

TÜRK HAVA YOLLARI ANONİM ORTAKLIđI

FINANCIAL STATEMENTS

PREPARED IN ACCORDANCE WITH

INTERNATIONAL FINANCIAL REPORTING STANDARDS

FOR THE YEAR ENDED

31 DECEMBER 2005

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Türk Hava Yolları Anonim Ortaklığı

1. We have audited the accompanying balance sheet of Türk Hava Yolları Anonim Ortaklığı (“the Company”) as at 31 December 2005, and the related statements of income, changes in shareholders' equity and cash flows for the year then ended, all expressed in the equivalent purchasing power of the New Turkish Lira at 31 December 2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

2. We conducted our audit in accordance with International Standards on Auditing. 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. 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 financial statements referred to above present fairly, in all material respects, the financial position of the Company as of 31 December 2005, and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards (“IFRS”).

Can Uluslararası Denetim A.Ş.
A Member Firm of INPACT International

İsmail USLU
Partner

13 April 2006, İstanbul, Turkey

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
BALANCE SHEETS
AS AT 31 DECEMBER 2005 AND 2004

*(All amounts expressed in New Turkish Lira (YTL) in terms of
purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)*

	<u>Note</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
ASSETS			
Cash and cash equivalents	5	482.910.555	382.255.154
Accounts receivable (net)	6	191.596.806	165.792.500
Due from related parties	7	970.701	849.867
Inventories	8	84.674.663	67.445.899
Prepaid tax	23	13.363.884	53.637.690
Other short-term receivables and assets	9	52.944.957	38.118.993
Total current assets		<u>826.461.566</u>	<u>708.100.103</u>
Investments at equity	10	17.490.282	17.465.262
Financial assets available for sale	10	19.993.581	27.108.556
Tangible fixed assets (net)	11	2.071.099.171	1.892.760.028
Intangible fixed assets (net)	12	6.360.178	7.802.787
Advances given for aircraft	13	573.169.605	414.950.866
Other long-term receivables and assets	14	11.557.821	13.953.943
Total non-current assets		<u>2.699.670.638</u>	<u>2.374.041.442</u>
Total assets		<u>3.526.132.204</u>	<u>3.082.141.545</u>

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
BALANCE SHEETS
AS AT 31 DECEMBER 2005 AND 2004

*(All amounts expressed in New Turkish Lira (YTL) in terms of
purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)*

	<u>Note</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
LIABILITIES			
Bank borrowings	15	363.235.861	294.026
Short-term portion of finance lease obligations	16	179.092.821	211.925.219
Accounts payable		252.279.781	195.027.513
Due to related parties	17	8.022.859	6.804.010
Other short-term payables	18	37.952.344	39.702.806
Deposits and advances received	19	56.412.654	40.432.199
Passenger flight liabilities	20	209.797.889	184.838.378
Other accrued liabilities	21	92.206.894	73.156.705
Total current liabilities		<u>1.199.001.103</u>	<u>752.180.856</u>
Long-term portion of finance lease obligations	16	856.730.859	1.001.256.055
Manufacturers' credit (net)	22	3.491.212	2.499.897
Deposits and advances received	19	7.124.266	8.945.711
Deferred tax liabilities	23	92.353.486	48.597.403
Retirement pay liability	24	113.641.242	104.312.102
Other long-term payables	18	-	3.782.773
Total non-current liabilities		<u>1.073.341.065</u>	<u>1.169.393.941</u>
SHAREHOLDERS' EQUITY			
Share capital	25	2.000.994.542	2.000.994.542
Reserves		147.576.470	147.576.470
Share premium		936.192	936.192
Accumulated losses		(895.717.168)	(988.940.456)
Total shareholders' equity		<u>1.253.790.036</u>	<u>1.160.566.748</u>
Total liabilities and shareholders' equity		<u>3.526.132.204</u>	<u>3.082.141.545</u>

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
STATEMENTS OF INCOME
FOR THE YEARS ENDED 31 DECEMBER 2005 AND 2004

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

	<u>Note</u>	<u>1 January - 31 December 2005</u>	<u>1 January- 31 December 2004</u>
Operating revenues	30 and 35	3.139.178.553	2.920.341.113
Operating expenses (-)	31 and 35	<u>(3.054.728.897)</u>	<u>(2.771.314.056)</u>
Main Operating Profit		84.449.656	149.027.057
Income from other operations	33 and 35	111.015.890	66.327.837
Loss from other operations (-)	34	<u>(27.159.903)</u>	<u>(16.588.648)</u>
Operating Profit		168.305.643	198.766.246
Financial income/(expense) (net)	32	(57.286.976)	34.459.166
Monetary gain/(loss) (net)		<u>28.073.365</u>	<u>(118.355.242)</u>
Profit Before Taxation		139.092.032	114.870.170
Taxation charge	23	(45.868.744)	(2.946.085)
Net Profit		<u>93.223.288</u>	<u>111.924.085</u>
Earnings Per Share (YTL, in full)	3.17	0,00053	0,00064

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED 31 DECEMBER 2005 AND 2004

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

	<u>Share capital</u>	<u>Reserves</u>	<u>Share premium</u>	<u>Accumulated losses</u>	<u>Total shareholders' equity</u>
Balances at 1 January 2004	2.000.994.542	147.576.470	936.192	(1.100.864.541)	1.048.642.663
Net profit for the year	-	-	-	111.924.085	111.924.085
Balances at 31 December 2004	<u>2.000.994.542</u>	<u>147.576.470</u>	<u>936.192</u>	<u>(988.940.456)</u>	<u>1.160.566.748</u>
Balances at 1 January 2005	2.000.994.542	147.576.470	936.192	(988.940.456)	1.160.566.748
Net profit for the year	-	-	-	93.223.288	93.223.288
Balances at 31 December 2005	<u>2.000.994.542</u>	<u>147.576.470</u>	<u>936.192</u>	<u>(895.717.168)</u>	<u>1.253.790.036</u>

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI
STATEMENTS OF CASH FLOW
FOR THE YEARS ENDED 31 DECEMBER 2005 AND 2004

*(All amounts expressed in New Turkish Lira (YTL) in terms of
purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)*

