CONVENIENCE TRANSLATION OF
THE REPORT AND FINANCIAL STATEMENTS
ORIGINALLY ISSUED IN TURKISH

PEGASUS HAVA TAŞIMACILIĞI
ANONİM ŞİRKETİ AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL
STATEMENTS FOR THE YEAR ENDED
31 DECEMBER 2016 TOGETHER WITH
THE INDEPENDENT AUDITOR'S REPORT

(CONVENIENCE TRANSLATION OF INDEPENDENT AUDITOR'S REPORT ORIGINALLY ISSUED IN TURKISH)

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Pegasus Hava Taşımacılığı A.Ş.

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Pegasus Hava Taşımacılığı A.Ş. ("the Company") and its subsidiaries (together will be referred as "the Group"), which comprise the consolidated balance sheet as at 31 December 2016, and the consolidated statement of profit or loss and other comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Turkish Accounting Standards ("TAS"), and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with standards on auditing issued by Capital Markets Board and Independent Auditing Standards which is a part of Turkish Auditing Standards published by the Public Oversight Accounting and Auditing Standards Authority ("POA"). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Pegasus Hava Taşımacılığı A.Ş. and its subsidiaries as at 31 December 2016, and of their financial performance and their cash flows for the year then ended in accordance with Turkish Accounting Standards.

Report on Other Legal and Regulatory Requirements

In accordance with paragraph four of the Article 398 of the Turkish Commercial Code No. 6102 ("TCC"), the auditor's report on the system and the committee of early detection of risk has been submitted to the Board of Directors of the Company on 6 March 2017.

In accordance with paragraph four of the Article 402 of TCC, nothing has come to our attention that may cause us to believe that the Group's set of accounts and financial statements prepared for the period 1 January-31 December 2016 does not comply with TCC and the provisions of the Company's articles of association in relation to financial reporting.

In accordance with paragraph four of the Article 402 of TCC, the Board of Directors provided us all the required information and documentation with respect to our audit.

DRT BAĞIMSIZ DENETİM VE SERBEST MUHASEBECİ MALİ MÜŞAVİRLİK A.Ş.
Member of **DELOITTE TOUCHE TOHMATSU LIMITED**

Z. Gaye Şentürk
Partner

İstanbul, 6 March 2017

INDEX		PAGE

PEGASUS HAVA TAŞIMACILIĞI A.Ş. AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEET
AS OF 31 DECEMBER 2016

(Amounts are expressed in TL unless otherwise stated.)

	Notes	Current year (Audited) 31 December 2016	Prior year (Audited) 31 December 2015
ASSETS			
Current assets		**1.459.825.834**	**1.833.732.173**
Cash and cash equivalents	35	692.270.625	954.974.093
Trade receivables	6	212.269.499	294.629.623
Trade receivables from third parties	*6*	*212.269.499*	*294.629.623*
Other receivables	7	118.760.830	189.515.187
Other receivables from related parties	*5*	*1.097.807*	*278.844*
Other receivables from third parties		*117.663.023*	*189.236.343*
Derivative financial instruments	30	1.127.368	2.341.144
Inventories	8	24.361.722	13.364.708
Prepaid expenses	9	399.994.707	347.664.779
Current income tax assets	27	3.586.742	29.034.468
Other current assets	19	7.454.341	2.208.171
Non-Current assets		**4.158.192.161**	**2.264.365.079**
Other receivables	7	21.031.698	29.274.800
Other receivables from third parties	*7*	*21.031.698*	*29.274.800*
Investments accounted by using the equity method	3	23.969.467	20.745.960
Property and equipment	10	3.848.615.403	2.113.308.165
Intangible assets	11	20.357.729	14.568.673
Prepaid expenses	9	237.363.891	77.827.374
Deferred tax assets	27	6.853.973	8.640.107
TOTAL ASSETS		**5.618.017.995**	**4.098.097.252**

PEGASUS HAVA TAŞIMACILIĞI A.Ş. AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEET
AS OF 31 DECEMBER 2016

(Amounts are expressed in TL unless otherwise stated.)

	Notes	Current year (Audited) 31 December 2016	Prior year (Audited) 31 December 2015
LIABILITIES			
Current liabilities		**1.038.827.055**	**991.845.572**
Short term financial liabilities	31	-	6.826.527
Short term portion of long term financial liabilities	31	338.293.216	201.887.265
Trade payables	6	317.877.743	245.899.093
Trade payables to related parties	*5*	*1.455.390*	*1.013.200*
Trade payables to third parties		*316.422.353*	*244.885.893*
Employee benefit obligations	17	24.600.271	12.636.938
Other payables	7	32.220.476	12.043.950
Other payables to third parties	*7*	*32.220.476*	*12.043.950*
Derivative financial instruments	30	-	178.165.534
Deferred income	9	302.378.913	300.686.908
Short term provisions		23.243.506	29.034.306
Short term provisions for employee benefits	*17*	*12.166.104*	*26.058.356*
Other short term provisions	*15*	*11.077.402*	*2.975.950*
Other current liabilities	19	212.930	4.665.051
Non-Current liabilities		**3.009.869.595**	**1.653.520.051**
Long term financial liabilities	31	2.338.272.374	1.206.722.990
Deferred income	9	6.660.918	9.831.545
Long term provisions		431.155.469	232.991.886
Long term provisions for employee benefits	*17*	*8.875.253*	*10.664.601*
Other long term provisions	*15*	*422.280.216*	*222.327.285*
Deferred tax liabilities	27	233.780.834	203.973.630
SHAREHOLDERS' EQUITY		**1.569.321.345**	**1.452.731.629**
Equity attributable to shareholders' of the parent		**1.575.439.911**	**1.455.437.269**
Paid-in share capital	20	102.272.000	102.272.000
Share premiums on capital stock		455.687.025	455.687.025
Effects of business acquisition		29.504.957	29.504.957
Other comprehensive income/expense not to be reclassified to profit or loss			
Actuarial gains/(losses) on defined benefit plans	26	(3.305.232)	(3.172.494)
Other comprehensive income/expense to be reclassified to profit or loss			
Currency translation differences	26	638.375.994	406.940.383
Hedge fund	26	291.850	(22.138.754)
Restricted profit reserves		5.016.306	490.332
Retained earnings		481.327.846	372.728.116
Net income/(loss) for the year		(133.730.835)	113.125.704
Non-controlling interest		**(6.118.566)**	**(2.705.640)**
TOTAL LIABILITIES AND EQUITY		**5.618.017.995**	**4.098.097.252**

PEGASUS HAVA TAŞIMACILIĞI A.Ş. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2016

(Amounts are expressed in TL unless otherwise stated.)

Profit or loss	Notes	Current year (Audited) 1 January- 31 December 2016	Prior year (Audited) 1 January- 31 December 2015
Sales	21	3.707.471.135	3.488.271.223
Cost of sales (-)	21	(3.511.301.803)	(3.054.983.806)
Gross profit		**196.169.332**	**433.287.417**
General administrative expenses (-)	22	(150.565.126)	(106.495.869)
Marketing expenses (-)	22	(182.641.780)	(149.815.601)
Other operating income	23	56.376.669	95.525.619
Other operating expenses (-)	23	(25.293.898)	(3.144.484)
Operating (loss)/income		**(105.954.803)**	**269.357.082**
Income from investing activities	24	25.860.568	17.619.167
Share of investments income accounted for using the equity method	3	2.580.188	2.610.196
Operating (loss)/income before financial expense		**(77.514.047)**	**289.586.445**
Financial income	25	34.584.113	60.270.143
Financial expense (-)	25	(100.739.642)	(167.477.218)
(Loss)/profit before tax		**(143.669.576)**	**182.379.370**
Tax income/(expense)		**7.486.578**	**(70.515.497)**
Current tax expense	27	-	(17.908.212)
Deferred tax income/(expense)	27	7.486.578	(52.607.285)
(Loss)/income for the year		**(136.182.998)**	**111.863.873**
Net (loss)/income attributable to:			
Non-controlling interest		(2.452.163)	(1.261.831)
Shareholders' of the parent		(133.730.835)	113.125.704
		(136.182.998)	**111.863.873**
(Loss)/gain per share (TL)	28	(1,31)	1,11
Other comprehensive income			
Items not to be reclassified to profit or loss			
Actuarial gains/(losses) on defined benefit plans	26	(165.923)	(3.965.618)
Deferred tax effect	26	33.185	793.124
Items to be reclassified to profit or loss			
Currency translation differences		230.474.848	146.923.530
Cash flow hedge	26	28.038.256	44.945.630
Deferred tax effect	26	(5.607.652)	(8.989.126)
Other comprehensive income		**252.772.714**	**179.707.540**
Total comprehensive income		**116.589.716**	**291.571.413**
Total comprehensive income attributable to:			
Non-controlling interest		(3.412.926)	(2.582.605)
Shareholders' of the parent		120.002.642	294.154.018
		116.589.716	**291.571.413**

PEGASUS HAVA TAŞIMACILIĞI A.Ş. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2016

(Amounts are expressed in TL unless otherwise stated.)

				Other comprehensive income items not to be reclassified to profit or loss	**Other comprehensive income items to be reclassified to profit or loss**		**Retained earnings**					
	Paid in share capital	Share premiums on capital stock	Effects of business acquisition	Actuarial gains/(losses) on defined benefit plans	Currency translation differences	Hedge fund	Restricted profit reserves	Retained earnings	Net profit/(loss) for the year	Equity attributable to shareholders' of the parent	Non-controlling interest	Shareholders' equity
As at 1 January 2015	**102.272.000**	**455.687.025**	**29.504.957**	**-**	**258.696.079**	**(58.095.258)**	**-**	**229.876.620**	**143.341.828**	**1.161.283.251**	**(123.035)**	**1.161.160.216**
Transfers	-	-	-	-	-	-	490.332	142.851.496	(143.341.828)	-	-	-
Total comprehensive income	-	-	-	(3.172.494)	148.244.304	35.956.504	-	-	113.125.704	294.154.018	(2.582.605)	291.571.413
As at 31 December 2015	**102.272.000**	**455.687.025**	**29.504.957**	**(3.172.494)**	**406.940.383**	**(22.138.754)**	**490.332**	**372.728.116**	**113.125.704**	**1.455.437.269**	**(2.705.640)**	**1.452.731.629**
As at 1 January 2016	**102.272.000**	**455.687.025**	**29.504.957**	**(3.172.494)**	**406.940.383**	**(22.138.754)**	**490.332**	**372.728.116**	**113.125.704**	**1.455.437.269**	**(2.705.640)**	**1.452.731.629**
Transfers	-	-	-	-	-	-	4.525.974	108.599.730	(113.125.704)	-	-	-
Total comprehensive income	-	-	-	(132.738)	231.435.611	22.430.604	-	-	(133.730.835)	120.002.642	(3.412.926)	116.589.716
As at 31 December 2016	**102.272.000**	**455.687.025**	**29.504.957**	**(3.305.232)**	**638.375.994**	**291.850**	**5.016.306**	**481.327.846**	**(133.730.835)**	**1.575.439.911**	**(6.118.566)**	**1.569.321.345**

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

PEGASUS HAVA TAŞIMACILIĞI A.Ş. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2016

(Amounts are expressed in TL unless otherwise stated.)

	Notes	Current year (Audited) 1 January- 31 December 2016	Prior year (Audited) 1 January- 31 December 2015
A. CASH FLOWS FROM OPERATING ACTIVITIES			
(Loss)/income for the year		**(136.182.998)**	**111.863.873**
Adjustments to reconcile the (loss)/net profit			
Depreciation and amortization	10-11	226.520.338	175.962.021
Adjustments related with impairments		2.885.777	913.951
Provision for doubtful receivable	6-7	*2.885.777*	*913.951*
Adjustments related with provisions		144.238.591	82.817.760
Provision for employee benefits	17	*5.152.103*	*15.251.259*
Legal provison	15	*4.188.334*	*850.502*
Change in redelivery provision	15	*134.898.154*	*66.715.999*
Interest and commission income	25	22.381.221	(3.697.937)
Gain on equity investments accounted for using the equity method	3	(2.580.188)	(2.610.196)
Current tax expense	27	(7.486.578)	70.515.497
Other provisions related with investing or financing activities	24	(148.913.502)	(17.576.772)
Changes in working capital			
Decrease/(increase) in trade receivables		78.337.437	(61.963.391)
Increase in other receivables, prepaid expenses and other current assets		(13.568.501)	(10.500.069)
Increase in inventories		(10.997.014)	(5.700.744)
Increase in trade payables		71.978.650	69.468.853
Increase in deferred income, other payables and other current liabilities		26.076.971	45.542.541
Net cash generated from operating activities		**252.690.204**	**455.035.387**
Payment for employee, executive bonus plan and retirement benefits	17	(21.463.259)	(16.631.564)
Taxes paid	27	(3.586.742)	(46.942.680)
Payment for other provisions	15	(215.713)	(636.102)
		227.424.490	**390.825.041**
B. CASH FLOWS FROM INVESTING ACTIVITIES			
Payment for purchase of joint-venture share		(4.409.850)	(11.499.750)
Proceeds from sale of property, equipment and intangible assets		3.906.316	6.983.486
Cash outflows from purchase of property, equipment and intangible assets (*)		(197.112.987)	(66.325.604)
Changes in cash advances and payables		(38.183.325)	(156.318.027)
		(235.799.846)	**(227.159.895)**
C. CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase in borrowings		697.352	869.726
Repayment of principal in financial lease liabilities		(251.678.772)	(189.667.055)
Interest and commission paid		(47.667.703)	(38.407.383)
Interest received		28.998.638	41.421.134
		(269.650.485)	**(185.783.578)**
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS BEFORE TRANSLATION EFFECT (A+B+C)		**(278.025.841)**	**(22.118.432)**
D. TRANSLATION DIFFERENCES EFFECT ON CASH AND CASH EQUIVALENTS		15.322.373	120.201.756
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS (A+B+C+D)		**(262.703.468)**	**98.083.324**
E. CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	35	954.974.093	856.890.769
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD (A+B+C+D+E)	**35**	**692.270.625**	**954.974.093**

(*) TL 1.206.134.276 of tangible and intangible assets acquisitions in total of TL 1.443.698.292 was financed through finance leases for the year ended 31 December 2016 (31 December 2015: TL 54.291.073 of tangible and intangible assets acquisitions in total of TL 120.616.677 was financed through finance leases).

NOTE 1 - ORGANIZATION AND OPERATIONS OF THE GROUP

Pegasus Hava Taşımacılığı A.Ş. (the "Company" or "Pegasus") and its subsidiaries (together "the Group") is a low cost airline. The Group operates under a low cost business model and employs low cost airline business practices which focus on providing affordable, reliable and simple service. Group management focuses on providing high-frequency services on short- and medium-haul, point-to-point routes on its domestic and international transit network primarily from its main hub, Sabiha Gökçen Airport in İstanbul. The Group also operates scheduled flights from three other domestic hubs in Adana, Antalya and İzmir. The Group operates with 82 aircraft (31 December 2015: 67) including 4 owned, 33 under finance lease and 45 under operating lease as of 31 December 2016.

The Group offers a number of services ancillary to the core air passenger services and generate revenue through the provision of these services. These ancillary services include, but not limited to, revenue related to in-flight sale of beverages and food, excess baggage fees, reservation change and cancellation fees, airport check-in fees and seat selection fees.

The Group also provides cargo services and provides various training services. These training services include crew training, type rating training (i.e., training to fly a certain aircraft type), dangerous goods training and crew resource management (CRM) training.

The shareholders and their respective holdings in the Company as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Esas Holding A.Ş. ("Esas Holding")	62,92%	62,92%
Publicly held	34,51%	34,51%
Sabancı Family Members	2,57%	2,57%
Total	**100,00%**	**100,00%**

Shares of the Company has been started to be traded in İstanbul Stock Exchange since 26 April 2013, after the book building between the dates of 18-19 April 2013.

The Group's total number of full time employees as of 31 December 2016 is 5.257 (31 December 2015: 4.967). The address of its principal executive office is Aeropark Yenişehir Mah. Osmanlı Bulvarı No: 11/A Kurtkoy-Pendik İstanbul.

Subsidiaries

IHY İzmir Havayolları A.Ş.

IHY İzmir Havayolları A.Ş. ("İzair"), commenced its operations in 2006, operates domestic and international flights from İzmir Adnan Menderes Airport. İzair operates as a capacity provider to Pegasus. Pegasus acquired a 72,57% share in İzair from its primary shareholder Esas Holding A.Ş. ("Esas Holding") on 28 September 2010 for TL 18.668.069. The Group increased its ownership to 96,79% in June 2011 via capital increase, and in March 2012, further increased its ownership to 97,82%. During September 2012, Pegasus sold 46,82% of its interest in İzair to Air Berlin Finance GmbH ("AirBerlin") as part of the "AirBerlin Turkey" agreement. As of that date, Izair had been accounted for using equity method. Following of the completion of the registration of the amendment to the articles of association and the capital increase approved by İzair's shareholders on 27 March 2013, in which AirBerlin decided not to exercise its pre-emption rights; in consequence of all other shareholders had not exercised their pre-emption rights and all the capital increase has been performed by Pegasus, the percentage of the shares and votes holded in İzair has increased up to 69,12%.

NOTE 1 - ORGANIZATION AND OPERATIONS OF THE GROUP (cont'd)

Subsidiaries (cont'd)

IHY İzmir Havayolları A.Ş. (cont'd)

Pegasus further provided a call option to AirBerlin as part of the capital increase and amendments to the articles of association approved on 27 March 2013. The call option, exercisable within one year as of the date of Izair's scheduled AOC which is 14 November 2013, allows AirBerlin to restore its shareholding in Izair to the level prior to the capital increase dated 27 March 2013 by purchasing the necessary amount of shares from Pegasus. However, in accordance with the agreement between Pegasus and AirBerlin, AirBerlin did not give notice to Pegasus of its decision to exercise the call option by the expiration date of 14 August 2014. Negotiations and process over the sale with Air Berlin is ongoing as of 31 December 2016.

Therefore, the Group has consolidated İzair on a line by line basis as a subsidary as of 1 April 2013.

Air Manas

Air Manas is a limited liability company established in Kyrgyz Republic on 27 October 2006. The Group acquired 49% of Air Manas in August 2012 and has the ability to control Air Manas. The remaining shares in Air Manas are held by individuals in the Kyrgyz Republic. The Company has the right to manage the operations of Air Manas with a share rate of 49% pursuant to its rights originating from Air Manas Articles of Incorporation, and therefore Air Manas has been consolidated on a line by line basis as a subsidiary as of 31 December 2016 and 2015. The Group operates domestic and international scheduled flights under the name of Air Manas in Kyrgyz Republic.

