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3D Insight

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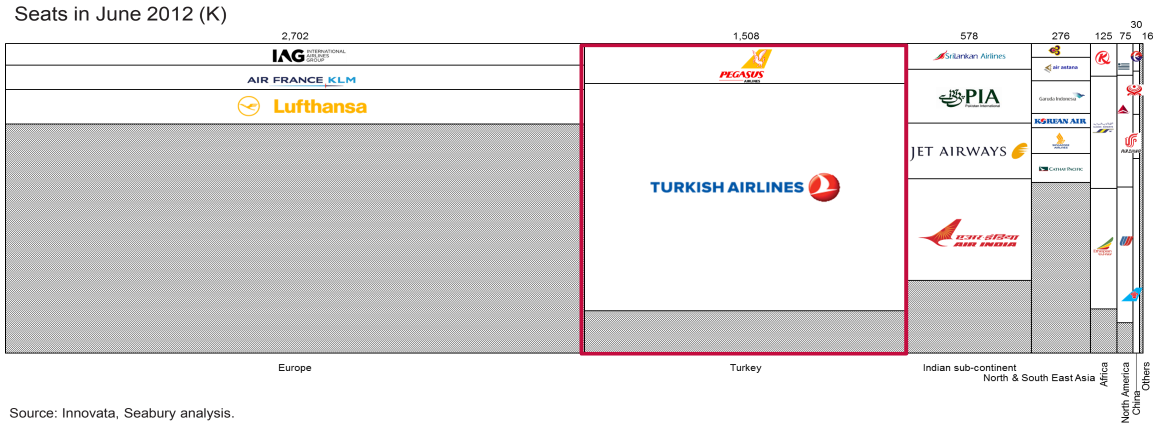
The Major Airlines Outside MENA

The latest article in a multi-part series

Background

This is the last article in the multi-part series on the AACO carriers' major non-AACO competitors examining the competition from Turkey, a country well connected to the MENA region, as shown in Figure 1. As with previous articles, there will be a particular focus on the carriers with greatest seat capacity between the focus region and MENA, in this case Turkish Airlines and Pegasus Airlines, which account for more than three quarters of the total capacity between the two regions. In addition to these two carriers, some attention will also be given to SunExpress, Onur Air and Atlasjet Airlines. Although these airlines are not the most significant players in the Turkey-MENA market, they are sizable airlines in Turkey and should be considered as major competitors in the Turkish domestic market.

Figure 1: Seat capacity breakdown from MENA excluding AACO carriers



Source: Innovata, Seabury analysis.

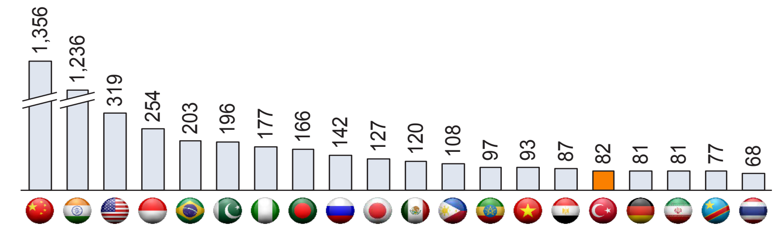
Focus on Turkey

Introduction

Turkey is one of the few transcontinental countries in the world. Geographically in the Middle-East, Turkey lies between Europe and Asia, where the majority of its territory is located. Throughout history, Turkey has always been a multicultural country, linking European, Arabian and Asian heritages. Its particular location at the crossroads of Europe and Asia makes it a country of significant geostrategic importance.

With an estimated population of 82 million in 2014 (CIA World Factbook), Turkey is also the 16th most populous country in the world, with a population higher than any European country.

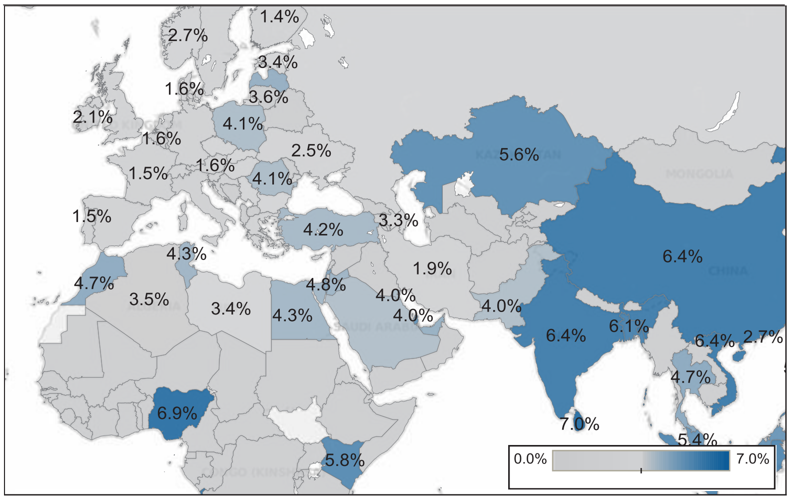
Figure 2: Top 20 largest countries in the world in terms of population



Source: CIA World Factbook, Seabury Analysis

Turkey is the 90th most prosperous economy in terms of Gross Domestic Product (GDP) per capita (on a purchasing power parity basis).[1] However, with an expected average annual GDP growth of 4.2% between 2013 and 2019, Turkey is expected to be one of the fastest growing economies, expanding at a much faster pace than surrounding countries in Europe and the Mediterranean region, outpaced only by Asian countries and a few sub-Saharan countries, as illustrated in figure 3.

Figure 3: 2013-2019 GDP growth forecast



Source: EIU, Seabury Analysis

Introduction to the Top 5 carriers

As mentioned earlier, the article will focus on five airlines: Turkish Airlines, Pegasus Airlines, SunExpress, Onur Air and Atlasjet Airlines.

Turkish Airlines was established in 1933 and became the flag carrier of Turkey. The airline is a traditional full service carrier, operating a fleet of narrowbody and widebody aircraft in a two-class configuration. Turkish Airlines is 49% owned by the Turkish government and has been a member of Star Alliance since 2008.

Pegasus Airlines was founded in 1990 as a joint venture by Aer Lingus Group, Silkar Yatırım ve Insaat Organizasyonu A.S. and Net Holding A.S to provide charter services. The airline transitioned from charter service to scheduled domestic service in 2005, when it was acquired by Esas Holding A.S. Today Pegasus Airlines defines itself as a low cost airline and operates domestic as well as international routes with a fleet of narrowbody aircraft. While self-proclaimed as an LCC, Pegasus Airlines demonstrates certain business activity that is mostly attributable to full service carriers such as offering connectivity, although limited, and distributing through indirect sales channels.

SunExpress, Onur Air and Atlasjet Airlines followed a similar path to Pegasus Airlines. All of them used to be predominantly charter and leisure carriers, but started focusing on scheduled services in order to benefit from the booming economy and the growing middle-class not only in Istanbul and other major metropolises, but also in smaller Anatolian cities.

SunExpress was founded in 1989 as a subsidiary of Turkish Airlines and Lufthansa with the aim of participating in the Turkish tourism market. Today, SunExpress is a medium-sized tourist airline focusing on international and Turkish domestic tourism.

Onur Air was established in 1992 as a private, tourist airline. It launched scheduled services in 2003 and today operates a mix of scheduled and charter flights with a narrowbody fleet.

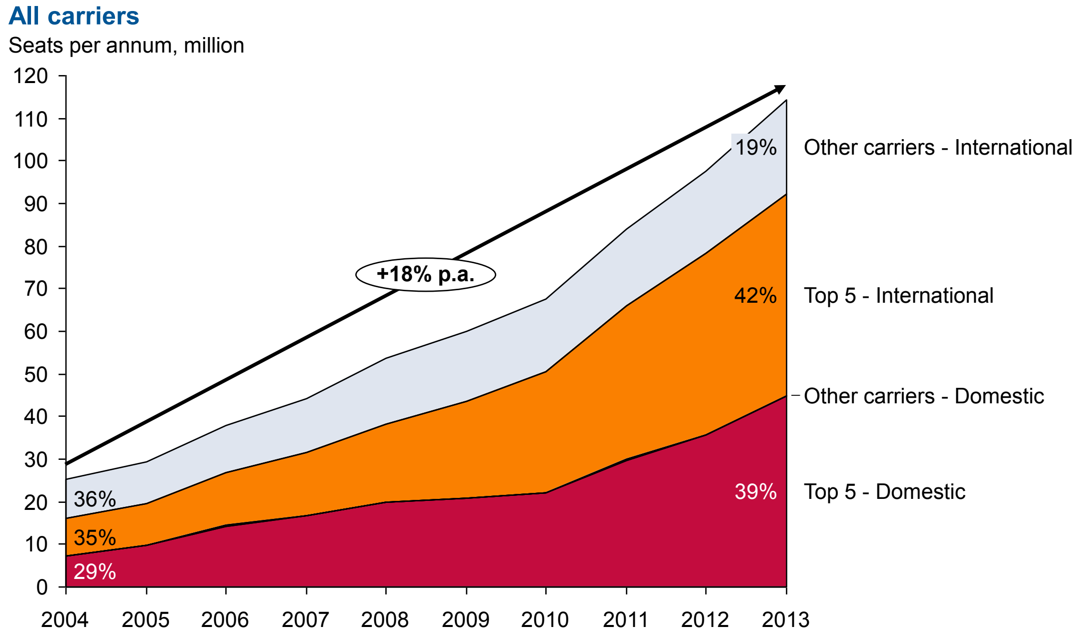
Atlasjet was established in 2001, licensed to carry out passenger and cargo unscheduled flights. Atlasjet is headquartered in Istanbul and operates domestic and international, scheduled and charter flights.

Capacity Development

Overview of capacity development in Turkey

Seat capacity to and from Turkey has grown annually by 18% on average between 2004 and 2013, as shown in figure 4. This is well above the global average growth rate of 4% per annum (Innovata) for the same period. Much of the expansion has come from the Top 5 carriers, namely Turkish Airlines, Pegasus, SunExpress, Onur Air and Atlasjet, whose combined capacity share has grown from 64% in 2004 to 81% in 2013. Other airlines represented less than a fifth of the total seat capacity to Turkey in 2013.

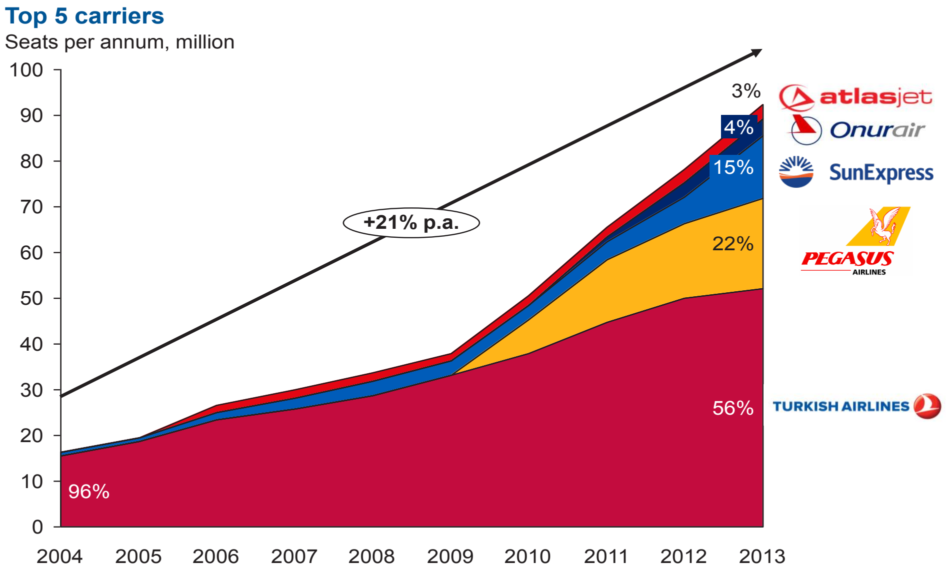
Figure 4: Capacity development to / from Turkey (all carriers)



Note: Top 5 airlines include Turkish Airlines, Pegasus Airlines, SunExpress (including SunExpress Germany), Onur Air and Atlasjet Airlines
Source: Innovata, Seabury analysis

Figure 5 shows the Top 5 carriers and details their above-market growth. While together their capacity grew by 21% per annum on average between 2004 and 2013, the increase was unequally distributed between the carriers. Turkish Airlines, which had over 95% capacity share among the Top 5 carriers in 2004, accounted for 56% of the capacity in 2013. This represents an average growth of 14% per annum, still higher than the world average of 4% between 2004 and 2013, but lower than those of its smaller competitors in Turkey. Founded as a charter airline in 1990, Pegasus grew rapidly to become the second largest airline in Turkey. While figure 5 does not capture the charter operations of Pegasus in its early years, it illustrates the airline's fast growth within the last few years. Pegasus was named "The Fastest Growing Airline" of Europe's major scheduled airlines in terms of seat capacity for 2011, 2012 and 2013 by the Official Airline Guide (OAG)[2]. SunExpress has grown at a similarly rapid rate within the last decade. The schedule data suggests an average annual growth of 38% in terms of capacity. However, this growth is likely to be an overestimate, driven by a shift from pure charter traffic – not captured by Innovata – to mixed traffic of both charter and scheduled flights. Onur Air and Atlasjet are the two smallest airlines of the Top 5, representing a combined capacity share of 7%.