	1 January- 31 December 2005	1 January- 31 December 2004
Cash flows from operating activities:		
Profit before taxation	139.092.032	114.870.170
Adjustments to reconcile profit for the period to net cash provided by operating activities:		
Depreciation	311.755.353	314.106.918
Provision for retirement pay liability	16.216.555	17.339.314
Interest income	(42.433.556)	(44.176.637)
Gain on sales of fixed asset	(3.035.861)	(632.565)
Monetary gain on deferred taxes liabilities	(2.112.661)	(6.318.246)
Change in provision for diminution in value of fixed assets	(63.511.531)	(23.260.405)
Income from financial investment accounted per equity method	(784.282)	(9.006.930)
Interest expense	57.821.640	48.793.420
Movement in manufacturers' credit	991.315	(2.558.749)
Foreign exchange (gain)/loss on financial leases (net of monetary gain)	(50.510.861)	32.325.608
Provision for diminution in value of financial assets available for sale	7.784.603	(7.325.359)
Amortization of deferred income from USAŞ shares transfer	(2.307.710)	(1.567.253)
Decrease in provision for doubtful receivables	(906.262)	(5.509.451)
Expensed portion of previous year's prepaid tax	2.378.934	-
Operating profit before working capital changes	370.437.708	427.079.835
Increase in accounts receivable	(24.898.044)	(19.679.318)
Increase in due from related parties	(120.834)	(708.761)
Increase in inventories	(17.228.764)	(12.916.026)
(Increase)/Decrease in other short term receivables and assets	(12.429.842)	91.505.069
Increase/(Decrease) in accounts payable	57.252.268	(7.195.714)
Increase in due to related parties	1.218.849	412.410
Increase/(Decrease) in other accrued liabilities and other long term payables	15.824.664	(39.798.829)
Increase/(Decrease) in deposits and advances received	14.159.010	(25.823.871)
Increase in passenger flight liabilities	24.959.511	60.061.136
Retirement benefits paid	(6.887.415)	(6.624.737)
Interest paid	(59.179.468)	(50.891.819)
Prepaid tax	(13.363.884)	(76.562.711)
Previous years prepaid tax to be returned	51.258.756	-
Net cash provided by operating activities	401.002.515	338.856.664
Cash flows from investing activities		
Cash outflow from purchase of financial assets	-	(8.580)
Cash inflow from sale of financial assets	89.634	-
Cash inflow from sale of tangible and intangible fixed assets	61.814.841	7.268.119
Interest received	42.433.556	44.176.637
Acquisition of tangible and intangible fixed assets	(483.919.336)	(123.952.512)
Advances given for aircraft	(158.218.739)	(405.344.077)
Net cash used in investing activities	(537.800.044)	(477.860.413)
Cash flows from financing activities		
Principal payment of financial leases	(387.625.942)	(264.304.167)
Change in financial lease obligations	262.137.037	-
Change in bank borrowings	362.941.835	294.026
Net cash provided by/(used in) financing activities	237.452.930	(264.010.141)
Net increase/(decrease) in cash and cash equivalents	100.655.401	(403.013.890)
Cash and cash equivalents at the beginning of period	382.255.154	785.269.044
Cash and cash equivalents at the end of period	482.910.555	382.255.154

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

1 THE COMPANY'S ORGANIZATION AND 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 31 December 2005, the shareholders and their respective shareholdings in the Company were as follows:

Republic of Turkey Prime Ministry Privatization Administration	75,18	%
Others	24,82	%
Total	<u>100,00</u>	%

The total number of employees working for the Company as of 31 December 2005 is 11.121 (2004: 10.956). The average number of employees working for the Company in the years 2005 and 2004 is 11.151 and 10.341, respectively. Financial assets of the Company are stated at note 10.

The Company is registered in İstanbul, Turkey and its head office address is as follows:

THY Genel Yönetim Binası, Atatürk Havalimanı, 34149 Yeşilköy- İstanbul.

2 BASIS OF PRESENTATION OF FINANCIAL STATEMENTS

Accounting Standards Applied:

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") (formerly referred to as International Accounting Standards "IAS"). The bases used in the preparation of the accompanying financial statements are as follows:

The Company maintains its books of account and prepares its statutory financial statements in accordance with accounting principles promulgated by Turkish Commercial Code (the "TCC"), Capital Market Board of Turkey ("CMB"), and tax legislation. The accompanying financial statements are based on the statutory records, with adjustments and reclassifications, including restatement for the changes in the general purchasing power of New Turkish Lira, for the purpose of fair presentation in accordance with IFRS.

The bases of the financial statements used in the preparation of the accompanying financial statements are set out below and in Note 3.

Inflation Accounting:

In the accompanying financial statements, restatement adjustments that are made to compensate for the effect of changes in the general purchasing power of New Turkish Lira are based on International Accounting Standard No: 29 "Financial Reporting in Hyperinflationary Economies" ("IAS 29").

IAS 29 requires that financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date and the corresponding figures for previous periods be restated in the same terms.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

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

One characteristic that leads to the classification of an economy as hyperinflationary, necessitating the application of IAS 29, is a cumulative three-year inflation rate approaching or exceeding 100%. Such cumulative rate in Turkey is 35,6% for the three-year ended 31 December 2005 (2004: 69,7%) based on the wholesale price index ("WPI") announced by the Turkish State Institute of Statistics. Based on the current trends and developments, Turkey will come of hyperinflationary status effective from 1 January 2006.

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 the accompanying financial statements were inflation adjusted.

The indices and the conversion factors used to restate the accompanying financial statements as at 31 December 2005 and 31 December 2004 are given below:

<u>Dates</u>	<u>Index</u>	<u>Conversion Factor</u>	<u>Three years cumulative inflation rates (%)</u>
31 December 2004	8.403,80	1,04545	69,7
31 December 2005	8.785,74	1,00000	35,6

As at 31 December 2005, the exchange rate announced by Central Bank of Turkey was YTL 1,3418=US Dollar 1 (2004: YTL 1,3421=US Dollar 1).

The main procedures for the application of IAS 29 are as follows:

- All amounts not already expressed in terms of the measuring unit current at the balance sheet date are restated by applying the relevant conversion factors. Corresponding figures for previous periods are similarly restated.
- Monetary assets and liabilities are not restated because they are already expressed in terms of the monetary unit at the balance sheet date. Monetary items are money held and items to be received or paid in money.
- Fixed assets, investments and similar assets are restated from the date of their purchase, not to exceed their market value. Depreciation is similarly restated. The components of shareholders' equity are restated by applying the relevant conversion factors from the dates the components are contributed or otherwise arose.
- All items in the statement of income, except for the non-monetary items in the balance sheet, which have an effect on the statement of income, are restated by applying the relevant conversion factors from the dates when the income and expense items are initially recorded in the financial statements.
- The gain or loss on the net monetary position is the result of the effect of general inflation and is the difference resulting from the restatement of non-monetary assets and liabilities, shareholders' equity and items of statement of income. The gain or loss on the net monetary position is included in net income.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

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

New Turkish Lira:

A new law, numbered as 5083 on the Monetary Unit of the Republic of Turkey was enacted with the effect from 1 January 2005, which deletes six zeroes from the former currency of Republic of Turkey, The Turkish Lira ("TL"), to form a new currency the New Turkish Lira ("YTL"). Thus, YTL 1 = TL 1.000.000. The New Turkish Lira is divided into 100 New Turkish cents ("YKr"). As per the CMB decision numbered MSD-10/832-43399 dated 1 December 2004, the financial statements to be announced publicly in 2005 should be prepared in YTL including comparatives. Accordingly, the accompanying financial statements are presented in YTL.

Comparative Information:

Current period financial statements have been prepared as comparative with the prior period financial statements. In order to provide an appropriate presentation of current period's financial statements, the comparative information have been re-classified in terms of any necessity occurrences.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

3.1 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.

Agency commissions to relating to the passenger revenue are recognized as expense when the transportation service is provided.

3.2 Inventory Valuation

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

3.3 Financial Investments

The Company designates its investments portfolio in accordance with IAS 39 ("Financial Instruments: Recognition and Measurement") 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 prices. Subsequent to initial recognition, held for trading securities are valued at their fair value if measured reliably. Gains or losses on these securities are recognized in net profit or loss for the period in which they arise.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

3.3 Financial Investments (cont'd)

Investments Held to Maturity:

Investments held-to-maturity 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:

Investments available-for-sale are those that the ownership rate is less than or equivalent to 20% and are not held for trading. Subsequent to acquisition, available for sale investments which are traded at stock markets is valued at market rate on balance sheet date. Otherwise, they are accounted for in accordance with IAS 29. Gains or losses on available for sale investments are recognized in net profit or loss for the period in which they arise.

