**Anadolubank Anonim Şirketi**
**And Its Subsidiaries**

Consolidated Financial Statements
As At and For The Year Ended
31 December 2018
With Independent Auditor's Report Thereon

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# Independent Auditor's Report

To the General Assembly of Anadolubank Anonim Şirketi,

## *Qualified Opinion*

We have audited the consolidated financial statements of Anadolubank 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 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 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 TL 50,000 thousands which was recognized as an expense in the current period provided by the Bank Management for possible effects of the negative circumstances which may arise in the economy or market conditions. Recognition of this general reserve constitutes a departure from IFRS. If this reserve was not recognized, retained earnings would be increased by TL 50,000 thousands and other liabilities and provisions would be decreased by TL 50,000 thousands as at 31 December 2018. Additionally, profit before tax and profit for the year would be increased by TL 50,000 thousands and other expenses would be decreased by TL 50,000 thousands for the year then ended.

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.

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*Key Audit Matters*

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the *Basis for Qualified Opinion* section, we have determined the matters described below to be the key audit matters to be communicated in our report.

*Impairment of loans and receivables measured at amortised cost*

Refer to "Significant accounting policies" Note 3.9 to the consolidated financial statements relating to the impairment of loans and receivables.

| Key audit matter | How the matter was addressed in our audit |
|---|---|
| As of 31 December 2018, loans and receivables measured at amortised cost comprise 66% of the Group's total assets.<br><br>The Bank recognizes its loans and receivables in accordance with the IFRS 9 Financial Instruments standard ("Standard").<br><br>As of 1 January 2018, due to the adoption of the Standard, in determining the impairment of loans and receivables is started to apply "expected credit loss model" rather than the "incurred loss model". The new model contains significant assumptions and estimates.<br><br>The significant assumptions and estimates of the Group's management are as follows:<br><br>✓ Significant increase in credit risk;<br><br>✓ Incorporating the forward looking macroeconomic information in calculation of credit risk; and<br><br>✓ Design and implementation of expected credit loss model.<br><br>The determination of the impairment of loans measured at amortised cost depends on the credit default status. Also, the model based on the change in the credit risk at the initial recognition date and the classification of the loans measured at amortised cost according to the model. Establishing an accurate classification is a significant process as the calculation of expected credit loss varies to the staging of the financial assets. | Our procedures for testing the impairment of loans included below:<br><br>• We tested the design and operating effectiveness of the controls on lending, collateralization, collection, follow-up, classification and impairment procedures with the involvement of information risk management specialists.<br><br>• We evaluated the Group's business model whose objective is to hold financial assets in order to collect contractual cash flows and we tested the appropriateness of the loan agreements with the model by selecting samples.<br><br>• We evaluated the adequacy of the subjective and objective criteria that is defined in the Group's impairment accounting policy compared with the Standard.<br><br>• We evaluated the Group's business model and methodology and the evaluation of the calculations were carried out with the control testing and detailed analysis with the involvement of specialist.<br><br>• We performed loan reviews for selected loan samples which include a detailed examination of loan files and related information and testing their classification. In this context, the current status of the loan customer has been evaluated by including prospective information and macroeconomic variables. |

| | |
|---|---|
| The Group calculates expected credit losses on both an individual and a collective basis. Individual provisions consider the estimated future performance of the business and the fair value of the collateral provided for credit transactions.<br><br>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.<br><br>Impairment on loans measured at amortised cost was considered to be a key audit matter, due to the significance of the estimates, assumptions, the level of judgments and its complex structure as explained above. | • We evaluated the adequacy of the expected credit loss calculations by selecting sample for the loans which are assessed on individual basis.<br><br>• 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.<br><br>• We assessed the macroeconomic models which are used to reflect forward looking expectations and tested the effect of the risk parameters by recalculation method.<br><br>• We evaluated the qualitative and quantitative assessments which are used in determining the significant increase in credit risk.<br><br>• Additionally, we also evaluated the adequacy of disclosures in the consolidated financial statements related to impairment provisions. |

*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.

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

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

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

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

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

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 auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

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

Alper Güvenç
Partner

31 July 2019
Istanbul, Turkey

**ANADOLUBANK ANONİM ŞİRKETİ AND ITS SUBSIDIARIES**

**CONSOLIDATED STATEMENT OF FINANCIAL POSITION**
**AS AT 31 DECEMBER 2018**
*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

| | *Notes* | **Audited 31 December 2018** | **Audited 31 December 2017** |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and cash equivalents | *5* | 167,778 | 59,818 |
| Balances with central bank | *6* | 590,161 | 511,426 |
| Reserve deposits at central bank | *6* | 701,940 | 1,310,653 |
| Loans and advances to banks and other financial institutions | *5* | 1,508,141 | 1,043,943 |
| Receivables from reverse repurchase transactions | *5* | 273,336 | 109,295 |
| Financial assets at fair value through profit or loss | *7* | 1,633 | |
| Trading assets | *7* | | 110,372 |
| Derivative financial assets held for trading | *8* | 23,950 | 28,871 |
| Investment securities | *9* | 1,318,129 | 1,236,588 |
| *Financial assets at fair value through other comprehensive income* | | *756,692* | |
| *Available-for-sale* | | | *1,236,588* |
| *Financial assets measured at amortised cost* | | *561,437* | |
| Loans and receivables | *10, 11* | 12,040,506 | 13,077,390 |
| Property and equipment | *12* | 202,080 | 219,035 |
| Intangible assets | *13* | 9,792 | 8,015 |
| Deferred tax assets | *18* | 53,837 | 25,403 |
| Other assets | *14* | 608,413 | 409,427 |
| **Total assets** | | **17,499,696** | **18,150,236** |
| **LIABILITIES** | | | |
| Deposits from banks | *15* | 144,362 | 366,325 |
| Deposits from customers | *15* | 12,726,125 | 12,980,125 |
| Obligations under repurchase agreements | *15* | 380,786 | 827,036 |
| Interbank money market borrowings | *15* | 337,551 | 393,731 |
| Funds borrowed | *16* | 722,936 | 801,662 |
| Derivative financial liabilities held for trading | *8* | 33,328 | 23,420 |
| Current tax liabilities | *18* | 35,552 | 22,845 |
| Deferred tax liabilities | *18* | - | 2,434 |
| Other liabilities and provisions | *17* | 794,593 | 564,657 |
| **Total liabilities** | | **15,175,233** | **15,982,235** |
| **EQUITY** | | | |
| Share capital | *19* | 602,619 | 602,619 |
| Legal reserves | *19* | 81,945 | 72,757 |
| Other reserves | *19* | 48,828 | 66,010 |
| Translation reserve | *19* | 249,568 | 194,666 |
| Fair value reserve | *19* | (59,656) | (9,346) |
| Retained earnings | | 1,397,694 | 1,238,484 |
| **Total equity attributable to equity holders of the Bank** | | **2,320,998** | **2,165,190** |
| **Non-controlling interests** | ***19*** | **3,465** | **2,811** |
| **Total equity** | | **2,324,463** | **2,168,001** |
| **Total liabilities and equity** | | **17,499,696** | **18,150,236** |