Figure 5: Capacity development to / from Turkey (Top 5)

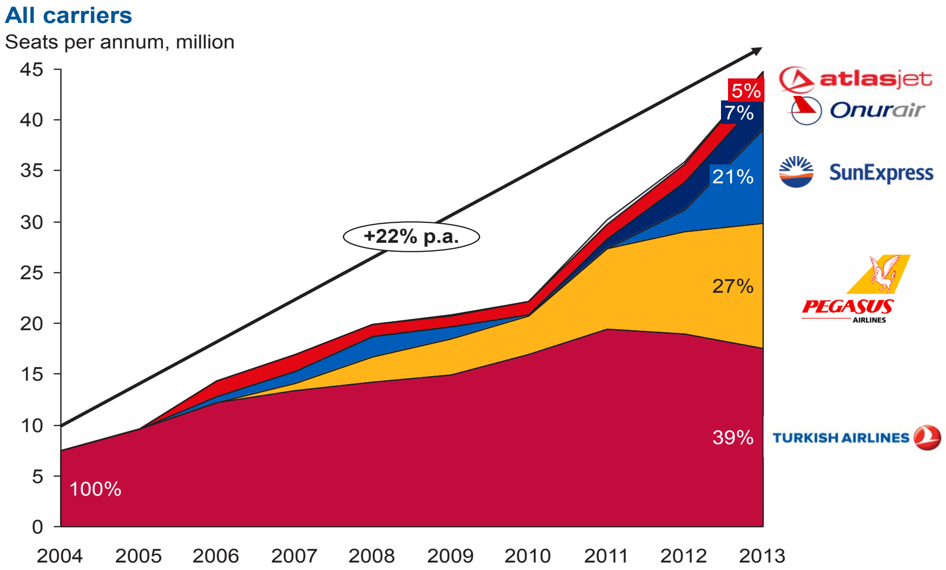


Note: Top 5 airlines include Turkish Airlines, Pegasus Airlines, SunExpress (including SunExpress Germany), Onur Air and Atlasjet Airlines
Source: Innovata, Seabury analysis

Domestic capacity development

A closer look at the domestic market highlights the growth of secondary carriers within the last decade. In 2004, Turkish Airlines was nearly in a monopoly, dominating the domestic scheduled market. Between 2004 and 2013, it grew by an average annual rate of 10%, less than the total market's 22% average growth rate. As a result, its capacity share in the domestic market shrank to 39% in 2013. Turkish Airlines remains the largest airline in Turkey in terms of domestic share but is now closely followed by Pegasus Airlines and SunExpress. Onur Air and Atlasjet remain significantly smaller in the domestic market, with a combined capacity share of 12%.

Figure 6: Capacity development within Turkey (all carriers)

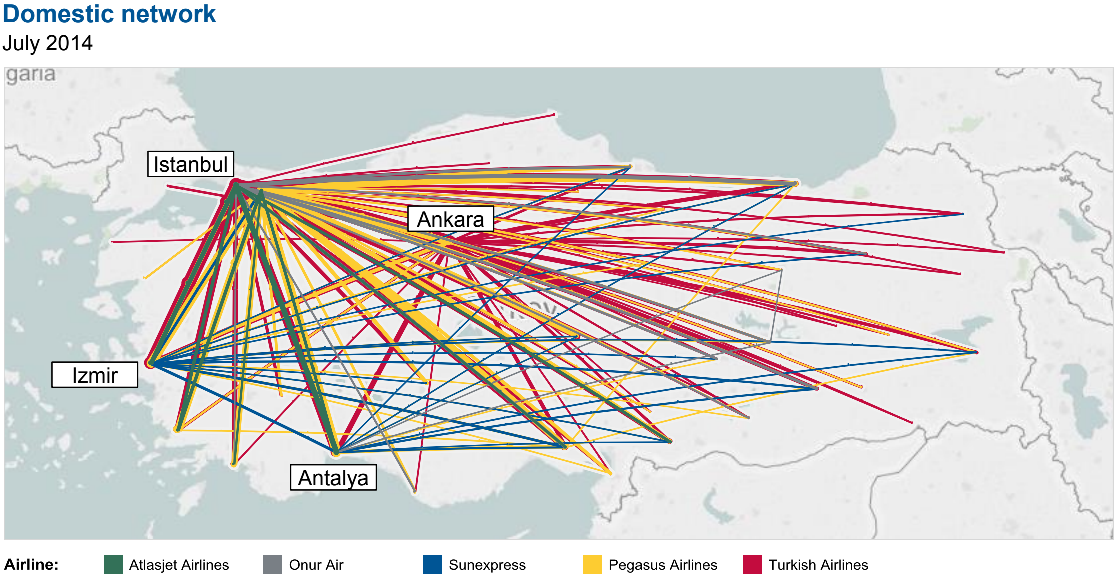


Source: Innovata, Seabury analysis

Figure 6 also highlights the development of low-cost carriers (LCC) and other leisure airlines in the domestic Turkish market. Pegasus Airlines, SunExpress, Onur Air and Atlasjet accounted for more than 60% of the domestic capacity in 2013, without taking into account pure charter flights. This represents a dramatic change since 2004 when the domestic market was dominated by Turkish Airlines.

Figure 7 illustrates the domestic network as of July 2014. It shows that Istanbul, the largest Turkish city, is well served from most parts of the country. All of the Top 5 airlines operate from Istanbul, which is, for most of them, their largest domestic hub. SunExpress is the only exception as the airline operated only two routes out of the city in July 2014, focusing its capacity on other domestic airports. Atlasjet and Onur Air primarily serve routes to and from Istanbul with scheduled flights. SunExpress' major base is in Izmir but it also links many cities to Antalya with domestic scheduled service. Primarily based in Istanbul, Pegasus Airlines also operates numerous point-to-point flights linking secondary cities. In contrast, Turkish Airlines operates a hub-and-spoke system with major bases in Istanbul and Ankara, as illustrated below.

Figure 7: Domestic network in July 2014

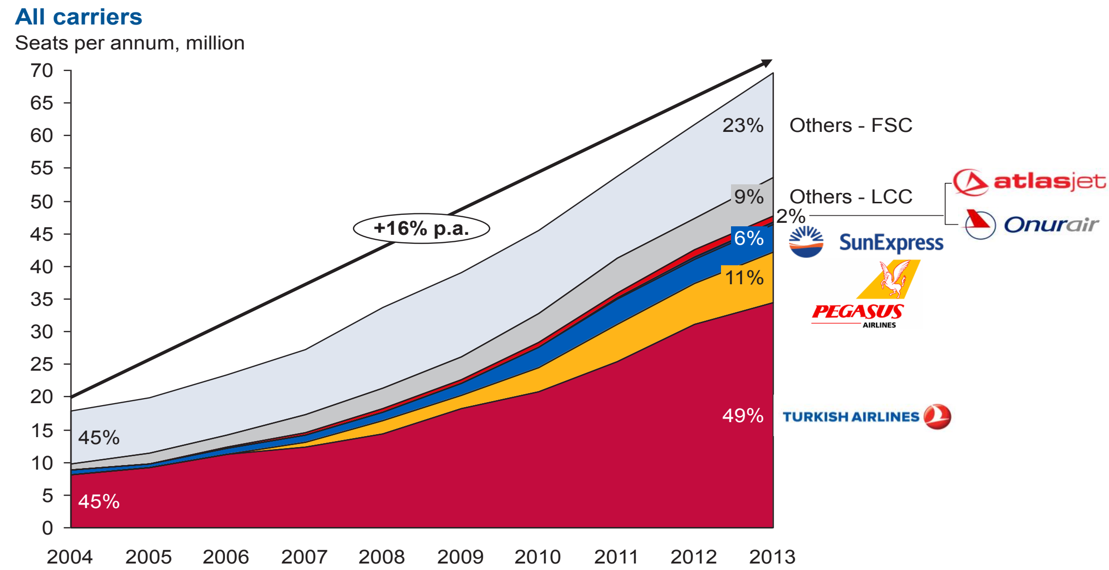


Source: Innovata, Seabury analysis

International capacity development

The development of the international market differs from that of the domestic market. While LCCs and leisure airlines have grown fast in both international and domestic markets, in international markets this growth has not come at the expense of the national carrier Turkish Airlines. In fact, the latter has seen its capacity share grow from 45% to 49% between 2004 and 2013, thus growing faster than the market, which grew at an average pace of 16% per annum. In 2013, Turkish Airlines had significant dominance amongst the international airlines serving Turkey with more than four times the capacity of the second international carrier, namely Pegasus Airlines.

Figure 8: International capacity development (all carriers)

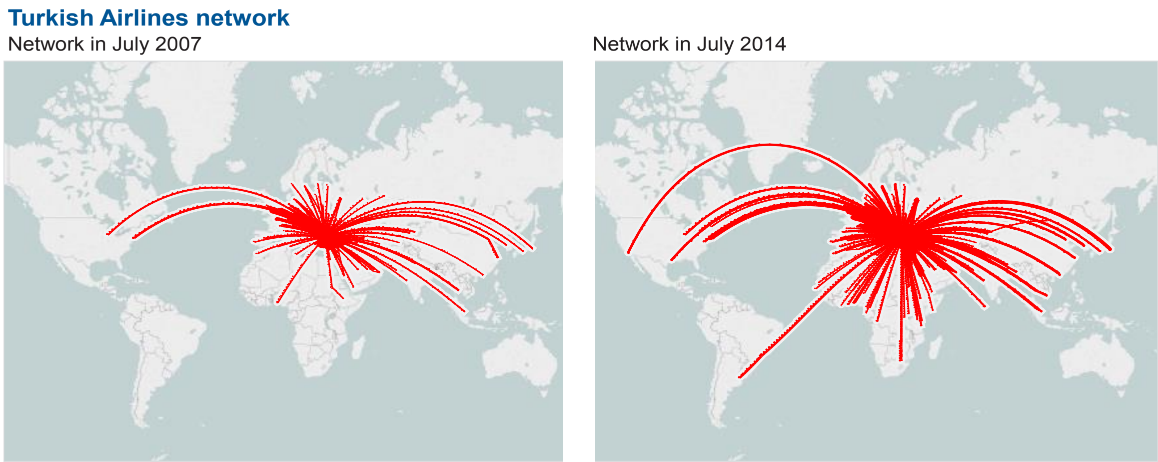


Note: SunExpress includes SunExpress Germany
Source: Innovata, Seabury analysis

Figure 8 also highlights the changes in the competitive landscape of Turkish Airlines. While the national carrier was facing competition mainly from other full service airlines in 2004 with LCCs representing only 10% of the total international capacity, it faced much stronger competition from LCCs in 2013. The latter represented about 28% of the entire international capacity in 2013 and produced more seats than the non-Turkish FSCs. Until today, their market share increase has been at the expense of other FSCs rather than Turkish Airlines.

Figure 9 illustrates the development of Turkish Airlines in the international market. The comparison between its network in 2007 and 2014 clearly demonstrates the aggressive growth of the national carrier. The airline developed its long-haul network dramatically with numerous additional destinations in North America and Asia supported by a large number of new destinations in sub-Saharan Africa and in South America, where the airline was not present in 2007.

