

**KUVEYT TRK KATILIM BANKASI
ANONİM ŐİRKETİ AND ITS SUBSIDIARIES**

**CONSOLIDATED FINANCIAL
STATEMENTS FOR THE
YEAR ENDED
31 DECEMBER 2017 AND
INDEPENDENT AUDITOR’S REPORT**

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of Kuveyt Türk Katılım Bankası Anonim Şirketi

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of Kuveyt Türk Katılım Bankası Anonim Şirketi (the “Bank”) and its subsidiaries (the “Group”), which comprise the consolidated statement of financial position as at 31 December 2017, the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and the notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (“IFRSs”).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (“ISAs”). Our responsibilities under those standards are further described in the Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants’ Code of Ethics for Professional Accountants (the “IESBA Code”), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current year. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key Audit Matter	How the matter was addressed in the audit
Allowance for probable losses on due from corporate and commercial financial activities At 31 December 2017, due from financing activities were TL 30,452,322 thousands against which allowance for impairment on due from financing activities of TL 766,954 thousands were recorded ending with a net carrying amount of TL 29,685,368 thousands. The details are disclosed in Note 7 of the consolidated financial statements. For impairment allowances, a management decision and judgement is required to determine when an impairment event has occurred and a necessary classification should be done. So there is a risk of misstatement in the calculation of the allowance related to the classification of performing / funds in arrears due from financial activities in accordance with IAS 39. Furthermore, the specific allowances are made against the carrying amount of due from financing activities that are identified as being impaired based on regular reviews of outstanding balances to reduce these due from financing activities to their recoverable amounts. In assessing the recoverable amounts of the due from financing activities, the estimated future cash flows are discounted to their present value using the loans' original yield which requires management's significant judgement to exercise. Because of the significance of these judgements and the size of due from financing activities, the audit of allowance for probable losses on due from corporate and commercial financing activities is a key area of focus. Furthermore there is a risk of misstatement in the calculation of allowance related to errors in the main parameters of allowance for probable losses on due from corporate and commercial financing activities (specific and collective) in accordance with IAS 39 in the IFRS financial statements.	We reviewed the provisioning methodology implemented by the Group. We understood and tested the key controls over the classification and provisioning methodology such as; system based and manual controls over the timely recognition of impaired due from financing activities, controls over the impairment calculation models including data inputs, controls over cash flow estimates and finally governance controls which includes the management meetings for the approval process of allowance for probable losses on due from financing activities. In addition to testing the key controls, we selected samples of due from financing activities outstanding at the reporting date and assessed critically the criteria for determining whether an impairment event had occurred and therefore whether there was a requirement to calculate an impairment provision. For the samples selected, we also verified whether all impairment events as identified by us had also been identified by the Group's management. Our selected samples also included non-performing due from financing activities, where we assessed management's forecast of recoverable cash flows, valuation of collaterals, estimates of recovery on default and other sources of repayment. For the performing due from financing activities, we assessed that the borrowers did not exhibit any possible default risk that may affect the repayment abilities. We also tested the appropriateness and accuracy of the inputs to those models, such as probability of default and loss given default rates, and where available, compared data and assumptions made to external benchmarks. Finally, we understood and tested the controls over related disclosures.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current year and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Yaman Polat.

DRT BAĞIMSIZ DENETİM VE SERBEST MUHASEBECİ MALİ MÜŞAVİRLİK A.Ş.

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

İstanbul, 6 June 2018

Kuveyt Türk Katılım Bankası Anonim Şirketi and its Subsidiaries

Consolidated statement of financial position as at December 31, 2017
(Currency – In thousands of Turkish Lira - TL)

	Notes	December 31, 2017	December 31, 2016
Assets			
Cash and balances with the Central Bank	4	1,857,063	1,875,863
Balances with other banks and financial institutions	4	4,951,453	5,979,425
Reserve deposits at the Central Bank	5	6,474,434	5,678,251
Financial assets – held for trading	6	88,624	166,762
<i>Derivative financial instruments</i>	20	26,699	110,049
<i>Share Certificates</i>	6	390	390
<i>Sukuk held for trading</i>	6	61,535	56,323
Financial assets – available-for-sale	6	4,428,672	3,751,680
Due from financing activities, net	7	34,997,542	27,087,876
Minimum finance lease payments receivable, net	8	1,929,863	1,545,637
Precious Metals		693,239	802,280
Construction projects, net	10	76,234	77,939
Joint venture		19,699	15,236
Investment properties, net	11	84,992	26,129
Property and equipment, net	13	430,177	426,867
Intangible assets, net	14	169,802	140,467
Deferred tax assets	17	127,072	110,410
Other assets	9	938,061	700,487
		57,266,927	48,385,309
Assets and a disposal group held for sale	12	53,199	42,667
Total assets		57,320,126	48,427,976
Liabilities and equity			
Due to other financial institutions and banks	15	3,387,127	3,273,326
Sukuk securities issued	15	5,651,841	4,763,981
Subordinated loans	15	1,360,338	1,981,646
Money market balances		750,524	1,219,873
Current and profit / loss sharing investors' accounts	16	40,354,741	32,016,053
Derivative financial instruments	20	151,493	257,556
Employee benefit obligations	18	177,829	122,508
Income taxes payable	17	56,271	27,851
Other liabilities and provisions	19	506,615	525,323
Total liabilities		52,396,779	44,188,117
Share capital	21	3,097,322	2,787,322
Share premium		22,841	22,933
Available for sale investments reserve, net of tax		(10,583)	(35,279)
Employee termination benefits reserve, net of tax		(26,947)	(13,753)
Legal reserves and retained earnings	22	1,838,947	1,443,117
Currency translation differences		79,618	126,484
Hedging fund		(60,854)	(70,863)
Other reserve	22	(24,763)	(22,162)
Non-controlling interest		7,766	2,060
Total equity attributable to equity holders of the parent		4,923,347	4,239,859
Total liabilities and equity		57,320,126	48,427,976

The policies and explanatory notes are an integral part of these consolidated financial statements.

Kuveyt Türk Katılım Bankası Anonim Şirketi and its Subsidiaries

Consolidated statement of comprehensive income for the year ended December 31, 2017
(Currency – In thousands of Turkish Lira - TL)

	Notes	2017	2016
Income from financing activities:			
Profit on originated loans from profit / loss sharing accounts		1,675,258	1,272,621
Profit on originated loans from current accounts and equity		1,535,513	1,350,757
Profit on deposits with other banks and financial institutions		87,447	42,866
Profit on finance leases		135,232	105,511
Profit on Sukuk investments		280,500	199,949
Total income from financing activities		3,713,950	2,971,704
Profit shares distributed to participation accounts		(1,204,485)	(943,006)
Profit shares distributed to other banks and financial institutions		(554,850)	(555,155)
Net financing income		1,954,615	1,473,543
Provision for impairment of amounts due from financing activities and lease receivables	7, 8	(756,644)	(574,792)
Net financing income after provision for impairment in due from financing activities and lease receivables		1,197,971	898,751
Foreign exchange gain, net		179,845	196,215
Net financing income after net foreign exchange gain / (loss)		1,377,816	1,094,966
Fees and commission income	25	559,589	477,345
Net trading income		206,736	162,970
Other income		145,442	191,077
Share of a joint venture income		5,860	1,938
Total other operating income		917,627	833,330
Fees and commission expense	25	(174,571)	(141,509)
Staff costs	26	(712,884)	(625,109)
Depreciation and amortization expense		(86,351)	(82,160)
Withholdings and other taxes		(8,616)	(47,337)
Rent expense		(115,127)	(101,352)
Other expenses	27	(294,250)	(234,868)
Share of (loss) of a joint venture		-	-
Total other operating expense		(1,391,619)	(1,232,335)
Income before taxation		903,824	695,961
Current tax charge	17	(197,600)	(124,960)
Deferred tax (charge)/credit	17	9,604	(6,277)
Net income for the year		715,828	564,724
Attributable to:			
- Owners of the equity		710,122	563,984
- Non-controlling interests		5,706	740
Other comprehensive income			
Items that are or may be reclassified subsequently to profit or loss:			
Exchange differences on translation of the foreign subsidiary		(36,857)	17,320
Available-for-sale investments reserve		24,696	(40,673)
-Net change in fair value		30,870	(50,841)
-Deferred tax relating to component of other comprehensive income		(6,174)	10,168
Items that will not be reclassified to profit or loss			
Employee termination benefits reserve		(13,194)	1,163
-Net change in fair value		(16,492)	1,454
-Deferred tax relating to component of other comprehensive income		3,298	(291)
Other comprehensive income for the year		(25,355)	(22,190)
Total comprehensive income for the year		690,473	542,534
Attributable to:			
- Owners of the equity		684,767	541,794
- Non-controlling interests		5,706	740
Basic and diluted earnings per share for net income attributable to the ordinary equity holders of the Group during the year (in full TL per share)	23	0.235	0.207

The policies and explanatory notes are an integral part of these consolidated financial statements.

Kuveyt Türk Katılım Bankası Anonim Şirketi and its Subsidiaries

Consolidated statement of changes in equity for the year ended December 31, 2017
(Currency – In thousands of Turkish Lira - TL)

	Share Capital	Share Premium	Legal Reserves	Retained Earnings	Other Reserves	Available-for-sale investments reserve	Employee termination benefits reserve	Currency Translation Differences	Hedging Funds	Non-Controlling Interest	Total
Balances at January 1, 2016	2,527,322	22,933	100,287	1,042,245	(22,162)	5,394	(14,916)	70,961	(32,660)	1,320	3,700,724
Share capital increase	260,000	-	-	(260,000)	-	-	-	-	-	-	-
from retained earnings	260,000	-	-	(260,000)	-	-	-	-	-	-	-
cash injection	-	-	-	-	-	-	-	-	-	-	-
Transfer from retained earnings to legal reserves	-	-	22,574	(22,574)	-	-	-	-	-	-	-
Hedging funds	-	-	-	-	-	-	-	-	-	-	-
Dividends paid	-	-	-	(3,399)	-	-	-	-	-	-	(3,399)
Total comprehensive income for the year	-	-	-	563,984	-	(40,673)	1,163	55,523	(38,203)	740	542,534
Other	-	-	-	-	-	-	-	-	-	-	-
Balances at December 31, 2016	2,787,322	22,933	122,861	1,320,256	(22,162)	(35,279)	(13,753)	126,484	(70,863)	2,060	4,239,859
Share capital increase	310,000	-	-	(310,000)	-	-	-	-	-	-	-
from retained earnings	310,000	-	-	(310,000)	-	-	-	-	-	-	-
cash injection	-	-	-	-	-	-	-	-	-	-	-
Transfer from retained earnings to legal reserves	-	-	27,528	(27,528)	-	-	-	-	-	-	-
Dividends paid	-	-	-	(4,291)	-	-	-	-	-	-	(4,291)
Total comprehensive income for the year	-	-	-	710,122	-	24,696	(13,194)	(46,866)	10,009	5,706	690,473
Other	-	(92)	-	-	(2,601)	-	-	-	-	-	(2,693)
Non-controlling interest	-	-	-	-	-	-	-	-	-	-	-
Balances at December 31, 2017	3,097,322	22,841	150,389	1,694,264	(24,763)	(10,583)	(26,947)	79,618	(60,854)	7,766	4,923,347

The policies and explanatory notes are an integral part of these consolidated financial statements.

Kuveyt Türk Katılım Bankası Anonim Şirketi and its Subsidiaries

Consolidated statement of cash flows for the year ended December 31, 2017
(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)

	Notes	2017	2016
Cash flows from operating activities:			
Income from continuing operations before taxation		903,824	695,961
Share of (profit) / loss of a joint venture		(5,860)	(1,938)
Depreciation and amortization	11, 13, 14	72,845	82,160
Provision for employee termination and other benefits	18	29,747	16,417
Provision for personnel bonus accrual	18	69,670	55,290
Provision for impairment in due from financing activities and lease receivables	7, 8	756,644	574,792
Income accrual of funds invested		148,126	(62,727)
Reversal of impairment in investment property	10	31,042	51
Deferred income		(67,264)	(37,806)
Impact of exchange difference on cash at banks and loans		(199,180)	(177,535)
Expense accrual of participation accounts		17,113	4,883
Expense and foreign exchange accrual of funds borrowed		(124)	39,184
Other provision		67,072	43,324
Net change in derivative financial instruments		(22,713)	21,940
Gain on sale of property and equipment, intangible assets, investment properties and asset held for sale		(18,580)	(12,469)
Operating income before changes in operating assets and liabilities		1,782,362	1,241,527
Net changes in :			
Reserve deposits at the Central Bank of Turkey		(796,183)	(536,956)
Due from financing activities		(9,416,332)	(2,904,393)
Minimum finance lease payments receivables		(384,226)	(371,399)
Other assets and construction projects		(262,307)	(202,899)
Current accounts and profit/loss sharing investors' accounts		8,263,561	3,809,798
Other liabilities		(461,610)	(59,188)
Payment for employee termination benefits	18	(5,297)	(7,881)
Payment for personnel bonuses	18	(55,290)	(49,677)
Precious metals		109,041	(330,577)
Income taxes paid		(170,987)	(140,600)
Net cash used in operating activities		(1,397,268)	447,755
Cash flows from investing activities:			
Purchase of available-for-sale, held-to-maturity and held-for-trading securities	6	(6,960,727)	(2,622,563)
Proceeds from sale of available-for-sale, held-to-maturity and held-for-trading securities	6	6,284,366	1,200,228
Purchase of property and equipment, intangible assets and investment properties	11, 13, 14	(189,395)	(106,552)
Proceeds from sale of property and equipment, intangible assets and investment properties		88,482	34,728
Proceeds from sale of asset and liabilities held for sale		13,439	(15,335)
Net cash used in investing activities		(763,835)	(1,509,494)
Cash flows from financing activities:			
Dividends paid	21	(4,291)	(3,399)
Increase / (decrease) in due to financial institutions and banks		(507,383)	344,772
Sukuk securities issued		3,085,860	2,329,600
Sukuk securities redeemed		(1,790,002)	(673,768)
Net cash provided by financing activities		784,184	1,997,205
Net increase in cash and cash equivalents		(1,376,919)	935,466
Net foreign exchange difference on cash and cash equivalents		(16,607)	140,046
Cash and cash equivalents at the beginning of the year	4	7,640,555	6,565,043
Cash and cash equivalents at the end of the year	4	6,247,029	7,640,555

The policies and explanatory notes are an integral part of these consolidated financial statements.

Kuveyt Türk Katılım Bankası Anonim Şirketi and its Subsidiaries

Notes to consolidated financial statements for the year ended December 31, 2017
(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)

1. Corporate information

General

Kuveyt Türk Katılım Bankası A.Ş., formerly Kuveyt Türk Evkaf Finans Kurumu A.Ş. , (a Turkish joint-stock company-the Bank) was formed in accordance with the provisions of Decree No. 83/7506, issued on December 16, 1983 relating to the establishment of Special Finance Houses in Turkey. The Bank obtained permission from the Central Bank of Turkey (CBT) on February 28, 1989 and commenced its operations on March 31, 1989. Currently, the Bank is continuing its operations under the purview of the Banking Regulation and Supervision Agency ("BRSA") and the Banking Law No. 5411, dated November 1, 2005. The Bank's head office is located at Büyükdere Caddesi No: 129, 34394 Esentepe Şişli/İstanbul/Turkey. The parent and the ultimate controlling party of the Bank is Kuwait Finance House (KFH) incorporated in Kuwait. Effective from April 8, 2006, the Bank's commercial title was changed from Kuveyt Türk Evkaf Finans Kurumu A.Ş. to Kuveyt Türk Katılım Bankası A.Ş. to comply with the Banking Law No. 5411, dated November 1, 2005.

The consolidated financial statements were authorized for issue by the General Manager and Chief Financial Officer on behalf of the Board of Directors of the Bank on June 6, 2018. The General Assembly has the power to amend the statutory financial statements after issue.

Nature of activities of the Bank and its subsidiaries

The Bank's core business is operating in accordance with the principles of interest-free banking as a participation bank by collecting funds through current and profit/loss sharing accounts, and disbursing funds to its customers.

The Bank's subsidiary, Körfez Gayrimenkul Yatırım Ortaklığı A.Ş., formerly known as Körfez Gayrimenkul İnşaat Taahhüt Turizm San. ve Tic. A.Ş. ("Körfez"), in which the Bank has 75% shareholding was incorporated in June 1996 in Turkey. Körfez's registered address is Büyükdere Caddesi, No: 129/1, 34394 Esentepe Şişli/İstanbul. Körfez is engaged in development and marketing of real estate projects in Turkey. Körfez's main sources of revenue are from the sales of these projects.

The Bank's other subsidiary, Körfez Tatil Beldesi A.Ş. ("Körfez Tatil Beldesi"), in which the Bank has a 100% shareholding was incorporated in 2001 in Edremit, Turkey. Körfez Tatil Beldesi is engaged in Güre Project, which comprises the construction, selling and operating of 199 "time-sharing" houses in Edremit-Balıkesir.

The Bank's other subsidiary, KT Sukuk Varlık Kiralama A.Ş. has been established on September 23, 2011 in Turkey in order to issue Sukuk Securities.

