KUVEYT TÜRK KATILIM BANKASI ANONİM ŞİRKETİ AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2018 AND INDEPENDENT AUDITOR’S REPORT

Table of contents

INDEPENDENT AUDITOR'S REPORT

To the General Assembly 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 2018, 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 2018, 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
Adoption of IFRS 9 Financial Instruments Standard for the first time and significant explanations on the recognition of the impairment of financial assets As of 1 January 2018, the Group has adopted "IFRS 9: Financial Instruments" regarding the classification and measurement of financial instruments to replace "IAS 39 Financial Instruments: Recognition and Measurement" . IFRS 9 Financial Instruments Standard consists of three phases: Phase 1 – Classification and measurement of financial assets and financial liabilities; Phase 2 – Expected credit losses Phase 3 – Hedge accounting IFRS 9 is an accounting standard with a new and complex design and implementation that requires considerable judgment and interpretation in practice. The classification of financial instruments is based on the business model used by the Group and the contractual cash flows with adoption of IFRS 9. The expected credit losses are calculated by using historic loss experience, current conditions and prospective macroeconomic models. The Group has developed new and complex models that require data from more than one system to calculate the IFRS 9 expected credit losses and to determine a significant increase in credit risk. The reason to focus on this area during our audit is; the significance of expected credit loss provision and loans within the balance sheet, classification of these loans within the framework of IFRS 9 and to determine the significant increase in credit default and credit risk accurately and timely and to determine the expected loss provision accurately. This matter has been determined as a key audit matter due to the classification and measurement of financial assets, calculation of expected credit losses, significant estimates and assumptions, management judgments and also because of the complex structure of the model. The impact of the first time adoption of IFRS 9 and relevant disclosures by the Group are presented in the Section 2 in the accompanying consolidated financial statements. The Group has elected to continue to apply the hedge accounting requirements of IAS 39.	As part of our audit work, the following procedures have been performed: The Group's IFRS 9 policy of the classification of financial assets and financial liabilities has been read and compared with the IFRS 9 standard. We have examined the Group's classification and measurement models of the financial instruments and compared them with the requirements of IFRS 9 standard. We have tested the appropriateness of criteria used to identify the financial assets having solely payments of principal and interest and checking the compliance to the Group's Business model. The appropriateness of the opening balance adjustments and the disclosures presented were checked. The processes, systems and controls created or reorganized to calculate expected credit losses have been reviewed and tested by our Information Systems and Processes auditors. Within the framework of IFRS 9, we have carried out review procedures for loans selected on the basis of samples to determine whether the classification by credit risk is reasonable, whether it is impaired, and whether the provision for impairment of the receivable is established in a timely manner and in accordance with the provisions of the new legislation. We have evaluated and tested the appropriateness of the methods used in calculation of Group's expected credit loss, significant increase in credit risk, default amount and significant assumptions on macroeconomic variables together with our risk modelling experts. We have tested model calculations through sampling together with our modelling specialists. In the framework of the discussions with the Group's management, we have evaluated whether the underlying assumptions and other judgments that constitute the basis for the impairment calculations are reasonable. We have reviewed disclosures made within the IFRS 9 framework in the consolidated financial statements of the Group with respect to loan and receivables and related impairment provision.

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.
Member of **DELOITTE TOUCHE TOHMATSU LIMITED**

İstanbul, 4 July 2019

Kuveyt Türk Katılım Bankası Anonim Şirketi and its Subsidiaries

Consolidated statement of financial position as at December 31, 2018
(Currency – In thousands of Turkish Lira - TL)

	Notes	December 31, 2018	December 31, 2017
Assets			
Cash and balances with the Central Bank	4	**3,139,716**	1,857,063
Balances with other banks and financial institutions	4	**11,986,381**	4,951,453
Reserve deposits at the Central Bank	5	**6,495,190**	6,474,434
Financial assets at fair value through profit or loss	6	**134,033**	88,624
Derivative financial instruments	*20*	**42,590**	26,699
Share Certificates	*6*	**390**	390
Sukuk	*6*	**91,053**	61,535
Financial assets valued at amortised cost	6	**37,156**	-
Financial assets at fair value through other comprehensive income	6	**6,171,745**	4,428,672
Due from financing activities, net	7	**39,130,394**	34,997,542
Minimum finance lease payments receivable, net	8	**2,454,677**	1,929,863
Precious metals		**957,110**	693,239
Construction projects, net	10	**74,614**	76,234
Joint venture		**28,815**	19,699
Investment properties, net	11	**118,574**	84,992
Property and equipment, net	13	**468,770**	430,177
Intangible assets, net	14	**202,908**	169,802
Deferred tax assets	17	**380,683**	127,072
Other assets	9	**2,836,596**	938,061
		74,617,362	57,266,927
Assets and a disposal group held for sale	12	**174,674**	53,199
Total assets		**74,792,036**	57,320,126
Liabilities and equity			
Due to other financial institutions and banks	15	**2,256,311**	3,387,127
Sukuk securities issued	15	**7,779,057**	5,651,841
Subordinated loans	15	**1,901,210**	1,360,338
Money market balances		**188,003**	750,524
Current and profit / loss sharing investors’ accounts	16	**54,983,611**	40,354,741
Derivative financial instruments	20	**170,742**	151,493
Employee benefit obligations	18	**217,989**	177,829
Income taxes payable	17	**175,685**	56,271
Other liabilities and provisions	19	**1,708,535**	506,615
Total liabilities		**69,381,143**	52,396,779
Share capital	21	**3,497,322**	3,097,322
Share premium		**22,841**	22,841
Investments at fair value through other comprehensive income reserve, net of tax		**(117,150)**	(10,583)
Employee termination benefits reserve, net of tax		**(13,296)**	(26,947)
Legal reserves and retained earnings	22	**1,953,675**	1,838,947
Currency translation differences		**166,734**	79,618
Hedging fund		**(87,494)**	(60,854)
Other reserve	22	**(24,763)**	(24,763)
Non-controlling interest		**13,024**	7,766
Total equity attributable to equity holders of the parent		**5,410,893**	4,923,347
Total liabilities and equity		**74,792,036**	57,320,126

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

Consolidated statement of comprehensive income for the year ended December 31, 2018
(Currency – In thousands of Turkish Lira - TL)

	Notes	2018	2017
Income from financing activities:			
Profit on originated loans from profit / loss sharing accounts		**2,443,276**	1,675,258
Profit on originated loans from current accounts and equity		**2,499,470**	1,535,513
Profit on deposits with other banks and financial institutions		**265,622**	87,447
Profit on finance leases		**222,373**	135,232
Profit on sukuk investments		**420,814**	280,500
Total income from financing activities		**5,851,555**	3,713,950
Profit shares distributed to participation accounts		**(1,917,147)**	(1,204,485)
Profit shares distributed to other banks and financial institutions		**(856,721)**	(554,850)
Net financing income		**3,077,687**	1,954,615
Provision for impairment of amounts due from financing activities and lease receivables		**(1,978,101)**	(756,644)
Net financing income after provision for impairment in due from financing activities and lease receivables		**1,099,586**	1,197,971
Foreign exchange gain, net		**468,305**	179,845
Net financing income after net foreign exchange gain / (loss)		**1,567,891**	1,377,816
Fees and commission income	25	**761,415**	559,589
Net trading income		**66,714**	206,736
Other income		**417,543**	145,442
Share of a joint venture income		**7,717**	5,860
Total other operating income		**1,253,389**	917,627
Fees and commission expense	25	**(248,280)**	(174,571)
Staff costs	26	**(847,510)**	(712,884)
Depreciation and amortization expense		**(134,399)**	(86,351)
Withholdings and other taxes		**(10,775)**	(8,616)
Rent expense		**(142,907)**	(115,127)
Other expenses	27	**(383,373)**	(294,250)
Total other operating expense		**(1,767,244)**	(1,391,619)
Income before taxation		**1,054,036**	903,824
Current tax charge	17	**(442,564)**	(197,600)
Deferred tax (charge)/credit	17	**210,534**	9,604
Net income for the year		**822,006**	715,828
Attributable to:			
- Owners of the equity		**816,748**	710,122
- Non-controlling interests		**5,258**	5,706
Other comprehensive income			
Items that are or may be reclassified subsequently to profit or loss:			
-Exchange differences on translation of the foreign subsidiary(including investment hedging funds)		20,718	(39,427)
-Cash flow hedge		39,758	2,570
Investments at fair value through other comprehensive income reserve		(106,567)	24,696
-Net change in fair value		(133,209)	30,870
-Deferred tax relating to component of other comprehensive income		26,642	(6,174)
Items that will not be reclassified to profit or loss			
Employee termination benefits reserve	18	13,651	(13,194)
-Net change in fair value		17,064	(16,492)
-Deferred tax relating to component of other comprehensive income		(3,413)	3,298
Other comprehensive income for the year		**(32,440)**	(25,355)
Total comprehensive income for the year		**789,566**	690,473
Attributable to:			
- Owners of the equity		**784,308**	684,767
- Non-controlling interests		**5,258**	5,706
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	**0.241**	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, 2018
(Currency – In thousands of Turkish Lira - TL)

		Share Capital	Share Premium	Legal Reserves	Retained Earnings	Other Reserves	At fair value through other comprehensive income reserve	Employee termination benefits reserve	Currency Translation Differences	Hedging Funds	Non-Controlling Interest	Total
Balances at January 1, 2017		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	21	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	22	-	-	-	(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)
Balances at December 31, 2017		**3,097,322**	**22,841**	**150,389**	**1,688,559**	**(24,763)**	**(10,583)**	**(26,947)**	**79,618**	**(60,854)**	**7,766**	**4,923,348**
Balances at January 1, 2018		**3,097,322**	**22,841**	**150,389**	**1,688,559**	**(24,763)**	**(10,583)**	**(26,947)**	**79,618**	**(60,854)**	**7,766**	**4,923,348**
Adoption of new standard	**2**				**(297,127)**							**(297,127)**
Balances at January 1, 2018		**3,097,322**	**22,841**	**150,389**	**1,391,432**	**(24,763)**	**(10,583)**	**(26,947)**	**79,618**	**(60,854)**	**7,766**	**4,626,221**
Share capital increase	21	400,000	-	-	(400,000)	-	-	-	-	-	-	-
from retained earnings		400,000	-	-	(400,000)	-	-	-	-	-	-	-
cash injection		-	-	-	-	-	-	-	-	-	-	-
Transfer from retained earnings to legal reserves		-	-	34,189	(34,189)	-	-	-	-	-	-	-
Dividends paid	22	-	-	-	(4,894)	-	-	-	-	-	-	(4,894)
Total comprehensive income for the year		-	-	-	816,748	-	(106,567)	13,651	87,116	(26,640)	5,258	789,566
Balances at December 31, 2018		**3,497,322**	**22,841**	**184,578**	**1,769,097**	**(24,763)**	**(117,150)**	**(13,296)**	**166,734**	**(87,494)**	**13,024**	**5,410,893**