Pegasus Havacılık Teknolojileri ve Ticaret A.Ş.

The Group, incorporated Pegasus Havacılık Teknolojileri ve Ticaret A.Ş. ("PHT") on 13 May 2016 in İstanbul for the operations of simulator technical support and maintenance. The Group owns 100% of the outstanding shares of PHT and consolidated on a line by line basis as a subsidiary.

Joint Ventures and Associates

Pegasus Uçuş Eğitim Merkezi A.Ş.

The Group incorporated Pegasus Uçuş Eğitim Merkezi A.Ş. ("PUEM") in October 2010 in Turkey, a joint venture flight training company, with SIM Industries B.V., a Dutch simulator manufacturing and marketing company. PUEM has a 737-800 "next generation" flight simulator and commenced its operations in İstanbul in January 2011. The Group owns 49,40% of the outstanding shares of PUEM and disclose as joint venture under investments accounted for using the equity method in the financial statements.

NOTE 1 - ORGANIZATION AND OPERATIONS OF THE GROUP (cont'd)

Joint Ventures and Associates (cont'd)

Hitit Bilgisayar Hizmetleri A.Ş.

Hitit Bilgisayar Hizmetleri A.Ş. ("Hitit Bilgisayar") was established in 1994, and as of 31 December 2014 it was merged with its related company Hitit Yazılım A.Ş. The scope of operations of the entity is to develop software solutions for airlines and travel agencies as well as airports, and be engaged with the activities concerning service of the foregoing operations, services and sales thereof. The Group acquired 40% of Hitit Bilgisayar's shares in March 2015 and started to disclose as joint venture under investments accounted for using the equity method in the financial statements.

The Group used its call option that is acquired during the share purchase agreement for additional Group (B) registered shares representing a further 10% of the share of Hitit Bilgisayar for a total consideration of US Dollar 1.500.000, by making the equivalent payment of TL 4.409.850 in 30 May 2016 and consequently as of 31 December 2016, participation rate has increased to 50% and weighted average participation rate has increased to 45,9% as well.

Approval of Financial Statements

Board of Directors has approved the consolidated financial statements as of 31 December 2016 and delegated authority for publishing it on 6 March 2017. General shareholders' meeting has the authority to modify the financial statements.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS

2.1 Basis of Presentation

Statement of Compliance with TAS

The Company and its subsidiaries registered in Turkey maintain their books of account and prepare their statutory financial statements in accordance with accounting principles in the Turkish Commercial Code and Tax Legislation.

Subsidiaries that are registered in foreign countries maintain their books of account and prepare their statutory statements in accordance with the prevailing accounting principles and the local currency in their registered countries.

The accompanying financial statements are prepared in accordance with the requirements of Capital Markets Board ("CMB") Communiqué Serial II, No: 14.1 "Basis of Financial Reporting in Capital Markets", which were published in the Official Gazette No:28676 on 13 June 2013. The accompanying financial statements are prepared based on the Turkish Accounting Standards / Turkish Financial Reporting Standards and interpretations ("TAS/TFRS") that have been put into effect by the Public Oversight Accounting and Auditing Standards Authority ("POA") under Article 5 of the Communiqué.

Also, the financial statements and its notes are presented in accordance with the disclosure requirements as announced by the CMB's statement on 7 June 2013.

The consolidated financial statements have been prepared on the historical cost basis except for certain financial instruments that are measured at fair values. The accompanying consolidated financial statements are based on the statutory records, with adjustments and reclassifications for the purpose of fair presentation in accordance with Turkish Accounting Standards.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.1 Basis of Presentation (cont'd)

Functional and Presentation Currency

Although there is no prominent currency affecting revenue and cost of sales, the Group's functional currency is determined as Euro for the reasons that, largest scale of scheduled flight revenue which is the Group's primary operation is generated from European flights, Euro is clearly effective on the financial liabilities of the Group and managemet reports and budget enabling the Company's management to make executive decisions are prepared in Euro. The functional currency of the Company and its subsidiaries is Euro except Air Manas. The functional curreny of Air Manas is US Dollar.

Presentation currency of the Group's financial statements is Turkish Lira ("TL"). Financial Statements have been translated from Euro and US Dollar to TL in accordance with the relevant provisions of TAS 21 ("The Effects of Changes in Foreign Exchange Rates") as follows:

- Assets and liabilities are translated using the Central Bank of the Republic of Turkey ("TCMB") Euro buying rate prevailing at the balance sheet date; 31 December 2016: 1 Euro (€) = TL 3,7099, 1 US Dollar ($)= TL 3,5192 (31 December 2015: 1 Euro (€) = TL 3,1776, 1 US Dollar ($)= TL 2,9076).
- Income and expenses are translated from Euro to TL at exchange rates at the dates of transactions and translated from US Dollar to TL using the TCMB US Dollar average buying rates.

Translation gains or losses arising from the translations stated above are presented as foreign currency translation reserve under equity. Share capital amount, representing the nominal share capital of the Company, all other equity items are presented in historic TL terms where all translation gains or losses in relation to these balances are accounted under foreign currency translation reserve.

Comparative Information and Reclassification of Prior Period Financial Statements

Consolidated financial statements of Group are prepared in comparison to prior period in order to identify financial position and performance trends. In order to maintain consistency with current period consolidated financial statements, comparative information is reclassified and significant changes are disclosed if necessary. In the current period, the Group has made several reclassifications in the prior period consolidated financial statements in order to maintain consistency with current year consolidated financial statements. There is no effect of these reclassifications in the prior period equity and statement of profit or loss. The nature, amount and reasons for each of the reclassifications are described below:

- In the balance sheet, TL 9.316.299 that was previously presented in restricted profit reserves under shareholders' equity has been reclassified and reported in retained earnings.
- In the statement of profit or loss, TL 2.283.996 that was previously presented in other expenses under cost of sales has been reclassified and reported in IT expenses under general administrative expenses.
- In the statement of profit or loss, TL 25.821.860 that was previously presented in foreign exchange gain under financial income has been reclassified and reported in foreign exchange gain from operating activities under other operating income.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.1 Basis of Presentation (cont'd)

Basis of Consolidation

The table below sets out the consolidated subsidiaries and participation rate of the Group in these subsidiaries as of 31 December 2016 and 2015:

		Participation rate		Country of registration
Name of the company	Principal activity	31 December 2016	31 December 2015	and operation
IHY İzmir Havayolları A.Ş. ("İzair")	Air transportation	69%	69%	Turkey
Air Company "Air Manas" LTD ("Air Manas") (*)	Air transportation	49%	49%	Kyrgyzstan
Pegasus Havacılık Teknolojileri ve Ticaret A.Ş.	Simulator technical support and maintenance	100%	-	Turkey

(*) In accordance with its rights arising from Air Manas Articles of Association, the Company has the right to control Air Manas operations with 49% shareholding rate and therefore, Air Manas was included in line by line consolidation as a subsidiary as of 31 December 2016 and 2015.

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company and its subsidiaries. Control is achieved when the Company:

- has power over the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

When the Company has less than a majority of the voting rights of an investee, it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally. The Company considers all relevant facts and circumstances in assessing whether or not the Company's voting rights in an investee are sufficient to give it power, including:

- the size of the Company's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;
- potential voting rights held by the Company, other vote holders or other parties;
- rights arising from other contractual arrangements; and
- any additional facts and circumstances that indicate that the Company has, or does not have, the current ability to direct the relevant activities at the time that decisions need to be made, including voting patterns at previous shareholders' meetings.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.1 Basis of Presentation (cont'd)

Basis of Consolidation (cont'd)

Consolidation of a subsidiary begins when the Company obtains control over the subsidiary and ceases when the Company loses control of the subsidiary. Specifically, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated statement of profit or loss and other comprehensive income from the date the Company gains control until the date when the Company ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income are attributed to the owners of the Company and to the non-controlling interests. Total comprehensive income of subsidiaries is attributed to the owners of the Company and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with the Group's accounting policies.

All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

Changes in the Group's Ownership Interests in Existing Subsidiaries

Changes in the Group's ownership interests in subsidiaries that do not result in the Group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognized directly in equity and attributed to owners of the Company.

When the Group loses control of a subsidiary, a gain or loss is recognised in profit or loss and is calculated as the difference between (i) the aggregate of the fair value of the consideration received and the fair value of any retained interest and (ii) the previous carrying amount of the assets (including goodwill), and liabilities of the subsidiary and any non-controlling interests. All amounts previously recognised in other comprehensive income in relation to that subsidiary are accounted for as if the Group had directly disposed of the related assets or liabilities of the subsidiary (i.e. reclassified to profit or loss or transferred to another category of equity as specified/permitted by applicable TFRSs). The fair value of any investment retained in the former subsidiary at the date when control is lost is regarded as the fair value on initial recognition for subsequent accounting under TAS 39, when applicable, the cost on initial recognition of an investment in an associate or a joint venture.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.1 Basis of Presentation (cont'd)

Associates and Joint Ventures

The table below sets out affiliates and joint ventures then indicates the proportion of ownership interest of the Company in these affiliates and joint bentures as of 31 December 2016 and 2015:

		Participation rate		Country of registration
Name of the company	Principal activity	31 December 2016	31 December 2015	and operation
Pegasus Uçuş Eğitim Merkezi A.Ş. ("PUEM")	Simulator training	49%	49%	Turkey
Hitit Bilgisayar Hizmetleri A.Ş. ("Hitit Bilgisayar") (*)	Information system solutions	50%	40%	Turkey

(*) The Group used its call option that is acquired during the share purchase agreement for additional Group (B) registered shares representing a further 10% of the share of Hitit Bilgisayar for a total consideration of US Dollar 1.500.000, by making the equivalent payment of TL 4.409.850 in 30 May 2016 and consequently participation rate increased to 50%.

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint arrangement. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

The results and assets and liabilities of associates or joint ventures are incorporated in these consolidated financial statements using the equity method of accounting, except when the investment, or a portion thereof, is classified as held for sale, in which case it is accounted for in accordance with TFRS 5. Under the equity method, an investment in associate or a joint venture is initially recognized in the consolidated statement of financial position at cost and adjusted thereafter to recognize the Group's share of the profit or loss and other comprehensive income of the associate or a joint venture. When the Group's share of losses of an associate or a joint venture exceeds the Group's interest in that associate or a joint venture (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate or a joint venture), the Group discontinues recognizing its share of further losses. Additional losses are recognized only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate or a joint venture.

When a group entity transacts with its jointly controlled entity, profits and losses resulting from the transactions with the jointly controlled entity are recognized in the Group's consolidated financial statements only to the extent of interests in the jointly controlled entity that are not related to the Group.

2.2 Changes in Accounting Policies

Significant changes in the accounting policies are applied retrospectively and prior period financial statements are restated.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.3 Changes in Accounting Estimates

Changes in accounting estimates should be applied prospectively, if only for a period in which the change in the current period. If it relates to future periods they are recognized to prospectively both in the current period and in the future period. Significant errors identified by the Group in the accounting estimates are applied retrospectively and prior period financial statements are restated. The Group has not made any changes in accounting estimates in the current year.

2.4 Application of New and Revised Turkish Accounting Standards (TAS)

(a) Amendments to TAS affecting amounts reported and/or disclosures in the financial statements

None.

(b) New and revised standards applied with no material effect on the consolidated financial statements

Amendments to TAS 16 and TAS 38	*Clarification of Acceptable Methods of Depreciation and Amortisation* [1]
Amendments to TAS 16 and TAS 41 and amendments to TAS 1, TAS 17, TAS 23, TAS 36 and TAS 40	*Agriculture: Bearer Plants* [1]
Amendments to TFRS 11 and TFRS 1	*Accounting for Acquisition of Interests in Joint operations* [1]
Annual Improvements to 2011-2013 Cycle	*TFRS 1* [2]
Amendments to TAS 1	*Disclosure Initiative* [2]
Annual Improvements to 2012-2014 Cycle	*TFRS 5, TFRS 7, TAS 34, TAS 19* [2]
Amendments to TAS 27	*Equity Method in Separate Financial Statements* [2]
Amendments to TFRS 10 and TAS 28	*Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* [2]
Amendments to TFRS 10, TFRS 12 and TAS 28	*Investment Entities: Applying the Consolidation Exception* [2]
TFRS 14	*Regulatory Deferral Accounts* [2]

[1] Effective for annual periods beginning on or after 31 December 2015.
[2] Effective for annual periods beginning on or after 1 January 2016.

(c) New and revised standards in issue but not yet effective

The Group has not applied the following new and revised standards that have been issued but are not yet effective:

TFRS 9	*Financial Instruments* [1]
TFRS 15	*Revenue from Contracts with Customers* [1]

[1] Effective for annual periods beginning on or after 1 January 2018.

The Group evaluate the effects of these standards on the consolidated financial statements.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies

Related Parties

Related parties comprise of any person or entity related to the entity preparing the financial statements (reporting entity).

a) Any individual or any one of the close family members of such individual are considered as being related with the reporting entity: In the event the subject matter individual,

(i) is in possession of control or joint control over the reporting entity,
(ii) is entitled to a crucial influence on the reporting entity,
(iii) is a member of the key management staff of the reporting entity or one of the major shareholders of the reporting entity.

(b) In the event any of the following circumstances is present in existence, the entity is considered to be in relation with the reporting entity:

(i) If the entity and the reporting entity are members of the same group (in other words, each major partnership, associated partnership and other associated partnership is related to the others).
(ii) If the entity is an affiliate or business partnership of the other entity (or a member of the group that such other entity is also a member of).
(iii) If both entities are business partnerships of the same third party.
(iv) If one of the entities is a business partnership of any third entity and the other entity is an affiliate of the subject matter third entity.
(v) If there are benefit plans for the post-retirement stage with respect to the employees of the entity, reporting entity or any other entity related to the reporting entity. In the event the reporting entity is itself in possession of such a plan, the sponsoring employers are likewise related to the reporting entity.
(vi) If the entity is controlled by any individual identified under article (a) or under joint control.
(vii) If any individual identified under item (i) of article (a) is in possession of a substantial influence on the entity or is a member of the key management personnel of the subject matter entity (or of the major shareholder of any such entity).

Consists of the transfer of sources, services or obligations between the related party and any party related to the reporting entity of the transaction performed, regardless of whether the same is in consideration for a charge or otherwise.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Revenue

The Group generates its revenues from international and domestic flight operations. Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes. These revenues are recognized as follows:

- Scheduled and charter flight revenues are recorded as revenue when the transportation service is provided. Tickets sold but not yet used are recorded as passenger flight liabilities.
- Ancillary revenues, cargo services and training services are recognized when services are provided.
- Service fees, which is the fee added to ticket price for providing the sale service is recognized when tickets are issued as they are non-refundable.

The Group also receives interest income, which is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable.

Pegasus Card and Pegasus Plus Loyalty Program

Pegasus Card

The Company started the Pegasus branded credit card ("Pegasus Card") program in cooperation with a bank in 2008. The holders of Pegasus Card earn and accumulate flight points for both ticket and non-ticket purchases each time they use the Pegasus Card.

If the points are earned by ticket purchases, the flight points are provided by Pegasus and recognized as a separately identifiable component of the sales transaction and measured at fair value. They are recorded as "flight liability from flight points" initially and recognized as revenue when the flight points are used. The nominal amount of the points earned approximates the fair value of the points, because 1 Flight Point = TL 1. Flight points can be redeemed at the purchase of flight tickets at minimum TL 5.

If the points are earned through non-ticket purchases, the bank funds the cost of the points through a payment to the Group. The Group defers this revenue, which it records as "flight liability from flight points" and recognizes the revenue when the points are used by the customer. Award points are valid for at least two years and expire at the last day of the second calendar year. Unused points are recognized as income based on historic usage.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Pegasus Card and Pegasus Plus Loyalty Program (cont'd)

Pegasus Plus Loyalty Program

The Group launched a new loyalty program in 2011, Pegasus Plus, which is integrated with the Pegasus Card. For each purchase of a ticket on a Pegasus flight and additional services such as excess luggage, pre-ordered meal or seat selection, customers receive 2% of the purchase price of the ticket and any additional services as flight points. The nominal amount of the points earned approximates the fair value of the points, because 1 Flight Point = TL 1. Flight points can be redeemed at the purchase of flight tickets at minimum TL 5. Flight points granted are recorded as "flight liability from flight points" initially and recognized in the statement of profit or loss when used. Award points are valid for at least two years and expire at the last day of the second calendar year. Unused points are recognized as income based on historic usage.

Inventories

Inventories are composed of consumables, spare parts, catering stocks and other stocks and they are valued at the lower of cost or net realizable value.

Tangible Assets

Tangible assets are carried at historical costs less accumulated depreciation and any accumulated impairment losses.

Depreciation is recognised over their estimated useful lives, less their residual values using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

The Group allocates the cost of an acquired aircraft to its service potential reflecting the maintenance condition of its engines and airframe. This cost, which can equate to a substantial element of the total aircraft cost, is depreciated over the shorter of the period to the next maintenance check or the remaining life of the aircraft. The costs of subsequent major airframe and engine maintenance checks are capitalised and depreciated over the shorter of the period to the next check or the remaining life of the aircraft.

All significant components and repairable spare parts are accounted separately and depreciated over their estimated useful lives.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of tangible assets is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Intangible Assets

Intangible assets with finite useful lives that are acquired separately are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is recognized on a straight-line basis over their estimated useful lives. The estimated useful life and amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

Acquired trademark, brands and licenses are shown at historical cost. Trademarks, brands and licenses have a finite useful life and are carried at cost less accumulated amortization. Amortization is calculated using the straight-line method to allocate the cost of trademarks and licenses over their estimated useful lives. The estimated useful life of the İzair brand is 20 years. The acquired software has a 5 year useful life.

Provisions, Contingent Assets and Contingent Liabilities

Provisions are recognized when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Impairment of Non-financial Assets

At the end of each reporting period, the Group reviews the carrying amounts of its aircraft to determine whether there is any indication that those assets have suffered an impairment loss. If such an indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). At the end of each reporting period, non-financial assets are reviewed for possible reversal of the impairment.

The fleet has been determined as the lowest level cash generating unit and analysed for impairment accordingly. For determination of recoverable amounts the higher value between value in use and sale expenses deducted net selling prices in US Dollars is used. Net selling price for the aircraft is determined according to second hand prices in international price guides.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Borrowing Costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization. There are no qualifying assets during the years ended 31 December 2016, and 2015. Therefore, no borrowing costs were capitalized during the years ended 31 December 2016, and 2015. All other borrowing costs are recognized in the statement of profit or loss in the period in which they are incurred.

