

**TÜRK HAVA YOLLARI
ANONİM ORTAKLIĞI
US GAAP CONSOLIDATED
FINANCIAL STATEMENTS
FOR THE YEAR ENDED
DECEMBER 31, 2006**

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Türk Hava Yolları Anonim Ortaklığı

1. We have audited the accompanying consolidated balance sheet of Türk Hava Yolları Anonim Ortaklığı ("the Company") as at 31 December 2006, and the consolidated statement of income, the consolidated statement of changes in shareholders' equity and the consolidated statement of cash flows for the year ended 31 December 2006, all expressed in thousand US Dollars. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.
2. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.
3. In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of 31 December 2006, and the results of its operations and its cash flows for the year ended 31 December 2006 in conformity with accounting principles generally accepted in the United States of America.

Can Uluslararası Bağımsız Denetim ve S.M.M.M. A.Ş.
A Member Firm of INPACT International

İsmail USLU
Partner

20 April 2007, İstanbul, Turkey

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
CONSOLIDATED BALANCE SHEETS
AS AT DECEMBER 31, 2006 AND 2005

ASSETS	Note	December 31, 2006 US \$ 000	December 31, 2005 US \$ 000
Cash and Cash Equivalents	5	259,717	359,898
Accounts Receivable (net)	6	194,507	142,791
Due from Related Parties (Short-Term)	7	15,167	723
Inventories	8	96,419	62,780
Prepaid Taxes	21	3,715	9,960
Short Term Deferred Tax Assets	21	17,276	47,272
Other Receivables and Current Assets	9	40,167	39,185
Total Current Assets		626,968	662,609
Due from Related Parties (Long-Term)	7	10,538	-
Investments at Equity	10	16,278	13,035
Financial Assets Available For Sale (net)	10	4,122	14,321
Tangible Assets (net)	11	2,045,808	1,473,905
Intangible Assets (net)	11	5,035	3,833
Advances Given for Aircraft	12	258,075	427,165
Other Long Term Receivables and Assets	13	16,831	8,614
Total Non-Current Assets		2,356,687	1,940,873
Total Assets		2,983,655	2,603,482

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
CONSOLIDATED BALANCE SHEETS
AS AT DECEMBER 31, 2006 AND 2005

LIABILITIES	Note	December 31, 2006 US \$ 000	December 31, 2005 US \$ 000
Bank Borrowings	14	3,454	270,708
Short Term Portion of Finance Lease Obligations	15	155,606	133,472
Accounts Payable		223,225	188,016
Due to Related Parties	16	10,578	5,979
Other Short Term Payables	17	32,421	27,108
Deposits and Advances Received	18	35,685	41,458
Passenger Flight Liabilities	19	186,679	143,197
Other Accrued Liabilities	20	85,143	68,719
Total Current Liabilities		732,791	878,657
Bank Borrowings	14	25,897	-
Long Term Portion of Finance Lease Obligations	15	1,027,272	638,494
Deposits and Advances Received	18	6,395	5,309
Manufacturers' Credit (net)	22	19,065	2,602
Long Term Deferred Tax Liabilities	21	79,182	102,926
Retirement Pay Liability	23	83,455	84,693
Total Non-Current Liabilities		1,241,266	834,024
SHAREHOLDERS' EQUITY			
Share Capital	24	775,381	775,381
Reserves	24	86,003	55,327
Accumulated Profit		148,214	60,093
TOTAL SHAREHOLDERS' EQUITY		1,009,598	890,801
Total Liabilities and Shareholders' Equity		2,983,655	2,603,482

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	Not e	December 31, 2006 US \$ 000	December 31, 2005 US \$ 000
Operating Revenues	28	2,809,161	2,316,327
Operating Expenses	29	(2,729,256)	(2,176,118)
OPERATING PROFIT		79,905	140,209
Income from Other Operations	31	64,283	72,619
Loss from Other Operations	32	(35,332)	(24,871)
INCOME BEFORE FINANCIAL EXPENSE AND TAXATION		108,856	187,957
Financial Expenses (net) (Net of Translation Gains and Losses)	30	(13,855)	(24,558)
INCOME BEFORE TAXATION		95,001	163,399
Taxation Charge	21	(6,880)	(32,469)
NET PROFIT FOR THE YEAR		88,121	130,930
Basic Earnings per Share (US \$, in Full)	4.16	0.0005	0.0007

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
Notes to the Financial Statements

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	<u>Share Capital</u> <u>US \$ 000</u>	<u>Reserves</u> <u>US \$ 000</u>	<u>Accumulated</u> <u>Profit / Losses</u> <u>US \$ 000</u>	<u>Total</u> <u>US \$ 000</u>
Balances at December 31, 2004	775,381	55,327	(70,837)	759,871
Profit for The Year	-	-	130,930	130,930
Balances at December 31, 2005	<u>775,381</u>	<u>55,327</u>	<u>60,093</u>	<u>890,801</u>
Profit for The Year	-	30,676	88,121	118,797
Balances at December 31, 2006	<u>775,381</u>	<u>86,003</u>	<u>148,214</u>	<u>1,009,598</u>

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
Notes to the Financial Statements

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit Prior to Taxation	95,001	163,399
Adjustments to reconcile net profit for the period to net cash provided by operating activities:		
Depreciation	207,827	151,502
Provision for Retirement Pay Liability	14,189	15,465
Interest Income	(18,293)	(31,564)
(Gain) / Loss on Sales of Fixed Asset	163	(600)
Translation (Gain)/ Loss on Deferred Tax Liability	280	(15,469)
Increase /(Decrease) in Provision for Diminution in Value of Fixed Assets	5,018	(36,527)
Income from Financial Investment Accounted per Equity Method	(3,243)	(587)
Interest Expense	50,899	43,076
Change in Provision for Diminution in Value of Financial Assets Available for Sale	1,476	3,773
Movement in Manufacturers' Credit	16,463	817
Amortization of Deferred Income from USAŞ Share Transfer	(2,742)	(990)
(Decrease) / Increase in Provision for Doubtful Receivables	816	(109)
Expensed Portion of Prepaid Tax of Previous Period	-	1,773
Operating Profit Before Working Capital Changes	367,854	293,959
Change in Trade Receivables	(52,532)	(24,520)
Change in Due From Related Parties	(24,982)	(117)
Change in Inventories	(33,639)	(20,062)
Change in Other Short and Long Term Receivables	(9,199)	(11,499)
Change in Trade Payables	35,209	49,018
Change in Due to Related Parties	4,599	1,130
Change in Accrued Expenses and Other Payables	24,479	15,345
Change in Deposits and Advances Received	(4,687)	11,575
Change in Passenger Flight Liabilities	43,482	26,684
Retirement Benefits Paid	(15,427)	(5,116)
Interest Paid	(50,899)	(43,076)
Prepaid Taxes	3,715	(9,960)
Reimbursement of Prepaid Tax in Previous Period	-	36,455
Net Cash Provided by Operating Activities	287,973	304,815
CASH FLOWS RELATED TO INVESTING ACTIVITIES		
Cash From Sales of Financial Assets	8,723	672
Cash Proceeds from Sale of Fixed Assets	6,956	44,827
Interest Received	18,293	31,564
Acquisition of Fixed Assets	(760,771)	(355,810)
Change in Advances Given for Aircraft	169,090	(131,426)
Net Cash Used in Investing Activities	(557,709)	(410,173)
Change in Finance Lease Obligations	410,912	(92,680)
Change in Bank Borrowings	(241,357)	270,498
Net Cash Provided by Financing Activities	169,555	177,818
NET (DECREASE) / INCREASE IN CASH AND CASH EQUIVALENTS	(100,181)	87,461
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	359,898	272,437
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	259,717	359,898

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the Financial Statements

1 THE COMPANY'S OPERATIONS

Türk Hava Yolları A.O. ("the Company" or "THY") was incorporated in Turkey in 1933. The principal activity of the Company is domestic and international air transportation of passengers and cargo.

