Aktif Yatırım Bankası Anonim Şirketi and Its Subsidiaries

Consolidated Financial Statements
As at and for the year ended
31 December 2018 with
Independent Auditor’s Report Thereon

29 March 2019

This report contains “Independent Auditor’s Report” comprising 5 pages and “Consolidated Financial Statements and Related Disclosures and Footnotes” comprising 68 pages.

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Independent Auditors' Report

To the General Assembly of Aktif Yatırım Bankası Anonim Şirketi,

Qualified Opinion

We have audited the consolidated financial statements of Aktif Yatırım Bankası Anonim Şirketi ("the Bank") and its subsidiaries (together will be referred as "the Group"), which comprise the consolidated statement of financial position as at 31 December 2018, the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

In our opinion, except for the effects of the matter described in the *Basis for Qualified Opinion* section of our report, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2018 and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Qualified Opinion

The accompanying consolidated financial statements as at 31 December 2018 include a general reserve of total of TL 133,000 thousands, of which TL 170,000 thousand was recognised in prior years and TL 37,000 thousands have been reversed in the current period, which is provided by the Bank management for the possible effects of the negative circumstances which may arise in the economy or market conditions.

We conducted our audit in accordance with International Standards on Auditing ("ISA"s). 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 ("IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in Turkey, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

The collective basis expected credit loss calculation is based on complex processes which are modelled by using current and past data sets and expectations and the forward looking expectations are reflected by macroeconomic models. Impairment on loans and advances to customers measured at amortised cost was considered to be a key audit matter, due to the significance of the estimates, assumptions, the level of judgements and its complex structure as explained above.	• We tested the accuracy and completeness of the data in the calculation models for the loans which are assessed on collective basis. The expected credit loss calculation was tested through recalculation. The models used for the calculation of the risk parameters were examined and the risk parameters for the selected sample portfolios were recalculated. • We assessed the macroeconomic models which are used to reflect forward looking expectations and tested the effect of the risk parameters by recalculation method. • We evaluated the qualitative and quantitative assessments which are used in determining the significant increase in credit risk. • Additionally, we also evaluated the adequacy of the consolidated financial statement disclosures related to impairment provisions.

Other Matter

The consolidated financial statements of the Group as at and for the year ended 31 December 2017 was audited by another auditor who expressed a qualified opinion due to the general reserve provisions provided by the Group Management on 26 April 2018.

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 IFRS, 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.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Responsibilities of auditors in an audit are as follows:

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 auditors' 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 judgement 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 auditors' 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 auditors' 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 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 period and are therefore the key audit matters. We describe these matters in our auditors' 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.

KPMG Bağımsız Denetim ve Serbest Muhasebeci Mali Müşavirlik A.Ş.
A member firm of KPMG International Cooperative

Alper Güvenç
Partner

29 March 2019
Istanbul, Turkey

Aktif Yatırım Bankası Anonim Şirketi and Its Subsidiaries

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AKTİF YATIRIM BANKASI ANONİM ŞİRKETİ AND ITS SUBSIDIARIES

Consolidated Statement of Financial Position
As at 31 December 2018
(Currency - In thousands of Turkish Lira ("TL"))

	Note	**31 December 2018**	**31 December 2017**
ASSETS			
Cash and cash equivalents	*10*	1,390,183	730,980
Reserve deposits at Central Bank	*11*	1,072,226	1,008,020
Financial assets at fair value through profit or loss	*12*	488,030	-
Trading assets	*12*	-	51,956
Trade and other receivables		75,567	254,154
Inventories		17,075	137,722
Loans and advances to customers	*14*	6,903,543	6,539,477
Investment securities	*13*	2,337,493	1,564,817
Equity accounted investees	*15*	50,798	54,052
Tangible assets	*16*	518,004	256,796
Intangible assets	*17*	216,488	143,337
Goodwill	*8*	504	504
Deferred tax assets	*23*	36,987	10,246
Assets held for sale	*19*	71,999	71,067
Other assets	*18*	703,626	247,863
Total assets		**13,882,523**	**11,070,991**
LIABILITIES			
Trading liabilities	*12*	23,017	8,987
Trade and other payables		288,240	114,787
Obligations under repurchase agreements	*20*	1,291,742	1,074,509
Financial lease liabilities		3,904	20,146
Debt securities issued	*22*	4,365,713	2,776,288
Funds borrowed	*21*	3,650,016	3,774,380
Provisions	*24*	221,552	240,966
Income taxes payable	*23*	48,589	18,392
Deferred tax liability	*23*	14,668	1,830
Other liabilities	*25*	2,400,980	1,817,756
Total liabilities		**12,308,421**	**9,848,041**
EQUITY			
Share capital	*26*	1,198,095	1,038,095
Legal reserves		56,353	38,343
Unrealised gain/(loss) on financial assets measured at fair value through other comprehensive income		(42,390)	(18,580)
Actuarial gain/ (loss)		773	(136)
Special funds		37,112	618
Translation reserves		2,290	(409)
Retained earnings		307,933	154,118
Total equity attributable to equity holders of the Bank		**1,560,166**	**1,212,049**
Non-controlling interests		13,936	10,901
Total equity		**1,574,102**	**1,222,950**
Total liabilities and equity		**13,882,523**	**11,070,991**

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statement of Profit or Loss and Other Comprehensive Income
As at 31 December 2018

(Currency - In thousands of Turkish Lira ("TL"))

	Note	2018	2017
Interest income	*27*	1,332,923	1,021,509
Interest expense	*27*	(907,349)	(450,990)
Net interest income		**425,574**	**570,519**
Fees and commission income	*28*	176,018	248,439
Fees and commission expense	*28*	(77,404)	(73,657)
Net fee and commission income		**98,614**	**174,782**
Net trading gain/loss	*29*	(10,442)	(38,740)
Sales income	*30*	589,303	407,270
Other income	*31*	179,300	82,370
Other expenses	*35*	-	(140,000)
Net impairment loss on financial assets	*14,32*	(31,341)	(55,362)
Operating expenses		(422,916)	(402,446)
- Personnel expenses	*33*	(176,726)	(166,246)
-Depreciation and amortisation	*16,17*	(45,490)	(71,624)
-Administrative expenses	*34*	(200,700)	(164,576)
Cost of sales		(184,091)	(65,794)
Cost of services	*30*	(100,387)	(170,031)
Other operating expenses	*35*	(57,161)	(61,956)
Total operating income		**486,453**	**300,612**
Share of profit of equity accounted investee	*15*	(6,003)	10,153
Profit before income tax		**480,450**	**310,765**
Income tax expense	*23*	(98,778)	(76,938)
Net profit for the year from continuing operations		**381,672**	**233,827**
Profit attributable to			
Equity holders of the Bank		378,291	231,726
Non-controlling interest		3,381	2,101
Profit for the year		**381,672**	**233,827**
Other comprehensive income			
Items that will not be reclassified to profit or loss:		**909**	**(577)**
Change in actuarial (loss) / gain related to employee benefits	*24*	1,166	(721)
Tax effect	*23*	(257)	144
Items that are or may be reclassified subsequently to profit or loss:		**(21,004)**	**6,378**
Change in fair value of financial assets measured at fair value through other comprehensive income		(30,526)	-
Change in fair value of available-for-sale financial assets		-	5,539
Foreign currency translation differences		2,699	1,947
Special fund		137	-
Income tax on other comprehensive income	*23*	6,686	(1,108)
Other comprehensive income for the year, net of tax		**(20,095)**	**5,801**
Total comprehensive income for the year		**361,577**	**239,628**
Total comprehensive income attributable to:			
Equity holders of the Bank		358,196	237,527
Non-controlling interest		3,381	2,101
Total comprehensive income for the year		**361,577**	**239,628**
Basic and diluted earnings per share (full TL amount per TL 1 face value each)		0.317	0.224

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity
For the Year Ended 31 December 2017
(Currency - In thousands of Turkish Lira ("TL"))

	Note	Share capital	Adjustment to share capital	Legal reserves	Unrealised gains/(losses) on available-for-sale assets	Translation reserve	Actuarial gain/(loss)	Special Funds	Retained earnings	Total	Non-controlling interest	Total equity
At 1 January 2017		**933,585**	**4,510**	**24,237**	**(23,011)**	**(2,356)**	**441**	**618**	**36,498**	**974,522**	**9,100**	**983,622**
Total comprehensive income for the year												
Profit for the year		-	-	-	-	-	-	-	231,726	231,726	2,101	233,827
Other comprehensive income		-	-	-	4,431	1,947	(577)	-	-	5,801	-	5,801
Net change in fair value of available-for-sale financial assets		-	-	-	*4,431*	-	-	-	-	*4,431*	-	*4,431*
Net change in actuarial gain related to employee benefits		-	-	-	-	-	*(577)*	-	-	*(577)*	-	*(577)*
Foreign currency translation differences		-	-	-	-	*1,947*	-	-	-	*1,947*	-	*1,947*
Total comprehensive income for the year		**-**	**-**	**-**	**4,431**	**1,947**	**(577)**	**-**	**231,726**	**237,527**	**2,101**	**239,628**
Transactions with owners, recorded directly in equity												
Capital increase		100,000	-	-	-	-	-	-	(100,000)	-	-	-
Transfer to reserves		-	-	14,106	-	-	-	-	(14,106)	-	-	-
Dividend paid		-	-	-	-	-	-	-	-	-	(300)	(300)
Total transactions with owners, recorded directly in equity		**100,000**	**-**	**14,106**	**-**	**-**	**-**	**-**	**(114,106)**	**-**	**(300)**	**(300)**
At 31 December 2017	**26**	**1,033,585**	**4,510**	**38,343**	**(18,580)**	**(409)**	**(136)**	**618**	**154,118**	**1,212,049**	**10,901**	**1,222,950**

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity
For the Year Ended 31 December 2018
(Currency - In thousands of Turkish Lira ("TL"))

	Note	Share capital	Adjustment to share capital	Legal reserves	Unrealised gain/(losses) on financial assets measured at fair value through other comprehensive income	Translation reserve	Actuarial gain/(loss)	Special funds	Retained earnings	Total	Non-controlling interest	Total equity
At 1 January 2018		**1,033,585**	**4,510**	**38,343**	**(18,580)**	**(409)**	**(136)**	**618**	**154,118**	**1,212,049**	**10,901**	**1,222,950**
Adjustment on initial application of IFRS 9, net of tax	*5*	-	-	-	-	-	-	-	(23,079)	(23,079)	-	(23,079)
Adjusted opening balance at 1 January 2018		**1,033,585**	**4,510**	**38,343**	**(18,580)**	**(409)**	**(136)**	**618**	**131,039**	**1,188,970**	**10,901**	**1,199,871**
Total comprehensive income for the year												
Profit for the year		-	-	-	-	-	-	-	378,291	378,291	3,381	381,672
Other comprehensive income		-	-	-	(23,810)	2,699	909	107	-	(20,095)	-	(20,095)
Net change in fair value of financial assets measured at fair value through other comprehensive income		-	-	-	*(23,810)*	-	-	-	-	*(23,810)*	-	*(23,810)*
Net change in actuarial gain related to employee benefits		-	-	-	-	-	*909*	-	-	*909*	-	*909*
Foreign currency translation differences		-	-	-	-	*2,699*	-	-	-	*2,699*	-	*2,699*
Other		-	-	-	-	-	-	*107*	-	*107*	-	*107*
Total comprehensive income for the year		**-**	**-**	**-**	**(23,810)**	**2,699**	**909**	**107**	**378,291**	**358,196**	**3,381**	**361,577**
Transactions with owners, recorded directly in equity												
Capital increase		160,000	-	-	-	-	-	-	(147,000)	13,000	654	13,654
Transfer to reserves		-	-	18,010	-	-	-	36,387	(54,397)	-	-	-
Dividend paid		-	-	-	-	-	-	-	-	-	(1,000)	(1,000)
Total transactions with owners, recorded directly in equity		**160,000**	**-**	**18,010**	**-**	**-**	**-**	**36,387**	**(201,397)**	**13,000**	**(346)**	**12,654**
At 31 December 2018	**26**	**1,193,585**	**4,510**	**56,353**	**(42,390)**	**2,290**	**773**	**37,112**	**307,933**	**1,560,166**	**13,936**	**1,574,102**

Consolidated Statement of Cash Flows
For the Year Ended 31 December 2018

(Currency - In thousands of Turkish Lira ("TL"))

	Note	2018	2017
Cash flows from operating activities			
Net profit for the year		381,672	233,827
Adjustments for:			
Depreciation and amortisation expenses	16,17	45,690	72,336
Retirement pay provision expense	24	2,985	2,579
Unused vacation provision expense		275	1,091
Bonus provision expense		52,279	19,051
Impairment on financial assets	32	31,341	55,362
Net interest income and expense		(467,560)	(534,296)
Share of profit of equity investee	15	6,003	(10,153)
(Reversal) / provision for possible losses	24	(37,000)	140,000
Unrealised foreign exchange loss / (gain)		(894,143)	(317,997)
Gain on sale of assets	31	(60,299)	(27,877)
Gain on sale of subsidiary	31	-	(43,232)
Other accruals		1,487	69,177
Income tax	23	98,778	76,938
		(838,492)	**(263,194)**
Change in reserve deposit at Central Bank		(64,206)	(300,425)
Change in trading assets		(387,976)	(4,685)
Change in loans and advances to customers		332,726	(951,917)
Change in other assets		(292,456)	(26,731)
Change in obligations under repurchase agreements		214,648	311,900
Proceeds from borrowings		(196,520)	1,055,273
Change in other liabilities		730,557	305,242
		336,773	**388,657**
Interest received		1,291,152	1,036,074
Interest paid		(841,150)	(501,165)
Retirement pay provision and unused vacation paid	24	(1,922)	(2,052)
Bonus payment		(37,390)	(19,051)
Income tax paid	23	(81,325)	(79,309)
Net cash used in operating activities		**329,365**	**434,497**
Cash flows from investing activities			
Purchase of investment securities		(7,271,391)	(2,507,415)
Sale of investment securities		6,519,266	2,083,077
Purchase of tangible assets	16	(421,612)	(11,788)
Equity accounted investees	15	(50)	(19,149)
Proceeds from the sale of tangible assets		244,200	68
Proceeds from the sale of subsidiary		-	50,000
Purchase of intangible assets	17	(29,370)	(19,376)
Acquisition of subsidiaries	38	(12,379)	-
Proceeds from the sale of intangible assets	17	-	899
Net cash used in investing activities		**(971,336)**	**(423,684)**
Cash flows from financing activities			
Proceeds from debt securities issued		35,982,068	23,692,443
Repayment of debt securities issued		(34,475,727)	(24,070,901)
Change in financial lease liabilities		(16,242)	(17,281)
Net cash provided from financing activities		**1,490,099**	**(395,739)**
Net increase/(decrease) in cash and cash equivalents		**346,409**	**(259,463)**
Effect of exchange rate fluctuations on cash	10	311,025	(668)
Cash and cash equivalents on 1 January	10	726,952	987,083
Cash and cash equivalents on 31 December	**10**	**1,384,386**	**726,952**

The accompanying notes are an integral part of these consolidated financial statements.

(Currency - In thousands of Turkish Lira ("TL"))

Notes to the consolidated financial statements

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(Currency - In thousands of Turkish Lira (“TL”))

1. Reporting entity

Aktif Yatırım Bankası Anonim Şirketi (‘‘the Bank”) was incorporated under the name of Çalık Yatırım Bankası A.Ş. in Turkey in July 1999. The Bank changed its name as Aktif Yatırım Bankası A.Ş. on 1 August 2008.

The Bank operates as an investment bank and is mainly involved in corporate and consumer services such as cash or non-cash, financial leasing, factoring, corporate lending. As an investment bank, the Bank borrows funds from other banks, financial markets, partners and credit customers but is not entitled to receive deposits from customers.

The head office of the Bank is located at Büyükdere Cad. No: 163/A Zincirlikuyu / İstanbul, and the Bank have also ten branches. The Bank employs 663 people as at 31 December 2018 (31 December 2017: 656).

As at 31 December 2018 and 2017, the composition of shareholders and their respective percentage of ownership are summarised as follows:

	31 December 2018		31 December 2017	
	Amount	**%**	**Amount**	**%**
Çalık Holding A.Ş.	1,186,791	99.43	1,027,636	99.42
Çalık Denim Tekstil San. ve Tic. A.Ş.	3,597	0.30	3,149	0.30
Ahmet Çalık	1,599	0.13	1,400	0.14
Başak Yönetim Sistemleri A.Ş.	799	0.07	700	0.07
Irmak Yönetim Sistemleri A.Ş.	799	0.07	700	0.07
Total paid-in-capital	**1,193,585**	**100.00**	**1,033,585**	**100.00**
Restatement effect per IAS 29	4,510		4,510	
Total share capital	**1,198,095**		**1,038,095**	

The Bank and its subsidiaries are hereafter referred to as ‘‘the Group”. The Group controls equity stakes in companies that are active in the areas of technology system integration, payment centre, insurance brokerage, consulting in real estate projects, real estate, Islamic financial leasing and electronic payment systems. Activities carried out in these business areas and main companies are explained below in summary.

Sigortayeri Sigorta ve Reasürans Brokerliği A.Ş.: Sigortayeri.com is an online insurance comparison website which ensures the best match between insurance products and customer needs in minutes. Operating across the global market since 2013, Sigortayeri has differentiated its corporate insurance services under the brand of “Asron Sigorta” since May 2017.

EPost Elektronik Perakende Otomasyon Satış Ticaret A.Ş.: Epost operates as a retail vendor sales channel and provides secured devices that businesses use in conducting sales and payments collection transactions.

E-Kent Teknoloji ve Ödeme Sistemleri Sanayi ve Ticaret A.Ş.: E-Kent is a technology integrator offering smart city solutions to provide infrastructural transformation and introduces value added profitable business models. In addition, as a result of the tender performed by Turkey Football Federation (TFF) in 2013, the Company is appointed as ‘E-Ticket System Integrator’ and realized the world's largest stadium transformation project including infrastructure transformation in 50 stadiums in 27 different cities, access control and monitoring systems, centralized integrated ticketing and stadium box office services infrastructure.