Figure 9: Turkish Airlines network



Source: DiioMi, Seabury analysis

Figure 10 illustrates the international capacity development from Turkey since 2004. In 2013, the largest capacity flow from Turkey was to the EECA region. The other flows were much smaller but grew faster in the last decade, at a rate of 17% and above. Africa and South America are new markets served directly from Turkey. It is interesting to note that capacity grew fast to all regions, at average annual rates well above 10%.

Figure 10: International traffic growth, by region

Capacity development by region since 2004

Capacity to and from Turkey, all carriers

Note: Line thickness proportional to number of seats in 2013; 100% growth implies there was no service previously
Source: DiioMi, Seabury analysis

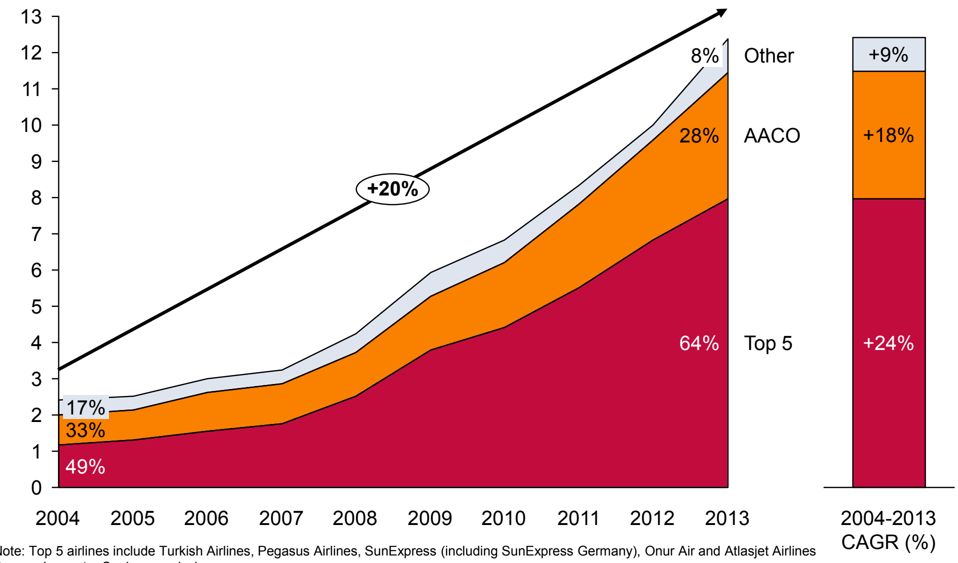
Focus on MENA

Capacity between Turkey and the MENA region has shown strong growth of 20% from 2004 to 2013, faster than the average international capacity to Turkey of 16% (Figure 8). The Top 5 Turkish carriers increased their capacity share from 49% in 2004 to 64% in 2013, achieving an average annual growth of 24%. During this period, the AACO carriers saw their market share decrease from 33% to 28% and grew slightly slower than the market, at an average pace of 18% per annum.

Figure 11: Turkey – MENA capacity development (all carriers)

All carriers

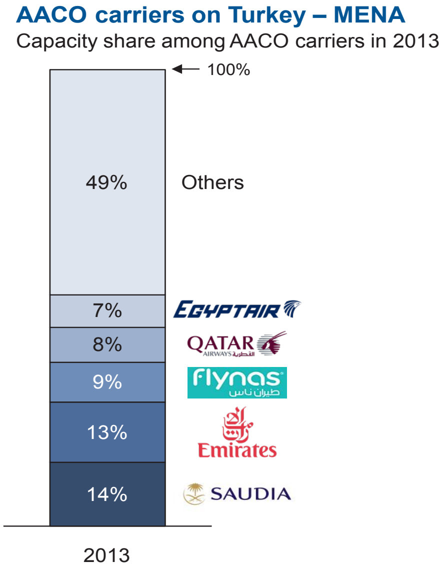
Seats per annum, million



Note: Top 5 airlines include Turkish Airlines, Pegasus Airlines, SunExpress (including SunExpress Germany), Onur Air and Atlasjet Airlines
Source: Innovata, Seabury analysis

Among the AACO carriers, there is no clear dominance of any airline. Saudia and Emirates are the largest two AACO carriers operating between Turkey and the MENA region, but their capacity shares are not dramatically different from those of flynas, Qatar Airways and Egyptair. Also, the fact that the largest five AACO carriers represent only 51% of the total capacity illustrates how the market is fragmented.

Figure 12: Capacity share among AACO carriers

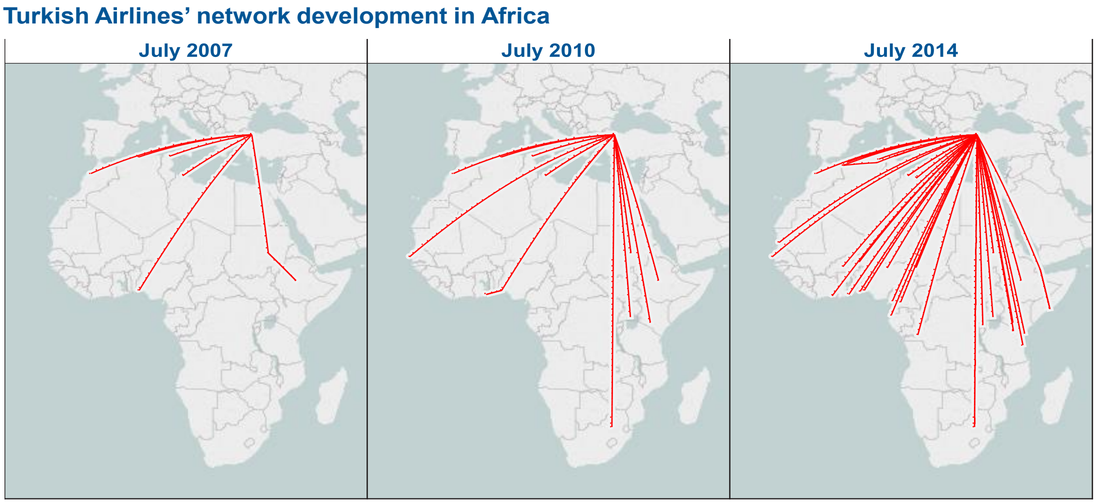


Source: DiioMi, Seabury analysis

Focus on Africa

Africa has been one of the focus regions for Turkish Airlines in the recent years. As shown below, the airline added many new routes between Istanbul and African countries in the last seven years. It grew from 7 destinations in Africa in July 2007 to 36 destinations in 2014.

Figure 13: Turkish Airlines' development in Africa



Source: Innovata, Seabury analysis

One of the strengths of the airline is that it can fly narrowbody aircraft into much of North and West Africa, as well as the western parts of Central Africa. But it is also and foremost its close cooperation with the Turkish government, whose relations with Africa constitutes one of the prime orientations of its foreign trade policy. Turkey-Africa relations have gained momentum since the declaration of Turkey as a strategic partner of the continent by the African Union in January 2008 and were further enhanced in 2013 with a reinforced political-economic partnership.[3] As an illustration, there are now 35 Turkish Embassies in Africa as opposed to only 12 in 2009. As the national airline of Turkey, Turkish Airlines has been benefiting from the strategy of its country to increase trade with Africa, with the government designating the carrier on new or extended bilateral agreements.

Turkish Airlines announced it will add up to 10 new African cities to its network in 2015 as it looks to strengthen its position on the continent including strengthening its position in markets between South Africa and the Democratic Republic of the Congo.

Alliances

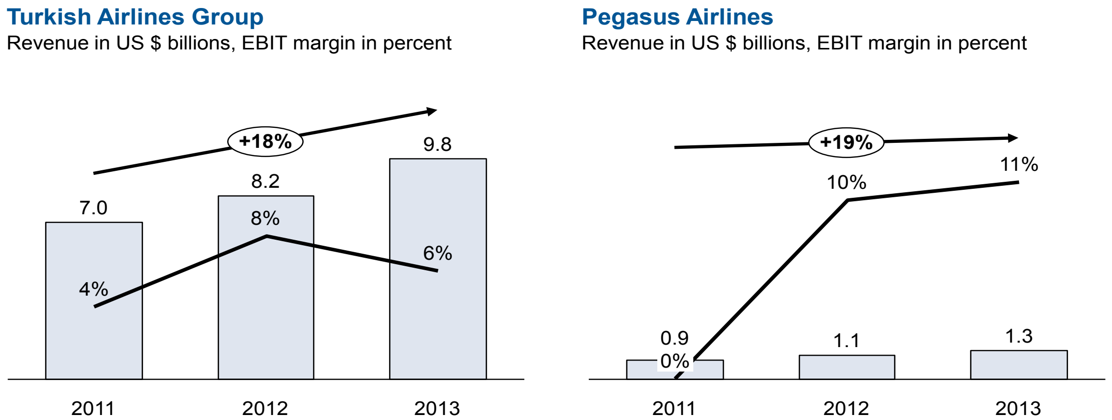
Turkish Airlines joined Star Alliance on 1 April 2008, sponsored by Lufthansa. This initiative was driven by its ambition to become a global brand to compete with the world's leading airlines and was considered as a vital milestone in the expansion of the airline. Joining the alliance enabled the Turkish carrier to provide its customers with a wider choice of flight options by expanding its network through code share agreements. It also extended the benefits of its frequent flier programme by unifying member privileges, such as lounge access and reciprocal earn and burn opportunities, with other Alliance members. In 2013, Turkish Airlines increased its strategic role in the alliance by taking part in newly formed strategic committees through representatives' reorganisation of the alliance. However, the airline's membership has also been tarnished with less fortunate events as when it made headlines with alliance partner member Lufthansa last year as tension arose between the two. The two carriers were originally seen as close strategic partners (they created SunExpress together as a joint-venture), but with Turkish Airlines' rapid expansion, Lufthansa accused the Turkish carrier of unfairly capturing market share from them on the German market. As a consequence, Lufthansa decided to drop mileage earning rates and codeshare flights with the Turkish airline.

The other airlines of the Top 5 do not take part in any of the three global alliances, in line with traditional LCC and leisure airline business models.

Revenue development

The following section will focus on the revenue development of the Top 5 Turkish carriers. As only Turkish Airlines and Pegasus Airlines disclose their financial figures, the analysis will focus on these two carriers.
As shown in Figure 14, both Turkish Airlines and Pegasus Airlines revenues grew by almost 20% per year on average between 2011 and 2013. In 2013, the national carrier generated almost ten times as much revenue as the low cost airline. However, except for 2011, the latter generated higher profit margins with EBIT margins above 10%.

Figure 14: Revenue and EBIT margin

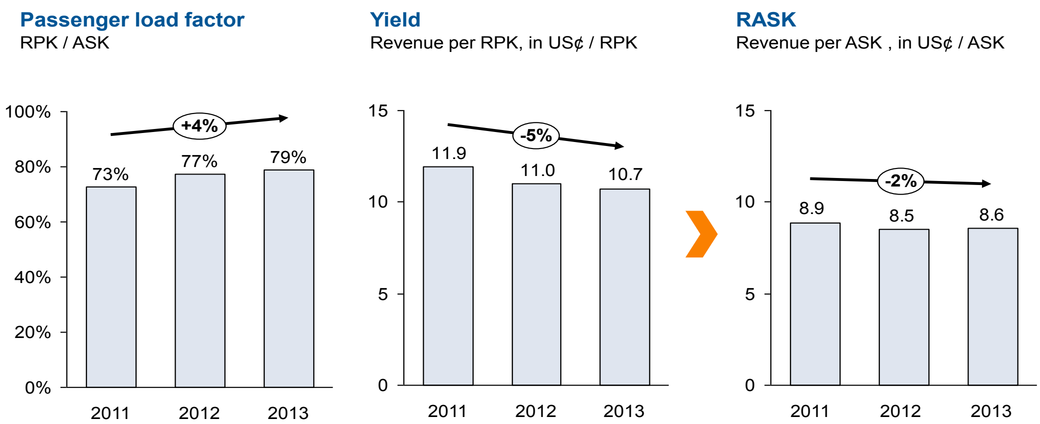


Note: Turkish Airlines Group = TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI and its subsidiaries
Source: S&P Capital IQ, Seabury analysis

Unit revenue development

Over the last few years, both Turkish Airlines and Pegasus Airlines saw dramatic revenue increases of almost 20% per year. The following section aims to understand the evolution of unit revenue during this period of aggressive capacity growth.
Turkish Airlines saw an increase in load factor over two consecutive years from 2011 to 2013, reducing the gap to the 81% European average (IATA). This steady increase in load factor was not sufficient to compensate for the loss in yield during the same period. As a result, Turkish Airlines' revenue per available seat kilometre dropped from US¢ 8.9 to US¢ 8.6. The decrease in yield can be partly explained by the depreciation of the Turkish lira compared to the US dollar. Between 2011 and 2013, the Turkish currency lost 25% against the US currency (Figure 21), negatively impacting the yield when analysed in the US dollar, although only 14.2% of Turkish Airlines' revenue was collected in Turkish lira[4].

