. It is sort of like a reserve accounting going on for the unsettled and remaining tonnages.

So this is the way it works and the reason why you have seen more of this coming through is because, if I'm not mistaken, you were talking about $67 at year-end and it went down to 50's and now we are talking about mid-40's fuel per barrel. This still generates the difference in the contract price less the market price, times the remaining ... outstanding funds, gives still a positive, an amount that needs to be added onto the expense and that is why we are adding onto the expense otherwise I wish – well, I don't know, it's a difficult position to be because you would be stuck between a rock and a hard place.

On one side, you don't want to incur more losses on the FX but that means lower fuel for more than 80% of your operation. On the other hand, if you want higher fuel, you are going to incur income ... in your hedge accounting. You are going to pay more for your 80% of the amount of your operational fuel bill. So it's a double-edged sword and therefore we are going to, given the volatility, still the existing volatility of the fuel prices and the way the fuel is behaving in the marketplace, meaning there is still a decent contango looking into the future at the current rates, we are revisiting this and we are going to readjust the policy of hedging fuel by year-end and we will let you know first thing.

Alper Paksoy

Serhan, thanks very much for the answer. I understand fully why you are hedging losses in financial expenses because of hedging. That's clear, thanks very much. The question I have is the price of the hedge cover, $887 for Q3. From the presentation, from what I can see is most probably it comes from choosers, which are financial contracts whose mark-to-market value is reflected in P&L as you mentioned. Because you have always written off, in line with the market value, as of the end of Q3, why is the choosers contracts price reflecting to the Q4 still so high because jet fuel ex-refinery prices was around $460-$470 per ton from what I remember? So the component to come from choosers, if they have already been mark-to-market, I thought would be much lower but they still seem very high and negatively affecting Q4. I'm sorry, if there is another mechanism, I don't understand.

Serhan Ulga

No, no, Alper, this reflects as of the end of Q3 the contract price of the hedge, not the mark-to-market value of the hedge. It's the contract price of the hedge, that $812, if that's what you're looking at, or $817 or $886 I think is what you are looking at if I am not mistaken.

Alper Paksoy

Correct.

Serhan Ulga

They reflect that way because we have restructured the hedges we had before in different portions and obviously at different pricing. So that reflects the contract price of the chooser forward for 2015 Q4. It doesn't reflect mark-to-market price. So we are giving you a prospective feeling of what it is priced at the end of Q4 yet this and the remaining, the left-over tonnages, have been reflected as a unrealized loss in our P&L. We have written more expense in our P&L based on these contractual prices and we [would route] that to the market price at September-end and that has been accounted for in the P&L as well.

So to the extent that, for example, it was $47, right, per barrel the end of September - $48, I am sorry, so to the extent that this $48.37 per barrel, if it goes up, based on the remaining volumes, we will report income this time for the outstanding leftover. I am putting – settling the ones that are standing in Q4 separately but for the outstanding for Q1 2016, if at the end of this we see $65 per barrel, then 65 less 48 compared to this, times the outstanding amount that is in Q1 2016, for example, that's the difference I am going to write as income this time because the previous one I have recorded earlier.

Alper Paksoy

I see. So the hedge impact to your fuel cost line in Q4 actually will only be from fuel swaps, which is 16%...

Serhan Ulga

Fuel cost is only impacted by swaps which are deemed effective in hedge accounting and you can write them to the relative P&L line but the chooser contracts, as we have been discussing for the past 9 months, chooser contracts are deemed ineffective and they are therefore considered or accounted for below the line in financial expense.

Alper Paksoy

I understand, thanks very much.

Operator

We have a question from Kerem Tezcan, Citi Group. Please go ahead.

Kerem Tezcan

Thanks for the presentation. Many of my questions actually have been answered by now, of course, but there are a couple of things I would like to ask still left. The first thing is regarding how you see the capacity coming into the market for 2016 and how is your feeling regarding the pricing for that period.