The Bank's other subsidiary, KT Kira Sertifikaları Varlık Kiralama A.Ş. has been established on September 3, 2013 in Turkey.

The Banks' other subsidiary, KT Sukuk Company Limited has been established in Cayman Island on 31 July 2015, for the need of subordinated loan for the Bank.

The Bank's other subsidiary, KT Bank AG which is 100% owned by the Bank was established in April, 2015. Main field of its operations are providing interest free corporate banking services and collecting funds through current and profit/loss sharing accounts in compliance with the regulation.

The bank established a pension company jointly with Albaraka Türk Katılım Bankası A.Ş, holding 50% of the shares. It is registered with the trade name "Katılım Emeklilik ve Hayat Anonim Şirketi", 895027 registry numbered dated 17 December 2013 by İstanbul Register of Commerce.

KT Portföy Yönetim Anonim Şirketi ("Company"), which is 100% owned by the bank was established in 26 May 2015 is operating in Turkey. The main aim of the company is to serve its customers in every aspect of the fund management business with a participation based portfolio management company.

The Bank established an IT company with holding 100% of the shares. It is registered with the trade name "Architect Bilişim Sistemleri ve Pazarlama Anonim Şirketi", dated 1 December 2015 by İstanbul Register of Commerce.

2. Summary of significant accounting policies

Basis of preparation

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”).

The consolidated financial statements have been prepared under the historical cost convention except for financial assets measured at fair value such as derivative financial instruments, financial assets at fair value through profit or loss and available-for-sale investments.

The consolidated financial statements are presented in Turkish Lira (“TL”) and except as indicated, financial information presented in TL has been rounded to the nearest thousand.

The Bank and its subsidiaries which are incorporated in Turkey, maintain their books of accounts and prepare their statutory financial statements in Turkish Lira (TL) in accordance with the regulations on accounting and reporting framework and accounting standards which are determined by the provisions of Turkish Banking Law and accounting standards promulgated by the Banking Regulation and Supervision Agency (BRSA), Turkish Commercial Code and Turkish tax legislation.

The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Use of available information and application of judgment are inherent in the formation of estimates in the following areas: valuation of over-the-counter (“OTC”) derivatives, unlisted securities, retirement benefits obligation, impairment of loans and receivables, provisions for taxes. Actual results in the future may differ from those reported.

The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 2.

Notes to consolidated financial statements for the year ended December 31, 2017

(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)

2. Summary of significant accounting policies (continued)

New and Revised International Financial Reporting Standards

a) Amendments to IFRSs that are mandatorily effective for the current year

Amendments to IAS 12	Recognition of Deferred Tax Assets for Unrealized Losses ¹
Amendments to IAS 7	Disclosure Initiative ¹
Annual Improvements to IFRS Standards 2014–2016 Cycle	IFRS 12 ¹

¹ Effective for annual periods beginning on or after 1 January 2017.

Amendments to IAS 12 Recognition of Deferred Tax Assets for Unrealized Losses

The amendments clarify how an entity should evaluate whether there will be sufficient future taxable profits against which it can utilize a deductible temporary difference.

The application of these amendments has had no impact on the Group's consolidated financial statements as the Group already assesses the sufficiency of future taxable profits in a way that is consistent with these amendments.

Amendments to IAS 7 Disclosure Initiative

This amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both cash and non-cash changes.

Annual Improvements to IFRS Standards 2014–2016 Cycle

IFRS 12: IFRS 12 states that an entity need not provide summarized financial information for interests in subsidiaries, associates or joint ventures that are classified (or included in a disposal group that is classified) as held for sale. The amendments clarify that this is the only concession from the disclosure requirements of IFRS 12 for such interests.

The application of these amendments has had no effect on the Group's consolidated financial statements as none of the Group's interests in these entities are classified, or included in a disposal group that is classified, as held for sale.

b) New and revised IFRSs in issue but not yet effective:

IFRS 9	<i>Financial Instruments</i> ¹
IFRS 15	<i>Revenue from Contracts with Customers</i> ¹
Amendments to IFRS 10 and IAS 28	<i>Sale or Contribution of Assets between an Investor and its Associate or Joint Venture</i>
IFRS 16	<i>Leases</i> ²
Amendments to IFRS 2	<i>Classification and Measurement of Share-Based Payment Transactions</i> ¹
IFRIC 22	<i>Foreign Currency Transactions and Advance Consideration</i> ¹
Amendments to IAS 40	<i>Transfers of Investment Property</i> ¹
Annual Improvements to IFRS Standards 2014–2016 Cycle	<i>IFRS 1</i> ¹ , <i>IAS 28</i> ¹
Amendments to IAS 28	<i>Long-term Interests in Associates and Joint Ventures</i> ²
IFRS 17	<i>Insurance Contracts</i> ³
IFRIC 23	<i>Uncertainty over Income Tax Treatments</i> ²
Amendments to IFRS 9	<i>Prepayment Features with Negative Compensation</i> ²
Annual Improvements to IFRS Standards 2015–2017 Cycle	<i>IFRS 3 and IFRS 11, IAS 12, IAS 23</i> ²

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

² Effective for annual periods beginning on or after 1 January 2019.

³ Effective for annual periods beginning on or after 1 January 2021.

2. Summary of significant accounting policies (continued)

New and Revised International Financial Reporting Standards (continued)

b) New and revised IFRSs in issue but not yet effective (cont'd):

IFRS 9 *Financial Instruments*

IFRS 9 issued in November 2009 introduced new requirements for the classification and measurement of financial assets / liabilities and for derecognition and for general hedge accounting.

Key requirements of IFRS 9:

- all recognized financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortized cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of subsequent accounting periods. Debt instruments that are held within a business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are generally measured at FVTOCI. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading nor contingent consideration recognized by an acquirer in a business combination) in other comprehensive income, with only dividend income generally recognized in profit or loss.
- with regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of a financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of such changes in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.
- in relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model, as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires an entity to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognized.
- the new general hedge accounting requirements retain the three types of hedge accounting mechanisms currently available in IAS 39. Under IFRS 9, greater flexibility has been introduced to the types of transactions eligible for hedge accounting, specifically broadening the types of instruments that qualify for hedging instruments and the types of risk components of non-financial items that are eligible for hedge accounting. In addition, the effectiveness test has been overhauled and replaced with the principle of an 'economic relationship'. Retrospective assessment of hedge effectiveness is also no longer required. Enhanced disclosure requirements about an entity's risk management activities have also been introduced.

Based on the analysis carried out, the Group considers that the new measurement and classification requirements under IFRS 9 did not have a significant impact on the total equity of the Group.

2. Summary of significant accounting policies (continued)

New and Revised International Financial Reporting Standards (continued)

b) New and revised IFRSs in issue but not yet effective (cont'd):

IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and the related Interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a 5-step approach to revenue recognition:

- Step 1: Identify the contract(s) with a customer
- Step 2: Identify the performance obligations in the contract
- Step 3: Determine the transaction price
- Step 4: Allocate the transaction price to the performance obligations in the contract
- Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation

Under IFRS 15, an entity recognizes revenue when (or as) a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer.

Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15.

In April 2016, the IASB issued Clarifications to IFRS 15 in relation to the identification of performance obligations, principal versus agent considerations, as well as licensing application guidance:

The Group recognizes revenue from the following major sources:

- Sale of leisure goods and electronic equipment, including the related loyalty programme 'Maxi-Points Scheme' as disclosed in Note N, servicing fees included in the price of products sold, as well as warranties granted under local legislation as disclosed in Note O;
- Installation of computer software for specialized business applications; and
- Construction of residential properties.

The directors of the Company have preliminarily assessed that the Maxi-Points Scheme and the after-sale services represent two separate performance obligations from the sale of the leisure goods and electronic equipment and accordingly, revenue will be recognized for each of these performance obligations when control over the corresponding goods and services is transferred to the customer. This is similar to the current identification of separate revenue components under IAS 18. Furthermore, even though IFRS 15 requires the transaction price to be allocated to the different performance obligations on a relative stand-alone selling price basis, the directors do not expect that the allocation of revenue to the Maxi-Points, the after-sale services and the leisure goods and electronic equipment sold will be significantly different from that currently determined. The timing of revenue recognition of each of these three performance obligations (i.e. upon redemption of the Maxi-Points taking breakage into account, at a point in time for sale of goods when the goods are delivered to the customer, and over the period the after-sale services are performed) are also expected to be consistent with current practice.

The sales-related warranties cannot be purchased separately and they serve as an assurance that the products sold comply with agreed-upon specifications. Accordingly, the Group will continue to account for the warranty in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets consistent with its current accounting treatment.

2. Summary of significant accounting policies (continued)

New and Revised International Financial Reporting Standards (continued)

b) New and revised IFRSs in issue but not yet effective (cont'd):

As regards the construction of residential properties, the directors have specifically considered IFRS 15's guidance on contract combinations, contract modifications arising from variation orders, variable consideration, and the assessment of whether there is a significant financing component in the contracts, particularly taking into account the reason for the difference in timing between the transfer of control of goods and services to the customer and the timing of the related payments. The directors have assessed that revenue from these construction contracts should be recognized over time as the customer controls the properties during the course of construction by the Group. Furthermore, the directors consider that the input method currently used to measure the progress towards complete satisfaction of these performance obligations will continue to be appropriate under IFRS 15.

As regards the installation of software services, the directors have assessed that these performance obligations are satisfied over time and that the method currently used to measure the progress towards complete satisfaction of these performance obligations will continue to be appropriate under IFRS 15.

The Group evaluates the effects of these standards, amendments and improvements on the consolidated financial statements.

Amendments to IFRS 10 and IAS 28 *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*

The amendments to IFRS 10 and IAS 28 deal with situations where there is a sale or contribution of assets between an investor and its associate or joint venture. Specifically, the amendments state that gains or losses resulting from the loss of control of a subsidiary that does not contain a business in a transaction with an associate or a joint venture that is accounted for using the equity method, are recognised in the parent's profit or loss only to the extent of the unrelated investors' interests in that associate or joint venture. Similarly, gains and losses resulting from the remeasurement of investments retained in any former subsidiary (that has become an associate or a joint venture that is accounted for using the equity method) to fair value are recognised in the former parent's profit or loss only to the extent of the unrelated investors' interests in the new associate or joint venture.

The effective date of the amendments has yet to be set by the IASB; however, earlier application of the amendments is permitted. The directors of the Company anticipate that the application of these amendments may have an impact on the Group's consolidated financial statements in future periods should such transactions arise.

IFRS 16 *Leases*

IFRS 16 introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessors and lessees. IFRS 16 will supersede the current lease guidance including IAS 17 Leases and the related interpretations when it becomes effective.

IFRS 16 distinguishes leases and service contracts on the basis of whether an identified asset is controlled by a customer. Distinctions of operating leases (off balance sheet) and finance leases (on balance sheet) are removed for lessee accounting, and is replaced by a model where a right-of-use asset and a corresponding liability have to be recognized for all leases by lessees (i.e. all on balance sheet) except for short-term leases and leases of low value assets.

2. Summary of significant accounting policies (continued)

New and Revised International Financial Reporting Standards (continued)

b) New and revised IFRSs in issue but not yet effective (cont'd):

IFRS 16 Leases

The right-of-use asset is initially measured at cost and subsequently measured at cost (subject to certain exceptions) less accumulated depreciation and impairment losses, adjusted for any remeasurement of the lease liability. The lease liability is initially measured at the present value of the lease payments that are not paid at that date. Subsequently, the lease liability is adjusted for interest and lease payments, as well as the impact of lease modifications, amongst others. Furthermore, the classification of cash flows will also be affected as operating lease payments under IAS 17 are presented as operating cash flows; whereas under the IFRS 16 model, the lease payments will be split into a principal and an interest portion which will be presented as financing and operating cash flows respectively.

In contrast to lessee accounting, IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17, and continues to require a lessor to classify a lease either as an operating lease or a finance lease.

In contrast, for finance leases where the Group is a lessee, as the Group has already recognized an asset and a related finance lease liability for the lease arrangement, and in cases where the Group is a lessor (for both operating and finance leases), the directors of the Company do not anticipate that the application of IFRS 16 will have a significant impact on the amounts recognized in the Group's consolidated financial statements.

Amendments to IFRS 2 *Classification and Measurement of Share-Based Payment Transactions*

The amendments clarify the following:

1. In estimating the fair value of a cash-settled share-based payment, the accounting for the effects of vesting and non-vesting conditions should follow the same approach as for equity-settled share-based payments.
2. Where tax law or regulation requires an entity to withhold a specified number of equity instruments equal to the monetary value of the employee's tax obligation to meet the employee's tax liability which is then remitted to the tax authority, i.e. the share-based payment arrangement has a 'net settlement feature', such an arrangement should be classified as equity-settled in its entirety, provided that the share-based payment would have been classified as equity-settled had it not included the net settlement feature.
3. A modification of a share-based payment that changes the transaction from cash-settled to equity-settled should be accounted for as follows:
 - i. the original liability is derecognised;
 - ii. the equity-settled share-based payment is recognised at the modification date fair value of the equity instrument granted to the extent that services have been rendered up to the modification date; and
 - iii. any difference between the carrying amount of the liability at the modification date and the amount recognised in equity should be recognised in profit or loss immediately.

The amendments are effective for annual reporting periods beginning on or after 1 January 2018 with earlier application permitted. Specific transition provisions apply. The directors of the Company do not anticipate that the application of the amendments in the future will have a significant impact on the Group's consolidated financial statements as the Group does not have any cash-settled share-based payment arrangements or any withholding tax arrangements with tax authorities in relation to share-based payments.

2. Summary of significant accounting policies (continued)

New and Revised International Financial Reporting Standards (continued)

b) New and revised IFRSs in issue but not yet effective (cont'd):

IFRIC 22 Foreign Currency Transactions and Advance Consideration

IFRIC 22 addresses how to determine the 'date of transaction' for the purpose of determining the exchange rate to use on initial recognition of an asset, expense or income, when consideration for that item has been paid or received in advance in a foreign currency which resulted in the recognition of a non-monetary asset or non-monetary liability (for example, a non-refundable deposit or deferred revenue).

The Interpretation specifies that the date of transaction is the date on which the entity initially recognizes the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. If there are multiple payments or receipts in advance, the Interpretation requires an entity to determine the date of transaction for each payment or receipt of advance consideration.

The Interpretation is effective for annual periods beginning on or after 1 January 2018 with earlier application permitted. Entities can apply the Interpretation either retrospectively or prospectively. Specific transition provisions apply to prospective application.

The directors of the Company do not anticipate that the application of the amendments in the future will have an impact on the Group's consolidated financial statements. This is because the Group already accounts for transactions involving the payment or receipt of advance consideration in a foreign currency in a way that is consistent with the amendments.

Amendments to IAS 40 Transfers of Investment Property

The amendments clarify that a transfer to, or from, investment property necessitates an assessment of whether a property meets, or has ceased to meet, the definition of investment property, supported by observable evidence that a change in use has occurred. The amendments further clarify that the situations listed in IAS 40 are not exhaustive and that a change in use is possible for properties under construction (i.e. a change in use is not limited to completed properties).

The amendments are effective for annual periods beginning on or after 1 January 2018 with earlier application permitted. Entities can apply the amendments either retrospectively (if this is possible without the use of hindsight) or prospectively. Specific transition provisions apply.

Annual Improvements to IFRS Standards 2014–2016 Cycle

The Annual Improvements include amendments to a number of IFRSs, which have been summarised below. The package also includes amendments to IFRS 12 Disclosure of Interests in Other Entities, which is effective for annual periods beginning on or after 1 January 2017 (see section 1A above for details).

- **IFRS 1:** The amendments delete certain short-term exemptions in IFRS 1 because the reporting period to which the exemptions applied have already passed. As such, these exemptions are no longer applicable.
- **IAS 28:** The amendments clarify that the option for a venture capital organisation and other similar entities to measure investments in associates and joint ventures at FVTPL is available separately for each associate or joint venture, and that election should be made at initial recognition of the associate or joint venture.

In respect of the option for an entity that is not an investment entity (IE) to retain the fair value measurement applied by its associates and joint ventures that are IEs when applying the equity method, the amendments make a similar clarification that this choice is available for each IE associate or IE joint venture.

2. Summary of significant accounting policies (continued)

New and Revised International Financial Reporting Standards (continued)

b) New and revised IFRSs in issue but not yet effective (cont'd):

The amendments apply retrospectively with earlier application permitted.

Amendments to IAS 28 *Long-term Interests in Associates and Joint Ventures*

This amendment clarifies that an entity applies IFRS 9 Financial Instruments to long-term interests in an associate or joint venture that form part of the net investment in the associate or joint venture but to which the equity method is not applied.

IFRS 17 *Insurance Contracts*

This new standard requires insurance liabilities to be measured at a current fulfillment value and provides a more uniform measurement and presentation approach for all insurance contracts. These requirements are designed to achieve the goal of a consistent, principle-based accounting for insurance contracts. IFRS 17 supersedes IFRS 4 Insurance Contracts as of 1 January 2021.

IFRIC 23 *Uncertainty over Income Tax Treatments*

This interpretation addresses the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, when there is uncertainty over income tax treatments under IAS 12. It specifically considers:

- Whether tax treatments should be considered collectively
- Assumptions for taxation authorities' examinations
- The determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates
- The effect of changes in facts and circumstances.