Maintenance and Repair Costs and Maintenance Reserve Contribution Receivables

The accounting for the cost of providing major airframe and certain engine maintenance checks for owned and financial leased aircraft is described in the accounting policy for tangible assets.

For aircraft held under operating lease agreements, the Group pays monthly supplemental amount called "Maintenance Reserve Contribution" to operating lease companies with respect to heavy maintenance expenditures. This reserve contribution is calculated based on the actual flight hours or the actual number of landings of the aircraft. These maintenance reserve payments are recognised as maintenance expense in the statement of profit or loss on a monthly basis during the lease term. However, when the Group incurs such heavy maintenance expenditures on behalf of the operating lease company, it claims these costs back and recognise an agreed maintenance reserve contribution receivable until it is collected. All other maintenance and repair costs are expensed as incurred.

Redelivery Provision

For aircraft held under operating lease agreements, the Group is contractually committed to either return the aircraft in a certain condition or to compensate the lessor to the level of return condition of the aircraft based on the actual condition of the airframe, engines and life-limited parts upon return. A provision is made over the lease term for this contractual obligation, based on the present value of the estimated future cost complying with the contractual commitment described above, by reference to the number of hours flown or cycles operated during the year.

The Group has entered into operating lease agreements with operating lease companies where the Group has transferred its right to buy the new aircraft and it is liable to perform the heavy maintenance expenditures after the end of the lease term (8 years). The total maintenance reserve has been calculated based on the present value of the estimated future cost by Group management in line with the accounting policies used in the aircraft held under operating lease agreements and they are recognised as maintenance expense in the statement of profit or loss on a monthly basis during the lease term.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Taxation and Deferred Income Taxes

Turkish Tax Legislation does not permit a parent company and its subsidiary to file a consolidated tax return. Therefore, provisions for taxes, as reflected in the accompanying consolidated financial statements, have been calculated on a separate-entity basis.

Income tax expense represents the sum of the tax currently payable and deferred tax.

Current Tax

The current tax payable is based on taxable profit for the year. Taxable profit differs from profit before tax as reported in the statement of profit or loss because of items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred Tax

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases which are used in the computation of taxable profit. Deferred tax assets are recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such assets and liabilities are not recognized if the difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Taxation and Deferred Income Taxes (cont'd)

Current and Deferred Tax for the Period

Taxes are recognised as an expense or income in profit or loss, except when they related to transactions that are recognised in equity. Otherwise, taxes are also recognized in equity with other related transactions.

Government Grants

Government grants are not recognized until there is reasonable assurance that the Group will comply with the conditions attaching to them and that the grants will be received. Government grants are recognized in profit or loss on a systematic basis over the periods in which the Group recognizes as expenses the related costs for which the grants are intended to compensate. As a financing instrument, governmet grants, rather than to be recognized in profit or loss to offset the expenses they are financing, are to be recognized in the balance sheet as deferred income and be recognized in profit or loss on a systematic basis over the economical life of the related assets. Government grants that are receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the Group with no future related costs are recognized in profit or loss in the period in which they become receivable. The benefit of a government loan at a below-market rate of interest is treated as a government grant, measured as the difference between proceeds received and the fair value of the loan based on prevailing market interest rates.

Investment Incentives

The Turkish Government has an Investment Incentive Program which became effective upon the issuance of the Council of Ministers‟ resolution "Government Assistance for Investments" No:2009/15199 ("Incentive Program") on 14 July 2009.

The Incentive Program aims to provide support to companies which make investments by providing a credit against taxable income related to those investments. The amount of credit is determined based on a "contribution rate" in the Incentive Program. An entity must obtain an investment certificate related to the associated incentives.

The Group obtained incentive certificates from the Undersecretariat of Treasury for 21 aircraft. According to the incentive certificate the Group will use 15% of the purchase value of the aircraft as the contribution rate which is the maximum amount that could be deducted against taxable income that is attributable to the operation of these aircraft. The deduction will be performed by the application of 50% of the effective tax rate for the (i.e. use of 10% instead of 20%) taxable income attributable to the operation of these aircraft. As the Group does not have taxable profits during the year ended 31 December 2016 it has not recognized any benefit in the financial statements associated with the Incentive Program (Note 13).

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Employee Benefits

Termination Benefits

Under Turkish law and union agreements, lump sum payments are made to employees retiring or involuntarily leaving the Group. Such payments are considered as being part of defined retirement benefit plan as per Turkish Accounting Standard No. 19 (revised) "Employee Benefits" ("TAS 19").

The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation. The calculated actuarial gains and losses are accounted under the other comprehensive income when material.

Employee Bonus Plan

The Group recognizes a liability and an expense for employee bonus, based on current year performance. The Group recognizes a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

Executive Bonus Plan

The Group recognizes a liability and an expense for executive bonus plan, based on a formula that takes into consideration the budget compared to actual performance. The Group recognizes a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

Foreign Currency Transactions

The individual financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency).

Based on the nature of the Group's business, there are various transactions entered into that are in currencies other than the functional currency. In preparing the financial statements of the individual entities, transactions in currencies other than the functional currency (foreign currencies) are recorded at the rates of exchange prevailing on the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Exchange differences are recognized either as finance income or finance costs in the period in which they arise.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Leasing - the Company as Lessee

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are recognized as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance expenses are recognised immediately in profit or loss.

Rentals payable under operating leases are charged to statement of profit or loss on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are also charged to statement of profit or loss on a straight-line basis over the lease term.

Financial Assets

All financial assets are recognised and derecognised on a trade date where the purchase or sale of a financial asset under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified into the following specified categories: financial assets as 'at fair value through profit or loss' (FVTPL), 'held-to-maturity investments', 'available-for-sale' (AFS) financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective Interest Method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

Income is recognized on an effective interest basis for debt instruments other than those financial assets designated as at FVTPL.

Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are measured at amortized cost using the effective interest method, less any impairment. Interest income is recognized by applying the effective interest rate, except for short-term receivables when the effect of discounting is immaterial.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Financial assets (cont'd)

Impairment of Financial Assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected. For loans and receivables, the amount of the impairment loss recognized is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account. When a trade receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

Cash and Cash Equivalents

Cash and cash equivalents comprise cash on hand and demand deposits and other short-term highly liquid investments which their maturities are three months or less from date of acquisition and that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value. The Group's cash and cash equivalents are classified under the category of "Loans and Receivables".

Financial Liabilities

Debt and equity instruments issued by the Group are classified as either financial liabilities or as equity in accordance with according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. The accounting policies adopted for specific financial liabilities and equity instruments are set out below.

Financial liabilities are classified as either financial liabilities at FVTPL or other financial liabilities.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Financial Liabilities (cont'd)

<u>Other Financial Liabilities</u>

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

The Group derecognizes financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit or loss.

Derivative Financial Instruments and Hedge Accounting

Derivative financial instruments are initially recognized at fair value on the date which a derivative contract is entered into and subsequently remeasured at fair value. Any gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are recognized in the statement of profit or loss. Fair values are obtained from quoted market prices in active markets, including recent market transactions, to the extent publicly available. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The Group is exposed to foreign exchange risk through the impact of currency rate changes on translation into the Euro of its foreign currency denominated assets and liabilities and non-Euro denominated currency transactions. To monitor the risk, the Group enters into forward transactions where the Group is liable to pay a certain amount of Euro and receive a certain amount of foreign currency (mainly US Dollars) at a specified date. Similarly, the Group enters into chooser forward option transactions to purchase US Dollars or brent oil on specified periods in order to monitor both foreign exchange and fuel price risk. The change in the fair value of the derivative financial assets that qualify for hedge accounting according to TAS 39 (Financial Instruments) are recognized in other comprehensive income and the change in the fair value of the derivative financial assets that do not qualify for hedge accounting according to TAS 39 are recognized in statement of profit or loss.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Derivative Financial Instruments and Hedge Accounting (cont'd)

Inherently, the Group is exposed to financial risks related to interest rate fluctuations. The most significant source of the interest rate risk is the financial lease liabilities. The policy of the Group is to transform a part of its floating rate financial liabilities into fixed rate financial liabilities by using derivative financial instruments. Derivative financial instruments procured for this purpose do not qualify for hedge accounting and the change in the fair value of these derivative financial assets are recognized immediately in profit or loss.

Fuel costs which are predominantly determined in US Dollars constitute a substantial portion of the Group's cost base. The Group enters into forward and option forward transactions with financial institutions based on acquisition of jet fuel or Brent oil on specified prices. These commodity forward transactions qualify for hedge accounting and they are accounted as cash flow hedges under equity as at 31 December 2016 and 2015.

Brent within framework of hedge transactions against cash flow risk is a substitute product of Jet Fuel, whereas the correlation between the two commodities is set forth in terms of past statistics. The correlation rate of 96% between Brent and Jet Fuel between years 2010-2016 is used at the same time as the effectiveness rate. The effectiveness rate of forward contracts that the Group entered into in respect of the Jet Fuel used as its direct physical requirement is considered as 100%. The excessive amount over the effective rate is accounted in profit or loss in the related period when the amount has material effect in the financial statements.

At the inception of the hedge relationship, the Group documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an on-going basis, the Group documents whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows of the hedged item attributable to the hedged risk.

Amounts previously recognized in other comprehensive income are reclassified to profit or loss in the periods when the hedged item is recognized in profit or loss, in the same line of the statement of comprehensive income as the recognized hedged item.

Hedge accounting is discontinued when the Group revokes the hedging relationship, when the hedging instrument expires or is sold, terminated, or exercised, or when it no longer qualifies for hedge accounting. Any gain or loss recognized in other comprehensive income and accumulated in equity at that time remains in equity and is recognized when the forecast transaction is ultimately recognized in profit or loss. When a forecast transaction is no longer expected to occur, the gain or loss accumulated in equity is recognized immediately in profit or loss.

The fair value of financial instruments that are not traded in an active market is determined using valuation techniques such as using the basis of recent market transactions on arm's length terms, using the fair value of similar financial instruments and using discounted cash flow analysis (Note 33).

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Business Combinations

The acquisition of subsidiaries and businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Group, liabilities incurred by the Group to the former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. Acquisition-related costs are generally recognized in profit or loss as incurred.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognized at their fair value, except that:

- deferred tax assets or liabilities and assets or liabilities related to employee benefit arrangements are recognized and measured in accordance with TAS 12 *Income Taxes* and TAS 19 *Employee Benefits* respectively;

- liabilities or equity instruments related to share-based payment arrangements of the acquiree or share-based payment arrangements of the Group entered into to replace share-based payment arrangements of the acquiree are measured in accordance with TFRS 2 *Share-based Payment* at the acquisition date; and

- assets (or disposal groups) that are classified as held for sale in accordance with TFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* are measured in accordance with that Standard.

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after reassessment, the net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held interest in the acquiree (if any), the excess is recognized immediately in profit or loss as a bargain purchase gain.

Non-controlling interests that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation may be initially measured either at fair value or at the non-controlling interests' proportionate share of the recognized amounts of the acquiree's identifiable net assets. The choice of measurement basis is made on a transaction-by-transaction basis. Other types of non-controlling interests are measured at fair value or, when applicable, on the basis specified in another TAS.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Business Combinations (cont'd)

When the consideration transferred by the Group in a business combination includes assets or liabilities resulting from a contingent consideration arrangement, the contingent consideration is measured at its acquisition-date fair value and included as part of the consideration transferred in a business combination. Changes in the fair value of the contingent consideration that qualify as measurement period adjustments are adjusted retrospectively, with corresponding adjustments against goodwill. Measurement period adjustments are adjustments that arise from additional information obtained during the 'measurement period' (which cannot exceed one year from the acquisition date) about facts and circumstances that existed at the acquisition date.

The subsequent accounting for changes in the fair value of the contingent consideration that do not qualify as measurement period adjustments depends on how the contingent consideration is classified. Contingent consideration that is classified as equity is not remeasured at subsequent reporting dates and its subsequent settlement is accounted for within equity. Contingent consideration that is classified as an asset or a liability is remeasured at subsequent reporting dates in accordance with TAS 39, or TAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, as appropriate, with the corresponding gain or loss being recognized in profit or loss.

When a business combination is achieved in stages, the Group's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date (i.e. the date when the Group obtains control) and the resulting gain or loss, if any, is recognized in profit or loss. Amounts arising from interests in the acquiree prior to the acquisition date that have previously been recognized in other comprehensive income are reclassified to profit or loss where such treatment would be appropriate if that interest were disposed of.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period (see above), or additional assets or liabilities are recognized, to reflect new information obtained about facts and circumstances that existed at the acquisition date that, if known, would have affected the amounts recognized at that date.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Goodwill

Goodwill arising on an acquisition of a business is carried at cost as established at the date of acquisition of the business less accumulated impairment losses, if any.

For the purposes of impairment testing, goodwill is allocated to each of the Group's cash-generating units (or groups of cash-generating units) that is expected to benefit from the synergies of the combination.

A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro rata based on the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognized directly in the consolidated profit or loss. An impairment loss recognized for goodwill is not reversed in subsequent periods.

On disposal of the relevant cash-generating unit, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Events After the Reporting Date

Events after the reporting period comprise any events between the balance sheet date and the date of authorization of the financial statements, even if the event after balance sheet date occurred subsequent to an announcement on the Group's profit or following any financial information that are released.

In the case of events requiring adjustments, the Group adjusts the amounts recognized in its financial statements to reflect the events. For non-adjusting events, disclosure is made in the notes to the financial statements.

Contingent Liabilities and Contingent Assets

Contingent liabilities are assessed continuously to determine the probability of outflow of the economically beneficial assets. For contingent liabilities, when an outflow of resources embodying economic benefits are probable, provision is recognized for this contingent liability in the period when the probability has changed, except for the cases where a reliable estimate cannot be made.

When the Group's contingent liabilities are probable but the amount of resources containing the economic benefits cannot be measured reliably, then the Group discloses this fact in the notes to the financial statements.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.5 Summary of Significant Accounting Policies (cont'd)

Earnings per Share

Earnings per share is calculated by dividing net profit by weighted average number of shares outstanding in the relevant period. In Turkey, companies are allowed to increase their capital by distributing free shares to shareholders from accumulated profits. In calculation of earnings per share, such free shares are considered as issued shares. Therefore, weighted average number of shares in the calculation of earnings per share is found by applying distribution of free shares retrospectively.

Cash Flow Statement

Cash flows for the period are classified and presented as operating, investing and financing activities in the cash flow statement.

Cash flows from operating activities present cash generated from the Group's airline operations.

Cash flows from investing activities present cash used in, generated from investing activities (capital investments and financial investments) of the Group.

Cash flows from financing activities present the funds used in financing operations and repayment regarding these operations.

Cash and cash equivalents are short term investments that are cash on hand, demand deposits, time deposits of with maturities not exceeding three months from purchase date and free of detoration of value with high liquidity.

Capital and Dividends

Common shares are classified as equity. Dividends distributed over common shares are accounted by deduction from retained earnings in the period decision for dividend payment is undertaken.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.6 Critical Accounting Estimates and Assumptions

Preparation of the financial statements requires the amounts of assets and liabilities being reported, explanations of contingent liabilities and assets and the uses of accounting estimates and assumptions which would affect revenue and expense accounts reported during the accounting period. The Group makes estimates and assumptions about the future periods. Actual results could differ from those estimations. Accounting estimates and assumptions which might cause material adjustments on the book values of assets and liabilities in future financial reporting period are given below:

Useful Lives and Residual Values of Tangible Assets and Aircraft

The Group has allocated depreciation over tangible assets by taking into consideration the useful lives and residual values which were explained in Note 10. While determining estimated useful lives and residual values, the Group makes estimations and assumptions by taking past experience and business plans into consideration.

Income Taxes

The Group recognizes deferred tax assets and liabilities using substantially enacted tax rates for the effect of temporary differences between book and tax bases of assets and liabilities. Currently, there are deferred tax assets resulting from operating loss carry-forwards and deductible temporary differences, all of which could reduce taxable income in the future. Based on available evidence, both positive and negative, it is determined whether it is probable that all or a portion of the deferred tax assets will be realized. The main factors which are considered include future earnings potential; cumulative losses in recent years; history of loss carry-forwards and other tax assets expiring; the carry-forward period associated with the deferred tax assets; future reversals of existing taxable temporary differences; tax-planning strategies that would, if necessary, be implemented, and the nature of the income that can be used to realize the deferred tax asset. Based on the available evidence, it is the Group's belief that sufficient taxable profit will be available to utilize these deferred tax assets as at 31 December 2016.

Redelivery Provision

For aircraft held under operating lease agreements, the Group is contractually committed to either return the aircraft in a certain condition or to compensate the lessor to the level of return condition of the aircraft based on the actual condition of the airframe, engines and life-limited parts upon return. A provision is made over the lease term for this contractual obligation, based on the present value of the estimated future cost complying with the contractual commitment described above, by reference to the number of hours flown or cycles operated during the year. The provision also incorporates management expectation on the cost of the maintenance and component compensation at the time of the redelivery.

NOTE 2 - BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

2.6 Critical Accounting Estimates and Assumptions (cont'd)

Litigation Provision

The Group, within its normal course of business, is party to various lawsuits, fines and claims that have been filed against it. These lawsuits and fines have been evaluated by the Group's management and provisions are provided where necessary. The Group has provided a provision at an amount of TL 6.373.258 as of 31 December 2016 (31 December 2015: TL 2.333.183) (Note 15).

Tax Audit

It has been filed an application with the purpose of making avail of and benefitting from relevant provisions of Law Number 6736 regarding Restructuring Of Certain Receivables in respect of ongoing disputes concerning value added tax in the amount of TL 30.872.430 as well as tax loss penalties in the amount of TL 46.308.645 accrued as a result of the appraisal by the Inspection Personnel of the Ministry of Finance such accounts and transactions of the Company pertaining to years 2009, 2010, 2011 and January 2012, in respect of Value Added Tax, and in this context, subject matter disputes are concluded and finalized by means of payment of the total liabilities in the approximate amount of TL 9.3 million including local ÜFE (Manufacturers Price Index) under installments of 18 months (Note 15).

Company's accounts as well as operations pertaining to year 2010 are inspected and examined in terms of Taxation Laws; and Corporation Tax Inspection Report number 2013-B-228/3, Corporation Tax Withholding Inspection Report number 2013-B-228/5, and Value Added Tax Withholding Tax Inspection Report number 2013-B-228/6 are hereby presented.

It is believed that as a result of the said action filed, the principal taxes anticipated to be accrued, including any fines charged thereon, are to be released. Therefore, in parallel to the opinions of the Company's legal advisors as well as taxation specialists, no provision has been provided on the accompanied consolidated financial statements, including the period not inspected (Note 15).