Pavo Teknik Servis Elektrik Elektronik Sanayi ve Ticaret A.Ş.: With its long-standing experience in cash register systems, Pavo offers local and foreign customers a solution in the field of payment systems, especially in financial approved cash registers (New Generation Payment Recorder).

1. Reporting entity *(continued)*

N Kolay Ödeme Kuruluşu A.Ş.: N Kolay is the biggest payment institution in Turkey by volume. N Kolay business model mainly focuses on bill payment, money transfers and other financial services.

Emlak Girişim Danışmanlığı A.Ş.: Emlak Girişim works on real estate projects, structures and systems, and makes active counselling and guidance.

İFM İstanbul Finans Merkezi İnşaat Taahhüt A.Ş.: İFM operates in special projects, land recreation, area sales and revenue sharing provisions for the immovable construction, construction and sales activity is independent sections.

Euroasian Leasing Company: ELC is the first in Russia to provide leasing solutions to the SME sector in accordance with the Islamic principles.

Kazakhstan Ijara Company Jsc.: KIC carries on Islamic leasing business. The aim of firm in Kazakhstan is to support the development of small and medium enterprises (SMEs) by providing alternative sources of Shariah compliant financing for their projects.

Euro Mediterranean Investment Company: EMIC is a real estate development and portfolio management company in North Cyprus.

UPT Ödeme Hizmetleri A.Ş.: UPT is Turkey's first and only local, global money transfer and payment platform for domestic and international transfers to account, credit cards or for cash payments in multiple currencies.

Mükafat Portföy Yönetimi A.Ş.: Mükafat strives to carve out a niche for itself with its alternative investment products such as Private Equity Funds and Real Estate Funds. Mükafat is also managing Mutual Funds as well as Pension Funds.

Haliç Finansal Kiralama A.Ş.: Being the first financial leasing company offering Islamic products to its customers in Turkey, Haliç develops customer-tailored development packages for its customers, especially SMEs, as well as financing options in order to provide support to their investments in technological machines and equipment. Haliç aims to bring long-term resources to Turkey from the Gulf and Asian countries through Sukuk issues by leveraging on Aktif Bank's knowledge in capital markets.

Aktif Halk Enerji Yatırımları A.Ş.: The company, which was established in April 2017, makes investments in the field of solar energy production.

Halk Yenilenebilir Enerji A.Ş.: The company, which was established in April 2017, is engaged in the construction of solar energy production facilities.

Epost Dış Ticaret A.Ş.: The company will engage in the trade of all kinds of different products that are valued in the world market such as basic needs of countries. EP Dış Ticaret which intends to conduct Turkey as a main hub aims to bring together trade facilities whether inside Turkey or different suppliers and sales opportunities. The Company provides structural trade finance models that make domestic production to reach wide geographies all around the World, being a bridge between different countries and regions.

Eko Biokütle Enerji Üretim A.Ş.: The company will establish two biomass power plants with a capacity of 10 MW in Şanlıurfa for the production of electricity from the cotton stalk within the scope of the electricity generation support of YEKDEM regulation – no: 5346 which entitles the company to sell the electricity by $13.3 cent per kWh for electricity generation from biomass through 10 years.

2. Basis of preparation

2.1 Statement of compliance

The Bank and its subsidiaries operating in Turkey maintain their books of account and prepare their statutory consolidated financial statements in Turkish Lira ("TL") in accordance with the accounting principles as promulgated by the Banking Regulation and Supervision Agency ("BRSA"), Turkish Accounting Standards promulgated by the Public Oversight Accounting and Auditing Standards Authority, Capital Markets Board of Turkey, the Turkish Commercial Code and tax legislation. The foreign subsidiaries maintain their books of account in accordance with the laws and regulations in force in the countries in which they are registered. The accounting policies and valuation principles applied in the preparation of financial statements are determined and applied in accordance with principles in the context of IAS and IFRS.

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") and its interpretations adopted by the International Accounting Standards Board ("IASB"). The consolidated financial statements were authorised for issue by the Group's management on 29 March 2019. The Bank's General Assembly and the other reporting bodies have the power to amend the consolidated financial statements after their issue.

This is the first set of the Group's annual financial statements in which IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers have been applied. In accordance with the transition rules of IFRS 9, the prior period financial statements and notes are not restated. Accounting policies and valuation principles used for the year 2018 and 2017 periods are separately presented in the footnotes.

IFRS 15 Revenue from contracts with customers standard provides single and comprehensive model and guidance regarding recognition of revenue and replaces IAS 18 Revenue standard. The standard is in effect starting from 1 January 2018 and does not have significant impact on the accompanying consolidated financial statements.

The Bank's adoption process continues regarding IFRS 16 Leases ("IFRS 16") which will be in effect starting from 1 January 2019.

2.2 Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis as adjusted for the effects of inflation, except for the following:

- derivative financial instruments are measured at fair value
- financial assets measured at fair value through profit or loss
- financial assets measured at fair value through other comprehensive income

2.3 Functional and presentation currency

These consolidated financial statements are presented in TL, which is the Bank's functional currency. Except as indicated, financial information presented in TL has been rounded to the nearest thousand.

2.4 Use of estimates and judgements

The preparation of the consolidated financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. In preparing these consolidated financial statements, the significant judgements made by management in applying the Bank's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the consolidated financial statements as at 31 December 2017.

The accounting policies set out below have been applied consistently by the Bank and its subsidiaries to prior periods presented in these consolidated financial statements except for the impact of transition to IFRS 9 and IFRS 15 as of 1 January 2018 as explained below.

2. Basis of preparation *(continued)*

2.5 Earnings per share

In Turkey, companies can increase their share capital by making a pro-rata distribution of shares ("bonus shares") to existing shareholders from retained earnings. For the purpose of earnings per share computations, the weighted average number of shares outstanding during the year has been adjusted in respect of bonus shares issued without a corresponding change in resources by giving them a retroactive effect for the year in which they were issued and for each earlier period.

There is no bonus share issuance as at 31 December 2018 (31 December 2017: None).

3. Significant accounting policies

3.1 Accounting in hyperinflationary economies

The consolidated financial statements of the Turkish entities have been restated for the changes in the general purchasing power of the Turkish Lira based on International Accounting Standard ("IAS") No. 29 "Financial Reporting in Hyperinflationary Economies" as at 31 December 2005. IAS 29 requires that consolidated financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current on the reporting date, and that corresponding figures for prior periods be restated in the same terms. One characteristic that necessitates the application of IAS 29 is a cumulative three-year inflation rate approaching or exceeding 100%. The cumulative three-year inflation rate in Turkey has been 35.61% as at 31 December 2005, based on the Turkish nation-wide wholesale price indices announced by the Turkish Statistical Institute ("TURKSTAT"). By taking this into consideration, together with the sustained positive trend in quantitative factors, such as the stabilisation in financial and monetary markets, decrease in interest rates and the appreciation of TL against USD and other hard currencies, it was declared that Turkey should be considered a non-hyperinflationary economy under IAS 29 from 1 January 2006 as stated in International Standards Alert No. 2006/17 issued on 8 March 2006. Therefore, IAS 29 has not been applied to the accompanying consolidated financial statements starting from 1 January 2006.

3.2 Foreign currency transactions

Foreign currency transactions

Transactions in the financial statements of the Group are recorded in TL, which is the Bank's functional currency and the presentation currency for the accompanying consolidated financial statements. Transactions in foreign currencies are translated into the functional currency of the Group at exchange rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into TL at the exchange rates ruling at date of the statement of financial position with the resulting exchange differences recognized in income as foreign exchange gain or loss. Gains and losses arising from foreign currency transactions are reflected in income as realized during the period.

Financial statements of foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to TL at foreign exchange rates ruling at the date of the statement of financial positions. The revenues and expenses of foreign operations are translated to TL using average exchange rates. Foreign exchange differences arising on translation are recognized directly in a separate component of equity. When a foreign operation is disposed of in part or in full, the relevant amount in the foreign currency translation reserve is transferred to profit or loss.

3. Significant accounting policies *(continued)*

3.3 Basis of consolidation

Subsidiaries

The consolidated financial statements incorporate the consolidated financial statements of the Bank and entities controlled by the Bank. The control exists if and only if; 1) when the Bank has the power over an affiliate which that power, directly or indirectly, give rights to govern the financial and operating policies of the entity so as to obtain benefits from its activities, 2) exposure, or rights, to variable returns from its involvement with the affiliate, 3) the ability to use its power over the affiliate to affect the amount of its returns. The Bank reassess its control power over its subsidiaries if there is an indication that there are changes to any of the three elements of control.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated statement of income from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Business combinations

The Group accounts for business combinations using the acquisition method when control is transferred to the Group.

The Group measures goodwill at the acquisition date as:

- the fair value of the consideration transferred; plus
- the recognised amount of any non-controlling interests in the acquiree; plus
- if the business combination is achieved in stages, the fair value of the pre-existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the excess is negative, a bargain purchase gain is recognised immediately in profit or loss. The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts generally are recognised in profit or loss.

Transactions costs, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination are expensed as incurred.

Any contingent consideration payable is measured at fair value at the acquisition date. If the contingent consideration is classified as equity, it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognised in profit or loss.

Interests in equity-accounted investees

The Group's interests in equity-accounted investees comprise interests in associates and joint ventures. Associates are those entities in which the Group has significant influence, but not control or joint control, over the financial and operating policies. A joint venture is an arrangement in which the Group has joint control, whereby the Group has rights to the net assets of the arrangement, rather than rights to its assets and obligations for its liabilities.

Interests in associates and the joint ventures are accounted for using the equity method. They are recognised initially at cost, which includes transaction costs. Subsequent to initial recognition, the consolidated financial statements include the Group's share of the profit or loss and other comprehensive income of equity-accounted investees, until the date on which significant influence or joint control ceases.

3. Significant accounting policies *(continued)*

3.3 Basis of consolidation *(continued)*

Non-controlling interests

Non-controlling interests are measured at their proportionate share of the acquiree's identifiable net assets at the acquisition date. Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

Loss of control

When the Group loses control over a subsidiary, it derecognises the assets and liabilities of the subsidiary, and any related non-controlling interests and other components of equity. Any resulting gain or loss is recognised in profit or loss. Any interest retained in the former subsidiary is measured at fair value when control is lost.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated. Unrealised gains arising from transactions with equity-accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Acquisitions from entities under common control

Business combinations arising from transfers of interests in entities that are under the control of the shareholder that controls the Group are accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date that common control was established. The assets and liabilities acquired are recognised at the carrying amounts recognised previously in the controlling shareholder's consolidated financial statements. The components of equity of the acquired entities are added to the same components within the Group equity and any gain/loss arising is recognised directly in equity.

(Currency - In thousands of Turkish Lira ("TL"))

3. Significant accounting policies *(continued)*

3.3 Basis of consolidation *(continued)*

Group entities

Subsidiaries	Country of Incorporation	Direct ownership 31 December 2018	Direct ownership 31 December 2017	Indirect ownership 31 December 2018	Indirect ownership 31 December 2017
Insurance Brokerage					
Sigortayeri Sigorta ve Reasürans Brokerliği A.Ş.	Turkey	100.00%	100.00%	-	-
Payment Systems					
Epost Elektronik Perakende Otomasyon Satış Tic. A.Ş.	Turkey	99.27%	99.27%	-	-
E-Kent Teknoloji ve Ödeme Sistemleri San ve Tic. A.Ş.	Turkey	-	-	99.27%	99.27%
N Kolay Mağazacılık A.Ş.	Turkey	99.99%	99.99%	-	-
UPT Ödeme Hizmetleri A.Ş.	Turkey	100.00%	100.00%	-	-
Real Estate					
Emlak Girişim Danışmanlığı A.Ş.	Turkey	100.00%	100.00%	-	-
Service					
Pavo Teknik Servis Elektrik Elektronik Sanayi ve Ticaret A.Ş.	Turkey	-	-	79.42%	79.42%
Mükafat Portföy Yönetimi A.Ş.	Turkey	80.00%	80.00%	-	-
Solar Energy					
Albatros Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Kamelya Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Kırlangıç Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Çöl Yıldızı Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Deniz Yıldızı Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
İpek Güneş Enerjisi Üretimi A.Ş.	Turkey	-	-	100.00%	-
Esen Güneş Enerjisi Üretimi A.Ş.	Turkey	-	-	100.00%	-
Mehtap Güneş Enerjisi Üretim A.Ş.	Turkey	-	-	100.00%	-
Tanyeri Güneş Enerjisi Üretim A.Ş.	Turkey	-	-	100.00%	-
Seher Güneş Enerjisi Üretimi A.Ş.	Turkey	-	-	100.00%	-
Ufuk Güneş Enerjisi Üretim A.Ş.	Turkey	-	-	100.00%	-
Yakamoz Güneş Enerjisi Üretim A.Ş.	Turkey	-	-	100.00%	-
Duru Güneş Enerjisi Üretimi A.Ş.	Turkey	-	-	100.00%	-
Deniz Güneş Enerjisi Üretimi A.Ş.	Turkey	-	-	100.00%	-
Pasifik Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Olimpos Solar Enerji Üretım A.Ş.	Turkey	-	-	100.00%	-
Yakut Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Seher Yıldızı Solar Enerji Üretim A.Ş.	Turkey	-	-	100.00%	-
Kuzey Yıldızı Solar Enerji Üretim A.Ş.	Turkey	-	-	100.00%	-
Gök Safir Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Kızıl Yıldızı Solar Enerji Üretim A.Ş.	Turkey	-	-	100.00%	-
Kasımpatı Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Martı Solar Enerji Üretim A.Ş	Turkey	-	-	100.00%	-
Nilüfer Solar Enerji Üretim A.Ş.	Turkey	-	-	100.00%	-
Mercan Solar Enerji Üretim A.Ş.	Turkey	-	-	100.00%	-
Other					
İnovaban İnovasyon ve Finansal Danışmanlık A.Ş.	Turkey	-	-	67.00%	-
Attivo Bilişim Anonim Şirketi	Turkey	-	-	90.00%	-
Epost Dış Ticaret Anonim Şirketi	Turkey	-	-	99.86%	-
Eko Biokütle Enerji Üretim A.Ş.	Turkey	-	-	100.00%	-

Equity accounted investees	Country of Incorporation	31 December 2018 Ownership	31 December 2017 Ownership
Kazakhstan Ijara Company Jsc	Kazakhstan	14.31%	14.31%
İFM İstanbul Finans Merkezi İnşaat Taahhüt A.Ş.	Turkey	5.00%	5.00%
Euroasian Leasing Company	Republic of Tatarstan	36.71%	36.71%
Haliç Finansal Kiralama Anonim Şirketi	Turkey	32.00%	32.00%
Aktif Halk Enerji Yatırımları Anonim Şirketi	Turkey	50.00%	50.00%
Halk Yenilenebilir Enerji Anonim Şirketi	Turkey	50.00%	50.00%
Soleren S4 Enerji Üretim Anonim Şirketi	Turkey	-	50.00%
Euro Mediterianean Investment Company	Turkish Republic of Northern Cyprus	25.53%	25.53%

3. Significant accounting policies *(continued)*

3.4 Interest income / expense

Interest is recorded according to the effective interest rate method (rate equal to the rate in calculation of present value of future cash flows of financial assets or liabilities) defined in the IFRS 9 Financial instruments standard by applying the effective interest rate to the gross carrying amount of a financial asset except for: purchased or originated credit-impaired financial assets or financial assets that are not purchased or originated credit-impaired financial assets but subsequently have become credit-impaired financial assets. In applying the effective interest method, an entity identifies fees that are an integral part of the effective interest rate of a financial instrument. Fees that are an integral part of the effective interest rate of a financial instrument are treated as an adjustment to the effective interest rate, unless the financial instrument is measured at fair value, with the change in fair value being recognised in profit or loss. In those cases, such fees are accounted as revenue or expense when the instrument is initially recognised in the financial statements.

When applying the effective interest method, it is amortised any fees, transaction costs and other premiums or discounts that are included in the calculation of the effective interest rate over the expected life of the financial instrument.

In case an interest was accrued on a security before its acquisition, the collected interest is divided into two parts as interest before and after the acquisition and only the interest income of the period after the acquisition is recorded as interest income in the financial statements.

If the expectations for the cash flows in the financial asset are revised for reasons other than the credit risk, the amendment is reflected in the carrying amount of the asset and in the related statement of profit or loss and other comprehensive income line and is amortised over the estimated life of the financial asset.

If the financial asset is impaired and classified as a non-performing receivable, the effective interest rate is applied to the amortized cost of the asset for subsequent reporting periods. Such interest income calculation is performed on an individual contract basis for all financial assets subject to impairment calculation. The effective interest rate is used for the calculation of loss given default parameter in the expected credit loss models and therefore the calculated expected credit losses, includes this calculated interest amount. Accordingly a reclassification is performed between the accounts of "expected credit losses" expense and "interest income from loans" for such calculated interest amount. If the credit risk of the financial instrument improves to the extent that the financial asset is no longer considered as impaired and the improvement can be attributed to an incident that eventually takes place (such as an increase in the loan's credit rating), the system calculates interest income at subsequent reporting periods by applying the effective interest rate to the gross amount.

3.5 Fees and commission

Fees and commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income are recognised as the related services are provided.

Other fees and commission expense relates mainly to transaction and service fees, which are expensed as the services are received.

3.6 Net trading income

Net trading income/(expense) includes gains and losses arising from sale of financial assets measured at fair value through profit or loss (FVPL) and through other comprehensive income (FVOCI) in addition to changes in fair value of financial assets measured at FVPL and derivatives.

3.7 Dividends

Dividend income is recognised when the right to receive income is established.

3. Significant accounting policies *(continued)*

3.8 Lease payments made

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent lease payments are accounted for by revising the minimum lease payments over the remaining term of the lease when the lease adjustment is confirmed.

3.9 Other operations revenue

Group recognises revenue based on the following five principles in accordance with the TFRS 15, "Revenue from Contracts with Customers Standard" effective from 1 January 2018:

- Identification of customer contracts
- Identification of performance obligations
- Determination of the transaction price in the contracts
- Allocation of transaction price to the performance obligations
- Recognition of revenue when the performance obligations are satisfied

Group evaluates each contracted obligation separately and respective obligations, committed to deliver the distinct goods or perform services, are determined as separate performance obligations.