As of December 31, 2006, the shareholders and their respective shareholdings in the Company were as follows:

Turkish Republic Prime Ministry Privatization Administration	49.12 %
Others	50.88 %
Total	<u>100.00 %</u>

The total number of employees working for Türk Hava Yolları A.O. and its subsidiary as of December 31, 2006 is 12,807 (December 31, 2005: 11,121). The average number of employees working for the Company in 2006 and 2005 is 12,778 and 11,151 respectively.

2 BASIS OF PRESENTATION OF FINANCIAL STATEMENTS

The Company maintains its books of account and prepares its statutory financial statements ("Statutory Financial Statements") in accordance with accounting principles in the Turkish Commercial Code (the "TCC") and tax legislation and generally accepted accounting principles promulgated by Capital Markets Board ("CMB"). The accompanying financial statements are based on these statutory records, with adjustments and reclassifications for the purpose of fair presentation in accordance with Accounting Principles Generally Accepted in the United States of America ("US GAAP").

Principles of Translation of Financial Statements into US \$:

Remeasurement of the local currency denominated financial statements into US \$ has been performed in accordance with the provisions of SFAS No 52 "Foreign Currency Translation", as they relate to hyperinflationary economies. The objective of this remeasurement process is to produce the same results that would have been reported if the accounting records had been kept in US \$.

SFAS 52 defines a hyperinflationary economy as one that has cumulative inflation of approximately 100% or more over a three-year period. Such cumulative rates in Turkey is 32.8 % for the three years ended December 31, 2006 based on the wholesale price index announced by the Turkish State Institute of Statistics. (December 31, 2005: 35.6 %).

Although the three year cumulative inflation rate was below the rate indicated in the preceding paragraph, since majority of the people keep their savings in foreign currencies, the prices of services and goods are set in terms of foreign currencies, interest rates and wages are expressed in terms of the inflation indexes, and the market prices are determined taking into account the losses due to the credit sales including the short term transactions, the economy shows the characteristics of a hyperinflationary environment and therefore SFAS 52 was applied to the accompanying financial statements.

Non-monetary assets and liabilities and revenues and expenses related to non-monetary items have been translated to US \$ at historical exchange rates prevailing on the transaction date. Monetary assets and liabilities have been translated at the exchange rates prevailing at balance sheet dates. All exchange gains and losses arising from remeasurement of monetary assets and liabilities that are not denominated in US \$ have been included in the determination of net income as "translation gain or loss".

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
Notes to the Financial Statements

2 BASIS OF PRESENTATION OF THE FINANCIAL STATEMENTS (cont'd)

The comparison of the periodical change of the value of YTL against the US \$ with the Turkish countrywide Wholesale Price Index ("WPI") is set out below:

Years:	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
Currency devaluation US \$	4.75%	(0.02)%	(3.8)%	(14.6)%	13.5%
WPI inflation	11.6%	4.5%	13.8%	13.9%	30.8%

New Turkish Lira:

As of 1 January 2005, a new local measurement and reporting currency unit has been introduced as YTL (New Turkish Lira) and YKr (New Turkish cents).

Basis of Consolidation:

a) The consolidated financial statements include the accounts of the parent company, Türk Hava Yolları A.O., its Subsidiary and its Associates on the basis set out in sections (b), (c) and (d) below. The financial statements of the companies included in the scope of consolidation have been prepared as of the date of the consolidated financial statements and have been prepared in accordance with accounting and reporting principles promulgated by US GAAP applying uniform accounting policies and presentation. The results of Subsidiary and Associates are included or excluded from their effective dates of acquisition or disposal respectively.

b) Subsidiary is the entity in which the Company has power to control the financial and operating policies for the benefit of the Company through the power to exercise more than 50% of the voting rights relating to shares in the companies owned directly and indirectly by itself, otherwise having the power to exercise control over the financial and operating policies for the benefit of the Company.

The table below sets out the consolidated Subsidiary and participation rate of the Company in this subsidiary at December 31, 2006:

<u>Name of the Company</u>	<u>Principal Activity</u>	<u>Direct Participation</u>	<u>Indirect Participation</u>	<u>Country of Registration</u>
THY Teknik A.Ş.	Technical Maintenance	100%	-	Turkey

The balance sheet and statement of income of the subsidiary were consolidated on the basis of full consolidation. The carrying value of the investment held by the Company and its Subsidiary were eliminated against the related shareholders' equity. Intercompany transactions and balances between the Company and its Subsidiary were eliminated during consolidation process.

c) The Company has two associates. The participation rate of the Company is 50%, and the associates are not controlled by the Company. The entities are valued by equity method.

The table below sets out consolidated associates and indicates the proportion of ownership interest of the Company in these associates at December 31, 2006:

<u>Name of the Company</u>	<u>Principal Activity</u>	<u>Direct Participation</u>	<u>Indirect Participation</u>	<u>Country of Registration</u>
Güneş Ekspres Havacılık A.Ş.	Air Transportation	50%	-	Turkey
THY DO&CO İkrâm Hizmetleri A.Ş.	Catering Services	50%	-	Turkey

In equity method, the associate is presented on the balance sheet at net asset value and the portion of the Company from its operations is added to the income statement.

d) Other investments in which the Company has direct or indirect participation below 20% or in case of participation over 20%, has no significant influence or which are immaterial for purposes of consolidated financial statements are classified as available for sale. Available for sale investments that do not have a quoted market price in active markets and whose fair value cannot be measured reliably are carried at cost less any provision for diminution in value. Available for sale investments that have a quoted market price in active markets and whose fair values can be measured reliably are carried at fair value.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the Financial Statements

3 SEGMENTAL REPORTING

3.1 Business Segments

The Company predominantly operates in one industry segment as of December 31, 2006; the primary businesses are air transportation of passengers and cargo within, to or from Turkey and to supply maintenance service for aircrafts.