Fair Value of Derivatives and Other Financial Instruments

The fair value of derivative financial instruments which are not traded in an active market is determined using valuation techniques based on market rates and expected yields. Fair value of non-derivative financial instruments is determined based on the present value of future principal and interest cash flows. These cash flows are calculated based on the discount rate prevailing at the reporting date.

NOTE 3 - INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

The details of investments accounted for using the equity method are as follows:

	31 December 2016	31 December 2015
Joint ventures		
Hitit Bilgisayar	19.395.216	17.332.163
PUEM	4.574.251	3.413.797
	23.969.467	**20.745.960**

Total profit from investments accounted for using the equity method is as follows:

	1 January- 31 December 2016	1 January- 31 December 2015
Hitit Bilgisayar	2.050.650	1.999.162
PUEM	529.538	611.034
Net profit	**2.580.188**	**2.610.196**

The summarized financial information of the investment accounted by using the equity method is as follows:

Pegasus Uçuş Eğitim Merkezi A.Ş.

	31 December 2016	31 December 2015
Current assets	1.055.078	1.405.528
Non-current assets	18.209.286	16.496.379
Current liabilities	(7.741.613)	(6.285.656)
Non-current liabilities	(2.263.134)	(4.705.731)
Net assets of joint venture	**9.259.617**	**6.910.520**
Group's ownership interest in the joint venture	49,40%	49,40%
Group's share in the net assets of the joint venture	**4.574.251**	**3.413.797**

	1 January- 31 December 2016	1 January- 31 December 2015
Revenue	6.129.688	5.958.749
Profit for the year	1.071.939	1.236.911
Group's ownership interest	49,40%	49,40%
Group's share in the net assets of the joint venture	**529.538**	**611.034**

NOTE 3 - INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD (cont'd)

Hitit Bilgisayar Hizmetleri A.Ş.

	31 December 2016	31 December 2015
Current assets	16.549.837	13.861.790
Non-current assets	25.960.551	32.891.666
Current liabilities	(5.390.180)	(5.496.308)
Non-current liabilities	(114.800)	(158.021)
Net assets of joint venture	**37.005.408**	**41.099.127**
Group's ownership interest in the joint venture	50%	40%
Goodwill	892.512	892.512
Group's share in the net assets of the joint venture	**19.395.216**	**17.332.163**

	1 January- 31 December 2016	1 April- 31 December 2015
Revenue	36.541.437	25.351.139
Profit for the year	6.479.044	4.997.904
Group's weighted average ownership interest (*)	45,9%	40%
Group's share in the net assets of the joint venture	**2.050.650**	**1.999.162**

(*) The Group used its call option that is acquired during the share purchase agreement for additional Group (B) registered shares representing a further 10% of the share of Hitit Bilgisayar for a total consideration of US Dollar 1.500.000, by making the equivalent payment of TL 4.409.850 in 30 May 2016 and consequently as of 31 December 2016, participation rate has increased to 50% and weighted average participation rate has increased to 45,9% as well.

NOTE 4 - SEGMENT REPORTING

The Group is managed as a single business unit that provides low fares airline-related services, including scheduled services, charter services, ancillary services and other services. The Group's Chief Operating Decision Maker is the Board of Directors. The resource allocation decisions are based on the entire network and the deployment of the entire aircraft fleet. The objective in making resource allocation decisions is to maximise consolidated financial results, rather than results on individual routes within the network. All other assets and liabilities have been allocated to the Group's single reportable segment.

NOTE 5 - RELATED PARTY TRANSACTIONS

The immediate parent and controlling party of the Group is Esas Holding. The Group has a number of operating and financial relationships with its shareholders and other entities owned by its shareholders. There are no set payment terms for any of the related party transactions. The related party receivables and payables resulting from operating activities are generally settled in normal course of business.

(i) Balances with Related Parties:

a) Other receivables from related parties

	31 December 2016	31 December 2015
Balances with joint ventures and subsidiaries:		
PUEM	999.811	-
Balances with other related parties:		
Air Berlin Plc&Co Luftverkehrs Kg	86.218	278.844
Doğan Burda Dergi Yayıncılık ve Pazarlama A.Ş. ("Doğan Burda")	11.778	-
	1.097.807	**278.844**

b) Trade payables to related parties

	31 December 2016	31 December 2015
Balances with parent company:		
Esas Holding	-	190.421
Balances with joint ventures and subsidiaries:		
Hitit Bilgisayar	1.277.402	595.265
PUEM	-	179.953
Balances with other related parties:		
Esasburda İnşaat Sanayi ve Ticaret A.Ş.	177.988	47.561
	1.455.390	**1.013.200**

NOTE 5 - RELATED PARTY TRANSACTIONS (cont'd)

(ii) Significant Transactions with Related Parties:

The significant transactions with Esas Holding consist of the financial guarantee that Esas provides for aircraft acquisitions and their related commissions. The Group records these commissions within finance expense.

The Group also leases their head office building from Esasburda İnşaat Sanayi ve Ticaret A.Ş. ("Esasburda"), another Esas Holding subsidiary, and records rent expense.

The Group receives services from Doğan Burda for magazine advertising and printing expenditures.

The Group receives simulator training services from PUEM for their pilots and generates revenues from labor hire and common area use.

The Group receives software and software support services from Hitit Bilgisayar that provides informations system solutions for transportation industry.

The Group, generates flight revenue from the ticket sales of Air Berlin Plc & Co Luftverkehrs Kg pursuant to the agreement between the parties.

a) Sale of services

	1 January- 31 December 2016	1 January- 31 December 2015
Balances with joint ventures and subsidiaries:		
PUEM	1.114.259	587.736
Balances with other related parties:		
Air Berlin Plc&Co Luftverkehrs Kg	5.761.303	13.405.547
Doğan Burda	-	620.799
	6.875.562	**14.614.082**

b) Purchases of goods or services

	1 January- 31 December 2016	1 January- 31 December 2015
Balances with joint ventures and subsidiaries:		
Hitit Bilgisayar	10.607.057	6.631.151
PUEM	6.129.688	5.958.749
Balances with other related parties:		
Callpex Çağrı Merkezi ve Müşteri Hizmetleri A.Ş.(*)	-	8.003.409
Esasburda	1.564.599	1.078.178
Doğan Burda	54.302	-
Other	21.260	22.897
	18.376.906	**21.694.384**

(*) Due to disposal of shares of the Company's Chairman of the Board, call center service provider Callpex Çağrı Merkezi ve Müşteri Hizmetleri A.Ş. was delisted from related parties list as of 31 December 2015.

NOTE 5 - RELATED PARTY TRANSACTIONS (cont'd)

(ii) Significant Transactions with Related Parties (cont'd):

c) Rent expenses

	1 January- 31 December 2016	1 January- 31 December 2015
Esasburda	5.168.853	4.389.809
	5.168.853	**4.389.809**

d) Surety commission expenses

	1 January- 31 December 2016	1 January- 31 December 2015
Esas Holding (Note 25)	11.955.096	12.214.137
	11.955.096	**12.214.137**

Commission expenses represent commissions and fees for Esas Holding's guarantee which is provided for financial leases of aircraft. The fee rate is 0,575% of the 115% of the amount guaranteed.

(iii) Compensation of Key Management Personnel:

Key management personnel include members of the board of directors, general managers and assistant general managers. The remuneration of key management paid during the period ended 31 December 2016 and 2015 are as follows:

	1 January- 31 December 2016	1 January- 31 December 2015
Salaries and other short term benefits	13.359.086	7.042.397
Other long term benefits	3.811.325	1.496.387
	17.170.411	**8.538.784**

NOTE 6 - TRADE RECEIVABLES AND PAYABLES

Short term trade receivables

The details of short term trade receivables as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Trade receivables	89.631.639	66.728.316
Credit card receivables	129.356.458	220.177.025
Income accruals	2.279.549	10.899.930
	221.267.646	**297.805.271**
Less: Allowance for doubtful receivables	(8.998.147)	(3.175.648)
	212.269.499	**294.629.623**

The average collection period of trade receivables is approximately 25 days (31 December 2015: 28 days).

The movement of provision for doubtful receivables for the years ended 31 December 2016 and 2015 are as follows:

	2016	2015
1 January	3.175.648	1.861.737
Charge for the year	6.208.984	1.054.427
Collections and written off allowances	(1.286.392)	(140.476)
Currency translation differences	899.907	399.960
31 December	**8.998.147**	**3.175.648**

The nature and level of risks related to trade receivables is disclosed in Note 32.

Short term trade payables

The details of short term trade payables as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Trade payables	235.037.980	173.295.633
Accrued direct operational costs	65.407.597	60.336.067
Other accrued expenses	15.976.776	11.254.193
Due to related parties (Note 5)	1.455.390	1.013.200
	317.877.743	**245.899.093**

The average credit period of trade payables is approximately 29 days (31 December 2015: 28 days).

NOTE 7 - OTHER RECEIVABLES AND PAYABLES

Short Term Other Receivables

	31 December 2016	31 December 2015
Deposits and guarantees given (*)	16.183.637	153.497.035
Incentive receivables from suppliers	14.397.411	21.213.166
Maintenance reserve contribution receivables	80.502.738	17.385.918
Due from related parties (Note 5)	1.097.807	278.844
Other receivables	8.286.049	3.124.524
Less: Allowance for doubtful receivables	(1.706.812)	(5.984.300)
	118.760.830	**189.515.187**

(*) The amount of TL 134.606.706 in deposits and gurantees given, consists of guarantee deposits given to banks related to valuation of derivative contracts as of 31 December 2015 (31 December 2016: None).

The movement of provision for doubtful other receivables for the years ended 31 December 2016 and 2015 are as follows:

	2016	2015
1 January	5.984.300	4.772.662
Collections	(2.654.387)	-
Written off allowances	(2.036.815)	-
Currency translation differences	413.714	1.211.638
31 December	**1.706.812**	**5.984.300**

Long Term Other Receivables

	31 December 2016	31 December 2015
Deposits given	21.031.698	17.067.064
Incentive receivables from suppliers	-	12.207.736
	21.031.698	**29.274.800**

Short Term Other Payables

	31 December 2016	31 December 2015
Taxes payables	25.452.496	9.549.919
Deposits received	6.767.980	2.494.031
	32.220.476	**12.043.950**

NOTE 8 - INVENTORIES

The details of inventories as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Consumables and spare parts	17.855.336	8.747.394
Operational and other inventories	6.268.255	4.353.730
Catering inventories	238.131	263.584
	24.361.722	**13.364.708**

NOTE 9 - PREPAID EXPENSES AND DEFERRED INCOME

The details of prepaid expenses as of 31 December 2016 and 2015 are as follows:

Short term prepaid expenses

	31 December 2016	31 December 2015
Advances on aircraft purchases	180.317.329	206.989.481
Advances to suppliers	156.973.574	93.557.209
Prepaid aircraft operating lease expenses	42.065.722	29.726.231
Prepaid insurance expenses	14.297.869	11.984.253
Prepaid advertising expenses	588.452	1.819.674
Other prepaid expenses	5.751.761	3.587.931
	399.994.707	**347.664.779**

Long term prepaid expenses

	31 December 2016	31 December 2015
Advances on aircraft purchases	224.414.166	62.324.466
Other prepaid expenses	12.949.725	15.502.908
	237.363.891	**77.827.374**

NOTE 9 - PREPAID EXPENSES AND DEFERRED INCOME (cont'd)

The details of deferred income as of 31 December 2016 and 2015 are as follows:

Short term deferred income

	31 December 2016	31 December 2015
Passenger flight liabilities	262.726.328	272.748.385
Advances received from customers	11.190.304	8.727.433
Deferred income from sale of subsidiary (*)	18.743.784	16.054.408
Other deferred income	9.718.497	3.156.682
	302.378.913	**300.686.908**

(*) The deferred income from sale of subsidiary, was not recognized in the statement of profit or loss as of 31 December 2016 due to on-going negotiations and process over the sale with Air Berlin.

The details of passenger flight liabilities as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Flight liability from ticket sales	177.504.919	187.347.110
Passenger airport fees received from customers	60.671.024	61.623.605
Flight liability from flight points	24.550.385	23.777.670
	262.726.328	**272.748.385**

Long term deferred income

	31 December 2016	31 December 2015
Income relating to future periods	6.660.918	9.831.545
	6.660.918	**9.831.545**

NOTE 10 - PROPERTY AND EQUIPMENT

31 December 2016	Machinery and equipment	Motor vehicles	Furniture and fixtures	Leasehold improvements	Components, spare engine and repairables	Owned and leased aircraft	Construction in process	Total
Cost:								
Opening	**9.746.987**	**11.637.132**	**54.184.095**	**37.279.765**	**112.911.844**	**2.706.657.545**	**55.291.499**	**2.987.708.867**
Additions	4.565.319	1.407.619	8.164.807	491.077	177.273.191	1.218.683.019	24.175.257	1.434.760.289
Disposals	-	(3.176.750)	(463.213)	(19.322)	(2.630.085)	-	-	(6.289.370)
Transfers	37.133.624	38.357.850	1.731.124	3.438.324	-	-	(80.660.922)	-
Currency translation differences	7.000.688	6.721.374	10.162.038	6.746.286	38.378.240	585.412.465	1.609.275	656.030.366
Closing	**58.446.618**	**54.947.225**	**73.778.851**	**47.936.130**	**325.933.190**	**4.510.753.029**	**415.109**	**5.072.210.152**
Accumulated depreciation:								
Opening	**(2.585.198)**	**(4.687.833)**	**(29.952.719)**	**(18.985.851)**	**(33.930.943)**	**(784.258.158)**	**-**	**(874.400.702)**
Depreciation for the year	(1.828.591)	(2.825.796)	(7.020.994)	(6.034.538)	(20.239.082)	(182.751.481)	-	(220.700.482)
Disposals	-	1.939.528	172.970	9.506	261.050	-	-	2.383.054
Currency translation differences	(650.551)	(889.145)	(5.784.056)	(3.865.363)	(7.877.931)	(111.809.573)	-	(130.876.619)
Closing	**(5.064.340)**	**(6.463.246)**	**(42.584.799)**	**(28.876.246)**	**(61.786.906)**	**(1.078.819.212)**	**-**	**(1.223.594.749)**
Net book value	**53.382.278**	**48.483.979**	**31.194.052**	**19.059.884**	**264.146.284**	**3.431.933.817**	**415.109**	**3.848.615.403**

NOTE 10 - PROPERTY AND EQUIPMENT (cont'd)

31 December 2015	Machinery and equipment	Motor vehicles	Furniture and fixtures	Leasehold improvements	Components, spare engine and repairables	Owned and leased aircraft	Construction in process	Total
Cost:								
Opening	**7.016.010**	**7.310.207**	**40.779.927**	**28.184.960**	**67.289.792**	**2.392.480.349**	**1.529.477**	**2.544.590.722**
Additions	4.315.880	4.307.344	8.019.777	1.169.276	39.425.695	-	57.583.835	114.821.807
Disposals	(2.618.605)	(1.111.626)	(262.973)	-	(4.212.668)	-	-	(8.205.872)
Transfers	-	-	57.085	4.063.967	-	-	(4.121.052)	-
Currency translation differences	1.033.702	1.131.207	5.590.279	3.861.562	10.409.025	314.177.196	299.239	336.502.210
Closing	**9.746.987**	**11.637.132**	**54.184.095**	**37.279.765**	**112.911.844**	**2.706.657.545**	**55.291.499**	**2.987.708.867**
Accumulated depreciation:								
Opening	**(1.900.821)**	**(3.757.948)**	**(21.909.947)**	**(12.388.565)**	**(22.916.369)**	**(550.204.426)**	**-**	**(613.078.076)**
Depreciation for the year	(619.997)	(1.302.371)	(5.214.568)	(4.770.994)	(7.845.030)	(151.974.883)	-	(171.727.843)
Disposals	84.592	813.385	209.283	-	115.126	-	-	1.222.386
Currency translation differences	(148.972)	(440.899)	(3.037.487)	(1.826.292)	(3.284.670)	(82.078.849)	-	(90.817.169)
Closing	**(2.585.198)**	**(4.687.833)**	**(29.952.719)**	**(18.985.851)**	**(33.930.943)**	**(784.258.158)**	**-**	**(874.400.702)**
Net book value	**7.161.789**	**6.949.299**	**24.231.376**	**18.293.914**	**78.980.901**	**1.922.399.387**	**55.291.499**	**2.113.308.165**

NOTE 10 - PROPERTY AND EQUIPMENT (cont'd)

The useful lives of the depreciable assets are as follows:

	Useful life	
Aircraft	23 years	
Engine and Engine LLP's	8 years	
Airframe and maintenance	7-8 years	
Repairables and components	3-7 years	
Machinery and equipment	7 years	
Furniture and fixtures	7 years	
Motor vehicles	5 years	
Leasehold improvements	5 years	or lease term

The Group has determined the residual value of the aircraft as 15% of market value of a new aircraft in the same model.

Depreciation and amortisation expense charged to cost of sales, general administrative expenses, and marketing expenses is summarized below:

	1 January- 31 December 2016	**1 January- 31 December 2015**
Current year depreciation	220.700.482	171.727.843
Current year amortization (Note 11)	5.819.856	4.234.178
	226.520.338	**175.962.021**

	1 January- 31 December 2016	**1 January- 31 December 2015**
Cost of sales (Note 21)	202.393.619	159.860.939
General administrative expenses (Note 22)	19.502.965	12.993.134
Marketing expenses (Note 22)	4.623.754	3.107.948
	226.520.338	**175.962.021**

The Group leases various property, plant and equipment under non-cancellable finance lease agreements. The net carrying amount of each class of asset is as follows:

Net carrying amounts of leased assets	**31 December 2016**	**31 December 2015**
Aircraft	3.201.594.234	1.814.636.037
Handling equipment	61.184.867	55.192.910
Simulator	23.252.700	-
	3.286.031.801	**1.869.828.947**

NOTE 11 - INTANGIBLE ASSETS

31 December 2016	Brand	Software	Total
Cost:			
Opening	**2.240.209**	**32.251.720**	**34.491.929**
Additions	-	8.938.003	8.938.003
Currency translation differences	145.089	6.274.603	6.419.692
Closing	**2.385.298**	**47.464.326**	**49.849.624**
Accumulated amortization:			
Opening	**(980.090)**	**(18.943.166)**	**(19.923.256)**
Amortization for the year	(96.415)	(5.723.441)	(5.819.856)
Currency translation differences	(66.449)	(3.682.334)	(3.748.783)
Closing	**(1.142.954)**	**(28.348.941)**	**(29.491.895)**
Net book value	**1.242.344**	**19.115.385**	**20.357.729**

31 December 2015	Brand	Software	Total
Cost:			
Opening	**1.988.594**	**23.204.104**	**25.192.698**
Additions	-	5.794.870	5.794.870
Currency translation differences	251.615	3.252.746	3.504.361
Closing	**2.240.209**	**32.251.720**	**34.491.929**
Accumulated amortization:			
Opening	**(770.579)**	**(12.951.075)**	**(13.721.654)**
Amortization for the year	(106.291)	(4.127.887)	(4.234.178)
Currency translation differences	(103.220)	(1.864.204)	(1.967.424)
Closing	**(980.090)**	**(18.943.166)**	**(19.923.256)**
Net book value	**1.260.119**	**13.308.554**	**14.568.673**

Remaining average useful life of intangible assets as of 31 December 2016 is 2,2 years (31 December 2015: 2,7 years).