Amendments to IFRS 9 *Prepayment Features with Negative Compensation*

This amendment amends the existing requirements in IFRS 9 regarding termination rights in order to allow measurement at amortized cost (or, depending on the business model, at fair value through other comprehensive income) even in the case of negative compensation payments.

Annual Improvements to IFRS Standards 2015–2017 Cycle

- **IFRS 3 and IFRS 11** - The amendments to IFRS 3 clarify that when an entity obtains control of a business that is a joint operation, it remeasures previously held interests in that business. The amendments to IFRS 11 clarify that when an entity obtains joint control of a business that is a joint operation, the entity does not remeasure previously held interests in that business.
- **IAS 12** - The amendments clarify that all income tax consequences of dividends (i.e. distribution of profits) should be recognized in profit or loss, regardless of how the tax arises.
- **IAS 23** - The amendments clarify that if any specific borrowing remains outstanding after the related asset is ready for its intended use or sale, that borrowing becomes part of the funds that an entity borrows generally when calculating the capitalization rate on general borrowings.

The Group evaluates the effects of these standards, amendments and improvements on the consolidated financial statements.

2. Summary of significant accounting policies (continued)

Significant accounting judgments and estimates

Deferred taxes: Deferred tax assets are recognized in respect of tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable profits, together with future tax planning strategies.

Fair value of financial instruments: Where the fair values of financial assets recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgment is required to establish fair values. The judgments include considerations of liquidity and model inputs such as volatility for longer dated derivatives.

Functional and presentation currency

The functional currency of the Bank and its subsidiaries located in Turkey is Turkish Lira (TL). The functional currency of KT Bank AG is EURO. The presentation currency of the Group is TL.

Until December 31, 2005, the consolidated financial statements were restated for the changes in the general purchasing power of TL based on IAS 29 ("Financial Reporting in Hyperinflationary Economies"). Since the objective conditions for the restatement in hyperinflationary economies was no longer applicable at that time, Turkey came off hyperinflationary status effective from January 1, 2006. The financial statements were restated until December 31, 2005 in accordance with IAS 29. Therefore, the non-monetary assets and liabilities and components of shareholders' equity including share capital reported in the balance sheet as of December 31, 2017 and 2016 are derived by indexing the additions that occurred until December 31, 2005 and carrying the additions after this date with their nominal amounts.

Notes to consolidated financial statements for the year ended December 31, 2017
(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)**2. Summary of significant accounting policies (continued)****Consolidation of subsidiaries**

The consolidated financial statements comprise the consolidated balance sheet of the Bank and its subsidiaries, as at December 31, 2017 and 2016 and the consolidated statements of comprehensive income, changes in equity and cash flows of the Bank and its subsidiaries for the years ended December 31, 2017 and 2016, respectively.

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

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

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

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

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

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

Details of the subsidiaries subject to consolidation are stated below:

Name of subsidiary	Country of incorporation	Effective shareholding by the Bank (%)	
		December 31, 2017	December 31, 2016
"Körfez Gayrimenkul İnş. Taah. Tur. San. Tic. A.Ş."	Turkey	91.89%	97.61%
"Körfez Tatil Beldesi San.ve Tic. A.Ş."	Turkey	99.99%	99.99%
"KT Sukuk Varlık Kiralama A.Ş."	Turkey	100%	100%
"KT Kira Sertifikaları Varlık Kiralama A.Ş."	Turkey	100%	100%
"KT Portföy Yönetimi A.Ş."	Turkey	100%	100%
"KT Bank AG."	Germany	100%	100%
"Architech Bilişim Sistemleri ve Pazarlama Tic. A.Ş."	Turkey	100%	100%

Notes to consolidated financial statements for the year ended December 31, 2017
(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)**2. Summary of significant accounting policies (continued)****Foreign currency transactions**

Transactions in foreign currencies are initially recorded at the functional currency rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the income statement as foreign exchange gain/loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. The financial statements of the Bank and its Turkish subsidiaries for the periods before 1 January 2006 were adjusted to compensate for the effect of changes in the general purchasing power of the Turkish Lira based on IAS 29 *Financial Reporting in Hyperinflationary Economies*. Turkish Economy is accepted to come off its highly inflationary status as of 1 January 2006. Based on this consideration, IAS 29 has not been applied in the preparation of the consolidated financial statements since 1 January 2006. Amounts expressed in the measuring unit current at 31 December 2005 were treated as the basis for the carrying amounts after 1 January 2006.

Foreign currency translation rates used by the Bank as of respective year ends are as follows:

Dates	USD / TL	EUR / TL
December 31, 2016	3.52	3.71
December 31, 2017	3.78	4.53

Foreign Subsidiary

As at the reporting date, the assets and liabilities of the Bank's foreign subsidiary are translated into the Bank's presentation currency at the rate of exchange at the balance sheet date, and its income statement is translated at the EUR/TL 4.119 average exchange rate for the year. Exchange differences arising on translation are taken directly to a separate component of comprehensive income.

Property and equipment

Property and equipment are stated at cost (as adjusted for inflation to December 31, 2005), less accumulated depreciation and accumulated impairment in value.

The initial cost of property and equipment comprises its purchase price, including import duties and non-refundable purchase taxes and any directly attributable costs of bringing the assets to its working condition and location for its intended use. Expenditure incurred after the property and equipment has been put into operation, such as repairs and maintenance, are normally charged to income statement in the year that costs are incurred. Expenditure incurred that result in an increase in the future economic benefits expected from the use of property and equipment is capitalized as an additional cost of property and equipment.

Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

Buildings	50 years
Furniture and office equipment	3-7 years
Motor vehicles	4-5 years
Leasehold improvements	Shorter of the lease or useful life

The property and equipment's residual values, useful lives and methods are reviewed, and adjusted if appropriate, at each financial year end.

An item of property and equipment is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognizing the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement in the year the asset is derecognized.

2. Summary of significant accounting policies (continued)

Construction projects

The Group has classified its time sharing houses as construction projects.

These houses are valued at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less estimated costs necessary to make the sale.

Investment property

Property held for long-term rental yields and/or capital appreciation which is not occupied by the Group is classified as investment property.

Investment property comprises land and buildings. Investment properties are stated at cost less any impairment in value. Depreciation for the building is calculated on a straight-line basis over the estimated useful lives of 50 years. Land is not depreciated.

Investment properties are derecognized when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognized in the income statement in the year of retirement or disposal.

Intangible assets

Intangible assets acquired separately from a business are capitalized at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

Intangible assets, excluding development costs, created within the business are not capitalized and expenditure is charged to the income statement in the year in which it is incurred. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortized on a straight-line basis over the best estimate of their useful lives of 3 to 5 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. There are no intangible assets with indefinite useful lives.

Gains or losses arising from derecognizing an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in the income statement when the asset is derecognized.

Impairment of non-financial assets

The carrying values of property and equipment, investment properties, intangible assets and construction projects are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount. The recoverable amount of the asset is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in the income statement. Impairment losses recognized during the period are included in "other expenses" in the income statement.

2. Summary of significant accounting policies (continued)

Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss (including those held for trading); due from financing activities (loans and receivables), held to maturity and available-for-sale financial assets. The Group determines the classification of its financial assets at initial recognition.

All investments are initially recognized at fair value plus in the case of financial assets not at fair value through profit and loss directly attributable incremental acquisition charges associated with the investment.

All regular way purchases and sales of financial assets are recognized on the settlement date. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place. Changes in fair value of assets to be received during the period between the trade date and the settlement date are accounted for in the same way as the acquired assets i.e. for assets carried at cost or amortized cost, change in value is not recognized; for assets classified as trading, the change in value is recognized through profit and loss.

Available-for-sale financial assets

Available-for-sale assets are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in profit sharing rates, exchange rates or equity prices. Available-for-sale financial assets are subsequently carried at fair value, except for equity investments where there is no quoted price in an active market and whose fair value cannot be reliably measured are carried at cost less any impairment. For investments that are actively traded in organized financial markets, fair value is determined by reference to market bid prices at the close of business on the balance sheet date.

Unrealized gains and losses are recognized directly in other comprehensive income under equity. When the security is disposed of or determined to be impaired, the cumulative gain or loss previously recognized in equity is recognized in the income statement.

Profit share earned while holding investment securities is reported as profit share income.

Financial assets at fair value through profit or loss

Financial assets classified as held for trading are included in this category. Trading securities are securities, which were either acquired for generating a profit from short-term fluctuations in price or dealer's margin, or are securities included in a portfolio in which a pattern of short-term profit taking exists. After initial recognition, trading securities are remeasured at fair value based on quoted closing average bid prices. All related realized and unrealized gains or losses are recognized in income.

Held to maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held to maturity when the Group has the positive intention and ability to hold to maturity. After initial measurement held to maturity investments are measured at amortized cost using the effective yield method. Gains or losses are recognized in profit or loss when the investments are derecognized as impaired, as well as through the amortization process.

Due from financing activities, net

Credits originated by the Bank by providing money directly to the borrower or to a sub-participation agent are categorized as "due from financing activities" and are carried at amortized cost using the effective profit rate. The effective profit rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective profit rate, transaction costs, and all other premiums or discounts. Direct third party expenses, such as legal fees, incurred in securing a credit are treated as part of the cost of the transaction and included in the effective profit rate of the instrument.

All credits and advances are recognized when cash is advanced to borrowers.

2. Summary of significant accounting policies (continued)

Precious metal accounts

Gold transactions are accounted under “precious metal account” and valuation is performed with the current ounce of gold prices in the market.

Derivative financial instruments

The Bank enters into transactions with derivative instruments including swaps in the foreign exchange and capital markets. All of these derivative transactions are considered as effective economic hedges under the Group’s risk management policies; however since they do not qualify for hedge accounting under the specific provisions of IAS 39 “Financial Instruments: Recognition and Measurement”, they are treated as derivatives held for trading. Derivative financial instruments are initially recognized in the balance sheet at fair value on the date which a derivative contract is entered into and subsequently are remeasured at their fair value. Gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the income statement, which are recognized in net trading income. The fair value of these derivatives is determined using principally a discounted cash flow analysis. Fair value of forward and swap contracts are determined based on the comparison of the original forward rate calculated by market interest rates of the related currency for the remaining maturity. Each derivative transaction is carried as asset when the fair value is positive and as liability when the fair value is negative.

The Group enters into profit share and cross currency swap transactions in order to hedge the change in fair value of fixed-rate financial instruments. While applying fair value hedge accounting, the changes in fair values of hedging instrument and hedged item are recognised in income statement. If the hedging is effective, the changes in fair value of the hedged item is presented in statement of financial position together with the fixed-rate loan, and in case of fixed-rate financial assets available for sale, such changes are reclassified from shareholders’ equity to income statement.

The Group performs effectiveness test at the beginning of the hedge accounting period and at each reporting period. The effectiveness tests are carried out using the “Dollar off-set model” and the hedge accounting is applied as long as the test results are between the range of 80%-125% of effectiveness. The hedge accounting is discontinued when the hedging instrument expires, is exercised, sold or no longer effective. When discontinuing fair value hedge accounting, the cumulative fair value changes in carrying value of the hedged item arising from the hedged risk are amortised to income statement over the life of the hedged item from that date of the hedge accounting is discontinued.

While discontinuing cash flow hedge accounting, the cumulative gains/losses recognised in shareholders’ equity and presented under hedging reserves are continued to be kept in this account. When the cash flows of hedged item are recognised in income statement, the gain/losses accounted for under shareholders’ equity, are recognised in income statement.

Embedded derivatives

Embedded derivatives are separated from the host contract if the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative and the hybrid instrument is not measured at fair value with changes in fair value recognized in profit or loss.

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported 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.

2. Summary of significant accounting policies (continued)

Derecognition of financial instruments

The Group derecognizes a financial asset (or, where applicable a part of a financial asset or part of a Group of similar financial assets) when:

- the rights to receive cash flows from the asset have expired;
- the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; or
- the Group has transferred their rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Group's continuing involvement in the asset.

The Group derecognizes a financial liability when the obligation under the liability is discharged or cancelled or expires.

When an existing liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and recognition of a new liability, and the difference in the respective carrying amounts is recognized in the income statement.

Business combinations and goodwill

Business combinations are accounted for using the acquisition method. This involves recognizing identifiable assets (including previously unrecognized intangible assets) and liabilities (including contingent liabilities but excluding future restructuring) of the acquired business at fair value. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognized as goodwill. If the cost of acquisition is less than the fair values of the identifiable net assets acquired, the discount on acquisition is recognized directly in the income statement in the year of acquisition. Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the business combination over the bank's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired.

In business combinations from 1 January 2010, if the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquire is remeasured to fair value at the acquisition date through profit or loss. Furthermore any acquisition costs incurred are expensed.

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually, or more frequently, if events or changes in circumstances indicate that the carrying value may be impaired. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the bank's cash-generating units (CGUs) or group of CGUs, which are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquire are assigned to those units.

Where goodwill forms part of a CGU (or group of CGUs) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the CGU retained.

2. Summary of significant accounting policies (continued)

Cash and cash equivalents

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise cash and balances with central banks (excluding obligatory reserve deposits), deposits with banks and other financial institutions and other money market placements with an original maturity of three months or less.

Impairment of financial assets

a) *Assets carried at amortized cost*

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Group about the following loss events:

- (a) significant financial difficulty of the issuer or obligor;
- (b) a breach of contract, such as a default or delinquency in interest or principal payments by more than 90 days;
- (c) the Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;
- (d) it becomes probable that the borrower will enter bankruptcy or other financial reorganization;
- (e) the disappearance of an active market for that financial asset because of financial difficulties; or
- (f) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the Bank, including:
 - (i) adverse changes in the payment status of borrowers; or
 - (ii) national or local economic conditions that correlate with defaults on the assets of the Group.

If there is objective evidence that an impairment loss on credits and receivables, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through the use of an allowance account. The amount of the loss is recognized in the income statement. The calculation of the present value of the estimated future cash flows includes the realization of collateral when appropriate.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment.

Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account. Any subsequent reversal of impairment loss is recognized in the income statement, to the extent that the carrying value of the asset does not exceed its amortized cost at the reversal date.

Notes to consolidated financial statements for the year ended December 31, 2017
(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)

2. Summary of significant accounting policies (continued)

Impairment of financial assets (continued)

a) *Assets carried at amortized cost (continued)*

A write off is made when all or part of a credit is deemed uncollectible or in the case of debt forgiveness. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Write offs are charged against previously established allowances and reduce the principal amount of a credit. Subsequent recoveries of amounts previously written off are included in “other income” in the income statement.

The Bank’s accounting treatment for the allowance for credit losses depends on the source of the credit itself. Allowance for the losses in credit that are entirely financed by the Bank’s equity or by current and saving accounts (self-financed credit) are reflected wholly in the income statement as a provision expense. The allowance for the credit in arrears that are funded by the corresponding profit or loss investment accounts (jointly financed credit) is reflected in the income statement as a provision expense to the extent the Bank has participated in the profit or loss which may arise from the fund utilized. The remaining portion of the allowance for such credit is reflected ultimately in the profit or loss sharing investor accounts as a loss.

If there is objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on equity instruments are not reversed.

b) *Available-for-sale financial assets carried at fair value*

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognized in profit or loss, is transferred from equity to the income statement. Reversals of impairment regarding equity instruments classified as available-for-sale are not recognized in the income statement. Reversals of impairment losses on debt instruments are reversed through the income statement; if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognized in the income statement.

c) *Renegotiated financing and leasing receivables*

Where possible, the Bank seeks to restructure financing and leasing receivables rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new conditions. Profit share income continues to be accrued at the original effective or the current profit rates at the renegotiation dates. The Bank does not offer a deduction in the loan amount to its customers. The financing and leasing receivables continue to be subject to an individual or collective impairment assessment calculated using the original effective yield.

Current accounts and profit / loss sharing investors’ accounts

Current accounts and profit/loss sharing investors’ accounts are initially recognized at cost, being the fair value. Current accounts are not entitled to profit participation. After initial recognition, all profit / loss sharing accounts are recognized at cost plus attributable profit (or less attributable loss) on credits granted taking into consideration amounts repaid and losses attributable. Profit or losses attributable to profit/loss sharing investors’ accounts that result from financing transactions are distributed among such accounts according to each party’s contribution to the financing investment.

2. Summary of significant accounting policies (continued)

Due to other financial institutions and banks

Deposits and funds borrowed are initially recognized at fair value of consideration received less directly attributable transaction costs. After initial recognition, all profit bearing liabilities are subsequently measured at amortized cost using the effective yield method. Amortized cost is calculated by taking into account any discount or premium.

Net Investment Hedge

The Group enters into foreign currency risk arising from net investments in foreign affiliates are hedged with long-term foreign currency borrowings&deposits and the currency translation differences arising from the conversion of net investments in foreign affiliates and accounts long-term foreign currency borrowings into TL for other profit reserves and hedging reserves, respectively in equity.

Employee benefits

The Group has both defined benefit and defined contribution plans as described below:

(a) Defined benefit plans:

In accordance with existing social legislation in Turkey, the Group is required to make lump-sum termination indemnities to each employee who has completed over one year of service with the Group and whose employment is terminated due to retirement or for reasons other than resignation or misconduct. Such defined benefit plan is unfunded. The cost of providing benefits under the defined benefit plan is determined using the actuarial valuation by independent actuary. All actuarial gains and losses are recognized in the comprehensive income statement.