3.2. Geographical Segments

The revenue analysis is based on the destinations that the Company serves. All passenger fare and cargo revenue within Turkey is attributed to the revenue from domestic services. Revenues from both scheduled and non-scheduled international flight are attributed to destinations' geographical areas.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies followed in the preparation of the accompanying financial statements are as follows:

4.1 Revenue Recognition and Commission Expenses

Passenger fares and cargo revenues are recorded as operating revenue when the transportation service is provided. Tickets sold but not yet used are recorded as passenger flight liabilities.

The Company develops estimations using historical statistics and data for unredeemed tickets. Total estimated unredeemed tickets were recognized as operating revenue.

Commissions to agencies relating to the passenger revenue are recognized as expense when the transportation service is provided.

4.2 Inventory Valuation

Inventories are valued at the lower of cost or net realizable value using the moving weighted average cost method.

4.3. Financial Investments

The Company designates its investment portfolio in accordance with SFAS 115 ("Accounting for Certain Investments in Debt and Equity Securities") as follows:

Securities Held for Trading:

Securities held for trading are those acquired principally for the purpose of generating profit from short-term fluctuations in their price. Subsequent to initial recognition, held for trading securities are valued at their fair value if reliably measured. Gains or losses on held for trading securities are recognized in net profit or loss for the period in which they arise.

Investments Held to Maturity:

Held-to-maturity investments are securities with fixed or determinable payments and fixed maturity that the Company has the positive intent and ability to hold to maturity.

Investments Available for Sale:

Available-for-sale investments are those that the ownership rate is less than 20% and are not held for trading. Subsequent to acquisition, available for sale investments which are traded at stock markets are valued at market rate. Otherwise, they are accounted at cost.

Investments at Equity:

Investment that the ownership rate is 50% and the Company is not in a position to exercise joint control are carried at equity.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
Notes to the Financial Statements

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

4.4 Tangible and Intangible Assets

Fixed assets are recorded at historical costs at the acquisition date. The Company makes an assessment for its fixed assets at the balance sheet date in accordance with SFAS 144 (“Accounting for Impairment or Disposal of Long Lived Assets”). Tangible and intangible assets are carried at historical cost as adjusted for their recoverable values; when the recoverable amount of an asset has declined below its carrying amount, the carrying amount is reduced to reflect the decline in value. Recoverable amount is determined as higher of asset’s net selling price or its value in use. Net selling price is determined based on the Company’s management estimation developed from the international aircraft price guide. The decrease in carrying amount is recorded as impairment loss under operating expenses.

Depreciation is provided on a periodical basis for all categories of tangible and intangible assets.

The useful lives and residual values used for the depreciable assets are as follows:

	<u>Useful Life (Years)</u>	<u>Residual Value</u>
- Buildings	25-50	-
- Aircraft	15	%30
- Spare engines	15	%30
- Rotable assets	4-10	-
- Repairables	2-3	-
- Simulator	10-15	-
- Machinery and equipment	3-15	-
- Furniture and fixtures	3-15	-
- Motor vehicles	4-7	-
- Other equipments	4-15	-

4.5 Manufacturers’ Credits

Manufacturers’ credits are received against acquisition and/or lease of aircraft and engines. The Company records these credits as a reduction to the cost of the owned or financial leased assets and amortizes them over the related asset’s remaining useful life. Manufacturers’ credits related to operational leases are recorded as deferred revenue and amortized over the lease term.

4.6 Maintenance and Repair Costs

Regular maintenance and repair costs for owned and leased flight equipment are charged to operating expense as incurred. Heavy maintenance checks for owned and finance leased aircraft are expensed as incurred and delivery maintenance checks of operational leased aircraft are accrued on a periodical basis.

4.7 Frequent Flyer Program

The Company provides a frequent flyer program which is called “Miles and Smiles” in the form of free travel award to its members on accumulated mileage. The estimated cost of providing free travel, using the incremental cost method as adjusted for estimated redemption rates, is recognized as a liability and charged to operations as program members accumulate mileage.

The Company also sells mileage credits to participating partners in the “Shop & Miles” program. A portion of such revenue is deferred and amortized as transportation is provided.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

4.8 Taxation and Deferred Taxes

Provision is made in the financial statements for the Company's estimated liability to Turkish corporation tax on its results for the period. The charge for current tax is based on the results for the period as adjusted for items, which are non-assessable or disallowed.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statements carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

In accordance with SFAS 109 ("Accounting for Income Tax"), the Company does not recognize any deferred tax liability or assets for differences related to assets and liabilities that, under SFAS 52 Foreign Currency Translation, are remeasured from the local currency into the functional currency using historical exchange rates.

Further, the Company's deferred tax assets and liabilities have been remeasured into US \$ in accordance with the provisions of SFAS 109 and the translation gains and losses that result from such remeasurement have been included within the tax provision line in the financial statements.

Deferred tax is charged or credited in the statement of income.

4.9 Employee Retirement and Termination Indemnities

Employee retirement and termination benefits as required by Turkish Labor Law are recognized in the accompanying financial statements as earned. According to SFAS 106 ("Employers' Accounting for Postretirement Benefits other than Pensions") future retirement payments are discounted to their present value at the balance sheet date at an interest rate which is net of inflation rate. The interest rate included in employee retirement expense is shown in the financial result as interest expense.

4.10 Related Parties

The associates, shareholders, top managers and Board Members of the Company, in each case together with their families and companies controlled by or affiliated with them, are considered and referred to as related parties in the accompanying financial statements.

4.11 Foreign Currency Transactions

In the statutory accounts of the Company, transactions in foreign currencies are translated into New Turkish Lira at the rates of exchange ruling at the transaction dates. Assets and liabilities denominated in foreign currencies are translated at the exchange rate ruling at the balance sheet date. Gains and losses arising on settlement and translation of foreign currency items are included in the statements of income.

4.12 Leases

The Company leases aircraft, simulator, computer equipment and vehicles in the form of either finance leases or operating leases. Finance leases are reflected in the Company's balance sheet by recording finance leased assets and liabilities equal to the present value of the lease payments. The finance leased assets are depreciated over their useful lives. Operating leases are accounted for as operating expense when incurred.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

4.13 Financial Instruments

Fair value is the amount for which an asset could be exchanged or a liability settled, between knowledgeable willing parties in an arm's length transaction. Market value is the amount obtainable from the sale or payable on the acquisition, of a financial instrument in an active market, if one exists.

The estimated fair values of financial instruments have been determined by the Company using available market information and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to develop the estimated fair value. Accordingly, the estimates presented here in may not necessarily be indicative of the amounts the Company could realize in a current market exchange.

Balances with banks, receivables, contingent liabilities like letters of guarantee, letters of credit are important financial instruments which would have negative effects on the financial structure of the Company if the other party failed to comply with the terms and conditions of the agreement.

The fair values of certain financial assets carried at cost are considered to be representative of carrying values due to their short-time nature.

The Company's principal financial assets are cash and cash equivalents, accounts receivable, due from related parties and available for sale financial assets.

