TURKISH EQUITIES / COMPANY UPDATE

THY

Climbing to all-time highs

19 August 2024

Outperform
(Maintained)

Close Price: TRY293.50
12M Target Price: TRY450.00
Upside Potential: 53%

We are reiterating our Outperform rating for THY with a revised 12-month target price of TRY450.00/share, suggesting 53% upside potential. Despite negative effect of Pratt & Whitney engine issues, THY maintained its capacity growth at 10.1% on YoY basis in 1H24 which is also 37.5% higher than its pre-pandemic level vs. a 3.3% higher level for global air traffic capacity. Although its analyst EBITDA generation was materialized at 17.3% lower in 1H24 on YoY basis, 2H24 outlook is much promising on softening passenger yield pressure on healthy demand environment and declining fuel costs. Accordingly, we revise up our 2024 EBITDA forecast by 10.0% to USD4.8bn which is broadly in line with its record high level of 2023. This implies an 11.0% EBITDA growth in USD-terms for the second half which is highly unique in BIST-Universe as the most of the company faces challenges of slow-down in economic activities on tight monetary and fiscal policies and/or loss of competition in the export market on strength of TRY compared to hard currencies while the cost bases have been increased on energy and personnel expenses. Based on our new assumptions, the stock trades 3.9x EV/EBITDA and 3.1x P/E at an average of 40.8 % discount to its global peers and 49.0% discount to its historical average. Along with on-going record high operational profitability and healthy tourism season, we maintain our Outperform rating for the stock.

Short-term visibility is still limited for the industry: The global air traffic kept its all-time high level in the first of 2024 when the total traffic reached to 13.4% higher level on YoY basis. Although expectations now point to stabilizing single digit growth for the domestic air traffic, solid momentum in the international segment still continues with a 12.3% YoY growth in June. Additionally, as the demand expansion is still outpacing the capacity, the load factor of the industry has also improved with a 1.3% in 1H24 on YoY basis. In terms of profitability, the outlook is now more promising given the depressed jet fuel prices - hovering around 27.7% lower - as the fuel expenses are the biggest item in the cash cost base of the airlines while the yield pressure is softening on healthy demand environment in the summer season.

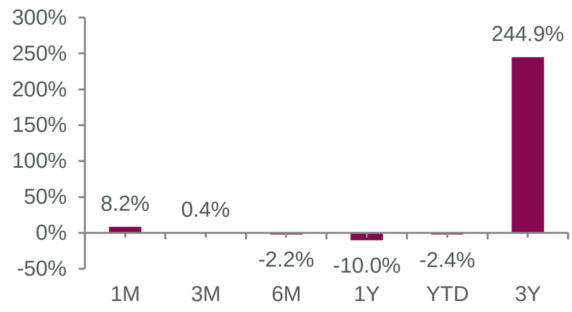
Tourism season is still strong: In the first 6 months of the year, tourist arrivals into Türkiye posted another solid growth of 13.9% while European tourists registered the highest portion in total mix again with an 14.4% increase compared to the same period of the last year. Although the negative impact of loss of purchasing power in local currency having led to some constraints to the tourism industry, we are not pessimistic for foreign tourist arrivals given as we calculate packaged holiday prices for our sample group in Europe is at 23.7% higher compared to its pre-pandemic level vs. a 4.8% lower level in Türkiye in EUR-terms. Accordingly, we think that ongoing momentum in tourist arrivals to be maintained in the coming months, which promises a better outlook for point to point air traffic for local airlines on top of the positive impact on the tourism industry.

Still keeping its record high operational profitability: THY's analyst EBITDA declined by 17.3% in 1H24 on the negative effect of grounded aircrafts and rise in the total CASK on rising personnel expenses while the yields were under pressure. For the second half, we are more positive for the outlook as yield pressure for the industry has relatively softened while the declining trend in the jet fuel prices suggest a much promising outlook for the cost management. Accordingly, we revise our EBITDA estimate for the full year by 10.0% to USD4.8bn, implying a 11% YoY growth in 2H24 which is very rare in BIST-Universe. With our new assumption of USD7.0bn net debt by the year-end, the stock trades at 3.9x EV/EBITDA and 3.1x P/E at an average of 40.8% discount to its global peers and 49.0% discount to its historical average.

Stock data

Bloomberg / Reuters	THYAO TI / THYAO.IS
Mcap (US$mn)	12,051
EV (US$mn)	19216.0
Avg. Trd. Vol. (US$mn)	291.2
Free Float	50%

Relative Performance to BIST100



Key Data (TRYmn)	2022	2023	2024F	2025F
Revenues	311,169	504,398	779,085	1,058,075
Growth	220%	62%	54%	36%
EBITDA	78,684	115,397	161,695	224,161
Growth	182%	47%	40%	39%
Net Profit	47,429	163,003	130,604	165,338
Growth	477%	244%	-20%	27%
P/E (x)	1.7	3.2	3.1	3.0
EV/EBITDA (x)	2.8	4.0	3.9	3.7
P/BV (x)	0.5	0.8	0.6	0.5
FCF yield (%)	6%	0%	17%	17%
Div. yield (%)	0%	0%	0%	0%