Investments at Equity:

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

3.4 Tangible and Intangible Fixed Assets

Tangible Fixed Assets:

Tangible fixed assets are measured at cost restated for the effects of inflation. Depreciation is provided on a periodical basis for all categories of tangible fixed assets.

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

	<u>Useful Life (years)</u>	<u>Residual Value</u>
- Land	-	-
- Buildings	25-50	-
- Aircraft	15	30%
- Engines	15	30%
- Components	5-8-10	-
- Repairables	2-3	-
- Simulators	10	-
- Machinery and Equipments	3-5-7-10	-
- Furniture and Fixtures	3-4-5	-
- Motor Vehicles	4-5-7	-
- Other Equipments	5	-

Intangible Fixed Assets:

Intangible fixed assets include leasehold improvements, rights, information systems and software. Intangible fixed assets are reflected at cost as of 31 December 2005, leasehold improvements are depreciated over their lease periods and other intangible fixed assets are depreciated over their useful life of 5 years, on a periodical basis.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

3.4 Tangible and Intangible Fixed Assets (cont'd)

Impairment on Assets:

According to IAS 29, the Company restates its fixed assets by using WPI. However, in international markets, purchasing and second hand trading of aircraft and similar assets are realized in US Dollar.

As a result of inflation rate being higher than devaluation of YTL against US Dollar in recent years, net book values of aircraft, spare engines and simulators adjusted for the effect of inflation have exceeded net book values of these assets based on their US Dollar acquisition costs. The Company's management considers that the situation explained above causes a fictitious increase in value. Therefore, the Company decreases the adjusted net book value of its aircraft, spare engines and simulators to net book value of these assets based on US Dollar acquisition costs. An examination is then made of whether net book values based on US Dollar acquisition costs may exceed their recoverable amount. Recoverable amount is determined higher of the present value of cash flows expected from the use of assets and their net selling price of these assets. Net selling price is determined according to the International Aircraft Price Guide. In the accompanying financial statements, the difference between adjusted net book values of these assets and net book values based on US Dollar acquisition costs is netted off against monetary gain. The difference between net book values of these assets based on US Dollar acquisition costs and recoverable amount is recognized as impairment loss under operating expenses.

3.5 Borrowing Costs

Banks loans are recognized initially at cost, less attributable transaction costs. Subsequent to initial recognition, borrowings are stated at amortized costs with any difference between cost and redemption value being recognized in the income statement over the period of the borrowings on an effective interest basis. Finance expense resulted from bank loans are recorded to income statement in the period in which they are incurred.

3.6 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.

3.7 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.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

3.8 Frequent Flyer Program

The Company provides a frequent flyer program named “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.

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

3.9 Taxation and Deferred Taxes

Taxes on income for the period comprise of current tax and deferred tax. The Company accounts for current and deferred taxation on the results for the period, in accordance with IAS 12 (“Income Taxes, Revised”).

Provision is made in the financial statements for the Company’s estimated liability for 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 using the liability method in respect of material temporary differences arising from different treatment of items for accounting and taxation purposes.

Deferred tax liabilities are recognized for all taxable temporary differences whereas deferred tax assets are only recognized when it is possible that future taxable profit will be available against which the deductible temporary differences can be utilized.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled. Deferred tax is charged or credited in the statement of income.

Prepaid corporation taxes and corporation tax liabilities are offset as they relate to income taxes levied by the same taxation authority. Deferred tax assets and liabilities are also offset.

3.10 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. Future retirement payments are discounted to their present value at the balance sheet date at an interest rate determined by the net of an expected inflation rate and an appropriate discount rate according to IAS 19 (“Employee Benefits”). The interest amount included in employee retirement expense is disclosed in the financial result as interest expense.

3.11 Related Parties

The shareholders, key management personnel 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. Transactions with related parties for ordinary operations have taken place at prices compliant with market conditions.

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

3.12 Foreign Currency Transactions

Transactions in foreign currencies are translated into New Turkish Lira at the rates of exchange ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated with 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.

The closing and average NTL to US Dollar exchange rates for the periods are as follows:

	<u>Closing Rate</u>	<u>Average Rate</u>
31 December 2004	1,3421	1,4223
31 December 2005	1,3418	1,3405

3.13 Leases

The Company leases aircraft, engines, simulators, computer equipments and vehicles by financial leases or operational leases. According to IAS 17 ("Leases"), finance leases are reflected in the Company's assets by recording leased assets and lease 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.

3.14 Financial Instruments and Financial Risk Management

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.

Financial Assets:

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 such as letters of guarantee and 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-term nature.

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

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

3.14 Financial Instruments and Financial Risk Management (cont'd)

Financial Assets (cont'd):

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.

Book values of trade liabilities and due to related parties are estimated to be their fair value except liabilities discounted to their present value when they hold significant credit periods.

Güneş Ekspres Havacılık A.Ş. is accounted for using the equity method as the Company exercises a significant influence. Uçak Servisi A.Ş. and France Telecom shares are classified as available for sale investments and changes in their fair value are recognized in net profit or loss.

Financial assets, other than Güneş Ekspres Havacılık A.Ş., Uçak Servisi A.Ş. and France Telecom where the Company is not in a position to exercise significant influence or joint control, are stated at cost as their fair value can not be measured reliably.

Financial Liabilities:

Financial liabilities are classified according to the substance of the contractual arrangements entered into. Significant financial liabilities include bank borrowings, financial lease obligations, accounts and other payables, due to related parties. Foreign currency bank loans are translated into New Turkish Lira at the rates of change ruling at the balance sheet date.

Book values of accounts payable and due to related parties are estimated to reach their fair value, except discounting of these liabilities.

Financial expenses are accounted for on an accrual basis and are traced under related financial liability account to the extent that they are not settled in the period in which they arise. 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.

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 and US Dollar or linked to these currencies and the major part of its expenses is denominated in US Dollar and New Turkish Lira.

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

3.14 Financial Instruments and Financial Risk Management (cont'd)

Interest Risk:

Some of the interest rates related to leasing transactions are 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 predominately on a daily, monthly or quarterly basis. Fair values of these investments fluctuate based on market conditions.

Liquidity Risk:

In general, 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 periods.

3.15 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.

3.16 Use of Estimates

The preparation of financial statements in conformity with International Financial Reporting Standards 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.

3.17 Earnings Per Share

IAS 33 ("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 separate diluted earnings per share.

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

3.17 Earnings Per Share (cont'd)

A summary of the weighted average number of shares outstanding and the basic earnings per share calculation are as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Number of shares outstanding at 1 January (in full)	175.000.000.000	175.000.000.000
New shares issued (cash increase) (in full)	-	-
Number of shares outstanding at 31 December (in full)	175.000.000.000	175.000.000.000
Weighted average number of shares outstanding during the year (in full)	<u>175.000.000.000</u>	<u>175.000.000.000</u>
Net profit for the year	93.223.288	111.924.085
Earnings per share (YTL, full amount)	0,00053	0,00064

4 SEGMENTAL REPORTING

4.1 Business Segments

The Company operates predominantly in one industry segment, its primary business being the air transportation of passengers and cargo within, to or from Turkey.

4.2 Geographical Segments

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. Revenue from both scheduled and non-scheduled international flights is attributed to flight destination's geographical area.