Book values of trade receivables and due from related parties along with the related allowances for uncollectibility are estimated to be their fair value except for discount of these receivables to their present value when they hold significant credit periods.

Güneş Ekspres Havacılık A.Ş. ("Sun Express") and THY DO&CO İkrâm Hizmetleri A.Ş. ("THY DO&CO") are accounted for using the equity method as the Company exercises a significant influence. Uçak Servisi A.Ş. ("USAŞ") is classified as available for sale investments and changes in their fair value are recognized in net profit or loss.

Financial assets, other than Sun Express, THY DO&CO and USAŞ are stated at their cost since their fair values can not be measured reliably.

Financial Liabilities

Financial liabilities are classified according to the substance of the contractual arrangements. Significant financial liabilities include bank loans, financial lease obligations and accounts payable.

Financial expenses are accounted for on an accrual basis. Accounts and other payables and due to related parties are recorded at their nominal value, which approximates their fair value.

Credit Risk

The Company's credit risk is primarily attributable to its trade receivables. The amounts disclosed in the balance sheet are net of allowances for doubtful receivables, estimated by the Company's management based on prior experience and the current economic environment. The Company has no significant concentration of credit risk, with exposure spread over a large number of counter parties and customers.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
Notes to the Financial Statements

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

4.13 Financial Instruments (cont'd)

Price Risk

- Currency Risk

The Company is exposed to exchange rate fluctuations between foreign currencies and New Turkish Lira due to the nature of its business. The major part of the Company's ticket income is in Euro, US Dollar and New Turkish Lira and the major part of its expenses is in US Dollar and New Turkish Lira.

- Interest Risk

Some of the interest rates related to leasing transactions is based on LIBOR; therefore the Company is exposed to interest rate fluctuations on international markets. The Company does not have hedging transactions to limit currency and interest rate risks.

- Market Risk

The Company invests in government bonds acquired under reverse repurchase agreements made for short periods or deposits to banks on a daily basis. Fair values of these investments fluctuate based on market conditions.

- Liquidity Risk

Usually, tickets are sold in advance and transportation is provided later. Therefore the Company takes advantage of collecting revenue in advance and incurring transportation cost later. The Company also benefits from the difference between the collection and the payment period to its counter parties.

4.14 Offsetting

Financial assets and liabilities are offset and the net amount recognized in the balance sheet when there is a legally enforceable right to set off the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

4.15 Use of Estimates

The preparation of financial statements in conformity with Generally Accepted Accounting Principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimations.

4.16 Earnings per Share

SFAS 128 "Earnings per Share" requires disclosure of basic earnings per share and diluted earnings per share (if applicable) for companies whose shares are publicly traded or which are in the process of issuing shares in a public market.

There were no dilutive equity instruments outstanding which would require the calculation of a separate diluted earnings per share.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
Notes to the Financial Statements

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

4.16 Earnings per Share (cont'd)

A summary of the weighted average number of shares outstanding during December 31, 2006 and 2005 and the basic earnings per share calculation is as follows:

	2006	2005
Number of shares outstanding at January 1 (in full)	175,000,000,000	175,000,000,000
New shares issued (cash increase) (in full)	-	-
Number of shares outstanding at December 31, (in full)	175,000,000,000	175,000,000,000
Weighted average number of shares outstanding during the period (in full)	175,000,000,000	175,000,000,000
Net profit for the year (US \$ 000)	88,121	130,930
Basic earnings per share (US \$ in full)	0.0005	0.0007

5 CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Banks	251,987	355,542
Cash	359	146
Cheques received	220	103
Other liquid assets	7,151	4,107
	<u>259,717</u>	<u>359,898</u>

Foreign currency bank balances are US \$ 225,636,144 at December 31, 2006. (2005: US \$ 220,308,579).

Time Deposits:

<u>Principal</u>	<u>Currency</u>	<u>Opening Date</u>	<u>Maturity</u>	December 31, 2006
				US \$ 000
33,582,312	YTL	04.12.2006 – 29.12.2006	04.01.2007	23,892
7,443,256	US \$	29.12.2006	04.01.2007	7,443
112,392,082	Euro	11.12.2006 – 29.12.2006	04.01.2007 – 12.01.2007	148,043
				<u>179,378</u>
				December 31, 2005
				US \$ 000
170,390,000	YTL	22.07.2005 - 30.12.2005	02.01.2006 - 30.01.2006	126,986
149,163,000	US \$	27.12.2005 - 30.12.2005	02.01.2006 - 30.01.2006	149,163
31,653,000	Euro	30.12.2005	02.01.2006	37,449
				<u>313,598</u>

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6 ACCOUNTS RECEIVABLE (NET)

Accounts receivable consists of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Trade receivables	210,024	156,840
Discount on receivables	(2,392)	(1,740)
Provision for doubtful receivables	(13,125)	(12,309)
	<u>194,507</u>	<u>142,791</u>

7 DUE FROM RELATED PARTIES

Short term due from related parties consists of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
THY DO&CO İkrım Hizmetleri A.Ş.	14,110	-
Güneş Ekspres Havacılık A.Ş. (Sun Express)	1,057	723
	<u>15,167</u>	<u>723</u>

Long term due from related parties consists of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
THY DO&CO İkrım Hizmetleri A.Ş.	10,538	-
	<u>10,538</u>	<u>-</u>

Due from THY DO&CO İkrım Hizmetleri A.Ş. comprised of short and long term credit receivables at amounts of Euro 10,700,000, Euro 8,000,000 respectively, in total Euro 18,700,000.

8 INVENTORIES

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Spare parts, flight equipment	84,756	51,903
Other inventories	11,663	10,877
	<u>96,419</u>	<u>62,780</u>

9 OTHER RECEIVABLES AND CURRENT ASSETS

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Prepaid sales commissions	9,975	8,125
Prepaid operating lease expenses	8,080	3,960
Tax to be refunded	4,998	2,210
Third party maintenance service income accrual	4,121	7,547
Interline passenger income accrual	2,765	2,864
Due from insurance firms	2,624	2,379
Other prepaid expenses	1,585	7,659
Income accruals	965	-
Receivables from personnel	618	488
Business advances given	549	72
Prepaid rent expenses	474	428
Prepaid aircraft financing expense	301	-
Receivable from SITA deposit certificates	134	116
VAT deductible	20	326
Other receivables	2,958	3,011
	<u>40,167</u>	<u>39,185</u>

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10 FINANCIAL ASSETS

i) The associates accounted for using the equity method are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
THY DO&CO İkrım Hizmetleri A.Ş.	10,813	-
Güneş Ekspres Havacılık A.Ş. (Sun Express)	5,465	13,035
	<u>16,278</u>	<u>13,035</u>

ii) Financial assets available for sale are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Uçak Servisi A.Ş. (USAŞ)	5,217	4,429
Increase / (decrease) in value of USAŞ shares	(1,844)	4,108
Sita Inc.	737	737
Emek İnşaat ve İşletme A.Ş.	12	12
France Telecom shares	-	8,723
Diminution in value of France Telecom shares	-	(3,688)
	<u>4,122</u>	<u>14,321</u>