Analyst
Can Alagoz
+90 212 336 7273
can.alagoz@qnbfi.com

Figure 1 – Summary financials & key metrics (TRYmn)

Income statement	2020	2021	2022	2023	2024F	2025F
Revenues	**46,448**	**97,378**	**311,169**	**504,398**	**779,085**	**1,058,075**
Gross profit	**2,683**	**22,145**	**75,641**	**119,446**	**162,971**	**234,562**
EBITDA	**8,261**	**27,922**	**78,684**	**115,397**	**161,695**	**224,161**
Depreciation	11,638	15,473	30,953	48,474	76,022	94,443
EBIT	**-3,377**	**12,449**	**47,731**	**66,923**	**85,673**	**129,719**
Net other income	3,339	2,921	6,589	28,693	56,379	68,275
Income from investing activities	-83	-52	-333	-1,669	-2,516	-3,320
Net financial income	-5,402	-6,870	-4,764	-9,381	-19,626	-22,213
Profit from associates	-578	743	2,180	6,716	5,897	7,254
PBT	**-6,101**	**9,191**	**51,403**	**91,282**	**125,808**	**179,715**
Taxes	513	-977	-3,971	71,716	4,796	-14,377
Minority interest	0	0	0	0	0	0
Net income	**-5,588**	**8,214**	**47,432**	**162,998**	**130,604**	**165,338**

Balance sheet	2020	2021	2022	2023	2024F	2025F
Current assets	**30,659**	**65,797**	**135,095**	**253,043**	**383,883**	**522,192**
Cash equivalents	13,293	35,679	76,192	20,115	97,368	159,600
Trade receivables	4,672	12,323	18,618	25,192	41,346	56,152
Inventories	2,236	3,481	6,196	12,311	14,376	19,216
Other current assets	10,458	14,314	34,089	195,425	230,792	287,223
Non-current assets	**156,743**	**287,911**	**443,476**	**797,048**	**1,090,135**	**1,465,625**
Tangibles	30,431	58,195	87,045	178,849	259,848	353,698
Intangibles	653	1,088	1,432	2,557	2,902	3,570
Other non-current assets	125,659	228,628	354,999	615,642	827,385	1,108,357
Total assets	**187,402**	**353,708**	**578,571**	**1,050,091**	**1,474,018**	**1,987,816**
Current liabilities	**47,379**	**90,443**	**154,040**	**267,956**	**366,893**	**465,532**
Short-term loans	32,600	53,361	70,184	109,810	131,012	169,837
Trade payables	6,322	11,896	22,482	38,060	52,164	69,723
Other current liabilities	8,457	25,186	61,374	120,086	183,717	225,972
Non-current liabilities	**100,512**	**172,615**	**243,104**	**325,023**	**419,685**	**570,057**
Long-term loans	89,994	145,647	192,799	310,362	403,045	549,589
Other non-current liabilities	10,518	26,968	50,305	14,661	16,640	20,468
Minority Interest	**0**	**0**	**0**	**0**	**0**	**0**
Shareholders' equity	**39,511**	**90,650**	**181,427**	**457,112**	**687,440**	**952,227**
Total liabilities and equity	**187,402**	**353,708**	**578,571**	**1,050,091**	**1,474,018**	**1,987,816**

Key metrics	2020	2021	2022	2023	2024F	2025F
Growth						
Revenue growth	-38%	110%	220%	62%	54%	36%
EBITDA growth	-31%	238%	182%	47%	40%	39%
Net income growth	-223%	-247%	477%	244%	-20%	27%
Profitability						
Gross Margin	5.8%	22.7%	24.3%	23.7%	20.9%	22.2%
EBITDA margin	17.8%	28.7%	25.3%	22.9%	20.8%	21.2%
Net margin	-12.0%	8.4%	15.2%	32.3%	16.8%	15.6%
Return on assets (ROA)	-3.3%	3.0%	10.2%	20.0%	10.3%	9.6%
Return on equity (ROE)	-13.9%	12.6%	34.9%	51.1%	22.8%	20.2%
Return on cap. emp. (ROCE)	-1.8%	9.1%	26.1%	35.7%	19.0%	17.4%
Leverage						
Net Debt	98,209	152,474	154,959	193,266	267,234	391,992
Net debt / Equity	2.5	1.7	0.9	0.4	0.4	0.4
Net debt / EBITDA	11.9	5.5	2.0	1.7	1.7	1.7
EBIT Interest coverage	-3.2	5.3	11.7	7.3	8.7	11.3
Efficiency						
Total asset turnover	0.2	0.3	0.5	0.5	0.5	0.5
Equity turnover	1.2	1.1	1.7	1.1	1.1	1.1
WC/Sales	3%	0%	0%	0%	0%	0%
Opex/Sales	12.0%	5.9%	1.0%	-0.8%	-0.2%	-1.0%