5 CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Cash	195.489	169.393
Cheques received	138.532	122.189
Banks	477.065.690	380.374.142
Other liquid assets	5.510.844	1.589.430
	<u>482.910.555</u>	<u>382.255.154</u>

Foreign currency bank balances are YTL 295.610.051 at 31 December 2005 (2004: YTL 258.806.299).

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5 CASH AND CASH EQUIVALENTS (cont'd)

Time Deposits:

<u>Amount</u>	<u>Currency</u>	<u>Opening date</u>	<u>Maturity</u>	<u>31 December 2005</u>
170.390.000	YTL	22.07.2005-30.12.2005	02.01.2006-24.01.2006	170.390.000
149.163.000	US Dollar	27.12.2005-30.12.2005	02.01.2006-03.01.2006	200.146.913
31.653.000	Euro	30.12.2005	02.01.2006	50.249.138
				<u>420.786.051</u>

<u>Amount</u>	<u>Currency</u>	<u>Opening date</u>	<u>Maturity</u>	<u>31 December 2004</u>
117.612.955	YTL	25.10.2004-31.12.2004	03.01.2005-24.01.2005	117.612.955
22.500.000	US Dollar	31.12.2004	03.01.2005	31.569.670
89.790.000	Euro	31.12.2004	03.01.2005	171.483.213
				<u>320.665.838</u>

6 ACCOUNTS RECEIVABLE (NET)

Accounts receivable comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Trade receivables	210.448.412	183.572.297
Discount on receivables	(2.334.886)	(356.815)
Provision for doubtful receivables	(16.516.720)	(17.422.982)
	<u>191.596.806</u>	<u>165.792.500</u>

7 DUE FROM RELATED PARTIES

Due from related parties comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Güneş Ekspres Havacılık A.Ş.(Sun Express)	970.701	849.702
Uçak Servisi A.Ş. (USAŞ)	-	165
	<u>970.701</u>	<u>849.867</u>

8 INVENTORIES

Inventories comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Spare parts, flight equipments	70.078.750	56.959.738
Other inventories	14.595.913	10.486.161
	<u>84.674.663</u>	<u>67.445.899</u>

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9 OTHER SHORT TERM RECEIVABLES AND ASSETS

Other short-term receivables and assets comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Prepaid sales commissions	11.268.599	10.887.709
Maintenance service income accruals	10.127.094	6.452.513
Deferred insurance expenses	6.787.420	6.433.938
Prepaid operating lease expenses	5.314.180	4.163.235
Interline passenger income accruals	3.843.430	190.878
Due from insurance firms	3.192.141	-
Tax to be refunded	2.965.389	2.804.727
Prepaid other expenses	2.739.482	1.723.700
Foreign receivables from technical suppliers	1.557.088	962.640
Prepaid Eximbank USA guarantee and exposure fee	1.092.408	1.142.056
Prepaid financial expense of bank borrowing	740.124	-
Prepaid rent expenses	574.125	460.146
Receivables relating to Rj aircraft modification	560.516	-
Prepaid aircraft financing expense	487.846	564.021
VAT deductible	437.170	159.737
Personnel salary advance	375.337	341.196
Due from personnel	278.853	259.098
Receivable from SITA deposit certificates	155.882	157.070
Business advances given	95.989	361.690
Bank deposits at banks having transfer difficulties(*)	-	883.929
Other receivables	351.884	170.710
	<u>52.944.957</u>	<u>38.118.993</u>

(*) As of 31 December 2004, the balance of this account is related to bank balance in Egypt.

10 FINANCIAL ASSETS (NET)

The investment accounted for using the equity method is as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Güneş Ekspress Havacılık A.Ş. (Sun Express)	17.490.282	17.465.262

Financial assets available for sale are as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
France Telecom shares	21.133.047	21.133.047
Diminution in value of France Telecom shares	(14.377.581)	(11.701.136)
Uçak Servisi A.Ş. (USAŞ)	8.431.536	8.587.009
Appreciation in value of USAŞ shares	3.021.190	7.193.170
Sita Inc.	1.755.955	1.866.896
Emek İnşaat ve İşletme A.Ş.	28.080	28.080
Other financial assets	1.354	1.490
	<u>19.993.581</u>	<u>27.108.556</u>

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10 FINANCIAL ASSETS (NET) (cont'd)

Tender for the catering service was won by Uçak Servisi A.Ş. (USAŞ) and service agreement was signed on 1 January 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 21 June 2002, 1,25% of shares was transferred on 2 January 2003 and 1,25% of shares was transferred on 2 January 2004, 1,25% of shares was transferred on 3 January 2005 and it will be completed to 15% by transferring 1,25% share in the year 2006. Consequently, 1.140 million shares corresponding to first 13,75% of USAŞ's share capital, transferred to the Company, was recorded to "financial assets" and "deferred income" accounts at market value of YTL 19.650.109. "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 and 1.026 million shares in 2005 at Istanbul Stock Exchange.

USAŞ gave 1.852.500.000 free shares to the Company based on the decision taken in Non-general Assembly held on 8 December 2004 related to the share capital increase originated from the inflation adjustment difference arising from capital restatement.

Details of the Company's financial assets at 31 December 2005 are as follows:

<u>Name of the Company</u>	<u>Place of Incorporation and Operation</u>	<u>Ownership Rate</u>	<u>Voting Power Rate</u>	<u>Principal Activity</u>
Güneş Ekspres Havacılık A.Ş. (Sun Express)	Turkey	50%	50%	Air transportation
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 Services
Uçak Servisi A.Ş. (USAŞ)	Turkey	4,75%	4,75%	Catering
France Telecom	France	Less than 0,1%	Less than 0,1%	Telecommunication

11 TANGIBLE FIXED ASSETS (NET)

Tangible fixed assets comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Tangible fixed assets (net)	2.061.622.940	1.892.760.028
Advances given for other tangible fixed assets	9.476.231	-
	<u>2.071.099.171</u>	<u>1.892.760.028</u>

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11 TANGIBLE FIXED ASSETS (NET) (cont'd)

	Land, Land Improvements and Buildings	Technical Equipments, Simulators and Vehicles	Other Equipments, Fixtures and Software	Aircraft and Spare Engines	Components and Repairable Spare Parts	Construction in Progress	Total Owned Assets	Leased Aircraft	Other Leased Fixed Assets and Simulators	Total Leased Assets	Total
Cost											
Opening balance 1 January 2005	171.865.462	306.448.868	226.473.271	1.329.241.237	297.315.877	403.815	2.331.748.530	3.511.893.506	18.605.426	3.530.498.932	5.862.247.462
Transfers from finance leased aircraft	-	-	-	752.650.230	-	-	752.650.230	(752.650.230)	-	(752.650.230)	-
Additions	-	5.113.540	5.082.869	92.644.878	105.802.241	1.675.910	210.319.438	262.118.349	-	262.118.349	472.437.787
Disposals	-	(3.254.662)	(22.374.956)	(57.092.445)	(83.111.079)	(390.865)	(166.224.007)	-	-	-	(166.224.007)
Closing balance 31 December 2005	171.865.462	308.307.746	209.181.184	2.117.443.900	320.007.039	1.688.860	3.128.494.191	3.021.361.625	18.605.426	3.039.967.051	6.168.461.242
Accumulated depreciation											
Opening balance 1 January 2005	47.711.103	264.146.565	205.653.933	813.819.146	146.221.685	-	1.477.552.432	979.122.702	5.504.459	984.627.161	2.462.179.593
Transfers from finance leased aircraft	-	-	-	222.563.758	-	-	222.563.758	(222.563.758)	-	(222.563.758)	-
Depreciation for the period	2.860.927	13.700.627	7.767.989	62.732.620	90.020.557	-	177.082.720	129.787.204	1.444.302	131.231.506	308.314.226
Disposals	-	(3.237.355)	(20.659.342)	(444.052)	(83.111.079)	-	(107.451.828)	-	-	-	(107.451.828)
Closing balance 31 December 2005	50.572.030	274.609.837	192.762.580	1.098.671.472	153.131.163	-	1.769.747.082	886.346.148	6.948.761	893.294.909	2.663.041.991
Accumulated impairment	-	6.368.370	-	576.412.045	-	-	582.780.415	856.116.001	4.899.895	861.015.896	1.443.796.311
31 December 2005 net book value	121.293.432	27.329.539	16.418.604	442.360.383	166.875.876	1.688.860	775.966.694	1.278.899.476	6.756.770	1.285.656.246	2.061.622.940
31 December 2004 net book value	124.154.359	34.007.636	20.819.339	212.152.724	151.094.193	403.815	542.632.066	1.341.838.750	8.289.212	1.350.127.962	1.892.760.028