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

**ANADOLUBANK ANONİM ŞİRKETİ AND ITS SUBSIDIARIES**

**CONSOLIDATED STATEMENT OF PROFIT OR LOSS**
**FOR THE YEAR ENDED 31 DECEMBER 2018**

*(Amounts expressed in thousands of Turkish Lira (“TL”) unless otherwise stated.)*

| | *Notes* | **Audited 2018** | **Audited 2017** |
|---|---|---|---|
| **Continuing operations:** | | | |
| ***Interest income:*** | | | |
| Interest on loans and receivables | *21* | 2,372,196 | 1,530,791 |
| Interest on marketable securities | *21* | 71,971 | 70,675 |
| Interest on loans and advances to banks and other financial institutions | *21* | 48,882 | 23,974 |
| Interest on other money market placements | *21* | 11,446 | 10,652 |
| Other interest income | *21* | 20,459 | 8,309 |
| **Total interest income** | | **2,524,954** | **1,644,401** |
| ***Interest expenses:*** | | | |
| Interest on deposits | *21* | (1,542,630) | (950,547) |
| Interest on other money market deposits | *21* | (18,138) | (32,669) |
| Interest on funds borrowed | *21* | (69,046) | (49,313) |
| Other interest expenses | *21* | (2,300) | (4,652) |
| **Total interest expenses** | | **(1,632,114)** | **(1,037,181)** |
| **Net interest income** | | **892,840** | **607,220** |
| Fee and commission income | *22* | 224,875 | 173,994 |
| Fee and commission expenses | *22* | (33,898) | (20,562) |
| **Net fee and commission income** | | **190,977** | **153,432** |
| Trading income from marketable securities | | 1,488 | 5,308 |
| Trading gains/(losses) from derivatives, net | | 75,426 | (101,567) |
| Foreign exchange gain/(loss), net | | (86,189) | 40,488 |
| Other income | | 47,642 | 15,376 |
| **Revenue** | | **1,122,184** | **720,257** |
| Salaries and employee benefits | *23* | (272,980) | (248,594) |
| Provision for possible loan losses, net of recoveries | *10* | (243,701) | (87,808) |
| Depreciation and amortisation | | (13,937) | (12,983) |
| Taxes other than on income | | (22,120) | (22,434) |
| Other expenses | *24* | (160,996) | (103,894) |
| **Profit before tax** | | **408,450** | **244,544** |
| Income tax expense | *18* | (99,266) | (48,471) |
| **Profit for the year** | | **309,184** | **196,073** |
| **Profit for the year attributable to:** | | | |
| Equity holders of the Bank | | 308,530 | 195,600 |
| Non-controlling interests | | 654 | 473 |
| **Profit for the year** | | **309,184** | **196,073** |
| **Basic earnings per share from continuing operations (full TL)** | | 0.00515 | 0.00326 |

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

## ANADOLUBANK ANONİM ŞİRKETİ AND ITS SUBSIDIARIES

## CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2018

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

| | *Notes* | **Audited 2018** | **Audited 2017** |
|---|---|---|---|
| **Profit for the year** | | **309,184** | **196,073** |
| **Other comprehensive income:** | | | |
| Foreign currency translation differences for foreign operations | | 134,339 | 69,231 |
| Revaluation of property and equipment, net of tax | *19* | (9,851) | 72,141 |
| Financial assets at fair value through other comprehensive income – net change in fair value | | (50,310) | 32,270 |
| **Other comprehensive income for the year, net of tax** | | **74,178** | **173,642** |
| **Total comprehensive income for the year** | | **383,362** | **369,715** |
| **Total comprehensive income attributable to:** | | | |
| Equity holders of the Bank | | 382,708 | 369,242 |
| Non-controlling interests | | 654 | 473 |
| **Total comprehensive income for the year** | | **383,362** | **369,715** |

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

## ANADOLUBANK ANONİM ŞİRKETİ AND ITS SUBSIDIARIES

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
## FOR THE YEAR ENDED 31 DECEMBER 2018

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

| | | Attributable to equity holders of the Bank | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | *Notes* | Share capital | Legal reserves | Other reserves | Translation reserve | Fair value reserve | Retained earnings | Total | Non-controlling interests | Total |
| **Balances at 1 January 2017** | *19* | **602,619** | **63,168** | **(6,065)** | **125,435** | **(41,616)** | **1,052,473** | **1,796,014** | **2,341** | **1,798,355** |
| **Net profit for the year** | | **-** | **-** | **-** | **-** | **-** | **195,600** | **195,600** | **473** | **196,073** |
| **Total other comprehensive income** | | **-** | **-** | **72,141** | **69,231** | **32,270** | **-** | **173,642** | **-** | **173,642** |
| Other comprehensive income | | - | - | 72,141 | - | 32,270 | - | 104,411 | - | 104,411 |
| Currency translation adjustments | | - | - | - | 69,231 | - | - | 69,231 | - | 69,231 |
| **Total comprehensive income for the year** | | **-** | **-** | **72,141** | **69,231** | **32,270** | **195,600** | **369,242** | **473** | **369,715** |
| **Transactions with owners, recorded directly in equity** | | **-** | **9,589** | **(66)** | **-** | **-** | **(9,589)** | **(66)** | **(3)** | **(69)** |
| Transfers to other reserves | | - | 9,589 | (66) | - | - | (9,589) | (66) | (3) | (69) |
| **Balances at 31 December 2017** | *19* | **602,619** | **72,757** | **66,010** | **194,666** | **(9,346)** | **1,238,484** | **2,165,190** | **2,811** | **2,168,001** |