Cash flow	2020	2021	2022	2023	2024F	2025F
EBITDA	8,261	27,922	78,684	115,397	161,695	224,161
Change in working capital	-8,121	12,977	2,794	-179	878	-1,267
Taxes (EBIT x 20%)	513	-977	-3,971	71,716	4,796	-14,377
Capital expenditure	-7,904	-6,811	-921	-1,032	-97,177	-78,287
Adjustment	9,752	11,621	-71,145	-185,286	0	0
FCFF	2,501	44,732	5,442	616	70,192	130,230

QNB Finansinvest vs Consensus		2024F			2025F	
	Estimate	Cons.	Deviation	Estimate	Cons.	Deviation
Revenues	779,085	765,786	2%	1,058,075	911,559	16%
EBITDA	161,695	163,299	-1%	224,161	193,267	16%
Net Income	130,604	95,961	36%	165,338	111,074	49%

Source: QNBFI Estimates

INVESTMENT THEME

We are reiterating our Outperform rating for THY with a revised 12-month target price of TRY450.00/share, suggesting 53% upside potential. The global air traffic figures have finally reached above its pre-pandemic level while the cumulative EBITDA generation of our global peer group is forecasted to stay 6.0% below its pre-pandemic level. When it comes to THY, the airline is still maintaining its record high operational performance despite the headwinds on Pratt & Whitney engine issues, resulted in grounding of 32 aircrafts of THY as of August, while the company maintained its ASK growth at 10.1%in the first six months. Despite a 17.3% analyst EBITDA contraction along with the negative effect of grounded aircrafts and 4.3% rise in the total CASK on rising personnel expenses. For the second half, we are more positive for the outlook as yield pressure for the industry has relatively softened while the declining trend in the jet fuel prices suggest a much promising outlook for the cost management. In terms of the passenger figures, we think that the tourism season is still maintaining its momentum on foreign tourist arrivals while the company's strategy to increase its capacity in relatively profitable regions such as Asia Pacific and North America hint for successful yield management until the end of the year. Accordingly, we increase our analyst EBITDA forecast by 10.0% to USD4.8bn for 2024, implying an 11.0% EBITDA growth for the second half in USD-terms while most of the BIST companies are forecasted to post operational earnings contraction. Along with our downward revision on the net debt position from USD9.0bn to USD7.0bn for the year end, the stock trades at 3.9x EV/EBITDA and 3.1x P/E vs. its historical averages of 6.4x and 7.5x, respectively. Along with unique operational earnings momentum in 2H24 compared to other BIST companies and supports of relatively lower fuel expenses and on-going healthy tourism season, we maintain our positive view for the stock and keep our Outperform rating.

The global air traffic hovering at all-time high levels: The global air traffic kept its all-time high level in the first of 2024 when the total traffic reached to 13.4% higher level on YoY basis with 17.4% rise in the international and 7.4% rise in the domestic flights. The major part of this growth was driven by the easing of travel restrictions, particularly in the Asia-Pacific region, where countries like China and India have seen a marked increase in both domestic and international travel. The reopening of these markets has not only fueled tourism but has also revitalized business travel, contributing to the overall increase in passenger numbers. In other destinations, the growth figures were also solid strong with almost all regions posted double digit YoY growth as of 1H24, excluding North America where the growth was materialized at 6.4%, much higher than its historical average.

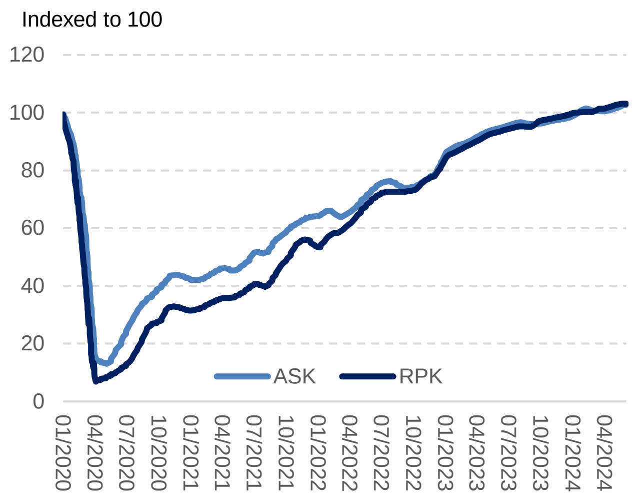
In terms of supply of sets, global capacity also registered a 11.6% rise in the same period while the demand expansion outpacing the capacity led to a healthy recovery in the load factors that the average load factor posted a 1.3% improvement and reached to 82.3%.

Regarding on-going high season, the latest monthly figure of June showed a 12.3% YoY industrywide growth for the international passenger traffic while all regions achieved growth rates in the double digits while Asia Pacific remained the one with the highest growth at 22.6%. In line with superb June figures, demand outlook for the all regions keep recording all-time highs, except Asia Pacific where the demand is still recovering its pre-pandemic values.

In domestic traffic, comprising 40% of the total market, the total demand posted a 7.4% growth vs. 3.6% capacity growth, having led to a 3.0% improvement in the load factor. Excluding China with a 16.1% YoY growth, the growth figures were relatively limited while YoY stable growth figure of 4.3% in June'24 compared to previous month suggest a return to the stability and consistency of single digit growth observed in the pre-pandemic period.