Group determines at contract inception whether the performance obligation is satisfied over time or at a point in time. When the Group transfers control of a good or service over time, and therefore satisfies a performance obligation over time, then the revenue is recognised over time by measuring the progress towards complete satisfaction of that performance obligation.

When a performance obligation is satisfied by transferring promised goods or services to a customer, the Group recognises the revenue as the amount of the transaction price that is allocated to that performance obligation. The goods or services are transferred when the control of the goods or services is delivered to the customers.

Following indicators are considered while evaluating the transfer of control of the goods and services:

a) presence of Group's collection right of the consideration for the goods or services,

b) customer's ownership of the legal title on goods or services,

c) physical transfer of the goods or services,

d) customer's ownership of significant risks and rewards related to the goods or services,

e) customer's acceptance of goods or services.

If Group expects, at contract inception, that the period between when the Group transfers a promised good or service to a customer and when the customer pays for that good or service will be one year or less, the promised amount of consideration for the effects of a significant financing component is not adjusted. On the other hand, when the contract effectively constitutes a financing component, the fair value of the consideration is determined by discounting all future receipts using an imputed rate of interest. The difference between the fair value and the nominal amount of the consideration is recognised on an accrual basis as other operating income.

3. Significant accounting policies *(continued)*

3.10 Financial assets and liabilities

Recognition

The Bank initially recognises loans and advances to customers, investment securities, funds borrowed, customer accounts and debt securities issued on the date that they are originated. Regular way purchases and sales of financial assets are recognised on the trade date at which the Bank commits to purchase or sell the asset. All other financial assets and liabilities are initially recognised on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

Derecognition

The Bank derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Bank is recognised as a separate asset or liability.

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

Offsetting

Financial assets and liabilities are set off and the net amount presented in the statement of financial position when, and only when, the Bank has a legal right to set off the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Group measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Group uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

3. Significant accounting policies *(continued)*

3.10 Financial assets and liabilities *(continued)*

Fair value measurement

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Group determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognized in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

The Group recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

Derivative financial instruments

The Group enters into transactions with derivative instruments including forwards, swaps, currency options and interest rate cap/floor agreements in the foreign exchange and capital markets. Most 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 International Accounting Standard 39 – Financial instruments: Recognition and measurement (“IAS 39”), they are treated as derivatives held for trading. IFRS 9 also includes new hedge accounting rules aiming alignment with risk management activities. IFRS 9 permits to defer application of IFRS 9 hedge accounting and continue to apply hedge accounting provisions of IAS 39 as a policy choice. Derivative financial instruments are initially recognised at fair value on the date which a derivative contract is entered into and subsequently remeasured at fair value. Any gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are recognised in profit or loss.

Fair values are obtained from quoted market prices in active markets, including recent market transactions, to the extent publicly available, and valuation techniques, including discounted cash flow models and options pricing models as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Identification and measurement of impairment

As of 1 January 2018, the Group recognizes provisions for impairment in accordance with IFRS 9 requirements. In this framework, as of 31 December 2017, method of provisions for impairment is changed by applying the expected credit loss model under 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. The Group calculates expected credit losses based on a probability-weighted estimate of credit losses (i.e. the present value of all cash shortfalls) over the expected life of the financial instrument. A cash shortfall is the difference between the cash flows that are due based on the contract and the cash flows that are expected to be received.

Probability of Default (PD): PD refers to the likelihood that a loan will default within a specified time horizon, which is usually set at 12 months, given certain characteristics. The Group uses two different probability of default rates while calculating expected credit losses as per the IFRS 9.

- 12-month PD: as the estimated probability of default occurring within the next 12 months (or over the remaining life of the financial instrument if that is less than 12 months) following the balance sheet date.

- Lifetime PD: as the estimated probability of default occurring over the remaining life of the financial instrument.

3. Significant accounting policies *(continued)*

3.10 Financial assets and liabilities *(continued)*

Identification and measurement of impairment (continued)

Loss Given Default (LGD): If a loan default occurs, it represents the economic loss incurred on the loan. It is expressed as a percentage.

Exposure at Default (EAD): For cash loans, it corresponds to the amount of loan granted as of the reporting date. For non-cash loans and commitments, it is the value calculated through using credit conversion factors. Credit conversion factor corresponds to the factor which adjust the potential increase of the exposure between the current date and the default date.

Stage 1: For the financial assets at initial recognition or that do not have a significant increase in credit risk since initial recognition. Impairment for credit risk is recorded in the amount of 12-month expected credit losses.

Stage 2: Includes financial assets which have a significant increase in credit risk since initial recognition but an unbiased evidence does not occur. Lifetime expected credit losses are recognized for these financial instruments.

Stage 3: Stage 3 includes financial assets that have objective evidence of impairment at the reporting date. For these assets, lifetime expected credit losses are recognized and interest revenue is calculated on the net carrying amount.

Rating system for corporate loans

Internal credit risk assessment system of the Bank grades loans in 12 categories in the wide range from the highest (AAA) to the lowest (D3).

The Bank utilizes an internal rating system, which is based on quantitative and qualitative data. Rating table for each customer is prepared annually by CRM and reviewed by the Credit Allocation Department based on year-end financials and updated information.

For Financial Risks (objective) the company can get maximum 70 points and for Business and Sector Risks (subjective) maximum 30 points, respectively. Financial risk is assessed considering financial indicators and ratios like equity strength, profitability, liquidity and profit margins. On the other hand, business risk is freely evaluated by the rater based on information available, intelligence and track record of the company and owners. Market position, prospects for growth, as well as ownership strength is appraised. These soft and hard facts lead us to reach final "Risk Rating" of the company.

Equity structure, profitability and liquidity are the basic parameters that affect financial risk (objective). Indebtedness, profitability and rational equity structure analysis are evaluated by means of 12 financial ratios which have 30 % effect on rating calculation. For the purpose of evaluating trend analysis based on company's financial statements, 21 ratios are calculated which have 30 % effect on rating calculation. Foreign currency position and effect on equity thereof are evaluated by means of 3 ratios which have 10 % effect on rating calculation.

Sector, shareholder's financial power, institutionalization and intelligence records are the parameters that affect business risk (subjective). Business risk is evaluated by means of 19 questions. Corporate branch executives are responsible for answering aforementioned questions accurately. As for financial statement analysis, Independent Auditor's Reports or Corporate Tax Declaration Reports (balance sheet and income statement) are taken into consideration. Financial statements of last 3 periods are evaluated and trend of financial structure in the course of these periods is taken into consideration.

3. Significant accounting policies *(continued)*

3.10 Financial assets and liabilities *(continued)*

Identification and measurement of impairment (continued)

Rating system for consumer loans (continued)

There is a comprehensive rule-based systematic infrastructure in personal loan. In this structure, besides the KKB (Credit Bureau) information, the customer's demographic information, employment information, risk center data, bank database information etc. is also used.

The structure, which includes rule-based and comprehensive strategy trees, enables the implementation of more common policy rules. A scorecard structure which works with Cut-off logic is only included in the N Kolay Personal Loans which is given by the digital channel, but not preferred in the application of PTT and Dealer loans.

PTT Retirement Loans are a credit system based on automatic collection from pension, therefore the systems have been developed especially to guarantee the collection process from the salary and prevent the customer from borrowing more than the amount of pension.

The credit policy in dealer loans is carried out with the parameters that show up as a result of the product type, distributor credit quality and dealer risk assessment and the credit policy to evaluate the customer is determined as one of the more flexible, stiffer or the most stringent policies.

In addition, the risk measurement of policy trees and rules is reviewed and analyzed as necessary, with the rejection / gray area / automatic approval rules and performance trees for all credit products being reviewed at least once a year.

The scorecard system for the digital channel -which includes N Kolay Personal Loans that receives too many loan applications-, was started in 2017 and validation will be completed in April 2019 when the portfolio matures enough.

Forward-looking macroeconomic information

The Bank incorporates forward-looking macroeconomic information when assessing the significant increase in credit risk and expected credit loss calculation.

Significant increase in credit risk

In the event of a significant increase in credit risk, the financial asset is transferred to Stage 2.

Qualitative and quantitative considerations taken into determining the significant increase in the credit risk of a financial asset as follows;

- Delay days as of the reporting date is 30 or more
- Refinancing and restructuring the credit account
- Loans under close monitoring
- Significant increase in probability of default.

Definition of the significant increase in the probability of default, the comparison of the probability of default at the opening date of the loan with the probability of default at the reporting date. If the probability of default calculated for the loan at the reporting date exceeds the set thresholds, it is considered to be a deterioration of the probability of default. The thresholds used in the probability of default are differentiated on the basis of segment/credit group.

3. Significant accounting policies *(continued)*

3.10 Financial assets and liabilities *(continued)*

Identification and measurement of impairment (continued)

Definition of default

The Group considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Group in full;
- the borrower is more than 90 days past due on any material credit obligation to the Group. Overdrafts are considered as being past due once the customer has breached an advised limit or been advised of a limit smaller than the current amount outstanding; or
- it is becoming probable that the borrower will restructure the asset as a result of bankruptcy due to the borrower's inability to pay its credit obligations.

In assessing whether a borrower is in default, the Group considers indicators that are:

- qualitative: e.g. breaches of covenant;
- quantitative: e.g. overdue status and non-payment on another obligation of the same issuer to the Group; and
- based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

3.11 Cash and cash equivalents

Cash and cash equivalents include cash on hand, unrestricted balances with Central Bank and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments.

When the Bank purchases a financial asset and simultaneously enters into an agreement to resell the asset (or a substantially similar asset) at a fixed price on a future date ("reverse repo or stock borrowing"), the arrangement is accounted for as cash and cash equivalents, and the underlying asset is not recognised in the Bank's consolidated financial statements. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

3.12 Explanations and disclosures on financial assets

The Group categorizes and recognizes its financial assets as "Financial Assets at Fair Value through Profit/Loss", "Financial Assets Measured at Fair Value through Other Comprehensive Income" or "Financial Assets at Measured at Amortized Cost". Such financial assets are recognized or derecognized according to IFRS 9 Financial Instruments. Financial assets are measured at fair value at initial recognition in the financial statements. During the initial recognition of financial assets other than "Financial Assets Measured at Fair Value through Profit or Loss", transaction costs are added to fair value or deducted from fair value.

The Group recognizes a financial asset into financial statements when it becomes a party to the contractual terms of a financial instrument. During the first recognition of a financial asset into the financial statements, business model determined by Group management and the nature of contractual cash flows of the financial asset are taken into consideration.

3. Significant accounting policies *(continued)*

3.12 Explanations and disclosures on financial assets *(continued)*

Financial assets measured at fair value through profit or loss

Financial assets at fair value through profit/loss” are financial assets other than the ones that are managed with business model that aims to hold to collect contractual cash flows or business model that aims to collect both the contractual cash flows and cash flows arising from the sale of the assets; and if the contractual terms of the financial asset do not lead to cash flows representing solely payments of principal and interest at certain date; that are either acquired for generating a profit from short term fluctuations in prices or are financial assets included in a portfolio aiming to short term profit making. Financial assets at the fair value through profit or loss are initially recognized at fair value and remeasured at their fair value after recognition. All gains and losses arising from these valuations are reflected in the income statement.

Financial assets measured at fair value through other comprehensive income

In addition to financial assets within a business model that aims to hold to collect contractual cash flows and aims to hold to sell, financial asset with contractual terms that lead to cash flows are solely payments of principal and interest at certain dates, they are classified as fair value through other comprehensive income.

Financial assets measured at fair value through other comprehensive income are recognized by adding transaction cost to acquisition cost reflecting the fair value of the financial asset. After the recognition, financial assets measured at fair value through other comprehensive income are remeasured at fair value. Interest income calculated with effective interest rate method arising from financial assets measured at fair value through other comprehensive income and dividend income from equity securities are recorded to income statement. “Unrealized gains and losses” arising from the difference between the amortized cost and the fair value of financial assets measured 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, and impairment of the asset and they are accounted under the “Accumulated other comprehensive income or expense to be reclassified through profit or loss” under shareholders’ equity.

Equity securities, which are classified as financial assets measured at fair value through other comprehensive income, are carried at fair value.

At initial recognition, it can be made an irrevocable election to present in other comprehensive income subsequent changes in the fair value of an investment in an equity instrument within the scope of IFRS 9 that is neither held for trading nor contingent consideration recognised by an acquirer in a business combination to which IFRS 3 applies. Such election is made on an instrument by instrument basis. Amounts presented in other comprehensive income shall not be subsequently recycled to profit or loss. However, the cumulative gain or loss shall be recycled to prior period’s profit or loss. Dividends on such investments are recognised in profit or loss unless the dividend clearly represents a recovery of part of the cost of the investment. IFRS 9 impairment requirements are not applicable for equity instruments.

3. Significant accounting policies *(continued)*

3.12 Explanations and disclosures on financial assets *(continued)*

Financial assets measured at amortized cost

Financial assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are classified as financial assets measured at amortized cost.

Financial assets measured at amortized cost are initially recognized at acquisition cost including the transaction costs which reflect the fair value of those instruments and subsequently recognized at amortized cost by using effective interest rate method. Interest income obtained from financial assets measured at amortized cost is accounted in income statement.

Loans

Loans are non-derivative financial assets that have fixed or determinable payments terms and are not quoted in an active market. Stated loans are initially recognized at acquisition cost plus transaction costs presenting their fair value and thereafter measured at amortized cost using the “Effective Interest Rate (internal rate of return) Method”.

The Group’s all loans are recorded under the “Measured at Amortized Cost” account.

3.13 Repurchase transactions

The Bank enters into purchases/sales of investments under agreements to resell/repurchase identical investments at a certain date in the future at a fixed price. Investments purchased subject to commitments to resell them at future dates are not recognised. The amounts paid are recognised as receivables from reverse repurchase agreements in the accompanying consolidated financial statements. The receivables are shown as collateralized by the underlying security. Investments sold under repurchase agreements continue to be recognised in the consolidated statement of financial position and are measured in accordance with the accounting policy for either assets held for trading, held to maturity or available-for-sale as appropriate. The proceeds from the sale of the investments are reported as obligations under repurchase agreements.

Income and expenses arising from the repurchase and resale agreements over investments are recognised on an accruals basis over the period of the transaction and are included in “interest income” or “interest expense”.

3.14 Trade receivables

Trade receivables that are created by way of providing goods or services directly to a debtor are carried at amortised cost. Trade receivables, net of unearned financial income, are measured at amortised cost, using the effective interest rate method, less the unearned financial income. Short duration receivables with no stated interest rate are measured at the original invoice amount unless the effect of imputing interest is significant.

As of 1 January 2018, the Group recognizes provisions for impairment in accordance with IFRS 9 requirements.

If the amount of the impairment subsequently decreases due to an event occurring after the write-down, the release of the provision is recognised in profit or loss.

3.15 Inventories

Inventories are valued at the lower of cost or net realisable value. Cost elements included in inventories are materials, labour and an appropriate amount for factory overheads. The cost of borrowings is not included in the costs of inventories. The cost of inventories is determined on the weighted average basis for each purchase. Net realisable value is the estimated selling price in the ordinary course of business, less the costs of completion and selling expenses. Inventories consist of raw material, semi-finished goods, finished goods, commercial goods and other stocks.

3. Significant accounting policies *(continued)*

3.16 Tangible assets

Recognition and measurement

Items of tangible assets are restated for the effects of inflation to 31 December 2005, less accumulated depreciation and impairment losses. Tangible assets acquired after 31 December 2005 is reflected at cost, less accumulated depreciation and impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset.

Subsequent costs

The cost of replacing part of an item of machinery or equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. The costs of the day-to-day servicing of tangible assets are recognised in profit or loss as incurred.

Depreciation

Depreciation is recognised in the profit or loss on a straight-line basis over the estimated useful lives of each part of an item of tangible assets. Leased assets are depreciated over the shorter of the lease term and their useful lives.

The estimated useful lives for as at 31 December 2018 and 2017 are as follows:

- machinery or equipment 3-25 years
- furniture and fixtures 2-60 years
- motor vehicles 5 years
- other fixed assets 2-50 years

Leasehold improvements are depreciated on a straight-line method over the shorter of the lease term and their useful lives.

3.17 Intangible assets

(i) Service agreements

Service agreements acquired in a business combination are recognised at fair value at the acquisition date. The service agreements have a finite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method over the expected life of the service agreements.

(ii) Software

Software acquired by the Bank is restated for the effects of inflation to 31 December 2005, less accumulated amortisation and impairment losses. Intangible assets acquired after 31 December 2005 are reflected at cost, less accumulated amortisation and impairment losses.

Expenditure on internally developed software is recognised as an asset when the Bank is able to demonstrate its intention and ability to complete the development and use the software in a manner that will generate future economic benefits, and can reliably measure the costs to complete the development. The capitalised costs of internally developed software include all costs directly attributable to developing the software, and are amortised over its useful life. Internally developed software is stated at capitalised cost less accumulated amortisation and impairment.

Subsequent expenditure on software assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

3. Significant accounting policies *(continued)*

3.17 Intangible assets *(continued)*

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful life of the software, from the date that it is available for use. The estimate useful life of software is 3 to 15 years.

(iii) Goodwill

Goodwill that arises upon the acquisition of subsidiaries the excess of the cost of the acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquiree. When the excess is negative (negative bargain), it is recognised immediately in profit or loss.

Acquisitions of non-controlling interests

Acquisition of non-controlling interests are accounted for as transactions with equity holders in their capacity as equity holders and therefore no goodwill is recognised as a result of such transactions.

Subsequent measurement

Goodwill is measured at cost less accumulated impairment losses.

(iv) Intangible assets acquired in a business combination

Intangible assets acquired in a business combination are identified and recognised separately from goodwill where they meet the definition of an intangible asset and their fair value can be measured reliably. Cost of such intangible assets is the fair value at the acquisition date.

Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and any accumulated impairment losses, on the same basis as intangible assets acquired separately.

3.18 Non-current assets held for sale

Certain non-current assets primarily related to the collateral collected on non-performing loans are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Non-current assets classified as held for sale are measured at the lower of carrying value and fair value less costs to sell.

3.19 Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets, other than deferred tax assets, are reviewed on each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

3. Significant accounting policies *(continued)*

3.19 Impairment of non-financial assets *(continued)*

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. 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.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

3.20 Leased assets - lessee

Leases in terms of which the Bank assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and, the leased assets are not recognised on the Bank's statement of financial position.