NOTE 12 - LEASING TRANSACTIONS

Details related to leasing transactions are disclosed in Note 31.

NOTE 13 - GOVERNMENT GRANTS AND INCENTIVES

The Group obtained incentive certificates from the Undersecretariat of Treasury for 21 aircraft. According to the incentive certificate the Company will use 15% of the purchase value of the aircraft as the contribution rate which is the maximum amount that could be deducted against taxable income that is attributable to the operation of these aircraft. The deduction will be performed by the application of 50% of the effective tax rate for the (i.e. use of 10% instead of 20%) taxable income attributable to the operation of these aircraft.

As the Group does not have taxable profits during the year ended 31 December 2016 it has not recognized any benefit in the financial statements associated with the incentive program (31 December 2015: TL 2.691.474).

NOTE 14 - BORROWING COSTS

For the years ended 31 December 2016 and 2015, as there are no qualifying assets that necessarily take a substantial period of time to get ready for their intended use or sale, borrowing costs for the respective periods are not capitalized. All other borrowing costs are recognized in the statement of profit or loss in the period in which they are incurred.

NOTE 15 - PROVISIONS, CONTINGENT ASSETS AND LIABILITIES

Short term provisions

	31 December 2016	**31 December 2015**
Provision for litigation claims	6.373.258	2.333.183
Redelivery provision	4.260.975	-
Provision for penalty and compensation	443.169	642.767
	11.077.402	**2.975.950**

Long term provisions

	31 December 2016	**31 December 2015**
Redelivery provision	422.280.216	222.327.285
	422.280.216	**222.327.285**

<u>Provision for Penalty and Compensation</u>

The movement of provision for penalty and compensation as of the years ended 31 December 2016 and 2015 are as follows:

	2016	**2015**
1 January	642.767	734.335
Charge for the year	(67.454)	(31.700)
Payment during the year	(132.144)	(59.868)
31 December	**443.169**	**642.767**

NOTE 15 - PROVISIONS, CONTINGENT ASSETS AND LIABILITIES (cont'd)

Redelivery Provision

The detail of redelivery provision is as follows:

	31 December 2016	31 December 2015
Short term	4.260.975	-
Long term	422.280.216	222.327.285
	426.541.191	**222.327.285**

The movement of redelivery provision as of the years ended 31 December 2016 and 2015 are as follows:

	2016	2015
1 January	222.327.285	118.912.191
Charge for the year	134.898.154	72.761.711
Disposals	-	(6.045.712)
Currency translation differences	69.315.752	36.699.095
31 December	**426.541.191**	**222.327.285**

Litigation

The movement of litigation provision is as follows:

	2016	2015
1 January	2.333.183	2.087.083
Charge for the year	4.644.328	1.088.332
Payments	(148.259)	(604.402)
Reversal of provision	(455.994)	(237.830)
31 December	**6.373.258**	**2.333.183**

The Group is party to various lawsuits and claims that have been filed against it, the total claims constituted by which, excluding reserved rights for claiming excess amounts, risk of litigation and interest, is TL 11.768.340 as of 31 December 2016 (31 December 2015: TL 7.164.906). These lawsuits and fines have been evaluated by the Group's management and a litigation provision of TL 6.373.258 (31 December 2015: TL 2.333.183) has been provided against claims for which management believes it is probable it will be required to make a payment. These lawsuits consist of guest complaints and claims by the Group's former employees, besides a limited number of commercial claims.

NOTE 15 - PROVISIONS, CONTINGENT ASSETS AND LIABILITIES (cont'd)

Contingent Liabilities

In addition to the above, in June 2008, the İstanbul Atatürk Airport Customs Directorate imposed a monetary fine against the Group in the amount of TL 545.366 on the grounds that the Group had violated temporary import regime regulations. The monetary fine was challenged before the relevant tax court which ruled against the Group in April 2009, in response to which the Group filed an appeal and refused to make payment, citing amendments in the temporary import regime legislation and providing a letter of credit for the amount of the fine and the accrued interest totaling TL 931.212. In January 2011 the Customs Directorate requested the liquidation of the letter of credit in a motion that was challenged by the Group, which resulted, first, in an injunction decision in February 2011, and later, in the cancellation of the liquidation request in September 2011. The Customs Directorate later appealed the cancellation decision of the tax court. As of 31 December 2016 the appellate review of both lawsuits have been finalized in the Group's favor, whereby the court decision turning down the Group's request for the cancellation of the monetary fines has been overturned and the court decision cancelling the liquidation of the letter of credit by the administration has been upheld. The Group management believes that significant cash outflow is not probable and has not provided any provision for this fine.

Tax Audit

It has been filed an application with the purpose of making avail of and benefitting from relevant provisions of Law Number 6736 regarding Restructuring Of Certain Receivables in respect of ongoing disputes concerning value added tax in the amount of TL 30.872.430 as well as tax loss penalties in the amount of TL 46.308.645 accrued as a result of the appraisal by the Inspection Personnel of the Ministry of Finance such accounts and transactions of the Company pertaining to years 2009, 2010, 2011 and January 2012, in respect of Value Added Tax, and in this context, subject matter disputes are concluded and finalized by means of payment of the total liabilities in the approximate amount of TL 9.3 Million including local ÜFE (Manufacturers Price Index) under installments of 18 months.

Company's accounts as well as operations pertaining to year 2010 are inspected and examined in terms of Taxation Laws; and Corporation Tax Inspection Report number 2013-B-228/3, Corporation Tax Withholding Inspection Report number 2013-B-228/5, and Value Added Tax Withholding Tax Inspection Report number 2013-B-228/6 are hereby presented.

Under such Corporation Tax Inspection Report number 2013-B-228/3, it is allegedly stated that deducted amount of TL 1.553.762,38 over the corporation tax return of such lump sum expenses calculated and deducted under scope of the provision of Article 40/1 of Corporation Tax Law over transport proceeds obtained abroad cannot possibly be subjected to any deduction, and further that such portion deducted over the tax return is not related to transport proceeds obtained abroad, while on the other hand it is expressed on the same Report that those minor fixed assets purchased in year 2010, and each to be entered as direct expenses according to Article 313 of Tax Procedures Law are required to be redeemed through amortization , and therefore it is pointed out that TL 76.798,80 as well is to be included in the income of the corporation pertaining to year 2010.

A lawsuit has been filed by the Company, claiming revocation of such determination act with respect to an income difference in the amount of TL 1.630.561,18. Lawsuit filed before Istanbul Tax Court is concluded in favor of the Company. In respect of this judgment, Major Taxpayers Tax Office has appealed in upper court council of state and appeal process has not been concluded yet.

NOTE 15 - PROVISIONS, CONTINGENT ASSETS AND LIABILITIES (cont'd)

Tax Audit (cont'd)

Under decrees of the 4th Department of the Supreme Court of State, dated 28 February 2007, numbers E:2006/2738 E., K:2007/610 and dated 31 March 2005, numbers E:2004/1293, K:2005/529, it is contained judgments reading that the lump sum income amount could possibly be subjected to deduction over the tax return, and further, since the minor fixed assets claimed on the Report and direct costs of which are taken into consideration as expense remain below those limits specified pursuant to the Law, it is opinionated that the matters alleged on the Tax Inspection Report are as to the revocation of the administrative transaction as a consequence of the action filed. Therefore, no provision has been provided and set aside in parallel to the opinions of Company's legal advisors and taxation specialists, including the period not inspected and reviewed on the attached consolidated financial statements.

On such Corporation Tax Inspection Report number 2013-B-228/5, it is stated that despite the fact that rental payments of the Company with respect to such aircraft subject matter of financial leasing from the acquisition of the same through financial leasing from companies with legal and principal places of business domiciled abroad, constitute commercial income of the company obtaining the same under scope of business revenues, alleging that such payments are real property capital income under Article 30 of Corporation Tax Law, they are subject to added value tax withholding at the rate of 1% and in the total amount of TL 706.539,70 as per the relevant months of year 2010, and further on the same Report, it is stated that such package computer software in the form of commercial commodity, purchased from any company with legal and principal places of business domiciled abroad, is subject to corporation tax withholding at the rate of 10% and in the amount of TL 12.968,63 as non-material right charge within framework of Article 30 of Corporation Tax Law.

Major Taxpayers Tax Office that we are affiliated to, accrued corporation tax withholding in the total amount of TL 719.508 for year 2010 through Tax Fine Notices issued as per the relevant months of year 2010 by basing on the said Tax Inspection Report, and charged tax loss fine in the total amount of TL 1.079.262 on grounds of such tax accrued.

Lawsuits have been filed within legal terms granted, before Istanbul Tax Courts as of the respective months of year 2010, with the demand for waiver of the assessments set forth under the subject matter tax inspection reports and rescission of any fines accrued. Actions with respect to the claim that any financial leasing payments made for abroad are subject to corporation tax withholding is concluded in favor of the Company as a result of the Judgment adopted by Tax Courts,which Judgments are brought to appeal by the Tax Administration, and the trial process is still ongoing.

Such lawsuit filed on grounds of the argument that any package computer software of commodity nature, purchased from any company domiciled abroad is subject to corporation tax withholding at the rate of 10% and in the amount of TL 12.968,63 as non-material right (royalty) fee under scope of Article 30 of Corporation Tax Law, is concluded against the Company and such Judgment is brought by the Company to appeal before the Council of State, and the trial process is still ongoing.

According to the specific communiqués issued by the Revenues Department on various dates, since such package computer software purchased from companies with legal and principal places of business domiciled abroad are submitted to the market in readily available form, not comprising of those programs prepared specific to the company, these are commercial commodities, and accordingly, it is opinionated that the purchasing prices of such programs are not subject to corporation tax withholding.

Under such capacity and in parallel to the relevant opinions of Company's legal advisors and taxation specialists, no provision has been provided therefore, including the periods on the accompanied consolidated financial statements not inspected.

NOTE 15 - PROVISIONS, CONTINGENT ASSETS AND LIABILITIES (cont'd)

Tax Audit (cont'd)

Value Added Tax Inspection Report Number 2013-B-228/6, is based on the allegation that corporation tax withholdings arising on grounds of such amounts set forth to be accrued under such Corporation Tax Withholding Inspection Report Number 2013-B-228/5, and corporation tax withholdings anticipated under the said Report are at the same time subject to value added tax withholding.

In the aforesaid process, all of the lawsuits filed with the demand for rescission of such fined value added tax assessments imposed in the name of the Company as per respective monthly periods of year 2010, with the claim that the rate of value added tax required to be calculated over corporation tax withholdings claimed as being payable over such leasing payments with respect to aircraft subject matter of financial leasing with the purpose of acquiring the same from companies with legal domiciles as well as principal places of business abroad being 18% are concluded, and such lawsuits filed in tax courts are concluded in favor of the Company. A part of the judgments were subject to appeal by Major Taxpayers Tax Office before Istanbul Tax Court due to their amounts, but in respect of judgment of İstanbul Regional Administrative Court, the appeals has been rejected and lawsuits were concluded in favor of the Company. A part of these lawsuits were brought to appeal before the Council of State due to their amounts, and the trial process is still ongoing.

It is believed that as a result of the said action filed, the principal taxes anticipated to be accrued, including any fines charged thereon, are to be released. Therefore, in parallel to the opinions of the Company's legal advisors as well as taxation specialists, no provision has been provided on the accompanied consolidated financial statements, including the period not inspected.

Tax and Regulatory Environment in Kyrgzystan

The Kyrgyz Republic has a number of laws related to various taxes imposed by both republican and local governmental authorities. Legislation related to taxes has not been in force for significant period of time, in contrast to more developed market economies and therefore, implementing regulations are often. The accompanying consolidated financial statements consist of management assumptions that are determined by consulting tax and legislative experts.

NOTE 16 - COMMITMENTS

Purchase Commitments

	31 December 2016	31 December 2015
Commitments to purchase aircraft	30.172.478.983	26.485.177.805
	30.172.478.983	**26.485.177.805**

As of 31 December 2016, the Group holds firm orders for 71 aircraft. The expected deliveries are: 5 aircraft in 2017, 13 aircraft in 2018, 14 aircraft in 2019, 13 aircraft in 2020, 13 aircraft in 2021, 13 aircraft in 2022. The purchase commitments for these aircraft were calculated based on their list prices and actual prices would be typically lower than the list prices.

The Group has provided advances on aircraft purchases amounting TL 404.731.495 (31 December 2015: TL 269.313.947) and TL 180.317.329 of this amount is reclassified under short term, TL 224.414.166 of this amount is reclassified under long term prepaid expenses (31 December 2015: TL 206.989.481 of this amount is reclassified under short term, TL 62.324.466 of this amount is reclassified under long term prepaid expenses).

The Company as Lessee

<u>Operating Lease Agreements:</u>

Payments recognised as expense:

	1 January- 31 December 2016	1 January- 31 December 2015
Minimum lease payments	466.867.310	324.574.674
	466.867.310	**324.574.674**

Operating leases have remaining lease terms of between 1 to 8 years. The Company does not have the option to purchase the leased aircraft at the expiration of the lease period.

The non-cancellable operating lease liabilities as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Less than 1 year	546.554.494	400.006.430
Between 1 - 5 years	1.619.658.343	1.311.457.028
Over 5 years	339.147.938	327.309.414
	2.505.360.775	**2.038.772.872**

NOTE 16 - COMMITMENTS (cont'd)

Collaterals-Pledges-Mortgages("CPM")

The details of the CPMs given by the Group as of 31 December 2016 is as follows:

31 December 2016	TL TOTAL	USD	EUR	TL	Other
A. Total amounts of CPM given on behalf of its own legal entity					
-Collateral	567.220.217	147.492.033	7.084.248	12.315.097	9.569.306
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
B. Total amounts of CPM given on behalf of subsidiaries that are included in full consolidation					
-Collateral	49.113.547	8.737.000	-	18.366.297	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
C. Total amounts of CPM given in order to guarantee third parties debts for routine trade operations (*)					
-Collateral	6.316.380	1.794.834	-	-	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
D. Total amounts of other CPM given					
i. Total amount of CPM given on behalf of the Parent					
-Collateral	-	-	-	-	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
ii. Total amount of CPM given on behalf of other group companies not covered in B and C					
-Collateral	-	-	-	-	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
iii. Total amount of CPM given on behalf of third parties not covered in C					
-Collateral	-	-	-	-	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
	622.650.144	**158.023.867**	**7.084.248**	**30.681.394**	**9.569.306**

(*) Consisted of given CPMs to third parties in order to guarantee PUEM's, joint venture company accounted for equity method, liabilities for routine trade operations.

The CPMs given by the Group are consisted of collaterals given to airports and terminals operators, aircraft leasing companies and service suppliers.

The other CPMs given by the Company constitute 0% of the Company's equity as of 31 December 2016.

NOTE 16 - COMMITMENTS (cont'd)

Collaterals-Pledges-Mortgages("CPM") (cont'd)

The details of the CPMs given by the Group as of 31 December 2015 is as follows:

31 December 2015	TL TOTAL	USD	EUR	TL	Other
A. Total amounts of CPM given on behalf of its own legal entity					
-Collateral	411.975.570	125.795.166	7.894.099	12.046.966	9.082.290
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
B. Total amounts of CPM given on behalf of subsidiaries that are included in full consolidation					
-Collateral	31.234.216	6.348.000	-	12.776.771	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
C. Total amounts of CPM given in order to guarantee third parties debts for routine trade operations (*)					
-Collateral	8.641.842	2.972.156	-	-	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
D. Total amounts of other CPM given					
i. Total amount of CPM given on behalf of the Parent					
-Collateral	-	-	-	-	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
ii. Total amount of CPM given on behalf of other group companies not covered in B and C					
-Collateral	-	-	-	-	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
iii. Total amount of CPM given on behalf of third parties not covered in C					
-Collateral	-	-	-	-	-
-Pledge	-	-	-	-	-
-Mortgage	-	-	-	-	-
	451.851.628	**135.115.322**	**7.894.099**	**24.823.737**	**9.082.290**

(*) Consisted of given CPMs to third parties in order to guarantee PUEM's, joint venture company accounted for equity method, liabilities for routine trade operations.

The CPMs given by the Group are consisted of collaterals given to airports and terminals operators, aircraft leasing companies and service suppliers.

The other CPMs given by the Company constitute 0% of the Company's equity as of 31 December 2015.

NOTE 17 - EMPLOYEE BENEFITS

Employee benefit obligations

The details of employee benefit obligations as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Social security premiums payable	16.930.197	7.036.350
Accrual of employee wages	7.670.074	5.600.588
	24.600.271	**12.636.938**

Short term provisions for employee benefits

The details of short term provisions for employee benefits as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Unused vacation accrual	10.757.021	11.079.494
Executive bonus plan	1.409.083	3.933.867
Employee bonus plan	-	11.044.995
	12.166.104	**26.058.356**

Long term provisions for employee benefits

The details of long term provisions for employee benefits as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Employment termination benefits	7.468.611	5.974.463
Executive bonus plan	1.406.642	4.690.138
	8.875.253	**10.664.601**

Unused Vacation Accrual

The movement of unused vacation accrual as of the years ended 31 December 2016 and 2015 are as follows:

	2016	2015
1 January	11.079.494	7.203.782
Charge for the year	1.339.550	4.466.709
Payment during the year	(1.662.023)	(590.997)
31 December	**10.757.021**	**11.079.494**

NOTE 17 - EMPLOYEE BENEFITS (cont'd)

Executive Bonus Plan

The composition of executive bonus plan provision is as follows:

	31 December 2016	31 December 2015
Short term	1.409.083	3.933.867
Long term	1.406.642	4.690.138
	2.815.725	**8.624.005**

The movement of executive bonus plan as of the years ended 31 December 2016 and 2015 are as follows:

	2016	2015
1 January	8.624.005	7.677.946
Charge for the year	-	3.126.758
Payment during the year	(6.271.913)	(2.539.282)
Reversal of provision	-	(346.148)
Currency translation differences	463.630	704.731
31 December	**2.815.722**	**8.624.005**

Employee Bonus Plan

The movement of employee bonus plan as of the years ended 31 December 2016 and 2015 are as follows:

	2016	2015
1 January	11.044.995	17.336.738
Charge for the year	-	11.044.994
Payment during the year	(9.970.922)	(15.234.256)
Reversal of provision	(1.074.073)	(2.102.481)
31 December	**-**	**11.044.995**

Employee Termination Benefits

The Group, according to Turkish Labor Law, has an obligation to pay legal termination benefits for every employee who has completed at least one year service and retired after completion of 25 years working life (for females 58 years, for males 60 years), fired from job, called up to military service or died.