| | | Attributable to equity holders of the Bank | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | *Notes* | Share capital | Legal reserves | Other reserves | Translation reserve | Fair value reserve | Retained earnings | Total | Non-controlling interests | Total |
| **Balances at 1 January 2018** | *19* | **602,619** | **72,757** | **66,010** | **194,666** | **(9,346)** | **1,238,484** | **2,165,190** | **2,811** | **2,168,001** |
| Adjustment on initial application of IFRS9 (Net of tax) | *2.6* | - | - | - | - | - | (140,132) | (140,132) | - | (140,132) |
| **Adjusted balance at 1 January 2018** | | **602,619** | **72,757** | **66,010** | **194,666** | **(9,346)** | **1,098,352** | **2,025,058** | **2,811** | **2,027,869** |
| **Net profit for the year** | | **-** | **-** | **-** | **-** | **-** | **308,530** | **308,530** | **654** | **309,184** |
| **Total other comprehensive income** | | **-** | **-** | **(9,851)** | **134,339** | **(50,310)** | **-** | **74,178** | **-** | **74,178** |
| Other comprehensive income | | - | - | (9,851) | - | (50,310) | - | (60,161) | - | (60,161) |
| Currency translation adjustments | | - | - | - | 134,339 | - | - | 134,339 | - | 134,339 |
| **Total comprehensive income for the year** | | **-** | **-** | **(9,851)** | **134,339** | **(50,310)** | **308,530** | **382,708** | **654** | **383,362** |
| **Transactions with owners, recorded directly in equity** | | **-** | **9,188** | **(7,331)** | **(79,437)** | **-** | **(9,188)** | **(86,768)** | **-** | **(86,768)** |
| Transfers to other reserves | | - | 9,188 | (7,331) | (79,437) | - | (9,188) | (86,768) | - | (86,768) |
| **Balances at 31 December 2018** | *19* | **602,619** | **81,945** | **48,828** | **249,568** | **(59,656)** | **1,397,694** | **2,320,998** | **3,465** | **2,324,463** |

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

**ANADOLUBANK ANONİM ŞİRKETİ AND ITS SUBSIDIARIES**

**CONSOLIDATED STATEMENT OF CASH FLOWS**
**FOR THE YEAR ENDED 31 DECEMBER 2018**

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

| | Notes | Audited 2018 | Audited 2017 |
|---|---|---|---|
| **Cash flows from operating activities:** | | | |
| Profit for the year | | 309,184 | 196,073 |
| **Adjustments for:** | | | |
| Taxation | 18 | 99,266 | 48,471 |
| Provision for loan losses | | 243,701 | 87,808 |
| Depreciation and amortisation | | 13,937 | 12,983 |
| Provision for retirement pay liability | 17 | 11,452 | 5,935 |
| Unused vacation accruals | 17 | 3,476 | 2,402 |
| Derivative financial instruments | | 14,829 | (11,844) |
| Net interest income | | (892,840) | (607,220) |
| Other | | (247,041) | (409,201) |
| | | **(444,036)** | **(674,593)** |
| **Changes in:** | | | |
| Reserve deposits at the Central Bank | | 422,018 | 346,981 |
| Financial assets at fair value through profit or loss | | 108,396 | (6,173) |
| Loans and receivables | | 1,170,252 | (3,173,190) |
| Funds borrowed (net) | | (84,185) | (221,062) |
| Other assets | | (161,262) | 1,421 |
| Deposits from other banks and customers | | (511,630) | 2,759,541 |
| Other liabilities and provisions | | (424,507) | 441,716 |
| | | **75,046** | **(525,359)** |
| Interest received | | 2,293,301 | 1,574,673 |
| Interest paid | | (1,589,981) | (1,007,553) |
| Retirement benefits paid | 17 | (6,791) | (4,761) |
| Unused vacation accruals | 17 | (1,585) | (1,528) |
| Income taxes paid | | (83,201) | (58,973) |
| **Net cash provided by operating activities** | | **686,789** | **(23,501)** |
| **Cash flows from investing activities** | | | |
| Acquisition of financial assets measured at amortised cost | 9 | (89,952) | |
| Acquisition of property and equipment | 12 | (2,241) | (16,105) |
| Proceeds from sale of property and equipment | 12 | 4,978 | 2,560 |
| Acquisition of intangible assets | 13 | (6,425) | (3,651) |
| Acquisitions of financial assets at FVOCI | | (49,103) | |
| Acquisitions of available-for-sale financial assets | | | (211,986) |
| Proceeds from sale of financial assets at FVOCI | | 166,777 | |
| Proceeds from sale of available-for-sale financial assets | | | 288,651 |
| Other | | 558 | 5,409 |
| **Net cash used in investing activities** | | **81,790** | **64,878** |
| **Cash flows from financing activities** | | | |
| Effect of exchange rate fluctuations on cash held | | 86,745 | 63,111 |
| Net increase in cash and cash equivalents | | 855,324 | 104,488 |
| Cash and cash equivalents at the beginning of the year | 5 | 1,669,037 | 1,564,549 |
| **Cash and cash equivalents at the end of the year** | 5 | **2,524,361** | **1,669,037** |

The accompanying policies and explanatory notes are an integral part of these consolidated financial statemen

**Notes to the consolidated financial statements**

## 1. General information

Anadolubank Anonim Şirketi (the "Bank") started its operations on 25 September 1997 in Turkey under the Turkish Banking Law and the Turkish Commercial Code pursuant to the permit of the Turkish Undersecretariat of Treasury dated 25 August 1997 and numbered 39692. The Bank provides corporate, commercial and retail banking services through a network of 112 (31 December 2017: 112) domestic branches. The address of the headquarters and registered office of the Bank is Saray Mahallesi Toya Sokak No: 3 Ümraniye / Istanbul-Turkey.

The ultimate parent of the Bank is Habaş Sınai ve Tıbbi Gazlar İstihsal Endüstrisi AŞ. Habaş Sınai ve Tıbbi Gazlar İstihsal Endüstrisi AŞ was founded by Hamdi Başaran in 1956 with the name "Hamdi Başaran Topkapı Oxygen Plant" to implement modern industrial gas production.

The Bank has three subsidiaries, which are Anadolu Yatırım Menkul Değerler AŞ ("Anadolu Yatırım"), Anadolu Faktoring AŞ ("Anadolu Faktoring") and Anadolubank Nederland NV ("Anadolubank Nederland").