Figure 15: Turkish Airlines' unit revenue development



Note: Turkish Airlines Group revenue, including subsidiaries
Source: S&P Capital IQ, Seabury analysis

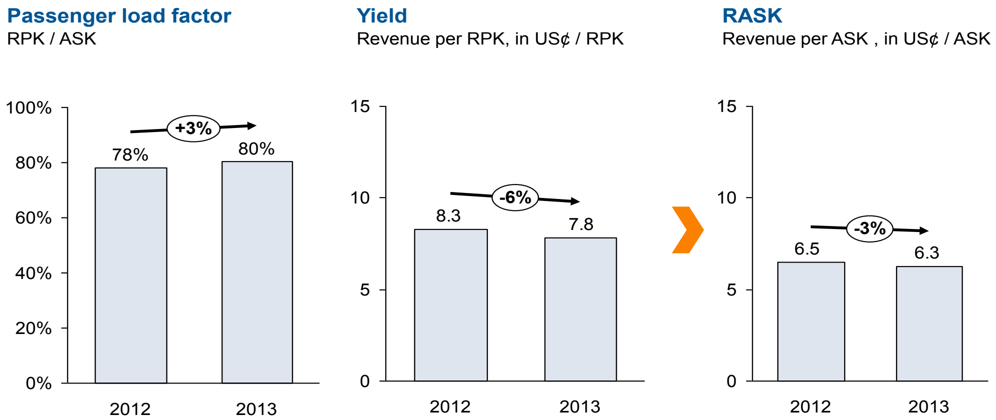
Pegasus Airlines showed similar trends in load factor and yield as Turkish Airlines.

Pegasus Airlines' load factor increased by 3% to 80% between 2012 and 2013 but remains lower than those of typical low cost airlines (e.g. easyJet achieved a 89% load factor in 2013). This can be partly explained by its fast growth (+16% yoy ASK growth vs. +4% for easyJet for the same period).

With 44% of its revenue collected in Turkish lira, the depreciation of the latter currency had negative effects on the yields when expressed in US dollars (currency in which Pegasus Airlines incurs more than half of its expenses)[5]. Therefore, the unit revenue increase reported by the airline in lira became a unit revenue decrease in US dollars.

With a 3% load factor increase and a 6% yield decrease, Pegasus Airlines' RASK decreased by 3% between 2012 and 2013. In the near future, Pegasus Airlines expects further pressure on yields offset by increasing load factors and a resulting stabilised RASK.

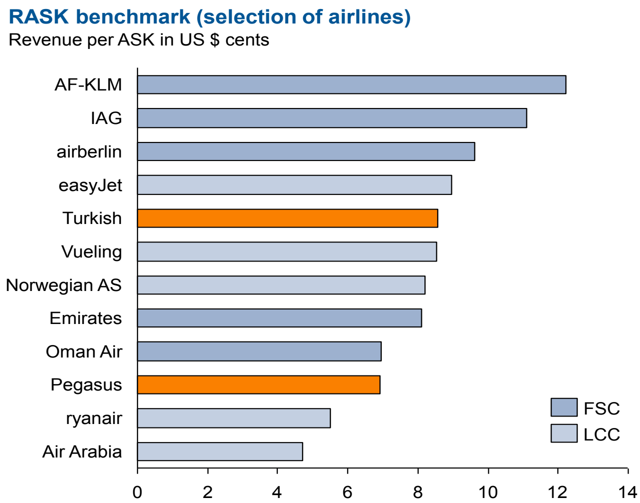
Figure 16: Pegasus Airlines' unit revenue development



Source: Pegasus Airlines Annual Report, S&P Capital IQ, Seabury analysis

Compared to other airlines, Pegasus Airlines found itself in the lower range of RASK, but still above other LCCs such as Ryanair and Air Arabia. However the latter benefit from the advantage of longer average stage lengths compared to Pegasus Airlines. Turkish Airlines, on the other hand, sits in the middle of the benchmark set, with higher revenue per ASK than Emirates but lower than those of Europe's major airline groups.

Figure 17: Unit revenue benchmark



Note: Values for most recent financial year (year ending September 2013, December 2013 or March 2014)
Source: S&P Capital IQ, Seabury analysis

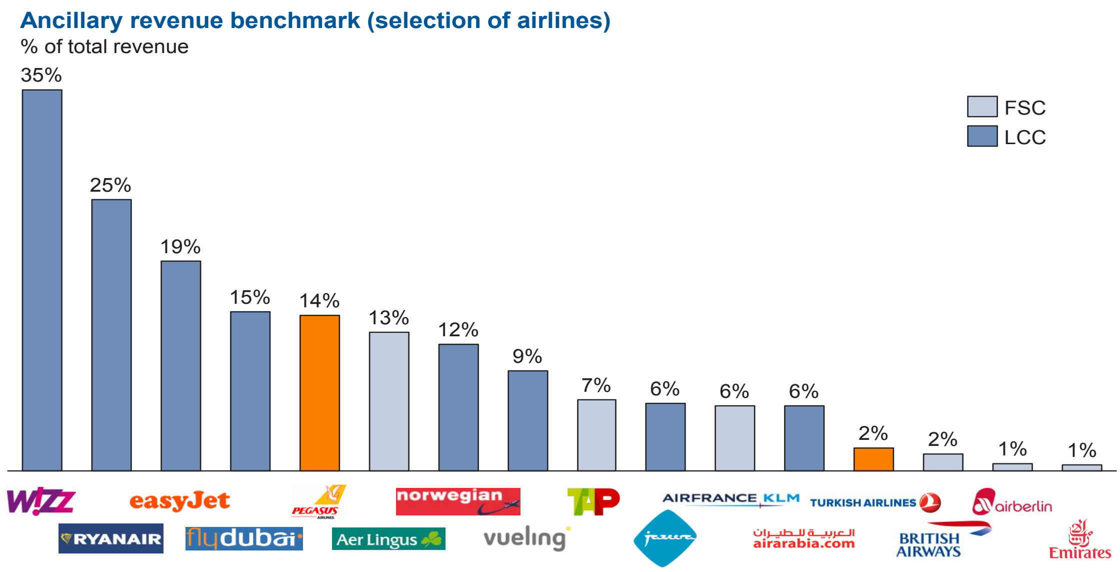
Revenue development initiatives

The role that ancillary revenue sources play in bolstering airline revenues continues to grow. With its roots among low-cost carriers, ancillary revenue generation is now a fundamental component of most airlines revenue generation strategies. As expected, the leaders in this field remain traditional low-cost carriers, as illustrated in Figure 17.

According to the 2014 Ideaworks Ancillary Revenue Yearbook, Pegasus Airlines reported that ancillary revenue accounted for around 15% of total revenue for the past period - an increase of 64% year-on-year. The carrier has implemented a number of rigorous ancillary revenue initiatives including pre-order and in-flight sales of food and beverage, duty-free sales on-board international flights, excess baggage charge, reservation change and cancellation fees, airport check-in and seat selection fees. The airline plans to keep growing its ancillary revenue stream and aims at increasing its ancillary revenues to at least 10 to 12 Euros (US$ 12-15) per passenger by 2017 (from approximately EUR 7 / US$ 8 in 2013 according to IdeaWorks).

As is the case with most full service legacy carriers, Turkish Airlines pursues a less aggressive ancillary revenue strategy compared to its LCC counterpart. The airline's ancillary revenue accounts for under 5% of total revenue, putting it in line with other global legacy carriers. Ancillary revenue sources for Turkish Airlines are driven from more traditional sources including excess baggage and ticket cancellation and change fees.

Figure 18: Ancillary revenue as % of total revenue



Source: 2014 Ideaworks Ancillary Revenue Yearbook, Seabury analysis

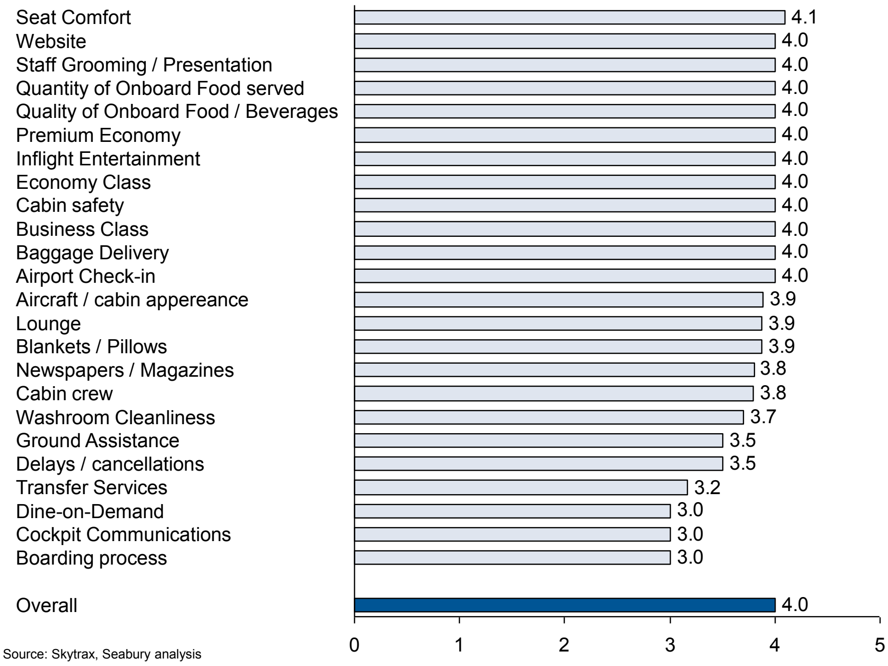
Product

Turkish Airlines became one of the most prestigious airlines in the world in terms of product. The airline has retained a four-star airline rating from Skytrax since 2007 and received several awards to mark its name in the aviation industry. It has been chosen "Best Airline in Europe", "Best Airline in Southern Europe", "Best Business Class On-board Catering" and "Best Business Class Lounge Dining" in the 2014 Skytrax World Airline Awards. The airline also received the "Best Airline in Europe" award for the fourth consecutive year, testament to the consistency of its product.

As shown below, Turkish Airlines scored highly on all of the many points covered by the survey.

Figure 19: Turkish Airlines' Skytrax review

Turkish Airlines' Skytrax ratings
Average rating



Source: Skytrax, Seabury analysis

Turkish Airlines has rolled out a new business class cabin on its Boeing 777-300ERs and Airbus A330-300s, now equipped with 180-degree lie-flat seats. The airline also offers complimentary Wi-Fi for all passengers on its Boeing long-haul fleet. Its new lounge at its Istanbul Atatürk hub, with over 63,500 square feet over two levels, has made headlines in 2014 and reinforced Turkish Airlines' positioning as a four star airline. The lounge offers a fully-stocked library, a children's playground, pool tables, showers, private rooms for napping, an arcade and a golf simulator.

Pegasus Airlines' overall rating by the latest Skytrax publication was two out of five. This rating is lower than those of most European and Middle Eastern low cost airlines. easyJet, germanwings, Norwegian, Transavia, Vueling and Wizz Air in Europe as well as Air Arabia in the Middle East are all three star airlines. The only notable exception in Europe is Ryanair, which is also a two star airline.