(b) Defined contribution plans:

For defined contribution plans the Group pays contributions to publicly administered Social Security Funds on a mandatory basis. The Group has no further payment obligations once the contributions have been paid. The contributions are recognized as employee benefit expense when they are due.

Provisions

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The expense relating to any provision is presented in the income statement net of any reimbursement. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as an expense.

Leases

The group as lessee

Operating leases

Leases where the lessor retains substantially all the risks and benefits of ownership of the assets are classified as operating leases. Operating lease payments are recognized as an expense in the income statement on a straight-line basis over the lease term.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognized as an expense in the period in which termination takes place.

2. Summary of significant accounting policies (continued)

Finance lease

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased items, are capitalized at the inception of the lease at the fair value of the leased property, or if lower, at the present value of the minimum lease payments. Lease payments are apportioned between finance charges and reduction of the lease liability so as to achieve a constant periodic rate of return on the remaining balance of the liability. Finance charges are reflected in the income statement.

The group as lessor

Finance lease

Under finance leases the Group transfers substantially all risks and benefits incidental to ownership of the leased item. The Group presents finance leased assets as a receivable equal to the net investment in the lease. Finance income is based on a pattern reflecting a constant periodic rate of return on the net investment outstanding. Initial direct costs are included in the initial measurement of the finance lease receivable and reduce the amount of income recognized over the lease term.

Income and expense recognition

Fees and commissions are recognized based on the purposes for which such fees and commissions are collected and the basis of accounting for any associated financial instrument. Commissions and fees that are collected as an integral part of the profit share rate of loans are treated as an adjustment to the profit share rate. Commissions and fees on loans that are collected as reimbursement of expenses incurred and are not considered as an adjustment to the profit share rate and commission income from various banking services are recognized as income when collected. Fees (such as credit card fees) that are related to servicing a loan are recognized on a straight-line basis over the period of the service is provided.

Income from funds invested from current accounts and equity is recognized on an accrual basis. Income from funds invested from profit/loss sharing accounts is accrued using the effective yield method and the net income is attributed to profit/loss sharing accounts. Accrued income from funds invested from profit/loss sharing accounts is recognized in full and generally 66% - 99% of this income is recorded as expense being the profit share distribution (as this is the legal and contractual range for the profit share quotas).

Dividend income is recognized when the Group's right to receive the payment is established.

Income earned on available-for-sale equity investments, which are carried at cost less any impairment is reported as dividend income.

Income from the sale of time sharing houses is recognized when the significant risks and rewards of ownership of the asset have passed to the buyer.

2. Summary of significant accounting policies (continued)

Income tax

Tax expense / (income) is the aggregate amount included in the determination of net profit or loss for the period in respect of current and deferred tax.

Current tax and deferred tax relating to items recognized directly in equity are also recognized in equity and not in the income statement.

Current tax

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date.

Deferred tax

Deferred tax is provided on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognized for all taxable temporary differences except:

- where the deferred tax liability arises from the initial recognition of goodwill of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investment in subsidiary and associates, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry forward of unused tax credits and unused tax losses can be utilized except:

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of goodwill of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investment in subsidiary and associates, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

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

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

2. Summary of significant accounting policies (continued)

The Group calculates and accounts for deferred income taxes for temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in these financial statements in accordance with “Turkish Accounting Standard for Income Taxes” (“TAS 12”). Deferred tax asset is calculated on all temporary differences other than general provisions to the extent that is probable that taxable profit will be available and deferred tax liability is calculated for all temporary differences. Deferred tax asset and liabilities are shown in the accompanying financial statements on a net basis. The tax rate used in the calculation of deferred tax assets and liabilities is 22% over the temporary timing differences expected to reverse in 2018, 2019 and 2020, and 20% over the temporary timing differences expected to reverse after 2021 (2016: 20%).

Fiduciary assets

Assets held by the Bank in a fiduciary, agency or custodian capacity are not included in the balance sheet, since such items are not treated as assets of the Bank.

Related parties

For the purposes of these financial statements, shareholders, key management personnel and Board of Directors’ Members, in each case together with companies controlled by/or affiliated with them and their close family members, associated companies are considered and referred to as related parties.

A related party is a person or entity that is related to the entity that is preparing its financial statements (in this Standard referred to as the ‘reporting entity’).

- (a) A person or a close member of that person's family is related to a reporting entity if that person:
 - (i) has control or joint control over the reporting entity;
 - (ii) has significant influence over the reporting entity; or
 - (iii) is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.
- (b) An entity is related to a reporting entity if any of the following conditions applies:
 - (i) The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
 - (ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
 - (iii) Both entities are joint ventures of the same third party.
 - (iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
 - (v) The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity.
 - (vi) The entity is controlled or jointly controlled by a person identified in (a).
 - (vii) A person identified in (a) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

A related party transaction is a transfer of resources, services or obligations between a reporting entity and a related party, regardless of whether a price is charged.

Dividends

Dividends on ordinary shares are recognized as a liability in the period in which they are approved by the Annual General Meeting of the Shareholders of the Bank and its subsidiaries.

Subsequent events

Post year-end events that provide additional information about the Group’s position at the balance sheet date (adjusting events), are reflected in the financial statements. Post-year-end events that are not adjusting events are disclosed in the notes when material.

2. Summary of significant accounting policies (continued)

Reclassifications

None.

3. Segment reporting

For management purposes, the Group is organized into six business segments:

Retail Banking – Principally handling individual customers’ current, saving and investment accounts and providing loans, consumer loans, credit cards facilities and funds transfer facilities. Segment portfolio comprised of all Turkish individuals that have deposits under TL 1.25 million and loans that are less than TL 750,000 (full amount) and all foreign nationals’ loans that are less than TL 500,000 (full amount).

Private Banking – Principally handling individual customers’ current, saving and investment accounts and providing loans, consumer loans, credit cards facilities and funds transfer facilities. Segment portfolio comprised of all Turkish individuals that have deposits more than TL 1.25 million and loans that are more than TL 750,000 (full amount) and all foreign nationals’ loans that are more than TL 500,000 (full amount).

Small Business Banking – Principally handling loans and other credit facilities and current, saving and investment accounts for institutional customers. Segment portfolio comprised of all businesses that have annual sales turnover between TL 3 million - TL 30 million and their individual owners.

Commercial Banking – Principally handling loans and other credit facilities and current, saving and investment accounts for institutional customers. Segment portfolio comprised of all businesses that have annual sales turnover more than TL 30 million and their individual owners except customer of corporate branches.

Corporate Banking – Principally handling loans and other credit facilities and current, saving and investment accounts for all corporate customers. Segment portfolio comprised of all businesses in corporate branches.

Kuveyt Türk Katılım Bankası Anonim Şirketi and its Subsidiaries

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3. Segment reporting

The following table presents income and profit and certain asset and liability information regarding the Group's business segments as of and for the years ended December 31, 2017 and 2016, respectively.

For the period ended December 31, 2017	Treasury, International & Investment Banking						Recon- ciliation	Notes	Grand Total
	Retail Banking	SME Banking	Commercial Banking	Corporate Banking	Banking	Segments Total			
Income from financing activities & sukuk	551,941	1,272,073	1,245,911	255,467	388,557	3,713,950	-	-	3,713,950
Intersegment income	1,207,721	(271,494)	(667,805)	(111,496)	(156,925)	-	-	-	-
Total financing income	1,759,662	1,000,579	578,106	143,971	231,633	3,713,950	-	-	3,713,950
Profit shares distributed	(951,721)	(217,028)	(64,194)	(25,534)	(548,956)	(1,807,432)	48,097	(a, b)	(1,759,335)
Credit loss expense	(22,226)	(208,920)	(411,609)	(113,890)	-	(756,644)	-	-	(756,644)
Net financing income	785,715	574,631	102,303	4,547	317,323	1,149,873	48,097		1,197,971
Foreign exchange gain/loss, net	59,173	50,519	35,362	35,969	(1,177)	179,845	-	(b)	179,845
Net trading income	-	-	-	-	206,736	206,736	-	-	206,736
Net fees & commission and other income	100,301	182,554	133,848	112,922	6,696	536,320	-	(b)	536,320
Other expenses / income (net)	(454,176)	(396,388)	(200,825)	(82,290)	(35,271)	(1,168,951)	(48,097)	(a, b)	(1,217,048)
Segment profit / (loss)	491,012	411,316	70,688	71,148	(140,340)	903,824	-	-	903,824
Tax expenses	-	-	-	-	-	-	(187,996)	(c)	(187,996)
Net profit / (loss) for the year	491,012	411,316	70,688	71,148	140,340	903,824	(187,996)		715,828
Segment Assets	6,363,331	13,791,453	15,709,386	2,853,694	18,602,262	57,320,126	-	-	57,320,126
Segment Liabilities & Equity	26,330,482	10,022,121	3,201,756	1,625,043	11,211,671	52,391,073	4,929,053	(d)	57,320,126

a) The difference resulted from the insurance fund premium expenses which included in this line in the performance reports but in the financials it is included in other expenses and classification to foreign exchange gain/loss in the performance reports.

b) In the performance reports some of the income and expense items related to precious metal, fx trading, fees and other incomes and other expenses treated in different ways than they are reported in the financials. So there are crossings in these income and expense items.

c) Since the tax is calculated on bank's total profit loss the tax amount is not included in the performance of segments.

d) Total equity is not allocated to the segments.

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3. Segment reporting (continued)

For the period ended December 31, 2016	Treasury, International & Investment Banking						Recon- ciliation	Notes	Grand Total
	Retail Banking	SME Banking	Commercial Banking	Corporate Banking	Segments Total	Segments Total			
Income from financing activities & sukuk	477,002	1,093,675	608,130	421,711	371,186	2,971,704	-	-	2,971,704
Intersegment income	845,028	(409,363)	(363,542)	(281,137)	209,014	-	-	-	-
Total financing income	1,322,030	684,312	244,588	140,574	580,200	2,971,704	-	-	2,971,704
Profit shares distributed	(719,165)	(159,483)	(32,186)	(24,038)	(566,574)	(1,501,446)	3,285	(a, b)	(1,498,161)
Credit loss expense	(20,010)	(200,616)	(284,810)	(75,138)	-	(580,574)	5,782	-	(574,792)
Net financing income	582,854	324,213	(72,408)	41,398	13,626	889,684	9,067	-	898,751
Foreign exchange gain/loss, net	37,833	51,896	23,541	15,206	992	129,468	66,747	(b)	196,215
Net trading income	-	-	-	-	162,970	162,970	-	-	162,970
Net fees & commission and other income	145,843	199,517	79,641	102,789	1,636	529,426	(575)	(b)	528,851
Other expenses / income (net)	(382,514)	(351,822)	(206,998)	(75,585)	(40,637)	(1,057,556)	(33,270)	(a, b)	(1,090,826)
Segment profit / (loss)	384,017	223,804	(176,224)	83,808	138,587	653,992	41,969	-	695,961
Tax expenses	-	-	-	-	-	-	(131,237)	(c)	(131,237)
Net profit / (loss) for the year	384,017	223,804	(176,224)	83,808	138,587	653,992	(89,268)	-	564,724
Segment Assets	6,452,954	12,097,769	8,201,624	5,445,802	16,229,827	48,427,976	-	-	48,427,976
Segment Liabilities & Equity	20,927,595	8,170,790	2,097,615	2,212,034	10,779,571	44,187,604	4,240,372	(d)	48,427,976

a) The difference resulted from the insurance fund premium expenses which included in this line in the performance reports but in the financials it is included in other expenses and classification to foreign exchange gain (loss) in the performance reports.

b) In the performance reports some of the income and expense items related to precious metal, fx trading, fees and other incomes and other expenses treated in different ways than they are reported in the financials. So there are crossings in these income and expense items.

c) Since the tax is calculated on bank's total profit/loss the tax amount is not included in the performance of segments.

d) Total equity is not allocated to the segments.

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4. Cash and balances with banks

	December 31, 2017	December 31, 2016
Cash on hand	1,602,840	1,615,907
Balances with the Central Bank of Turkey	254,223	259,956
Cash and balances with the Central Bank of Turkey	1,857,063	1,875,863
Balances with banks and other financial institutions	4,951,453	5,979,425
Sub Total	6,808,516	7,855,288
Deposit with maturity more than three months	(211,564)	(119,142)
Less: Interbank gold deposits	(349,923)	(95,591)
Total	6,247,029	7,640,555

As of December 31, 2017 and 2016, “balances with other banks and financial institutions” are made up of demand and time deposits. The time deposits, all of which have original maturities less than three months, can be analyzed as follows:

	2017					2016		
	Amount		Effective profit rate			Amount		Effective profit rate
	TL	Foreign currency	TL	Foreign currency	TL	Foreign currency	TL	Foreign currency
Deposits with other banks and financial institutions	-	1,269,080	-	0.49%	-	1,383,293	-	0.71%
Total		1,269,080				1,383,293		

5. Reserve deposits at the Central Bank of Turkey

	2017		2016	
	Foreign currency (full)	TL	Foreign currency (full)	TL
USD	1,146,176,997	4,330,165	1,115,882,587	3,927,014
EUR	110,396,631	499,696	100,000,000	370,990
XAU (Standard Gold)	10,137,961	1,644,573	10,499,864	1,380,247
		6,474,434		5,678,251

In accordance with the “Communiqué Regarding the Reserve Requirements no. 2013/15, the Bank is required to maintain reserves in CBRT for TL and foreign currency liabilities. The reserve requirements can be maintained as TL, USD, EUR and standard gold. CBRT started paying profit share on reserve balances held in USD starting from May 2015 and held in TL starting from November 2014. The reserve rates for TL liabilities vary between 4% and 10.5% for TL deposits and other liabilities according to their maturities as of 31 December 2017 (31 December 2016: 4% and 10.5% for all TL liabilities). The reserve rates for foreign currency liabilities vary between 4% and 24% for deposit and other foreign currency liabilities according to their maturities as of 31 December 2017 (31 December 2016: 4% and 24% for all foreign currency liabilities).

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6. Financial assets

Available-for-sale

	2017	2016
Financial Sukuk	4,254,312	3,653,310
Unlisted Shares	17,084	16,594
Fund	157,276	81,776
Total available-for-sale financial assets	4,428,672	3,751,680

The breakdown of unlisted shares is as follows:

			2017		2016
	Nature of business	Ownership%	Amount	Ownership%	Amount
Kredi Garanti Fonu A.Ş. (KGF)	Financial institution	1.69	4,719	1.69	4,719
Neova Sigorta A.Ş.	Insurance company	6.99	5,201	6.99	5,201
Borsa İstanbul A.Ş.	Exchange entity	0.0035	15	0.0035	15
VISA INC.	Financial service	-	7,149	-	6,659
			17,084		16,594

The fair value of the above listed available-for-sale investments can not be reliably estimated. There is no market price for these investments.

Information on financial assets available-for-sale:

The details of the Rent Certificates which are in Bank's Portfolio "Financial Assets Available for-Sale" are presented below as of 31 December 2017.

- a) In addition; the Bank included rent certificates which are presented below and these amounts are classified under "Government debt securities" at the accompanying financial statements.

REFERENCE	CURRENCY	COUPON FREQUENCY	ISSUER	PURCHASE DATE	MATURITY DATE	COST VALUE	RATE (%)
TRD140721T18	TL	Semi-annually	T.C. HAZİNE	20/07/2016	14/07/2021	3.176	9.40
TRD140218T18	TL	Semi-annually	T.C. HAZİNE	17/02/2016	14/02/2018	21.435	10.64
TRD220921T16	TL	Semi-annually	T.C. HAZİNE	28/09/2016	22/09/2021	176.340	2.24
TRD260918T17	TL	Semi-annually	T.C. HAZİNE	28/09/2016	26/09/2018	17.317	8.80
TRD211118T18	TL	Semi-annually	T.C. HAZİNE	23/11/2016	21/11/2018	980	2.80
TRD130219T18	TL	Semi-annually	T.C. HAZİNE	15/02/2017	13/02/2019	22.391	11.04
TRD190619T18	TL	Semi-annually	T.C. HAZİNE	21/06/2017	19/06/2019	172.675	10.72
TRD100822T10	TL	Semi-annually	T.C. HAZİNE	16/08/2017	10/08/2022	24.540	10.76
TRD121022T14	TL	Semi-annually	T.C. HAZİNE	18/10/2017	12/10/2022	97.180	2.80
XS0831353361	USD	Semi-annually	REPUBLIC OF TURKEY	26/09/2012	26/03/2018	61.633	2.80
XS1586385178	USD	Semi-annually	REPUBLIC OF TURKEY	06/04/2017	06/04/2023	9.651	5.00
XS1141043296	USD	Semi-annually	REPUBLIC OF TURKEY	25/11/2014	25/11/2024	31.610	4.48
XS0975124180	USD	Semi-annually	REPUBLIC OF TURKEY	26/04/2016	10/10/2018	41.174	4.56
XS1303467077	USD	Semi-annually	REPUBLIC OF TURKEY	08/06/2016	08/06/2021	42.342	4.26

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6. Financial assets (continued)

Available-for-sale (continued)

Information on financial assets available-for-sale (continued)

- b) The Bank purchased the rent certificates (“sukuk”) as details given table below from private entities that are stated under “Other Securities” in given financial statements.