The Bank has 91.90% ownership in Anadolu Yatırım, a brokerage and investment company, located in Istanbul. Anadolu Yatırım was established on 21 September 1998 and is mainly involved in trading of and investing in securities, stocks, treasury bills and government bonds provided from capital markets; the management of mutual funds and performing intermediary services.

The Bank acquired 99.99% of Anadolu Faktoring from Habaş Petrol Ürünleri Sanayi ve Ticaret AŞ (which is a related party) on 27 October 2008. Anadolu Faktoring was established in Istanbul on 20 March 2007 by obtaining the factoring license which is required to operate in the factoring sector.

The Bank has 100.00% ownership in Anadolubank Nederland, located in Amsterdam –Netherlands. The Bank engages in banking operations in the Netherlands.

For the purposes of the consolidated financial statements, the Bank and its subsidiaries are referred to as "the Group".

## 2. Basis of preparation

### 2.1. Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The Bank and its subsidiaries which is located in Turkey, maintain their books of account and prepare their statutory financial statements in Turkish Lira ("TL") in accordance with the accounting practices as promulgated by the Banking Regulation and Supervision Agency ("BRSA"), Turkish Accounting Standards promulgated by the Public Oversight Accounting and Auditing Standards Authority, the Turkish Commercial Code, and the Turkish Tax Legislation. The Bank's foreign subsidiary Anadolubank Nederland maintains its books of account and prepare its statutory financial statements in EUR in accordance with the regulations of the country in which it operates.

The consolidated financial statements of the Group as at and for the year ended 31 December 2018 are authorised for issue by the management on 31 July 2019. The General Assembly and certain regulatory bodies have the power to amend the statutory financial statements after issue.

The amendments to IAS / IFRS effective from 1 January 2018 do not have any significant effect on the Group's accounting policies, financial position and performance. The amendments to IAS and IFRS that were issued but not yet effective as of the date of finalization of the financial statements will have no material effect on the Group's accounting policies, financial position and performance, except for IFRS 9 Financial Instruments.

### 2.2. Basis of measurement

The consolidated financial statements are prepared on the historical cost basis as adjusted for the effects of inflation that lasted until 31 December 2005, except that the following assets and liabilities are stated at their fair values: derivative financial assets and liabilities held for trading purposes, financial assets at fair value through profit or loss ("FVTPL"), financial assets at fair value through other comprehensive income ("FVOCI"), loans and receivables at FVTPL, and real estates.

### 2.3. Functional currency and presentation currency

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

### 2.4. Accounting in hyperinflationary countries

Financial statements of the Turkish entities have been restated for the changes in the general purchasing power of the Turkish Lira based on IAS 29 – *Financial Reporting in Hyperinflationary Economies* as at 31 December 2005. IAS 29 requires that financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the reporting date, and that corresponding figures for previous years 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 was 35.61% as at 31 December 2005, based on the Turkish nation-wide wholesale price indices announced by the Turkish Statistical Institute ("TURKSTAT"). This, together with the sustained positive trend in quantitative factors, such as the stabilization in capital and money markets, decrease in interest rates and the appreciation of TL against the USD and other hard currencies have been taken into consideration to categorize Turkey as a non-hyperinflationary economy under IAS 29 effective from 1 January 2006.

## 2. Basis of preparation *(continued)*

### 2.5. Use of estimates and judgments

The preparation of the consolidated financial statements requires management to make judgments, 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.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected.

In particular, information about significant areas at estimation uncertainty and critical judgment in applying accounting policies that have the most significant effect on the amount recognized in the financial statements are described in the following notes:

- Note 8 – Derivative financial assets and liabilities held for trading purpose
- Note 10 – Loans and receivables
- Note 17 – Other liabilities and provisions
- Note 18 – Income taxes
- Note 26 – Financial risk management

### 2.6. Changes in accounting policies

The accounting policies adopted in the preparation of the financial statements as at 31 December 2018 are consistent with those followed in the preparation of the financial statements of the prior year, except for the new standards and amendments to standards, including any consequential amendments to other standards summarized in related notes.

**The new and amended standards which are effective for annual periods beginning on or after "1 January 2018"**

**IFRS 15 Revenue from Contracts with customers**

IFRS 15 "Revenue from Contracts with Customers" is effective from 1 January 2018, but it does not have significant impact on the Group's financial statements.

## 2. Basis of preparation *(continued)*

### 2.6. Changes in accounting policies *(continued)*

**The new and amended standards which are effective for annual periods beginning on or after "1 January 2018"** *(continued)*

**IFRS 9 Financial Instruments**

IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments "Recognition and Measurement".

***i. Classification and measurement of financial assets and financial liabilities***

IFRS 9 largely retains the existing requirements in IAS 39 for the classification and measurement of financial liabilities. However, it eliminates the previous IAS 39 categories for financial assets of held to maturity, loans and receivables and available for sale.

The adoption of IFRS 9 has not had a significant effect on the Group's accounting policies related to financial liabilities and derivative financial instruments.

The impact of IFRS 9 on the classification and measurement of financial assets is set out below:

Under IFRS 9, on initial recognition, a financial asset is classified as measured at: amortised cost; FVOCI – debt investment; FVOCI – equity investment; or FVTPL. The classification of financial assets under IFRS 9 is generally based on the business model in which a financial asset is managed and its contractual cash flow characteristics. Derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never separated. Instead, the hybrid financial instrument as a whole is assessed for classification.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is to hold assets to collect contractual cash flows; and

- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at FVOCI if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and

- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

## 2. Basis of preparation *(continued)*

### 2.6. Changes in accounting policies *(continued)*

**The new and amended standards which are effective for annual periods beginning on or after "1 January 2018"** *(continued)*

**IFRS 9 Financial Instruments** *(continued)*

***i. Classification and measurement of financial assets and financial liabilities*** *(continued)*

On initial recognition of an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in the investment's fair value in OCI. This election is made on an investment-by-investment basis.

All financial assets not classified as measured at amortised cost or FVOCI as described above are measured at FVTPL. On initial recognition, the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

A financial asset (unless it is a trade receivable without a significant financing component that is initially measured at the transaction price) is initially measured at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition.