The amount payable consists of one month's salary limited to a maximum of TL 4.297,21 for each period of service at 31 December 2016 (31 December 2015: TL 3.828,37).

NOTE 17 - EMPLOYEE BENEFITS (cont'd)

Employee Termination Benefits (cont'd)

There are no agreements for pension commitments other than the legal requirement as explained above. The liability is not funded, as there is no funding requirement.

The reserve has been calculated by estimating the present value of the future probable obligation of the Group arising from the retirement of the employees. TAS 19 "Employee Benefits" requires actuarial valuation methods to be developed to estimate the enterprise's obligation under defined benefit plans. Accordingly actuarial assumptions were used in the calculation of the total liability as these actuarial assumptions apply to each individual company's defined benefit plan and legal framework in which those companies operate.

The principal assumption is that the maximum liability for each year of service will increase parallel with inflation. Thus, the discount rate applied represents the expected real rate after adjusting for the anticipated effects of future inflation. Consequently, in the accompanying financial statements as of 31 December 2016, the provision has been calculated by estimating the present value of the future probable obligation of the Company arising from the retirement of the employees. The provisions at the respective balance sheet dates have been calculated assuming an annual inflation rate of 6,50% (2015: 6,50%) and a discount rate of 10,75% (2015: 10,75%), resulting in a real discount rate of approximately 3,99% (2015: 3,99%). Estimated amount of retirement pay not paid due to voluntary leaves is also taken into consideration as 13,46% (2015: 16,86%) for employees with 0-15 years of service, and 0% for those with 16 or more years of service. As the maximum liability is revised annually, the maximum amount of TL 4.426,16 effective from 1 January 2017 has been taken into consideration in calculation of provision from employee termination benefits.

The movement of employee termination benefits as of the years ended 31 December 2016 and 2015 are as follows:

	2016	**2015**
1 January	5.974.463	1.214.446
Actuarial loss / (gain)	165.923	3.965.618
Service cost	4.548.664	1.698.106
Interest cost	337.962	34.866
Retirement benefits paid	(3.558.401)	(938.573)
31 December	**7.468.611**	**5.974.463**

Service cost and interest expenses are recognized in payroll expenses. Calculated actuarial gains and losses are accounted under other comprehensive income as of 31 December 2016 and 2015.

Significant assumptions used in the calculation of employee termination benefits are the discount rate and anticipated turnover rate.

- If the discount rate had been 1% lower, provision for employee termination benefits would increase by TL 935.018 (2015: TL 700.387); if the rate had been 1% higher, it would decrease by TL 783.346 (2015: TL 592.697).
- If the anticipated turnover rate had been 1% higher while all other variables were held constant, provision for employee termination benefits would decrease by TL 126.378 (2015: TL 57.477); if the rate had been 1% lower, it would increase by TL 145.517 (2015: TL 66.690).

NOTE 18 - EXPENSES BY NATURE

The details of expenses by nature for the years ended 31 December 2016 and 2015 are as follows:

	1 January-31 December 2016	1 January-31 December 2015
Jet fuel expenses	985.775.955	1.118.567.032
Personnel expenses	645.214.424	442.603.089
Operating lease expenses	466.867.310	324.574.674
Maintenance expenses	360.570.191	270.582.494
Handling and station fees	309.062.974	270.327.708
Navigation expenses	257.145.897	239.957.446
Depreciation and amortisation expenses	226.520.338	175.962.021
Landing expenses	124.823.419	102.127.063
Advertising expenses	70.417.454	68.123.074
Commission expenses	68.481.782	54.618.585
Passenger service and catering expenses	47.161.845	40.969.621
Other expenses	282.467.120	202.882.469
	3.844.508.709	**3.311.295.276**

NOTE 19 - OTHER ASSETS AND LIABILITIES

Other current assets

The details of other current assets as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
VAT receivables	7.241.807	1.823.293
Other	212.534	384.878
	7.454.341	**2.208.171**

Other short term liabilities

The details of other short term liabilities as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Call option liability of joint-venture share	-	3.833.250
Other	212.930	831.801
	212.930	**4.665.051**

NOTE 20 - SHAREHOLDERS' EQUITY

The Company's shareholding structure as of 31 December 2016 and 2015 is as follows:

	31 December 2016		**31 December 2015**	
Shareholders:	**(%)**	**TL**	**(%)**	**TL**
Esas Holding	62,92	64.353.570	62,92	64.353.570
Publicly held	34,51	35.294.000	34,51	35.294.000
Emine Kamışlı	0,86	874.810	0,86	874.810
Ali İsmail Sabancı	0,86	874.810	0,86	874.810
Kazım Köseoğlu	0,43	437.405	0,43	437.405
Can Köseoğlu	0,43	437.405	0,43	437.405
TL historic capital	**100,0**	**102.272.000**	**100,0**	**102.272.000**

The Company's share capital consists of 102.272.000 shares of par value TL 1 each (31 December 2015: 102.272.000 shares). All issued shares are fully paid in cash.

Dividend distribution

Shares of the Company have been started to be traded in İstanbul Stock Exchange ("ISE") since 26 April 2013, after the demand collection between the dates of 18-19 April 2013. Listed companies distribute dividend in accordance with the Communiqué No. II-19.1 issued by the CMB which is effective from February 1, 2014.

Companies distribute dividends in accordance with their dividend payment policies settled and dividend payment decision taken in general assembly and also in conformity with relevant legislations. The communiqué does not constitute a minimum dividend rate. Companies distribute dividend in accordance with the method defined in their dividend policy or articles of associations.

Resources Available for Profit Distribution:

The Company does not have any distributable equity in statutory accounts as of balance sheet date (31 December 2015: TL 80.026.021).

Currency translation differences

For the purpose of preparation of the consolidated financial statements and disclosures, according to TAS 21, balance sheet items except shareholders' equity in financial statements are translated to TL using balance sheet date EUR exchange rates; equity items, income/expenses and cash flow are translated to TL by using the exchange rate of the transaction date (historic rate), and currency translation differences are presented under shareholders' equity.

NOTE 20 - SHAREHOLDERS' EQUITY (cont'd)

Gain/losses from cash flow hedges

Hedge gain/losses against cash flow risk arise from the accounting of the changes in the fair values of effective derivative financial instruments designated against financial risks of future cash flows under equity. Total of deferred gain/loss arising from hedging against financial risk are accounted in profit or loss when the effect of the hedged item has effect on profit or loss.

Share premiums on capital stock

The surplus of sales price over nominal value amounted to TL 455.687.025 during the inital public offering on 18-19 April 2013 was accounted as share premium.

Effects of business acquisitions

As the acquisition of İzair's majority shares by the Group on 28 September 2010 had no effect over Esas Holding A.Ş. being the ultimately controlling shareholder which had ultimate control over both subsidiaries pre and post the acquisition, it is defined as business combination under common control.

Non-controlling interests

Non-controlling shareholders' shares on subsidiaries' net assets and operational outcomes are disclosed as non-controlling interests in the consolidated balance sheet and in the consolidated statement of profit or loss and other comprehensive income.

Actuarial gain/losses on defined benefit plans

The effects of the change in actuarial valuations that is calculated with respect to TAS 19"Employee Benefits" is presented in actuarial gains/losses on defined benefit plans.

Restricted profit reserves

In the statutory accounts, profit restricted from retained earnings and not subject to distribution is presented in the restricted profit reserves.

NOTE 21 - SALES AND COST OF SALES

The details of sales and cost of sales for the years ended 31 December 2016 and 2015 are as follows:

Sales:

	1 January- 31 December 2016	1 January- 31 December 2015
Scheduled flights	2.704.834.882	2.667.831.123
International scheduled flights	*1.607.104.008*	*1.654.642.063*
Domestic scheduled flights	*1.097.730.874*	*1.013.189.060*
Ancillary revenue	816.586.154	663.333.772
Charter flights	114.487.922	102.632.083
Other revenue	71.562.177	54.474.245
	3.707.471.135	**3.488.271.223**

Geographical details of revenue from the scheduled flights are as follows:

	1 January- 31 December 2016	1 January- 31 December 2015
Europe	1.182.937.849	1.281.835.442
Domestic	1.097.730.874	1.013.189.060
Other	424.166.159	372.806.621
	2.704.834.882	**2.667.831.123**

Cost of sales:

	1 January- 31 December 2016	1 January- 31 December 2015
Jet fuel expenses	985.775.955	1.118.567.032
Personnel expenses	574.448.235	390.162.323
Operating lease expenses	466.867.310	324.574.674
Maintenance expenses	360.570.191	270.582.494
Handling and station fees	309.062.974	270.327.708
Navigation expenses	257.145.897	239.957.446
Depreciation and amortisation expenses	202.393.619	159.860.939
Landing expenses	124.823.419	102.127.063
Passenger service and catering expenses	47.161.845	40.969.621
Other expenses	183.052.358	137.854.506
	3.511.301.803	**3.054.983.806**

NOTE 22 - GENERAL ADMINISTRATIVE EXPENSES AND MARKETING EXPENSES

	1 January- 31 December 2016	1 January- 31 December 2015
Marketing expenses	182.641.780	149.815.601
General administrative expenses	150.565.126	106.495.869
	333.206.906	**256.311.470**

The details of general administrative expenses and marketing expenses for the years ended 31 December 2016 and 2015 are as follows (there are no research & development expenses in the periods ended in respective dates):

General administrative expenses:

	1 January- 31 December 2016	1 January- 31 December 2015
Personnel expenses	53.617.503	40.859.267
IT expenses	22.904.779	12.902.865
Depreciation and amortisation expenses	19.502.965	12.993.134
Rent expenses	16.667.867	12.234.279
Consultancy expenses	10.254.269	5.600.038
Legal and notary expenses	5.294.901	4.697.167
Travel expenses	3.206.675	4.403.036
Office utility expenses	2.335.674	1.503.355
Training expenses	1.918.917	1.662.589
Communication expenses	1.729.643	1.662.589
Other expenses	13.131.933	7.977.550
	150.565.126	**106.495.869**

Marketing expenses:

	1 January- 31 December 2016	1 January- 31 December 2015
Advertising expenses	70.417.454	68.123.074
Commission expenses	68.481.782	54.618.585
Personnel expenses	17.148.686	11.581.499
Call center expenses	10.485.131	8.485.587
Depreciation and amortisation expenses	4.623.754	3.107.948
Other expenses	11.484.973	3.898.908
	182.641.780	**149.815.601**

NOTE 23 - OTHER OPERATING INCOME AND EXPENSES

The details of other operating income and expenses for the years ended 31 December 2016 and 2015 are as follows:

Other operating income:

	1 January- 31 December 2016	1 January- 31 December 2015
Foreign exchange gain from operating activities	53.643.960	92.173.595
Reversal of discounts	20.071	178.126
Other income	2.712.638	3.173.898
	56.376.669	**95.525.619**

Other operating expenses:

	1 January- 31 December 2016	1 January- 31 December 2015
Tax restructuring expenses	13.935.961	-
Penalty and compensation expenses	584.138	133.291
Doubtful receivable expense	231.390	913.951
Uncollectible other tax receivables	-	625.652
Other expense	10.542.409	1.471.590
	25.293.898	**3.144.484**

NOTE 24 - INCOME FROM INVESTING ACTIVITIES

The details of income from investing activities for the years ended 31 December 2016 and 2015 are as follows:

Income from investing activities:

	1 January- 31 December 2016	1 January- 31 December 2015
Foreign exchange gain from investing activities	23.029.095	16.826.179
Other income	2.831.473	792.988
	25.860.568	**17.619.167**

NOTE 25 - FINANCIAL INCOME AND EXPENSES

The details of financial income and expenses for the years ended 31 December 2016 and 2015 are as follows:

Financial income:

	1 January- 31 December 2016	1 January- 31 December 2015
Interest income	27.921.205	44.019.954
Gain on derivative contracts	6.662.908	-
Foreign exchange gain	-	16.250.189
	34.584.113	**60.270.143**

Financial expenses:

	1 January- 31 December 2016	1 January- 31 December 2015
Foreign exchange loss	50.437.216	-
Other commission expenses	22.207.867	17.341.838
Interest expense on financial lease	16.139.463	8.818.137
Surety commission expenses	11.955.096	12.214.137
Losses from derivative contracts	-	129.103.106
	100.739.642	**167.477.218**

NOTE 26 - ANALYSIS OF OTHER COMPREHENSIVE INCOME ITEMS

Currency Translation Differences

	2016	2015
1 January	406.940.383	258.696.079
Exchange differences arising on translating the non-monetary items of the the parent	244.757.500	157.756.341
Exchange differences arising on translating the non-monetary items of the domestic subsidiaries	5.142.304	1.323.604
Exchange differences arising on translating the non-monetary items of the subsidiaries abroad	(18.464.193)	(10.835.641)
31 December	**638.375.994**	**406.940.383**

Hedge Fund

	2016	2015
1 January	(22.138.754)	(58.095.258)
Gain/(loss) from the accounting of cash flow hedges against financial risk	28.038.256	44.945.630
Deferred tax related with the accounting of cash flow hedges against financial risk	(5.607.652)	(8.989.126)
31 December	**291.850**	**(22.138.754)**

The cash flow hedging reserve represents the cumulative effective portion of gains or losses arising on changes in fair value of hedging instruments entered into for cash flow hedges. The cumulative gain or loss arising on changes in fair value of the hedging instruments that are recognized and accumulated under the heading of cash flow hedging reserve will be reclassified to profit or loss only when the hedged transaction affects the profit or loss, or included as a basis adjustment to the non-financial hedged item, consistent with the relevant accounting policy.

Actuarial gains/(losses) on defined benefit plans

	2016	2015
1 January	(3.172.494)	-
Actuarial gains/(losses) on defined benefit plans	(165.923)	(3.965.618)
Deferred tax effect of actuarial gains/(losses) on defined benefit plans	33.185	793.124
31 December	**(3.305.232)**	**(3.172.494)**

NOTE 27 - TAXATION ON INCOME (INCLUDING DEFERRED TAX ASSETS AND LIABILITIES

	31 December 2016	31 December 2015
Current corporate tax provision	-	17.908.212
Less: Prepaid taxes and funds	(3.586.742)	(46.942.680)
Current tax assets (*)	**(3.586.742)**	**(29.034.468)**

(*) The exceeding portion of the prepaid taxes over current corporate tax provision is reported in current tax assets.

	1 January- 31 December 2016	1 January- 31 December 2015
Income tax expense		
- Current tax expense	-	(17.908.212)
- Deferred tax income/(expense)	7.486.578	(52.607.285)
Total tax income/(expense)	**7.486.578**	**(70.515.497)**

Corporate Tax

The Group is subject to Turkish corporate taxes. Provision is made in the accompanying financial statements for the estimated charge based on the Group's results for the years and periods. Turkish tax legislation does not permit a parent company and its subsidiary to file a consolidated tax return. Therefore, provisions for taxes, as reflected in the accompanying consolidated financial statements, have been calculated on a separate-entity basis.

Corporate tax is applied on taxable corporate income, which is calculated from the statutory accounting profit by adding back non-deductible expenses, and by deducting dividends received from resident companies, other exempt income and investment incentives utilized.

The corporate tax rate in Turkey is 20% (2015: 20%).

Deferred Tax

The Group recognizes deferred tax assets and liabilities based upon temporary differences arising between its financial statements as reported for TAS purposes and its statutory tax financial statements. These differences usually result in the recognition of revenue and expenses in different reporting periods for TAS and tax purposes and they are given below.

For calculation of deferred income tax asset and liabilities, the rate of 20% is used (2015: 20%).

In Turkey, companies cannot declare a consolidated tax return, therefore their deferred tax balances are not netted off and are disclosed separately.

NOTE 27 - TAXATION ON INCOME (INCLUDING DEFERRED TAX ASSETS AND LIABILITIES (cont'd)

Deferred Tax (cont'd)

The consolidated deferred tax asset position as of 31 December 2016 is as follows:

	1 January - 31 December 2016				
	31 December	Currency translation effect	Other comprehensive income tax effect	Deferred tax charge for the year	1 January
Difference between tax base and carrying value of tangible assets and intangible assets	(6.766.467)	(608.984)	-	(7.535.406)	1.377.923
Provision for employee termination benefits	532.464	7.334	33.185	(35.398)	527.343
Provision for litigation claims	7.926	1.071	-	1.389	5.466
Unused vacation and bonus plans provision	633.051	(6.287)	-	639.338	-
Carry forward tax losses	42.603.926	1.117.607	-	10.252.355	31.233.964
Relivery provisions for the leased aircraft	4.515.719	594.198	-	1.118.670	2.802.851
Other	(953.617)	23.861	-	(588.778)	(388.700)
Deferred tax provision (*)	(33.719.029)	(9.006)	-	(6.791.283)	(26.918.740)
Deferred tax asset	**6.853.973**	**1.119.794**	**33.185**	**(2.939.113)**	**8.640.107**

(*) Deferred tax provision has been provided for the carried forward tax losses of Izair.