3.21 Funds borrowed and debt securities issued

Funds borrowed and debt securities issued are initially measured at fair value plus transaction costs, and subsequently measured at their amortised cost using the effective interest method.

3.22 Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. 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.

A provision for restructuring is recognised when the Bank has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating costs are not provided for.

A provision for onerous contracts is recognised when the expected benefits to be derived by the Bank from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Bank recognises any impairment loss on the assets associated with that contract.

3.23 Employee benefits

As a result of IAS 19, the Group has changed its accounting policy with respect to the basis for determining the income or expense related to defined benefit.

Under IAS 19, the Group determines the net interest expense (income) for the period on the net defined benefit liability by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability at the beginning of the annual period, taking into account any changes in the net defined benefit liability during the period as a result of contributions and benefit payments.

3. Significant accounting policies *(continued)*

3.23 Employee benefits *(continued)*

Consequently, the net interest on the net defined benefit liability now comprises:

- interest cost on the defined benefit obligation;
- interest income on plan assets; and
- interest on the effect on the asset ceiling.

As per revised IAS 19, all actuarial gain or losses are recognized under other comprehensive income starting from 1 January 2013.

3.24 Trade and other payables

Trade payables are payments to be made arising from the purchase of goods and services from suppliers within the ordinary course of business. Trade and other payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

3.25 Income tax expense

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in the profit or loss except to the extent that it relates to items recognised directly in equity or in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted on the reporting date, and any adjustment to tax payable in respect of prior years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed on each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

3.26 Events after the reporting period

Events after the reporting period that provide additional information about the Group's position at the reporting dates (adjusting events) are reflected in the consolidated financial statements. Events after the reporting period that are not adjusting events are disclosed in the notes when material.

3.27 Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components, whose operating results are reviewed regularly by the Board of Directors (being chief operating decision maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

3. Significant accounting policies *(continued)*

3.28 Borrowing costs

The Group, whenever required, generates funds from domestic and foreign sources in the form of borrowings, and bill and bond issuances in the local and international markets. The funds borrowed are recorded at their purchase costs and valued at amortised costs using the effective interest method.

An entity shall capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. An entity shall recognise other borrowing costs as an expense in the period in which it incurs them.

3.29 New and Revised International Financial Reporting Standards

Standards and interpretations issued but not yet effective

Standards issued but not yet effective and not early adopted

New standards, interpretations and amendments to existing standards are not effective at reporting date and earlier application is permitted; however, the Group has not early adopted are as follows. The Group will make the necessary changes if not indicated otherwise, which will be affecting the consolidated financial statements and disclosures, after the new standards and interpretations become in effect.

IFRS 16 Leases

On 13 January 2016, IASB issued the new leasing standard which will replace IAS 17 Leases, IFRIC 4 Determining Whether an Arrangement Contains a Lease, SIC 15 Operating Leases – Incentives, and SIC 27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease and consequently changes to IAS 40 Investment Properties. IFRS 16 Leases eliminates the current dual accounting model for lessees, which distinguishes between on-balance sheet finance leases and off-balance sheet operating leases. Instead, there is a single, on-balance sheet accounting model that is similar to current finance lease accounting. Lessor accounting remains similar to current practice. IFRS 16 is effective for annual periods beginning on or after 1 January 2019, with early adoption permitted provided that an entity also adopts IFRS 15 Revenue from Contracts with Customers. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 16.

IFRIC 23 –Uncertainty over Income Tax Treatments

On 17 June 2017, IASB issued IFRIC 23 Uncertainty over Income Tax Treatments to specify how to reflect uncertainty in accounting for income taxes. It may be unclear how tax law applies to a particular transaction or circumstance, or whether a taxation authority will accept a company's tax treatment. IAS 12 Income Taxes specifies how to account for current and deferred tax, but not how to reflect the effects of uncertainty. IFRIC 23 provides requirements that add to the requirements in IAS 12 by specifying how to reflect the effects of uncertainty in accounting for income taxes. IFRIC 23 is effective from 1 January 2019, with earlier application is permitted. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRIC 23.

3. Significant accounting policies *(continued)*

3.29 New and Revised International Financial Reporting Standards *(continued)*

The revised Conceptual Framework

The revised Conceptual Framework issued on 28 March 2018 by the IASB. The Conceptual Framework sets out the fundamental concepts for financial reporting that guide the Board in developing IFRS Standards.

It helps to ensure that the Standards are conceptually consistent and that similar transactions are treated the same way, so as to provide useful information for investors, lenders and other creditors. The Conceptual Framework also assists companies in developing accounting policies when no IFRS Standard applies to a particular transaction, and more broadly, helps stakeholders to understand and interpret the Standards. The revised Framework is more comprehensive than the old one – its aim is to provide the Board with the full set of tools for standard setting. It covers all aspects of standard setting from the objective of financial reporting, to presentation and disclosures. For companies that use the Conceptual Framework to develop accounting policies when no IFRS Standard applies to a particular transaction, the revised Conceptual Framework is effective for annual reporting periods beginning on or after 1 January 2020, with earlier application permitted.

Annual Improvements to IFRSs 2015-2017 Cycle

Improvements to IFRSs

IASB issued Annual Improvements to IFRSs - 2015–2017 Cycle for applicable standards. The amendments are effective as of 1 January 2019. Earlier application is permitted. The Group does not expect that application of these improvements to IFRSs will have significant impact on its consolidated financial statements.

IFRS 3 Business Combinations and *IFRS 11 Joint Arrangements*

IFRS 3 and IFRS 11 are amended to clarify how a company accounts for increasing its interest in a joint operation that meets the definition of a business. If a party obtains control, then the transaction is a business combination achieved in stages and the acquiring party remeasures the previously held interest at fair value. If a party maintains (or obtains) joint control, then the previously held interest is not remeasured.

IAS 12 Income Taxes

IAS 12 is amended to clarify that all income tax consequences of dividends (including payments on financial instruments classified as equity) are recognised consistently with the transactions that generated the distributable profits – i.e. in profit or loss, other comprehensive income (OCI) or equity.

IAS 23 Borrowing Costs

IAS 23 is amended to clarify that the general borrowings pool used to calculate eligible borrowing costs excludes only borrowings that specifically finance qualifying assets that are still under development or construction. Borrowings that were intended to specifically finance qualifying assets that are now ready for their intended use or sale – or any non-qualifying assets – are included in that general pool.

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

On 12 October 2017, IASB has issued amendments to IAS 28 to clarify that entities also apply IFRS 9 to other financial instruments in an associate or joint venture to which the equity method is not applied. These include long-term interests that, in substance, form part of the entity's net investment in an associate or joint venture. An entity applies IFRS 9 to such long-term interests before it applies related paragraphs of IAS 28. In applying IFRS 9, the entity does not take account of any adjustments to the carrying amount of long-term interests that arise from applying IAS 28. The amendments are effective for periods beginning on or after 1 January 2019, with earlier application permitted.

3. Significant accounting policies *(continued)*

3.29 New and Revised International Financial Reporting Standards *(continued)*

***Annual Improvements to IFRSs 2015-2017 Cycle** (continued)*

Amendments to IFRS 9 - Prepayment Features With Negative Compensation

On 12 October 2017, IASB has issued amendments to IFRS 9 to clarify those financial assets containing prepayment features with negative compensation can now be measured at amortised cost or at fair value through other comprehensive income (FVOCI) if they meet the other relevant requirements of IFRS 9. Under IFRS 9, a prepayment option in a financial asset meets this criterion if the prepayment amount substantially represents unpaid amounts of principal and interest, which may include 'reasonable additional compensation' for early termination of the contract. The amendments are effective for periods beginning on or after 1 January 2019, with earlier application permitted.

Amendments to IAS 19 - Plan Amendment, Curtailment or Settlement

On 7 February 2018, IASB issued Plan Amendment, Curtailment or Settlement (Amendments to IAS 19). The amendments clarify the accounting when a plan amendment, curtailment or settlement occurs. A company now uses updated actuarial assumptions to determine its current service cost and net interest for the period; and the effect of the asset ceiling is disregarded when calculating the gain or loss on any settlement of the plan and is dealt with separately in other comprehensive income (OCI). The amendments are effective for periods beginning on or after 1 January 2019, with earlier application permitted.

Improvements to IFRSs

Amendments to IAS 1 and IAS 8 - Definition of Material

In October 2018, the IASB issued Definition of Material (Amendments to IAS 1 and IAS 8). The amendments clarify and align the definition of 'material' and provide guidance to help improve consistency in the application of that concept whenever it is used in IFRS Standards. Those amendments are prospectively effective for annual periods beginning on or after 1 January 2020 with earlier application permitted.

Amendments to IFRS 3 - Definition of a Business

Determining whether a transaction results in an asset or a business acquisition has long been a challenging but important area of judgement. The IASB has issued amendments to IFRS 3 Business Combinations that seek to clarify this matter. The amendments include an election to use a concentration test. This is a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or a group of similar identifiable assets. If a preparer chooses not to apply the concentration test, or the test is failed, then the assessment focuses on the existence of a substantive process. The amendment applies to businesses acquired in annual reporting periods beginning on or after 1 January 2020. Earlier application is permitted.

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

4. Use of estimates and judgements

Management decides to the development, selection and disclosure of the Group’s critical accounting policies and estimates, and the application of these policies and estimates.

These disclosures supplement the commentary on financial risk management (see note 7).

Key sources of estimation uncertainty

Allowances for loan losses

Assets accounted for at amortised cost are evaluated for impairment on a basis described in accounting policy 3.10.

As of 1 January 2018, the Group recognizes provisions for impairment in accordance with IFRS 9 requirements. In this framework, as of 31 December 2017, method of provisions for impairment is changed by applying the expected credit loss model under IFRS 9.

Probability of Default (PD): PD refers to the likelihood that a loan will default within a specified time horizon, which is usually set at 12 months, given certain characteristics. The Group uses two different probability of default rates while calculating expected credit losses as per the IFRS 9.

- 12-month PD: as the estimated probability of default occurring within the next 12 months (or over the remaining life of the financial instrument if that is less than 12 months) following the balance sheet date.

- Lifetime PD: as the estimated probability of default occurring over the remaining life of the financial instrument.

Loss Given Default (LGD): If a loan default occurs, it represents the economic loss incurred on the loan. It is expressed as a percentage.

Exposure at Default (EAD): For cash loans, it corresponds to the amount of loan granted as of the reporting date. For non-cash loans and commitments, it is the value calculated through using credit conversion factors. Credit conversion factor corresponds to the factor which adjust the potential increase of the exposure between the current date and the default date.

Stage 1: For the financial assets at initial recognition or that do not have a significant increase in credit risk since initial recognition. Impairment for credit risk is recorded in the amount of 12-month expected credit losses.

Stage 2: Includes financial assets which have a significant increase in credit risk since initial recognition but an unbiased evidence does not occur. Lifetime expected credit losses are recognized for these financial instruments.

Stage 3: Stage 3 includes financial assets that have objective evidence of impairment at the reporting date. For these assets, lifetime expected credit losses are recognized and interest revenue is calculated on the net carrying amount.

The Group considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Group in full;
- the borrower is more than 90 days past due on any material credit obligation to the Group. Overdrafts are considered as being past due once the customer has breached an advised limit or been advised of a limit smaller than the current amount outstanding; or
- it is becoming probable that the borrower will restructure the asset as a result of bankruptcy due to the borrower’s inability to pay its credit obligations.

In assessing whether a borrower is in default, the Group considers indicators that are:

- qualitative: e.g. breaches of covenant;
- quantitative: e.g. overdue status and non-payment on another obligation of the same issuer to the Group; and
- based on data developed internally and obtained from external sources.

4. Use of estimates and judgements *(continued)*

Key sources of estimation uncertainty *(continued)*

Allowances for loan losses (continued)

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Determining fair values

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques as described in accounting policy 3.10. For financial instruments that require varying degrees of judgement depending liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument. See also “Valuation of financial instruments” below.

Critical accounting judgements in applying the Bank’s accounting policies

Critical accounting judgements made in applying the Bank’s accounting policies include:

Valuation of financial instruments

The Bank’s accounting policy on fair value measurements is discussed in accounting policy 3.10.

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements.

Level 1: Quoted market price (unadjusted) in an active market for identical instrument.

Level 2: Valuation techniques based on observable inputs, either directly (i.e., as prices) or indirectly (i.e., derived from prices). This category includes instruments using valuation techniques where all significant inputs are directly or indirectly observable from market data.

Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument’s valuation.

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Bank determines fair values using valuation techniques.

Valuation techniques include net present value and discounted cash flow models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm’s length.

The Bank uses widely recognised valuation models for determining the fair value of common and more simple financial instruments, like forwards and currency swaps that use only observable market data and require little management judgement and estimation. Observable prices and model inputs are usually available in the market for listed debt securities. Availability of observable market prices and model inputs reduces the need for management judgement and estimation and also reduces the uncertainty associated with determination of fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

(Currency - In thousands of Turkish Lira ("TL"))

4. Use of estimates and judgements *(continued)*

Critical accounting judgements in applying the Bank's accounting policies *(continued)*

This table below analyses financial instruments measured at fair value at the end of the reporting period, by the level in the fair value hierarchy into which the fair value measurement is categorised:

At 31 December 2018	Note	Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit or loss	*12*	33,263	454,767	-	488,030
Investment securities – FVOCI portfolio	*13*	898,075	1,077,518	-	1,975,593
		931,338	**1,532,285**	**-**	**2,463,623**
Trading liabilities	*12*	**-**	(23,017)	**-**	(23,017)
		-	**(23,017)**	**-**	**(23,017)**

At 31 December 2017	Note	Level 1	Level 2	Level 3	Total
Trading assets	*12*	42,313	9,643	-	51,956
Investment securities – AFS portfolio	*13*	704,173	606,524	-	1,310,697
		746,486	**616,167**	**-**	**1,362,653**
Trading liabilities	*12*	**-**	(8,987)	**-**	(8,987)
		-	**(8,987)**	**-**	**(8,987)**

Financial asset and liability classification

The Bank's accounting policies provide scope for assets and liabilities to be designated on inception into different accounting categories in certain circumstances. The classification of financial assets is explained in footnote 3.12.

Deferred taxes

Deferred tax assets and liabilities are recorded using substantially enacted tax rates for the effect of temporary differences between book and tax bases of assets and liabilities. Currently, there are deferred tax assets resulting from operating loss carry-forwards and deductible temporary differences, all of which could reduce taxable income in the future. Based on available evidence, both positive and negative, it is determined whether it is probable that all or a portion of the deferred tax assets will be realized.

The main factors which are considered include future earnings potential; cumulative losses in recent years; history of loss carry-forwards and other tax assets expiring; the carry-forward period associated with the deferred tax assets; future reversals of existing taxable temporary differences; tax-planning strategies that would, if necessary, be implemented, and the nature of the income that can be used to realize the deferred tax asset. If based on the weight of all available evidence, it is the Group's belief that taxable profit will not be available sufficient to utilize some portion of these deferred tax assets, then some portion of or all of the deferred tax assets are not recognized.

(Currency - In thousands of Turkish Lira (“TL”))

4. Use of estimates and judgements *(continued)*

Critical accounting judgements in applying the Bank’s accounting policies *(continued)*

Impairment of tangible and intangible assets

At the end of each reporting period, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). When it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. When a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

5. Explanations of IFRS 9 financial instruments

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

IFRS 9 sets out the new principles for the classification and measurement of financial instruments, impairment for credit risk on financial assets and general hedge accounting.

In accordance with the transition rules option provided by the IFRS 9 “Financial Instruments”, the Group did not restated the prior period financial statements and recognized the transition effect of the standard as of 1 January 2018 under equity’s “prior year profit or loss” accounts.

Explanation of the effect of the Group’s application of IFRS 9 is stated below:

5.1. Classification and measurement of financial assets

	Before IFRS 9		**In scope of IFRS 9**	
	31 December 2017		**1 January 2018**	
	Measurement bases	**Book Value**	**Measurement bases**	**Book Value**
Cash and Cash Equivalents	Loans and receivables	730,980	Measured at amortized cost	730,980
Reserve Deposits at Central Bank	Loans and receivables	1,008,020	Measured at amortized cost	1,008,020
Investment Securities	Trading assets	42,971	Fair value through profit and loss	42,971
	Available for sale financial assets	1,310,697	Fair value through other comprehensive income	1,310,697
	Investment securities held to maturity	254,120	Measured at amortized cost	254,120
Derivative Financial Assets	Trading assets	8,985	Fair value through profit and loss	8,985
	Fair value through other comprehensive income	-	Fair value through other comprehensive income	-
Loans and Advances to Customers	Loans and receivables	6,670,024	Measured at amortized cost	6,670,024

5.2. Reconciliation of statement of financial position balances to IFRS 9

There is no classification in financial assets within the scope of IFRS 9.

(Currency - In thousands of Turkish Lira ("TL"))

5. Explanations of IFRS 9 financial instruments *(continued)*

5.3. Reconciliation of the opening balances of the provision for expected credit losses to IFRS 9

The table below shows the reconciliation of the provision for impairment of the Group as of 31 December 2017 and the provision for the expected loss model as measured in accordance with IFRS 9 as of 1 January 2018.

	Before IFRS 9		**In scope of IFRS 9**
	31 December 2017	**Remeasurements**	**1 January 2018**
Allowances for individual impairment	96,405	10,324	106,729
Allowances for collective impairment	34,142	18,385	52,527
Total allowances for impairment	**130,547**	**28,709**	**159,256**

5.4. Effects on equity with IFRS 9 transition

According to paragraph 15 of Article 7 of IFRS 9 Financial Instruments Standards, it is stated that it is not compulsory to restate previous period information in accordance with IFRS 9 and if the previous period information is not revised, it is stated that the difference between the book value of 1 January 2018 at the date of application should be reflected in the opening aspect of equity. The explanations about the transition effects to IFRS 9 presented in the equity items under the scope of this article are given below.

The amounting to TL 28,709 of additional impairment losses which is a difference between the provision for impairment of the previous period of the Group and the provision for loss that is measured in accordance with IFRS 9 impairment model as of 1 January 2018 is classified as "Retained earnings" in shareholders' equity. Deferred tax assets amounting to TL 6,866 and corporate tax liability which have been cancelled due to IFRS 9 transition amounting to TL 1,236 have been reflected to the opening financials of 1 January 2018 and the related amounts have been classified under "Retained earnings".