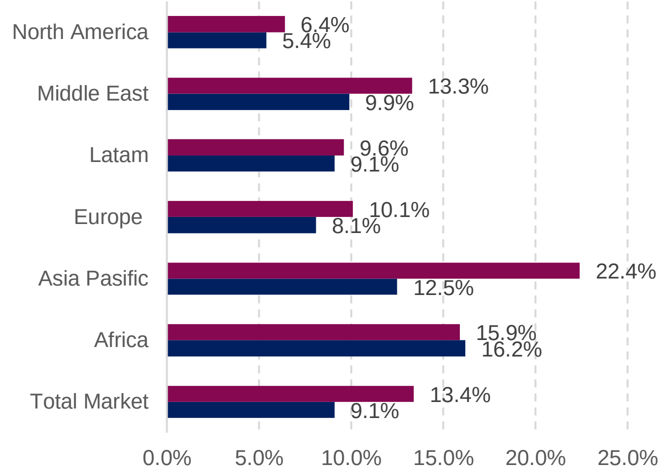
According to the latest publication of IATA air passenger market analysis on the trip bookings made in June and July for the travel during July and August, international segment is expected to maintain its solid momentum with a 5.4% YoY rise while the domestic segment peaked its level in the previous year with a 0.9% YoY decline this year. All in all, the global air traffic demand is forecasted to maintain in its healthy growth in the coming period in a milder pace compared to after-pandemic period. However, on-going growth momentum in all time high demand outlook shows promise for the future, especially in the international segment.

Figure 2– **Global Capacity and Traffic Performance**



Source: IATA , QNBFI Calculations

Figure 3– **Global RPK Breakdown (June'24)**



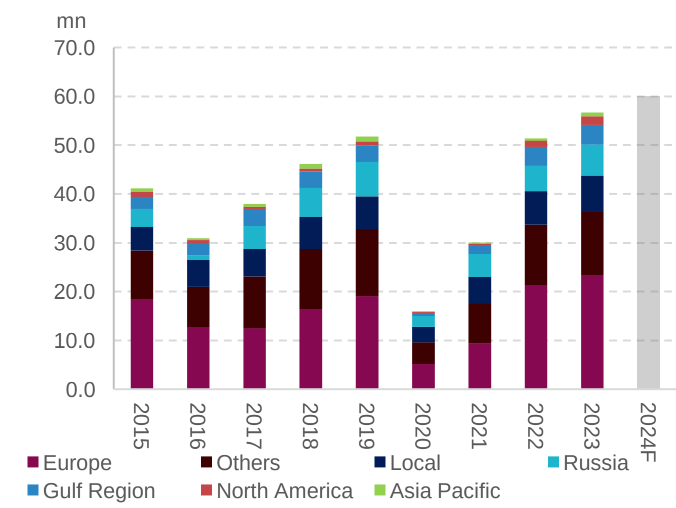
Source: IATA, QNBFI Calculations

Tourism season is still maintaining its solid pace: In the first 6 months of the year, tourist arrivals into Türkiye posted another solid growth of 13.9% while European tourists registered the highest portion in total mix again with an 14.4% increase compared to the same period of the last year. For the full year, official target is 5.8% growth in tourist arrivals on top of 10.3% increase in 2023 which had already reached to its all-time high level. Due to its geographic location with rich sea side summer locations, the share of total tourist arrivals in the second half of the year is around 60% of the total. Accordingly, although the first half figures are not fully indicator for the full year pattern, we consider the strength in the first half is well enough to reach the full year target as similar pattern compared to 2H23 is well enough to reach the target.

We are aware of the negative impact of loss of purchasing power in local currency having led to some constraints to the tourism industry in Türkiye. However, we think that the negative effect has been mostly driven by local tourists in such an environment as the planned slow-down in economic activities by the authorities having been started to be observe. Accordingly, the consumer confidence index has declined over the two consecutive months from its level of 80.5 in May'24 to 75.9 in July'24.

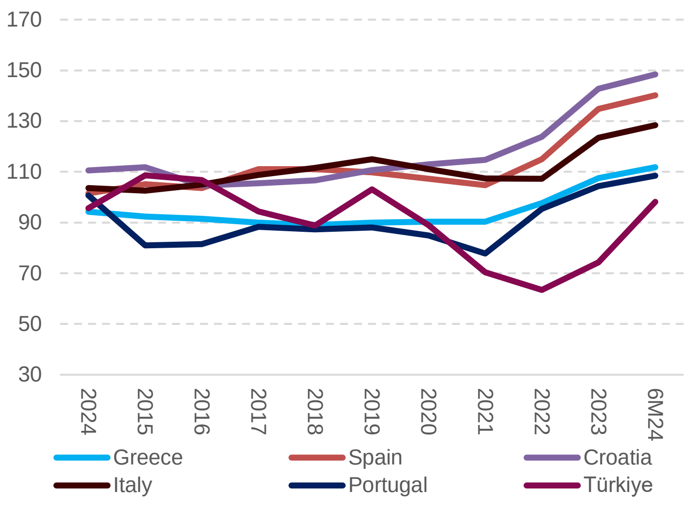
On the contrary, we are not pessimistic for overall industry given we still calculate the average price level of packaged holiday tours for our sample group is at 23.7% higher compared to its pre-pandemic level vs. a 4.8% lower level in Türkiye in EUR-terms. 10.8% rise in the hotel arrivals by the foreign tourists in 6M24 is also supportive for our argument of on-going price competitiveness of our tourism industry compared to European peers. Last but not least, especially in the after-pandemic period, we have observed the extended summer seasons in sea side tourist destinations in Türkiye which also positively being reflected to the international air passenger figures as it did over the last 2 years. Accordingly, we think that on-going momentum in tourist arrivals from Europe to be maintained in the coming months, which promises a better outlook for point to point air traffic for local airlines on top of the positive impact on the tourism industry.