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12 INTANGIBLE FIXED ASSETS (NET)

	<u>Rights</u>	<u>Leasehold Improvements</u>	<u>Total</u>
Cost			
Opening balance 1 January 2005	62.829.830	19.684.974	82.514.804
Additions	1.541.345	463.973	2.005.318
Disposals	-	(60.692)	(60.692)
Closing balance 31 December 2005	<u>64.371.175</u>	<u>20.088.255</u>	<u>84.459.430</u>
Accumulated depreciation			
Opening balance 1 January 2005	55.723.863	18.988.153	74.712.016
Amortization charge for the period	2.915.458	525.669	3.441.127
Disposals	-	(53.891)	(53.891)
Closing balance 31 December 2005	<u>58.639.321</u>	<u>19.459.931</u>	<u>78.099.252</u>
Accumulated impairment	-	-	-
31 December 2005 net book value	<u>5.731.854</u>	<u>628.324</u>	<u>6.360.178</u>
31 December 2004 net book value	<u>7.105.966</u>	<u>696.821</u>	<u>7.802.787</u>

13 ADVANCES GIVEN FOR AIRCRAFT

	<u>31 December 2005</u>	<u>31 December 2004</u>
Prepayments for aircraft purchases	570.531.933	413.653.138
Advances given for operational leases	2.637.672	1.297.728
	<u>573.169.605</u>	<u>414.950.866</u>

14 OTHER LONG TERM RECEIVABLES AND ASSETS

	<u>31 December 2005</u>	<u>31 December 2004</u>
Prepaid Eximbank USA guarantee and exposure fee	5.889.372	7.319.414
Prepaid aircraft financing expense	2.067.151	2.810.289
Deposits given	1.325.066	1.815.805
Due from personnel	1.006.711	1.178.673
Receivables from SITA deposit certificate	804.107	734.673
Prepaid operating lease expenses	374.744	-
Other receivables	90.670	95.089
	<u>11.557.821</u>	<u>13.953.943</u>

15 BANK BORROWINGS

	<u>31 December 2005</u>	<u>31 December 2004</u>
T.İş Bankası /Citibank NA London	362.903.225	-
Other (*)	332.636	294.026
	<u>363.235.861</u>	<u>294.026</u>

<u>Bank Name</u>	<u>Maturity</u>	<u>Currency</u>	<u>Interest accruals</u>	<u>YTL</u>
T.İş Bankası / Citibank NA London	31.03.2006	270.000.000 US Dollar	459.998 US Dollar	362.903.225

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

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16 FINANCE LEASE OBLIGATIONS

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

	<u>31 December 2005</u>	<u>31 December 2004</u>
Not later than one year	221.054.754	248.605.545
Between 1 - 5 years	699.473.041	813.888.304
Over 5 years	299.805.674	293.693.684
	<u>1.220.333.469</u>	<u>1.356.187.533</u>
Less: Future interest expense	<u>(184.509.789)</u>	<u>(143.006.259)</u>
Principal value of future rentals shown in the balance sheets	<u>1.035.823.680</u>	<u>1.213.181.274</u>
	<u>31 December 2005</u>	<u>31 December 2004</u>
<i>Represented by :</i>		
Current liabilities	179.092.821	211.925.219
Long term liabilities	856.730.859	1.001.256.055
	<u>1.035.823.680</u>	<u>1.213.181.274</u>
<i>Interest range:</i>		
Floating rate obligations	982.205.221	912.597.686
Fixed rate obligations	53.618.459	300.583.588
	<u>1.035.823.680</u>	<u>1.213.181.274</u>

As of 31 December 2005, the US Dollar denominated lease obligations' interest rates for the fixed rate obligations are between %7,12 and %7,70; and for the floating rate obligations are a margin ranging between LIBOR minus %0,05 and LIBOR plus 3,00%.

17 DUE TO RELATED PARTIES

Due to related parties comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Güneş Ekpres Havacılık A.Ş. (Sun Express)	459.029	220.646
Uçak Servisi A.Ş. (USAŞ)	7.563.830	6.583.364
	<u>8.022.859</u>	<u>6.804.010</u>

18 OTHER SHORT TERM AND LONG TERM PAYABLES

Other short term payables comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Taxes and funds payable	16.204.908	20.219.443
Social security premiums payable	14.840.062	12.742.270
Deferred income from USAŞ shares transfer	5.257.836	3.782.773
Debt to personnel	276.417	264.946
State Airport Administration (DHMI) protocol payable	-	1.905.028
Discount on DHMI protocol payable	-	(38.055)
Other liabilities	1.373.121	826.401
	<u>37.952.344</u>	<u>39.702.806</u>

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18 OTHER SHORT TERM AND LONG TERM PAYABLES (cont'd)

Other long term payables comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Deferred income from USAŞ share transfer	-	3.782.773
	-	3.782.773

19 DEPOSITS AND ADVANCES RECEIVED

Short term deposits and advances received comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Advances received for mileage credit sales	21.649.478	24.151.490
MCO advances	16.262.840	8.740.046
E-pos ticket advance	9.675.611	364.658
Deposits and guarantees received	3.715.141	4.413.694
Special rent advances	3.413.900	2.503.369
Advances received for financial leases	1.151.059	-
Other advances received	544.625	258.942
	<u>56.412.654</u>	<u>40.432.199</u>

Long term deposits and guarantees received comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Deposits and guarantees received	7.124.266	8.945.711

20 PASSENGER FLIGHT LIABILITIES

Passenger flight liabilities comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Flight liability resulting from ticket sales	154.949.961	130.399.934
Flight liability resulting from mileage sales	54.847.928	54.438.444
	<u>209.797.889</u>	<u>184.838.378</u>

21 OTHER ACCRUED LIABILITIES

Other accrued liabilities comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Frequent flyer program liability	30.577.262	7.310.997
Accrued salaries	17.993.508	16.329.852
Maintenance service income accruals	12.585.613	16.669.232
Expense accruals of insurance premiums	10.468.387	10.532.147
Provisions for legal claims	9.202.870	9.665.943
Accruals for sales incentive premiums	6.684.627	8.085.906
Other accrued liabilities	347.266	373.527
Accruals for other expenses	4.347.361	4.189.101
	<u>92.206.894</u>	<u>73.156.705</u>

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22 MANUFACTURERS' CREDIT (NET)

Unearned income about manufacturers' credit comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Gross manufacturers' credit	19.690.997	17.726.720
Accumulated amortization	(16.199.785)	(15.226.823)
	<u>3.491.212</u>	<u>2.499.897</u>

23 TAXATION

Corporation tax payable is as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Prepaid taxes and funds	(13.363.884)	(53.637.690)
	<u>(13.363.884)</u>	<u>(53.637.690)</u>

Tax expense is as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Deferred tax expense	45.868.744	2.946.085
Tax expense	<u>45.868.744</u>	<u>2.946.085</u>

Corporate tax:

The Company is subject to Turkish corporate taxes. There is provision for the estimated tax liabilities based on the Company's financial results for the period.