6. Explanations on prior period accounting policies not valid for the current period

"IFRS 9: Financial Instruments" standard came into effect instead of "IAS 39 Financial Instruments: Recognition and Measurement" as of 1 January 2018. Accounting policies lost their validity with the transition of IFRS 9 are given below.

The Group categorizes and records its financial assets as "Financial Assets at Fair Value through Profit and Loss", "Financial Assets Available for Sale", "Loans and Receivables" or "Financial Assets Held to Maturity".

Sale and purchase transactions of the financial assets mentioned above are recognized at the settlement dates. Revaluation surplus between accounting date and settlement date for financial assets measured at fair value through profit/loss and financial assets available-for-sale is recorded in the financial statements. The appropriate classification of financial assets is determined and accounted at the time of purchase by the Group management taking into consideration the purpose of the investment.

6.1. Financial assets at fair value through profit or loss

Financial assets at fair value through profit and loss are classified in three categories as " Financial assets held for trading", "Financial assets classified at inception as financial assets at fair value through profit and loss" and "Derivative financial assets held for trading".

Financial assets held for trading purposes are the ones which are purchased in order to profit from the short-term fluctuations of price and other similar conditions in the market, or independently from their purpose of purchase, the ones which are a part of a portfolio that held for obtaining profit in the short term.

6. Explanations on prior period accounting policies not valid for the current period *(continued)*

6.1. Financial assets at fair value through profit or loss *(continued)*

Trading securities are initially recognized at cost. Subsequent to initial recognition, trading securities are measured at fair value. Any gains or losses resulting from such valuation are recorded in the profit and loss accounts. Any profit or loss between sales price and amortized cost resulting from the disposal of those assets before their maturity date is recognized under the "securities trading gains/losses" account as per the explanations of the Uniform Chart of Accounts (UCA).

The derivative transactions that are not qualified to be a hedging instrument are reclassified as derivative financial assets held for trading.

6.2. Financial assets available for sale

Financial assets classified as financial assets available for-sale-are subsequently measured at their fair values. Financial assets available for sale that have a quoted market price in an active market and whose values can be reliably measured are carried at fair value. Financial assets available for sale that do not have quoted market price and whose fair values cannot be reliably measured are carried at amortized cost for financial assets having fixed maturities and fair value computed using fair value modelling or discounted cash flow method for equity securities. The unrealized gain/loss originating from the difference between the amortized cost and the fair value is recorded in "Marketable Securities Value Increase Fund" under the equity. At the disposal of available for sale financial assets, value increases/decreases recorded in the securities value increase fund under equity are transferred to income statement.

6.3. Investments held to maturity

Investments held to maturity include securities with fixed or determinable payments and fixed maturity where there is an intention of holding until maturity and the relevant conditions for fulfilment of such intention, including the funding ability. This portfolio excludes loans and receivables. Investments held to maturity are initially recognized at cost including transaction cost. After initial recognition held to maturity investments are measured at amortized cost by using effective interest rate less impairment losses, if any. The interests received from held to maturity investments are recorded as interest income in the income statement.

There are no financial assets that were previously classified as held to maturity but cannot be subject to this classification for two years due to the violation of the tainting rule.

6.4. Loans and other receivables

Loans and receivables are financial assets originated by the Group providing money, goods or services to debtors and classified other than those classified as trading financial assets. Such assets are initially recognized at cost and are carried at amortized cost using "the effective interest (internal efficiency) method" subsequently.

6.5. Allowances for loan losses

The Bank reviews its loan portfolio to assess impairment at least on a monthly basis. In determining whether an impairment loss should be recorded in the profit or loss, the Bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and individual loans. All loans with principal and/or interest overdue for more than 90 days are considered as impaired and individually assessed. Other evidence for impairment may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Bank.

Due to the increase in the consumer loan portfolio of the Bank and the availability of the historical trends of the probability of default the Bank started to provide collective loan loss allowance established for groups of homogeneous assets in respect of losses that have been incurred but have not been identified except for loans and receivables subject to individual assessment for impairment.

6. Explanations on prior period accounting policies not valid for the current period *(continued)*

6.6 Trade receivables

A doubtful receivable provision for trade receivables is established if there is objective evidence that the Group will not be able to collect all amounts due. The amount of provision is the difference between the carrying amount and the recoverable amount, being the present value of all cash flows, including amounts recoverable from guarantees and collateral, discounted based on the original effective interest rate of the originated receivables at inception.

7. Financial risk management

Introduction and overview

The Bank has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risks
- Operational risks.

This note presents information about the Bank’s exposure to each of the above risks, the Bank’s objectives, policies and processes for measuring and managing risk, and the Bank’s management of capital.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Bank’s risk management framework. The Board has established the Audit Committee and Risk Management Department, which are responsible for developing and monitoring Bank risk management policies in their specified areas. The Audit Committee has non-executive members and report regularly to the Board of Directors on their activities.

The Bank’s risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Audit Committee is responsible for monitoring compliance with the Bank’s risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Audit Committee is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank’s loans and advances to customers and other banks and investment securities. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

For risk management purposes, credit risk arising on trading securities is managed independently, but reported as a component of market risk exposure.

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Credit risk *(continued)*

Management of credit risk

The Bank's credit risk management strategy is based on a three-part methodology that embraces the customer selection, credit allocation, and credit pricing stages. Since it was founded, the Bank has always managed its credit risks by taking a portfolio-logic approach. This sums up the Bank's basic risk management strategy.

In the first stage of the lending process, industry weightings are determined and firms that are seeking credit are given a preliminary screening. This initial check is followed by the credit allocation stage in which firms are individually rated and the Bank's guarantee strategy is determined according to the results of this rating. In the final stage of the lending process, prices are determined by taking a risk-premium approach.

The disclosures set out in the tables below include financial assets and financial liabilities that:

- are offset in the Group's statement of financial position; or
- are subject to an enforceable master netting arrangement or similar agreement that covers similar financial instruments, irrespective of whether they are offset in the statement of financial position.

The similar agreements include derivative clearing agreements. Similar financial instruments include derivatives. Financial instruments such as loans and funds are not disclosed in the tables below unless they are offset in the statement of financial position.

Such collateral is subject to each agreement terms. The terms also give each party the right to terminate the related transactions on the counterparty's failure to post collateral.

The Bank receives and gives collateral in the form of cash in respect of the derivative transactions.

Financial assets and liabilities subject to offsetting, enforceable master netting arrangements and similar agreements

					Related amounts not offset in the statement of financial position		
	Types of financial assets	**Gross amounts of recognised financial assets**	**Gross amounts of recognised financial liabilities offset in the statement of financial position**	**Net amounts of financial assets presented in the statement of financial position**	**Financial instruments (including non-cash collateral)**	**Cash collateral received**	**Net amount**
31 December 2018	Derivatives trading assets	52,589	-	52,589	(52,589)	-	-
31 December 2017	Derivatives trading assets	8,985	-	8,985	(8,985)	-	-

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Credit risk *(continued)*

Financial assets and liabilities subject to offsetting, enforceable master netting arrangements and similar agreements (continued)

					Related amounts not offset in the statement of financial position		
	Types of financial liabilities	**Gross amounts of recognised financial liabilities**	**Gross amounts of recognised financial assets offset in the statement of financial position**	**Net amounts of financial liabilities presented in the statement of financial position**	**Financial instruments (including non-cash collateral)**	**Cash collateral received**	**Net amount**
31 December 2018	Derivatives trading liabilities	23,017	-	23,017	(23,017)	-	-
31 December 2017	Derivatives trading liabilities	8,987	-	8,987	(8,987)	-	-

Definition of default

The Group considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Group in full;
- the borrower is more than 90 days past due on any material credit obligation to the Group. Overdrafts are considered as being past due once the customer has breached an advised limit or been advised of a limit smaller than the current amount outstanding; or
- it is becoming probable that the borrower will restructure the asset as a result of bankruptcy due to the borrower's inability to pay its credit obligations.

In assessing whether a borrower is in default, the Group considers indicators that are:

- qualitative: e.g. breaches of covenant;
- quantitative: e.g. overdue status and non-payment on another obligation of the same issuer to the Group; and
- based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Allowance for impairment

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Group's historical experience and expert credit assessment and including forward-looking information.

The objective of the assessment is to identify whether a significant increase in credit risk has occurred for an exposure by comparing:

- the remaining lifetime probability of default (PD) as at the reporting date; with
- the remaining lifetime PD for this point in time that was estimated at the time of initial recognition of the exposure (adjusted where relevant for changes in prepayment expectations).

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Credit risk *(continued)*

Write-off policy

The Bank writes off a loan balance, and any related allowances for impairment losses, when Bank determines that the loan is uncollectible. This determination is reached after considering information such as occurrence of significant changes in the borrower's / issuer's financial position such that the borrower / issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure.

Set out below is an analysis of the gross and net (of allowances for impairment) amounts of individually impaired assets by risk grade.

	Loans and advances to customers	
	Gross	**Net**
31 December 2018		
Individually impaired	270,617	122,814
31 December 2017		
Individually impaired	190,700	94,295

Concentration risk by location

The Bank's total risk for loans and advances to customers and investment debt securities (held-to-maturity portfolio) is mainly concentrated on Turkey.

The Bank monitors concentrations of credit risk for cash loans and advances to customer and non-cash loans to customers by sector. An analysis of concentrations of credit risk at the reporting date is shown below:

	31 December 2018				31 December 2017			
Sector	**Cash loans**	**%**	**Non-cash loans**	**%**	**Cash loans**	**%**	**Non-cash loans**	**%**
Construction	71,938	1	62,239	5	433,373	7	250,609	19
Financial institution	314,098	5	152,159	12	136,294	2	205,023	16
General services	1,848,901	27	85	-	1,419,654	22	3,744	-
Textile	572,451	8	39,520	3	348,289	5	53,560	4
Mining	176,751	3	2,758	-	158,802	2	2,746	-
Telecommunication	169,954	2	850	-	130,617	2	850	-
Electricity industry	17,098	-	135,391	11	48,585	1	112,542	9
Public	152,897	2	-	-	6,925	-	-	-
Energy industry	739,435	11	410,991	34	660,937	10	380,049	29
Trade	74,087	1	3,998	-	122,789	2	20,941	2
Sports	819,712	12	3,278	-	851,478	13	3,278	-
Other (*)	1,946,221	28	420,956	35	2,221,734	34	275,615	21
Total	**6,903,543**	**100**	**1,232,225**	**100**	**6,539,477**	**100**	**1,308,957**	**100**

(*) Includes consumer loans, unclassified loans, factoring and leasing receivables.

Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations from its financial liabilities.

Management of liquidity risk

The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Liquidity risk *(continued)*

The Bank funds its short-term liquidity with interbank. In the case of long-term liquidity need, the Bank utilises capital market instruments. Additionally, the Bank also funds itself from the domestic and foreign market when it needs additional funds.

Exposure to liquidity risk

The key measure used by the Bank for managing liquidity risk is the ratio of net liquid assets to short-term funds borrowed. For this purpose, net liquid assets are considered as including cash and cash equivalents and trading debt securities for which there is an active and liquid market less any short-term funds borrowed and commitments. A similar, but not identical, calculation is used to measure the Bank's compliance with the liquidity limit established by the BRSA.

	31 December 2018	31 December 2017
Average for the year	117%	108%
Maximum for the year	154%	125%
Minimum for the year	103%	100%

Residual contractual maturities of financial liabilities

	Note	Carrying amount	Gross nominal inflow / (outflow)	On demand	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	More than 5 years
31 December 2018									
Non-derivative liabilities									
Obligations under repurchase agr.	20	1,291,742	(1,298,327)	-	(761,182)	(474,643)	(62,502)	-	-
Debt securities issued	22	4,365,713	(4,792,732)	-	(1,252,347)	(1,737,282)	(1,102,546)	(700,557)	-
Funds borrowed	21	3,650,016	(3,682,727)	-	(1,441,634)	(1,187,354)	(925,285)	(128,454)	-
Trade and other payables		288,240	(308,113)	(177,385)	(52,274)	(18,173)	(60,281)	-	-
Financial lease liabilities		3,904	(4,289)	-	(594)	(712)	(1,005)	(1,324)	(654)
Customer accounts (*)	25	1,624,270	(1,624,270)	(1,624,270)	-	-	-	-	-
Derivative financial instruments									
Inflow	12	(52,589)	2,171,450	-	851,270	134,242	747,081	438,857	-
Outflow	12	23,017	(2,156,712)	-	(857,995)	(114,800)	(750,096)	(433,821)	-
		11,194,313	**(11,695,720)**	**(1,801,655)**	**(3,514,756)**	**(3,398,722)**	**(2,154,634)**	**(825,299)**	**(654)**

(*) Included in other liabilities.

	Note	Carrying amount	Gross nominal inflow / (outflow)	On demand	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	More than 5 years
31 December 2017									
Non-derivative liabilities									
Obligations under repurchase agr.	20	1,074,509	(1,076,603)	-	(967,025)	(104,113)	(5,465)	-	-
Debt securities issued	22	2,776,288	(2,885,059)	-	(1,459,468)	(1,040,540)	(363,324)	(21,727)	-
Funds borrowed	21	3,774,380	(3,844,069)	-	(1,132,318)	(1,300,354)	(1,353,049)	(58,348)	-
Trade and other payables		114,787	(114,787)	(114,787)	-	-	-	-	-
Financial lease liabilities		20,146	(20,473)	-	(400)	(4,706)	(11,522)	(3,845)	-
Customer accounts (*)	25	1,201,545	(1,201,545)	(1,201,545)	-	-	-	-	-
Derivative financial instruments									
Inflow	12	(8,985)	2,027,621	-	595,916	792,911	638,794	-	-
Outflow	12	8,987	(2,031,723)	-	(597,945)	(793,310)	(640,468)	-	-
		8,961,657	**(9,146,638)**	**(1,316,332)**	**(3,561,240)**	**(2,450,112)**	**(1,735,034)**	**(83,920)**	**-**

(*) Included in other liabilities.

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Liquidity risk *(continued)*

The gross nominal inflow / (outflow) disclosed in the table above is the contractual, undiscounted cash flow on the financial liability or commitment.

Market risk

Market risk is the risk that, measured by changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) which will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Overall authority for market risk is vested in Asset and Liability Committee ("ALCO").

Exposure to market risks – trading portfolios

The principal tool used to measure and control market risk exposure within the Bank's portfolios is Standard Method.

A summary of the Standard Method position of the Bank's portfolios on 31 December 2018 and 2017 and during the period is as follows:

	31 December 2018	**31 December 2017**
Interest rate risk	104,409	61,370
Foreign currency risk	2,623	2,533
Other risk	656	7,168
	107,688	**71,071**

The following table sets out the allocation of assets subject to market risk.

	Carrying amount	**Market risk measuring**
31 December 2018		
Financial assets measured at fair value through profit or loss	435,441	435,441
Financial assets measured at fair value through other comprehensive income	1,975,593	1,975,593
Derivative financial assets	52,589	52,589
31 December 2017		
Trading assets	51,956	51,956
Available for sale financial assets	1,310,697	1,310,697

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Interest rate risk

Exposure to interest rate risk – non-trading portfolios

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market interest rates. Interest rate risk is managed principally through monitoring interest rate gaps and by having pre-approved limits for repricing bands. The ALCO is the monitoring body for compliance with these limits and is assisted by Risk Management Department of the Bank in its day-to-day monitoring activities. A summary of the Bank's interest rate gap position on non-trading portfolios is as follows:

	Note	Carrying amount	Unallocated	On demand	Less than 3 months	3-6 months	6-12 months	1-5 years	More than 5 years
31 December 2018									
Cash and cash equivalents	10	1,390,183	-	154,224	1,205,036	30,923	-	-	-
Reserve deposits at Central Bank	11	1,072,226	-	-	1,072,226	-	-	-	-
Financial assets at fair value through profit or loss	12	488,030	52,589	363,378	19,177	37,649	5,192	10,045	-
Loans and advances to customers	14	6,903,543	81,975	-	4,296,885	49,883	119,958	1,865,044	489,798
Investment securities	13	2,337,493	5,059	-	127,889	51,278	888,371	801,282	463,614
		12,191,475	**139,623**	**517,602**	**6,721,213**	**169,733**	**1,013,521**	**2,676,371**	**953,412**
Obligations under repurchase agr.	20	1,291,742	-	-	1,230,333	59,665	1,744	-	-
Debt securities issued	22	4,365,713	-	-	2,891,688	442,169	513,073	518,783	-
Financial lease liabilities		3,904	-	-	540	621	902	1,226	615
Funds borrowed	21	3,650,016	-	-	2,617,711	691,543	212,307	128,455	-
		9,311,375	**-**	**-**	**6,740,272**	**1,193,998**	**728,026**	**648,464**	**615**
Interest rate gap		**2,880,100**	**139,623**	**517,602**	**-19,059**	**-1,024,265**	**285,495**	**2,027,907**	**952,797**

	Note	Carrying amount	Unallocated	On demand	Less than 3 months	3-6 months	6-12 months	1-5 years	More than 5 years
31 December 2017									
Cash and cash equivalents	10	730,980	-	179,675	551,305	-	-	-	-
Reserve deposits at Central Bank	11	1,008,020	-	-	1,008,020	-	-	-	-
Trading assets	12	51,956	8,985	42,220	-	-	-	658	93
Loans and advances to customers	14	6,539,477	60,153	-	1,824,427	1,010,405	1,256,668	1,958,957	428,867
Investment securities	13	1,564,817	2,560	-	66,492	52,494	413,781	544,757	484,733
		9,895,250	**71,698**	**221,895**	**3,450,244**	**1,062,899**	**1,670,449**	**2,504,372**	**913,693**
Obligations under repurchase agr.	20	1,074,509	-	-	1,069,130	5,379	-	-	-
Debt securities issued	22	2,776,288	-	-	2,421,584	136,072	200,243	18,389	-
Financial lease liabilities		20,146	-	-	5,034	1,107	10,160	3,845	-
Funds borrowed	21	3,774,380	-	-	2,424,334	548,001	749,653	52,392	-
		7,645,323	**-**	**-**	**5,920,082**	**690,559**	**960,056**	**74,626**	**-**
Interest rate gap		**2,249,927**	**71,698**	**221,895**	**-2,469,838**	**372,340**	**710,393**	**2,429,746**	**913,693**