Figure 4– Türkiye: Breakdown of Tourist Arrivals



Source: Ministry of Culture and Tourism, QNBFI Calculations

Figure 5– Packaged Holiday Price Index



Source: ESTAT, QNBFI Calculations

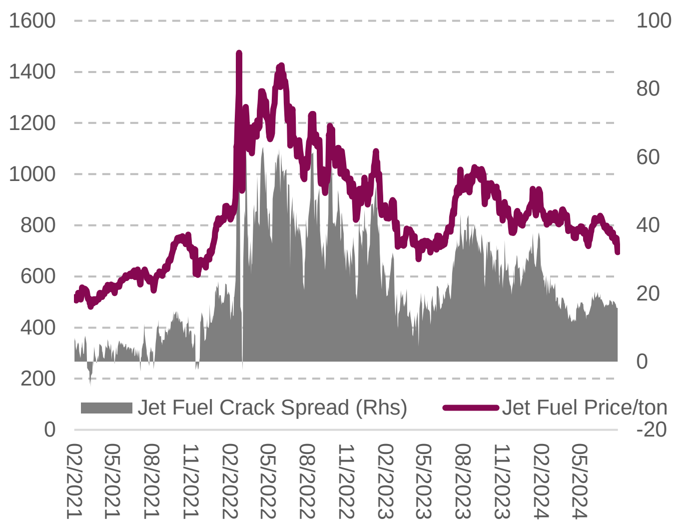
Fuel prices are in the declining trend: In line with our bearish view for the oil industry, the sectoral profitability is still in its normalization trend following the record high profitability environment after pandemic that Russia-Ukraine war also positively affected both oil and product crack spreads. Currently, the oil prices are 8.5% down on YoY basis and 3.0% compared to its 2023 average levels. In terms of product prices, we observe a much higher pressure on the middle distillate product prices given the average crack spreads are now 51.9% lower compared to the same period of the previous year, implying an average of 22.0% decline in the prices of diesel and jet fuel.

We currently maintain our bearish stance for the oil and oil derivative products given an imbalance between supply and demand in favor of supply while net refining capacity additions in 2025 may limit the upside risk in the middle distillate product crack spreads on the potential improvement in the demand environment in Asia Pacific in the coming months.

Compared to local airlines, most of the airline companies in our global peer group, the hedge ratios have increased over the year which are averaged around 70.0% level vs. THY's level around 50.0%. For the coming period, we are still pessimistic for the middle distillate crack spreads, especially for jet fuel, which are averaged at 22.7% lower compared to same period of the last year despite around 10.6% higher air traffic.

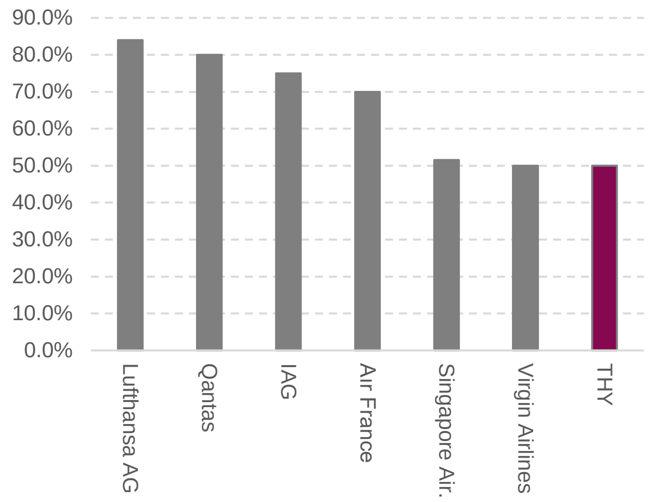
Fuel expenses comprise nearly 30-35% of airlines as the largest portion of its operating cash costs. Accordingly, the declining jet fuel prices are both sentimentally and operationally positive for the airlines while the main determinant of the pricing is the supply and demand balance. Thus, we welcome declining fuel prices positive for the industry, especially for the airlines with relatively lower hedge ratios, in such an environment where the demand dynamics are promising, which pave a way for a rise in the operating margins.