Tender for the catering service was won by Uçak Servisi A.Ş. (USAŞ) and service agreement was signed on January 1, 2002. Based on share transfer agreement made between USAŞ's main shareholder Gate Gourmet Holding A.G. (GGH) and the Company, USAŞ will transfer its group B free shares corresponding to 15% of its total share capital to the Company. According to the agreement, ownership of first 10% of shares was transferred on September 21, 2002, 1.25% of shares was transferred on January 2, 2003, 1.25% of shares was transferred on January 2, 2004, 1.25% of shares was transferred on January 3, 2005 and 1.25% of shares was transferred on January 2, 2006 and the transfer was completed to 15%. Consequently, 1,567,500,000 shares corresponding to 15% of USAŞ's share capital, transferred to the Company, were recorded to "financial assets" and "deferred income" accounts at market value of US \$ 11,981,860. "Deferred income" amount is amortized to income during 5 years catering service agreement on a straight-line basis. The Company has sold 342 million USAŞ shares in 2003, 1,026 million shares in 2005 and 1,026 million shares in 2006 at İstanbul Stock Exchange.

USAŞ gave 1,852,500,000 free shares to the Company based on the decision taken in Non-general Assembly held on December 8, 2004 related to the share capital increase originated from the inflation adjustment difference arising from capital restatement.

Sun Express's total assets and equity are US \$ 35,063,772 and US \$ 6,299,727 respectively at December 31, 2006. (December 31, 2005: US \$ 37,075,480 and US \$ 17,855,634).

THY DO&CO İkrım Hizmetleri A.Ş. was established with US \$ 39,556,962 capital on September 27, 2006. THY DO&CO İkrım Hizmetleri A.Ş.'s total assets and equity are US \$ 76,775,555 and US \$ 21,626,393 respectively at December 31, 2006.

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10 FINANCIAL ASSETS (cont'd)

Details of the Company's long-term financial assets at December 31, 2006 are as follows:

<u>Name of the Company</u>	<u>Place of Incorporation and Operation</u>	<u>Proportion of Ownership Interest</u>	<u>Proportion of Voting Power Held</u>	<u>Principal Activity</u>
Güneş Ekspres Havacılık A.Ş. (Sun Express)	Turkey	50%	50%	Air transportation
THY DO&CO İkrâm Hizmetleri A.Ş.	Turkey	50%	50%	Catering services
Uçak Servisi A.Ş.(USAŞ)	Turkey	3% (*)	3% (*)	Catering
Emek İnşaat ve İşletme A.Ş.	Turkey	0,3%	0,3%	Construction
Sita Inc.	Holland	Less than 0,1%	Less than 0,1%	Information & telecommunication serv.

(*) As of December 31, 2005: 4,75% .

11 TANGIBLE AND INTANGIBLE ASSETS (NET)

Tangible assets comprised the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Tangible assets (net)	2,041,033	1,466,843
Advances given for other tangible fixed assets	4,775	7,062
	<u>2,045,808</u>	<u>1,473,905</u>

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11 TANGIBLE AND INTANGIBLE ASSETS (NET) (cont'd)

	Land, Land Improvements & Building	Technical Equipments, Simulators and Vehicles	Other Equipments, Fixtures and Software	Aircraft and Spare Engines	Rotables and Repeirable Spare Parts	Construction In Progress	Total Owned Assets	Leased Aircraft	Other Leased Fixed Assets & Simulators	Total Leased Assets	Total
<u>Cost</u>											
Opening balance 1 January 2006	66,834	130,801	93,229	866,123	194,554	1,214	1,352,755	1,347,273	7,588	1,354,861	2,707,616
Transfers from finance leases	-	1,872	-	219,026	-	-	220,898	(213,310)	(7,588)	(220,898)	-
Additions	1,150	22,183	5,652	30,102	100,840	286	160,213	594,661	-	594,661	754,874
Disposals	(277)	(11,700)	(10,510)	-	(64,759)	(1,010)	(88,256)	-	-	-	(88,256)
Revaluation	32,297	-	-	-	-	-	32,297	-	-	-	32,297
Closing balance December 31, 2006	100,004	143,156	88,371	1,115,251	230,635	490	1,677,907	1,728,624	-	1,728,624	3,406,531
<u>Accumulated Depreciation</u>											
Opening balance 1 January 2006	19,704	113,793	82,977	430,921	84,625	-	732,020	370,446	2,756	373,202	1,105,222
Transfers from finance leases	-	1,683	-	99,573	-	-	101,256	(98,500)	(2,756)	(101,256)	-
Depreciation for the year	1,164	5,565	3,659	39,553	88,787	-	138,728	67,113	-	67,113	205,841
Disposal	(172)	(11,371)	(9,830)	-	(64,759)	-	(86,132)	-	-	-	(86,132)
Closing balance December 31, 2006	20,696	109,670	76,806	570,047	108,653	-	885,872	339,059	-	339,059	1,224,931
Accumulated impairment	-	-	-	119,783	-	-	119,783	20,784	-	20,784	140,567
December 31, 2006 net book value	79,308	33,486	11,565	425,421	121,982	490	672,252	1,363,781	-	1,368,781	2,041,033
December 31, 2005 net book value	47,130	17,008	10,252	328,927	109,929	1,214	514,460	947,551	4,832	952,383	1,466,843

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11 TANGIBLE AND INTANGIBLE ASSETS (NET) (cont'd)

Intangible assets comprised the following:

	Rights	Leasehold Improvements	Total
Cost			
Opening balance 1 January 2006	29,306	9,906	39,212
Additions	2,763	425	3,188
Disposals	(3)	-	(3)
Closing balance 31 December 2006	<u>32,066</u>	<u>10,331</u>	<u>42,397</u>
Accumulated Depreciation			
Opening balance 1 January 2006	25,873	9,506	35,379
Amortization charge for the period	1,691	295	1,986
Disposals	(3)	-	(3)
Closing balance 31 December 2006	<u>27,561</u>	<u>9,801</u>	<u>37,362</u>
31 December 2006 net book value	<u>4,505</u>	<u>530</u>	<u>5,035</u>
31 December 2005 net book value	<u>3,432</u>	<u>401</u>	<u>3,833</u>

12 LONG TERM ADVANCES GIVEN FOR AIRCRAFT

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Prepayments for aircraft purchases	254,934	425,199
Advances given for operating leases	3,141	1,966
	<u>258,075</u>	<u>427,165</u>

13 OTHER LONG TERM RECEIVABLES AND ASSETS

Other long term receivables and assets consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Maintenance reserve for engines	4,061	-
Prepaid Eximbank USA guarantee and exposure fee	3,413	4,389
Income accruals	2,666	-
Prepaid operating lease expenses	2,612	279
Deposits given	1,450	988
Prepaid aircraft financing expense	1,226	1,541
Due from personnel	702	750
Receivables from SITA deposit certificate	701	599
Other receivables	-	68
	<u>16,831</u>	<u>8,614</u>