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Interest rate risk *(continued)*

Interest rate sensitivity

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and non-standard interest rate scenarios. Standard scenarios that are considered on a monthly basis include a 100 basis point (bp) parallel fall or rise in all yield curves. An analysis of the Bank's sensitivity to an increase or decrease in market interest rates (assuming no asymmetrical movement in yield curves and a constant statement of financial position) is as follows:

		31 December 2018		31 December 2017	
Currency	**Applied Shock (+/- x basis points)**	**Gains /Losses**	**Gains (Losses)/ Shareholder's Equity**	**Gains /Losses**	**Gains (Losses)/ Shareholder's Equity**
TL	500	(45,645)	(3.09)%	(125,266)	(10.11)%
	(400)	43,284	2.93%	116,170	9.37%
EUR	200	(807)	(0.05) %	5,810	0.47%
	(200)	708	0.05%	2,246	0.18%
USD	200	(45,511)	(3.09) %	(43,955)	(3.55)%
	(200)	52,561	3.56%	52,370	4.23%
Total (for negative shocks)		**96,553**	**6.54%**	**170,786**	**13.78%**
Total (for positive shocks)		**(91,963)**	**(6.23)%**	**(163,411)**	**(13.19)%**

Summary of average interest rates

As at 31 December 2018 and 2017, the summary of average interest rates for different assets and liabilities is as follows:

	31 December 2018			31 December 2017		
	Euro	**USD**	**TL**	**Euro**	**USD**	**TL**
Assets						
Cash and cash equivalents	1.47	1.79	-	-	1.35	13.25
Loans and advances to customers	8.38	9.07	29.39	7.23	7.82	21.06
Investment securities – Financial assets measured at fair value through other comprehensive income	3.78	8.02	13.87	-	-	-
Investment securities – Financial assets measured at amortized cost	-	6.32	19.77	-	-	-
Investment securities – AFS	-	-	-	-	6.41	9.84
Investment securities – HTM	-	-	-	-	7.12	15.78
Liabilities						
Obligations under repurchase agreements	2.82	5.25	20.26	2.58	4.31	12.89
Debt securities issued	3.57	5.67	25.96	3.04	4.86	14.96
Funds borrowed	1.92	4.10	25.05	1.67	3.27	12.44

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Foreign currency risk

31 December 2018	**Euro**	**USD**	**Other**	**Total**
Cash and cash equivalents	400,534	514,769	60,383	975,686
Reserve deposits at Central Bank	562,303	323,332	186,867	1,072,502
Financial assets at fair value through profit or loss	-	9,207	-	9,207
Trade and other receivables	-	4,136	-	4,136
Loans and advances to customers	2,481,083	1,226,108	-	3,707,191
Investment securities	24,836	987,365	-	1,012,201
Equity accounted investees	-	7,196	4,292	11,488
Other assets	19,472	35,823	12	55,307
Trade and other payables	(1,226)	(24,413)	(7)	(25,646)
Funds borrowed	(2,009,099)	(1,160,455)	(160,474)	(3,330,028)
Obligations under repurchase agreements	(176,680)	(1,038,531)	(2,659)	(1,217,870)
Debt securities issued	(87,261)	(366,999)	-	(454,260)
Other liabilities	(1,086,764)	(713,521)	(78,085)	(1,878,370)
Net statement of financial position	**127,198**	**(195,983)**	**10,329**	**(58,456)**
Derivative financial instruments	(126,239)	105,065	(21,523)	(42,697)
Net total position	**959**	**(90,918)**	**(11,194)**	**(101,153)**

31 December 2017	**Euro**	**USD**	**Other**	**Total**
Cash and cash equivalents	181,976	130,939	39,838	352,753
Reserve deposits at Central Bank	568,271	439,749	-	1,008,020
Trading assets	-	658	-	658
Trade and other receivables	737	6,088	-	6,825
Loans and advances to customers	2,202,620	1,357,622	-	3,560,242
Investment securities	140	695,102	-	695,242
Equity accounted investees	-	7,196	4,292	11,488
Other assets	5,785	12,089	-	17,874
Trade and other payables	(1,019)	(70,111)	-	(71,130)
Funds borrowed	(1,901,434)	(1,500,728)	-	(3,402,162)
Obligations under repurchase agreements	(37,953)	(355,819)	(33)	(393,805)
Debt securities issued	(247,601)	(214,604)	-	(462,205)
Other liabilities	(593,702)	(596,939)	(252,679)	(1,443,320)
Net statement of financial position	**177,820**	**(88,758)**	**(208,582)**	**(119,520)**
Derivative financial instruments	(152,320)	76,675	214,353	138,708
Net total position	**25,500**	**(12,083)**	**5,771**	**19,188**

(Currency - In thousands of Turkish Lira (“TL”))

7. Financial risk management *(continued)*

Foreign currency risk *(continued)*

Sensitivity analysis

A 10 percent weakening of TL against the foreign currencies on 31 December 2018 and 2017 would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant.

31 December 2018	Equity	Profit or loss
Euro	96	96
USD	(9,092)	(9,528)
Other currencies	(1,119)	(1,125)
	(10,115)	**(10,557)**

31 December 2017	Equity	Profit or loss
Euro	2,550	2,550
USD	(1,208)	(266)
Other currencies	577	577
	1,919	**2,861**

A 10 percent strengthening of the TL against the foreign currencies on 31 December 2018 and 2017 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank’s processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks, such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Bank’s operations and are faced by all business entities.

The operational risk items in the Bank are determined in accordance with the definition of operational risk by considering as whole processes, products and departments. The control areas are set for operational risks within the Bank and all operational risks are followed by assigning the risks to these control areas. In this framework, an appropriate monitoring methodology is developed for each control area that covers all operational risks and control frequencies are determined.

All the operational risks that are exposed during the operations, the risk levels of the operations and/or new products/services, together with the losses of the Bank arising from operational risks are regularly monitored by the Risk Management Department of the Bank, and if deemed necessary, the risk levels are updated and periodically reported to the Risk Committee and the Board of Directors.

The Bank calculated the value of operational risk in accordance with the fourth section regarding the “Computation of Value of Operational Risk” of the circular, “Regulation on Measurement and Assessment of Capital Adequacy of Banks” Communiqué, using gross profit of the last three years 2017, 2016 and 2015 (“the Basic Indicator Approach). The amount calculated as TL 79,197 as at 31 December 2018 (31 December 2017: TL 57,285) represents the operational risk that the Bank may be exposed to and the amount of minimum capital requirement to eliminate this risk. Value of operational risk amounted to TL 989,965 (31 December 2017: TL 716,059) and is calculated as 12.5 times the operational risk.

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Capital management

The Bank's lead regulator, BRSA, sets and monitors capital requirements for the Bank as a whole.

Capital adequacy ratio has been calculated in accordance with the "Regulation on Measurement and Assessment of Capital Adequacy of Banks", "Credit Risk Mitigation Techniques" and "Calculation of Risk weighted Amounts for Securitizations" Communiqués.

Capital adequacy ratio is calculated based on total capital requirements needed for credit risk, market risk and operational risk. Credit risk is calculated by holding risk-weighted assets and non-cash loans subject to risk weights in the relevant legislation and considering risk mitigation techniques; the standard method is used to calculate market risk and the basic indicator approach is used to calculate operational risk. In implementing current capital requirements, the BRSA requires the banks to maintain a prescribed ratio of minimum 8% of total capital.

The Bank's regulatory capital positions are as follows:

	2018	**2017**
Tier 1 Capital	1,432,901	1,180,350
Tier 2 Capital	42,316	58,816
Total regulatory capital	1,475,217	1,239,166
Value at credit, market and operational risks	11,459,270	9,266,654
Capital ratios (%)		
Total regulatory capital ratio	12.87	13.37
Total tier 1 capital ratio	12.50	12.74

Financial assets and liabilities

Accounting classification and fair values

The determination of fair values of financial assets and financial liabilities is based on quoted market prices or dealer price quotations for financial instruments traded in active markets or valuation techniques. However, the Bank expects no significant difference between the fair value and carrying value of the financial instruments below since most of the financial instruments' maturities are short-term except for the loans and advances to customers and investment securities- financial assets measured at amortised cost.

For disclosure purpose, valuation technique used for determining the fair value of the loans and advances to customers is net present value model. Assumptions and inputs used in net present value model include benchmark interest rates, credit spreads or other premium used in estimating discount rates. The fair value measurement for fixed rate loans and receivables are calculated by using the discounted cash flow method and has been categorised as a Level 2 fair value based on the inputs to the valuation technique used.

For disclosure purpose, the fair value of the investment securities-financial assets measured at amortised cost is determined based on by using the discounted cash flow method and has been categorised as a Level 2 fair value based on the inputs to the valuation technique used.

The objective of valuation technique is to arrive at a fair value determination that reflects the prices of the loans and advances to customers and investment securities at the reporting date that would have been determined by market participants acting at arm's length.

The fair value hierarchy for the financial instruments measured at fair value at the end of the reporting period is presented in note 4, Use of estimates and judgements.

(Currency - In thousands of Turkish Lira ("TL"))

7. Financial risk management *(continued)*

Financial assets and liabilities *(continued)*

Accounting classification and fair values *(continued)*

The table below sets out the Group's classification of each class of financial assets and liabilities and their fair values.

	Note	Financial assets at fair value through profit or loss	Financial assets measured at amortized cost	Financial assets measured at FVOCI	Total carrying amount	Fair value
31 December 2018						
Cash and cash equivalents	*10*	-	1,390,183	-	1,390,183	1,390,183
Trade and other receivables		-	75,567	-	75,567	75,567
Reserve deposits at Central Bank	*11*	-	1,072,226	-	1,072,226	1,072,226
Financial assets at fair value through profit or loss	*12*	488,030	-	-	488,030	488,030
Loans and advances to customers	*14*	-	6,903,543	-	6,903,543	6,682,245
Investment securities	*13*	-	361,900	1,975,593	2,337,493	2,312,095
		488,030	**9,803,419**	**1,975,593**	**12,267,042**	**12,020,346**
Trading liabilities	*12*	23,017	-	-	23,017	23,017
Trade and other payables		-	288,240	-	288,240	288,240
Financial lease liabilities		-	3,904	-	3,904	3,904
Obligations under rep. agr.	*20*	-	1,291,742	-	1,291,742	1,291,742
Debt securities issued	*22*	-	4,365,713	-	4,365,713	4,365,713
Funds borrowed	*21*	-	3,650,016	-	3,650,016	3,650,016
		23,017	**9,599,615**	**-**	**9,622,632**	**9,622,632**

	Note	Trading	Loans and receivables	Available-for-sale	Held–to-maturity	Other amortised cost	Total carrying amount	Fair value
31 December 2017								
Cash and cash equivalents	*10*	-	730,980	-	-	-	730,980	730,980
Trade and other receivables		-	-	-	-	254,154	254,154	254,154
Reserve deposits at Central Bank	*11*	-	1,008,020	-	-	-	1,008,020	1,008,020
Trading assets	*12*	51,956	-	-	-	-	51,956	51,956
Loans and advances to customers	*14*	-	6,539,477	-	-	-	6,539,477	6,463,765
Investment securities	*13*	-	-	1,310,697	254,120	-	1,564,817	1,564,817
		51,956	**8,278,477**	**1,310,697**	**254,120**	**254,154**	**10,149,404**	**10,073,692**
Trading liabilities	*12*	8,987	-	-	-	-	8,987	8,987
Trade and other payables		-	-	-	-	114,787	114,787	114,787
Financial lease liabilities		-	-	-	-	20,146	20,146	20,146
Obligations under rep. agr.	*20*	-	-	-	-	1,074,509	1,074,509	1,074,509
Debt securities issued	*22*	-	-	-	-	2,776,288	2,776,288	2,776,288
Funds borrowed	*21*	-	-	-	-	3,774,380	3,774,380	3,774,380
		8,987	**-**	**-**	**-**	**7,760,110**	**7,769,097**	**7,769,097**

8. Business combinations

Goodwill arising on acquisition of Pavo is TL 504 (31 December 2017: TL 504).

(Currency - In thousands of Turkish Lira ("TL"))

9. Segment reporting

2018	Retail banking	Corporate banking	Investment banking	Other banking	Total banking	Brokerage	Other	Combined	Adjustments	Total
Operating income	497,269	904,629	419,845	82,151	1,903,894	64,717	641,659	2,610,270	(338,729)	2,271,541
Operating expense	(452,547)	(158,821)	(227,799)	(744,031)	(1,583,198)	(19,320)	(488,988)	(2,091,506)	300,415	(1,791,091)
Income from operations	**44,722**	**745,808**	**192,046**	**(661,880)**	**320,696**	**45,397**	**152,671**	**518,764**	**(38,314)**	**480,450**
Income tax expense	-	-	-	(58,026)	(58,026)	(10,354)	(30,441)	(98,821)	43	(98,778)
Net income for the year	**44,722**	**745,808**	**192,046**	**(719,906)**	**262,670**	**35,043**	**122,230**	**419,943**	**(38,271)**	**381,672**
Segment assets	1,928,436	5,285,167	5,198,940	-	12,412,543	119,419	370,360	12,902,322	(618,205)	12,284,117
Investments in equity participations	-	-	387,358	-	387,358	-	283,412	670,770	(619,972)	50,798
Other assets	-	-	-	716,841	716,841	1,495	726,366	1,444,702	102,906	1,547,608
Total assets	**1,928,436**	**5,285,167**	**5,586,298**	**716,841**	**13,516,742**	**120,914**	**1,380,138**	**15,017,794**	**(1,135,271)**	**13,882,523**
Segment liabilities	4,678,732	3,261,717	3,731,450	-	11,671,899	6,067	674,863	12,352,829	(2,730,198)	9,622,631
Equity and other liabilities	-	-	-	1,844,843	1,844,843	114,847	705,275	2,664,965	1,594,927	4,259,892
Total liabilities and equity	**4,678,732**	**3,261,717**	**3,731,450**	**1,844,843**	**13,516,742**	**120,914**	**1,380,138**	**15,017,794**	**(1,135,271)**	**13,882,523**
Other segment items										
Capital investment	-	-	-	-	-	-	-	-	-	600,485
Depreciation	-	-	-	-	-	-	-	-	-	45,690

2017	Retail banking	Corporate banking	Investment banking	Other banking	Total banking	Brokerage	Other	Combined	Adjustments	Total
Operating income	472,787	800,146	167,381	14,500	1,454,814	75,566	438,894	1,969,274	(199,533)	1,769,741
Operating expense	(233,142)	(121,676)	(50,897)	(815,114)	(1,220,829)	(17,701)	(363,104)	(1,601,634)	142,658	(1,458,976)
Income from operations	**239,645**	**678,470**	**116,484**	**(800,614)**	**233,985**	**57,865**	**75,790**	**367,640**	**(56,875)**	**310,765**
Income tax expense	-	-	-	(56,038)	(56,038)	(11,380)	(16,647)	(84,065)	7,127	(76,938)
Net income for the year	**239,645**	**678,470**	**116,484**	**(856,652)**	**177,947**	**46,485**	**59,143**	**283,575**	**(49,748)**	**233,827**
Segment assets	2,080,582	4,828,009	3,270,241	-	10,178,832	111,399	517,010	10,807,241	(520,115)	10,287,126
Investments in equity participations	-	-	357,708	-	357,708	-	286,665	644,373	(590,321)	54,052
Other assets	-	-	-	569,143	569,143	8,972	165,057	743,172	(13,359)	729,813
Total assets	**2,080,582**	**4,828,009**	**3,627,949**	**569,143**	**11,105,683**	**120,371**	**968,732**	**12,194,786**	**(1,123,795)**	**11,070,991**
Segment liabilities	2,155,727	2,830,759	4,534,069	-	9,520,555	646	601,262	10,122,463	(2,353,366)	7,769,097
Equity and other liabilities	-	-	-	1,585,128	1,585,128	119,725	367,470	2,072,323	1,229,571	3,301,894
Total liabilities and equity	2,155,727	2,830,759	4,534,069	1,585,128	11,105,683	120,371	968,732	12,194,786	(1,123,795)	11,070,991
Other segment items										
Capital investment	-	-	-	-	-	-	-	-	-	50,265
Depreciation	-	-	-	-	-	-	-	-	-	72,336

(Currency - In thousands of Turkish Lira ("TL"))

10. Cash and cash equivalents

	31 December 2018	31 December 2017
Cash and balances with Central Bank	1,124,518	576,814
- Cash on hand	*136,011*	*24,934*
- Unrestricted balances with Central Bank	*988,507*	*551,880*
Placements with other banks	265,665	154,166
Cash and cash equivalents	**1,390,183**	**730,980**
Less: Interest income accruals on cash and cash equivalents	(5,797)	(4,028)
Cash and cash equivalents in the statement of cash flows	**1,384,386**	**726,952**

Explanation for statement cash flows

The effect of changes in foreign exchange rates on cash and cash equivalents includes the foreign exchange differences resulted from the translations of cash and cash equivalents in foreign currencies into TL at the exchange rates prevailing at the three months periods.

Expected credit losses on cash and cash equivalents (-)

	Stage 1	Stage 2	Stage 3	Total
Balances at 1 January 2018	**19**	**-**	**-**	**19**
Provision for the period	*54*	-	-	*54*
Recoveries and reversals	*(8)*	-	-	*(8)*
Balances at 31 December 2018	**65**	**-**	**-**	**65**

11. Reserve deposits at Central Bank

	31 December 2018	31 December 2017
Foreign currency	1,072,226	1,008,020
	1,072,226	**1,008,020**

According to the regulations of the Central Bank of Turkish Republic (the "Central Bank"), banks are obliged to reserve a portion of certain liability accounts as specified in the related decree. Such mandatory reserves are not available for use in the Bank's day-to-day operations.

The banks operating in Turkey keep reserve deposits for Turkish currency and foreign currency liabilities in TL and USD at the rates of 1.5-8% and 4-20%, respectively according to their maturity terms as per the Communiqué no. 2005/5 "Reserve Deposits" of the Central Bank of Turkey (31 December 2017: 4-10.5% for TL and 4-24% for USD).