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

Consolidated statement of cash flows for the year ended December 31, 2018
(Currency – In thousands of Turkish Lira - TL unless otherwise indicated)

	Notes	2018	2017
Cash flows from operating activities:			
Income from continuing operations before taxation		**1,054,036**	903,824
Share of (profit) / loss of a joint venture		**(7,717)**	(5,860)
Depreciation and amortization	11, 13, 14	**134,399**	86,351
Provision for employee termination and other benefits	18	**13,421**	29,747
Provision for personnel bonus accrual	18	**86,617**	69,670
Provision for impairment in due from financing activities and lease receivables		**1,978,101**	756,644
Income accrual		**(985,400)**	148,126
Impairment in investment property	10	**29,915**	31,042
Deferred income		**109,536**	(67,264)
Impact of exchange difference on cash at banks, sukuk and loans		**1,170,635**	(199,180)
Expense accrual of participation accounts		**86,304**	17,113
Expense and foreign exchange accrual of funds borrowed		**16,363**	(124)
Other provision		**135,634**	67,072
Net change in derivative financial instruments		**3,359**	(22,713)
Gain on sale of property and equipment, intangible assets, investment properties and asset held for sale		**(12,520)**	(18,580)
Operating income before changes in operating assets and liabilities		**3,812,683**	1,782,362
Net changes in :			
Reserve deposits at the Central Bank of Turkey		**(20,756)**	(796,183)
Due from financing activities		**(6,671,544)**	(9,416,332)
Minimum finance lease payments receivables		**(524,814)**	(384,226)
Other assets and construction projects		**(2,040,177)**	(262,307)
Current accounts and profit/loss sharing investors' accounts		**14,115,851**	8,263,561
Other liabilities		**315,086**	(461,610)
Payment for employee termination benefits	18	**(7,272)**	(5,297)
Payment for personnel bonuses	18	**(69,670)**	(55,290)
Precious metals		**(263,871)**	109,041
Income taxes paid	17	**(334,344)**	(170,987)
Net cash used in operating activities		**8,311,172**	(1,397,268)
Cash flows from investing activities:			
Cash obtained from sale of jointly controlled operations, associates and subsidiaries	31	**16,901**	-
Purchase of FVTOCI, FVTPL and amortised cost investment securities	6	**(5,016,369)**	(6,960,727)
Proceeds from FVTOCI, FVTPL and amortised cost investment securities	6	**3,194,359**	6,284,366
Purchase of property and equipment, intangible assets and investment properties	11, 13, 14	**(248,972)**	(189,395)
Proceeds from sale of property and equipment, intangible assets and investment properties		**44,308**	88,482
Proceeds from sale of asset and liabilities held for sale		**42,652**	13,439
Net cash used in investing activities		**(1,967,121)**	(763,835)
Cash flows from financing activities:			
Dividends paid	22	**(4,894)**	(4,291)
Increase / (decrease) in due to financial institutions and banks		**(606,307)**	(507,383)
Sukuk securities issued		**4,744,065**	3,085,860
Sukuk securities redeemed		**(4,335,000)**	(1,790,002)
Net cash provided by financing activities		**(202,136)**	784,184
Net increase in cash and cash equivalents		**6,141,915**	(1,376,919)
Net foreign exchange difference on cash and cash equivalents		**(66,621)**	(16,607)
Cash and cash equivalents at the beginning of the year	4	**6,247,029**	7,640,555
Cash and cash equivalents at the end of the year	4	**12,322,323**	6,247,029

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

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 July 4, 2019. 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., 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 July 31, 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 December 17, 2013 by İstanbul Register of Commerce.

KT Portföy Yönetim Anonim Şirketi ("Company"), which is 50% owned by the bank was established in May 26, 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 December 1, 2015 by Istanbul 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 financial assets at fair value through other comprehensive income.

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, expected credit loss, 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.

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, 2018 and 2017 are derived by indexing the additions that occurred until December 31, 2005 and carrying the additions after this date with their nominal amounts.

2. Summary of significant accounting policies (continued)

New and amended IFRS Standards that are effective for the current year

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

The amendments clarify the standard in respect of 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.

Amendments to IAS 40 *Transfers of Investment Property*

The amendments to IAS 40:

- Amends paragraph 57 to state that an entity shall transfer a property to, or from, investment property when, and only when, there is evidence of a change in use. A change of use occurs if property meets, or ceases to meet, the definition of investment property. A change in management's intentions for the use of a property by itself does not constitute evidence of a change in use.

- The list of examples of evidence in paragraph 57(a) – (d) is now presented as a non-exhaustive list of examples instead of the previous exhaustive list.

Amendments to IAS 40 have no impact on the Group's consolidated financial statements.

Annual Improvements to IFRS Standards 2014–2016 Cycle

- **IFRS 1:** Deletes the short-term exemptions in paragraphs E3–E7 of IFRS 1, because they have now served their intended purpose.

- **IAS 28:** Clarifies that the election to measure at fair value through profit or loss an investment in an associate or a joint venture that is held by an entity that is a venture capital organization, or other qualifying entity, is available for each investment in an associate or joint venture on an investment-by-investment basis, upon initial recognition.

Annual improvements to IFRS Standards 2014-2016 cycle have no impact on the Group's consolidated financial statements.

IFRS Interpretation 22 *Foreign Currency Transactions and Advance Consideration*

The interpretation addresses foreign currency transactions or parts of transactions where:

- there is consideration that is denominated or priced in a foreign currency;
- the entity recognizes a prepayment asset or a deferred income liability in respect of that consideration, in advance of the recognition of the related asset, expense or income; and
- the prepayment asset or deferred income liability is non-monetary.

The Interpretations Committee came to the following conclusion:

- The date of the transaction, for the purpose of determining the exchange rate, is the date of initial recognition of the non-monetary prepayment asset or deferred income liability.
- If there are multiple payments or receipts in advance, a date of transaction is established for each payment or receipt.

IFRS Interpretation 22 has no impact on the Group's consolidated financial statements.

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

2. Summary of significant accounting policies (continued)

New and revised IFRS Standards in issue but not yet effective

At the date of prepation of these financial statements, The Group has not applied the following new and revised IFRS Standards that have been issued but are not yet effective:

IFRS 16	Leases [1]
IFRS 17	Insurance Contracts
Amendments to IFRS 9	*Prepayment Features with Negative Compensation*
Amendments to IAS 28	*Long-term Interests in Associates and Joint Ventures*
IFRIC 23	*Uncertainty over Income Tax Treatments*
IFRS 10 *Consolidated Financial Statements* and IAS 28 (amendments)	*Sale of Contribution of Assets between an Investor and its Associate or Joint Venture*
Amendments to *IAS 19 Employee Benefits*	*Plan Amendment, Curtailment or Settlement* [1]
Annual Improvements to IFRS Standards 2015–2017 Cycle	*Amendments to IFRS 3 Business Combinations, IFRS 11 Joint Arrangements*, *IAS 12 Income Taxes and IAS 23 Borrowing Costs* [1]

[1] Effective from periods on or after 1 January 2019.

The directors do not expect that the adoption of the Standards listed above will have a material impact on the financial statements of the Group in future periods, except IFRS 16.

Explanations on IFRS 16 Leases Standard

IFRS 16 Leases Standard is to be applied in the accounting periods beginning after December 31, 2018. According to this standard, the difference between operating leases and financial leases has been eliminated and leasing transactions will be shown by the lessee on the balance sheet as the asset (utilization right) and financial debt related to lease payment. The Group has started its operations to comply with IFRS 16 Leases standard as of January 1, 2019, which is still continuing as of December 31, 2018.

The Group will apply this standard from January 1, 2019, the mandatory application date. The Group plans not to use the simplified migration application and to rearrange the comparable amounts for the year prior to the first implementation.

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 Interpretation 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.

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

IFRS 10 Consolidated Financial Statements and IAS 28 (amendments) *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.

2. Summary of significant accounting policies (continued)

New and revised IFRS Standards in issue but not yet effective (continued)

Annual Improvements to IFRS Standards 2015–2017 Cycle

Annual Improvements to IFRS Standards 2015–2017 Cycle include amendments to IFRS 3 Business Combinations and IFRS 11 Joint Arrangements in when a party that participates in, but does not have joint control of, IAS 12 Income Taxes; income tax consequences of dividends in profit or loss, and IAS 23 Borrowing Costs in capitalized borrowing costs.

Amendments to IAS 19 Employee Benefits Plan Amendment, Curtailment or Settlement

The amendments clarify that the past service cost (or of the gain or loss on settlement) is calculated by measuring the defined benefit liability (asset) using updated assumptions and comparing benefits offered and plan assets before and after the plan amendment (or curtailment or settlement) but ignoring the effect of the asset ceiling (that may arise when the defined benefit plan is in a surplus position).

The directors of the Group assess the possible impacts of the application of the amendments on the Group's consolidated financial statements.

Consolidation of subsidiaries

The consolidated financial statements comprise the consolidated balance sheet of the Bank and its subsidiaries, as at December 31, 2018 and 2017 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, 2018 and 2017, 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:

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

2. Summary of significant accounting policies (continued)

Consolidation of subsidiaries (continued)

		Effective shareholding by the Bank (%)	
Name of subsidiary	Country of incorporation	**December 31, 2018**	December 31, 2017
"Körfez Gayrimenkul İnş. Taah. Tur. San. Tic. A.Ş."	Turkey	**91.89%**	**91.89%**
"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 Bank AG."	Germany	**100%**	**100%**
"Architecht Bilişim Sistemleri ve Pazarlama Tic. A.Ş"	Turkey	**100%**	**100%**

(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 December 31, 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, 2017	3.78	4.53
December 31, 2018	5.28	6.04

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 5.6856 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.

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

2. Summary of significant accounting policies (continued)

IFRS 9

Details of the Records of Classifications and Amendments Regarding the Initial Implementation of IFRS 9 Financial Instruments dated 1 January 2018 are stated below.

A- As of 1 January 2018, securities portfolio amounting to TL 88,624 classified under "Financial Assets - Held for Trading" in the prior period were reclassified under "Financial Assets at the Fair Value through Profit or Loss" as they were considered within the scope of a business model whose objective is to collect and to sell contractual cash flows.