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

The effective tax rates are as follows:

- In 2004: 33% (the corporate tax rate was increased from 30% to 33% by Law No. 5035 published in the Official Gazette on 2 January 2004)
- In 2005: 30 %

In Turkey, prepaid taxes are calculated and accrued on a quarterly basis. In 2004, the prepaid corporate income tax rate was applied 33%. Prepaid corporate income tax rate is 30% in 2005.

Tax losses can be carried forward for offsetting against future taxable income for up to 5 years. However, losses cannot be carried back for offsetting against profits from previous periods.

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23 TAXATION (cont'd)

Corporate tax (cont'd):

In Turkey, there is no procedure for a final and definitive agreement on tax assessments. Companies file their tax returns until 15 April following the close of the accounting period to which they relate. The tax authorities may, however, examine such returns and the underlying accounting records and may revise assessments within five years.

Income withholding tax:

In addition to corporate taxes, companies should also calculate income withholding taxes and funds surcharge on any dividends distributed, except for companies receiving dividends who are resident companies in Turkey and Turkish branches of foreign companies. The rate of income withholding tax is 10% starting from 24 April 2003. Undistributed dividends incorporated in share capital are not subject to income withholding taxes.

Income withholding tax which was calculated in 2002 and prior years on various types of income and gains exempt from corporation tax, whether distributed or not, has been removed in general. However, 19.8% withholding tax is still applied to investment allowances relating to investment incentive certificates obtained prior to 24 April 2003. Such allowances may be used to relieve corporation tax liability until the profits reach the calculated level of exemption. If companies fail to make a profit or incur losses, any allowance outstanding may be carried forward to following years so as to be deducted from taxable income of subsequent profitable years. Carried forward investment incentives to be deducted from corporate tax liability in the following periods are revalued with the applicable WPI.

Deferred tax:

The Company recognizes deferred tax assets and liabilities based upon temporary differences arising from the differences between its financial statements as reported for IFRS purposes and its statutory tax financial statements. These differences generally result in the recognition of revenue and expenses in different reporting periods considering IFRS and tax standards. The deferred tax rate is 30%.

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23 TAXATION (cont'd)

Temporary differences: Deferred tax assets/ (liabilities)

	<u>31 December 2005</u>	<u>31 December 2004</u>
Allowance for unrecoverable bank accounts	246	289
Provision for doubtful receivables	230.607	435.630
Restatement of inventory	394.576	9.112.607
Appreciation in value of financial assets	(666.579)	(1.551.257)
Other current assets	-	63.731
Short term lease obligation	36.369.506	50.042.494
Deferred income and expense	420.258	303.593
Expense accruals	18.270.507	13.722.079
Provision for advance ticket sales	(21.519.668)	(18.790.825)
Deferred income	1.504.979	1.935.960
Adjustments to non-current assets	-	(648.731)
Fixed assets	(368.749.380)	(444.712.894)
Long term lease obligation	185.266.465	300.376.817
Retirement pay liability	34.092.373	31.293.632
Manufacturers' credit	1.392.681	749.969
Discount on receivables	772.994	106.711
Discount on payables	(811.742)	(20.905)
Unused investment incentives	20.048.657	3.872.562
Unused tax losses	630.034	5.111.135
Deferred tax liability	<u>(92.353.486)</u>	<u>(48.597.403)</u>

Movement in deferred tax liability is as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Net deferred tax charge related to temporary differences	45.868.744	2.946.085
Net deferred tax charge	45.868.744	2.946.085
Monetary gain on deferred tax liabilities	(2.112.661)	(6.318.246)
Net change in deferred tax	<u>43.756.083</u>	<u>(3.372.161)</u>

Reconciliation from the expected to the disclosed tax charge is as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Profit before taxation	139.092.032	114.870.171
Expected tax expense (2005:30%, 2004:33%)	41.727.610	37.907.156
<i>Reconciling items:</i>		
Non-deductible expenses	9.054.039	724.664
Tax-exempt income	(5.163.626)	(31.028.227)
Non-deductible monetary losses	240.554	10.084.299
Tax benefit due to using tax rate of 30% for calculation of deferred tax	-	(5.758.110)
Investment incentive used	-	(3.872.562)
Unused tax losses	-	(5.111.135)
Taxation charge	<u>45.868.744</u>	<u>2.946.085</u>

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24 RETIREMENT PAY LIABILITY

Under Turkish Labor Law, employees 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), or are called up for military service. 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 a limit of YTL 1.727 as at 31 December 2005 (2004: YTL 1.575). The number of years service required before retirement is rising according to a sliding scale based on new legislation enacted in 1999. The system described here can be named as an unfunded defined benefit system. 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:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Current service cost	15.156.287	12.234.000
Interest cost	5.594.993	5.105.319
	<u>20.751.280</u>	<u>17.339.319</u>

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

	<u>31 December 2005</u>	<u>31 December 2004</u>
Provision at 1 January	104.312.102	93.597.525
Charge for the year	20.751.280	20.287.849
Payments during the year	(6.887.415)	(6.624.737)
Restatement effect	(4.534.725)	(2.948.535)
Provision at 31 December	<u>113.641.242</u>	<u>104.312.102</u>

The estimated value of the vested benefit obligation is discounted with an approximate rate of 5,61% (2004: 5,45%) per annum considering the effect of increase in eligible pay and its limit.

25 SHARE CAPITAL/RECIPROCAL ASSOCIATE CAPITAL ADJUSTMENT

The ownership of the Company's share capital is as follows:

	<u>Group</u>	<u>%</u>	<u>31 December 2005</u>	<u>%</u>	<u>31 December 2004</u>
Republic of Turkey Prime Ministry Privatization Administration(*)	A, C	75,18(**)	131.565.696	75,17	131.538.948
Others	A	24,82(**)	43.434.304	24,83	43.461.052
Share capital (historic)			175.000.000		175.000.000
Restatement effect			1.825.994.542		1.825.994.542
Restated Share Capital			<u>2.000.994.542</u>		<u>2.000.994.542</u>

(*) 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 30 October 1990.

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25 SHARE CAPITAL/RECIPROCAL ASSOCIATE CAPITAL ADJUSTMENT (cont'd)

(**) YTL 26.748 nominal valued shares of the Company subject to the second public offering during 1, 2 and 3 December 2004 were transferred to the accounts of the Republic of Turkey Prime Ministry Privatization Administration by İş Yatırım Menkul Değerler A.Ş. The transfer was made due to default of private shareholders who did not transfer the amounts of the shares following the conclusion of last installment.