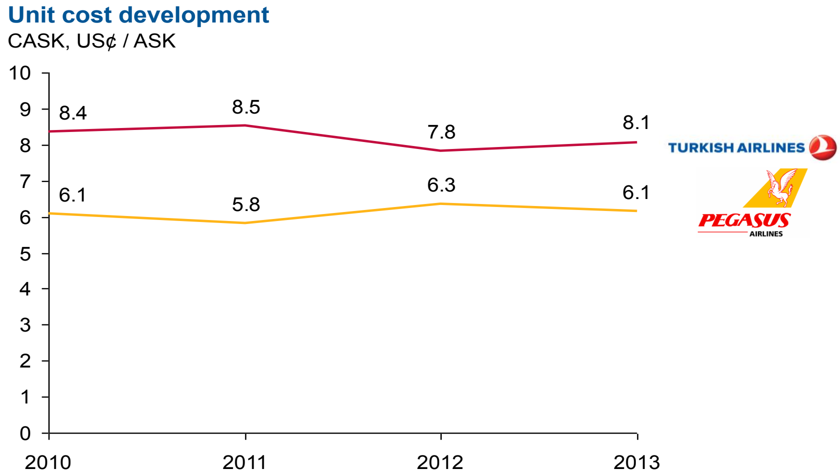
Like Pegasus Airlines, Onur Air is classified as a two star airline by Skytrax. Atlasjet and SunExpress are not rated by Skytrax.

Cost management

Airlines around the world are putting increasing emphasis on cost management in an industry suffering from declining yields and cost structures with high shares of non-controllable, external costs (e.g. fuel costs or airport costs). Most large network carriers conduct recurrent cost cutting exercises to address declining yields and to reduce the gap with competing low cost airlines on the short and medium haul markets. As in the revenue improvement section, this section will focus on Turkish Airlines and Pegasus Airlines, the only two airlines of the Top 5 airlines that disclose their financial results.

Both Turkish Airlines and Pegasus Airlines have been able to keep their unit cost stable since 2010, as shown in the figure below. Pegasus Airlines has managed to keep its unit cost at the same level of US¢ 6.1 per ASK despite a jet fuel price increase from approximately US$ 90 per barrel in 2010 to approximately US$ 120 per barrel in 2013. During the same period of time, Turkish Airlines has managed to reduce its unit cost from US¢ 8.4 per ASK to US¢ 8.1 per ASK, i.e. a reduction of 4%.

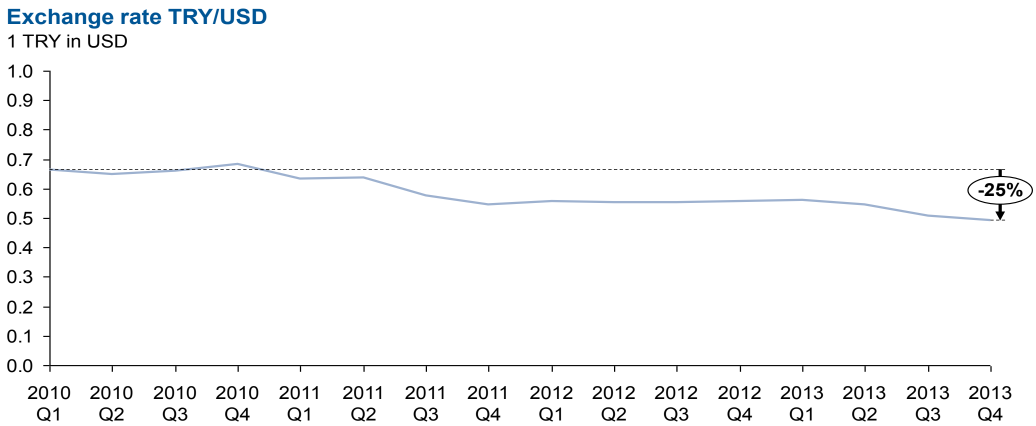
Figure 20: Unit cost development



Source: S&P Capital IQ, Seabury analysis

Both airlines have been helped by the depreciation of the Turkish Lira that dropped 25% between the first quarter of 2010 and the fourth quarter of 2013, as shown below.

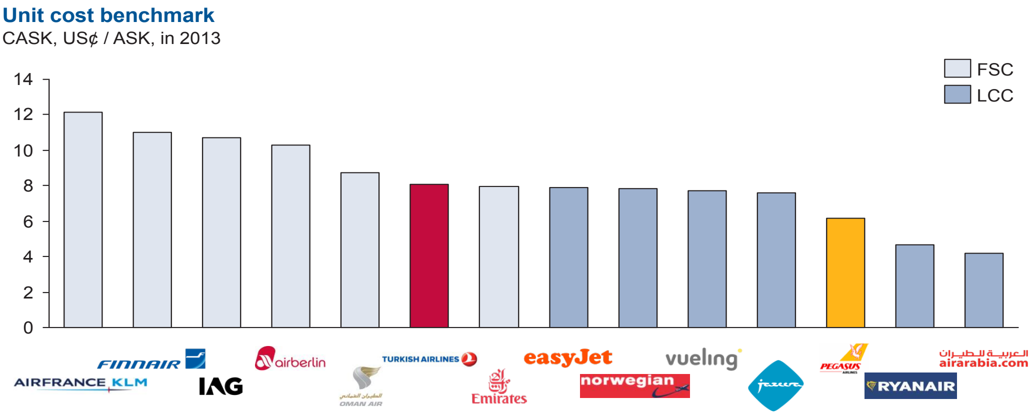
Figure 21: Exchange rate



Source: OANDA, Seabury analysis

Overall, both airlines are competitive in terms of unit costs in their respective categories. With a unit cost of US¢ 8.1 per ASK, Turkish Airlines was one of the full service carriers with the lowest cost per ASK in 2013. Out of the selection of FSC, only Emirates had a slightly lower unit cost, the latter benefiting from a longer average stage length. Pegasus Airlines also benefits from a low cost structure. Its unit cost was about 30% higher than ultra-low cost Ryanair but more than 20% lower than easyJet and other major European LCCs in 2013.

Figure 22: Unit cost comparison with selection of airlines



Note: figures correspond to FY13 (as defined by each individual carrier)
Source: S&P Capital IQ, Seabury analysis

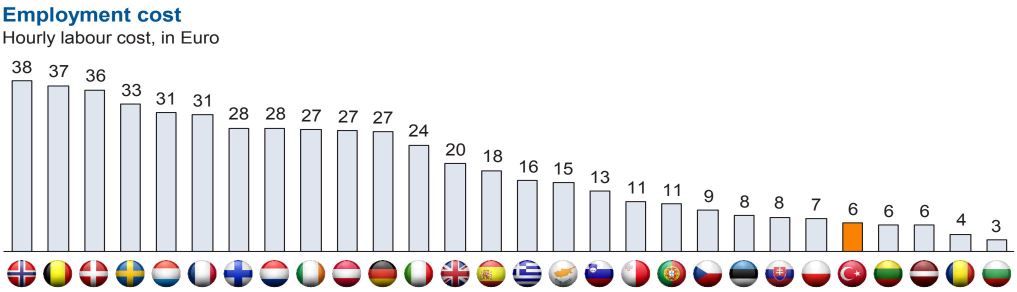
Labour

Turkish Airlines has increased its personnel efficiency from 1,644 passengers per employee in 2010 to 2,084 passengers per employee in 2013[6]. This increase in labour efficiency (combined with the depreciation of the Turkish lira) was translated into a decrease in personnel cost per ASK of almost 25% in US dollars.

Pegasus Airlines followed the opposite trend as its labour efficiency decreased from 6,641 passengers per employee in 2012 (almost at easyJet's level of 6,797 passengers per employee in 2013) to 5,417 passengers per employee in 2013.[7] The gap in terms of passengers per employee between the two Turkish carriers can be explained by their different business models (long haul vs. short haul and FSC vs. LCC).

Turkish carriers have access to affordable labour forces as shown in Figure 22, which compares employment costs across different European countries. With an hourly employment cost of €6, Turkey has one of Europe's lowest costs of employment. Employment in Turkey is three times less expensive than in Spain, more than four times less expensive than in Germany and five times less expensive than in France. This is a material advantage for the Turkish carriers ensuring lower labour cost (corresponding to employees directly employed by the airlines) but also lower handling costs (ground handling, catering, airport services, etc.).

Figure 23: Employment cost by country in Europe



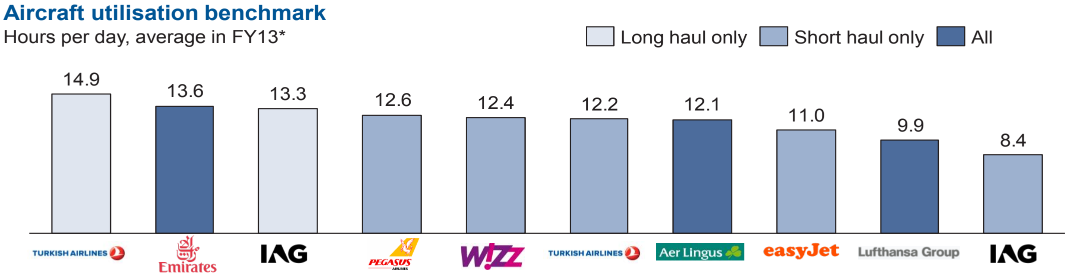
Note: excluding apprentices, cost per employee in full-time units in business economy, average by country
Source: Eurostat (2008), Seabury analysis

Aircraft utilisation

Turkish Airlines increased its average aircraft utilisation by 5% between 2010 and 2013. According to the airline, its narrowbody utilisation went from 11.9 to 12.2 hours per day (+3%) and its widebody utilisation from 13.3 to 14.9 (+12%). Pegasus Airlines also improved aircraft utilisation between 2012 and 2013, and reported a daily utilisation of 12.6 hours in 2013, up 8% compared to the previous year.

The production rates reached by the two Turkish carriers are among the highest in the industry. With almost 15 hours per day, Turkish airlines utilises its widebody fleet more than any airline of the benchmark set. Pegasus Airlines achieved the highest narrowbody aircraft utilisation, more productive with its aircraft than other European LCCs such as WizzAir and easyJet. Turkish Airlines also achieved very high asset utilisation, with its narrowbody utilisation being higher than easyJet's.

Figure 24: Aircraft utilisation



Note: *except WizzAir (FY14)
Source: Airlines' annual reports and investor presentations, CAPA, Seabury analysis

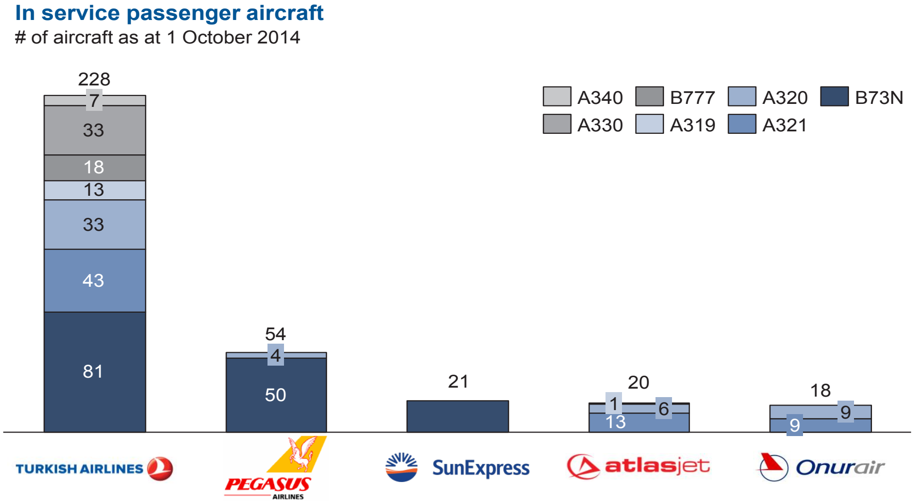
Fleet

Turkish Airlines is by far the largest Turkish airline in terms of fleet of passenger aircraft. With 228 aircraft as of October 2014, the national carrier is more than four times the size of the second largest Turkish operator, Pegasus Airlines. Turkish Airlines is also the only Turkish operator with widebody aircraft in its fleet, with 40 Airbus aircraft (33 A330s and 7 A340s) and 18 Boeings.

The narrowbody fleet of Turkish Airlines is comprised of a mix of B737s and A320 Family aircraft, each of them representing approximately half of the narrowbody fleet. Both sub-fleets include the three variants of the types: the Boeing sub-fleet comprises B737-700s, -800s and -900ERs, while the Airbus sub-fleet comprises A319s, A320s and A321s. This mix gives the airline maximum flexibility to adjust aircraft capacity to best match the market demand.