B- As of 1 January 2018, securities portfolio amounting to TL 4,428,672 classified under "-Financial Assets Available for Sale" in the prior period, were reclassified under "Financial Assets classified as Fair Value through Other Comprehensive Income" as they were considered within the scope of a business model whose objective is to collect and to sell contractual cash flows.

C- In accordance with IFRS 9, as of 1 January 2018, prior period "Collective Provisions" item has been written off and the impact of "Expected Loss Provisions" is reflected thorugh relevant lines. As per the scope of IFRS 9, expected credit losses for financial assets and loans are classified as "Expected Loss Provisions" under Assets, credit losses for non-cash loans are classified as "Other Provisions" under in Liabilities.

Reconciliation of provision of impairment opening balances in transition to IFRS 9 is stated below.

Reconciliation of provision of impairment opening balances in transition to IFRS 9			
Group	Book Value Before IFRS 9	Remeasurements and Classification	Book Value after IFRS 9
	31/12/2017		**01/01/2018**
Collective Provisions	**300,284**	**(300,284)**	**-**
Expected Credit Losses	**457,427**	**369,448**	**826,875**
12 Month Expected Credit Losses (Stage I)	-	131,074	131,074
Significant Increase in Credit Risk (Stage II)	-	199,313	199,313
Credit-Impaired Losses (Stage III/Specific Provision)	457,427	32,965	490,392
Financial Assets	-	6,096	6,096
Other Provisions	-	**208,115**	**208,115**
Total RE Impact	**757,711**	**277,279**	**1,034,990**
Depositors' accounts (provision for participation accounts)(*) (Stage III/Specific Provision)	78,619	(78,619)	-
Total IFRS 9 Impact	**836,330**	**198,660**	**1,034,990**

(*) This amount was reversed from depositors' accounts.

D- With the initial application of IFRS 9, as of January 1, 2018, a total increase after tax amounting TL 297,127 has occurred, due to the increase of TL 277,279 from the calculation of expected loss provisions and the increase of TL 19,848 from the effect of deferred tax.

Disclosures of IFRS 9 Financial Instruments:

IFRS 9 "Financial Instruments", which is effective as at January 1, 2018 replaced IAS 39 Financial Instruments: recognition and measurement, related to the classification and measurement of financial instruments.

IFRS 9 also includes new principles for general hedge accounting which aims to harmonize hedge accounting with risk management applications. In the admission of the accounting policies, IFRS 9 presents the option of postponing the adoption of IFRS 9 hedge accounting and continuing to apply the hedge accounting provisions of IAS 39. Within this context, the Group will continue to apply the hedge accounting provisions of IAS 39.

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 profit share 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

2. Summary of significant accounting policies (continued)

Disclosures of IFRS 9 Financial Instruments (continued):

irrevocable election to present subsequent changes in the fair value of an equity investment in other comprehensive income, with only dividend income generally recognized in profit or loss.

Dividends obtained from such investments are accounted in the financial statements as profit or loss unless they are evidently a part of the recoverable cost of investment.

The Group applied the classification, measurement and impairment requirements retrospectively by adjusting the opening balance sheet and opening equity at January 1, 2018, with no restatement of comparative periods.

The combined application of the contractual cash flow characteristics and business models as at January 1, 2018 is expected to result in no major difference in the classification of financial assets when compared to the classification under IAS 39.

The Group has not restated the comparative information for the financial instruments that are under the scope IFRS 9, for the year of 2017 and as of January 1, 2018, the cumulative effect of the first application of the standard has been presented under "Retained Earnings" in the statement of changes in shareholders' equity for the current period.

Classification and measurement of financial assets:

According to IFRS 9 requirements, classification and measurement of financial assets depend on the business model within which financial assets are managed and their contractual cash flow characteristics whether the cash flows represent "solely payments of principal and profit share (SPPI)".

As per IFRS 9, financial assets at fair value through profit or loss, financial assets available for sale and financial assets held to maturity which are the financial instrument categories under IAS 39; are replaced with financial assets at fair value through profit or loss, financial assets at fair value through other comprehensive income and financial assets measured at amortised cost; respectively.

Upon initial recognition each financial asset will be classified as either fair value through profit or loss ("FVTPL"), amortized cost or fair value through other comprehensive income ("FVOCI"). As the requirements under IFRS 9 are different than the assessments under the existing IAS 39 rules, the classification and measurement of financial liabilities remain largely unchanged under IAS 39.

Impairment:

Some modelling works were made in relation to the basic components of Expected Credit Loss in advance of the adoption of IFRS 9, and developed models for Probability of Default (PD) on the basis of various credit porfolio. Credit portfolio is determined in accordance with customer segments constituting the basis of banking activities. Cylical Probabilities of Default made with these models developed in order to use in the Internal Ratings-Based Approach (IRBA) are converted into Instant Probabilities of Default, and these instant probabilities of default are used to calculate Expected Credit Loss in scope of IFRS 9. Loss Given Default (LGD) calculation reflects state witholding rates and the bank's prior collection performance in unsecured loans. Default Amount (DA) corresponds to the used balance in the reporting date for money loans, and to the balance after the application of the credit conversion rate for Non-cash loans and commitment risks.

Macroeconomis scenarios impact values of PD and LGD. Three scenarios as Base, Good and Bad and expected credit loss are calculated. The default probabilities of borrowers and the loss given default ratios are changing for each scenario.

Stage 1: IFRS 9 replaces the 'incurred loss' model in IAS 39 with the 'expected credit loss' model. The Group has created a 3-stage impairment model based on a change in credit quality after initial recognition.

Stage 2: Includes financial assets having significant increase in their credit risk subsequent to the initial recognition, but not having objective evidence about impairment. It is recognized life time expected credit losses for such financial assets.

Within this scope, main considerations that are taken into account in determining the significant increase in the credit risk of a financial asset and transferring to Stage 2 are not limited to these but the following.

2. Summary of significant accounting policies (continued)

Impairment (continued):

- Default for 30 days and over as of reporting date
- Being in the scope of restructuring
- Performing close monitoring
- Assessment of rating impairment

The definition of rating note distortion is the comparison by Group between rating note at reporting date and rating note at credit opening date by using credit rating models on the basis of Bank's models of credit rating models depending on internal ratings. It is accepted as a rating distortion when a credit note that is calculated for the credit at reporting date, exceeds the determined threshold.

Stage 3: Includes financial assets having objective evidence about impairment at the reporting date. It is recognized life time expected credit losses for such financial assets.

The impact of the adoption of IFRS 9 on the financial statements as of January 1, 2018, is recorded. Besides, the Group calculated deferred tax on the expected credit losses calculated on Stage 1 and 2 loans and the impact regarding calculated deferred tax asset was accounted for under equity during transition.

Explanations on IFRS 15 Revenue from Contracts with Customers

IFRS 15 Revenue from Customer Contracts provides a single and comprehensive model and guide to registering revenue and replaces the IAS 18 Revenue standard. The standard became effective on January 1, 2018 and has no material impact on the consolidated financial statements of the Group.

Explanations on forward transactions and option contracts and derivative instruments

The Group enters into forward agreements to mitigate its currency risk and to manage its foreign currency liquidity. The Group classifies its derivative instruments as "Derivative Financial Instruments Held for Hedging Purposes" and "Financial asset at fair value through profit or loss" in accordance with "IFRS 9". Even though some derivative transactions economically hedge risk, since all necessary conditions for hedge accounting are not met, they are accounted for as "Financial assets at fair value through profit or loss" within the framework of "IFRS 9", and are reflected in the "Derivative Financial Assets / Liabilities" account in the balance sheet.

The payables and receivables arising from derivative transactions are recorded in off-balance sheet accounts at their notional amounts.

Fair values of foreign currency forward transactions and swaps are calculated by using the discounted cash flow model. Differences resulting from the changes in the fair values of derivatives held for trading are accounted under 'Trading Income/Loss' line in the income statement.

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. Embedded derivatives are accounted as derivative instruments in-line with "IFRS 9". If the embedded derivatives are closely related with the host contract, embedded derivatives are accounted for in-line with the relevant standard applicable for the host contract.

While choosing the accounting policy under IFRS 9, the Group has the option to defer the adoption of hedge accounting policy and to continue apply the accounting terms of IAS 39. Within this scope, the Bank will continue to apply the terms of hedge accounting policy specified under IAS 39. In addition to this, the Group enters into profit share rate and cross currency swap transactions in order to hedge the changes in cash flows of the floating-rate financial instruments While applying cash flow hedge accounting, the effective portion of the changes in the fair value of the hedging instrument is accounted for under hedging reserves in shareholders' equity, and the ineffective portion is recognised in income statement. The changes recognised in shareholders' equity is removed and included in income statement in the same period when the hedged cash flows effect the income or loss.

2. Summary of significant accounting policies (continued)

Explanations on forward transactions and option contracts and derivative instruments (continued)

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 at fair value through profit or loss, 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.

Explanations on financial assets

The Group classifies and accounts for its financial assets as 'Fair Value Through Profit/Loss', 'Fair Value Through Other Comprehensive Income,' or 'Amortized Cost.' Such financial assets, are recognized and derecognized as per the terms of "Recognition and Derecognition in Financial Statements" under the section three of the "TFRS 9 Financial Instruments" regarding the classification and measurements of financial instruments. When financial assets are included in the financial statements for the first time, they are measured at fair value. Transaction costs are initially added to fair value or deducted from fair value at the initial measurement of financial assets other than the "Fair Value at Fair value Through Profit or Loss".

The Group recognizes a financial asset in the financial statements only when it becomes a party to the contractual terms of a financial instrument. During the initial recognition of a financial asset, the business model determined by Bank management and the nature of contractual cash flows of the financial asset are taken into consideration. When the business model determined by the Parent Bank management is changed, all affected financial assets are reclassified and this reclassification is applied prospectively. In such cases, no adjustments is made to gains, losses or profit shares that were previously recorded in the financial statements.

Financial assets at fair value through profit or loss:

Financial assets at fair value through profit or loss are financial assets that are managed within a business model other than the business model whose objective is achieved by holding contractual cashflows for collection and the business model whose objective is achieved by collecting and selling contractual cash flows. Also, in case that the contractual terms of financial assets do not give rise on specified dates to cash flows that are solely payments of principal and profit share on the principal amount, such assets are those that are, obtained with the aim of providing profit from the short-term price or other factor fluctuations in the market or are part of a portfolio aiming to obtain short-term profit, regardless of the reason of acquisition. Financial assets at fair value through profit or loss are recorded at their fair value and as of record date they are valued at their fair values. Profits or losses caused by valuation are included in profit/loss accounts.