The second thing is the change in the fleet structure has been affecting the non-fuel cost, speaking about this year. How much of that might prevail next year and how do you see the unit cost would be – actually will be settled for 2016 considering that the ramp handling impact might be going down in the second half...

Serhan Ulga

Kerem, thanks. If I got them right, our growth is going to be in the range of 20% plus based on YoY overall production and almost of all of them will be at Sabiha Gökçen. So I see us going full fledge at Sabiha Gökçen and I don't know of the other airline or other airlines' exact plans. I am not sure but I'm sure, based on the given congestion at the other airport, there will be other air traffic coming in other than Pegasus in Sabiha Gökçen.

That's why our continued efforts and pressure to implement some quick recommendations will have a good positive benefit on the air traffic movement per hour. This may include Sabiha Gökçen maybe because – you know, I am hopeful it will be but maybe this may include stopping ... to taking Sabiha Gökçen as the ultimate airport to the other airports. This may include simply decreasing the distance between approaching aircraft from currently 8 miles to we said 5 miles but 6 miles will give the operators a lot of breathing room, quick fixtures on connecting taxi-way, not even the exit speedy taxi-ways but a very simple connection that will prevent aircraft turning around, staying longer on the runway; really quick, easy fixtures which can be done easily and I think it is all recognized and understood but I'm just saying these may be done and, if they are not done, we will be probably looking at another challenging operational year in 2016.

On unit revenue pressure, as I said, we have decent visibility into winter and winter is looking challenging for various reasons. Some of them are beyond our control – geopolitical issues, overall supply/demand in the marketplace and what-not. So there will be challenges coming ahead for the winter I can tell but, beyond, I cannot give you clear guidance. As we approach towards the year-end, we will sharpen our pens and try to show you what we see into the summer.

For the fleet, I am not too sure what the question regarding the fleet was but the fleet, I will tie that into your final question if I am correct, that you were asking the impact of fleet composition, how that impacts cost ex-fuel. I just need to remind you that we will be taking delivery of seven Airbus 320neos and those 320neos will, obviously, somehow stabilize ongoing growth via operational leasing even though there will be some operational leases involved in the coming year, so there will be a stability. You will see less of that fleet composition come in through the cost line as a marginal expense.

Also one other good thing that is going to come in, Kerem, I am very glad that I remembered, is that we are seeing that our [direction] with the CFM engine arena, the 320neo fleet order, is duly proven right and that we are seeing significant fuel burn coming from Airbus data more than what was anticipated initially. So based on the seven aircraft that is coming in throughout the year, starting let's say towards the end of the summer and into the late months, we may even reach roughly and this is a rough calculation, close to 1% fuel burn reduction quantity-wise just a like-for-like basis, having these new aircraft, the 320neos with the CFM engine.

So there will be positive things coming into place. We still have some disruption costs and we may have some additional headcounts to launch the ramp operation at Sabiha Gökçen but these are good things, a better fleet mixture in terms of more owned and also slightly close to 1% lower fuel burn even with the seven aircraft quantity-wise in 2016. I hope that should wrap up and give you clarity for what you are looking.

Kerem Tezcan

Thank you though just one last question. Regarding the expansion at Sabiha Gökçen, the new runway, at some point in time, correct me if I am wrong but are they talking about putting in a satellite terminal in addition to the new runway because at some point of time, after the additional, new runway, the existing terminal might not be enough to handle the increasing passing traffic?

Kerem Tezcan

Yes, Kerem. By the way, to all our audience, in our meeting tomorrow we will take more detailed questions and I intend to present the map overlay, the model of the two runways, the satellite terminal, the new Sabiha Gökçen overlaid on the map and see how things are progressing. I intend to share that with you and discuss that more in detail with you but, exactly, there will be a satellite terminal built in the middle of two runways, which will be basically taking all the passengers which are landing on the other runway and there will be underground passages that will be connecting people and also the cargo and the luggage into the satellite terminal, where the operations will be deployed from.