14 BANK BORROWINGS

Short-term bank borrowings comprised the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Bank Borrowings (*)	3,188	270,460
Other (**)	266	248
	<u>3,454</u>	<u>270,708</u>

Long-term bank borrowings comprised the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Bank Borrowings (*)	25,897	-
	<u>25,897</u>	<u>-</u>

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14 BANK BORROWINGS (cont'd)

(*) Short-term portion of long-term bank borrowing is as follows at December 31, 2006:

<u>Bank Name</u>	<u>Maturity</u>	<u>Original Amount</u>	<u>Interest Accruals</u>
Akbank	15.08.2009	2,959,707 US \$	228,368 US \$

Long-term bank borrowing is as follows at December 31, 2006:

<u>Bank Name</u>	<u>Maturity</u>	<u>Original Amount</u>	<u>Interest Accruals</u>
Akbank	15.08.2009	25,897,440 US \$	-

Bank Borrowings comprised the following short-term bank credit at December 31, 2005:

<u>Bank Name</u>	<u>Maturity</u>	<u>Original Amount</u>	<u>Interest Accruals</u>
T.İş Bankası / Citibank NA London	31.03.2006	270,000,000 US \$	459,998 US \$

(**) Other bank borrowings consist of overnight interest free borrowings for the purpose of settlement of tax and social security premium payments.

15 FINANCE LEASE OBLIGATIONS

The future lease rental payments under finance leases are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Not later than one year	208,626	164,745
Between 1 – 5 years	732,433	521,294
Over 5 years	516,227	223,436
	<u>1,457,286</u>	<u>909,475</u>
Less: Future interest expense	<u>(274,408)</u>	<u>(137,509)</u>
Present value of future rentals shown in the balance sheets	<u>1,182,878</u>	<u>771,966</u>
Represented by :		
Current liabilities	155,606	133,472
Long term liabilities	1,027,272	638,494
	<u>1,182,878</u>	<u>771,966</u>
Interest Range:		
Floating rate obligations	1,088,790	732,006
Fixed rate obligations	94,088	39,960
	<u>1,182,878</u>	<u>771,966</u>

As of 31 December 2006, the US Dollar and Euro denominated lease obligations' interest rates for the fixed rate obligations are between 4.075% and 5.59%; and for the floating rate obligations are on a margin ranging between EURIBOR minus 0.01% and LIBOR minus 0.057% and LIBOR plus 3.00%.

16 DUE TO RELATED PARTIES

Due to related parties consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Uçak Servisi A.Ş. (USAŞ)	8,179	5,637
Sun Express	2,399	342
	<u>10,578</u>	<u>5,979</u>

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17 OTHER SHORT TERM AND LONG TERM PAYABLES

Other short term payables consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Taxes and funds payable	18,208	12,077
Social security premiums payable	12,022	11,060
Debt to personnel	267	206
Deferred income from USAŞ share transfer	-	2,742
Other liabilities	1,924	1,023
	<u>32,421</u>	<u>27,108</u>

18 DEPOSITS AND ADVANCES RECEIVED

Short term advances received consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Advances received for mileage credit sales	13,088	16,135
MCO advances	13,603	11,536
Advances received for finance and operating leases	3,322	858
Deposits and guarantees received	3,094	2,769
Charter advances	1,485	2,544
E-pos ticket advance	499	7,211
Other advances received	594	405
	<u>35,685</u>	<u>41,458</u>

Long term advances received consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Deposits and advances received	6,395	5,309
	<u>6,395</u>	<u>5,309</u>

19 PASSENGER FLIGHT LIABILITIES

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Flight liability – advanced ticket sales	152,244	115,023
Flight liability resulting from sales of mileage	34,435	28,174
	<u>186,679</u>	<u>143,197</u>

20 OTHER ACCRUED LIABILITIES

Other accrued liabilities consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Accrued frequent flyer liability	30,083	22,788
Accrued salaries	15,491	13,410
Sales incentive premium accrual	13,679	4,982
Accrued maintenance costs	9,442	9,380
Expense accruals of insurance premiums	7,551	-
Accruals for other expenses	4,916	-
Provision for legal claims	3,945	6,859
Other liabilities	36	11,300
	<u>85,143</u>	<u>68,719</u>

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21 TAXATION

Corporate tax payable is as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Provision for corporate tax payable	5,104	-
Prepaid taxes and funds	(3,715)	(9,960)
	<u>1,389</u>	<u>(9,960)</u>

Tax expense is as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Deferred tax expense	-	-
Current period tax expense	6,880	32,469
Tax expense	<u>6,880</u>	<u>32,469</u>

Turkish tax legislation does not permit a parent company, its subsidiaries, joint ventures and associates to file a consolidated tax return. Therefore, provisions for taxes, as reflected in these consolidated financial statements, have been calculated on a separate-entity basis.

Corporate Income Tax Law numbered 5520 was published in the official gazette numbered 26205 dated 21 June 2006 and came into effect immediately. Herewith, Corporate Income Tax Law numbered 5422 has been abolished.

The corporate tax rate of the fiscal year 2006 is 20% (30% those for benefiting from investment allowances.) (2005: 30%). Corporate tax is payable at a rate of 20% on the total income of the Company after adjusting for certain disallowable expenses, exempt income and allowances. The annual corporate income tax return is required to be filled in the period between the 1st and 25th days of the fourth month following the close of the related fiscal year. Payments can be made up until the end of the month in which the tax return is to be filed.

In accordance with Income Tax Law Temporary Article 69, investment allowances available as of 31 December 2005 due to insufficiency of profit and transferable to next years; depending on taxpayers' choice can be deducted from the profits of 2006, 2007 and 2008. Investment allowances can be forwarded to next years by restatement with WPI.

In case of benefiting from investment allowances, the Corporate Tax rate is 30 % instead of 20%. Taxpayers have the option to benefit from investment allowances in all the years 2006, 2007 and 2008 or in any of these years.

The parent company preferred to deduct the investment allowances of 2005 from the earnings in 2006. Therefore, the applicable current corporate tax rate is 30%. However, since the parent company assumes that investment allowances will not be benefited in 2007 and in the following years, and due to the fact that the deferred tax assets and liabilities are of long-term, deferred tax rate is applied as 20%.

Corporations are required to pay advance corporation tax quarterly, at the current rate on their corporate income. Advance tax is to be filed in the following second month's 14th day and paid on 17th day. Advance tax paid by corporations is credited against the annual corporation tax liability. The balance of the advance tax paid may be refunded or used to set off against other liabilities to the government.

Under the Turkish taxation system, tax losses can be carried forward to offset against future taxable income for up to 5 years. Tax losses cannot be carried back to offset profits from previous periods.

In Turkey, there is no procedure for a final and definitive agreement on tax assessments. Companies file their tax returns within the 25th of the fourth month following the close of the related financial year. Tax authorities have the right to audit tax declarations and accounting records for 5 years, and may issue re-assessment based on their findings.