As at 31 December 2005, 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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26 FOREIGN CURRENCY POSITION

Foreign currency risk arises from the change of the value of financial instruments due to change in exchange rates. The Company has a foreign currency risk because of the foreign currency denominated debts. As of 31 December 2005, the Company does not have derivative financial instruments to hedge its foreign currency risks. US Dollar, Euro and Sterling are the main currencies that make the foreign currency position of the Company.

The foreign currency position of the Company as of 31 December 2005 and 31 December 2004 in terms of YTL is as follows:

31 December 2005	US Dollar	Euro	Sterling	Other	Total
<i>Foreign currency denominated assets</i>					
Cash and cash equivalents	209.110.558	63.411.560	1.701.717	27.041.304	301.265.139
Account receivables (net)	24.881.620	45.615.416	5.907.491	40.429.558	116.834.085
Due from related parties	469.066	446.745	-	-	915.811
Other short term receivables and assets	32.369.277	3.469.191	374.251	9.138.411	45.351.130
Inventories-advances	1.117.566	53.958	71.109	18.599	1.261.232
Other long term receivables and assets	10.485.217	463.364	71.791	414.991	11.435.363
Advances given for the tangible fixed assets	9.333.540	-	142.691	-	9.476.231
Advances given for the aircraft	573.169.605	-	-	-	573.169.605
	860.936.449	113.460.234	8.269.050	77.042.863	1.059.708.596
<i>Foreign currency denominated liabilities</i>					
Bank borrowings	362.903.225	-	-	-	362.903.225
Financial lease obligations (short term)	179.092.821	-	-	-	179.092.821
Accounts payable (net)	67.907.303	54.755.274	3.166.398	27.703.755	153.532.730
Due to related parties	8.022.859	-	-	-	8.022.859
Deposits and advances received (short term)	23.697.313	1.970.250	29.313	315.965	26.012.841
Other accrued liabilities	17.657.538	6.848.702	2.836.665	4.149.043	31.491.948
Passenger flight liabilities	71.477.493	76.609.577	10.221.707	41.047.092	199.355.869
Financial lease obligations (long term)	856.730.859	-	-	-	856.730.859
Gross manufacturers' credit	3.491.212	-	-	-	3.491.212
Deposits and advances received (long term)	428.254	5.270.953	103.467	1.321.592	7.124.266
	1.591.408.877	145.454.756	16.357.550	74.537.447	1.827.758.630
Net foreign currency position (*)	(730.472.428)	(31.994.522)	(8.088.500)	2.505.416	(768.050.034)

(*) Whereas, the Company seems to be in an open position based on its monetary assets and liabilities, as explained in Note 3.4, the Company values its aircraft and spare engines according to their US Dollar acquisition costs or US Dollar selling prices. In this respect, the Company's management is of the opinion that the Company's those tangible assets which are carried by their US Dollar values should also be considered in the overall evaluation of the sensitivity of the Company's assets and liabilities against the changes in foreign exchange rates.

As of 31 December 2005, the net book value of aircraft and spare engines, which are carried by their US Dollar acquisition costs or US Dollar selling prices is YTL 1.735.882.362 (2004: YTL 1.572.744.705).

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26 FOREIGN CURRENCY POSITION (cont'd)

31 December 2004	US Dollar	Euro	Sterling	Other	Total
<i>Foreign currency denominated assets</i>					
Cash and cash equivalents	42.187.828	186.405.611	2.423.148	29.595.968	260.612.555
Account receivables (net)	37.135.597	34.400.214	5.668.346	40.398.161	117.602.318
Due from related parties	499.350	325.564	-	-	824.914
Other short term receivables and assets	29.720.433	2.609.137	534.178	2.955.157	35.818.905
Inventories-advances given	289.795	43.593	49.168	67.016	449.572
Other long term receivables and assets	2.007.060	-	-	-	2.007.060
Advances given for the aircraft	414.950.866	-	-	-	414.950.866
	<u>526.790.929</u>	<u>223.784.119</u>	<u>8.674.840</u>	<u>73.016.302</u>	<u>832.266.190</u>
<i>Foreign currency denominated liabilities</i>					
Financial lease obligations (short term)	211.925.219	-	-	-	211.925.219
Accounts payable	27.972.762	40.767.554	3.538.322	19.336.983	91.615.621
Due to related parties	225.774	1.326	-	-	227.100
Deposits and advances received	29.141.955	8.775.870	718.247	1.948.966	40.585.038
Other accrued liabilities	20.273.716	13.600.846	4.400.261	5.129.285	43.404.108
Passenger flight liabilities	69.674.784	58.772.230	10.885.323	42.521.709	181.854.046
Financial lease obligations (long term)	1.001.256.054	-	-	-	1.001.256.054
Manufacturers' credit (net)	2.499.897	-	-	-	2.499.897
	<u>1.362.970.161</u>	<u>121.917.826</u>	<u>19.542.153</u>	<u>68.936.943</u>	<u>1.573.367.083</u>
Net foreign currency position(*)	<u>(836.179.232)</u>	<u>101.866.293</u>	<u>(10.867.313)</u>	<u>4.079.359</u>	<u>(741.100.893)</u>

27 PROVISIONS, CONTINGENT ASSETS AND CONTINGENT LIABILITIES

a) Guarantees Given:

Amount of letter of guarantees given is YTL 38.040.225 as of 31 December 2005 (2004: YTL 35.592.250).

b) Purchase Commitments:

The Company has signed agreements for delivery of 59 aircraft with delivery dates between years 2005-2008. Total value of these aircraft 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 421 million as of 31 December 2005 related to these aircraft.

c) Letters of comfort:

	<u>31 December 2005</u>		<u>31 December 2004</u>	
	US Dollar	2.900.000	US Dollar	2.900.000
Letters of comfort given to Sun Express	Euro	2.556.459	Euro	2.556.459

d) The Company's discounted retirement pay provision is YTL 113.641.242. The Company's undiscounted liability for retirement pay would be approximately YTL 184 million as of 31 December 2005, if all employees were dismissed on that date.

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28 OPERATING LEASE COMMITMENTS

Operating lease commitments of the Company comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Not later than one year	118.983.335	78.224.911
Between 1-5 years	200.387.903	124.630.224
Over 5 years	100.928.325	-
	<u>420.299.563</u>	<u>202.855.135</u>

29 EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

a) Market price of 202.735 France Telecom securities, which is quoted at the Paris Stock Exchange, included in the financial investments available for sale as of 31 December 2005, has decreased from Euro 20,99 at 31 December 2005 to Euro 17,82 at 12 April 2006. Hence, the total market value of these securities decreased by YTL 1.020.239 compared to balance sheet date.

b) Market price of 1.624,5 million USAŞ securities, which is traded in İstanbul Stock Exchange, and included in the financial investments available for sale as of 12 April 2006, has decreased from YTL 7,05 at 31 December 2005 to YTL 7,00 at 12 April 2006. Hence, the total market value of these securities decreased by YTL 81.225 compared to balance sheet date.

c) The Company has sold 1.026 million of USAŞ shares in January 2006 at İstanbul Stock Exchange. After the transaction, the percentage of the shares owned by the company within the capital of USAŞ is 3 %.

d) According to the decision dated 20.03.2006 and numbered 2006/19 of Privatization High Commission, 25% of A group shares of the Company owned by Turkish Republic Prime Ministry Privatization Administration have been decided to be sold through public offering. It has been also decided to use the right for selling of additional shares and to complete public offering within the twelve months beginning from the decision date.

e) Retirement pay ceiling has been increased to YTL 1.770,62 as of 1 January 2006.

f) The Company has cancelled financial the lease contracts of two A340 aircraft of which lease contracts would be due by 22 July 2006 and 19 June 2007, by paying the remaining lease payments before the maturity date thus having the ownership of these two aircraft.

g) The Company took the delivery of 3 aircraft within January and February 2006 whose purchase agreements was signed before.