Starting from November 2014, interest is paid on reserve requirements held in Turkish Lira and starting from May 2015, interest is paid on reserve requirements held in USD.

Expected credit losses on reserve deposits at Central Bank (-)

	Stage 1	Stage 2	Stage 3	Total
Balances at 1 January 2018	**210**	**-**	**-**	**210**
Provision for the period	*67*	-	-	*67*
Recoveries and reversals	-	-	-	-
Balances at 31 December 2018	**277**	**-**	**-**	**277**

(Currency - In thousands of Turkish Lira ("TL"))

12. Financial assets at fair value through profit or loss and trading liabilities

	31 December 2018
Financial assets at fair value through profit or loss	
- Government bonds and treasury bills	14,253
- Corporate Bonds	48,866
- Investment funds	372,322
Derivative assets	
- Foreign exchange	52,589
-Swap contracts	*24,174*
-Forward contracts	*27,074*
-Options	*1,341*
	488,030

	31 December 2017
Trading securities	
- Government bonds and treasury bills	93
- Corporate Bonds	658
- Investment funds	42,220
Derivative assets	
- Foreign exchange	8,985
-Swap contracts	*7,287*
-Forward contracts	*1,687*
-Options	*11*
	51,956

Trading liabilities

	31 December 2018	31 December 2017
Derivative liabilities		
- Foreign exchange	23,017	8,987
-Swap contracts	*11,366*	*7,275*
-Forward contracts	*10,304*	*1,712*
-Options	*1,347*	-
	23,017	**8,987**

As at 31 December 2018 and 2017, no trading securities are kept for legal requirements and as a guarantee for stock exchange and money market operations.

On the reporting date, the total notional amounts of outstanding derivative financial instruments contracts to which the Bank is committed are as follows:

	31 December 2018	31 December 2017
Forward foreign exchange contracts – buy (*)	450,544	238,929
Forward foreign exchange contracts – sell (*)	433,465	238,992
Swap foreign exchange contracts – buy	1,361,677	1,069,644
Swap foreign exchange contracts – sell	1,362,936	1,073,658
Option contracts – buy	359,229	719,048
Option contracts – sell	360,311	719,073
Future contracts – buy	-	-
Future contracts – sell	-	-

(*) Includes spot and forward transactions

(Currency - In thousands of Turkish Lira ("TL"))

13. Investment securities

31 December 2018	Interest rate %	Latest maturity	Carrying amount
Financial assets measured at amortized cost			
- Corporate bonds	7.12-29.42	10 May 2024	361,900
Financial assets measured at fair value through other comprehensive income			
- Government bonds	3.22-26.54	11 May 2047	891,394
- Corporate bonds	3.65-31.84	10 May 2024	1,084,199
			2,337,493

31 December 2017	Interest rate %	Latest maturity	Carrying amount
Held-to-maturity investment securities			
- Corporate bonds	7.12-20.45	10 May 2024	254,120
Available-for-sale investment securities			
- Government bonds	1.66-13.16	11 May 2047	704,173
- Corporate bonds	4.53-19.95	10 May 2024	606,524
			1,564,817

As at 31 December 2018, TL 48,534 and TL 1,578,960 of investment securities are given as collateral for performing transaction at stock exchange and repurchase agreement, respectively (31 December 2017: TL 625,162 and TL 598,404, respectively).

Expected credit losses on financial assets measured at fair value through other comprehensive income

	Stage 1	Stage 2	Stage 3	Total
Balances at 1 January 2018	**167**	**-**	**-**	**167**
Provision for the period	*137*	-	-	*137*
Recoveries and reversals	*(42)*	-	-	*(42)*
Balances at 31 December 2018	**262**	**-**	**-**	**262**

Expected credit losses on financial assets measured at amortized cost

	Stage 1	Stage 2	Stage 3	Total
Balances at 1 January 2018	**34**	**-**	**-**	**34**
Provision for the period	*17*	-	-	*17*
Recoveries and reversals	*(3)*	-	-	*(3)*
Balances at 31 December 2018	**48**	**-**	**-**	**48**

(Currency - In thousands of Turkish Lira ("TL"))

14. Loans and advances to customers

As at 31 December 2018 and 2017, all loans and advances to customers are recognized at amortised cost.

	Gross amount	Impairment allowance	Carrying amount	Gross amount	Impairment allowance	Carrying amount
	31 December 2018			**31 December 2017**		
-Other lending	7,092,185	(188,642)	6,903,543	6,670,024	(130,547)	6,539,477
Corporate loans	5,038,492	(37,281)	5,001,211	4,539,122	(32,031)	4,507,091
Consumer loans	2,053,693	(151,361)	1,902,332	2,130,902	(98,516)	2,032,386
	7,092,185	**(188,642)**	**6,903,543**	**6,670,024**	**(130,547)**	**6,539,477**

Allowance for impairment

	31 December 2018
Allowances for individual impairment	
Balance on 31 December 2017	96,405
Impact of adopting IFRS 9 at 1 January 2018	10,324
Balance on 1 January 2018	106,729
Impairment loss for the year	41,074
- Charge for the year	75,742
- Recoveries	(34,668)
Balance at the end of the period	**147,803**
Allowances for collective impairment	
Balance on 31 December 2017	34,142
Impact of adopting IFRS 9 at 1 January 2018	17,505
Balance on 1 January 2018	51,647
Impairment loss for the year	(10,808)
- Charge for the year	21,757
- Recoveries	(32,565)
Balance at the end of the period	**40,839**
Total allowances for impairment	**188,642**

	31 December 2017
Allowances for individual impairment	
Balance on 1 January 2017	57,481
Impairment loss for the year	38,924
- Charge for the year	38,924
Balance at the end of the period	**96,405**
Allowances for collective impairment	
Balance on 1 January 2018	17,830
Impairment loss for the year	16,312
- Charge for the year	16,312
Balance at the end of the period	**34,142**
Total allowances for impairment	**130,547**

(Currency - In thousands of Turkish Lira ("TL"))

14. Loans and advances to customers *(continued)*

Expected credit losses on loans and advances to customers

	Stage 1	Stage 2	Stage 3	Total
Balances at 1 January 2018	**23,305**	**28,342**	**106,729**	**158,376**
Provision for the period	*12,203*	*9,554*	*75,742*	*97,499*
Recoveries and reversals	*(13,554)*	*(19,011)*	*(34,668)*	*(67,233)*
Balances at 31 December 2018	**21,954**	**18,885**	**147,803**	**188,642**

Credit quality of loans and advances to customer

	2018				
	Stage 1	**Stage 2**	**Stage 3**	**Total**	**2017 Total**
Current	6,443,637	78,935	-	6,522,572	6,404,547
Overdue < 30 days	-	184,922	-	184,922	-
Overdue > 30 days	-	114,074	270,617	384,691	265,477
Total	**6,443,637**	**377,931**	**270,617**	**7,092,185**	**6,670,024**

The collaterals held against loans including accruals are presented below as per the collateral type, up to the outstanding total amount of exposures.

2018	Corporate/Commercial Loans	Consumer Loans	Credit Cards	Total
Cash collateral	192,396	-	-	192,396
Pledge assets	920,444	156,504	-	1,076,948
Unsecured	3,925,652	1,845,239	51,950	5,822,841
Total	**5,038,492**	**2,001,743**	**51,950**	**7,092,185**

2017	Corporate/Commercial Loans	Consumer Loans	Credit Cards	Total
Cash collateral	106,299	-	-	106,299
Pledge assets	737,047	-	-	737,047
Unsecured	3,695,776	2,094,578	36,324	5,826,678
Total	**4,539,122**	**2,094,578**	**36,324**	**6,670,024**

Finance lease receivables

None (31 December 2017: None).

(Currency - In thousands of Turkish Lira ("TL"))

15. Equity accounted investees

Carrying amount of equity accounted investees is summarized below:

	31 December 2018	31 December 2017
Kazakhstan Ijara Company Jsc.	12,685	9,299
Aktif Yatırım Bankası Sukuk Varlık Kiralama A.Ş.(*)	100	100
Euroasian Leasing Company	5,069	4,372
Company Euro Mediterranean Investment	6,452	6,415
Haliç Finansal Kiralama Anonim Şirketi	7,271	6,670
Aktif Halk Enerji Yatırımları A.Ş.	-	9,128
Halk Yenilenebilir Enerji A.Ş.	11,076	10,915
Solaren S4 Enerji Üretim A.Ş.	-	(942)
Idea Farm Ventures Limited	8,095	8,095
Epost Dış Ticaret A.Ş.	50	-
Equity accounted investees	**50,798**	**54,052**

(*) Aktif Bank Sukuk Varlık Kiralama A.Ş. ("VKŞ") engages in the operating activities of issuance of Sukuk. According to IFRS 10, the Bank should have the power, exposure to variable returns and the ability to use such power to affect those returns over the company. On the other hand, the Bank does not have power on VKŞ's financial statements, exposure or rights to variable returns from its involvement with VKŞ and the ability to use its power over VKŞ to affect the VKŞ's returns. Thus, VKŞ does not comply with consolidation requirements of IFRS 10 so, it is not being consolidated in the financial statements as at 31 December 2018 and 2017.

	2018	2017
Balance at 1 January	54,052	22,803
Share of profit/(loss) of equity-accounted investees	(6,003)	10,153
Additions	50	19,149
Currency translation difference	2,699	1,947
Balance at the end of the year	**50,798**	**54,052**

Summary financial information for equity accounted investees, not adjusted for the percentage ownership held by the Group, is as follows:

2018	**Ownership (%)**	**Total assets**	**Total liabilities and Equity**	**Profit / (loss) in the year**
Kazakhstan Ijara Company Jsc.	14.31	106,728	97,086	9,642
Aktif Bank Sukuk Varlık Kiralama A.Ş.	100	1,013,295	1,013,273	22
Euroasian Leasing Company	36.71	16,155	16,144	11
Euro Mediterranean Investment Company	25.53	49,760	49,616	144
Haliç Finansal Kiralama Anonim Şirketi	32	36,855	34,976	1,879
Aktif Halk Enerji Yatırımları A.Ş.	50	129,569	147,825	(18,256)
Halk Yenilenebilir Enerji A.Ş.	50	8,768	8,446	322
Idea Farm Ventures Limited	30	8,095	8,095	-
Epost Dış Ticaret A.Ş.	99.86	50	50	-

2017	**Ownership (%)**	**Total assets**	**Total liabilities and Equity**	**Profit / (loss) in the year**
Kazakhstan Ijara Company Jsc.	14.31	75,572	73,013	2,559
İFM İstanbul Finans Merkezi İnşaat Taahhüt A.Ş.	5	-	-	-
Aktif Bank Sukuk Varlık Kiralama A.Ş.	100	685,608	685,597	11
Euroasian Leasing Company	36.71	14,490	14,323	167
Euro Mediterranean Investment Company	25.53	25,085	22,906	2,179
Haliç Finansal Kiralama Anonim Şirketi	32	24,822	24,454	368
Aktif Halk Enerji Yatırımları A.Ş.	50	57,166	58,910	(1,744)
Halk Yenilenebilir Enerji A.Ş.	50	51,616	29,887	21,729
Solaren S4 Enerji Üretim A.Ş.	50	10,289	12,173	(1,884)

(Currency - In thousands of Turkish Lira ("TL"))

16. Tangible assets

	Machinery and equipment	Furniture and fixtures	Leasehold improvements	Motor vehicles	Construction in progress	Other fixed assets	Total
Cost							
Balance on 1 January 2017	67,962	24,826	10,405	198	235,368	868	339,627
Additions	1,804	5,833	163	108	50	3,830	11,788
Transfers to intangible assets	-	-	-	-	(1,113)	-	(1,113)
Capitalized borrowing costs	-	-	-	-	23,173	-	23,173
Disposals	(50)	(5)	(69)	(52)	(32,400)	-	(32,576)
Balance on 31 December 2017	**69,716**	**30,654**	**10,499**	**254**	**225,078**	**4,698**	**340,899**
Balance on 1 January 2018	69,716	30,654	10,499	254	225,078	4,698	340,899
Acquisitions through business combinations (note 38)	83,797	-	-	-	-	-	83,797
Additions	12,157	8,041	81	8,945	389,822	2,566	421,612
Transfers to intangible assets	(1,146)	(52)	(3,534)	-	-	-	(4,732)
Capitalized borrowing costs	-	-	-	-	23,814	-	23,814
Disposals	(91)	(391)	(73)	-	(244,132)	-	(244,687)
Balance on 31 December 2018	**164,433**	**38,252**	**6,973**	**9,199**	**394,582**	**7,264**	**620,703**
Depreciation and impairment							
Balance on 1 January 2017	42,690	15,845	5,388	28	-	(240)	63,711
Depreciation for the year	12,644	5,937	450	23	-	1,446	20,500
Disposals	(4)	(3)	(69)	(32)	-	-	(108)
Balance on 31 December 2017	**55,330**	**21,779**	**5,769**	**19**	**-**	**1,206**	**84,103**
Balance on 1 January 2018	55,330	21,779	5,769	19	-	1,206	84,103
Depreciation for the year	13,396	6,825	1,593	188	-	1,813	23,815
Disposals	(116)	(366)	-	(5)	-	-	(487)
Transfers to intangible assets	(1,146)	(52)	(3,534)	-	-	-	(4,732)
Balance on 31 December 2018	**67,464**	**28,186**	**3,828**	**202**	**-**	**3,019**	**102,699**
Carrying amounts							
Balance on 1 January 2017	25,272	8,981	5,017	170	235,368	1,108	275,916
Balance on 31 December 2017	14,386	8,875	4,730	235	225,078	3,492	256,796
Balance on 31 December 2018	96,969	10,066	3,145	8,997	394,582	4,245	518,004

(Currency - In thousands of Turkish Lira ("TL"))

17. Intangible assets

	Software	Computer programme	Rights (*)	Total
Cost				
Balance on 1 January 2017	46,796	44,318	191,396	282,510
-Acquisitions from subsidiaries	386	-	-	386
Additions:				
-Purchases	7,467	9	65	7,541
-Internally developed	-	11,449	-	11,449
Disposals	-	-	(4,834)	(4,834)
Transfers from property and equipment	-	193	920	1,113
Balance on 31 December 2017	**54,649**	**55,969**	**187,547**	**298,165**
Balance on 1 January 2018	54,649	55,969	187,547	298,165
- Acquisitions through business combinations (note 38)	-	-	65,656	65,656
Additions:				
-Purchases	997	-	1,299	2,296
-Acquisitions from subsidiaries	-	-	-	-
-Internally developed	-	27,074	-	27,074
Disposals	-	-	(5,764)	(5,764)
Transfers from property and equipment	-	-	4,732	4,732
Balance on 31 December 2018	**55,646**	**83,043**	**253,470**	**392,159**
Amortisation and impairment				
Balance on 1 January 2017	20,313	21,919	64,695	106,927
Impairment charges for the year	-	-	-	-
Amortisation for the year	9,493	11,758	30,585	51,836
Disposals	-	-	(3,935)	(3,935)
Transfers from property and equipment	-	-	-	-
Balance on 31 December 2017	**29,806**	**33,677**	**91,345**	**154,828**
Balance on 1 January 2018	29,806	33,677	91,345	154,828
Amortisation for the year	4,292	3,731	13,852	21,875
Disposals	-	-	(5,764)	(5,764)
Transfers from property and equipment	-	-	4,732	4,732
Balance on 31 December 2018	**34,098**	**37,408**	**104,165**	**175,671**
Carrying amounts				
Balance on 1 January 2017	26,483	22,399	126,701	175,583
Balance on 31 December 2017	24,843	22,292	96,202	143,337
Balance on 31 December 2018	21,548	45,635	149,305	216,488

There is no capitalised borrowing cost related to the internally developed software during the year (31 December 2017: None).

(*) A ten-year General Contract dated 27 August 2013, has been signed between the Bank and Turkish Football Federation (TFF) about the E-Ticket System which will be used for the entrance of the sport halls in Sport Clubs' league matches. Within the scope of the contract, the Bank has capitalized TL 12,946 amount as intangibles which was paid to Football Clubs in return of the consent for ticketing. As of the balance sheet, following the TFF acceptances of the stadiums in the E-Ticket System, the Bank has paid TL 159,423 to TFF, TL 52,309 has been recognized as an expense, and the remaining amount of TL 107,114 has been classified under other assets that will be recognized as an expense during the upcoming years the E-Ticket System will be used (31 December 2017: As of the balance sheet, following the TFF acceptances of the stadiums in the E-Ticket System, the Bank has paid TL 157,332 to TFF, TL 33,191 has been recognized as an expense, and the remaining amount of TL 124,141 has been classified under other assets that will be recognized as an expense during the upcoming years the E-Ticket System will be used.

(Currency - In thousands of Turkish Lira ("TL"))

18. Other assets

	31 December 2018	31 December 2017
Advances given	123,506	128,247
Prepaid expenses	84,310	31,653
Suspense accounts	37,446	24,885
Guarantees given	27,543	5,693
Income accrual	14,292	22,940
Fund service fee accrual	7,929	7,928
Credit card accounts	63	9,902
Others (*)	408,537	16,615
	703,626	**247,863**

(*) Includes the flats that not expected to be disposed within one year, which are amounting to TL 244,570, purchased by preliminary contract for sale.

19. Assets held for sale

	2018	2017
Balance at 1 January	71,067	-
Transfer from assets to be disposed-off	-	71,067
Addition	8,837	-
Disposal	(7,905)	-
Balance at 31 December	**71,999**	**71,067**

20. Obligations under repurchase agreements

	31 December 2018	31 December 2017
Obligations under repurchase agreements-TL	73,872	31,351
Obligations under repurchase agreements-FC	1,217,870	387,694
Money market fundings-TL	-	655,464
	1,291,742	**1,074,509**

21. Funds borrowed

	31 December 2018	31 December 2017
Domestic banks – TL	265,878	349,477
Domestic banks – Foreign currency	226,115	321,645
Foreign banks – TL	83,964	22,741
Foreign banks – Foreign currency	3,074,059	3,080,517
	3,650,016	**3,774,380**

22. Debt securities issued

As at 31 December 2018 and 2017, all debt securities issued are at amortised cost.