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21 TAXATION (cont'd)

Except for the dividends paid to non-resident corporations, which have a representative office in Turkey, or resident corporations, dividends that are paid to non-resident corporations or corporations exempt from taxation in accordance with Income Tax Law article 75 paragraph 2 lines (1), (2) and (3) are subject to withholding tax at the rate of 15%. An increase in capital via issuing bonus shares is not considered as a profit distribution and thus does not incur withholding tax.

Deferred Tax:

The Group recognized deferred tax assets and liabilities based upon temporary differences arising from the differences between its financial statements as reported for US GAAP purposes and its statutory tax financial statements. These differences usually result in the recognition of revenue and expenses in different reporting periods for US GAAP and tax purposes and are calculated over accounts like retirement pay provision and provision for doubtful receivables. The deferred tax rate is 20% (2005: 30%).

Temporary Differences: Deferred Tax Assets / (Liabilities)

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Short term finance lease obligation	17,914	27,105
Accrued liabilities	7,268	13,211
Discount on receivables	478	576
Appreciation / (diminution) in value of financial assets	447	349
Allowance for doubtful receivables	352	-
Income and expenses relating to future periods	157	-
Provision for advance ticket sales	(8,637)	(9,252)
Discount on payables	(703)	(605)
Prepaid expenses	-	340
Provision for doubtful receivables	-	172
Changes in inventories	-	(36)
Unused investment incentives	-	14,942
Unused tax losses	-	470
Short term deferred tax asset	<u>17,276</u>	<u>47,272</u>
Long term finance lease obligation	71,352	138,073
Retirement pay liability	16,691	25,408
Useful life of fixed assets and finance lease adjustment	(167,505)	(268,267)
Manufacturers' credit	-	1,038
Deferred income	-	822
Other	280	-
Long term deferred tax liability	<u>(79,182)</u>	<u>(102,926)</u>
Total deferred tax liability	<u>(61,906)</u>	<u>(55,654)</u>

Movement in deferred tax liability per balance sheet can be reconciled with net deferred tax charge per income statement as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Deferred tax charge related to the origination and reversal of temporary differences	6,880	32,469
Net deferred tax charge	<u>6,880</u>	<u>32,469</u>
Translation gain on deferred tax liabilities	(628)	(15,469)
Changes in net deferred tax	<u>6,252</u>	<u>17,000</u>

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22 MANUFACTURERS' CREDIT (NET)

Manufacturers' credits consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Gross manufacturers' credit	20,201	14,675
Accumulated amortization	(1,136)	(12,073)
	<u>19,065</u>	<u>2,602</u>

23 RETIREMENT PAY LIABILITY

Under labor laws effective in Turkey, employees who worked for at least one year are entitled to receive a lump sum payment when their employment is terminated without due cause or when they retire, completing 25 years of service (20 years for women), are called up for military service or die. The amount payable consists of one month's gross salary per year of service. The gross salary is the salary at the date of termination, but subject to an upper limit of YTL 1,857 (US \$ 1,321) as at December 31, 2006 (December 31, 2005: YTL 1,727 – US \$ 1,287). The number of service years required before retirement is rising according to a sliding scale (60 for men, 58 for women) based on new legislation enacted in 1999. Provision for retirement pay liability is not subject to any kind of funding and no funding is required. The total provision recognized in the financial statements represents the estimated present value of the vested benefit obligation.

Amounts recognized in the income statement as provision for retirement pay liability are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Current service cost	9,569	11,295
Interest cost	4,620	4,170
	<u>14,189</u>	<u>15,465</u>

Movements in the provision for termination benefit in the balance sheet are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Provision at January 1	84,693	74,344
Charge for the year	14,189	15,465
Payments during the year	(15,427)	(5,116)
Provision at December 31	<u>83,455</u>	<u>84,693</u>

The estimated value of the vested benefit obligation is discounted with an approximate rate of 5.71% per annum after considering the effect of increase in eligible pay and its limit. (December 31, 2005: 5.61%).

24 SHARE CAPITAL

The Company's share capital was held in each period as follows:

	Class	%	31 December 2006	%	31 December 2005
			US \$ 000		US \$ 000
Republic of Turkey Prime Ministry Privatization Administration(*)	A, C	49.12(**)	380,867	75.18	582,854
Others	A	50.88(**)	394,514	24.82	192,527
			<u>775,381</u>		<u>775,381</u>
Nominal Share Capital (YTL)			<u>175,000,000</u>		<u>175,000,000</u>

24 SHARE CAPITAL (cont'd)

(*) 1.644 shares belonging to various private shareholders were not taken into consideration when the Company was included to the privatization program in 1984. Subsequently, these shares were registered on behalf of Privatization Administration according to Articles of Association of the Company, approved by the decision of the Turkish Republic High Planning Board on October 30, 1990.

(**) The shares of the stock owned by Turkish Republic Privatization Administration are offered to the public between 16-18.05.2006 with the 12.05.2006 dated and 22/569 numbered allowance of CMB. The A group registered shares with the total of YTL 50,312,500 (28,75% of the issued capital) which were sold in İstanbul Stock Exchange Whole Sales Market in 24.05.2006 with the nominal value of YTL 1 consists of the YTL 43,750,000 amount of shares which is 25% of the total amount of the issued capital which is YTL 175,000,000 and the rest of the A Group registered shares consist of the additional selling amount of shares which is 15% of the total amount of the public offering as well as which comes out to the 3.75% of the issued capital which is YTL 6,562,500. The Privatization Administration's share on capital approached to 49.12 percent after Privatization Administration had acquired the 212.254 THY shares which are returned from credit sales.

As at December 31, 2006, the Company's issued and paid-in share capital consists of 174,999,999,999 Class A shares and 1 Class C share, all with a par value of YKr 0.1 each. These shares are issued to the name. The Class C share belongs to the Republic of Turkey Prime Ministry Privatization Administration and has the following privileges:

Articles of Association 7: Positive vote of the Board member representing class C share and approval of the Board of Directors are necessary for transfer of shares issued to the name.

Articles of Association 10: The Board of Directors consists of seven members of which one member has to be nominated by the class C shareholder.

Articles of Association 14: The following decisions of the Board of Directors are subject to the positive vote of the class C Shareholder:

- a) As defined in Article 3.1 of the Articles of Association, taking decisions that will negatively affect the Company's mission
- b) Suggesting change in the Articles of Association at General Assembly
- c) Increasing share capital
- d) Approval of transfer of the shares issued to the name and their registration to the "Share Registry"
- e) Making decisions or taking actions which will put the Company under commitment over 5% of its total assets considering the latest annual financial statements prepared for Capital Market Board per agreement (this statement will expire when the Company's shares held by Turkish State is below 20%)
- f) Making decisions relating to merges and liquidation
- g) Making decisions to cancel flight routes or significantly decrease number of flights except for the ones that cannot recover even its operational expenses subject to the market conditions

Articles of Association Temporary Article 1: Head of the Board of Directors, members of the Board of Directors, auditors and general manager meeting the conditions defined in law numbered 4046, are to be selected from candidates suggested by A group shareholders, by the offer of Republic of Turkey Prime Ministry Privatization Administration and the approval of the Prime Minister or authorized minister, as long as the Company's shares held by Turkish State are not below 50%. The article 315 of Turkish Commercial Code is applicable for the members representing non-public membership.