REFERENCE	CURRENCY	COUPON FREQUENCY	ISSUER	PURCHASE DATE	MATURITY DATE	COST VALUE	RATE (%)
TRDKTVK31810	TL	Quarterly	KT KİRA SERTİFİKALARI V.K.Ş.	22/11/2017	16/03/2018	2,580	16.16
TRDKTVK31828	TL	Quarterly	KT KİRA SERTİFİKALARI V.K.Ş.	19/12/2017	16/03/2018	6,570	11.64
TRDKTVK11812	TL	Quarterly	KT KİRA SERTİFİKALARI V.K.Ş.	19/09/2017	03/01/2018	20,101	13.92
TRDKTVK11820	TL	Quarterly	KT KİRA SERTİFİKALARI V.K.Ş.	06/10/2007	17/01/2018	51	13.64
TRDKTVK21811	TL	Quarterly	KT KİRA SERTİFİKALARI V.K.Ş.	22/11/2017	06/02/2018	324	11.92
XS1505149325	USD	Semi-annually	KT KİRA SERTİFİKALARI V.K.Ş.	21/12/2017	02/11/2021	7,780	5.14
US71567RAD89	USD	Semi-annually	REPUBLIC OF INDONESIA	12/10/2017	28/05/2025	3,950	4.32
XS1082151868	USD	Semi-annually	ALBARAKA TURK	30/06/2014	30/06/2019	16,623	6.26
XS0922143382	USD	Semi-annually	TÜRKİYE FİNANS K.B.A.Ş.	02/05/2013	02/05/2018	126,255	3.96
XS1057852912	USD	Semi-annually	TÜRKİYE FİNANS K.B.A.Ş.	24/04/2014	24/04/2019	27,654	3.96
XS1241110300	USD	Semi-annually	DİB	03/06/2015	03/06/2020	7,563	0.58
XS1696457289	USD	Quarterly	IILM	10/10/2017	23/01/2018	56,669	1.88

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6. Financial assets (continued)

Held for trading

Financial assets held for trading includes sukuk and share certificates. Balance of Financial assets held for trading is as below:

	2017	2016
Sukuk	61,535	56,323
Share Certificates	390	390
	61,925	56,713

The movement in financial assets excluding derivatives may be summarized as follows:

Financial investments	Current Period		Previous Period	
	Available for sale	Held for trading	Available for sale	Held for trading
At the beginning of the year	3,751,680	56,713	2,354,196	45,214
Additions	4,893,546	2,067,181	2,565,115	57,448
Disposals (sale and redemption)	(4,226,156)	(2,058,210)	(1,155,714)	(44,514)
Change in fair value	9,602	(3,759)	(11,917)	(1,435)
Balance at the end of the year	4,428,672	61,925	3,751,680	56,713

Kuveyt Türk Katılım Bankası Anonim Şirketi and its Subsidiaries

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6. Financial assets (continued)

Hierarchy of valuation techniques which establishes basis for fair value calculation of financial assets and liabilities

Level I: Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level II: Inputs other than quoted prices included within Level I that are observable for the asset or liability, either directly or indirectly

Level III: Inputs for the asset or liability that are not based on observable market data

Fair value hierarchy of the financial assets and liabilities of the Bank carried at fair value according to the foregoing principles as of December 31, 2017 are given in the table below:

Current Period	Level 1	Level 2	Level 3	Total
Financial assets				
Financial assets held for trading	61,535	26,699	-	88,234
Forward transactions	-	16,467	-	16,467
Swap transactions	-	10,232	-	10,232
Sukuk held for trading	61,535	-	-	61,535
Available-for-sale financial assets	4,254,312	-	-	4,254,312
Equity securities	-	-	-	-
Government debt securities	3,984,982	-	-	3,984,982
Other marketable securities	269,330	-	-	269,330
Financial liabilities				
Financial liabilities held for trading	-	151,493	-	151,493
Forward transactions	-	16,467	-	16,467
Swap transactions	-	135,026	-	135,026
Previous Period	Level 1	Level 2	Level 3	Total
Financial assets				
Financial assets held for trading	56,323	110,049	-	166,372
Forward transactions	-	22,304	-	22,304
Swap transactions	-	87,745	-	87,745
Sukuk held for trading	56,323	-	-	56,323
Available-for-sale financial assets	3,653,310	-	-	3,653,310
Equity securities	-	-	-	-
Government debt securities	2,944,445	-	-	2,944,445
Other marketable securities	708,865	-	-	708,865
Financial liabilities				
Financial liabilities held for trading	-	257,556	-	257,556
Forward transactions	-	16,753	-	16,753
Swap transactions	-	240,803	-	240,803

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7. Due from financing activities, net

December 31, 2017	Corporate and Commercial	Consumer	Credit Cards	Mortgage	Total
Neither past due nor impaired	28,676,433	767,981	554,904	5,735,566	35,734,884
Past due not impaired	991,559	30,230	7,016	165,383	1,194,188
Impaired	784,330	10,409	5,906	17,338	817,983
Total gross loans	30,452,322	808,620	567,826	5,918,287	37,747,055
Less: Allowance for impairment on loans	(766,954)	(11,966)	(6,859)	(33,871)	(819,650)
Net loans (*)	29,685,368	796,654	560,967	5,884,416	36,927,405

December 31, 2016	Corporate and Commercial	Consumer	Credit Cards	Mortgage	Total
Neither past due nor impaired	21,405,083	572,106	319,624	4,705,722	27,002,535
Past due not impaired	1,373,487	12,331	8,198	144,022	1,538,038
Impaired	758,831	11,440	13,144	16,292	799,707
Total gross loans	23,537,401	595,877	340,966	4,866,036	29,340,280
Less: Allowance for impairment on loans	(665,472)	(11,463)	(14,613)	(15,219)	(706,767)
Net loans (*)	22,871,929	584,414	326,353	4,850,817	28,633,513

(*) Also includes minimum finance lease payment receivables.

	2017	2016
Performing		
Funds invested from profit/loss sharing accounts	17,562,109	12,599,038
Funds invested from current accounts and equity	16,103,803	12,903,729
Income accruals on due from financing activities (*)	1,333,917	1,493,263
	34,999,829	26,996,030
Funds in arrears		
Funds invested from profit / loss sharing accounts	305,616	386,043
Funds invested from current accounts and equity	507,327	400,444
	812,943	786,487
Total	35,812,772	27,782,517
Impairment allowance		
Funds invested from profit / loss sharing accounts	288,504	268,886
Funds invested from current accounts and equity	526,726	425,755
	815,230	694,641
Total due from financing activities	34,997,542	27,087,876

(*) Also includes foreign currency evaluation differences of foreign currency indexed loans.

Notes to consolidated financial statements for the year ended December 31, 2017
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7. Due from financing activities, net (continued)

Movement in impairment allowance for funds disbursed is as follows:

	December 31, 2017	December 31, 2016
Balance at January 1,	694,641	390,279
Charge for the period	698,630	683,792
Charges for the bank	490,145	529,210
Charge for the participation accounts	208,485	154,582
Recoveries of amounts previously provided for	(116,688)	(230,037)
Reserves written off in current year	(461,353)	(149,393)
Balance at the end of the year	815,230	694,641

The impairment allowance of TL 815,230 (December 31, 2016 – TL 694,641) is made up of a specific and collective allowance. The movements in the collective and specific allowances are analyzed below.

The movements in the collective allowance for financing activities are as follows:

	2017	2016
Balance at beginning of year	162,924	111,456
Provisions - bank	65,033	32,839
Provisions - participation accounts	55,647	18,629
Allowance at the end of the year	283,604	162,924

The movement in specific allowance is as follows:

	2017	2016
Balance at the beginning of the year	531,717	278,823
Provisions - bank	425,112	496,371
Provisions - participation accounts	152,838	135,953
Recoveries of amounts previously provided for	(116,688)	(230,037)
Reserves written off in current year	(461,353)	(149,393)
Balance at the end of the year	531,626	531,717

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8. Minimum finance lease payments receivable, net

Minimum finance lease payments receivable (net) is as follows:

	2017	2016
Gross investment in finance leases	2,244,253	1,745,190
Unearned finance income	(315,010)	(200,647)
Total impaired receivables	5,040	13,220
Impairment allowance	(4,420)	(12,126)
Minimum lease payments receivable, net	1,929,863	1,545,637

Movements in the impairment allowance for leasing receivables is as follows:

	2017	2016
Balance at January 1	12,126	2,940
Charge for the period	16,237	11,951
Charges for the bank	15,654	11,400
Charge for the participation accounts	583	551
Recoveries of amounts previously provided for	(11,007)	(1,296)
Impairment allowance written off in current period	(12,936)	(1,469)
Balance at the end of the period	4,420	12,126

Gross investment in finance leases as to their maturity:

	2017	2016
Not later than 1 year	1,499,972	1,119,851
Later than 1 year and not later than 5 years	565,336	493,529
Later than 5 years	178,945	131,810
Non-performing receivables	5,040	13,220
Minimum lease payments receivable, gross	2,249,293	1,758,410
Less : Unearned finance income	(315,010)	(200,647)
Net investment in finance leases	1,934,283	1,557,763
Less : Allowance for impairment	(4,420)	(12,126)
Minimum lease payments receivable, net	1,929,863	1,545,637

As of December 31, 2017 TL 1,343,269 (December 31, 2016 - TL 1,188,060) gross lease receivables are denominated in foreign currency (USD and EUR).

Net investment in finance leases as to their maturity:

	2017	2016
Less than 1 year (*)	1,223,929	958,746
1 - 5 year	537,865	475,036
More than 5 years	172,489	123,981
Net investment in finance leases	1,934,283	1,557,763

(*) Includes total impaired receivables amounting to TL 5,040 (December 31, 2016 – TL 13,220).

Material finance leasing arrangements of the Group includes several machinery and equipment with a contractual maturity of 4 to 5 years.

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9. Other assets

Other assets comprise the following:

	2017	2016
Clearing accounts	99,553	192,677
Prepaid expenses	61,076	42,055
Blockage for letter of guarantee	571,787	420,596
Receivables from banking operations	8,081	7,623
Value added tax (VAT) receivable	23,437	725
Other receivables from finance activities	153,758	4,762
Other	20,369	32,049
	938,061	700,487

(*) KT Sukuk Varlık Kiralama A.Ş. has issued a lease certificate (TRDKTSK61912 ISIN code) on behalf of Derindere Turizm Otomotiv San. Tic. A.Ş., with a nominal value amounting to TL 50,000,000, with a term of 728-days, with interim profit share payments in every 3 months, with an annual return of 14.8335% and with a periodic return of 3.6982% and a lease certificate (TRDKTSK21617 ISIN code) on behalf of Toprak Mahsulleri Ofisi A.Ş. (TMO), with a nominal value amounting to TL 100,000,000, with a term of 88-days, with an annual return of 12.95%, with a periodic return of 3.12219% and with the principal and coupon payment due on 23 February 2018.

10. Construction projects, net

Construction projects mainly include the Dumankaya Project (time sharing houses) which belong to the subsidiary of the Bank, Körfez GYO.

	2017	2016
Uncompleted construction projects	27,612	21,499
Kartal Project		
Cost of land	-	19,886
Cost of project	25,999	-
Kilyos Land		
Cost of land	1,613	1,613
Güre Tesisi	79,664	56,440
Completed construction projects (inventories)	79,664	56,440
	107,276	77,939
(Less) Impairment provision for net realizable value	(31,042)	-
Total construction projects, net	76,234	77,939

11. Investment properties, net

	2017	2016
Balance at the beginning of the year	26,129	33,807
Additions	30,947	858
Disposal	(8,829)	(7,471)
Depreciation charge	(158)	(1,014)
Transfer from assets held for resale (Note 12)	36,903	-
Reversal / (charge) of provisions for investment property	-	(51)
Balance at the end of the year	84,992	26,129
Cost	88,548	29,464
Accumulated depreciation	(3,502)	(2,809)
Accumulated impairment	(54)	(526)
Net carrying amount	84,992	26,129

Fair value of the investment properties is TL 118,849 (December 31, 2016 - TL 46,093) which is determined based on the valuations performed by independent qualified values on December 2017.

In the current economic conditions, some of the assets held for sale could not be sold during the year and were transferred to investment property. As the assets classified to investment property are lands, they are not subject to depreciation and such transfer does not have an effect on the current and prior year results.

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12. Assets and a disposal group held for sale

At December 31, 2017, the Bank classified non-current assets; mainly land and buildings; being collateral repossessed in this period amounting to TL 60,874 (December 31, 2016 – TL 15,535), which are expected to be sold in a time period less than 1 year as non-current assets held for sale. The assets and the determined sales prices have been announced to the public via website of the Bank. Movement of non-current assets held for sale is as follows:

	2017	2016
Balance at the beginning of the year	42,667	27,332
Additions	60,874	15,335
Transfer to investment property (Note 11)	(36,903)	-
Disposals	(13,439)	-
Balance at the end of the year	53,199	42,667

Gain on sale of assets held for sale amounting to TL 27,776 is included in other income in the comprehensive income statement (December 31, 2016 – TL 5,380).

13. Property and equipment, net

	Land and buildings	Furniture and office equipment (*)	Leasehold improvements	Motor vehicles	Total
At January 1, 2016	235,640	147,914	46,615	259	430,428
Cost					
Additions (*)	571	43,226	13,279	50	57,126
Disposals	(325)	(4,729)	(1,200)	(120)	(6,374)
Depreciation charge for the year	(6,590)	(36,730)	(10,962)	(31)	(54,313)
At December 31, 2016, net of accumulated depreciation and impairment	229,296	149,681	47,732	158	426,867
Additions (*)	1,466	70,613	22,122	1,100	95,301
Disposals	(25,370)	(7,677)	(11,261)	(50)	(44,358)
Depreciation charge for the year	(6,614)	(29,769)	(11,075)	(175)	(47,633)
At December 31, 2017, net of accumulated depreciation and impairment	198,778	182,848	47,518	1,033	430,177

(*) TL 7,957 and TL 7,694 of furniture and office equipment consist of assets obtained through financial leasing as of December 31, 2017 and 2016, respectively. There is no property and equipment that are pledged for borrowings.

	Land and Buildings	Furniture and office equipment	Leasehold improvements	Motor vehicles	Total
At December 31, 2016					
Cost	254,048	274,768	88,189	795	617,800
Accumulated depreciation	(24,752)	(125,087)	(40,457)	(637)	(190,933)
Net carrying amount	229,296	149,681	47,732	158	426,867
At December 31, 2017					
Cost	231,353	339,572	87,996	1,821	660,742
Accumulated depreciation	(32,575)	(156,724)	(40,478)	(788)	(230,565)
Net carrying amount	198,778	182,848	47,518	1,033	430,177

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14. Intangible assets, net

	Internally Generated Software	Other Software	Total
At January 1, 2016	82,114	37,338	119,452
Additions	47,704	8,559	56,263
Disposals	(8,414)	-	(8,414)
Amortization charge for the year	(16,795)	(10,039)	(26,834)
At December 31, 2016, net of accumulated amortization	104,608	35,859	140,467
Additions	52,569	18,535	71,104
Disposals	(16,715)	-	(16,715)
Amortization charge for the year	(11,298)	(13,756)	(25,054)
At December 31, 2017, net of accumulated amortization	129,165	40,637	169,802
At December 31, 2016			
Cost (gross carrying amount)	127,084	72,337	199,421
Accumulated amortization	(22,476)	(36,478)	(58,954)
Net carrying amount	104,608	35,859	140,467
At December 31, 2017			
Cost (gross carrying amount)	201,398	80,360	281,758
Accumulated amortization	(72,233)	(39,723)	(111,956)
Net carrying amount	129,165	40,637	169,802

15. Due to other financial institutions and banks, Sukuk securities issued and subordinated loans

Due to other financial institutions and banks as of December 31, 2017 and 2016 is as follows;

Original currency	Amount in TL	
	2017	2016
USD	2,959,839	3,118,503
Euro	215,713	95,477
TL	109,974	59,346
Other	101,601	-
Total	3,387,127	3,273,326

As of December 31, 2017 borrowings remaining maturities of which is less than 12 months amount to TL 3,163,905 (As of December 31, 2016 – TL 3,116,471).

As of 31.12.2017 Bank has no syndicated loans. As of 31.12.2016 the Bank had a syndicated loan, with a maturity of 31.03.2017 amounting to USD 200 million with a profit share rate of 5.50% paid in two equal installments on March 30 and September 30 each year.