Financial assets at fair value through other comprehensive income:

A financial asset is classified as at fair value through other comprehensive income when the asset is managed within a business model whose objective is achieved by collecting contractual cash flows and selling the financial asset, as well as when the contractual terms of the financial asset give rise on specified dates to cash flows are solely payments of principal and profit share on the principal amount.

2. Summary of significant accounting policies (continued)

Financial assets at fair value through other comprehensive income: (continued)

Financial assets at fair value through other comprehensive income are recognized by adding transaction cost to acquisition costs that reflect the fair value of the financial asset. After the recognition, financial assets at fair value through other comprehensive income are remeasured at fair value. Profit share income calculated with effective profit share method regarding the financial assets at fair value through other comprehensive income and dividend income from equity securities are recorded to income statement. “Unrealized gains and losses,” which is the difference between the amortized cost and the fair value of financial assets at fair value through other comprehensive income, are not reflected in the income statement of the period until the acquisition of the asset, sale of the asset, the disposal of the asset, or the impairment of the asset. “Unrealized gains and losses” are accounted under the “Accumulated other comprehensive income or expense to be reclassified through profit or loss” under shareholders’ equity. When these assets are collected or disposed of, the accumulated fair value differences reflected in the equity are reflected to the income statement.

Equity securities, which are classified as financial assets at fair value through other comprehensive income, are carried at fair value, in the case that the securities have a quoted market price in an active market and/or the fair values of the securities can be reliably measured. In contrary case, the securities are carried at cost, less provision for impairment.

During initial recognition an entity can make an irrevocable election regarding the presentation of the subsequent changes in the fair value of the investment in an equity instrument, that is not held for trading purposes, in the other comprehensive income. In the case that the entity elects to present the changes as described, dividends arising from the investment is accounted in the financial statements as profit or loss.

Financial assets measured at amortized cost:

In the case that a financial asset is held within a business model whose objective is achieved both by collecting contractual cash flows and that the contractual terms of the financial asset give rise to cash flows on specified dates that are solely payments of principal and profit share on the principal amount, the financial asset is classified as financial asset measured at amortized cost.

Financial assets measured at amortized cost; are financial assets, other than loans and receivables, which are held for the purpose of custody until maturity, with conditions necessary for such assets to be held until contractual maturity met, including funding ability; and which have fixed or determinable payments and fixed maturities. Financial assets measured at amortized cost are initially recognized at cost and subsequently measured at amortized cost using the internal rate of return method. Profit share income related to financial assets measured at amortized cost is reflected in the income statement. As of the balance sheet date, the Group does not have any financial assets to be held until maturity.

Derivative Financial Assets:

The major derivative instruments utilized by the Group are foreign currency swaps, cross currency swaps and currency forwards.

Payables and receivables arising from the derivative instruments are recorded in the off-balance sheet accounts at their contractual values.

Derivative transactions are valued at their fair values subsequent to their acquisition. In accordance with the classification of derivative financial instruments, the positive fair value amounts are classified as the “Derivative Financial Assets Designated at Fair Value through Profit or Loss” or the “Derivative Financial Assets Designated at Fair Value through Other Comprehensive Income”; and the negative fair value amounts are classified as the “Derivative Financial Liabilities Designated at Fair Value through Profit or Loss” or the “Derivative Financial Liabilities Designated at Fair Value through Other Comprehensive Income”. The fair value differences of derivative financial instruments of fair value through profit or loss derivative transactions are recognized in the income statement under trading profit/loss line in profit/loss from derivative financial transactions. The fair value of derivative instruments is calculated by taking into account the market value of the derivatives or by using the discounted cash flow model.

2. Summary of significant accounting policies (continued)

Derivative Financial Assets (continued):

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 and 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.

Explanations on expected loss provisions

The Group allocates impairment for expected loss on financial assets measured at amortized cost and measured at fair value through other comprehensive income.

As of January 1, 2018, the Group has started to apply the terms of IFRS 9. The expected credit loss estimates are required to be unbiased, probability-weighted and include supportable information about past events, current conditions, and forecasts of future economic conditions.

These financial assets are divided into three categories depending on the gradual increase in credit risk observed since their initial recognition:

Stage 1: Includes financial assets not having significant increase in their credit risk from initial recognition till the following reporting date or financial assets having low credit risk at the reporting date. It is recognized 12-month expected credit losses for such financial assets.

Stage 2: Includes financial assets having significant increase in their credit risk subsequent to the initial recognition, but not having objective evidence about impairment. It is recognized life time expected credit losses for such financial assets.

Stage 3: Includes financial assets having objective evidence about impairment at the reporting date. It is recognized life time expected credit losses for such financial assets.

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.

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.

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.

2. Summary of significant accounting policies (continued)

Derecognition of financial instruments (continued)

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 January 1, 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.

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.

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.

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.

2. Summary of significant accounting policies (continued)

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 60% - 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 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 (2017: 20%-22%).

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

Please refer to IFRS 9 section for the reclassifications.

Explanations on Prior Period Accounting Policies Not Valid For The Current Period

IFRS 9 Financial Instruments" standard came into effect to replace "IAS 39 Financial Instruments: Recognition and Measurement" as of January 1, 2018. Accounting policies no longer applicable after the transition of IFRS 9 are given below:

The Group categorized its financial assets as “Fair value through profit/loss”, “Available-forsale”, “Loans and receivables” or “Held-to-maturity” in prior periods.

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.

2. Summary of significant accounting policies (continued)

Explanations on Prior Period Accounting Policies Not Valid For The Current Period (continued)

Financial assets (continued)

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.

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.

2. Summary of significant accounting policies (continued)

Explanations on Prior Period Accounting Policies Not Valid For The Current Period (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.

Impairment of financial assets

a) Assets carried at amortized cost

The Group assets 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 profit 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 profit rate (i.e. the effective profit 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.

2. Summary of significant accounting policies (continued)

Explanations on Prior Period Accounting Policies Not Valid For The Current Period (continued)

Impairment of financial assets (continued)

a) Assets carried at amortized cost (continued)

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.

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.

3. Segment reporting

For management purposes, the Group is organized into three main business groups and six sub-segments:

Retail Banking

Principally handling individual customers' current, saving and investment accounts and providing loans, consumer loans, credit cards facilities and funds transfer facilities. There are two sub-segments, Retail and Private, under Retail Banking Group.

Retail Segment, portfolio comprised of all Turkish individuals that have deposits or sukuk and investment funds under TL 2 million, real estate loans that are less than TL 750,000 in İstanbul Regions, TL 500,000 in Anatolian Regions, vehicle loans that are less than TL 150,000 in all regions and all foreign nationals' real estate loans that are less than TL 500,000.

Private segment, portfolio comprised of all Turkish individuals that have deposits or sukuk and investment funds more than TL 2 million and real estate loans that are more than TL 750,000 in İstanbul Regions, TL 500,000 in Anatolian Regions, vehicle loans that are more than TL 150,000 in all regions and all foreign nationals' real estate loans that are more than TL 500,000.

SME Banking

Principally handling loans and other credit facilities and current, saving and investment accounts for institutional customers. There are two sub-segments, Small Business and Micro, under SME Banking Group.

Small Business segment, portfolio comprised of all businesses that have annual sales turnover between TL 5 million - TL 50 million and their individual owners.

Micro segment, portfolio comprised of all businesses that have annual sales turnover below TL 5 million and their individual owners.

Commercial Banking

Principally handling loans and other credit facilities and current, saving and investment accounts for institutional customers. There are two sub-segments, Commercial and Corporate, under Commercial Banking Group.

Commercial segment, portfolio comprised of all businesses that have annual sales turnover more than TL 50 million and their individual owners except customers of corporate branches.

Corporate segment, portfolio comprised of all businesses in corporate branches.

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

3. Segment reporting (continued)

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, 2018 and 2017, respectively.

For the period ended December 31, 2018	Retail Banking	SME Banking	Commercial Banking	Corporate Banking	Tresaury, International & Investment Banking	Segments Total	Recon-ciliation	Notes	Grand Total
Income from financing activities & sukuk	639,275	1,950,622	2,146,615	364,174	750,869	**5,851,555**	-		**5,851,555**
Intersegment income	2,305,230	(305,700)	(1,142,940)	(157,709)	(698,881)	-	-		-
Total financing income	**2,944,505**	**1,644,922**	**1,003,675**	**206,465**	**51,988**	**5,851,555**	**-**		**5,851,555**
Profit shares distributed	(1,538,681)	(351,717)	(101,291)	(40,358)	(801,116)	**(2,833,163)**	59,295	(a)	**(2,773,868)**
Credit loss expense	(8,797)	(368,555)	(1,209,451)	(222,744)	(168,554)	**(1,978,101)**	-		**(1,978,101)**
Net financing income	**1,397,027**	**924,650**	**(307,067)**	**(56,637)**	**(917,682)**	**1,040,291**	**59,295**		**1,099,586**
Foreign exchange gain/loss, net	86,132	64,857	52,046	6,036	259,234	**468,305**	-		**468,305**
Net trading income	-	-	-	-	66,714	**66,714**	-		**66,714**
Net fees & commission and other income	212,304	365,574	264,987	43,429	52,101	**938,395**	-		**938,395**
Other expenses / income (net)	(725,970)	(507,455)	(211,116)	(41,316)	(33,107)	**(1,518,964)**	-		**(1,518,964)**
Segment profit / (loss)	**969,493**	**847,626**	**(201,150)**	**(48,488)**	**(572,740)**	**994,741**	**59,295**		**1,054,036**
Tax expenses	-	-	-	-	-	-	(232,030)	(b)	**(232,030)**
Net profit / (loss) for the year	**969,493**	**847,626**	**(201,150)**	**(48,488)**	**(572,740)**	**994,741**	**(172,735)**		**822,006**
Segment Assets	**7,164,815**	**15,338,933**	**19,508,689**	**3,239,805**	**29,539,794**	**74,792,036**	**-**		**74,792,036**
Segment Liabilities & Equity	**36,518,097**	**13,517,234**	**4,520,743**	**2,308,365**	**12,512,479**	**69,376,918**	**5,415,118**	**(c)**	**74,792,036**

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

c) Total equity is not allocated to the segments.