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30 OPERATING REVENUES

Operating revenues comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Scheduled flights		
- Passenger	2.714.345.012	2.435.195.680
- Cargo and mail	269.339.731	275.335.623
Non-scheduled flights	31.421.773	48.173.144
Other revenues	124.072.037	161.636.666
Total revenues	<u>3.139.178.553</u>	<u>2.920.341.113</u>

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

	<u>31 December 2005</u>	<u>31 December 2004</u>
- Europe	1.279.626.580	1.140.235.299
- Middle East	285.849.922	261.061.561
- North Africa	78.527.254	72.105.177
- North America	155.703.990	160.752.433
- Far East	491.153.258	458.570.386
	<u>2.290.861.004</u>	<u>2.092.724.856</u>
Domestic	692.823.739	617.806.447
Total revenue from the scheduled flights	<u>2.983.684.743</u>	<u>2.710.531.303</u>

31 OPERATING EXPENSES

Operating expenses comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Cost of Sales		
Fuel expenses	735.752.048	540.808.137
Staff expenses	528.249.062	435.359.963
Depreciation expenses	297.770.441	300.329.889
Landing and overflight expenses	247.780.680	251.133.294
Handling expenses	159.531.910	170.265.340
Passenger service and catering expenses	148.563.895	135.353.522
Maintenance expenses	138.128.759	146.822.414
Operating lease expenses	101.903.865	61.514.807
Insurance expenses	51.914.206	68.954.618
Other rent expenses	15.151.215	13.983.013
Aircraft wet-lease expenses	10.575.369	27.100.841
Communication expenses	8.043.138	9.198.505
Service expenses	7.014.244	5.911.241
Other taxes	5.164.437	2.794.615
Lighting, heating and water expenses	3.842.818	4.432.578
Transportation expenses	2.705.369	1.554.287
Cost of other sales	6.392.867	3.593.865
	<u>2.468.484.323</u>	<u>2.179.110.929</u>

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31 OPERATING EXPENSES (cont'd)

	<u>31 December 2005</u>	<u>31 December 2004</u>
Sales and marketing expenses		
Commission and promotion expenses	214.501.933	216.980.518
Staff expenses	126.781.998	117.661.542
Reservation system expenses	56.047.954	51.463.749
Communication expenses	13.544.727	14.836.192
Other rent expenses	13.354.869	13.722.854
Service expenses	8.291.621	5.866.740
Advertisement expenses	7.673.850	4.728.621
Transportation expenses	5.084.273	4.045.169
Passenger service and catering expenses	4.444.829	4.028.055
Other taxes	4.157.010	2.817.713
Code share expenses	2.075.866	1.955.047
Lighting, heating, energy and water expenses	1.507.183	1.537.323
Maintenance expenses	1.068.664	1.664.005
Software and computer equipment expenses	646.166	707.532
Fuel expenses	531.717	409.463
Insurance expenses	292.405	522.753
Other sales and marketing expenses	13.403.148	13.555.537
	<u>473.408.213</u>	<u>456.502.813</u>

	<u>31 December 2005</u>	<u>31 December 2004</u>
General administrative expenses		
Staff expenses	72.771.686	93.644.680
Depreciation expenses	13.984.912	13.777.029
Maintenance expenses	3.921.390	4.317.601
Other taxes	3.760.074	3.700.069
Software and computer equipment expenses	3.536.043	4.148.321
Communication expenses	2.483.204	2.509.652
Commission and promotion expenses	2.259.052	1.919.888
Service expenses	2.034.056	2.470.913
Lighting, heating, energy and water expenses	1.659.631	826.843
Other rent expenses	1.257.747	886.828
Insurance expenses	402.356	1.269.087
Fuel expenses	223.809	6.069
Other general administrative expenses	4.542.401	6.223.334
	<u>112.836.361</u>	<u>135.700.314</u>
Total operating expenses	<u>3.054.728.897</u>	<u>2.771.314.056</u>

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32 FINANCIAL INCOME/(EXPENSE) (NET)

Financial income/ (expense) comprised the following:

	31 December 2005	31 December 2004
Foreign exchange gains	211.917.117	261.424.838
Interest income	42.433.556	44.176.637
Income from investment accounted for equity method	784.282	9.006.930
Discount income	596.515	-
Increase in value of available for sale financial assets	-	7.325.359
Financial income	<u>255.731.470</u>	<u>321.933.764</u>

	31 December 2005	31 December 2004
Foreign exchange losses	(241.601.663)	(232.757.139)
Financial lease interest expense	(45.658.088)	(44.272.076)
Interest expenses for bank borrowings	(12.163.552)	-
Diminution in value of financial assets	(5.779.778)	-
Retirement pay interest cost	(5.594.993)	(5.105.319)
Interest expenses-third parties	-	(4.521.344)
Discount expense	-	(818.720)
Other financial expense	(2.220.372)	-
Financial expense	<u>(313.018.446)</u>	<u>(287.474.598)</u>
Financial income/(expense) (net)	<u>(57.286.976)</u>	<u>34.459.166</u>

33 INCOME FROM OTHER OPERATIONS

Income from other operations comprised the following:

	31 December 2005	31 December 2004
Change in provision for diminution in value of fixed assets	59.560.153	23.260.405
Reversal of unnecessary provision	10.751.884	14.383.149
Discounts received from spare parts suppliers	10.555.819	8.945.079
Dividend income	8.356.877	4.736.992
Cost free materials income	5.109.245	1.579.946
Profit on sale of marketable securities	3.579.775	-
Compensation received	3.517.714	5.898.612
Gain on sale of fixed assets	3.035.861	632.565
Manufacturers' credit income	1.774.210	1.772.672
Other income	4.774.352	5.118.417
	<u>111.015.890</u>	<u>66.327.837</u>

34 LOSS FROM OTHER OPERATIONS

Loss from other operations comprised the following:

	31 December 2005	31 December 2004
Provision expenses	24.385.555	8.526.791
Rent expense of RJ aircraft to be returned	-	4.712.668
Expenses incurred for passengers with no visas	800.524	1.776.430
Other expenses	1.973.824	1.572.759
	<u>27.159.903</u>	<u>16.588.648</u>

TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) in terms of purchasing power of the Turkish Lira at 31 December 2005 unless otherwise stated)

35 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 comprised the following:

	31 December 2005	31 December 2004
Services rendered to Sun Express	3.682.604	1.999.603
Services rendered to USAŞ	376.002	268.496
	<u>4.058.606</u>	<u>2.268.099</u>

	31 December 2005	31 December 2004
Services received from Sun Express	873.363	2.721.718
Services received from USAŞ	80.172.618	69.820.280
	<u>81.045.981</u>	<u>72.541.998</u>

Dividend received comprised the following:

	31 December 2005	31 December 2004
Sun Express	7.066.005	4.430.142
Uçak Servisi A.Ş. (USAŞ)	1.131.509	201.609
Emek İnşaat ve İşletme A.Ş.	69	6.858
France Telecom	159.294	98.383
	<u>8.356.877</u>	<u>4.736.992</u>