NOTE 27 - TAXATION ON INCOME (INCLUDING DEFERRED TAX ASSETS AND LIABILITIES (cont'd)

Deferred Tax (cont'd)

The consolidated deferred tax liability position as of 31 December 2016 is as follows:

	1 January - 31 December 2016				
	31 December	Currency translation effect	Other comprehensive income tax effect	Deferred tax charge for the year	1 January
Difference between tax base and carrying value of tangible assets and intangible assets	(427.405.508)	(57.974.056)	-	(78.293.113)	(291.138.339)
Carry forward tax losses	99.366.670	9.963.790	-	89.402.880	-
Provision for employee termination benefits	1.421.273	79.853	-	213.953	1.127.467
Provision for litigation claims	1.266.728	150.283	-	655.273	461.172
Unused vacation and bonus plans provision	1.376.362	279.544	-	(268.140)	1.364.958
Deferred revenue from flight points	4.910.078	732.246	-	(577.700)	4.755.532
Relivery provisions for the leased aircraft	80.792.518	10.203.018	-	28.926.899	41.662.601
Change in fair value of derivative contracts	(225.473)	1.479.434	(5.607.652)	(31.262.132)	35.164.877
Other	4.716.518	460.645	-	1.627.771	2.628.102
Deferred tax liability	**(233.780.834)**	**(34.625.243)**	**(5.607.652)**	**10.425.691**	**(203.973.630)**

NOTE 27 - TAXATION ON INCOME (INCLUDING DEFERRED TAX ASSETS AND LIABILITIES (cont'd)

Deferred Tax (cont'd)

The consolidated deferred tax asset position as of 31 December 2015 is as follows:

	1 January - 31 December 2015			
	31 December	Currency translation effect	Deferred tax charge for the year	1 January
Difference between tax base and carrying value of tangible assets and intangible assets	1.377.923	532.172	(5.846.871)	6.692.622
Provision for employee termination benefits	527.343	(33.588)	520.350	40.581
Provision for litigation claims	5.466	2.693	(32.204)	34.977
Carry forward tax losses	31.233.964	927.408	10.798.488	19.508.068
Relivery provisions for the leased aircraft	2.802.851	319.372	(70.689)	2.554.168
Other	(388.700)	99.200	(1.314.418)	826.518
Deferred tax provision (*)	(26.918.740)	(482.645)	(10.180.163)	(16.255.932)
Deferred tax asset	**8.640.107**	**1.364.612**	**(6.125.507)**	**13.401.002**

(*) Deferred tax provision has been provided for the carried forward tax losses of Izair.

NOTE 27 - TAXATION ON INCOME (INCLUDING DEFERRED TAX ASSETS AND LIABILITIES (cont'd)

Deferred Tax (cont'd)

The consolidated deferred tax liability position as of 31 December 2015 is as follows:

	1 January - 31 December 2015				
	31 December	Currency translation effect	Other comprehensive income tax effect	Deferred tax charge for the year	1 January
Difference between tax base and carrying value of tangible assets and intangible assets	(291.138.339)	(30.062.326)	-	(40.442.178)	(220.633.835)
Provision for employee termination benefits	1.127.467	31.033	793.124	101.002	202.308
Provision for litigation claims	461.172	49.939	-	28.793	382.440
Unused vacation and bonus plans provision	1.364.958	217.860	-	(161.007)	1.308.105
Carry forward tax losses	-	-	-	-	-
Deferred revenue from flight points	4.755.532	465.275	-	1.066.699	3.223.558
Relivery provisions for the leased aircraft	41.662.601	3.592.311	-	16.842.023	21.228.267
Change in fair value of derivative contracts	35.164.877	3.800.195	(8.989.126)	(7.315.550)	47.669.358
Other	2.628.102	1.251.137	-	(16.601.560)	17.978.525
Deferred tax liability	**(203.973.630)**	**(20.654.576)**	**(8.196.002)**	**(46.481.778)**	**(128.641.274)**

NOTE 27 - TAXATION ON INCOME (INCLUDING DEFERRED TAX ASSETS AND LIABILITIES (cont'd)

Deferred Tax (cont'd)

The Group's carryforward tax losses subject to recognition of deferred tax asset as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
2017	1.046.604	1.043.244
2018	24.487.645	20.231.949
2019	45.744.099	37.794.255
2020 and after	97.316.797	75.524.252
	168.595.145	**134.593.700**

Tax effects related to other comprehensive income as of 31 December 2016 and 2015 are as follows:

	1 January - 31 December 2016		
	Amount before tax	Tax income / (expense)	Amount after tax
Change in foreign currency translation	230.474.848	-	230.474.848
Actuarial gains/(losses) on defined benefit plans	(165.923)	33.185	(132.738)
Change in cash flow hedge reserve	28.038.256	(5.607.652)	22.430.604
Other comprehensive income	**258.347.181**	**(5.574.467)**	**252.772.714**

	1 January - 31 December 2015		
	Amount before tax	Tax income	Amount after tax
Change in foreign currency translation	146.923.530	-	146.923.530
Actuarial gains/(losses) on defined benefit plans	(3.965.618)	793.124	(3.172.494)
Change in cash flow hedge reserve	44.945.630	(8.989.126)	35.956.504
Other comprehensive income	**187.903.542**	**(8.196.002)**	**179.707.540**

NOTE 27 - TAXATION ON INCOME (INCLUDING DEFERRED TAX ASSETS AND LIABILITIES (cont'd)

Deferred Tax (cont'd)

Reconciliation of tax expense in consolidated statement of profit or loss for the years ending 31 December 2016 and 2015 is as follows:

	1 January- 31 December 2016	1 January- 31 December 2015
(Loss) / profit before tax	**(143.669.576)**	**182.379.370**
Enacted local tax rate	20%	20%
Tax calculated at the enacted tax rate	28.733.915	(36.475.874)
Tax effect of disallowable expenses	(5.594.390)	(1.093.924)
Tax-exempt revenue	4.427.581	2.187.702
Tax losses over which deferred tax asset was not recognized	(16.859.514)	(13.403.162)
Subsidiary effect that have different tax rate	(16.742.514)	(13.370.105)
Translation effect and other	13.521.500	(8.360.134)
Taxation income / (expense)	**7.486.578**	**(70.515.497)**

NOTE 28 - EARNINGS / LOSS PER SHARE

Earnings/loss per share disclosed in the consolidated statements of income are determined by dividing the net income by the weighted number of shares that have been outstanding during the period concerned. Number of total shares and calculation of earnings per share at 31 December 2016 and 2015 are as follows:

	1 January- 31 December 2016	1 January- 31 December 2015
Net income/(loss) attributable to the shareholders of the parent	(133.730.835)	113.125.704
Weighted average number of shares issued in the year	102.272.000	102.272.000
Gain/(loss) per share	**(1,31)**	**1,11**

NOTE 29- EFFECTS OF EXCHANGE RATE CHANGES

Details related to effects of exchange rate changes are disclosed at foreign currency risk management in Note 32.

NOTE 30 - DERIVATIVE INSTRUMENTS

Fair Value of Derivative Instruments

	31 December 2016		31 December 2015	
	Asset	**Liability**	**Asset**	**Liability**
Short term	1.127.368	-	2.341.144	178.165.534
	1.127.368	**-**	**2.341.144**	**178.165.534**

Explanations related to derivative instruments are disclosed in Note 2.5 and Note 33.

NOTE 31 - FINANCIAL INSTRUMENTS

Financial Liabilities

The details of financial liabilities as of 31 December 2016 and 2015 are as follows:

Short term financial liabilities	**31 December 2016**	**31 December 2015**
Short term bank borrowings	-	6.826.527
Short term portion of long term financial lease obligations	338.293.216	201.887.265
	338.293.216	**208.713.792**

Long term financial liabilities	**31 December 2016**	**31 December 2015**
Long term financial lease obligations	2.338.272.374	1.206.722.990
	2.338.272.374	**1.206.722.990**

a) Bank Borrowings

The effective interest rates, original currency and TL equivalents of the borrowings as of 31 December 2015 is as follows (31 December 2016: None):

31 December 2015	**Weighted average interest rate (%)**	**Currency**	**Original amount**	**TL equivalent**
Short term bank borrowings	0,00 (*)	TL	6.826.527	6.826.527
				6.826.527

(*) Amount consists of non-interest bearing loans for monthly social security premiums and tax payments.

NOTE 31 - FINANCIAL INSTRUMENTS (cont'd)

Financial Liabilities (cont'd)

b) Financial Lease Liabilities

The details of financial lease liabilities as of 31 December 2016 and 2015 are as follows:

	31 December 2016	**31 December 2015**
Less than 1 year	389.599.184	207.191.438
Between 1 - 5 years	1.549.886.614	820.080.814
Over 5 years	1.118.924.055	407.230.694
	3.058.409.853	1.434.502.946
Less: Future interest expenses	(381.844.263)	(25.892.691)
	2.676.565.590	**1.408.610.255**

Present value of minimum lease payments of financial lease liabilities are as follows;

	31 December 2016	**31 December 2015**
Less than 1 year	338.293.216	201.887.265
Between 1 - 5 years	1.348.471.440	801.394.966
Over 5 years	989.800.934	405.328.024
	2.676.565.590	**1.408.610.255**

The Group purchases certain of its aircraft and handling equipment through financial lease arrangements. The average lease term is 6,48 years. For the year ended 31 December 2016, the floating interest rate applicable to Euro-denominated lease obligations is 0,50% (31 December 2015: 0,08%) and the floating rate applicable to US Dollar-denominated lease obligations is 4,61% (31 December 2015: 2,32%).

Net carrying amounts of leased assets as of the balance sheet date is TL 3.286.031.801 (31 December 2015: TL 1.869.927.536)

NOTE 31 - FINANCIAL INSTRUMENTS (cont'd)

Financial Liabilities (cont'd)

b) Financial Lease Liabilities (cont'd)

The Group's obligations under finance leases of aircraft are guaranteed by the Export-Import Bank of the United States ("Ex-Im Bank").

The aircraft manufacturer, the Group, the lender, Ex-Im Bank, Special Purpose Vehicle Company ("SPV") and orphan trust which managed the SPV and a security trustee with whom the orphan trusts securities are pledged enter into a Participation Agreement to structure the financing deal. The Lender enters into a commitment with the Group and loan documentation with a SPV as borrower, owner and lessor. The SPV draws down the loan from lender and purchases the aircraft from Boeing on the delivery date. The equity interests in the SPV are indirectly beneficially owned by an unrelated orphan trust which in turn its shares are pledged to a security trustee in favor of Ex-Im Bank.

The Group indemnifies the SPV against all of their obligations under the finance lease, with Esas Holding providing a guarantee for the full obligation.

All Ex-Im Bank supported credit facilities also contain cross-default and cross-collateralization provisions. These provisions provide for mandatory pre-payment of Ex-Im Bank guaranteed loans (without penalties, but with applicable breakage costs) in the event of total loss or seizure of any of the Group's aircraft in the event of default which had not been cured or equivalent events affecting the aircraft, including the sale or disposal of such aircraft before the pay down of the debt to lender and extinguishment of US Ex-Im Bank guarantee. The termination of Esas Holding's ownership of the Group may also result in the acceleration of the finance leases. Additionally, Ex-Im Bank documentation governing these guaranteed loans also imposes restrictive covenants on the SPV in respect of their liabilities and the nature of their business and a restriction on other pledges of interests on the aircraft and other assets of the SPV, and imposes on the Group a restriction on mergers, consolidations and sale of substantially all of the Group's assets.

In respect of the aircraft purchased by the Group in December 2013 through financial lease without using US Ex-Im guarantee, the same method of finance is used as in under US Ex-Im structure only to the extent that all rights on SPV as the proprietor of the aircraft are pledged by the bank providing the financing. There are no guarantees provided by Esas Holding in connection with the subject matter aircraft.

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS

Capital Risk Management

The Group manages its capital with the goal of ensuring that the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance.

The capital structure of the Group consists of debt, which includes the financial liabilities and obligations under finance leases disclosed in Note 31, cash and cash equivalents and equity, comprising issued capital, reserves and retained earnings, respectively. The Group meets working capital requirement with the cash generated from its operations and through credit lines from Turkish and foreign banks, if needed.

The Group's management reviews the cost of capital together with the risk associated with each class in the capital structure. As a part of this review, the management considers the cost of capital and the risks associated with each class of capital and obtains approval from Board of Directors in the form of a resolution. Based on evaluations of management and Board of Directors, the Group balances its overall capital structure from time to time through capital increases as well as the issue of new debt or the redemption of existing debt. The Group's overall capital risk management strategy remains unchanged from prior periods.

The debt-capital ratio that is calculated as net debt (total borrowings less cash and cash equivalents) divided by total capital as of 31 December 2016 and 2015 are as follows.

	31 December 2016	31 December 2015
Financial Liabilities	2.676.565.590	1.415.436.782
Less: Cash and Cash Equivalents	(692.270.625)	(954.974.093)
Net Debt	1.984.294.965	460.462.689
Total Equity	1.569.321.345	1.452.731.629
Total Capital	3.553.616.310	1.913.194.318
Net Debt/Total Capital Ratio	**0,6**	**0,2**

Financial Risk Factors

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, fair value interest rate risk, cash flow interest rate risk and price risk), credit risk and liquidity risk. The Group's overall risk management plan focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain risk exposures.

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Credit risk management

	Receivables					
	Trade Receivables		Other Receivables			
31 December 2016	Related Party	Other	Related Party	Other	Bank Deposits	Derivative Instruments
Maximum exposed credit risk as of reporting date (A+B+C+D) (*)	**-**	**212.269.499**	**1.097.807**	**138.694.721**	**691.853.303**	**1.127.368**
Secured portion of the maximum credit risk by guarantees, etc. (**)	-	21.463.681	-	-	-	-
A. Net book value of financial asset neither are not due or nor impaired	-	201.795.193	1.097.807	138.694.721	691.853.303	1.127.368
B. Net book value of financial assets that are past due but not impaired	-	10.474.306	-	-	-	-
-The part under guarantee with collateral etc.	-	997.922	-	-	-	-
C. Net book value of impaired assets						
- Past due (gross carrying amount)	-	8.998.147	-	1.706.812	-	-
- Impairment(-)	-	(8.998.147)	-	(1.706.812)	-	-
- The part of net value under guarantee with collateral etc.	-	-	-	-	-	-
- Not Past due (gross carrying amount)	-	-	-	-	-	-
- Impairment(-)	-	-	-	-	-	-
- The part of net value under guarantee with collateral etc.	-	-	-	-	-	-
D. Off-balance sheet items with credit risk	-	-	-	-	-	-

(*) The factors that increase in credit reliability such as guarantees received are not considered in the balance.
(**) Guarantees consist of the letters of guarantee obtained from the customers

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Credit risk management (cont'd)

	Receivables					
	Trade Receivables		Other Receivables			
31 December 2015	**Related Party**	**Other**	**Related Party**	**Other**	**Bank Deposits**	**Derivative Instruments**
Maximum exposed credit risk as of reporting date (A+B+C+D) (*)	**-**	**294.629.623**	**278.844**	**218.511.143**	**954.831.942**	**2.341.144**
Secured portion of the maximum credit risk by guarantees, etc. (**)	-	13.171.064	-	-	-	-
A. Net book value of financial asset neither are not due or nor impaired	-	292.126.053	278.844	218.511.143	954.831.942	2.341.144
B. Net book value of financial assets that are past due but not impaired	-	2.503.570	-	-	-	-
-The part under guarantee with collateral etc.	-	442.013	-	-	-	-
C. Net book value of impaired assets						
- Past due (gross carrying amount)	-	3.175.648	-	5.984.300	-	-
- Impairment(-)	-	(3.175.648)	-	(5.984.300)	-	-
- The part of net value under guarantee with collateral etc.	-	-	-	-	-	-
- Not Past due (gross carrying amount)	-	-	-	-	-	-
- Impairment(-)	-	-	-	-	-	-
- The part of net value under guarantee with collateral etc.	-	-	-	-	-	-
D. Off-balance sheet items with credit risk	-	-	-	-	-	-

(*) The factors that increase in credit reliability such as guarantees received are not considered in the balance.
(**) Guarantees consist of the letters of guarantee obtained from the customers

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Credit risk management (cont'd)

Aging of the past due receivables is as follows:

31 December 2016	Trade receivables	Other receivables	Bank deposits	Total
1-30 days past due	140.444	-	-	140.444
1-3 months past due	10.145.537	-	-	10.145.537
3-12 months past due	81.345	-	-	81.345
1-5 years past due	9.105.127	1.706.812	-	10.811.939
Receivables secured by guarantees	(997.922)	-	-	(997.922)
	18.474.531	**1.706.812**	**-**	**20.181.343**

31 December 2015	Trade receivables	Other receivables	Bank deposits	Total
1-30 days past due	754.870	-	-	754.870
1-3 months past due	815.665	-	-	815.665
3-12 months past due	1.978.429	-	-	1.978.429
1-5 years past due	2.130.254	5.984.300	-	8.114.554
Receivables secured by guarantees	(442.013)	-	-	(442.013)
	5.237.205	**5.984.300**	**-**	**11.221.505**

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Liquidity risk management

The Group manages liquidity risk by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

The following tables show the Group's remaining contractual maturity for its financial liabilities. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The table includes both interest and principal cash flows.

31 December 2016 **Due date on the contract**	**Carrying value**	**Contractual cash-flows (I+II+III+IV)**	**Up to 3 months (I)**	**3 months-12 months (II)**	**1 year-5 years (III)**	**More than 5 years (IV)**
Non-derivative financial liabilities						
Obligations under financial leases	2.676.565.590	3.058.409.853	93.835.591	295.763.593	1.549.886.614	1.118.924.055
Trade payables	317.877.743	317.877.743	317.877.743	-	-	-
Passenger airport fees liability	60.671.024	60.671.024	47.827.606	12.843.418	-	-
	3.055.114.357	**3.436.958.620**	**459.540.940**	**308.607.011**	**1.549.886.614**	**1.118.924.055**

Due date on the contract	**Carrying value**	**Contractual cash-flows (I+II+III+IV)**	**Up to 3 months (I)**	**3 months-12 months (II)**	**1 year-5 years (III)**	**More than 5 years (IV)**
Derivative financial liabilities						
Derivative cash inflows outflows, net	1.127.368	1.165.173	121.411	1.043.762	-	-

31 December 2015 **Due date on the contract**	**Carrying value**	**Contractual cash-flows (I+II+III+IV)**	**Up to 3 months (I)**	**3 months-12 months (II)**	**1 year-5 years (III)**	**More than 5 years (IV)**
Non-derivative financial liabilities						
Financial liabilities	6.826.527	6.826.527	6.826.527	-	-	-
Obligations under financial leases	1.408.610.255	1.434.502.946	52.148.901	155.042.537	820.080.814	407.230.694
Trade payables	245.899.093	245.899.093	245.899.093	-	-	-
Passenger airport fees liability	61.623.605	61.623.605	42.062.877	19.560.728	-	-
	1.722.959.480	**1.748.852.171**	**346.937.398**	**174.603.265**	**820.080.814**	**407.230.694**

Due date on the contract	**Carrying value**	**Contractual cash-flows (I+II+III+IV)**	**Up to 3 months (I)**	**3 months-12 months (II)**	**1 year-5 years (III)**	**More than 5 years (IV)**
Derivative financial liabilities						
Derivative cash inflows outflows, net	(175.824.390)	(177.570.271)	(35.655.653)	(141.914.618)	-	-

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Market risk

The Group's activities expose it primarily to the financial risks of changes in foreign currency exchange rates, fuel price and interest rates. The Group enters into a variety of derivative financial instruments to manage its exposure to foreign currency, fuel price and interest rate risk.