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(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)

15. Due to other financial institutions and banks, Sukuk securities issued and subordinated loans (continued)

Sukuk securities as of December 31, 2017 and 2016 is as follows;

	Amount in TL	
	2017	2016
Sukuk certificates issued USD	3,795,719	3,536,069
Sukuk certificates issued TL	1,096,838	588,915
Sukuk certificates issued MYR	759,284	638,997
Total	5,651,841	4,763,981

Subordinated loans as of December 31, 2017 and 2016 is as follows;

	Amount in TL	
	2017	2016
Subordinated loan provided by Kuwait Finance House	-	713,881
Subordinated loan provided by other foreign banks ⁽¹⁾	1,360,338	1,267,765
Total	1,360,338	1,981,646

(1)The Bank has acquired 350 million US dollars contribution capital loan, with having the requirements defined by BRSA Regulation on the Capital Adequacy, from Special Purpose Vehicle (SPV) KT Sukuk Company Limited that resides in Cayman Island that acquired the amount via issuance of Sukuk on 17 February 2016. Annual rate of return for the loan that is included in contributonal capital calculation in accordance with the BRSA Letter of Conformity dated 2 September 2015 and No 20008792101.01[93]E.12819 is 7.90%, has a maturity of 10 years with a repayment option for the bank after 5 year from the opening date. Returns will be calculated with the implementation of annual rate of return to the loan amount defined as transfer price of the assets, and installements will be made on 17 July and 17 February each year.

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16. Current and profit / loss sharing investors' accounts

	2017	2016
Current accounts:		
Turkish lira	6,986,424	5,946,657
Foreign currency	9,311,336	6,047,823
	16,297,760	11,994,480
Profit/loss sharing investors' accounts:		
Turkish lira	12,971,587	11,948,950
Foreign currency	10,971,569	7,969,594
	23,943,156	19,918,544
Blocked accounts:		
Turkish lira	23,558	28,152
Foreign currency	3,660	5,383
	27,218	33,535
Total current accounts and profit/loss investors' accounts	40,268,134	31,946,559
Expense accrual on current accounts and profit/loss sharing investors' accounts	86,607	69,494
Total current accounts and profit/loss sharing investors' accounts	40,354,741	32,016,053

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16. Current and profit / loss sharing investors' accounts (continued)

Blocked accounts include receivables of point of sales machine holding depositors which become current account within an average of one month period.

Current accounts and profit/loss sharing investors' accounts, excluding expense accruals, can be analyzed according to their original maturities as follows:

	Current Period			Previous Period		
	TL	Foreign currency	Total	TL	Foreign currency	Total
Up to 1 month	11,317,810	12,454,993	23,772,803	9,735,304	8,111,472	17,846,776
From 1 month to 3 months	7,254,309	5,990,876	13,245,185	6,979,753	4,376,237	11,355,990
From 3 months to 1 year	1,004,647	1,627,293	2,631,940	872,522	1,333,651	2,206,173
Over one year	404,803	213,403	618,206	336,180	201,440	537,620
	19,981,569	20,286,565	40,268,134	17,923,759	14,022,800	31,946,559

At December 31, 2017 and 2016, foreign currency and precious metals linked current and profit/loss sharing investors' accounts, excluding expense accruals, are as follows:

	Current Period		Previous Period	
	Foreign currency (full)	TL equivalent	Foreign currency (full)	TL equivalent
Current and blocked accounts:				
USD	1,584,904,657	5,987,643	1,003,796,742	3,532,561
Euro	373,591,909	1,691,015	296,023,858	1,098,219
Precious metals		1,478,276		1,299,314
Other		158,062		123,112
		9,314,996		6,053,206
Profit/loss sharing investors' accounts:				
USD	1,782,054,678	6,732,460	1,407,280,348	4,952,502
Euro	617,458,803	2,794,847	532,867,490	1,976,884
Precious metals		1,444,262		1,040,208
		10,971,569		7,969,594
		20,286,565		14,022,800

The Bank mainly collects profit/loss sharing accounts from domestic companies and domestic individuals.

Profit/loss sharing accounts include the gain or loss resulting from the investment activities of the Bank and there is no predetermined return on these accounts when depositing money.

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17. Income taxes

Corporate Tax

The Group is subject to Turkish corporate taxes. Provision is made in the accompanying financial statements for the estimated charge based on the Group's results for the years and periods. Turkish tax legislation does not permit a parent company and its subsidiary to file a consolidated tax return. Therefore, provisions for taxes, as reflected in the accompanying condensed consolidated interim financial statements, have been calculated on a separate-entity basis. Corporate tax is applied on taxable corporate income, which is calculated from the statutory accounting profit by adding back non-deductible expenses, and by deducting dividends received from resident companies, other exempt income and investment incentives utilized.

In Turkey, corporate income tax is levied at the rate of 20% on the statutory corporate income tax base for the year ended December 31, 2017. This rate was 20% for the year ended December 31, 2016 as well. Capital gains arising from the disposal of property and equipment and investments owned for at least two years are exempt at a rate of 75% from corporate tax provided that such gains are reflected in equity with the intention to be utilized in a share capital increase within five years from the date of the disposal. The remaining 25% of such capital gains are subject to corporate tax.

In Turkey, advance tax returns are filed on a quarterly basis. The advance corporate income tax rate applied in 2017 is 20%. (2016: 20%). Losses can be carried forward for offset against future taxable income for up to 5 years. However, losses cannot be carried back for offset against profits from previous periods.

Furthermore, there is no procedure for a final and definitive agreement on tax assessments. Companies file their tax returns between 1-25 April following the close of the accounting year to which they relate. Tax authorities may, however, examine such returns and the underlying accounting records and may revise assessments within five years.

"Law on the Amendment of Certain Tax Laws and Some Other Laws" numbered 7061 was published in the Official Gazette dated 5 December 2017 and numbered 30261.

With Article 91 of this law, with the provisional article 10 added to the Corporate Tax Law, the rate of 20% corporate tax will be applied as 22% for the corporate earnings for the taxation periods of 2018, 2019 and 2020 (the accounting periods for the institutions that are designated for the special accounting period). This rate will be applied for the first time in the first temporary tax period of 2018.

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 Turkish residents and Turkish branches of foreign companies. From 23 July 2006, withholding income tax rate is 15% upon the Council of Ministers' Resolution No: 2006/10731. Undistributed dividends incorporated in share capital are not subject to income withholding tax.

In addition, it is decided to stay of execution until the publication of the decision in the Official Gazette, to avoid the circumstances and losses that are difficult or impossible to compensate subsequently and for that the annulment decision does not remain inconclusive, due to the fact that aforementioned sentence is repealed by the decision no: E. 2010/93 K. 2012/20 as of February 9, 2012 at the same meeting.

The details of income tax expense are as follows;

	2017	2016
Current tax expense	199,407	124,838
Prepaid tax (-)	(143,136)	(96,987)
Income taxes payable	56,271	27,851
	2017	2016
Current tax expense	197,600	124,960
Deferred tax (credit)/charge	(9,604)	6,277
Total income tax charge/(credit)	187,996	131,237

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17. Income taxes (continued)

A reconciliation of income tax expense applicable to profit from operating activities before income tax at the statutory income tax rate to income tax expense at the Bank's effective income tax rate for the years December 31, 2017 and 2016 is as follows:

	2017	2016
Profit before income tax from continuing operations	903,824	695,961
At Turkish statutory income tax rate of 20%	180,765	139,192
Effect of income not subject to tax	(5,605)	(13,717)
Effect of expenditure not allowable for income tax purposes	12,836	5,762
Income tax charge	187,996	131,237

Deferred tax as of December 31, 2017 and 2016 is attributable to the following items:

	Deferred tax assets/(liabilities)	
	2017	2016
Deferred income	46,597	29,683
Derivative accrual	26,181	27,731
Provision for impairment in due from financing activities	8,543	8,728
Impairment provision for subsidiaries, fixed assets and assets held for sale	36,436	36,641
Bonus accrual of personnel	22,244	14,755
Deferred tax accounted under shareholders' equity	12,489	12,841
Reserve for employee termination benefits	10,495	7,858
Effect of precious metals valuation	2,803	-
Deferred tax assets	165,788	138,237
Provision for non cash loans and check commitments	(19,592)	(15,874)
Restatement and pro-rate depreciation of property and equipment, intangible assets and other non-monetary items	(10,044)	(7,754)
Available for sale valuation differences	(3,556)	(220)
Effect of precious metals valuation	(652)	(3,131)
Effect of other temporary differences	(4,872)	(848)
Deferred tax liabilities	(38,716)	(27,827)
Deferred tax asset – net	127,072	110,410

Movement of net deferred tax asset is as follows:

	2017	2016
Balance at the beginning of the year	110,410	98,469
Deferred tax (charge)/credit recognized in income statement	9,604	(6,277)
Deferred tax (charge)/credit recognized in equity	7,058	18,218
Balance at the end of the year	127,072	110,410

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18. Employee benefit obligations

	2017	2016
Personnel bonus accrual	69,670	55,290
Employee termination benefits	108,159	67,218
Total employee benefit obligations	177,829	122,508

The movement in reserve for personnel bonus accrual is as follows:

	2017	2016
Balance at January 1	55,290	49,677
Utilized/paid	(55,290)	(49,677)
Charge for the year	69,670	55,290
Balance at the end of the year	69,670	55,290

The movement in reserve for employee termination benefits and other provisions related with employee are as follows:

	2017	2016
Balance at January 1	67,218	57,228
Utilized/paid	(5,297)	(7,881)
Service cost	21,936	10,659
Interest cost	7,811	5,758
Actuarial loss (*)	16,492	1,454
Balance at the end of the year	108,159	67,218

(*) Retirement pay liability arising from current period and amounting TL 16,492 (2016: TL 1,454) is an actuarial loss amount and deferred tax amounting to TL 3,298 (2016: TL 291) related with the retirement pay liability is accounted under statement of other comprehensive income.

Reserve for employee termination benefits

In accordance with existing social legislation, the Group is required to make lump-sum payments to employees whose employment is terminated due to retirement or for reasons other than resignation or misconduct. In Turkey, such payments are calculated on the basis 30 days' pay (limited to a maximum of TL 3.1 and TL 3.1 at December 31, 2017 and 2016, respectively) per year of employment at the rate of pay applicable at the date of retirement or termination. In the financial statements as of December 31, 2017 and 2016, the Group reflected a liability calculated using the actuarial valuation by independent actuary and based on upon factors derived using their experience of personnel terminating their services and being eligible to receive retirement pay and discounted by using the current market yield at the balance sheet date on government bonds.

The amount payable consists of one month's salary limited to a maximum of TL 4,732 (2016: TL 4,297) for each period of service at 31 December 2017.

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

The provisions for employment termination benefits of the Group, since the employment termination benefit ceiling is rearranged every six months, is calculated over TL 5,001.76 that is effective commencing on January 1, 2018 (January 1, 2017: TL 4,426.16)

Notes to consolidated financial statements for the year ended December 31, 2017
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18. Employee benefit obligations (continued)

The following actuarial assumptions were used in the calculation of the total liability:

	2017	2016
Discount rate (%)	2.5	3.4
Expected salary / ceiling increase rate (%)	9.9	8.8
Anticipated turnover rate (%)	89	89

19. Other liabilities and provisions

	2017	2016
Clearing accounts	108,082	228,575
Withholding tax and other tax payables	66,518	57,384
Payables to exporters and suppliers	49,721	24,436
Security premium for participation funds	21,779	18,287
Deferred revenue for non cash loans	14,186	11,099
Deductions on resource utilization fund	2,048	1,753
Provision for non-cash loans	124,514	76,375
Other provisions and liabilities	118,808	162,200
Total other liabilities	506,615	525,323

20. Derivative financial instruments

A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instruments, reference rates or indices.

The table below shows the fair values of derivative financial instruments together with the notional amounts analyzed by the term to maturity. The notional amount is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at year-end and are neither indicative of the market risk nor credit risk.

The fair values of foreign currency and precious metals forward and swap transactions are determined by comparing the foreign currency rates prevailing on the date of the financial statements to the discounted value of the transaction's forward exchange rates to the date of these financial statements.

December 31, 2017								
	Fair value assets	Fair value liabilities	Notional amount in Turkish Lira equivalent	Up to 1 months	1 to 3 months	3 to 6 months	6 to 12 months	Over 1 year
Derivatives held for trading								
Inflows	26,699	-	7,677,585	4,828,992	1,140,288	351,151	610,714	746,440
Outflows	-	151,493	7,647,008	4,859,152	1,142,688	357,704	468,401	819,063
December 31, 2016								
	Fair value assets	Fair value liabilities	Notional amount in Turkish Lira equivalent	Up to 1 months	1 to 3 months	3 to 6 months	6 to 12 months	Over 1 year
Derivatives held for trading								
Inflows	110,049	-	9,957,843	7,203,785	671,043	684,691	765,162	633,162
Outflows	-	257,556	10,090,188	7,217,924	698,916	650,932	754,515	767,901

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21. Share capital

	2017	2016
Number of ordinary shares, 1 TL, par value. Authorized, issued and outstanding.	3,097 million	2,787 million

The movement of the share capital of the Bank (in number and in historical TL) is as follows:

		2017		2016
	Number	TL	Number	TL
At January 1	2,787,322,000	2,787,322	2,527,322,000	2,527,322
Shares issued in				
- bonus shares from retained earnings	310,000,000	310,000	260,000,000	260,000
-other	-	-	-	-
At year end	3,097,322,000	3,097,322	2,787,322,000	2,787,322

The Bank has increased its share capital on March 28, 2017. The share capital increase was funded from the retained earnings amounting to TL 310,000 (2016 - TL 260,000).

The Bank does not have any share type other than common shares. There is no differentiation in the rights, preferences and restriction of the common shares.

As of December 31, 2017 and 2016, the composition of shareholders and their respective % of ownership can be summarized as follows:

	2017		2016	
	Amount	%	Amount	%
Kuwait Finance House	1,929,479	62.2	1,737,136	62.2
Directorate of Vakıf Foundations, Turkey	580,297	18.7	522,449	18.7
The Public Institution for Social Security, Kuwait	279,000	9	251,187	9
Islamic Development Bank	279,000	9	251,187	9
Other	29,546	1	25,363	1
Total share capital	3,097,322	100	2,787,322	100

22. Legal reserves, retained earnings, dividends paid and proposed and other reserves

Legal reserves

The legal reserves consist of first and second legal reserves in accordance with the Turkish Commercial Code. The first legal reserve is appropriated out of the statutory profits at the rate of 5%, until the total reserve reaches a maximum of 20% of the share capital. The second legal reserve is appropriated at the rate of 10% of all distributions in excess of 5% of the share capital. The first and second legal reserves are not available for distribution unless they exceed 50% of the share capital, but may be used to absorb losses in the event that the general reserve is exhausted.

Dividends paid and proposed

During the current year, the Bank has paid a dividend of TL 4,291 (2016 – TL 3,399) from the profit of the year 2017.

	2017	2016
Ordinary shares		
Amount	4,291	3,399
TL (full) per share	0.001	0.001

22. Legal reserves, retained earnings, dividends paid and proposed and other reserves (continued)**Other reserves**

The Bank bought 25% share of the joint venture called Körfez Gayrimenkul Yatırım Ortaklığı A.Ş. on September 23, 2011, which was established by Körfez and a third party company who had 75% and 25% stakes, respectively. The Bank bought the 25% stake of the third party company in Körfez Gayrimenkul Yatırım Ortaklığı A.Ş. for a total consideration of TL 22,589 in exchange of releasing the debt of the third party company to the Bank amounting to TL 15,888 and taking over the debt of the third party company to Körfez Gayrimenkul Yatırım Ortaklığı A.Ş. amounting to TL 6,701. The purchase price has been determined based on the expected discounted future cash flows of Körfez Gayrimenkul Yatırım Ortaklığı A.Ş. Since the amount of the non-controlling interest in Körfez İnşaat İş Ortaklığı is negligible, the total consideration amounting to TL 22,589 recognized as a separate component of equity as being the difference between the amount by which the non-controlling interest is adjusted and the fair value of the consideration paid.

23. Earnings per share

Basic earnings per share (EPS) amounts are calculated by dividing the net profit for the year attributable to ordinary equity holders of the Bank by the weighted average number of ordinary shares outstanding during the year.

In Turkey, companies can increase their share capital by making a pro rata distribution of shares ("Bonus Shares") to existing shareholders without consideration for amounts resolved to be transferred to share capital from retained earnings and revaluation surplus. For the purpose of the EPS calculation such Bonus Share issues are regarded as stock dividends. Dividend payments, which are immediately reinvested in the shares of the Bank, are similarly treated. Accordingly the weighted average number of shares used in EPS calculation is derived by giving retroactive effect to the issue of such shares.

There is no dilution of shares as of December 31, 2017 and 2016.

The following reflects the income and per share data used in the basic earnings per share computations:

	2017	2016
Net profit attributable to continuing operations of the Bank for basic earnings per share	710,122	563,984
Net profit/(loss) attributable to discontinued operations for basic earnings per share	-	-
-		
Net profit attributable to ordinary equity holders of the Bank for basic earnings per share	710,122	563,984
Weighted average number of ordinary shares for basic earnings per share (thousands)	3,023,432	2,719,125
Basic earnings per share (expressed in full TL per share)	0.235	0.207

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24. Related party disclosures

The Group is controlled by Kuwait Finance House, which owns 62.2% (December 31, 2016 - 62.2%) of ordinary shares. Directorate of Vakıf Foundations, The Public Institution for Social Security and Islamic Development Bank are major shareholders owning 18.7% (December 31, 2016 - 18.7%), 9.0% (December 31, 2016 - 9.0%) and 9.0% (December 31, 2016 - 9.0%) of ordinary shares, respectively. For the purpose of these financial statements, shareholders of the Bank and parties under common control of the majority Shareholder are referred to as related parties. The related parties also include individuals who are principal owners, key management and members of the Group's Board of Directors and their families.