The following accounting policies apply to the subsequent measurement of financial assets.

| | |
|---|---|
| Financial assets at FVTPL | These assets are subsequently measured at fair value. Net gains and losses, including any interest or dividend income, are recognised in profit or loss. |
| Financial assets at amortised cost | These assets are subsequently measured at amortised cost using the effective interest method. The amortised cost is reduced by impairment losses. Interest income, foreign exchange gains and losses and impairment are recognised in profit or loss. Any gain or loss on derecognition is recognized in profit or loss. |
| Debt investments at FVOCI | These assets are subsequently measured at fair value. Interest income calculated using the effective interest method, foreign exchange gains and losses and impairment are recognised in profit or loss. Other net gains and losses are recognised in OCI. On derecognition, gains and losses accumulated in OCI are reclassified to profit or loss. |
| Equity investments at FVOCI | These assets are subsequently measured at fair value. Dividends are recognised as income in profit or loss unless the dividend clearly represents a recovery of part of the cost of the investment. Other net gains and losses are recognised in OCI and are never reclassified to profit or loss. |

**2. Basis of preparation** *(continued)*

**2.6. Changes in accounting policies** *(continued)*

**The new and amended standards which are effective for annual periods beginning on or after "1 January 2018"** *(continued)*

***IFRS 9 Financial Instruments*** *(continued)*

***ii. Impairment of financial assets***

IFRS 9 replaces the "incurred loss" model in IAS 39 with an expected credit loss ("ECL") model. The new impairment model applies to financial assets measured at amortised cost, contract assets and debt investments at FVOCI, but not to investments in equity instruments. Under IFRS 9, credit losses are recognised earlier than under IAS 39.

The financial assets at amortised cost consist of cash and cash equivalents, loans and investment securities.

Under IFRS 9, loss allowances are measured on either of the following bases:

-12-month ECLs: these are ECLs that result from possible default events within the 12 months after the reporting date; and

-lifetime ECLs: these are ECLs that result from all possible default events over the expected life of a financial instrument.

*Expected credit loss calculation:*

The Group considers macroeconomic adjusted forward looking PD, LGD and EAD components in the estimation of expected credit loss from a financial asset. Expected credit loss is calculated under three different scenarios with different macroeconomic expectations and final outcome is a weighted average of the calculations.

Expected credit loss is calculated through three stages as described below;

Stage 1: 12 month expected credit loss is calculated for financial assets in stage 1. 12 month expected credit loss represents the expected credit loss that results from default events on a financial instrument that are possible within the 12 months after the reporting date.

Stage 2: There is a significant increase in credit risk for a financial assets in stage 2 since their origination and lifetime expected credit loss is calculated for stage 2.

Stage 3: Financial assets considered as impaired are in stage 3. Lifetime expected credit loss is calculated for stage 3.

## 2. Basis of preparation *(continued)*

### 2.6. Changes in accounting policies *(continued)*

**The new and amended standards which are effective for annual periods beginning on or after "1 January 2018"** *(continued)*

***IFRS 9 Financial Instruments*** *(continued)*

***ii. Impairment of financial assets*** *(continued)*

*Probability of default, exposure at default and loss given default models:*

Internal Probability of Default ("PD") models consider financial standing and demographical, internal-external behavioral data of customers. The Bank adopts different PD models for customers with different characteristics. Loss Given Default ("LGD") models are segment level models and represent time value of money by calculating present value of all future cash flows by using the effective interest rate. Bank uses future cash flows and behavioral data in estimating exposure at default ("EAD").

*Transfer logic:*

The Bank uses quantitative and qualitative methods in identifying significant increase in credit risk. As a quantitative analysis, the Bank measures the significant credit deterioration by comparing the risk of default at inception (initial rating) and the reporting date. The Bank uses watch-list, memzuc and customer days past due information as qualitative criteria and classifies loans in stage 2. The change in the loan payment plan (restructuring) due to financial difficulty or concession is also considered as stage 2.

*Individual assessment*

For financial assets above a threshold in stage 3, the Bank conducts individual assessments in calculation of expected credit loss. The Bank has proper documentation of the calculations and the methodology for individual assessment. Calculations are performed by discounting the expected cash flows for the individual financial instrument to its present value using the effective interest rate. Future cash flows are determined based on two scenarios: going concern and gone concern scenarios. The choice of these scenarios depends on whether the customer is still operating and has operating cash flows that may be used to repay the debt, or whether the customer is not operating anymore and has collateral that may be used to pay the debt.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 2. Basis of preparation *(continued)*

### 2.6. Changes in accounting policies *(continued)*

**The new and amended standards which are effective for annual periods beginning on or after "1 January 2018"** *(continued)*

***IFRS 9 Financial Instruments*** *(continued)*

| ASSETS | 31 December 2017 | IFRS 9 Reclassification effect | IFRS 9 Measurement effect | 1 January 2018 |
|---|---|---|---|---|
| Cash and cash equivalents | 59,818 | - | - | 59,818 |
| Balances with central bank | 511,426 | - | - | 511,426 |
| Reserve deposits at central bank | 1,310,653 | - | - | 1,310,653 |
| Loans and advances to banks and other financial institutions | 1,043,943 | - | - | 1,043,943 |
| Expected credit losses on loans and advances to banks and other financial institutions | | (696) | (1,057) | (1,753) |
| Money market placements | 109,295 | - | - | 109,295 |
| Trading assets | 110,372 | (110,372) | - | - |
| Financial assets at fair value through profit or loss | | 110,372 | - | 110,372 |
| Derivative financial assets | 28,871 | - | - | 28,871 |
| Investment securities | 1,236,588 | - | - | 1,236,588 |
| *Available for sale* | *1,236,588* | *(1,236,588)* | - | - |
| *Financial assets at fair value through other comprehensive income* | - | *769,295* | - | *769,295* |
| *Financial assets measured at amortised cost* | - | *467,293* | - | *467,293* |
| Loans and receivables | 13,318,545 | - | - | 13,318,545 |
| Provision for possible loan losses | (241,155) | 241,155 | - | - |
| Expected credit losses on loans | | (241,155) | (174,828) | (415,983) |
| Property and equipment | 219,035 | - | - | 219,035 |
| Intangible assets | 8,015 | - | - | 8,015 |
| Deferred tax assets | 25,403 | - | 42,267 | 67,670 |
| Other assets | 409,427 | - | - | 409,427 |
| **Total assets** | **18,150,236** | **(696)** | **(133,618)** | **18,015,922** |
| **LIABILITIES** | | | | |
| Deposits from banks | 366,325 | - | - | 366,325 |
| Deposits from customers | 12,980,125 | - | - | 12,980,125 |
| Obligations under repurchase agreements | 827,036 | - | - | 827,036 |
| Interbank money market borrowings | 393,731 | - | - | 393,731 |
| Funds borrowed | 801,662 | - | - | 801,662 |
| Derivative financial liabilities | 23,420 | - | - | 23,420 |
| Current tax liabilities | 22,845 | - | - | 22,845 |
| Deferred tax liabilities | 2,434 | - | - | 2,434 |
| Other liabilities and provisions | 564,657 | (696) | 6,514 | 570,475 |
| **Total liabilities** | **15,982,235** | **(696)** | **6,514** | **15,988,053** |
| **EQUITY** | | | | |
| Share capital | 602,619 | - | - | 602,619 |
| Legal reserves | 72,757 | - | - | 72,757 |
| Other reserves | 66,010 | - | - | 66,010 |
| Translation reserve | 194,666 | - | - | 194,666 |
| Fair value reserve | (9,346) | - | - | (9,346) |
| Retained earnings | 1,238,484 | - | (140,132) | 1,098,352 |
| **Total equity attributable to equity holders of the Bank** | **2,165,190** | **-** | **(140,132)** | **2,025,058** |
| **Non-controlling interests** | **2,811** | **-** | **-** | **2,811** |
| **Total equity** | **2,168,001** | **-** | **(140,132)** | **2,027,869** |
| **Total liabilities and equity** | **18,150,236** | **(696)** | **(133,618)** | **18,015,922** |