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

3. Segment reporting (continued)

For the period ended December 31, 2017	**Retail Banking**	**SME Banking**	**Commercial Banking**	**Corporate Banking**	**Tresaury, International & Investment Banking**	**Segments Total**	**Recon-ciliation**	**Notes**	**Grand 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.

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

4. Cash and balances with banks

	December 31, 2018	December 31, 2017
Cash on hand	**2,001,414**	1,602,840
Balances with the Central Bank of Turkey	**1,138,302**	254,223
Cash and balances with the Central Bank of Turkey	**3,139,716**	1,857,063
Balances with banks and other financial institutions	**11,986,381**	4,951,453
Sub Total	**15,126,097**	6,808,516
Deposit with maturity more than three months	**(1,846,664)**	(211,564)
Less: Interbank gold deposits	**(957,110)**	(349,923)
Total	**12,322,323**	6,247,029

As of December 31, 2018 and 2017, "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:

	2018				2017			
	Amount		**Effective profit rate (average)**		Amount		Effective profit rate (average)	
	TL	**Foreign currency**	**TL**	**Foreign currency**	TL	Foreign currency	TL	Foreign currency
Deposits with other banks and financial institutions	**-**	**3,645,862**	**-**	**3.24%**	-	1,269,080	-	0.49%
Total		**3,645,862**				**1,269,080**		

5. Reserve deposits at the Central Bank of Turkey

	2018		2017	
	Foreign currency	**TL**	Foreign currency	TL
USD	**516,570,819**	**2,707,174**	1,146,177	4,330,165
EUR	**9,506,605**	**2,037,427**	110,396,631	499,696
XAU (Standard Gold)	**337,369,759**	**1,750,589**	10,137,961	1,644,573
		6,495,190		6,474,434

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 1.5% and 8% for TL deposits and other liabilities according to their maturities as of December 31, 2018 (December 31, 2017: 4% and 10.5% for all TL liabilities). The reserve rates for foreign currency liabilities vary between 4% and 20% for deposit and other foreign currency liabilities according to their maturities as of December 31, 2018 (December 31, 2017: 4% and 24% for all foreign currency liabilities).

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

6. Financial assets

At Fair Value Through Other Comprehensive Income

	2018	2017
Financial Sukuk	**6,034,020**	4,254,312
Unlisted Shares	**27,158**	17,084
Fund	**110,567**	157,276
Total	**6,171,745**	4,428,672

The breakdown of unlisted shares is as follows:

		2018		2017	
	Nature of business	**Ownership%**	**Amount**	Ownership%	Amount
Kredi Garanti Fonu A.Ş. (KGF)	Financial institution	**1.54**	**4,897**	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	**-**	**17,045**	-	7,149
			27,158		17,084

The fair value of the above listed investments cannot be reliably estimated. There is no market price for these investments.

At Fair Value Through Profit Or Loss

Financial at fair value through profit or loss includes sukuk and share certificates. Balance of financial assets at fair value through profit or loss is as below:

	2018	2017
Sukuk	**91,053**	61,535
Share Certificates	**390**	390
	91,443	61,925

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

Financial investments		**2018**		2017	
	FVTOCI	**FVTPL**	**AC**	Available for sale	Held for trading
At the beginning of the year	**4,428,672**	**61,925**	**-**	3,751,680	56,713
Additions	**4,375,900**	**640,469**	**-**	4,893,546	2,067,181
Transfer from FVTOCI	**(37,156)**	**-**	**37,156**	-	-
Disposals (sale and redemption)	**(2,574,423)**	**(619,936)**	**-**	(4,226,156)	(2,058,210)
Change in fair value	**(21,248)**	**8,985**	**-**	9,602	(3,759)
Balance at the end of the year	**6,171,745**	**91,443**	**37,156**	4,428,672	61,925

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

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 1 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 Group carried at fair value according to the foregoing principles as of December 31, 2018 and 2017 are given in the table below:

Current Period	Level 1	Level 2	Level 3	Total
Financial assets				
At fair value through profit or loss	**91,443**	**42,590**	**-**	**134,033**
Share certificates	390	-	-	390
Forward transactions	-	38,731	-	38,731
Swap transactions	-	3,859	-	3,859
Sukuk	91,053	-	-	91,053
At fair value through other comprehensive income	**6,171,745**	**-**	**-**	**6,171,745**
Equity securities	-	-	-	-
Government debt securities	5,836,213	-	-	5,836,213
Other marketable securities	335,532	-	-	335,532
Amortised cost				
Government debt securities	37,156	-	-	**37,156**
Financial liabilities				
Financial liabilities held for trading	**-**	**170,742**	**-**	**170,742**
Forward transactions	-	29,913	-	29,913
Swap transactions	-	140,829	-	140,829

Previous Period	Level 1	Level 2	Level 3	Total
Financial assets				
Financial assets held for trading	**61,925**	**26,699**	**-**	**88,624**
Share certificates	390	-	-	390
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

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

7. Due from financing activities, net

	Gross Amount				ECL Allowance			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
Cash and cash equivalents (including reserves at Central Bank) (Note 4 and 5)	9,654,823	-	-	**9,654,823**	19,917	-	-	**19,917**
Balances with other banks and financial institutions (Note 4)	12,067,740	-	-	**12,067,740**	81,359	-	-	**81,359**
Securities (Note 6)	6,373,659	-	-	**6,373,659**	30,725	-	-	**30,725**
Due from financing activities and Minimum finance lease payments receivable (Note 7,8)	37,964,453	4,376,465	1,206,368	**43,547,286**	450,825	648,935	862,456	**1,962,216**
Total on-balance sheet financial assets in scope of ECL requirements	**66,060,676**	**4,376,465**	**1,206,368**	**71,643,509**	**582,826**	**648,935**	**862,456**	**2,094,217**

December 31, 2018	**Corporate and Commercial**	**Consumer**	**Credit Cards**	**Mortgage**	**Total**
Stage 1	30,691,119	1,377,957	323,720	5,571,657	37,964,453
Stage 2	4,117,558	60,107	11,838	186,962	4,376,465
Stage 3	1,146,685	31,676	6,467	21,540	1,206,368
Total gross loans	**35,955,362**	**1,469,740**	**342,025**	**5,780,159**	**43,547,286**
Stage 1&2	(907,448)	(37,230)	(8,664)	(146,418)	**(1,099,760)**
Stage 3	(829,688)	(21,813)	(4,564)	(6,390)	**(862,456)**
Net loans (*)	**34,218,226**	**1,410,697**	**328,797**	**5,627,351**	**41,585,071**

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**

(*) Also includes minimum finance lease payment receivables.

	Stage 1	**Stage 2**	**Stage 3**	**Total**
Internal Rating Grade				
Performing	**450,825**	**648,935**	**-**	**1,099,760**
High Quality	51,996	578	-	52,574
Medium Quality	51,363	34,831	-	86,194
Average	76,804	97,878	-	174,682
Below Average	270,661	515,649	-	786,310
Nonperforming	**-**	**-**	**862,456**	**862,456**

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

7. Due from financing activities, net (continued)

	2018	2017
Performing		
Funds invested from profit/loss sharing accounts	**20,464,779**	17,562,109
Funds invested from current accounts and equity	**17,166,434**	16,103,803
Income accruals on due from financing activities (**)	**2,259,008**	1,333,917
	39,890,221	34,999,829
Funds in arrears		
Funds invested from profit / loss sharing accounts	**603,983**	305,616
Funds invested from current accounts and equity	**591,209**	507,327
	1,195,192	812,943
Total	**41,085,413**	35,812,772
Impairment allowance		
Funds invested from profit / loss sharing accounts	**940,625**	288,504
Funds invested from current accounts and equity	**1,014,394**	526,726
	1,955,019	815,230
Total due from financing activities	**39,130,394**	34,997,542

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

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

7. Due from financing activities, net (continued)

The total provision of TL 1,955,019 (December 31, 2017 – TL 815,230) is made up of impaired loans and loans classified as Stage 1 and 2. The movements are analyzed below.

The movements for loans classified as Stage 1 and 2 for financing activities are as follows:

	2018	2017
Balance at beginning of year	**283,604**	162,924
Provisions - bank	**515,270**	65,033
Provisions - participation accounts	**300,886**	55,647
Allowance at the end of the year	**1,099,760**	283,604

The movement for impaired loans (Stage 3) is as follows:

	2018	2017
Balance at the beginning of the year	**531,626**	531,717
Provisions - bank	**454,203**	425,112
Provisions - participation accounts	**281,026**	152,838
Recoveries of amounts previously provided for	**(308,456)**	(116,688)
Reserves written off in current year	**(103,141)**	(461,353)
Balance at the end of the year	**855,258**	531,626

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

8. Minimum finance lease payments receivable, net

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

	2018	2017
Gross investment in finance leases	**2,881,888**	2,244,253
Unearned finance income	**(431,191)**	(315,010)
Total impaired receivables	**11,176**	5,040
Impairment allowance	**(7,197)**	(4,420)
Minimum lease payments receivable, net	**2,454,677**	1,929,863

Movements in the specific provisions for leasing receivables is as follows:

	2018	2017
Balance at January 1	**4,420**	12,126
Charge for the period	**4,285**	16,237
Charges for the bank	**2,885**	15,654
Charge for the participation accounts	**1,400**	583
Recoveries of amounts previously provided for	**(1,192)**	(11,007)
Impairment allowance written off in current period	**(316)**	(12,936)
Balance at the end of the period	**7,197**	4,420

Gross investment in finance leases as to their maturity:

	2018	2017
Not later than 1 year	**1,674,227**	1,499,972
Later than 1 year and not later than 5 years	**999,689**	565,336
Later than 5 years	**207,972**	178,945
Non-performing receivables	**11,176**	5,040
Minimum lease payments receivable, gross	**2,893,064**	2,249,293
Less : Unearned finance income	**(431,190)**	(315,010)
Net investment in finance leases	**2,461,874**	1,934,283
Less : Allowance for impairment	**(7,197)**	(4,420)
Minimum lease payments receivable, net	**2,454,677**	1,929,863

As of December 31, 2018 TL 1,692,122 (December 31, 2017 - TL 1,343,269**)** gross lease receivables are denominated in foreign currency (USD and EUR).

Net investment in finance leases as to their maturity:

	2018	2017
Less than 1 year (*)	**1,307,276**	1,223,929
1 -5 year	**951,670**	537,865
More than 5 years	**202,928**	172,489
Net investment in finance leases	**2,461,874**	1,934,283

(*) Includes total impaired receivables amounting to TL 11,176 (December 31, 2017 – TL 5,040).