The following significant balances exist as at December 31, 2017 and 2016 and transactions have been entered into with related parties during the years ended:

i) Balances with financial institutions and due from financing activities:

		2017		2016	
		Foreign currency (full)	TL equivalent	Foreign currency (full)	TL equivalent
Kuwait Finance House ⁽¹⁾	Kuwaiti Dinar	93,935	1,176	82,190	941
	XAU (gr.)	144,948	22,808	112,369	14,771
KFH – Bahrain	BHD	35,208	353	21,339	199
	USD	156,675	592	103,219	363
Auto Land A.S.	TL	-	82,973	-	72,473
Kuwait finance Malaysia	USD	508	2	5,063	18
	XAU(gr)	51,973	48	-	-
Other related parties	-	-	69,000	-	63,903
			176,952		152,668

ii) Due to other financial institutions and banks:

		2017		2016	
		Foreign currency (full)	TL equivalent	Foreign currency (full)	TL equivalent
Public Institute for Social Securities KW ⁽¹⁾	USD	166,499,555	629,022	221,784,496	780,504
Kuwait Finance House ⁽¹⁾	USD	575,914,524	2,175,759	414,976,131	1,460,384
			2,804,781		2,240,888

iii) Profit/loss sharing investors' and current accounts:

		2017		2016	
		Foreign currency (full)	TL equivalent	Foreign currency (full)	TL equivalent
Kuwait Finance House ⁽¹⁾	USD	2,858,361	10,799	2,197,081	7,732
Kuwait Finance House ⁽¹⁾	TL	-	1,558	-	1,000
Islamic Development Bank ⁽¹⁾	USD	-	-	5115	18
Kuwait Finance Malaysia	XAU (gr.)	572,547	90,092	724,547	95,245
Kuwait Finance House, Bahrain	USD	1,259	5	1,243	4
Directorate of Vakıf Foundations, Turkey ⁽¹⁾	TL	-	32,923	-	31,793
Neova Sigorta AS ^(*)	TL	-	319,159	-	5,781
	USD	191,138	722	285,111	1,003
	EUR	4,524	20	-	-
Public Institute for Social Securities KW ⁽¹⁾	USD	167,692	634	164,644	579
			455,912		143,155

(*) Determined as related party as the Company is under the common control of the ultimate parent.

(1) Shareholders.

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24. Related party disclosures (continued)

iv) Profit shares distributed:

		2017		2016	
		Foreign currency (full)	TL equivalent	Foreign currency (full)	TL equivalent
Kuwait Finance House ⁽¹⁾	USD	11,203,800	42,327	8,307,994	29,237
Directorate of Vakıf Foundations, Turkey ⁽¹⁾	TL	-	3,029	-	2,670
Neova Sigorta AŞ ⁽¹⁾	TL	-	10,967	-	2,607
Public Institute for Social Securities KW ⁽¹⁾	USD	1,684,222	6,363	3,127,430	11,006
			62,686		45,520

⁽¹⁾ Determined as related party as the Company is under the common control of the ultimate parent.

⁽¹⁾ Shareholders.

v) Non cash credits issued:

		2017		2016	
		Foreign currency (full)	TL equivalent	Foreign currency (full)	TL equivalent
Kuwait Finance House ⁽¹⁾	USD	74,800	283	10,378,355	36,524
Kuwait Finance Malaysia	USD	40,000	151	40,000	140
Other related parties	TL	-	1,717	-	575
			2,151		37,239

(1) Shareholders.

As of December 31, 2017 no provisions have been recognized in respect of loans given to related parties (December 31, 2016 - none).

Directors' remuneration

The executive members of the Board of Directors and key management received remuneration totaling TL 29,814 during the year ended December 31, 2017 (December 31, 2016 – TL 27,255)

The key management personnel of the Bank are as follows ;

Hamad Abdulmohsen AL MARZOUQ	B.O.D. Chairman
Adnan ERTEM	B.O.D. Vice Chairman and Audit Committee Chairman
Nadir ALPASLAN	B.O.D. Member
Khaled Nasser Abdulaziz AL FOUZAN	B.O.D. Member
Fawaz KH E AL SALEH	B.O.D. Member
Mazin S.A.S AL NAHEDH	B.O.D. Member
Ahmed S. AL KHARJI	B.O.D. Member and Audit Committee
Mohamad AI-MIDANI	B.O.D. Member and Audit Committee
Ufuk UYAN	B.O.D. Member - Chief Executive Officer

Key management includes 19 other officers together with the above B.O.D. members.

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25. Fees and commission income and expense

	2017	2016
Fees and commission income		
Commissions on loans	167,184	167,003
Commission income from commitments	114,850	96,005
POS commission income	56,034	46,027
Income from insurance & agency activities	40,860	26,193
Credit card fees and commissions	69,832	45,656
Money transfer commissions	31,458	27,385
Import letter of credit commissions	7,837	8,333
Commissions from checks and notes	17,669	15,334
Other	53,865	45,409
Total	559,589	477,345

	2017	2016
Fees and commission expense		
Credit card machine and fees paid for credit cards	81,030	60,150
Brokerage fees on borrowings	12,951	9,832
Mortgage expertise expenses	23,735	19,800
Correspondent bank fees	14,150	17,366
Fees for funds borrowed from banks and OFI	12	914
Money transfer commissions	9,616	8,361
Other	33,077	25,086
Total	174,571	141,509

26. Salaries and employee benefits

	2017	2016
Staff costs		
Wages and salaries	437,617	383,198
Bonus	76,786	63,252
Social security premiums	83,850	79,524
Other fringe benefits	67,595	53,331
Health expenses	14,496	13,711
Provision for employee termination benefits	17,395	16,546
Other	15,145	15,547
Total	712,884	625,109

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27. Other expenses

	2017	2016
Impairment on construction projects (Note 10)	31,042	-
Impairment on investment property (Note 11)	-	51
Impairment charges/(reversal)	31,042	51
Insurance fund premium expense	38,944	33,441
Professional fees	22,307	26,691
Advertising expenses	27,275	27,883
Communication	23,399	26,906
Cleaning expense	23,848	24,854
Repair and maintenance expenses	37,499	24,295
Energy expenses	13,497	12,390
Grants and donations	1,548	1,279
Subscription and membership expenses	13,505	7,031
Travel and representation expenses	6,024	4,943
Non taxable income	4,651	4,698
Stationery and publishing expenses	5,753	4,236
Insurance expenses	3,522	2,249
Loss from sale of assets	110	366
Other	41,326	33,555
Other expenses	263,208	234,817
Total	294,250	234,868

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28. Commitments and contingencies

In the normal course of its banking activities, the Group undertakes various commitments and incurs certain contingent liabilities that are not presented in the financial statements. Such commitments include mainly letters of guarantee, letters of credit and acceptance credits.

The following is a brief summary of significant contingencies and commitments as of December 31, 2017 and 2016.

	2017	2016
Letters of guarantee issued by the Bank	9,570,179	8,116,025
Letters of credit	932,100	1,019,786
Commitments	4,254,951	3,281,611
Acceptance credits	55,958	52,044
Other guarantees	513,816	701,362
Total	15,327,004	13,170,828

Letters of Guarantee -- are mainly issued on behalf of domestic customers who entered into commitments in the domestic and international markets.

Commitments -- are mainly check payment commitments, credit cards and other guarantees and commitments.

Except for the Head-Office and three branch buildings, all branch premises of the Bank are leased under operational leases. The lease periods vary between 2-10 years and lease arrangements are cancellable. There are no restrictions placed upon the lessee by entering into these leases.

The allocation of operational lease obligations due to rent agreements of branches within lease periods as of December 31, 2017 and 2016 is as follows:

	2017	2016
Within one year	198	14
After one year but not more than five years	295,303	247,117
More than five years	494,644	474,424
	790,145	721,555

Fiduciary activities

Assets, other than cash deposits, held by the Bank and its subsidiaries in fiduciary for its customers are not included in the consolidated statement of financial position, since such items are not under the ownership of the Group. The fiduciary activities of the group is as follows:

	December 31, 2017	December 31, 2016
Cheques received for collection	7,022,459	5,831,286
Notes received for collection	2,059,454	1,175,022
	9,081,913	7,006,308

29. Financial risk management

Introduction

Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. Procedures and operations throughout the Group are designed towards effectively addressing risk. The Group is exposed to several risks such as credit risk, market risk, operational risk, liquidity risk, profit rate risk, reputational risk, legal risk, etc. Also, the Banks' capital adequacy ratio has to exceed the minimum requirements of the Banking Regulations and Supervision Agency (BRSA). BRSA is the regulatory body for banking industry in Turkey.

Organization of the risk management function

The Board of Directors is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

The mission of the Group Risk Management function is to ensure together with executive management that risks taken by the Group align with its policies and are compatible with its profitability and credit-rating objectives.

The Group Risk Management reports to the Board of Directors through the Internal Systems Committee. Internal Systems Committee is responsible for identifying, measuring, monitoring and reporting regarding risk types including credit risk, market risk, operational risk, liquidity risk, profit rate risk, reputational risk, legal risk, etc. These risks are continually monitored and controlled according to the policies and limits set by the Board of Directors by using tools and software for monitoring and controlling.

The risk management process consists of the stages of defining and measuring the risks; establishing the risk policies and procedures and their implementation; and the analysis, review, reporting, research, recognition and assessment of risks within the framework of the basis set by the Board of Directors, the Internal Systems Committee and the Audit Committee.

Internal systems and risk management policies

The Group's Risk Management Policies established by the Board of Directors via Internal Systems Committee are implemented and executed by Risk Management Department. The primary objectives of the Risk Management Department are to coordinate the integration of the Risk Management Policies among various business departments and to assess and analyze the risks associated with new products, business processes and key risk indicators. This risk assessment is carried by the Credit Risk Management and Modelling and Market Risk, Operational Risk and Capital Management functions. The Risk Management Department is managed by the Head of Risk Management. Internal Systems, which comprise of Risk Management, Internal Audit, Internal Control and Compliance Departments, are overseen by the Chief Risk Officer who reports directly to the Internal Systems Committee and coordinates communication, reporting and monitoring between the Internal Systems Committee and the Risk Management Department.

29. Financial risk management (continued)

Board of directors

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles.

The Internal Systems Committee of Board of Directors, which consists of three non-executive directors, oversees, develops and monitors all of risk management and internal systems, policies and guidelines as well as the scope and structure of overall risk management organization and activities. Current Risk Management Policies are approved by Board of Directors and are being reviewed on a yearly basis and updated in case of necessities. The Audit Committee oversees the efficiency and adequacy of internal control and internal audit systems, the functioning of these systems and any related accounting, reporting or legal matters. In addition, the Audit Committee is responsible for coordinating the work of Internal Audit Department, preparing internal audit plans and providing information to the Board of Directors about any non-compliance with the relevant regulations and deficiencies in internal controls, including those highlighted by the BRSA or internal auditors.

Audit committee

The Audit Committee is in charge of and responsible for monitoring the effectiveness and efficiency of the internal systems of the Group, the operation of these systems as well as the accounting and reporting systems within the framework of the Banking Law and relevant regulations and the integrity of the information generated, making preliminary assessments as necessary for the Board of Directors' election of independent auditing firms as well as rating institutions, evaluation and support services firms, monitoring on a regular basis the activities of these establishments which are elected by the Board of Directors and with which contracts are concluded, ensuring the maintenance and coordination, on a consolidated basis, of the internal auditing activities of partnerships which are subject to consolidation pursuant to regulations which take effect as per the Banking Law.

Risk Management Department

Risk Management Department was constituted in order to assess the main risks of the Group. In accordance with the Risk Policies, Risk Management Activities are composed of the following activities;

- Identification of risks that the Group exposes,
- Measurement of risks,
- Monitoring of risks,
- Control and reporting of risks,
- Business Continuity Plan, Process and Procedures.

Internal Audit Department

Risk management processes throughout the Group are audited periodically by the internal audit function, which examines both the adequacy of the procedures and the Group's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

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29. Financial risk management (continued)

Credit risk

Credit risk represents risk that the Group will incur a loss because a customer, client or counterparty fails to fulfill, either partially or totally, its contractual obligations.

A customer's credit limit is established taking into consideration the customer's financial performance and is then used to monitor the customer's credit risk.

Maximum exposure to credit risk without taking account of any collateral and other credit enhancements

The table below shows an analysis of the Group's maximum exposure to credit risk for the components of the balance sheet, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through the collaterals. Where financial instruments are recorded at fair value, the amounts shown represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

Gross maximum exposure	2017	2016
Cash and balances with Central Bank (including reserve deposits, excluding cash on hand)	6,728,657	5,938,207
Balances with banks and other financial institutions	4,951,453	5,979,425
Due from financing activities	34,997,542	27,087,876
Minimum financial lease payments receivable, net	1,929,863	1,545,637
Financial assets-available for sale	4,428,672	3,751,680
Financial assets-held for trading	61,925	56,713
Other assets	938,061	700,487
Derivative financial instruments	26,699	110,049
Total	54,062,872	45,170,074
Contingent liabilities	10,502,279	9,135,811
Other guarantees	569,774	753,406
Commitments	4,254,951	3,281,611
Total	15,327,004	13,170,828
Total credit risk exposure	69,389,876	58,340,902

Risk concentrations of the maximum exposure to credit risk

Concentration of risk is managed by counterparty and by industry sector.

The maximum cash credit exposure to any counterparty other than the Central Bank as of December 31, 2017 was TL 415,571 (December 31, 2016 - TL 404,708) and non-cash credit exposure as of December 31, 2017 was TL 173,071 (December 31, 2016 - TL 189,162) before taking account of collateral or other credit enhancements.

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29. Financial risk management (continued)

An industry sector analysis of the Group's financial assets, before taking into account collateral held or other credit enhancements, is as follows:

	2017	2016
	Gross exposure	Gross exposure
Financial services	20,762,386	20,306,738
Construction and materials	15,051,525	12,780,479
General retailers	10,605,616	7,368,450
Manufacturing	7,438,475	5,386,723
Electricity	2,488,666	1,973,831
Health care and social services	2,275,987	1,713,034
Food and beverages	1,438,536	1,128,846
Mining operations	777,259	467,388
Forestry	254,844	185,034
Telecommunications	261,266	209,301
Real estate	355,277	375,134
Other	7,680,039	6,445,944
Total	69,389,876	58,340,902

Collateral and other credit enhancements

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty.

The main types of collateral obtained are as follows:

For commercial lending, charges over real estate properties, vehicles, cash blockages and trade receivables.

For retail lending, mortgages over residential properties.

Management monitors the market value of collateral during its review of the adequacy of the allowance for impairment losses, and when necessary requests additional collateral in accordance with the underlying agreement.

Credit quality per class of financial assets

Rating and scoring models for Corporate/Commercial/SME portfolios are developed based on statistical methods by Risk Management Department. Classes of financial assets graded by ratings and scoring models are shown the table below as of 31 December 2017.

	Cash Loans	Non-Cash Loans	Total
High Quality	54%	69%	57%
Medium Quality	28%	20%	26%
Average	9%	6%	9%
Below Average	5%	2%	4%
Unrated	5%	3%	4%

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29. Financial risk management (continued)

Aging analysis of past due but not impaired loans per class of financial assets:

Current Period	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Due from financing activities:					
Corporate lending	700,855	137,828	152,846	-	991,559
Consumer lending	20,996	132,728	41,889	-	195,613
Credit cards	4,531	1,736	749	-	7,016
Total	726,412	272,292	195,484	-	1,194,188
Previous Period	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Due from financing activities:					
Corporate lending	904,414	276,634	171,426	-	1,352,474
Consumer lending	33,502	90,083	53,342	-	176,927
Credit cards	4,416	2,743	1,478	-	8,637
Total	942,332	369,460	226,246	-	1,538,038

Collaterals obtained from customers for the past due or impaired loans as of December 31, 2017 and 2016 comprise of blocked accounts, property and machinery pledges.

Liquidity risk

Liquidity risk is the risk that the Group will be unable to meet its payment obligations when they fall due under normal and stressed circumstances. The ability to fund existing and prospective debt requirements is managed by maintaining the availability of adequate committed funding lines from high quality lenders. In addition, the Group maintains a statutory reserve deposit with the Central Bank of Turkey.

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29. Financial risk management (continued)

The table below shows an analysis of assets and liabilities analyzed according to when they are expected to be recovered or settled.