Figure 6– Jet Fuel Prices and Crack Spread



Source: Reuters, QNBFI Calculations

Figure 7– Fuel Hedge Ratios



Source: Company Presentations, QNBFI Calculations

Operational outlook is still healthy: Despite the grounded 32 aircrafts due to technical issues as of August'24, THY successfully ended the first half of 2024 with a 10.1% ASK growth while its ASK level reached to 37.5% higher level compared to its pre-pandemic level. In terms of profitability, the company's analyst EBITDA level declined by %17.3 on YoY basis on both 4.2% decline in the revenue yields, mostly on normalizing passenger yields, while the total CASK level increased by 4.3% mostly on 23% rise in the personnel CASK and GTF related groundings on YoY basis. Despite a YoY contraction in its EBITDA level, this level was almost 3 times higher than its pre-pandemic level vs. 16.2% lower cumulative EBITDA generation of its global peers.

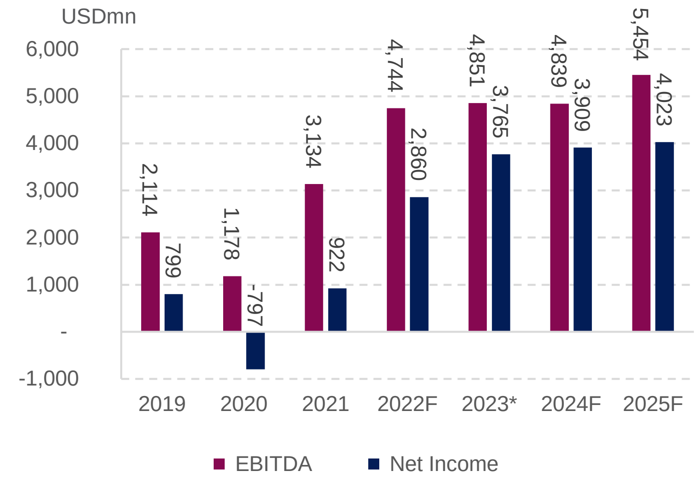
Along with on-going momentum in the air travel demand with softening passenger yield pressure in the second half of the year vs. its impact in 1H24, we think that THY will maintain its solid operational performance in such an environment where most of the industries in the domestic market has been negatively effecting from slow-down in the economic activities on tight monetary and fiscal policies and/or loss of competition in the export market on strength of TRY compared to hard currencies while the cost bases have been increased on energy and personnel expenses.

For the full year, we plug in 10.0% ASK growth with an almost 2.0% decline in the passenger yields on YoY basis vs. 3.8% rise in CASK on 6.6% increase in ex-fuel CASK. Along with our assumption of 15.0% cargo volume growth, we calculate the company to generate USD4.8bn analyst EBITDA for the full year, broadly in line with its record-high level in 2023. This level is also 128.9% higher than its pre-pandemic level vs. an expected 6.1% lower level for our peer group's cumulative EBITDA.

With our assumption of USD4.8bn EBITDA generation for 2024, we calculate the company's bottom-line to materialize around USD3.9bn for the full year. This implies a ROE level of 22.8% vs. the global industrial's forecasted average of 3.6% level.

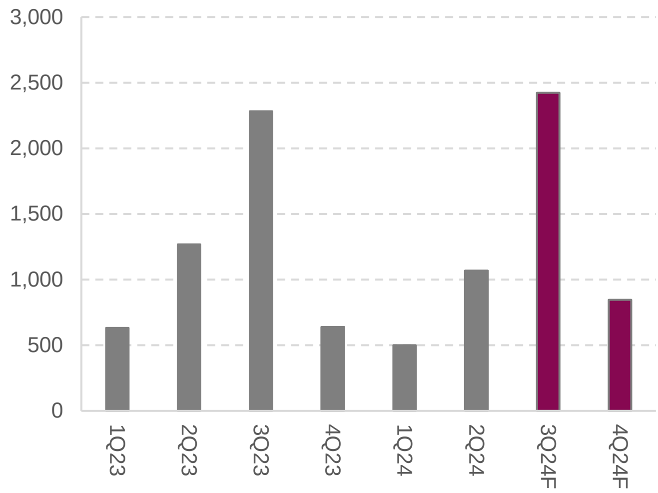
For 2025, along with our initial assumption of 11.0% ASK growth with an almost stable RASK-CASK spread compared to 2024, we calculate 13.0% EBITDA growth, implying a net income generation of USD4.0bn, implying a 27.0% net income growth in TRY-terms.