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

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

9. Other assets

Other assets comprise the following:

	2018	2017
Clearing accounts	**716,193**	99,553
Prepaid expenses	**57,505**	61,076
Blockage for guarantees given	**1,968,224**	571,787
Receivables from banking operations	**22,106**	8,081
Value added tax (VAT) receivable	**17,508**	23,437
Other receivables from finance activities	**-**	153,758
Other	**55,060**	20,369
	2,836,596	938,061

10. Construction projects, net

Construction projects mainly include construction activities of Körfez Gayrimenkul Yatırım Ortaklığı A.Ş. subsidiary.

	2018	2017
Uncompleted construction projects	**27,612**	27,612
Kartal Project		
Cost of land	-	-
Cost of project	**25,699**	25,999
Kilyos Land		
Cost of land	**1,613**	1,613
Güre Tesisi	**77,217**	79,664
Completed construction projects (inventories)	**77,217**	79,664
	104,529	107,276
(Less) Impairment provision for net realizable value	**(29,915)**	(31,042)
Total construction projects, net	**74,614**	76,234

11. Investment properties, net

	2018	2017
Balance at the beginning of the year	**84,992**	26,129
Additions	**7,498**	30,947
Disposal	**(8,233)**	(8,829)
Depreciation charge	**(80)**	(158)
Transfer from assets held for resale (Note 12)	**38,763**	36,903
Transfer from other assets	**(4,366)**	-
Balance at the end of the year	**118,574**	84,992
Cost	**122,881**	88,548
Accumulated depreciation	**(3,582)**	(3,502)
Accumulated impairment	**(725)**	(54)
Net carrying amount	**118,574**	84,992

Fair value of the investment properties is TL 275,017 (December 31, 2017 - TL 118,849) which is determined based on the valuations carried out by independent qualified valuation companies in December 2018.

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.

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

12. Assets and a disposal group held for sale

At December 31, 2018, the Bank classified non-current assets; mainly land and buildings; being collateral repossessed in this period amounting to TL 174,674 (December 31, 2017 – TL 53,199), 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:

	2018	2017
Balance at the beginning of the year	**53,199**	42,667
Additions	**202,890**	60,874
Transfer to investment property (Note 11)	**(38,763)**	(36,903)
Disposals	**(42,652)**	(13,439)
Balance at the end of the year	**174,674**	53,199

Gain on sale of assets held for sale amounting to TL 9,579 is included in other income in the comprehensive income statement (December 31, 2017 – TL 27,776).

13. Property and equipment, net

	Land and buildings	Furniture and office equipment (*)	Leasehold improvements	Motor vehicles	Total
At January 1, 2017	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**
Additions (*)	529	56,377	19,584	45,642	122,132
Disposals	(6,369)	(4,551)	(1,762)	(126)	(12,808)
Depreciation charge for the year	(6,381)	(52,578)	(11,330)	(442)	(70,731)
At December 31, 2018, net of accumulated depreciation and impairment	**186,557**	**182,096**	**54,010**	**46,107**	**468,770**

(*) TL 8,153 and TL 7,957 of furniture and office equipment consist of assets obtained through financial leasing as of December 31, 2018 and 2017, 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, 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**
At December 31, 2018					
Cost	208,880	384,337	104,802	47,228	745,247
Accumulated depreciation	(22,323)	(202,241)	(50,792)	(1,121)	(276,477)
Net carrying amount	**186,557**	**182,096**	**54,010**	**46,107**	**468,770**

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

14. Intangible assets, net

	Total
At January 1, 2017	140,467
Additions	71,104
Disposals	(16,715)
Amortization charge for the year	(25,054)
At December 31, 2017, net of accumulated amortization	169,802
Additions	119,342
Disposals	(22,648)
Amortization charge for the year	(63,588)
At December 31, 2018, net of accumulated amortization	**202,908**

At December 31, 2017	
Cost (gross carrying amount)	281,758
Accumulated amortization	(111,956)
Net carrying amount	169,802
At December 31, 2018	
Cost (gross carrying amount)	**344,563**
Accumulated amortization	**(141,655)**
Net carrying amount	**202,908**

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, 2018 and 2017 is as follows;

		Amount in TL
Original currency	**2018**	2017
USD	**1,515,343**	2,959,839
Euro	**643,968**	215,713
TL	**97,000**	109,974
Other	**-**	101,601
Total	**2,256,311**	3,387,127

As of December 31, 2018 borrowings remaining maturities of which is less than 12 months amount to TL 1,706,789 (As of December 31, 2017 – TL 3,163,905).

As of December 31, 2018, the Bank has no syndicated loans (December 31, 2017 - None).

(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, 2018 and 2017 is as follows;

		Amount in TL
	2018	2017
Sukuk certificates issued USD	**5,118,302**	3,795,719
Sukuk certificates issued TL	**1,622,081**	1,096,838
Sukuk certificates issued MYR	**1,038,674**	759,284
Total	**7,779,057**	5,651,841

Subordinated loans as of December 31, 2018 and 2017 is as follows;

		Amount in TL
	2018	2017
Subordinated loan provided by Kuwait Finance House	**-**	-
Subordinated loan provided by other foreign banks [(1)]	**1,901,210**	1,360,338
Total	**1,901,210**	1,360,338

[(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 issuence of Sukuk on February 17, 2016. Annual rate of return for the loan that is included in contibutional capital calculation in accordance with the BRSA Letter of Conformity dated September 2, 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 trasfer price of the assets, and installements will be made on July 17, and February 17, each year.

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

16. Current and profit / loss sharing investors' accounts

	2018	2017
Current accounts:		
Turkish lira	**7,706,734**	6,986,424
Foreign currency	**14,715,320**	9,311,336
	22,422,054	16,297,760
Profit/loss sharing investors' accounts:		
Turkish lira	**14,536,671**	12,971,587
Foreign currency	**17,806,168**	10,971,569
	32,342,839	23,943,156
Blocked accounts:		
Turkish lira	**26,708**	23,558
Foreign currency	**19,099**	3,660
	45,807	27,218
Total current accounts and profit/loss investors' accounts	**54,810,700**	40,268,134
Expense accrual on current accounts and profit/loss sharing investors' accounts	**172,911**	86,607
Total current accounts and profit/loss sharing investors' accounts	**54,983,611**	40,354,741

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

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	**13,029,213**	**20,646,734**	**33,675,947**	11,317,810	12,454,993	23,772,803
From 1 month to 3 months	**8,014,812**	**9,449,528**	**17,464,340**	7,254,309	5,990,876	13,245,185
From 3 months to 1 year	**988,139**	**1,986,056**	**2,974,195**	1,004,647	1,627,293	2,631,940
Over one year	**348,736**	**347,482**	**696,218**	404,803	213,403	618,206
	22,380,900	**32,429,800**	**54,810,700**	19,981,569	20,286,565	40,268,134

At December 31, 2018 and 2017, 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	**1,705,043,927**	**9,001,302**	1,584,904,657	5,987,643
Euro	**470,994,262**	**2,844,405**	373,591,909	1,691,015
Precious metals		**2,588,233**		1,478,276
Other		**300,479**		158,062
		14,734,419		9,314,996
Profit/loss sharing investors' accounts:				
USD	**1,885,305,405**	**9,952,942**	1,782,054,678	6,732,460
Euro	**886,600,429**	**5,354,313**	617,458,803	2,794,847
Precious metals		**2,498,913**		1,444,262
		17,806,168		10,971,569
		32,540,587		20,286,565

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.

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

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 22% on the statutory corporate income tax base for the year ended December 31, 2018. This rate was 20% for the year ended December 31, 2017. 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 2018 is 22% (2017: 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 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;

	2018	2017
Current tax expense	**453,758**	199,407
Prepaid tax (-)	**(278,073)**	(143,136)
Income taxes payable	**175,685**	56,271

	2018	2017
Current tax expense	**442,564**	197,600
Deferred tax (credit)/charge	**(210,534)**	(9,604)
Total income tax charge/(credit)	**232,030**	187,996

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

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, 2018 and 2017 is as follows:

	2018	2017
Profit before income tax from continuing operations	**1,054,036**	903,824
At Turkish statutory income tax rate of 22% (*2017: 20%*)	**231,888**	180,765
Effect of income not subject to tax	**(26,023)**	(5,605)
Effect of expenditure not allowable for income tax purposes	**26,165**	12,836
Income tax charge	**232,030**	187,996

Deferred tax as of December 31, 2018 and 2017 is attributable to the following items:

	Deferred tax assets/(liabilities)	
	2018	2017
IFRS 9 provisions	**192,935**	-
Deferred income	**55,507**	46,597
Derivative accrual	**30,080**	26,181
Carryforward tax losses	**34,043**	-
Bonus and other benefits	**31,297**	22,244
Reserve for employee termination benefits	**17,412**	10,495
Effect of precious metals valuation	**2,031**	2,803
Other	**32,834**	57,468
Deferred tax assets	**396,139**	165,788
Restatement and pro-rate depreciation of property and equipment, intangible assets and other non-monetary items	**(7,293)**	(10,044)
FVTOCI valuation differences	**(3,691)**	(3,556)
Effect of precious metals valuation	**-**	(652)
Effect of other temporary differences	**(4,472)**	(24,464)
Deferred tax liabilities	**(15,456)**	(38,716)
Deferred tax asset – net	**380,683**	127,072

Movement of net deferred tax asset is as follows:

	2018	2017
Balance at the beginning of the year	**127,072**	110,410
Deferred tax (charge)/credit recognized in income statement	**210,534**	9,604
Deferred tax (charge)/credit recognized in equity	**23,229**	7,058
IFRS 9 effect	**19,848**	-
Balance at the end of the year	**380,683**	127,072

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

18. Employee benefit obligations

	2018	2017
Personnel bonus accrual	**86,617**	69,670
Employee termination benefits	**131,372**	108,159
Total employee benefit obligations	**217,989**	177,829

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

	2018	2017
Balance at January 1	**69,670**	55,290
Utilized/paid	**(69,670)**	(55,290)
Charge for the year	**86,617**	69,670
Balance at the end of the year	**86,617**	69,670

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

	2018	2017
Balance at January 1	**108,159**	67,218
Utilized/paid	**(7,272)**	(5,297)
Service and interest cost	**47,549**	29,747
Actuarial loss (*)	**(17,064)**	16,492
Balance at the end of the year	**131,372**	108,159

(*) Retirement pay liability arising from current period and amounting TL 17,064 (2017: TL 16,492) is an actuarial loss amount and deferred tax amounting to TL 3,413 (2017: TL 3,298) 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 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, 2018 and 2017, 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 5,434 (2017: TL 4,732) for each period of service at December 31, 2018.