Maturity analysis of assets and liabilities as of December 31, 2017

31 December 2017	Less than 3 months	3 to 12 months	1 to 5 years	More than 5 years	Unallocated	Total
Cash and balances with the Central Bank	1,857,063	-	-	-	-	1,857,063
Balances with other banks and financial institutions	4,739,889	211,564	-	-	-	4,951,453
Reserve deposits at the Central Bank	6,474,434	-	-	-	-	6,474,434
Financial assets – held for trading	84,661	3,573	-	390	-	88,624
<i>Derivative financial instruments</i>	23,126	3,573	-	-	-	26,699
<i>Share Certificates</i>	-	-	-	390	-	390
<i>Sukuk held for trading</i>	61,535	-	-	-	-	61,535
Financial assets – available-for-sale	1,642,843	434,763	1,490,617	677,363	183,086	4,428,672
Due from financing activities, net	9,342,018	12,129,449	13,025,786	2,382,969	47,183	36,927,405
Precious Metals	693,239	-	-	-	-	693,239
Other assets	-	-	-	-	938,061	938,061
Construction projects, net	-	-	-	-	76,234	76,234
Joint venture	-	-	-	-	19,699	19,699
Investment properties, net	-	-	-	-	84,992	84,992
Property and equipment, net	-	-	-	-	430,177	430,177
Intangible assets, net	-	-	-	-	169,802	169,802
Deferred tax assets	-	-	-	-	127,072	127,072
Assets and a disposal group held for sale	53,199	-	-	-	-	53,199
Total assets	24,887,346	12,779,349	14,516,403	3,060,722	2,076,306	57,320,126
Due to other financial institutions and banks	450,532	2,713,373	223,222	-	-	3,387,127
Sukuk securities issued	1,020,007	93,169	4,538,665	-	-	5,651,841
Subordinated Loans	-	-	-	1,360,338	-	1,360,338
Money market balances	750,524	-	-	-	-	750,524
Current and profit / loss sharing investors' accounts	38,939,429	1,226,759	88,775	-	99,778	40,354,741
Derivative financial instruments	59,494	20,338	71,661	-	-	151,493
Employee benefit obligations	-	153,807	-	-	24,022	177,829
Income taxes payable	56,271	-	-	-	-	56,271
Other liabilities and provisions	-	-	-	-	506,615	506,615
Liabilities	41,276,257	4,207,446	4,922,323	1,360,338	630,415	52,396,779
Net	(16,388,911)	8,571,903	9,594,080	1,700,384	1,445,891	4,923,347

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29. Financial risk management (continued)

Maturity analysis of assets and liabilities as of December 31, 2016.

31 December 2016	Less than 3 months	3 to 12 months	1 to 5 years	More than 5 years	Unallocated	Total
Cash and balances with the Central Bank	1,875,863	-	-	-	-	1,875,863
Balances with other banks and financial institutions	4,667,469	1,192,814	119,142	-	-	5,979,425
Reserve deposits at the Central Bank	5,678,251	-	-	-	-	5,678,251
Financial assets – held for trading	154,572	11,800	-	390	-	166,762
<i>Derivative financial instruments</i>	98,249	11,800	-	-	-	110,049
<i>Share Certificates</i>	-	-	-	390	-	390
<i>Sukuk held for trading</i>	56,323	-	-	-	-	56,323
Financial assets – available-for-sale	1,836,605	43,704	1,331,415	440,199	99,757	3,751,680
Due from financing activities, net	8,747,141	8,341,283	9,708,931	1,673,819	162,339	28,633,513
Precious Metals	802,280	-	-	-	-	802,280
Other assets	-	-	-	-	700,487	700,487
Construction projects, net	-	-	-	-	77,939	77,939
Joint venture	-	-	-	-	15,236	15,236
Investment properties, net	-	-	-	-	26,129	26,129
Property and equipment, net	-	-	-	-	426,867	426,867
Intangible assets, net	-	-	-	-	140,467	140,467
Deferred tax assets	-	-	-	-	110,410	110,410
Assets and a disposal group held for sale	42,667	-	-	-	-	42,667
Total assets	23,804,848	9,589,601	11,159,488	2,114,408	1,759,631	48,427,976
Due to other financial institutions and banks	1,554,426	1,562,045	156,855	-	-	3,273,326
Sukuk securities issued	-	588,987	4,174,994	-	-	4,763,981
Subordinated Loans	-	-	-	1,981,646	-	1,981,646
Money market balances	1,219,873	-	-	-	-	1,219,873
Current and profit / loss sharing investors' accounts	30,961,329	1,035,668	15,468	-	3,588	32,016,053
Derivative financial instruments	115,586	4,141	137,829	-	-	257,556
Employee benefit obligations	-	55,927	-	-	66,581	122,508
Income taxes payable	27,851	-	-	-	-	27,851
Other liabilities and provisions	-	-	-	-	525,323	525,323
Liabilities	33,879,065	3,246,768	4,485,146	1,981,646	595,492	44,188,117
Net	(10,074,217)	6,342,833	6,674,342	132,762	1,164,139	4,239,859

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29. Financial risk management (continued)

Analysis of financial liabilities by contractual maturities on an undiscounted basis:

Financial liabilities	On demand	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
As at December 31, 2017						
Due to other financial institutions and banks	-	452,553	2,713,692	223,222	-	3,389,467
Subordinated loans	-	52,230	52,230	417,838	1,687,880	2,210,178
Sukuk issued	-	1,051,433	316,981	4,729,336	-	6,097,750
Derivative financial instruments (*)	-	6,001,840	826,105	819,063	-	7,647,008
Current accounts	16,297,760	-	-	-	-	16,297,760
Profit and loss sharing accounts (**)	-	22,741,447	1,226,759	88,775	-	24,056,981
Total undiscounted financial liabilities	16,297,760	30,299,503	5,135,766	6,278,234	1,687,880	59,699,144
As at December 31, 2016						
Due to other financial institutions and banks	-	1,554,426	1,591,414	171,162	-	3,317,002
Subordinated loans	-	16,258	16,258	833,640	1,264,059	2,130,216
Sukuk issued	-	596,812	165,605	4,459,973	-	5,222,390
Money market balances	-	1,258,349	-	-	-	1,258,349
Derivative financial instruments (*)	-	7,885,060	1,437,227	4,929	762,972	10,090,188
Current accounts	11,994,480	-	-	-	-	11,994,480
Profit and loss sharing accounts (**)	-	18,966,849	639,444	411,692	3,588	20,021,573
Total undiscounted financial liabilities	11,994,480	30,277,754	3,849,948	5,881,397	2,030,619	54,034,198

(*) As such derivatives will be settled in gross amounts, notional amounts have been disclosed.

(**) Customers have choice of demanding their accounts anytime by abandoning profit share income.

The table below shows the contractual expiry by maturity of the Group's contingent liabilities and commitments.

	On demand	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
December 31, 2017						
Contingent liabilities and other guarantees(*)	5,523,720	1,157,413	2,551,236	1,777,148	62,536	11,072,053
Commitments	4,254,951	-	-	-	-	4,254,951
Total	9,778,671	1,157,413	2,551,236	1,777,148	62,536	15,327,004
December 31, 2016						
Contingent liabilities and other guarantees	4,461,265	1,087,254	2,475,498	1,751,369	113,831	9,889,217
Commitments	3,281,611	-	-	-	-	3,281,611
Total	7,742,876	1,087,254	2,475,498	1,751,369	113,831	13,170,828

(*) Such liabilities may be liquidated and paid by the Group in case of default or the customers.

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29. Financial risk management (continued)

Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as foreign exchange rates, interest rates and precious metals prices.

The exchange rate risk of the financial positions taken by the Group related to balance sheet and off-balance sheet accounts are measured.

The Group has determined market risk management operations and has taken precautions in order to economically hedge market risk within its financial risk management purposes, in accordance with the Communiqué on "Internal Systems of Banks".

The Board of Directors of the Group evaluates basic risks that it can be exposed to and determines limits accordingly. Those limits are revised periodically in line with the strategies of the Group. Additionally, the Board of Directors oversees that the Risk Management Group and Senior Management have taken precautions to describe, evaluate, control and manage risks faced by the Group.

Market risk – Non-trading

The Group classifies exposures to market risk into either trading or non-trading portfolios. Trading portfolio of the Group is not significant. Except for the concentration within foreign currency, the Group has no significant concentration of market risk. The Bank has precious metal transactions. Such transactions have also market risk. The analysis below calculates the effect of a reasonably possible movement of the gold price against the TL, with all other variables held constant on the income statement and equity. A negative amount in the table reflects a potential net reduction in income statement or equity, while a positive amount reflects a net potential increase.

	December 31, 2017			December 31, 2016		
	Increase/ decrease in metal price in %	Effect on profit before tax	Effect on equity	Increase/ decrease in metal price in %	Effect on profit before tax	Effect on equity
Precious metal						
Gold	-10	11,072	11,072	-10	11,023	11,023
Gold	+10	(11,072)	(11,072)	+10	(11,023)	(11,023)

Interest risk

The Group operates in non-interest banking sector therefore there is no interest risk.

Currency risk

Exchange rate risk indicates the possibilities of the potential losses that the Group is subject to due to the exchange rate movements in the market. This exposure is managed by using natural hedges that arise from offsetting foreign currency denominated assets and liabilities.

The analysis below calculates the effect of a reasonably possible movement of the currency rate against the TL, with all other variables held constant on the income statement and equity. A negative amount in the table reflects a potential net reduction in income statement or equity, while a positive amount reflects a net potential increase.

	December 31, 2017			December 31, 2016		
	Increase/ decrease in metal price in %	Effect on profit before tax	Effect on equity	Increase/ decrease in metal price in %	Effect on profit before tax	Effect on equity
Currency						
USD	+10	96,356	98,116	+10	14,755	11,720
USD	-10	(96,356)	(98,116)	-10	(14,755)	(11,720)
EUR	+10	50,702	50,702	+10	21,166	21,166
EUR	-10	(50,702)	(50,702)	-10	(21,166)	(21,166)

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29. Financial risk management (continued)

The concentrations of assets, liabilities and off balance sheet items:

December 31, 2017

	EUR	USD	Other	Precious Metals	Total
Cash and balances with the Central bank	378,598	611,174	71,584	172,222	1,233,578
Deposits with other banks and financial institutions	3,285,540	2,641,995	99,159	349,923	6,376,617
Reserve deposits at the Central Bank	499,696	4,330,165	-	1,644,573	6,474,434
Financial assets – available-for-sale	26,614	2,368,821	-	-	2,395,435
Financial assets – held for trading	-	63,130	3,337	-	66,467
Due from financing activities, net	3,952,281	7,791,574	4	56,356	11,800,215
Minimum finance lease payments receivable, net	517,511	825,758	-	-	1,343,269
Precious metals	-	-	-	693,239	693,239
Other assets	548,919	33,427	28	62	582,436
Property and equipment, net	5,701	-	-	-	5,701
Intangible assets, net	49,766	-	-	-	49,766
Total assets	9,264,626	18,666,044	174,112	2,916,375	31,021,157
Due to other financial institutions and banks	215,713	2,959,839	101,601	-	3,277,153
Sukuk issued	-	3,795,719	759,284	-	4,555,003
Subordinated loans	-	1,360,338	-	-	1,360,338
Current and profit / loss sharing investors' accounts	4,636,105	12,584,728	160,039	2,922,535	20,303,407
Other liabilities & provisions	65,463	105,955	23,024	461	194,903
Derivative financial instruments	-	126,711	3,335	-	130,046
Total liabilities and equity	4,917,281	20,933,290	1,047,283	2,922,996	29,820,850
Net balance sheet position	4,347,345	(2,267,246)	(873,171)	(6,621)	1,200,307
Net off-balance sheet position	(3,840,325)	3,230,809	859,395	(10,722)	239,157

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29. Financial risk management (continued)

December 31, 2016

	EUR	USD	Other	Precious Metals	Total
Cash and balances with the Central bank	378,584	720,778	67,561	19,657	1,186,580
Deposits with other banks and financial institutions	4,702,569	1,088,544	108,929	95,591	5,995,633
Reserve deposits at the Central Bank	370,990	3,927,014	-	1,380,247	5,678,251
Financial assets – available-for-sale	17,327	1,900,932	-	-	1,918,259
Financial assets – held for trading	-	126,015	-	-	126,015
Due from financing activities, net	3,278,547	7,081,879	5	108,137	10,468,568
Minimum finance lease payments receivable, net	504,505	683,959	-	-	1,188,464
Precious metals	-	-	-	802,280	802,280
Other assets	409,892	1,614	139	6	411,651
Property and equipment, net	5,469	89	-	-	5,558
Intangible assets, net	45,138	-	-	-	45,138
Total assets	9,713,021	15,530,824	176,634	2,405,918	27,826,397
Due to other financial institutions and banks	95,477	3,118,503	-	-	3,213,980
Sukuk issued	-	3,536,069	638,997	-	4,175,066
Subordinated loans	-	1,981,646	-	-	1,981,646
Current and profit / loss sharing investors' accounts	2,937,259	8,545,795	123,059	2,339,522	13,945,635
Other liabilities & provisions	20,933	41,326	5,005	372	67,636
Derivative financial instruments	-	216,960	16	-	216,976
Total liabilities and equity	3,053,669	17,440,299	767,077	2,339,894	23,600,939
Net balance sheet position	6,659,352	(1,909,475)	(590,443)	66,024	4,225,458
Net off-balance sheet position	(6,447,687)	1,761,924	86,906	446,475	(4,152,382)

Pricing risk

The Group issues loans with a pre-determined profit rate and receives deposits on the understanding that the depositors participate in the profit or loss resulting from the investment activities and funds utilized by the Group, rather than giving them a pre-determined rate of profit. In this aspect, there is no repricing structure for the financial assets and liabilities of the Group.

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29. Financial risk management (continued)

Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, it is managing the risks. Controls include segregation of duties, access, authorization and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

Capital adequacy

To monitor the adequacy of its capital, the Bank uses ratios established by the BRSA and is obliged to comply with the minimum requirements of the capital adequacy ratio. These ratios measure capital adequacy (minimum 12% as required by BRSA) by comparing the Bank's eligible capital with its balance sheet assets, off-balance sheet commitments and market and other risk positions at weighted amounts to reflect their relative risk.

As of December 31, 2017 and 2016, the Bank's statutory capital adequacy ratio exceeded the minimum requirement of BRSA.

Capital management

The primary objectives of the Bank's capital management are to ensure that the Bank complies with externally imposed capital requirements and that the Bank maintains strong credit ratings and healthy capital ratios in order to support its business.

The Bank manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payments to shareholders. No changes were made in the objectives, policies and processes from the previous years. Below table is in accordance with unconsolidated financial statements prepared in accordance with BRSA accounting principles.

Regulatory capital

	2017	2016		
Tier 1 capital	4,394,331	3,815,622		
Tier 2 capital	1,602,684	2,014,393		
Deductions from capital	(171,117)	(100,647)		
Total capital	5,825,898	5,729,368		
Risk weighted assets amount subject to credit, market & operational risk	33,628,878	31,499,103		
	Actual	Required	Actual	Required
Tier 1 capital ratio	13.07%		12.11%	
Total capital ratio	17.32%	12%	18.19%	12%

30. Fair value of financial instruments

Fair values

The fair value of the fixed rate financial assets and liabilities carried at amortized cost are estimated by comparing market profit rates when they were first recognized with current market rates offered for similar financial instruments. As of December 31 2017, the fair value of financing and leasing receivables has been estimated as TL 34,664,282 (December 31, 2016 – TL 28,358,119) whereas their carrying amount is TL 36,927,405 (December 31, 2016 – TL 28,633,513).

Notes to consolidated financial statements for the year ended December 31, 2017
(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)

30. Fair value of financial instruments (continued)

Fair values (continued)

Fair value of borrowings at amortized cost is estimated as TL 12,382,142 (December 31, 2016 – TL 11,587,174), whereas their carrying amount is TL 11,149,830 (December 31, 2016 – TL 11,238,826). Fair values of profit/loss sharing accounts stated at amortized cost are considered to approximate their respective carrying values as the profit share rates applicable to those accounts are in line with the market rates and the maturities of these accounts are mainly short-term.

For other short-term financial assets and liabilities, fair value is estimated to approximate carrying value due to their short term or non-interest bearing structures.

To the extent relevant and reliable information is available from financial markets in Turkey, the fair value of financial instruments is based on such market data. The fair values of other financial instruments are determined by using estimation techniques that include reference to the current market value of another instrument with similar characteristic or by discounting the expected future cash flows at prevailing profit rates.

31. Subsequent events

The Bank's subsidiary KT Kira Sertifikaları Varlık Kiralama A.Ş. has issued a sukuk with four month maturity, TL 200,000 nominal and 12.60 % borrowing rate and with three month maturity, TL 350,000 nominal and 12.55 % borrowing rate during January 2018.

"Law on the Amendment of Certain Tax Laws and Some Other Laws" numbered 7061 was published in the Official Gazette dated 5 December 2017 and numbered 30261.

With Article 91 of this law, with the provisional article 10 added to the Corporate Tax Law, the rate of 20% corporate tax will be applied as 22% for the corporate earnings for the taxation periods of 2018, 2019 and 2020 (the accounting periods for the institutions that are designated for the special accounting period). This rate will be applied for the first time in the first temporary tax period of 2018.

In the Ordinary General Assembly Meeting dated 29 March 2018, the Bank has decided to appropriate I. legal reserves amounting to TL 33,700, other reserves funded via retained profit from sales of real estate's amounting to TL 12,418, not to pay cash dividends to shareholders, to pay dividend to management amounting to TL 4,894, increasing capital account from internal sources via remaining net income amounting to TL 387,142 with distributing additional capitalized shares proportioned to shareholders' stake in share capital, to appropriate II. Legal reserves amounting to TL 489,412 and carry out remaining amount of TL 234,908 as extraordinary legal reserves. In accordance with the article 3 of the law on support for research and development activities numbered 5746, the Bank has decided to carry out the amount of 439 TL, received for the development activities, to the other reserves and to use for capital increase from internal sources.