Pegasus Airlines, as a traditional low-cost airline, uses mainly B737-800 aircraft. However, its fleet also includes 4 A320s. SunExpress operates a single-type fleet of 21 B737-800s, while Atlas Jet and Onur Air operate fleets of Airbus narrowbodies.

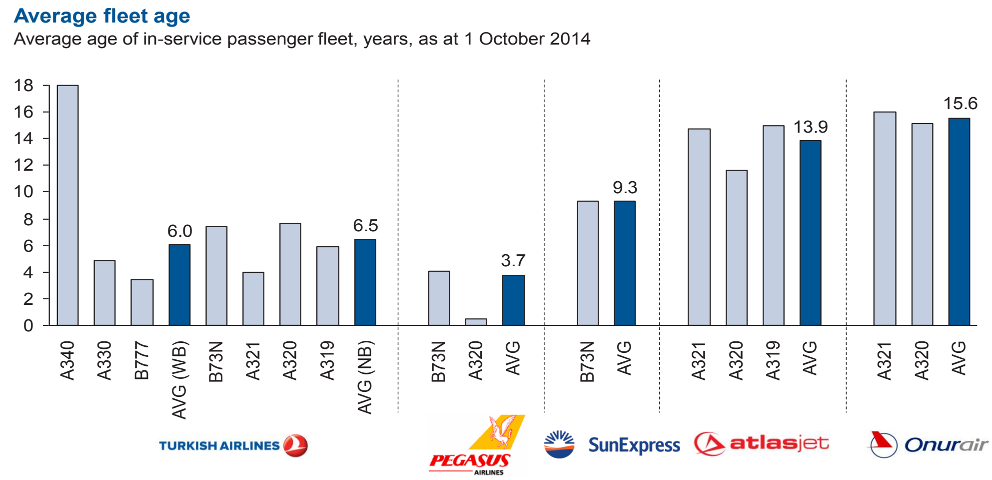
Figure 25: Aircraft utilisation



Source: ASCEND, Pegasus Airlines' investor presentation Q3 2014, Seabury analysis

The two largest operators, Turkish Airlines and Pegasus Airlines, have relatively young fleets. Even with its ageing, soon to be phased out A340s, the average age of Turkish Airlines' widebody fleet does not exceed 6 years. Its narrowbody fleet's average age is 6.5 years. Pegasus Airlines' fleet is even younger with an average age of only 3.7 years. The other Turkish operators operate older fleets. While SunExpress' average fleet age remains under the 10 year mark, Atlasjet and Onur Air operate significantly older aircraft.

Figure 26: Average fleet age of Turkish Operators



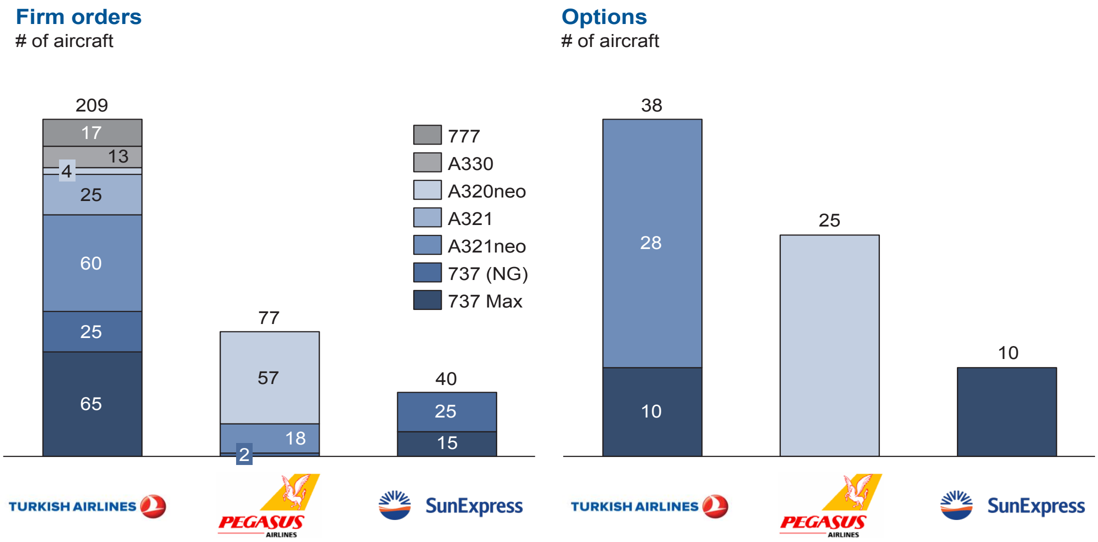
Note: average Pegasus B73N fleet age of based on 43 of the 50 aircraft, as available in ASCEND
Source: ASCEND, Seabury analysis

Despite their ageing fleet, Atlasjet and Onur Air are the only Turkish operators with no current orders. Turkish Airlines has firm orders for 30 new widebody aircraft. Some of these aircraft will surely be used to replace its ageing seven A340s while most of its new deliveries are likely to be used for growth on long-haul markets. The national carrier is also expected to receive 179 new narrowbody aircraft between 2015 and 2020. These new aircraft are likely to be used for both fleet replacement and fleet expansion. In addition to these firm orders, Turkish Airlines also placed options for an additional 38 narrowbody aircraft, all of which are next generation aircraft (MAX and neo).

In late 2012, Pegasus Airlines placed an order for 100 new Airbus aircraft. This order of A320neo and A321neo aircraft was the largest ever aircraft order in the history of Turkish Civil Aviation.[8] This order is split between 75 firm orders (57 A320neo and 18 A321neo) and 25 options (all A320neo), with deliveries expected between 2015 and 2022.

More recently, SunExpress finalised an order for 15 737 MAX 8s and 25 Next-Generation 737-800 airplanes. The order, revealed in February 2014, also includes options for 10 additional 737 MAX 8s.[9]

Figure 27: Airlines backlogs as at 9 October 2014



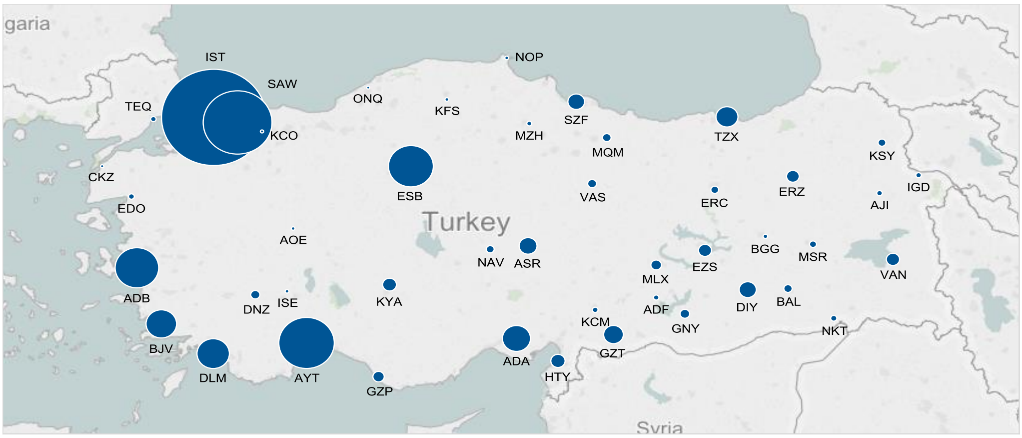
Source: ASCEND, Seabury analysis

Infrastructure development

45 airports served the Turkish aviation market in July 2014, geographically distributed across the Turkish territory. The largest, Istanbul Atatürk Airport (IST), handled more than twice the traffic of the second largest Turkish airport, Sabiha Gökçen International Airport (SAW). Antalya Airport (AYT) was the third largest airport in July 2014, with more departing seats than the airport of the Turkish capital Ankara, Esenboğa International Airport (ESB).

Figure 28: Airports in Turkey

Turkish airports

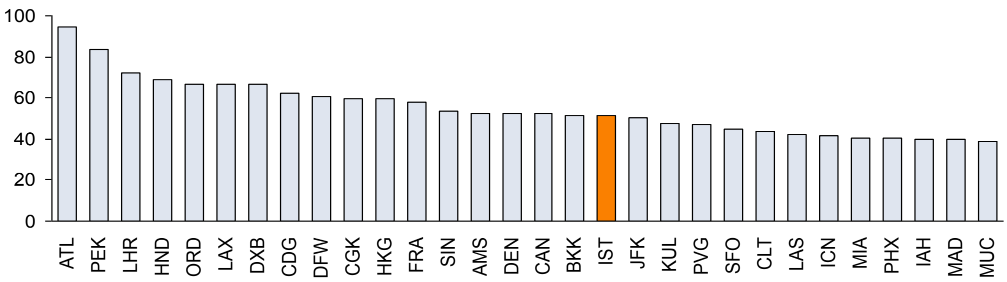


Note: Size proportional to departing seats in July 2014
Source: DiioMi, Seabury analysis

With more than 50 million passengers handled in 2013, Istanbul Atatürk Airport is the 18th largest airport in the world. It is also the fifth largest airport in Europe, after London Heathrow, Paris Charles de Gaulle, Frankfurt and Amsterdam Schiphol. It serves the city of Istanbul, together with the Sabiha Gökçen International Airport which sits across the Bosphorus and handled over 18 million passengers in 2013.[10]

Figure 29: Largest airports worldwide

World's 30 largest airports
Passengers in 2013, in millions

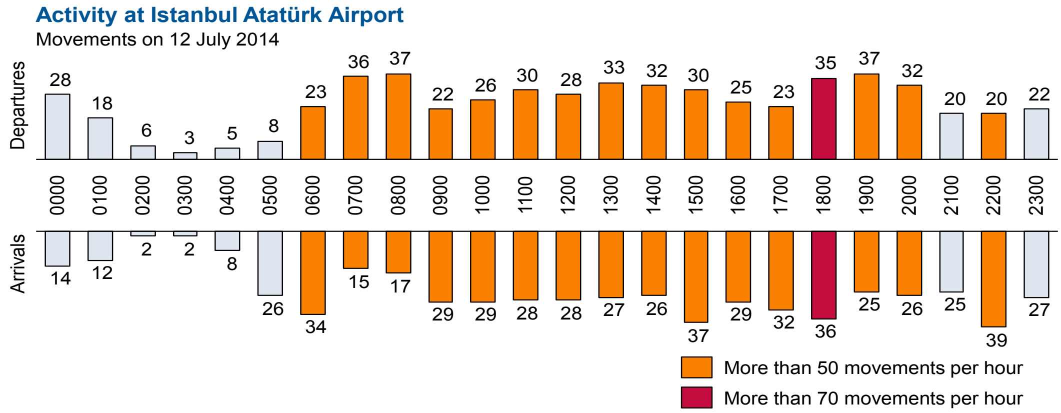


Source: Airports Council International via Port authority of NY & NJ, Seabury analysis

Focus on Istanbul

Istanbul Atatürk Airport (IST) currently has three runways, with capacity for 55 movements per hour and official terminal capacity of around 40 million passengers[11]. The airport handled more than 50 million passengers in 2013 and aircraft movements exceed 55 per hour during most of the day (Figure 29). Studies are currently being conducted on a potential addition of a fourth runway, as requested by Turkish Airlines. The project, which has been approved by the Government[12], would increase the airport's runway capacity to 70 movements per hour. Increases in terminal capacity, aircraft stands and aircraft parking capacity are also being planned but the lack of available land is a significant constraint.

Figure 30: Current activity level at IST



Source: DiioMi, Seabury analysis

Sabiha Gökçen International Airport (SAW) has one runway, with capacity for 28 movements per hour and has plans to add a second runway. Its terminal capacity is around 25 million passengers per annum (the airport handled approximately 18 million passengers in 2013).