## 2. Basis of preparation *(continued)*

### 2.6. Changes in accounting policies *(continued)*

**Standards issued but not yet effective and not early adopted**

A number of new standards, interpretations of 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.

**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.

**IFRS 17 –Insurance Contracts**

On 18 May 2017, IASB issued IFRS 17 Insurance Contracts. This first truly international standard for insurance contracts will help investors and others better understand insurers' risk exposure, profitability and financial position. IFRS 17 replaces IFRS 4, which was brought in as an interim Standard in 2004. IFRS 4 has given companies dispensation to carry on accounting for insurance contracts using national accounting standards, resulting in a multitude of different approaches. As a consequence, it is difficult for investors to compare and contrast the financial performance of otherwise similar companies. IFRS 17 solves the comparison problems created by IFRS 4 by requiring all insurance contracts to be accounted for in a consistent manner, benefiting both investors and insurance companies. Insurance obligations will be accounted for using current values – instead of historical cost. The information will be updated regularly, providing more useful information to users of financial statements. IFRS 17 has an effective date of 1 January 2021 but companies can apply it earlier. The Group does not expect that application of IFRS 17 will have significant impact on its consolidated financial statements.

**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 adoption process regarding the mentioned amendments continues as of the reporting date.

## 2. Basis of preparation *(continued)*

### 2.6. Changes in accounting policies *(continued)*

**Standards issued but not yet effective and not early adopted** *(continued)*

**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. The Group does not expect that application of these amendments to IAS 28 will have significant impact on its consolidated financial statements.

**Amendments to IFRS 9 - Prepayment features with negative compensation**

On 12 October 2017, IASB has issued amendments to IFRS 9 to clarify that 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. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of the amendments to IFRS 9.

**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. The Group does not expect that application of these amendments to IAS 19 will have significant impact on its consolidated financial statements.

**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.

## 2. Basis of preparation *(continued)*

### 2.6. Changes in accounting policies *(continued)*

**Standards issued but not yet effective and not early adopted** *(continued)*

***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 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. The Group does not expect that application of these amendments to IAS 1 and IAS 8 will have significant impact on its consolidated financial statements.

**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 does not expect that application of these amendments to IFRS 3 will have significant impact on its consolidated financial statements.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 3. Significant accounting policies

Except the changes disclosed in Note 2.6, the accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements.

### 3.1. Basis of consolidation

***(i) Subsidiaries***

Subsidiaries are investees controlled by the Group. The Group 'controls' an investee if it is exposed to, or has rights to, variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date when control ceases.

***(ii) Non-controlling interests***

Non-controlling interests ("NCI") 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.

***(iii) Loss of control***

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

***(iv) Transactions eliminated on consolidation***

Intra-group balances and transactions, and any unrealised income and expenses (except for foreign currency transaction gains or losses) arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

### 3.2. Foreign currency

***i) Foreign currency transactions***

Transactions are recorded in TL, which represents the Group's functional currency except for Anadolubank Nederland of which they are recorded in Euro. Transactions denominated in foreign currencies are recorded at the exchange rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies on the reporting date are retranslated to the functional currency at the exchange rate on that date. Foreign currency differences arising on retranslation are recognised in the statement of profit or loss and other comprehensive income. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

The official TL exchange rates used by the Group for foreign currency translation are as follows:

| | EUR / TL | USD / TL |
|---|---|---|
| 31 December 2018 | 6.0280 | 5.2609 |
| 31 December 2017 | 4.5155 | 3.7719 |

**3. Significant accounting policies** *(continued)*

**3.2. Foreign currency** *(continued)*

***ii) Foreign operations***

The assets and liabilities of foreign subsidiaries are translated into presentation currency of the Group at the rate of exchange ruling at the reporting date. The statement of profit or loss of foreign subsidiaries is translated at the weighted average exchange rates after the acquisition date. On consolidation exchange differences arising from the translation of the net investment in foreign entity are included in equity as currency translation reserve.

Foreign currency differences, arising from foreign subsidiaries, are recognised in other comprehensive income ("OCI"), under the foreign currency translation reserve. 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, as part of the profit or loss on disposal.

**3.3 Interest**

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability.

When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment, call and similar options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts.

Interest income and expense presented in the statement of profit or loss and OCI include:

- interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis;
- interest for financial assets at FVOCI calculated on an effective interest basis,

**3.4. Fees and commission**

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

Other fees and commission income, including account servicing fees, investment management fees, sales commission, placement fees and syndication fees are recognised as the related services are provided. When a loan commitment is not expected to result in the draw-down of a loan, loan commitment fees are recognised on a straight-line basis over the commitment period.

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

**3.5. Net trading income**

Net trading income comprises gains less loss related to trading assets and liabilities, and includes all realised and unrealised fair value changes, except for the unrealised gains of financial assets at FVOCI.