	31 December 2018	31 December 2017
Debt securities issued-TL	3,903,309	2,314,083
Debt securities issued-FC	462,404	462,205
	4,365,713	**2,776,288**

	31 December 2018	31 December 2017
Nominal of debt securities issued	5,145,125	3,059,585
Unaccrued interest expense	(779,412)	(283,297)
	4,365,713	**2,776,288**

(Currency - In thousands of Turkish Lira ("TL"))

23. Taxation

General information

The Bank is subject to taxation in accordance with the tax procedures and the legislation effective in Turkey.

In Turkey, effective from 1 January 2006 corporate tax rate is 20% (Corporate tax rate is going to be 22% for 2018, 2019 and 2020). The tax legislation provides for a temporary tax of 20% to be calculated and paid based on earnings generated for each quarter. The amounts which are calculated and paid are offset against the final corporate tax liability for the year.

Corporate tax losses can be carried forward for a maximum period of five years following the year in which the losses were incurred. The tax authorities can inspect tax returns and the related accounting records for a retrospective maximum period of five years. Corporate tax returns are required to be filed by the twenty-fifth day of the fourth month following the year-end balance sheet date and taxes must be paid in one instalment by the end of the fourth month.

As at 31 December 2018 and 2017, the current tax liability is as follows:

	31 December 2018	31 December 2017
Income tax liability	114,396	85,783
Prepaid taxes	(65,807)	(67,391)
Income taxes payable	**48,589**	**18,392**

For the year ended 31 December 2018 and 2017, the income tax expense recognised in profit or loss and income tax recognised directly in equity are as follows:

Recognised in profit or loss

	2018	2017
Current tax expense from continuing operations	(113,830)	(92,603)
Deferred tax from continuing operations	15,052	15,665
Total income tax	**(98,778)**	**(76,938)**

Reconciliation of effective tax rate

Reconciliation between tax expense and the accounting profit multiplied by the statutory income tax rate of the Bank for the year ended 31 December 2018 and 2017 is as follows:

	2018	Rate %	2017	Rate %
Profit for the year	381,672		233,827	
Total income tax expense	98,778		76,938	
Profit before income tax	**480,450**		**310,765**	
Income tax using the domestic corporation tax rate	(105,699)	(22.00)	(62,153)	(20.00)
Non-deductible expenses	(12,169)	(2.53)	(27,763)	(8.93)
Non-utilized tax losses	(49)	(0.01)	(3,233)	(1.04)
Tax exempt income	8,140	1.69	-	-
Other	10,999	2.29	16,211	5.22
Total income tax in the profit or loss	**(98,778)**	**(20.56)**	**(76,938)**	**(24.75)**

(Currency - In thousands of Turkish Lira ("TL"))

23. Taxation *(continued)*

Deferred tax

Recognised deferred tax assets and liabilities

The deferred tax included in the statement of financial position and recognised in profit or loss and in equity are as follows:

	31 December 2018			31 December 2017		
	Assets	**Liabilities**	**Net**	**Assets**	**Liabilities**	**Net**
Financial assets measured at fair value through other comprehensive income	462	(310)	152	(857)	-	(857)
Reserve for employee benefits	2,147	-	2,147	2,137	-	2,137
Tangible assets and intangible assets	7,835	(591)	7,244	5,870	(14,463)	(8,593)
Tax losses carried forward	7,824	-	7,824	1,098	-	1,098
Expected credit losses(*)	15,358	-	15,358	-	-	-
Acquisition of subsidiaries	-	(14,444)	(14,444)	-	-	-
Other	13,804	(9,766)	4,038	16,939	(2,308)	14,631
Deferred tax	**47,430**	**(25,111)**	**22,319**	**25,187**	**(16,771)**	**8,416**

(*) The balance includes the IFRS 9 transition impact of TL 6,866.

Recognised deferred tax assets and liabilities in the statement of financial position are as follows:

	31 December 2018	**31 December 2017**
Deferred tax assets	36,987	10,246
Deferred tax liabilities	(14,668)	(1,830)
	22,319	**8,416**

Movements in temporary differences during the year

2018	**Opening balance**	**Transition impact of IFRS 9**	**Recognised in profit or loss**	**Recognised in equity**	**Acquired in Business Combinations**	**Closing balance**
Financial assets measured at fair value through other comprehensive income	(857)	-	(5,646)	6,655	-	152
Reserve for employee benefits	2,137	-	266	(257)	-	2,146
Tangible assets and intangible assets	(8,593)	-	15,837	-	-	7,244
Tax losses carried forward	1,098	-	6,726	-	-	7,824
Impact of adopting IFRS 9	-	6,866	-	-	-	6,866
Acquisition of subsidiaries	-	-	-	-	(14,444)	(14,444)
Other	14,631	-	(2,131)	31	-	12,531
	8,416	**6,866**	**15,052**	**6,429**	**(14,444)**	**22,319**

(Currency - In thousands of Turkish Lira ("TL"))

23. Taxation *(continued)*

Deferred tax *(continued)*

Movements in temporary differences during the year *(continued)*

2017	Opening balance	Recognised in profit or loss	Recognised in equity	Closing balance
Available-for-sale investment securities	1,242	(991)	(1,108)	(857)
Reserve for employee benefits	1,670	323	144	2,137
Tangible assets and intangible assets	(9,864)	1,271	-	(8,593)
Tax losses carried forward	919	179	-	1,098
Other	(252)	14,883	-	14,631
	(6,285)	**15,665**	**(964)**	**8,416**

Expiration schedule of carry forward tax losses is as follows:

	31 December 2018	31 December 2017
Expiring in 2018	-	-
Expiring in 2019	-	-
Expiring in 2020	894	5,490
Expiring in 2021	570	-
Expiring in 2022	882	-
Expiring in 2023	33,218	-
Total	**35,564**	**5,490**

24. Provisions

	31 December 2018	31 December 2017
Provision for possible losses (*)	133,000	170,000
Vacation pay liability	4,360	4,085
Employee termination benefits	6,499	6,602
Other (**)	77,693	60,279
Total	**221,552**	**240,966**

(*) As at 31 December 2018, the accompanying consolidated statement of financial position includes a free provision amounting to TL 133,000 provided by the Bank management in line with conservatism principle considering the circumstances which may arise from any changes in the economy or market conditions (31 December 2017: TL 170,000).

(**) Includes bonus, lawsuit and other provisions.

Employee termination benefits

In accordance with existing social legislation in Turkey, 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 of 30 days' pay (limited to a maximum of TL 5.43 and TL 4.73 on 31 December 2018 and 2017, respectively) per year of employment at the rate of pay applicable on the date of retirement or termination. In the consolidated financial statements as at 31 December 2018 and 2017, the Group reflected a liability calculated using the hypothetical method and based 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 on government bonds on the reporting date.

(Currency - In thousands of Turkish Lira ("TL"))

24. Provisions *(continued)*

The principal actuarial assumptions used on the reporting dates are as follows:

	31 December 2018	31 December 2017
Discount rate	14.50%	11.50%
Inflation rate	9.50%	8.30%

The movement in provision for employee termination benefits is as follows:

	2018	2017
Opening balance	6,602	5,354
Interest cost	899	184
Service cost	2,086	2,395
Payment during the year	(1,922)	(2,052)
Actuarial loss/(gain)	(1,166)	721
Balance at the end of the year	**6,499**	**6,602**

25. Other liabilities

	31 December 2018	31 December 2017
Customer accounts (*)	1,624,270	1,201,545
Intermediary payment account	472,121	364,037
Blocked amounts (**)	64,401	87,316
Suspense accounts	55,044	26,028
Taxes and due payable	32,616	27,577
Unearned income	30,286	31,780
Credit card accounts	14,472	15,353
Payables to compulsory government funds	6,037	6,602
Expense accrual	4,681	5,567
Cash collaterals received	-	3,071
Other	97,052	48,880
	2,400,980	**1,817,756**

(*) The Bank is not entitled to collect deposits. The customer accounts represent the current balances of loan customers.

(**) The balance is resulted from wage payment accounts blocked until the date of wage payment.

26. Capital and reserves

	31 December 2018	31 December 2017
Number of common shares, TL 1,000 (in full TL), par value (Authorised and issued)	1,193,585	1,033,585

As at 31 December 2018 and 2017, all issued shares are fully paid and there is no preference shares assigned to shareholders of the Bank.

(Currency - In thousands of Turkish Lira ("TL"))

26. Capital and reserves *(continued)*

Share capital and share premium

As at 31 December 2018 and 2017, the composition of shareholders and their respective percentage of ownership are summarised as follows:

	31 December 2018		31 December 2017	
	Amount	**%**	**Amount**	**%**
Çalık Holding A.Ş.	1,186,791	99.43	1,027,636	99.42
Çalık Denim Tekstil San. ve Tic. A.Ş.	3,597	0.30	3,149	0.30
Ahmet Çalık	1,599	0.13	1,400	0.14
Başak Yönetim Sistemleri A.Ş.	799	0.07	700	0.07
Irmak Yönetim Sistemleri A.Ş.	799	0.07	700	0.07
Total paid-in-capital	**1,193,585**	**100.00**	**1,033,585**	**100.00**
Restatement effect per IAS 29	4,510		4,510	
Total share capital	**1,198,095**		**1,038,095**	

At the general assembly meeting held on 13 December 2018 the paid-in capital of the Bank increased by amounting to TL 160,000 from TL 1,033,585 to TL 1,193,585 which has been provided by amounting to TL 147,000 from internal resources and increased by amounting to TL 13,000 in cash (31 December 2017: At the extraordinary general meeting dated 24 March 2017, the Bank's paid-in capital of TL 933,585 reaches TL 1,033,585 with an increase of TL 100,000, which consist of TL 100,000 from retained earnings).

Reserves

Fair value reserve

As at 31 December 2018, this reserve includes the cumulative net change in the fair value of financial assets measured at fair value through other comprehensive income until the investment is derecognised or impaired. As at 31 December 2017, this reserve includes the cumulative net change in the fair value of financial assets measured at fair value through other comprehensive income until the investment is derecognised or impaired.

Other reserves

Other reserves consist of legal reserves. The legal reserves consist of first and second legal reserves. 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 entity's share capital. The second legal reserve is appropriated at the rate of 10% of all distributions in excess of 5% of the entity's 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.

Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations.

Special funds

Special funds refer to the funds allocated from net income or retained earnings due to the tax advantage of local legal regulations.

(Currency - In thousands of Turkish Lira ("TL"))

27. Net interest income

	2018	2017
Interest income		
Loans and advances to customers	1,023,425	853,228
Investment securities	253,987	133,781
Cash and cash equivalents	50,349	31,156
Other	5,162	3,344
Total interest income	**1,332,923**	**1,021,509**
Interest expense		
Debt issued	595,177	349,513
Funds borrowed	182,492	43,402
Money market transactions	126,937	56,486
Other	2,743	1,589
Total interest expense	**907,349**	**450,990**
Net interest income	**425,574**	**570,519**

28. Net fee and commission income

	2018	2017
Fees and commission income		
Intermediary commissions	69,204	44,238
Commitment fee	32,081	33,683
Delivery fee	31,926	9,849
Financial guarantee contracts issued	15,662	13,308
Remittance fee	15,423	108,340
Insurance fee	13	3,092
Other	11,709	35,929
Total fees and commission income	**176,018**	**248,439**
Fees and commission expense		
Clearance commissions	49,291	55,196
Credit card commissions	15,802	11,298
Financial guarantee contracts issued	1,919	1,193
Other	10,392	5,970
Total fees and commission expense	**77,404**	**73,657**
Net fees and commission income	**98,614**	**174,782**

29. Net trading loss / Income

	2018	2017
Foreign exchange gain/(loss)	(128,296)	5,468
Trading account gain/(loss)	(26,704)	8,512
Gain/(loss) from derivative financial instruments	144,558	(52,720)
Total	**(10,442)**	**(38,740)**

(Currency - In thousands of Turkish Lira ("TL"))

30. Sales income and cost of services

Sales income:

	2018	2017
Revenue from sale of goods	400,112	180,157
Transaction and other commission income	77,617	59,994
Insurance commission income	52,779	60,739
Revenue from cash register POS	41,185	96,065
Revenue from license fee	1,245	381
Other sales income	16,365	9,934
Total	**589,303**	**407,270**

Cost of services:

	2018	2017
Dealer commission and other commission expenses	22,081	25,646
Maintenance expenses	20,591	48,034
Cost of merchandises sold	18,462	6,906
Cost of cash register POS	15,318	72,389
Rent expenses	4,273	4,383
Consultancy expenses	860	1,129
Depreciation and amortization expenses	200	712
Other expenses	18,602	10,832
Total	**100,387**	**170,031**

31. Other income

	2018	2017
Gain on sale of assets	60,299	27,877
Income from business combination	40,692	-
Reversal of provision for possible losses	37,000	-
Reversal of provision for corporate tax	13,216	3,050
Asset-backed security profit sharing	652	310
Gain on sale of subsidiary	-	43,232
Other	27,441	7,901
Total	**179,300**	**82,370**

32. Net impairment on financial assets

	2018	2017
Individual impairment for loans	41,074	38,924
Collective impairment provision for loans	(10,808)	16,312
Other	1,075	126
Total	**31,341**	**55,362**

33. Personnel expenses

	2018	2017
Wages and salaries	111,247	108,875
Social security premiums	16,512	13,636
Provision for employee benefits	3,564	2,664
Other	45,403	41,071
Total	**176,726**	**166,246**

(Currency - In thousands of Turkish Lira ("TL"))

34. Administrative expenses

	2018	2017
Publicity expenses	49,301	43,862
Taxes and dues other than on income	27,657	14,471
Rent expenses	24,097	16,902
Consultancy expenses	14,112	7,968
Maintenance expenses	11,091	17,600
Outsource expenses	10,798	10,701
Communication expenses	9,462	9,595
Expenses on vehicles	8,111	6,254
Others	46,071	37,223
Total	**200,700**	**164,576**

35. Other operating expenses

	2018	2017
Marketing expenses	9,021	4,587
Provision expenses	5,416	16,316
Other	42,724	41,053
Total	**57,161**	**61,956**

Other expenses

	2018	2017
Provision for possible losses	-	140,000
Total	**-**	**140,000**

36. Related parties

Parent and ultimate controlling party

The Bank is controlled by Çalık Holding A.Ş. which owns 99.43% of ordinary shares (31 December 2017: 99.42%).

Compensation of key management personnel of the Group

Total salaries and other benefits paid to the Board of Members and top management during the year is TL 32,278 (31 December 2017: TL 22,973).

Balances with related parties

31 December 2018	Related party balances	Total balance	Rate (%)
Loans and advances to customers	2,890,750	6,903,543	41.87
Other liabilities (Customer accounts)	7,584	1,624,270	0.47
Debt securities issued	21,000	4,365,713	0.48
31 December 2017	**Related party balances**	**Total balance**	**Rate (%)**
Loans and advances to customers	2,185,383	6,539,477	33.42
Other liabilities (Customer accounts)	61,482	1,201,545	5.12
Debt securities issued	28,317	2,776,288	1.02

(Currency - In thousands of Turkish Lira ("TL"))

36. Related parties *(continued)*

Off statement of financial position balances with related parties

31 December 2018	Related party balances	Total balance	Rate (%)
Non-cash loans	418,678	1,232,225	33.98

31 December 2017	Related party balances	Total balance	Rate (%)
Non-cash loans	640,395	1,308,957	48.92

Transactions with related parties

	2018	2017
Interest income on loans	308,598	165,315
Fee and commission income	6,940	5,966
Other expenses	8,011	4,476

37. Commitments and contingencies

	31 December 2018	31 December 2017
Letters of guarantee	1,007,343	1,151,664
Letters of credit	58,122	136,693
Other guarantees	166,760	20,600
Total non-cash loans	**1,232,225**	**1,308,957**
Check limits	2,037	1,718
Other commitments	203,355	410,207
Total	**1,437,617**	**1,720,882**

38. Acquisitions of subsidiaries

Business combinations/acquisition of solar energy SPVs

According to share transfer agreements dated 9 June 2017, 4 May 2018 and 7 May 2018, Emlak Girişim Danışmanlığı A.Ş. decided to purchase 100% of shares of Solar Energy SPVs for a total consideration of TL 12,636. On 30 September 2018, share transfers were finalised and Emlak Girişim Danışmanlığı A.Ş. obtained control by acquiring 100% of shares and voting rights in SPVs.

Preacquisition carrying amounts were determined based on the applicable IFRSs immediately before the acquisition. The values of assets, liabilities and contingent liabilities recognised on acquisition are their estimated fair values.

(Currency - In thousands of Turkish Lira ("TL"))

38. Acquisitions of subsidiaries *(continued)*

Business combinations/acquisition of solar energy SPVs (continued)

The following summarises the major classes of consideration transferred and the recognised amounts of assets acquired and liabilities assumed at the acquisition date:

Consideration transferred	
Cash paid	12,636
Total consideration	**12,636**
Identifiable assets acquired and liabilities assumed	**Recognized values on acquisition**
Cash & cash equivalents	257
Trade and other receivables	7,924
Other assets	33,040
Tangible assets (note 16)	83,797
Intangible assets (note 17)	65,656
Total assets	**190,674**
Funds borrowed	135,680
Trade and other payables	9,749
Other liabilities	18,061
Deferred tax liability	14,444
Total liabilities	**177,934**
Total net identifiable assets	**12,740**
Total consideration transferred	**12,636**
Less: Value of net identifiable assets	(12,740)
Amount recognized in profit or loss as income	**(104)**
Cash consideration transferred	12,636
Cash & cash equivalents acquired	(257)
Net cash outflow arising from acquisition	**12,379**

38. Acquisitions of subsidiaries *(continued)*

Business combinations/acquisition of solar energy SPVs (continued)

Measurement of fair values

The valuation techniques used for measuring the fair value of material assets acquired were as follows.

Assets acquired	**Valuation technique**
Tangible assets	Cost technique: Depreciated replacement cost when appropriate. Depreciated replacement cost reflects adjustments for physical deterioration as well as functional and economic obsolescence.
Intangible assets	Discounted cash flows: The valuation model considers the present value of the net cash flows expected to be generated by the right of solar energy production. The expected net cash flows are discounted using a risk-adjusted discount rate. Significant unobservable inputs are expected revenue growth rate and risk adjusted discount rates.

39. Subsequent events

None.