Even with the planned enhancements to capacity at the two existing airports, the Turkish Government and the Turkish aviation sector have agreed that the construction of a third Istanbul airport is needed. A tender for a Build Operate Transfer contract was completed on 3 May 2013 and won by a consortium of construction companies. Cengiz-Kolin-Limak-Mapa-Kalyon Consortium, a Turkish joint venture, won the tender to build the third Istanbul airport after bidding 22 billion euros for a 25-year lease to build and operate the planned airport.[13] The first stage of the six-runway airport is planned to accommodate 90 million passengers and, in its completed state, will be able to accommodate 150 million passengers. In its final phase, it will have four connected terminals and six runways. The new airport is planned to open in late 2017.[14]

The new Istanbul airport aims to rival Dubai's Al Maktoum International Airport (DWC), which opened in October last year and is expected to eventually accommodate 160 million passengers a year. However, its construction faces regular hurdles that may delay its opening. In early 2014, the Istanbul Administrative Court ordered the suspension of the construction after an environmental organisation filed a lawsuit. This decision triggered active debates between the airlines, the airport operator, the government and other political parties. Besides environmental concerns, location and investor/contractor insurance issues were also raised and the perceived urgent need for a third airport suddenly appeared to be in danger. Nevertheless, the new airport project has rallied and Turkey's (then) Prime Minister Erdogan laid the first stone in June, reiterating that the airport is expected to open in late 2017 and to be fully operational the following year.

Regulatory Environment

Turkey remains under bilateral agreements, allowing the country to actively control the competition. But with the aggressive growth plan of its national carrier, Turkish Airlines, Turkey has grown its international network rapidly, increasing the number of bilateral agreements from 81 in 2003 to 162 in 2014.

In March 2010, the European Union and the Turkish authorities initiated a “horizontal” air transport agreement which removes nationality restrictions in the bilateral air services agreements between EU Member States and Turkey. This allows any EU airline to operate flights between any EU Member State and Turkey, where a bilateral agreement with Turkey exists and traffic rights are available.[15]

Closing thoughts

Turkey has played a major role in the global aviation industry in the last decade. Its national airline, Turkish Airlines, has become one of the largest global airlines and has invested heavily in its product and its brand to establish itself as a reference airline. With the aim to be the airline serving the largest number of countries worldwide, Turkish Airlines has grown its international network and will continue to do so. With a distinctive slogan, “Globally Yours”, Turkish Airlines aims at becoming an airline of choice to connect the world via Istanbul. Turkey is also the home of dynamic leisure airlines that are transitioning from charter carriers to scheduled airlines. The largest of them, Pegasus Airlines, is on its way to becoming one of the reference low cost airlines in Europe. With a low cost structure, it is expected to stimulate traffic by giving access to air travel to the growing middle class, both in Turkey and abroad. Armed with successful network and budget carriers, Turkey is expected to have a growing role in the global aviation market. The country seems to be working together with all actors of the aviation industry with an ambitious global aviation strategy. It will be the home of one of the largest airports in the world, the third Istanbul airport, and actively supports the national carrier in its expansion into emerging markets such as Africa.

1 Source: CIA World Factbook
2 Source: Press article “Pegasus Airlines’ Secrets of Success Shared At World Low Cost Airlines Congress 2014”, flypgs.com
3 Source: Ministry of Foreign Affairs of Turkey, http://www.mfa.gov.tr/turkey-africa-relations.en.mfa
4 Source: Turkish Airlines’ Dec. 2013 investor presentation: http://investor.turkishairlines.com/documents/ThyInvestorRelations/download/trafik/sunum_aralik_2013.pdf
5 Source: Pegasus Airlines’ FY2013 investor presentation
6 Source: Turkish Airlines 2014 Q3 Results Summary
7 Source: Seabury analysis based on airline’s investor presentations and annual reports
8 Source: http://www.flypgs.com/en/about-pegasus/news/690/pegasus-airlines-places-the-largest-ever-aircraft-order-in-the-history-of-turkish-civil-aviation.aspx
9 Source: http://boeing.mediaroom.com/2014-02-19-Boeing-SunExpress-Finalize-Order-for-15-737-MAXs-25-Next-Generation-737s
10 Source: http://www.sabihagokcen.aero/corporate-info/airport-traffic-report
11 Source: http://centreforaviation.com/analysis/turkeys-aviation-market-healthy-growth-to-continue-at-one-of-the-worlds-oldest-cross-roads-133780
12 Source: http://www.routesonline.com/news/37/momberger-airport-information/168563/istanbuls-ataturk-airport-to-get-4th-runway/
13 Source: http://english.alarabiya.net/en/business/aviation-and-transport/2014/02/11/Turkey-defies-court-order-vows-to-build-new-airport.html
14 Source: http://www.dailysabah.com/money/2014/10/17/turkeys-aviation-sector-to-carry-170-million-passengers-by-end2014
15 Source: http://ec.europa.eu/transport/modes/air/international_aviation/country_index/turkey_en.htm

Statistics

Executive Summary Statistics

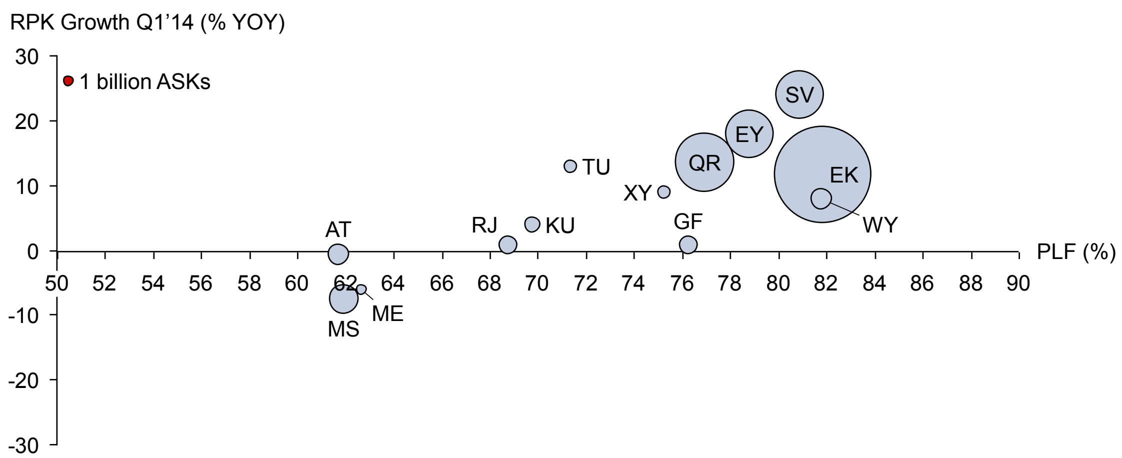
Source: AACO
Note: Includes scheduled operations for AT, EK, EY, GF, KU, ME, MS, QR, RJ, SV, TU, WY, XY

	Total	Q1 Year-on-Year Change	International	Q1 Year-on-Year Change	Domestic	Q1 Year-on-Year Change
No. of Pax	37,209,752	11.6%	31,978,248	11.8%	5,231,504	10.6%
Tonnes Cgo	1,169,845	8.9%	1,141,252	9.4%	28,592	-10.2%
RPKs (000)	126,772,626	12.0%	122,475,341	12.0%	4,297,285	12.2%
ASKs (000)	161,696,187	11.7%	156,556,400	11.6%	5,139,787	12.4%
Pax Load Factor	**78.40%**	**0.25%**	**78.23%**	**0.26%**	**83.6%**	**-0.15%**
RTKs (000)	16,048,776	11.8%	15,701,152	12.0%	338,475	3.80%
ATKs (000)	23,878,679	9.2%	23,329,155	9.3%	525,968	0.5%
Weight Load Factor	**67.21%**	**1.61%**	**67.30%**	**1.59%**	**64.35%**	**2.05%**

AACO members passenger size and growth

Fig 1 - Year-on-year revenue passenger kilometers (RPKs) growth versus passenger load factor (PLF). Bubble size indicates carrier size measured as available seat kilometers (ASKs)

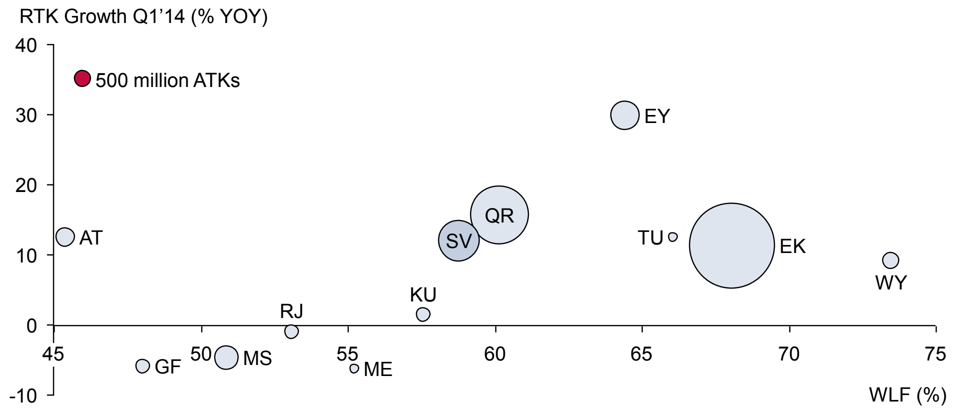
Source: AACO



AACO members cargo size and growth

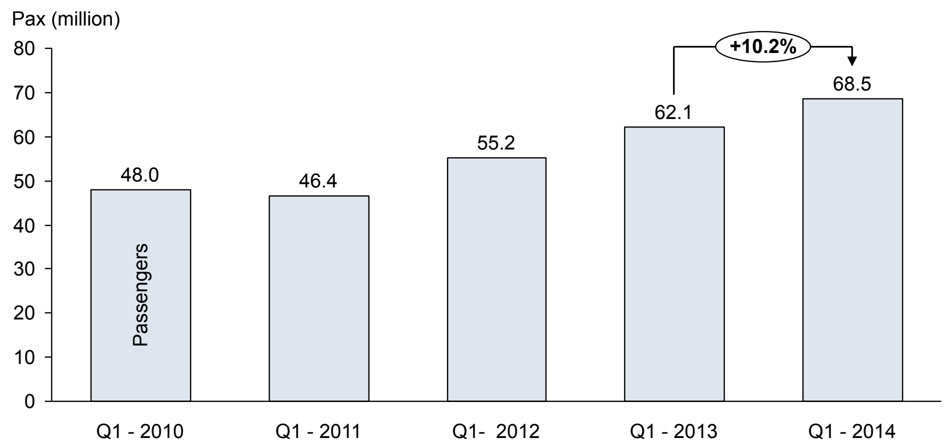
Fig 2 - Year-on-year revenue tonne kilometers (RTKs) growth versus weight load factor (WLF). Bubble size indicates carrier size measured as available tonnes kilometers (ATKs)

Source: AACO



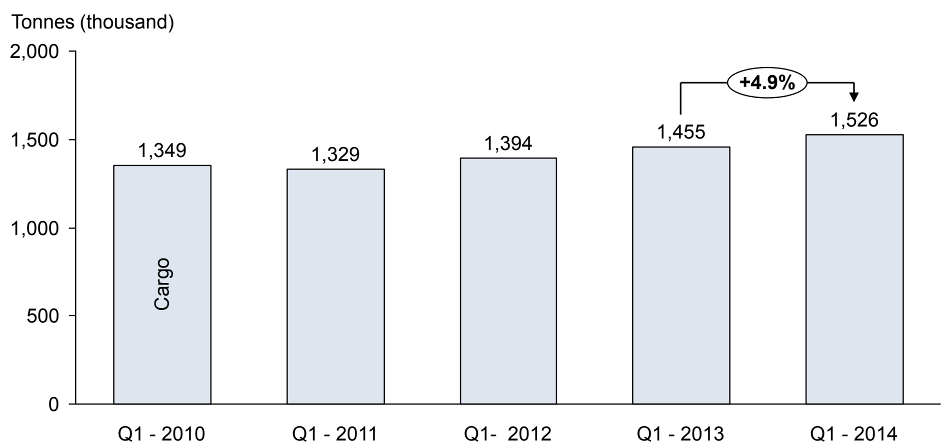
Arab passenger growth

Fig 3 - Historical trend of first quarter passenger transit volume in most Arab airports
Source: AACO, ACI