Figure 8– THY: EBITDA and Net Income Generation



Source: QNBFI Calculations and Estimates
**Deferred tax income adjusted*

Figure 9– THY: EBITDA Quarterly Generation Projection

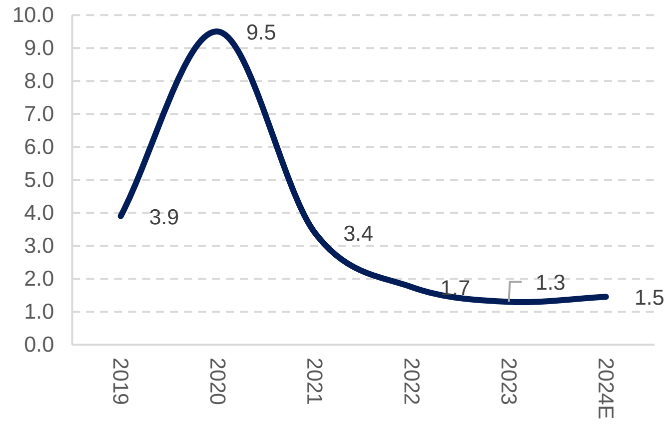


Source: QNBFI Calculations and Estimates

Debt matrices under control with strong cash generation capability: With accelerating cash generation capability and cost management programs, THY successfully deleveraged its balance sheet that its net debt position of USD14.0bn by the end of 2020 to have lowered to USD5.8bn as of 1H24. In other words, its net debt/EBITDA of 3.9x by the end of 2019, had reached to 9.5x in 2020, declined to 1.1x by the end of 1H24, based on its 12-month trailing EBITDA figure. On top of it, the company's liquidity position increased from its level of USD1.9bn by the end of 2020 to USD6.4bn as of 1H24, comprising 29.0% of its trailing 12-month revenues vs. its pre-pandemic level of 19.0%.

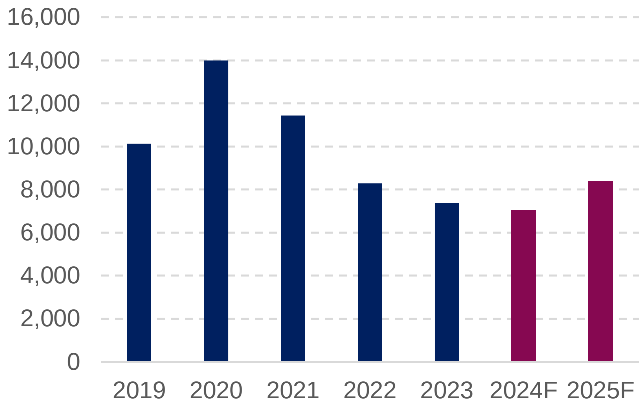
By the end of 2024, we now calculate its net debt position to materialize around USD7.0bn vs. our previous assumption of USD9.0bn, implying 1.5x net debt/EBITDA for the year-end. Airlines should be considered as growth plays and their balance sheet management is highly important for the existence of their businesses due to high investment requirements. We highly welcome THY's successful deleveraging process over the last 3 years which differentiated its position from its global peers on balance sheet health as an average of net debt/EBITDA level in the industry hovering around 2.9x while their capacity growth is mostly relatively lower compared to THY. Last but not least, on-going successful deleveraging strategy is likely to be more important on its way through its growth plans including a fleet target above 800 aircrafts and revenue target of USD50bn by 2033.

Figure 10– THY: Net Debt / EBITDA



Source: QNBFI Calculations & Estimates

Figure 11– THY: Net Debt Development (USD,mn)



Source: QNBFI Calculations & Estimates

Valuation

We base our valuation on a pure multiple valuation analysis, as the long-term forecasts in DCF modelling are highly sensitive to changes in the industry outlook and oil prices, which are highly unpredictable.

- We factor in a target EV/EBITDA multiple of 5.0x for 2024 and 5.1x for 2025 in our multiple valuation analysis– in line with the average of its global peers.
- We base our valuation on an 50-50 weighing of the results derived from 2024 and 2025 prospective earnings, respectively.
- The stock trades at an EV/EBITDA of 3.9x on our 2024 forecasts vs. an average of 5.0x among global peers.
- The airline trades at an EV/EBITDA of 3.7x on 2025 prospective earnings vs. an average of 5.1x for its global peers.

Figure 12 – THY: Valuation Summary (USDmn)

THY (USDmn)	2024F	2025F
Target EV/EBITDA	5.0	5.1
THY- EV/EBITDA	3.9	3.7
EBITDA (USDmn)	4,839	5,454
Net Debt (USDmn)	7,032	8,387
Target EV	24,009	27,788
Implied Equity Value	16,976	19,402
Weight (%)	50.0%	50.0%
Implied Equity Value (USDmn)	**18,189**	

Source: QNBFI Estimates

Figure 13 – Peer Analysis

Company	Mcap (USDmn)	P/E 24x	P/E 25x	EV/EBITDA 24x	EV/EBITDA 25x
Aır France	2213	2.9	1.9	2.9	2.5
Deutsche Lufthansa AG	7319	6.6	4.3	3.1	2.6
Finnair	508	7.8	5.8	2.9	2.7
IAG	9061	4.1	3.8	2.7	2.6
Alaska Air Group	4387	8.7	6.3	4.5	3.6
American Airlines Group Inc	6365	9.7	5.4	8.8	7.3
Delta Airlines	24971	6.3	5.5	5.2	4.7
Hawaiian Holdings Inc	776	n.a.	n.m.	n.m.	21.4
JetBlue Airways Corp	1599	n.a.	n.a.	18.4	8.3
United Continental Holding	13231	4.1	3.5	4.0	3.6
Copa Holding	3687	5.9	5.4	4.0	3.7
Air China Ltd	14988	20.1	11.3	n.m.	n.m.
Cathay Pacifc Airways	6417	7.2	6.7	4.2	4.2
China Airlines Ltd	3936	10.9	17.5	4.1	3.9
Eva Airways Corp	5771	8.7	11.0	2.8	3.2
Korean Air Lines Co Ltd	5595	n.a.	6.1	3.4	3.4
Singapore Airlines Ltd	13762	9.0	12.1	5.0	5.4
Qantas Airways Ltd	6493	6.9	6.2	3.5	3.2
Average		7.9	7.1	5.0	5.1
THY	12051	3.1	3.0	3.9	3.7
Discount/Premium		-61.1%	-57.5%	-20.5%	-26.5%