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 calculated over TL 6,017.60 that is effective commencing on January 1, 2019 (January 1, 2018: TL 5,001.76)

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

18. Employee benefit obligations (continued)

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

	2018	2017
Discount Rate (%)	**16.30**	11.60
Inflation rate (%)	**12.00**	8.90
Interest rate (%)	**13.00**	9.90

19. Other liabilities and provisions

	2018	2017
Clearing accounts	**757,125**	108,082
Withholding tax and other tax payables	**86,401**	66,518
Payables to exporters and suppliers	**80,511**	49,721
Security premium for participation funds	**27,243**	21,779
Deferred revenue for non-cash loans	**42,893**	64,801
Deductions on resource utilization fund	**2,658**	2,048
Provision for non-cash loans	**386,283**	124,514
Provision for distributed profits of the participation accounts	**129,152**	30,422
Other provisions and liabilities	**196,269**	38,730
Total other liabilities	**1,708,535**	506,615

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, 2018
	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 & Hedging Purposes								
Inflows	42,590	-	**11,633,162**	7,688,220	2,699,172	224,786	-	1,020,984
Outflows	-	170,742	**11,750,656**	7,691,214	2,692,695	222,198	-	1,144,549

								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 & Hedging Purposes								
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

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

21. Share capital

	2018	2017
Number of ordinary shares, TL 1, par value. Authorized, issued and outstanding.	**3,497 million**	3,097 million

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

	2018		2017	
	Number	**TL**	Number	TL
At January 1	**3,097,322,000**	**3,097,322**	**2,787,322,000**	**2,787,322**
Shares issued in				
- transfer from retained earnings	**400,000,000**	**400,000**	**310,000,000**	**310,000**
At year end	**3,497,322,000**	**3,497,322**	**3,097,322,000**	**3,097,322**

The Bank has increased its share capital on April 3, 2018. The share capital increase was funded from the retained earnings amounting to TL 400,000 (2017 - TL 310,000).

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, 2018 and 2017, the composition of shareholders and their respective % of ownership can be summarized as follows:

	2018		2017	
	Amount	**%**	Amount	%
Kuwait Finance House	**2,178,444**	**62.2**	1,929,479	62.2
Directorate of Vakıf Foundations, Turkey	**655,174**	**18.7**	580,297	18.7
The Public Institution for Social Security, Kuwait	**315,000**	**9**	279,000	9
Islamic Development Bank	**315,000**	**9**	279,000	9
Other	**33,704**	**1**	29,546	1
Total share capital	**3,497,322**	**100**	3,097,322	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 4,894 (2017 – TL 4,291) from the profit of the year 2018.

	2018	2017
Ordinary shares		
Amount	**4,894**	**4,291**
TL (full) per share	**0.001**	**0.001**

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

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, 2018 and 2017.

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

	2018	2017
Net profit attributable to continuing operations of the Bank for basic earnings per share	**822,006**	715,828
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	**816,748**	710,122
Weighted average number of ordinary shares for basic earnings per share (thousands)	**3,386,918**	3,423,432
Basic earnings per share (expressed in full TL per share)	**0.241**	0.207

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

24. Related party disclosures

The Group is controlled by Kuwait Finance House, which owns 62.2% (December 31, 2017 - 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, 2017 - 18.7%), 9.0% (December 31, 2017 - 9.0%) and 9.0% (December 31, 2017 - 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, 2018 and 2017 and transactions have been entered into with related parties during the years ended:

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

			2018		2017
		Foreign currency (full)	**TL equivalent**	Foreign currency (full)	TL equivalent
Auto Land A.S.	TL	**-**	**114,310**	-	82,973
Other related parties	-	**-**	**90,678**	-	69,000
			204,988		151,973

ii) Due to other financial institutions and banks:

			2018		2017
		Foreign currency (full)	**TL equivalent**	Foreign currency (full)	TL equivalent
Kuwait Finance House (1)	USD	**151,936,904**	**802,108**	575,914,524	2,175,759
			802,108		2,175,759

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

			2018		2017
		Foreign currency (full)	**TL equivalent**	Foreign currency (full)	TL equivalent
Kuwait Finance House (1)	USD	**1,775,382**	**9,388**	2,858,361	10,799
Kuwait Finance House (1)	TL	**-**	**3,369**	-	1,558
Kuwait Finance House, Bahrain	USD	**1,282**	**7**	1,259	5
Directorate of Vakıf Foundations, Turkey (1)	TL	**-**	**-**	-	32,923
Neova Sigorta AS (*)	TL	**-**	**227,544**	-	319,159
	USD	**2,618,101**	**13,843**	191,138	722
	EUR	**30,289**	**183**	4,524	20
Public Institute for Social Securities KW (1)	USD	**171,268**	**905**	167,692	634
			255,239		365,820

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

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

24. Related party disclosures (continued)

iv) Profit shares distributed:

		2018			2017
		Foreign currency (full)	**TL equivalent**	Foreign currency (full)	TL equivalent
Neova Sigorta AŞ [(*)]	TL	**-**	**30,190**	-	10,967
Public Institute for Social Securities KW [(1)]	USD	**4,279**	**22**	1,684,222	6,363
Depolar Properties CO W LL	USD	**2,493**	**13**	-	-
Iskan Gayrimenkul Yatırım ve Geliştirme A.Ş.	TL		**281**	-	-
	USD	**39,648**	**203**	-	-
			30,709		17,330

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

v) Non cash credits issued:

		2018			2017
		Foreign currency (full)	**TL equivalent**	Foreign currency (full)	TL equivalent
Other related parties	TL	**-**	**520**	-	1,717
			520		1,717

(1) Shareholders.

As of December 31, 2018 no specific provisions have been recognized in respect of loans given to related parties (December 31, 2017 - none).

Directors' remuneration

The executive members of the Board of Directors and key management received remuneration totaling TL 31,813 during the year ended December 31, 2018 (December 31, 2017 – TL 29,814)

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 Al-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.

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

25. Fees and commission income and expense

	2018	2017
Fees and commission income		
Commissions on loans	198,320	167,184
Commission income from commitments	132,793	114,850
POS commission income	91,786	56,034
Income from insurance & agency activities	60,342	40,860
Credit card fees and commissions	123,245	69,832
Money transfer commissions	45,735	31,458
Import letter of credit commissions	10,383	7,837
Commissions from checks and notes	19,810	17,669
Other	79,001	53,865
Total	**761,415**	559,589

	2018	2017
Fees and commission expense		
Credit card machine and fees paid for credit cards	**133,224**	81,030
Brokerage fees on borrowings	**8,919**	12,951
Mortgage expertise expenses	**20,905**	23,735
Correspondent bank fees	**25,493**	14,150
Money transfer commissions	**9,183**	9,628
Other	**50,556**	33,077
Total	**248,280**	174,571

26. Salaries and employee benefits

	2018	2017
Staff costs		
Wages and salaries	**512,759**	437,617
Bonus	**96,738**	76,786
Social security premiums	**96,508**	83,850
Other fringe benefits	**82,395**	67,595
Health expenses	**18,902**	14,496
Provision for employee termination benefits	**25,151**	17,395
Other	**15,057**	15,145
Total	**847,510**	712,884

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

27. Other expenses

	2018	2017
Impairment on construction projects (Note 10)	**-**	31,042
Impairment on investment property (Note 11)	**671**	**-**
Impairment charges/(reversal)	**671**	31,042
Insurance fund premium expense	**90,487**	38,944
Professional fees	**29,421**	22,307
Advertising expenses	**32,879**	27,275
Communication	**27,495**	23,399
Cleaning expense	**29,826**	23,848
Repair and maintenance expenses	**47,907**	37,499
Energy expenses	**18,354**	13,497
Grants and donations	**1,756**	1,548
Subscription and membership expenses	**54,314**	13,505
Travel and representation expenses	**8,582**	6,024
Non taxable income	**3,844**	4,651
Stationery and publishing expenses	**8,809**	5,753
Insurance expenses	**5,137**	3,522
Loss from sale of assets	**3,829**	110
Other	**20,062**	41,326
Other expenses	**382,702**	263,208
Total	**383,373**	294,250

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

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, 2018 and 2017.

	2018	2017
Letters of guarantee issued by the Bank	**10,391,279**	9,570,179
Letters of credit	**1,079,876**	932,100
Commitments	**4,877,587**	4,254,951
Acceptance credits	**74,098**	55,958
Other guarantees	**330,828**	513,816
Total	**16,753,668**	15,327,004

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, Banking Base and four 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, 2018 and 2017 is as follows:

	2018	2017
Within one year	**20**	198
After one year but not more than five years	**52,006**	295,303
More than five years	**860,393**	494,644
	912,419	790,145

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, 2018	December 31, 2017
Cheques received for collection	**8,063,707**	7,022,459
Notes received for collection	**1,742,813**	2,059,454
	9,806,520	9,081,913

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.

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

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	**2018**	2017
Cash and balances with Central Bank (including reserve deposits, excluding cash on hand)	**7,633,492**	6,728,657
Balances with banks and other financial institutions	**11,986,381**	4,951,453
Due from financing activities	**39,130,394**	34,997,542
Minimum financial lease payments receivable, net	**2,454,677**	1,929,863
Financial assets at FVTOCI	**6,171,745**	4,428,672
Financial assets at FVTPL	**91,443**	61,925
Other assets	**2,836,596**	938,061
Derivative financial instruments	**42,590**	26,699
Total	**70,347,318**	54,062,872
Contingent liabilities	**11,471,156**	10,502,279
Other guarantees	**404,925**	569,774
Commitments	**4,877,587**	4,254,951
Total	**16,753,668**	15,327,004
Total credit risk exposure	**87,100,986**	69,389,876

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, 2018 was TL 923,864 (December 31, 2017 - TL 415,571) and non-cash credit exposure as of December 31, 2018 was TL 241,763 (December 31, 2017 - TL 173,071) before taking account of collateral or other credit enhancements.

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

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:

	2018	2017
	Gross exposure	Gross exposure
Financial services	**31,005,795**	20,762,386
Construction and materials	**16,706,945**	15,051,525
General retailers	**11,387,822**	10,605,616
Manufacturing	**8,665,196**	7,438,475
Electricity	**4,490,154**	2,488,666
Health care and social services	**2,905,745**	2,275,987
Food and beverages	**1,803,213**	1,438,536
Mining operations	**623,391**	777,259
Forestry	**170,075**	254,844
Telecommunications	**377,303**	261,266
Real estate	**406,510**	355,277
Other	**8,558,837**	7,680,039
Total	**87,100,986**	69,389,876

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/Retail portfolios are developed based on statistical methods by Risk Management Department. Classes of financial assets graded by ratings and scoring models or External Credit Assesment Institutions are shown the table below as of December 31, 2018.