**3.6. Dividends**

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

## 3. Significant accounting policies *(continued)*

### 3.7. 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 rate on the remaining balance of the liability.

### 3.8. Income tax expense

While the corporate tax rate was at the rate of 20% since 1 January 2016, for all companies, such rate has been set as 22% for the tax bases of the years 2018, 2019, and 2020 based on the legislation of the Amendment on Certain Tax Laws and Other Laws no. 7061. Furthermore, the Council of Ministers has been authorized to reduce the rate of 22% down to 20%.

This rate is applied to tax base which is calculated by adding certain non deductable expenses for tax purposes and deducting certain exemptions (like dividend income) and other deductions on accounting income. If there is no dividend distribution, no further tax charges are made.

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

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

Deferred tax assets are recognised for all deductible temporary differences, carry-forward of unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, carry-forward of unused tax losses can be utilised.

Deferred tax is not recognised for:

- temporary differences on the initial recognition of assets and liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss;
- temporary differences related to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future; and
- taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at 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 at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

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

## 3. Significant accounting policies *(continued)*

### 3.8. Income tax expense *(continued)*

Effective between 1 January 2017 and 4 December 2017, earnings generated through transfer of real estates, equity shares, founders' shares, redeemed shares and pre-emption rights owned by the companies being under legal proceedings due to their debts to the banks or liable to the Savings Deposit Insurance Fund or by their guarantors and mortgage providers and earnings generated by the banks through sale of such assets are exempt from corporate tax at the rate of 75%.

Effective between 1 January 2017 and 4 December 2017, 75% of earnings generated through sale of real estates, equity shares, founders' shares, redeemed shares and pre-emption rights held as asset at least for two years by the institutions are exempt from the corporate tax with the conditions that such earnings shall be held in a special reserve account under equity until the end of five years following the year of sale and shall be collected as cash until the end of the following two fiscal years.

On the other hand, based on the legislation of the Amendment on Certain Tax Laws and Other Laws no. 7061, effective from 5 December 2017, the aforementioned exemption rate is set as 50% for the earnings generated through sale of real estates and 75% for the earnings generated through sale of other items.

### 3.9. Financial assets and liabilities

*Recognition*

The Group initially recognises loans, factoring receivables and advances, deposits and funds borrowed on the date that they are originated. Regular way purchases and sales of financial assets are recognised on the trade date on which the Group commits to purchase or sell the asset. All other financial assets and liabilities (including assets and liabilities designated at fair value profit or loss) are initially recognised on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue.

*Classification*

Financial assets:

The Group classifies its financial assets into one of the following categories:

Loans and receivables,

Financial assets measured at amortised cost,

Financial assets at FVOCI; and

At fair value through profit or loss, and within this category as:

- Financial assets at FVTPL.

Financial liabilities:

The Group classifies its financial liabilities as measured at amortised cost. See 3.19.

*Derecognition*

The Group 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.

## 3. Significant accounting policies *(continued)*

### 3.9. Financial assets and liabilities *(continued)*

*Derecognition (continued)*

The Group does not have any assets where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset that is recognised to the extent of the Group's continuing involvement in the asset.

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

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

The Group enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all risks or rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised from the financial position. Transfers of assets with retention of all or substantially all risks and rewards include, for example, securities lending and repurchase transactions.

*Offsetting*

Financial assets and liabilities are set off and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to set off the recognised amounts and it 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 Group'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 rate method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

*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") or IFRS 9, because IFRS 9 permits to defer application of IFRS 9 hedge accounting and continue to apply hedge accounting in accordance with IAS 39 as a policy choice, they are treated as derivatives held for trading.

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.

## 3. Significant accounting policies *(continued)*

### 3.9. Financial assets and liabilities *(continued)*

*Derivative financial instruments (continued)*

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*

At each reporting date, the Group assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows on the asset that can be estimated reliably.

Loans and receivables are presented net of specific and portfolio basis allowances for uncollectibility. Specific allowances are made against the carrying amount of loans and receivables that are identified as being impaired based on regular reviews of outstanding balances to reduce these loans and receivable to their recoverable amounts. In assessing the recoverable amounts of the loans and receivables, the estimated future cash flows are discounted to their present value. Portfolio basis allowances are maintained to reduce the carrying amount of portfolios of similar loans and receivables to their estimated recoverable amounts at the reporting date. In order to determine allowance rate for portfolio basis, the Group uses historical allowance rates based on its own statistical data.

Objective evidence that financial assets are impaired includes observable data that comes to the attention of the Group about the following loss events:

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

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

## 3. Significant accounting policies *(continued)*

### 3.9. Financial assets and liabilities *(continued)*

*Identification and measurement of impairment (continued)*

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and estimated recoverable amount. The carrying amount of the asset is reduced through use of an allowance account. Losses are recognised in profit or loss and reflected in an allowance account against loans and receivables.

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss.

Impairment losses on financial assets at FVOCI are recognised by transferring the difference between the amortised acquisition cost and current fair value out of equity to profit or loss.

When a subsequent event causes the amount of impairment loss on a debt security classified under financial assets at FVOCI to decrease, the impairment loss is reversed through profit or loss.

However, any subsequent recovery in the fair value of an impaired equity security classified under financial assets at FVOCI is recognised directly in other comprehensive income. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

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

*Repurchase and resale transactions*

The Group enters into sales of securities under agreements to repurchase such securities. Such securities, which have been sold subject to a repurchase agreement ("repos"), continue to be recognised in the statement of financial position and are measured in accordance with the accounting policy of the security portfolio which they are part of securities sold subject to repos are reclassified in the consolidated financial statements as loaned securities when the transferee has the right by contract or custom to sell or repledge the collateral. The counterparty liability for amounts received under these agreements is included in other money market deposits. The difference between sale and repurchase price is treated as interest expense and accrued over the life of the repurchase agreements using effective interest method.

Securities purchased with a corresponding commitment to resell at a specified future date ("reverse repos") are not recognised in the statement of financial position, as the Group does not obtain control over the assets. Amounts paid under these agreements are included in other money market placements. The difference between purchase and resale price is treated as interest income and accrued over the life of the reverse repurchase agreement using effective interest method.

### 3.10. Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with central banks 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 Group in the management of its short-term commitments.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

## 3. Significant accounting policies *(continued)*

### 3.11. Trading assets and liabilities

Trading assets and liabilities are those assets and liabilities that the Group acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking.