Source: QNBFI Estimates

QNB Finansinvest Rating System

We employ a relative scale in our rating system (i.e. Market **Outperform, Neutral, Underperform**) in order to better present relative value propositions and more actively pursue long vs. short ideas at the BIST. The relevant benchmark is the broader Turkish stock market, using the BIST-100 index as a basis. The ratings also incorporate a certain degree of relativity within the analyst's own stock coverage universe due to asymmetric return expectations among the industries under our BIST coverage. The rating system combines analysts' views on a stock relative to the sectors under coverage, and the sector call relative to the market, together providing a view on the stock relative to the market.

Individual ratings reflect the expected performance of the stock relative to the broader market over the next 6 to 12 months. The assessment of expected performance includes a function of near-term company fundamentals, industry outlook, confidence in earnings estimates and valuation, and other factors.

An essential element of our rating methodology involves benchmarking a 12-month expected return against the cost of equity. We set a required rate of return for each stock, calculated from our risk-free rate and equity risk premium assumptions. The price target for a stock represents the value that the stock is expected to reach or sustain over the performance horizon of 12 months, according to the view of the analyst.

We have separated the stocks under our coverage into two groups, mainly with respect to their liquidity (market cap, free float market cap and historical average daily trading volume) as small-cap stocks exhibit different risk/return characteristics to more-liquid large-caps. For the purposes of the relative stock rating, however, stocks within each group will be considered on an unweighted basis with regard to their market capitalization.

For a stock to be assigned an **Outperform** rating, the implied return *must* exceed the required rate of return by at least 5 percentage points over the next 12 months for our larger-cap stock coverage, or by 10 percentage points for the small-cap group. For a stock to be assigned an **Underperform** rating, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months. Stocks between these bands will be classified as **Neutral**.

When the potential upside of an *average* stock in our coverage exceeds its required rate of return (i.e. the market upside exceeding the implied average cost of capital), a greater number of stocks would fall into the aforementioned Outperform (Buy) category, illustrating the significance of the "relative return" concept (vis-à-vis absolute return) in picking better investment ideas with a positive alpha. The same holds true when the potential upside of an *average* stock in our coverage falls short of its required rate of return.

In this regard, as a supplemental methodology, we rank the stocks in our coverage according to their notional target price with respect to their current market price, and then categorise the top group (approximately 40-50% of the companies under coverage) as Outperform, the next 40-50% as Neutral and the lowest 10-20% (and no less than 10%) as Underperform.

It should be noted that the expected returns on some stocks may at times fall outside the relevant ranges of the applicable respective rating category because of market price movements and/or other short-term volatility or trading patterns. Such interim deviations from specified ranges are permitted but becomes subject to review.

Also note that the analyst's short-term view may occasionally diverge from the stock's longer-term fundamental rating.

Outperform. We expect the stock to outperform the BIST-100 over the next 6 to 12 months.

Neutral (Market Perform). We expect the stock to broadly perform in line with the BIST-100 index over the next 6 to 12 months. (Although we would normally have a neutral assessment of stocks in this category, if a stock has gone through a period of market underperformance, it would be an indication that the stock may be expected to improve its performance relative to market averages in the coming period, and vice versa).

Underperform. We expect the stock to underperform the BIST-100 over the next 6 to 12 months.

N/R. Not Rated.

U/R. Under Review.

Analyst Certification

The following analysts hereby certify that the views expressed in this research report accurately reflect their own personal views regarding the securities and issuers referred to therein and that no part of their compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in the research report: **Can Alagöz.**

Unless otherwise stated, the individuals listed on the cover page of this report are research analysts.

Disclaimer

All information given in this document has been obtained from sources believed to be reliable, and while QNB FINANSINVEST has taken reasonable care in verifying the accuracy and completeness of the information presented herein, it cannot be held responsible for any errors, omissions or for consequences arising from the use of such information. The investment information, commentary and advice contained within this document does not constitute investment advisory activity or any solicitation to buy or sell the securities mentioned herein. Investment advisory services are provided by authorized institutions to persons and entities privately by considering their risk and return preferences, while the commentary and advice included in this document is of a general nature and therefore may not be appropriate for your financial situation or your risk and return preferences. As such, investment decisions based only on the information herein may not produce results that fit your expectations. The affiliates, officers, partners and employees, including persons involved in the preparation or issuance of this material may have a direct or indirect position in any security mentioned in this report.