We will show that to you tomorrow on the screen and discuss the potential impact all this is going to have for us and for anybody else, for that matter. I think overall it looks to be a very promising development that we have seen in the past few months. We are very excited about this ongoing second runway construction progress. The people we have met, the calibre of how they handle this thing and their knowledge and so forth look all good.

Kerem Tezcan

Thank you.

Operator

We have a question from Osman Memisoglu, Bank of America Merrill Lynch. Please go ahead.

Osman Memisoglu

Thank you for your time. I really appreciate the conference call. Just a quick question and clarification on the hedges. Next year fuel hedges are mostly chooser forwards if I remember. I just wanted to confirm that and that means we won't see the effect of the hedges on the EBITDAR. Is that a correct assumption?

Serhan Ulga

That is a correct assumption, yes.

Osman Memisoglu

Okay. I think in your response to Cenk, the 27 million and the 77 million, were they for the effect of chooser forwards so far or something else? I missed that.

Serhan Ulga

I'm sorry, I missed that question. Can you repeat that, Osman?

Osman Memisoglu

You mentioned there was TL27 millions of hedging effect I would assume. I couldn't really hear.

PEGASUS HAVA TAŞIMACILIĞI A.Ş.
AEROPARK Yenişehir Mah. Osmanlı Bul. No.11 Kurtköy 34912
PENDİK/İSTANBUL-TURKEY **T** *+90 216 560 7000* **F** *+90 216 560 7400*

Serhan Ulga

It will be coming from swaps for Q3 that went to the fuel expense and hence went to cost line on EBITDAR line.

Osman Memisoglu

Okay, so these are the fuel swap-related figures, and 77...

Serhan Ulga

In 2016, there will be no swaps so it will be all chooser forwards remaining.

Osman Memisoglu

Okay. And you mentioned also a 30% target hedge level for '16.

Serhan Ulga

No, I mentioned that, as we have been sharing with you, we have had a minimum policy of 30% on a 12 month rolling basis, which right before our next month board meeting we are short by 2%, which can be easily levelled up to 30% but it's management's intention to take the hedging fuel, the policy and the program, back to the board (we are working on it) and present a new page and get board [inaudible] again to see if we are going to continue ... this 30% or accepted percentage or no percentage. As I said, we are testing the market every day and we are seeing other companies engage with those things. It's just that there's so much volatility, it seems like hedging may be ... creating a lot of pressure on the bottom-line but, if the hedging will come into place, then there will be consistent growth in fuel prices, continued growth or wobbly and continued lack of supply and then at that point I think when the direction is set, hedges will be more effective economically as well as accounting-wise as well.

Osman Memisoglu

Okay. And finally on the demand side, October was probably a weak month anyway with the religious holiday not being there this year. Did you see any positive development after the elections or is it a continuing downward trend from October onwards?

Serhan Ulga

I don't think there is a significant change in trend, Osman, because of this or that although market dynamics seem to be [playing].

Osman Memisoglu

Okay, so it is going to be a tough quarter from a demand perspective. Thanks a lot.

Operator

We will take questions from our Turkish audience.

[Question in Turkish]...

Serhan Ulga

I told Alican Bey that I am going to answer this in English but he is going to get the answer in Turkish on the translation side. Alican Bey, there is no trend of such a share capital increase. A share capital increase rests with the Board of Directors ... but, as management, we don't have any intention or any plans to bring any agenda item forward to the board at this time.

Operator

We have no further questions. Back to you, Mr Serhan Ulga, for the conclusion.

Serhan Ulga

Thank you for joining us early in the morning. We just wanted to make sure we can explain our numbers and take questions as soon as we went public with the figures. I hope this has helped you and I hope to see most of you or all of you tomorrow at our headquarters and look forward to talking to you and meeting you tomorrow. Thank you.

Operator

This concludes our conference call. Thank you all for participating. You may now disconnect.