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Notes to the Financial Statements

25 CONTINGENT LIABILITIES

a) Guarantees Given:

	December 31, 2006	December 31, 2006
	US \$	US \$
Letter of Guarantees Given	<u>39,388,148</u>	<u>28,350,145</u>

b) Purchase Commitments:

The Company has signed agreements for delivery of 59 aircrafts with delivery dates between years 2005-2008. 5 of above mentioned aircrafts are delivered on 2005 and 23 of these aircrafts are delivered on 2006. Total value of these aircrafts is approximately US Dollar 4.7 billion according to the list prices before any discounts applicable by aircraft manufacturers. The Company paid a deposit of US Dollar 255 million as of December 31, 2006 related to these aircrafts.

c) Letter of Comfort:

	December 31, 2006	December 31, 2005
Letters of Comfort Given to Sun Express	US \$ 2,900,000	US \$ 2,900,000
	EURO 2,556,459	EURO 2,556,459

d) The Company discounted its retirement pay provision to US \$ 83,455,400. The Company's total undiscounted liability for retirement pay would be US \$ 142,444,094 as of December 31, 2006, if all employees were dismissed on that date.

e) An investigation has been started in early 2006 simultaneously both at Europe and USA about many airlines, including major ones, on the fixed cargo fees by the USA Department of Justice Antitrust Division and European Antitrust Authorities. In the context of this investigation, on 06 April 2006, USA Columbia District Court requested the company to present the information and documents regarding the air cargo fees. Similar notifications were sent to other airlines mentioned, too.

26 OPERATING LEASE COMMITMENTS

Commitments for future operating leases are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Not later than one year	121,650	88,674
Between 1 and 5 years	323,053	149,343
Over than 5 years	365,998	75,219
	<u>810,701</u>	<u>313,236</u>

27 EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

a) The collective bargaining agreement between THY and Turkish Civil Aviation Labour Union ended at December 31, 2006. The collective bargaining agreement meetings have been continuing as of report date.

b) Market price of 1,026,000,000 USA\$ shares, which are traded in İstanbul Stock Exchange, and included in the financial investments available for sale as of 19 April 2007, has decreased from YTL 4,62 at December 31, 2006 to YTL 3,68 at 19 April 2007. Hence, the total market value of these shares decreased by US \$ 718,445 compared to balance sheet date.

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28 OPERATING REVENUES

Operating revenues are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Scheduled services		
Passenger	2,422,932	2,005,079
Cargo and mail	222,002	198,785
	<u>2,644,934</u>	<u>2,203,864</u>
Non-Scheduled services	26,189	23,035
Other revenue	138,038	89,428
Total revenue	<u><u>2,809,161</u></u>	<u><u>2,316,327</u></u>

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

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
International		
- Europe	1,118,845	945,807
- Far East	470,077	362,723
- Middle East	248,347	210,058
- North America	129,803	115,033
- North Africa	64,266	58,004
- Middle Africa	5,436	-
- West Africa	3,194	-
	<u>2,039,968</u>	<u>1,691,859</u>
Domestic	604,966	512,005
Total scheduled services traffic revenue	<u><u>2,644,934</u></u>	<u><u>2,203,864</u></u>

29 OPERATING EXPENSES

Operating expenses consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Fuel-oil expenses	767,997	544,122
Staff expenses	584,617	536,766
Marketing and selling expenses	286,941	249,572
Landing and navigation expenses	230,534	182,889
Depreciation expenses	207,827	151,502
Maintenance expenses	157,974	108,925
Handling and station expenses	135,251	117,341
Passenger service and catering expenses	127,852	112,631
Operating lease expenses	120,702	75,215
General operations	36,884	33,597
Insurance expenses	31,038	38,597
General administrative expenses	24,059	15,813
Aircraft and seat rent expense	17,580	9,148
	<u><u>2,729,256</u></u>	<u><u>2,176,118</u></u>

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Notes to the Financial Statements

30 FINANCIAL EXPENSES (NET)

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Foreign exchange gains	446,595	157,028
Interest income	18,293	31,564
Discount income	627	445
Income from investment accounted per equity method	-	587
Financial income	<u>465,515</u>	<u>189,624</u>
Foreign exchange losses	(430,537)	(177,627)
Finance lease interest expense	(50,899)	(34,027)
Loss from financial investment accounted per equity method	(8,509)	-
Interest expenses for bank borrowings	(7,279)	-
Retirement pay interest cost	(4,620)	(4,170)
Decrease in value of available for sale financial assets	(2,264)	(3,773)
Interest expenses- Third parties	-	(9,049)
Other financial expenses	(564)	(1,639)
Financial expenses	<u>(504,672)</u>	<u>(230,285)</u>
Translation gain / loss	25,302	16,103
Financial expenses (net)	<u>(13,855)</u>	<u>(24,558)</u>

31 INCOME FROM OTHER OPERATIONS

Income from other operations consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Dividend income	10,430	6,172
Discounts received from spare parts suppliers	8,409	7,825
Reversal of unnecessary provision	5,903	8,163
Impairment gain	5,018	36,527
Free of cost materials income	4,721	3,750
Compensations received	4,522	2,588
Profit on sale of marketable securities	4,071	-
Yapı Kredi protocol income	2,109	-
Manufacturers' credit income	466	817
Gain from sale of fixed assets	77	600
Other	18,557	6,177
	<u>64,283</u>	<u>72,619</u>

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Notes to the Financial Statements

32 LOSS FROM OTHER OPERATIONS (-)

Losses from other operations consist of the following:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Provision expenses	21,992	22,722
Indemnity and penalty expenses	5,349	-
Loss on sale of marketable securities	1,508	-
Expenses incurred for passengers with no visas	999	-
Loss on sale of fixed assets	240	-
Other expenses	5,244	2,149
	<u>35,332</u>	<u>24,871</u>

33 TRANSACTIONS WITH RELATED PARTIES

For the purposes of the accompanying financial statements, the Company's shareholders and the Company's equity participations are referred to as related parties.

Transactions with related parties are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Services given to Sun Express	3,438	2,723
Services given to USAŞ	320	277
	<u>3,758</u>	<u>3,000</u>
Services taken from USAŞ	67,842	59,151
Services taken from Sun Express	7,967	646
	<u>75,809</u>	<u>59,797</u>

Dividend income from equity investments are as follows:

	December 31, 2006	December 31, 2005
	US \$ 000	US \$ 000
Sun Express	9,813	5,240
Uçak Servisi A.Ş.	288	815
France Telecom	241	117
	<u>10,342</u>	<u>6,172</u>