	Cash Loans	**Non-Cash Loans**	**Total**
High Quality	49%	73%	54%
Medium Quality	29%	12%	26%
Average	12%	11%	12%
Below Average	10%	4%	8%

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

29. Financial risk management (continued)

Aging analysis of Stage 2 on 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	**2,869,347**	**639,881**	**608,330**	-	**4,117,558**
Consumer lending	**16,015**	**139,499**	**91,555**	-	**247,069**
Credit cards	**6,661**	**4,395**	**782**	-	**11,838**
Total	**2,892,023**	**783,775**	**700,667**	**-**	**4,376,465**

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	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**

Collaterals obtained from customers for the past due or impaired loans as of December 31, 2018 and 2017 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.

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

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, 2018

31 December 2018	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	3,139,716	-	-	-	-	**3,139,716**
Balances with other banks and financial institutions	7,602,596	4,036,676	327,312	19,797	-	**11,986,381**
Reserve deposits at the Central Bank	6,495,190	-	-	-	-	**6,495,190**
Financial Assets At Fair Value Through Profit Or Loss	133,643	-	-	390	-	**134,033**
Derivative financial instruments	42,590	-	-	-	-	**42,590**
Share Certificates	-	-	-	390	-	**390**
Sukuk	91,053	-	-	-	-	**91,053**
Financial assets at fair value through other comprehensive income	559,664	277,283	4,813,983	415,375	105,440	**6,171,745**
Financial assets valued at amortised cost	37,156	-	-	-	-	**37,156**
Due from financing activities, net	11,917,677	14,135,506	13,268,455	2,263,433	-	**41,585,071**
Precious metals	-	-	-	-	957,110	**957,110**
Other assets	-	-	-	-	2,836,596	**2,836,596**
Construction projects, net	-	-	-	-	74,614	**74,614**
Joint venture	-	-	-	-	28,815	**28,815**
Investment properties, net	-	-	-	-	118,574	**118,574**
Property and equipment, net	-	-	-	-	468,770	**468,770**
Intangible assets, net	-	-	-	-	202,908	**202,908**
Deferred tax assets	-	-	-	-	380,683	**380,683**
Assets and a disposal group held for sale	174,674	-	-	-	-	**174,674**
Total assets	**30,060,316**	**18,449,465**	**18,409,750**	**2,698,995**	**5,173,510**	**74,792,036**
Due to other financial institutions and banks	806,059	1,302,063	148,189	-	-	**2,256,311**
Sukuk securities issued	1,371,224	3,215,751	3,192,082			**7,779,057**
Subordinated Loans	-	-	-	1,901,210	-	**1,901,210**
Money market balances	188,003	-	-	-	-	**188,003**
Current and profit / loss sharing investors' accounts	53,134,256	1,623,929	225,426	-	-	**54,983,611**
Derivative financial instruments	59,032	5,357	106,352	-	-	**170,742**
Employee benefit obligations	-	86,617	-	-	131,372	**217,989**
Income taxes payable	-	175,685	-	-	-	**175,685**
Other liabilities and provisions	-	-	-	-	1,708,535	**1,708,535**
Liabilities	**55,558,574**	**6,409,402**	**3,672,049**	**1,901,210**	**1,839,907**	**69,381,142**
Net	**(25,498,258)**	**12,040,063**	**14,737,701**	**797,785**	**3,333,603**	**5,410,893**

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

29. Financial risk management (continued)

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**
Derivative financial instruments	23,126	3,573	-	-	-	**26,699**
Share Certificates	-	-	-	390	-	**390**
Sukuk held for trading	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**

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

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, 2018						
Due to other financial institutions and banks	-	808,234	1,338,532	163,998	-	**2,310,764**
Subordinated loans	-	72,985	72,985	583,882	2,212,653	**2,942,505**
Sukuk issued	-	1,398,812	3,544,299	4,554,629	-	**9,497,740**
Derivative financial instruments (*)	-	10,383,909	222,198	1,144,549	-	**11,750,656**
Current accounts	22,422,054	-	-	-	-	**22,422,054**
Profit and loss sharing accounts (**)	-	30,712,202	1,623,929	225,426	-	**32,561,557**
Total undiscounted financial liabilities	**22,422,054**	**43,376,142**	**6,801,943**	**6,672,484**	**2,212,653**	**81,485,276**
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**	**5,135,767**	**6,278,234**	**1,687,880**	**59,699,144**

(*) 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, 2018						
Contingent liabilities and other guarantees(*)	**6,314,813**	**931,206**	**2,831,374**	**1,674,984**	**123,703**	**11,876,080**
Commitments	**4,877,587**	**-**	**-**	**-**	**-**	**4,877,587**
Total	**11,192,400**	**931,206**	**2,831,374**	**1,674,984**	**123,703**	**16,753,668**
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

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

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

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, 2018			December 31, 2017		
Precious metal	**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
Gold	-10	**(568)**	(568)	-10	**11,072**	11,072
Gold	+10	**568**	568	+10	**(11,072)**	(11,072)

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, 2018			December 31, 2017		
Currency	**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
USD	+10	**(8,663)**	**13,807**	+10	96,356	98,116
USD	-10	**8,663**	**(13,807)**	-10	(96,356)	(98,116)
EUR	+10	**1,880**	**1,880**	+10	50,702	50,702
EUR	-10	**(1,880)**	**(1,880)**	-10	(50,702)	(50,702)

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

29. Financial risk management (continued)

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

December 31, 2018

	EUR	USD	Other	Precious Metals	Total
Cash and balances with the Central bank	862,855	1,082,888	30,769	-	1,976,512
Deposits with other banks and financial institutions	5,403,095	4,368,153	293,818	1,922,154	11,987,220
Reserve deposits at the Central Bank	2,037,427	2,707,174	-	1,750,590	6,495,191
Financial assets – financial assets at FVTPL	1,812,825	2,240,753	-	-	4,053,578
Financial assets – financial assets at OCI	6,345	101,929	422	-	108,696
Financial assets – amortised cost	-	37,156	-	-	37,156
Due from financing activities, net	5,505,277	9,615,265	-	48,589	15,169,131
Minimum finance lease payments receivable, net	301,134	711,375	-	-	1,012,509
Precious metals	-	-	-	957,110	957,110
Other assets	1,945,587	29,683	10,963	131	1,986,364
Property and equipment, net	7,697	-	-	-	7,697
Intangible assets, net	63,785	-	-	-	63,785
Total assets	**17,946,027**	**20,894,376**	**335,972**	**4,678,574**	**43,854,949**
Due to other financial institutions and banks	643,968	1,515,343	-	-	2,159,311
Sukuk issued	-	5,118,302	1,038,674	-	6,156,976
Subordinated loans	-	1,901,210	-	-	1,901,210
Current and profit / loss sharing investors' accounts	8,093,638	18,969,822	300,369	5,090,336	32,454,165
Other liabilities & provisions	127,962	251,855	69,116	17,507	466,440
Derivative financial instruments	-	148,279	9	-	148,288
Total liabilities and equity	**8,865,568**	**27,904,811**	**1,408,168**	**5,107,843**	**43,286,390**
Net balance sheet position	**9,080,459**	**(7,010,435)**	**(1,072,196)**	**(429,269)**	**568,559**
Net off-balance sheet position	**(9,061,656)**	**6,923,802**	**1,053,164**	**423,586**	**(661,104)**

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

29. Financial risk management (continued)

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**

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.

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

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, 2018 and 2017, 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

	2018	2017
Tier 1 capital	**5,156,887**	4,394,331
Tier 2 capital	**2,316,366**	1,602,684
Deductions from capital	**(84,146)**	(171,117)
Total capital	**7,389,107**	5,825,898
Risk weighted assets amount subject to credit, market & operational risk	**42,921,666**	33,628,878

	Actual	**Required**	**Actual**	**Required**
Tier 1 capital ratio	**12.01%**		**13.07%**	
Total capital ratio	**17.22%**	**12%**	**17.32%**	**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 2018, the fair value of financing and leasing receivables has been estimated as TL 40,238,153 (December 31, 2017 – TL 34,664,282) whereas their carrying amount is TL 41,585,071 (December 31, 2017 – TL 36,927,405).

30. Fair value of financial instruments (continued)

Fair values (continued)

Fair value of borrowings at amortized cost is estimated as TL 12,554,014 (December 31, 2017 – TL 12,382,142), whereas their carrying amount is TL 12,124,581 (December 31, 2017 – TL 11,149,830). 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

At the Ordinary General Assembly Meeting dated April 3, 2019, the Parent Bank decided to reserve TL 43,491 of primary reserve, transferring TL 71,861 obtained from real estate sales to other reserves instead of distributing to shareholders,not to make dividend payments in cash to shareholders, to make TL 6,546 of dividend payment to management, TL 499,681 to be used in the capital increase to be made from the internal sources without being distributed to the shareholders and to be given to the shareholders in the form of bonus shares proportionate to the shareholding shares in the capital,to allocate the secondary reserve amounting to TL 655 and to leave the remaining TL 247,261 as extraordinary reserves; to support the research and development activities numbered 5746, TL 319 support received for development activities shall be distributed to the other reserves without being distributed.

In January 2019, the Bank has exported three different sukuks via its subsidiary KT Kira Sertifikaları Varlık Kiralama A.Ş. with 105 days maturity, TL 470,000 Nominal, 21.50% borrowing rate in January 15, 2019, with 130 days maturity, TL 65,000 nominal, 21.70% borrowing rate on January 25, 2019, with 101 days maturity, TL 300,000 nominal, 21.00% borrowing rate, in January 29, 2019.

As a result of the decision to acquire the Kuwait Finance House (KFH), which is a shareholder of the Group, by acquiring the AUB B.S.C Bank in Bahrain, the Bank has started to perform financial due diligence assessments on the Bank.

The Bank signed a contract with KFH Capital Investment Company on October 5, 2017 for the transfer of 50% of the shares of KT Portföy Yönetimi A.Ş. (Subsidiary) to KFH Capital Investment Company on July 20, 2018 with an amount of TL 16,901. 50% of the transferred shares was decided to be bought back with the same price on January 27, 2019 and a contract was signed with KFH Capital Investment Company on March 27, 2019. The transfer was completed on April 2, 2019.