Foreign currency risk management

The Group has significant transactions in non-euro currencies including, but not limited to, Turkish Lira revenues, non-euro borrowings and US dollar fuel purchases. These non-euro denominated transactions expose the Group to foreign currency risk. Exchange rate exposures are managed within approved policy parameters utilising forward foreign exchange contracts.

The Group's foreign currency position of monetary and non-monetary assets/liabilities for the years ended 31 December 2016 and 2015 are as follows:

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Foreign currency risk management (cont'd)

31 December 2016	TL Total	USD	TL	GBP	Other
1. Trade receivables	136.119.410	10.462.426	39.600.493	3.176.579	45.980.220
2a. Monetary financial assets	479.857.123	115.814.353	56.509.870	998.995	11.458.822
2b. Non monetary financial assets	-	-	-	-	-
3. Other	289.345.009	75.327.858	20.187.181	59.823	3.805.661
4. CURRENT ASSETS	905.321.542	201.604.637	116.297.544	4.235.397	61.244.703
5. Trade receivables	-	-	-	-	-
6a. Monetary financial assets	-	-	-	-	-
6b. Non monetary financial assets	-	-	-	-	-
7. Other	244.691.900	68.925.723	587.209	19.800	1.455.772
8. NON CURRENT ASSETS	244.691.900	68.925.723	587.209	19.800	1.455.772
9. TOTAL ASSETS	1.150.013.442	270.530.360	116.884.753	4.255.197	62.700.475
10. Trade payables	201.568.025	34.159.184	71.634.896	294.638	8.447.617
11. Financial liabilities	134.221.362	38.139.737	-	-	-
12a. Other liabilitites, monetary	72.402.420	(1.597.712)	77.729.155	-	295.933
12b. Other liabilitites, non monetary	-	-	-	-	-
13. CURRENT LIABILITIES	408.191.807	70.701.209	149.364.051	294.638	8.743.550
14. Trade payables	-	-	-	-	-
15. Financial liabilities	1.125.413.365	319.792.386	-	-	-
16a. Other liabilitites, monetary	-	-	-	-	-
16b. Other liabilitites, non monetary	-	-	-	-	-
17. NON CURRENT LIABILITIES	1.125.413.365	319.792.386	-	-	-
18. TOTAL LIABILITIES	1.533.605.172	390.493.595	149.364.051	294.638	8.743.550
19. Net asset / (liability) position of Off-balance sheet derivatives (19a-19b)	-	-	-	-	-
19.a Off-balance sheet foreign currency derivative assets	-	-	-	-	-
19b. Off-balance sheet foreign currency derivative liabilities	-	-	-	-	-
20. Net foreign currency asset/(liability) position	(383.591.730)	(119.963.235)	(32.479.298)	3.960.559	53.956.925
21. Net foreign currency asset / (liability) position of monetary items (1+2a+5+6a-10-11-12a-14-15-16a)	(917.628.639)	(264.216.816)	(53.253.688)	3.880.936	48.695.492

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Foreign currency risk management (cont'd)

31 December 2015	TL Total	USD	TL	GBP	Other
1. Trade receivables	226.687.234	10.031.702	151.034.836	3.267.090	32.433.447
2a. Monetary financial assets	916.249.777	219.569.098	260.544.132	910.080	13.372.555
2b. Non monetary financial assets	-	-	-	-	-
3. Other	375.633.399	128.322.141	272.995	16.456	2.180.175
4. CURRENT ASSETS	1.518.570.410	357.922.941	411.851.963	4.193.626	47.986.177
5. Trade receivables	-	-	-	-	-
6a. Monetary financial assets	-	-	-	-	-
6b. Non monetary financial assets	-	-	-	-	-
7. Other	78.541.837	26.641.085	206.007	19.800	789.057
8. NON CURRENT ASSETS	78.541.837	26.641.085	206.007	19.800	789.057
9. TOTAL ASSETS	1.597.112.247	384.564.026	412.057.970	4.213.426	48.775.234
10. Trade payables	147.330.836	29.835.970	57.519.641	132.890	2.488.609
11. Financial liabilities	49.774.224	14.770.841	6.826.527	-	-
12a. Other liabilitites, monetary	36.906.314	177.205	32.655.077	-	3.735.996
12b. Other liabilitites, non monetary	-	-	-	-	-
13. CURRENT LIABILITIES	234.011.374	44.784.016	97.001.245	132.890	6.224.605
14. Trade payables	-	-	-	-	-
15. Financial liabilities	224.872.496	77.339.557	-	-	-
16a. Other liabilitites, monetary	-	-	-	-	-
16b. Other liabilitites, non monetary	-	-	-	-	-
17. NON CURRENT LIABILITIES	224.872.496	77.339.557	-	-	-
18. TOTAL LIABILITIES	458.883.870	122.123.573	97.001.245	132.890	6.224.605
19. Net asset / (liability) position of Off-balance sheet derivatives (19a-19b)	408.227.040	140.400.000	-	-	-
19.a Off-balance sheet foreign currency derivative assets	408.227.040	140.400.000	-	-	-
19b. Off-balance sheet foreign currency derivative liabilities	-	-	-	-	-
20. Net foreign currency asset/(liability) position	1.138.228.377	262.440.453	315.056.725	4.080.536	42.550.629
21. Net foreign currency asset / (liability) position of monetary items (1+2a+5+6a-10-11-12a-14-15-16a)	684.053.141	107.477.227	314.577.723	4.044.280	39.581.397

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Foreign currency risk management (cont'd)

Foreign currency sensitivity

The Group is exposed to foreign exchange risk arising primarily with respect to the US Dollar and Turkish Lira.

The following table details the Group's sensitivity to a 10% increase and decrease in US Dollar, and TL. 10% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated items and adjusts their translation at the period end for a 10% change in foreign currency rates.

Foreing currency sensitivity tables as of 31 December 2016 and 2015 are as follows:

31 December 2016	**Profit/(Loss)**		**Shareholders' equity**	
	If foreign currency appreciated 10%	**If foreign currency depreciated 10%**	**If foreign currency appreciated 10%**	**If foreign currency depreciated 10%**
Effect of 10% change in USD rate				
USD net asset / (liability)	(92.983.182)	92.983.182	-	-
Part of hedged from USD risk	-	-	-	-
USD net effect	**(92.983.182)**	**92.983.182**	**-**	**-**
Effect of 10% change in TL rate				
TL net asset / (liability)	(5.325.369)	5.325.369	156.902.950	(156.902.950)
Part of hedged from TL risk	-	-	-	-
TL net effect	**(5.325.369)**	**5.325.369**	**156.902.950**	**(156.902.950)**

31 December 2015	**Profit/(Loss)**		**Shareholders' equity**	
	If foreign currency appreciated 10%	**If foreign currency depreciated 10%**	**If foreign currency appreciated 10%**	**If foreign currency depreciated 10%**
Effect of 10% change in USD rate				
USD net asset / (liability)	31.250.079	(31.250.079)	-	-
Part of hedged from USD risk	40.822.704	(40.822.704)	-	-
USD net effect	**72.072.783**	**(72.072.783)**	**-**	**-**
Effect of 10% change in TL rate				
TL net asset / (liability)	31.457.772	(31.457.772)	121.925.547	(121.925.547)
Part of hedged from TL risk	-	-	-	-
TL net effect	**31.457.772**	**(31.457.772)**	**121.925.547**	**(121.925.547)**

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Interest rate risk management

The Group is exposed to interest rate risk as the Group borrows funds at floating interest rates. The risk is managed by the Group by maintaining an appropriate mix between floating rate borrowings, by the use of interest rate swap contracts based on the approved policies.

<u>Foreign currency sensitivity</u>

The Group's distribution of interest rate-sensitive financial instruments is as follows:

	31 December 2016		**31 December 2015**	
	Floating rate	**Fixed rate**	**Floating rate**	**Fixed rate**
Finance leases	2.438.000.537	238.565.053	1.364.807.077	43.803.178
Interest swap agreements not subject to hedge accounting (net)	762.555	-	(35.113)	-

For floating rate liabilities, the analysis is prepared assuming the amount of liability outstanding at the balance sheet date was outstanding for the whole year.

If interest rates had been 0,5% lower/higher during the reporting period keeping all other variables constant:

The Group's profit before tax would have increased/decreased by TL 9.443.891 (2015: TL 8.278.936). This is mainly attributable to the Company's exposure to interest rates on its variable rate obligations under finance leases.

NOTE 32 - NATURE AND LEVEL OF RISKS DERIVING FROM FINANCIAL INSTRUMENTS (cont'd)

Financial Risk Factors (cont'd)

Price risk management

Fuel price risk management

The Group is exposed to commodity risk due to the significant of fuel purchases to its business. Fuel prices have been subject to wide fluctuations based on geopolitical issues, exchange rate fluctuations, supply and demand as well as market speculation. The fluctuations in fuel prices have had a significant impact on the cost of sales, and results of operations of the Group.

The Group manages its risk to fuel prices through the use of derivative financial instruments. The Group's policy since 2011 includes a primary non-discretionary program for the first 30% of anticipated fuel consumption and a supplemental discretionary program for an additional 30% of our anticipated fuel consumption up to twelve months. Both programs use swap and option arrangements on jet fuel and Brent oil. There has been no change to the Group's exposure to market risks or the manner in which it manages and measures the risk.

Fuel price sensitivity

The Group entered into fuel purchase and option forward contracts in order to manage the cash flow risks arising from fuel purchases. Due to forward fuel purchase and option forwward contracts subject to hedge accounting, as a result of a 1% increase in fuel prices, the shareholders' equity of the Group will increase by TL 443.862 (2015: TL 5.272.628) excluding deferred tax effect. In case of a 1% decrease in fuel prices, the shareholders' equity of the Group will decrease by TL 443.862 (2015: TL 5.272.628) excluding deferred tax effect.

NOTE 33 - FINANCIAL INSTRUMENTS (FAIR VALUE AND HEDGE ACCOUNTING DISCLOSURES)

Fair Value of Financial Instruments

31 December 2016	Loans and receivables	Derivative instruments which are reflected at fair value in shareholders' equity	Derivative instruments which are reflected at fair value in profit/loss	Financial liabilities at amortized cost	Carrying amount (*)	Note
Financial assets						
Cash and cash equivalents	692.270.625	-	-	-	692.270.625	35
Trade receivables	212.269.499	-	-	-	212.269.499	6
- Related party	-	-	-	-	-	
- Other	*212.269.499*	-	-	-	*212.269.499*	*6*
Other receivables	139.792.528	-	-	-	139.792.528	7
- Related party	*1.097.807*	-	-	-	*1.097.807*	*5*
- Other	*138.694.721*	-	-	-	*138.694.721*	
Pre-delivery payment for purchase of aircraft	404.731.495	-	-	-	404.731.495	9
Derivative financial assets	-	364.813	762.555	-	1.127.368	30
Financial liabilities						
Obligations under financial leases	-	-	-	2.676.565.590	2.676.565.590	31
Trade payables	-	-	-	317.877.743	317.877.743	6
- Related party	-	-	-	*1.455.390*	*1.455.390*	*5*
- Other	-	-	-	*316.422.353*	*316.422.353*	
Passenger airport fees liability	-	-	-	60.671.024	60.671.024	9
Derivative financial liabilities	-	-	-	-	-	30

(*) The Group’s management believes that carrying amount of financial instruments approximates their fair value.

NOTE 33 - FINANCIAL INSTRUMENTS (FAIR VALUE AND HEDGE ACCOUNTING DISCLOSURES) (cont'd)

Fair Value of Financial Instruments (cont'd)

31 December 2015	Loans and receivables	Derivative instruments which are reflected at fair value in shareholders' equity	Derivative instruments which are reflected at fair value in profit/loss	Financial liabilities at amortized cost	Carrying amount (*)	Note
Financial assets						
Cash and cash equivalents	954.974.093	-	-	-	954.974.093	35
Trade receivables	294.629.623	-	-	-	294.629.623	6
- Related party	-	-	-	-	-	
- Other	*294.629.623*	-	-	-	*294.629.623*	*6*
Other receivables	218.789.987	-	-	-	218.789.987	7
- Related party	*278.844*	-	-	-	*278.844*	*5*
- Other	*218.511.143*	-	-	-	*218.511.143*	
Pre-delivery payment for purchase of aircraft	269.313.947	-	-	-	269.313.947	9
Derivative financial assets	-	2.341.144	-	-	2.341.144	30
Financial liabilities						
Bank borrowings	-	-	-	6.826.527	6.826.527	31
Obligations under financial leases	-	-	-	1.408.610.255	1.408.610.255	31
Trade payables	-	-	-	245.899.093	245.899.093	6
- Related party	-	-	-	*1.013.200*	*1.013.200*	*5*
- Other	-	-	-	*244.885.893*	*244.885.893*	
Passenger airport fees liability	-	-	-	61.623.605	61.623.605	9
Derivative financial liabilities	-	30.014.587	148.150.947	-	178.165.534	30

(*) The Group's management believes that carrying amount of financial instruments approximates their fair value.

NOTE 33 - FINANCIAL INSTRUMENTS (FAIR VALUE AND HEDGE ACCOUNTING DISCLOSURES) (cont'd)

Fair Value of Financial Instruments (cont'd)

The fair values of financial assets and financial liabilities are determined and grouped as follows:

- Level 1: the fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices:

- Level 2: the fair value of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions; and

- Level 3: the fair value of financial assets and liabilities are determined by the input that does not reflect an actual data observed in the market while finding the fair value of an asset or liability.

Financial assets / (Financial liabilities)	**Fair value as at**		**Fair value hierarchy**	**Valuation technique**
	31 December 2016	**31 December 2015**		
Option forward contracts	364.813	-	Level 2	Discounted cash flow method
Fuel purchase forward contracts	-	(30.014.587)	Level 2	Discounted cash flow method
Currency forward contracts	-	2.341.144	Level 2	Discounted cash flow method
Chooser forward contracts	-	(148.115.834)	Level 2	Discounted cash flow method
Interest rate swap contracts	762.555	(35.113)	Level 2	Discounted cash flow method

31 December 2016	**Fuel purchase forward contracts**	**Currency forward contracts**	**Chooser forward contracts**	**Option forward contracts**	**Interest rate swap contracts**	**Total**
Fair value:						
Opening	(30.014.587)	2.341.144	(148.115.834)	-	(35.113)	(175.824.390)
Fair value increase / (decrease)						
Reflected at equity	30.014.587	(2.341.144)	-	364.813	-	28.038.256
Reflected at profit or loss	-	-	148.115.834	-	797.668	148.913.502
Closing	**-**	**-**	**-**	**364.813**	**762.555**	**1.127.368**
Assets	-	-	-	364.813	762.555	1.127.368
Total net assets and liabilities	**-**	**-**	**-**	**364.813**	**762.555**	**1.127.368**

NOTE 33 - FINANCIAL INSTRUMENTS (FAIR VALUE AND HEDGE ACCOUNTING DISCLOSURES) (cont'd)

Fair Value of Financial Instruments (cont'd)

31 December 2015	Fuel purchase forward contracts	Currency forward contracts	Chooser forward contracts	Interest rate swap contracts	Total
Fair value:					
Opening	(72.619.073)	5.925.404	(172.304.604)	651.481	(238.346.792)
Fair value increase / (decrease)					
Reflected at equity	42.604.486	2.341.144	-	-	44.945.630
Reflected at profit or loss	-	(5.925.404)	24.188.770	(686.594)	17.576.772
Closing	**(30.014.587)**	**2.341.144**	**(148.115.834)**	**(35.113)**	**(175.824.390)**
Assets	-	2.341.144	-	-	2.341.144
Liabilities	(30.014.587)	-	(148.115.834)	(35.113)	(178.165.534)
Total net assets and liabilities	**(30.014.587)**	**2.341.144**	**(148.115.834)**	**(35.113)**	**(175.824.390)**

As of 31 December 2016, the Group has fuel purchase forward contracts subject to hedge accounting on the purpose of covering 3,7% (2015: 41,2%) of the expected total fuel consumption for the upcoming one-year period. Weighted average price of these contracts is US Dollars 544,4 (2015: US Dollars 435,8).

NOTE 33 - FINANCIAL INSTRUMENTS (FAIR VALUE AND HEDGE ACCOUNTING DISCLOSURES) (cont'd)

Derivative Instruments Risk Management

31 December 2016	Positive fair value	Negative fair value	Total
Option forward contracts	364.813	-	364.813
Fair values of derivative instruments subject to hedge accounting	364.813	-	364.813
Interest rate swap contracts	762.555	-	762.555
Fair values of derivative instruments not subject to hedge accounting	762.555	-	762.555
Total	**1.127.368**	**-**	**1.127.368**

31 December 2015	Positive fair value	Negative fair value	Total
Currency forward contracts	2.341.144	-	2.341.144
Fuel purchase forward contracts for hedging against cash flow risk of fuel price	-	(30.014.587)	(30.014.587)
Fair values of derivative instruments subject to hedge accounting	2.341.144	(30.014.587)	(27.673.443)
Chooser forward contracts	-	(148.115.834)	(148.115.834)
Currency swap contracts	-	(35.113)	(35.113)
Fair values of derivative instruments not subject to hedge accounting	-	(148.150.947)	(148.150.947)
Total	**2.341.144**	**(178.165.534)**	**(175.824.390)**

NOTE 34 - EVENTS AFTER THE REPORTING PERIOD

None.

NOTE 35 - EXPLANATIONS RELATED TO STATEMENT OF CASH FLOW

The details of cash and cash equivalents as of 31 December 2016 and 2015 are as follows:

	31 December 2016	31 December 2015
Cash on hand	417.322	142.151
Cash at banks	691.853.303	954.831.942
- Demand deposits	60.841.952	48.690.232
- Time deposits	631.011.351	906.141.710
	692.270.625	**954.974.093**

The weighted average interest rates of time deposits are as presented below:

31 December 2016	Weighted average interest rates	Total
USD deposits	3,32%	393.498.961
TL deposits	9,74%	51.897.924
EUR deposits	1,05%	185.614.466
		631.011.351

31 December 2015	Weighted average interest rates	Total
USD deposits	2,61%	618.556.817
TL deposits	13,46%	259.118.343
EUR deposits	1,19%	24.754.305
GBP deposits	1,00%	2.365.450
CHF deposits	0,30%	1.346.795
		906.141.710

All of the time deposits as of 31 December 2016 and 2015 have maturities less than 90 days.