Arab cargo growth

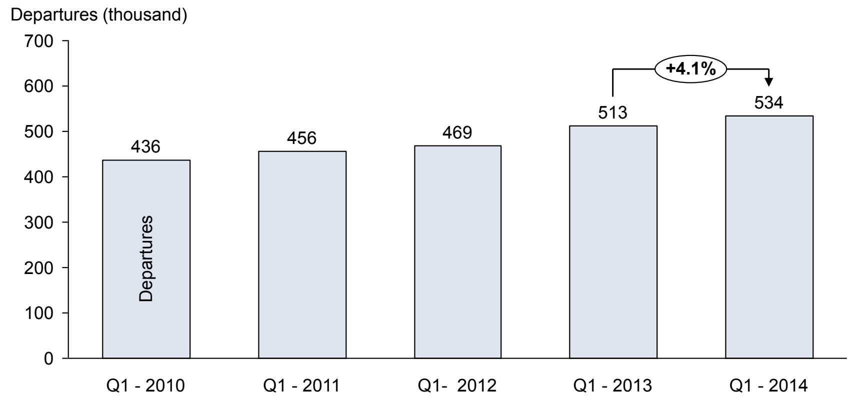
Fig 4 - Historical trend of first quarter cargo transported in most Arab airports
Source: AACO, ACI



Arab departure growth

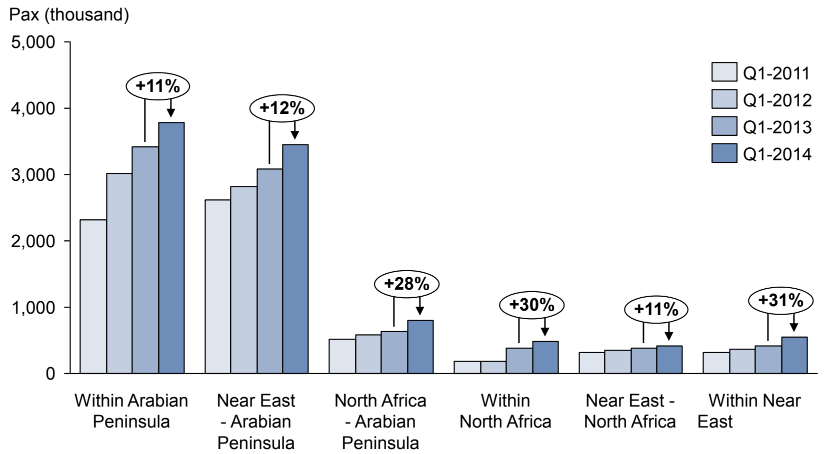
Fig 5 - Historical trend of first quarter traffic volume in most Arab airports

Source: AACO, ACI



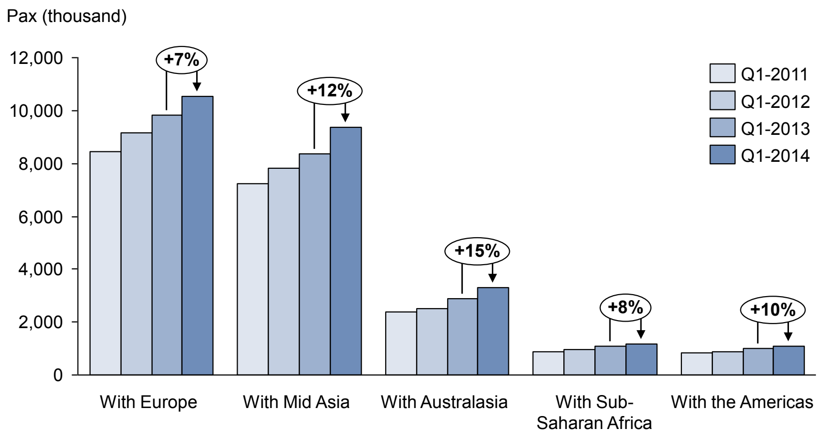
Intra-regional Arab market

Fig 6 – First quarter international Arab market passenger numbers within the Arab World
Source: AACO, IATA



Inter-regional Arab market

Fig 7 - First quarter Arab market passenger numbers to/from the Arab world
Source: AACO, IATA



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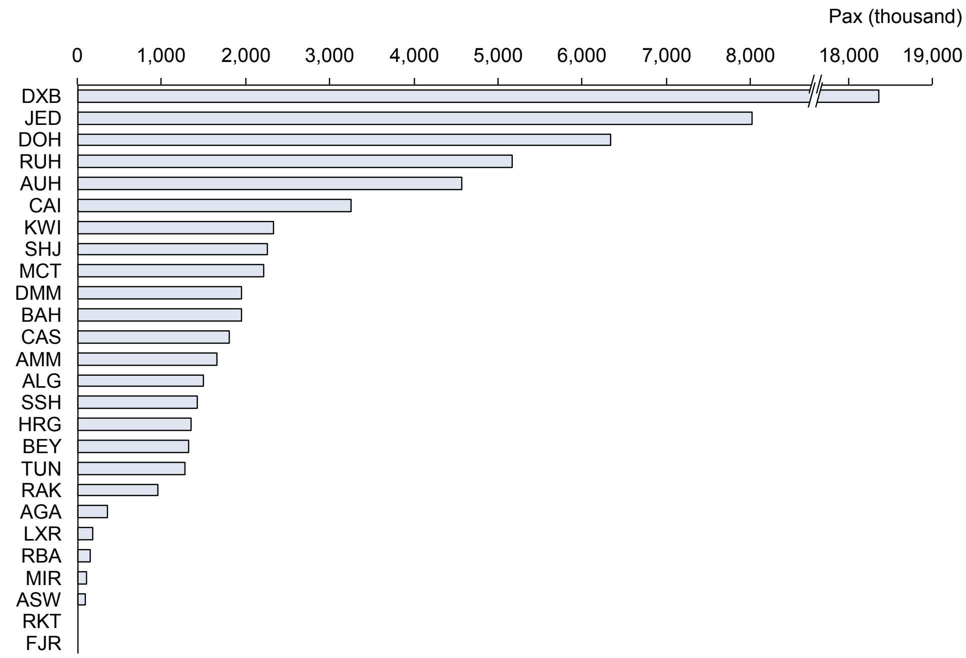
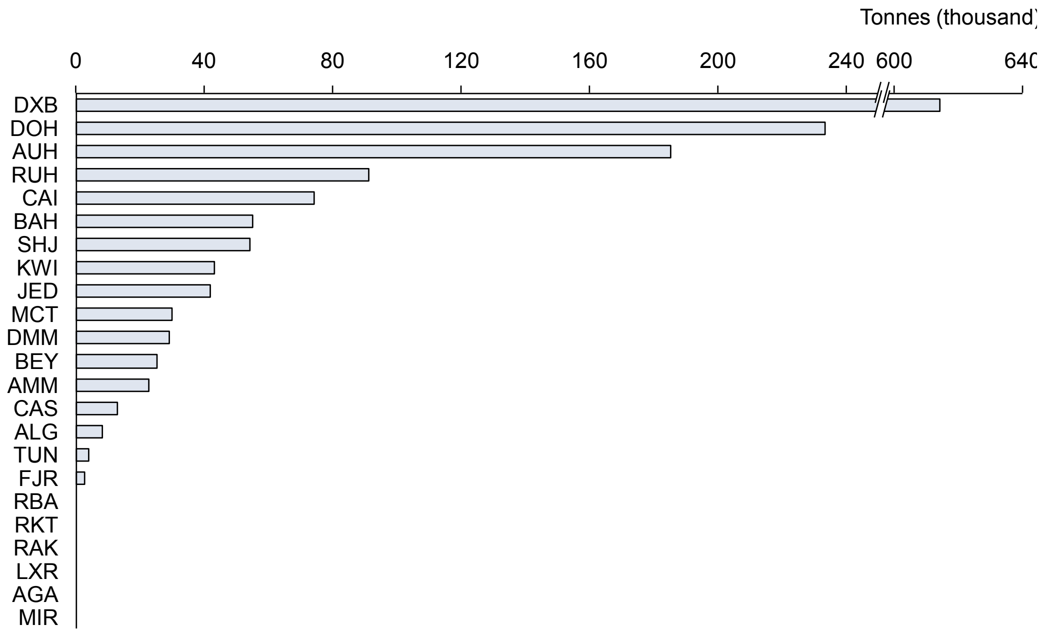
Airport passenger volume

Fig 8 - 2014 first quarter passenger volume in most Arab airports by port
Source: AACO, ACI



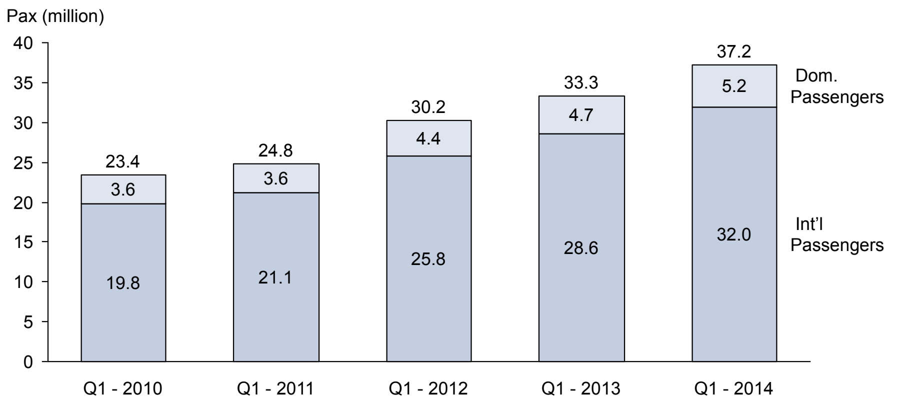
Airport cargo volume

Fig 9 – 2014 first quarter cargo volume in most Arab airports by port
Source: AACO, ACI



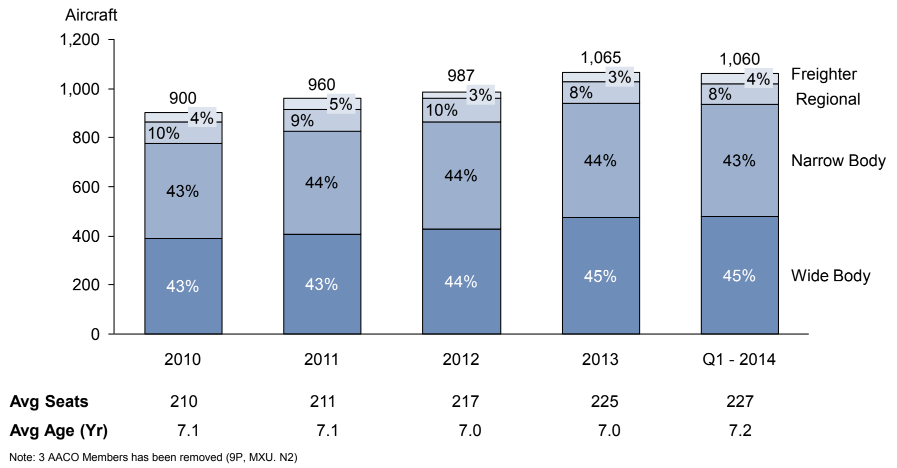
Domestic and international

Fig 10 - First quarter AACO members' domestic/regional and international passenger volume historical trend
Note: Includes scheduled operations for AT, EK, EY, GF, KU, ME, MS, QR, RJ, SV, TU, WY, XY
Source: AACO



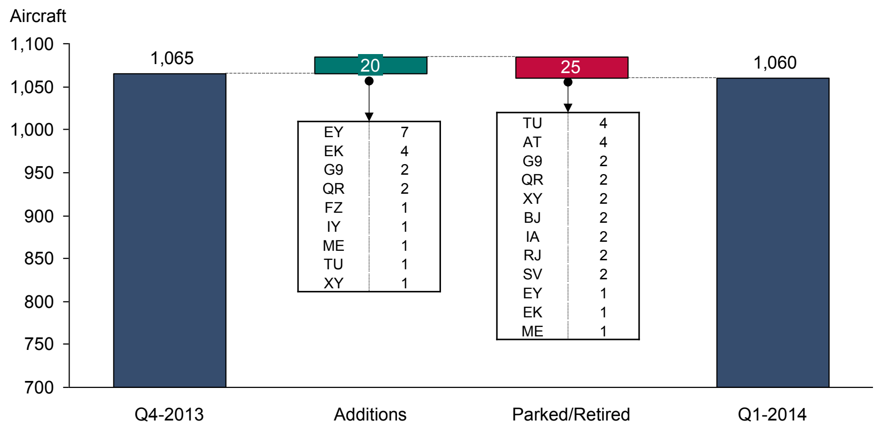
Fleet growth

Fig 11 - AACO members combined fleet growth by aircraft type
Source: AACO, ASCEND



Fleet changes this quarter

Fig 12 – First quarter changes to the AACO fleet by carrier
Source: AACO, ASCEND



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