Trading assets and liabilities are initially recognised and subsequently measured at fair value in the statement of financial position, with transaction costs recognised in profit or loss. All changes in fair value are recognised as part of net trading income in profit or loss. Trading assets and liabilities are not reclassified subsequent to their initial recognition, except that non-derivative trading assets, other than those designated at fair value through profit or loss on initial recognition, may be reclassified out of the fair value through profit or loss – i.e. trading – category if they are no longer held for the purpose of being sold or repurchased in the near term and the following conditions are met.

- If the financial asset would have met the definition of loans and receivables (if the financial asset had not been required to be classified as financial asset at fair value through profit or loss at initial recognition), then it may be reclassified if the Group has the intention and ability to hold the financial asset for the foreseeable future or until maturity.
- If the financial asset would not have met the definition of loans and receivables, then it may be reclassified out of the trading category only in rare circumstances.

### 3.12. Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments and fixed maturities that are not quoted in active market. They are not entered into with the intention of immediate or short-term resale and are not classified as "Financial assets held for trading", designated as "Financial assets designated at fair value through other comprehensive income" or "Financial assets designated at fair value through profit or loss". After initial measurement, loans, receivables and advances are subsequently measured at amortised cost using the effective interest rate method, less allowance for impairment. Certain loans are subsequently designated irrevocably as financial assets at FVTPL as permitted by IFRS 9. The Bank classifies certain loans at their origination dates, as financial assets at fair value through profit or loss in compliance with IAS 39. Financial assets at fair value through profit or loss are initially recorded at cost and measured at fair value in subsequent periods. The amortisation is included in "Interest income" in profit or loss. The losses arising from impairment are recognised in profit or loss in "Net impairment loss on financial assets".

"Loans and receivables" captions in the statement of financial position include:

- loans and receivables measured at amortised cost: they are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;
- loans and receivables mandatorily measured at FVTPL or designated as at FVTPL: these are measured at fair value with face value changes recognised immediately in profit or loss; and
- finance lease receivables

## 3. Significant accounting policies *(continued)*

### 3.13. Investment securities

*Financial assets measured at amortised cost*

Financial assets measured at amortised cost are financial assets with fixed maturities that the Group has the intent and ability to hold until maturity. Financial assets measured at amortised cost are initially recognised at cost. Financial assets measured at amortised cost are accounted for by using a discounting method based on internal rate of return applied on the net investment amounts after the deduction of provision for impairments. Interest earned on financial assets measured at amortised cost are recognised as interest income and reflected in the consolidated statement of profit or loss.

*Financial assets at FVOCI*

Financial assets at FVOCI are non-derivative investments that are not designated as another category of financial assets. If a quoted market price is not available, fair value of an instrument is estimated using the available market information and the appropriate valuation methodologies. All other financial assets at FVOCI are carried at fair value. Unrealised gains and losses are recognised directly in equity in the "Fair value reserves".

Interest income is recognised in profit or loss using the effective interest method. Dividend income is recognised in profit or loss when the Group becomes entitled to the dividend. Foreign exchange gains or losses on debt security investments at FVOCI are recognised in the consolidated statement of profit or loss.

If a financial asset at FVOCI is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in profit or loss, is transferred from other comprehensive income to profit or loss. Reversals in respect of equity instruments classified as at FVOCI are not recognised in profit or loss. Reversals of impairment losses on debt instruments are reversed through profit or loss; if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

Other fair value changes are recognised directly in other comprehensive income until the investment is sold or impaired and the balance in other comprehensive income is recognised in profit or loss.

### 3.14. Property and equipment

*Recognition and measurement*

Items of property and equipment are measured at cost less accumulated depreciation and impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located.

As of 1 January 2017, changing the existing accounting policy, it has been decided to apply revaluation model for properties recorded under tangible and intangible assets instead of cost model in accordance with IAS 16 "Property, Plant and Equipment".

Accordingly, for all real estates registered in the ledger, a valuation study was performed by independent expertise firms authorized by Capital Markets Board ("CMB") and BRSA. Revaluations are performed in line with IFRS 13 "Fair Value Measurement Financial Reporting Standard". Valuation method used by expertise firms is the market approach. As a result of the revaluation of the buildings, as of 31 December 2018, the value of property and equipment was decreased to TL 70,304 (31 December 2017: The amount is TL 80,157) in the non-current assets item before taxation.

## 3. Significant accounting policies *(continued)*

### 3.14. Property and equipment *(continued)*

*Subsequent costs*

The cost of replacing part of an item of property 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 property and equipment are recognised in profit or loss as incurred.

*Depreciation*

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives. Land is not depreciated.

The estimated useful lives for the current and comparative periods are as follows:

| | **Years** |
|---|---|
| Buildings and improvements | 50 |
| Machinery and equipment | 5 |
| Office equipment | 5 |
| Furniture, fixtures and vehicles | 5 |
| Leasehold improvements | 4-10 |

Leasehold improvements are depreciated on a straight-line method over a period of time of their lease contract.

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

### 3.15. Intangible assets

Software acquired by the Group is stated at cost less accumulated amortisation and accumulated impairment losses.

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.

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 lives of software are three to five years.

Amortisation methods, useful lives and residual values are reserved at each reporting date and adjusted if appropriate.

### 3.16. Assets held for sale

Non-current assets, or disposal groups comprising assets and liabilities, are classified as held for sale if it is highly probable that they will be recovered primarily through sale rather than through continuing use. Such assets, or disposal groups, are generally measured at the lower of their carrying amount and fair value less costs to sell.

Impairment losses on initial classification as held for sale or held for distribution and subsequent gains and losses on remeasurement are recognised in profit or loss. Once classified as held for sale, intangible assets and property, plant and equipment are no longer amortised or depreciated, and any equity-accounted investee is no longer equity accounted.

## 3. Significant accounting policies *(continued)*

### 3.17. Leases

**The Group as lessee**

***Operating leases***

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

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

A part of the Bank's branch buildings is used through operating leases and lease payments made on operating leases during the lease term, expenses are recorded in equal amounts.

***Finance leases***

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased item or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability.

Finance charges are charged directly against income. Capitalised leased assets are depreciated over the estimated useful life of the asset.

### 3.18. Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets, other than deferred tax assets, are reviewed at 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 statement of other comprehensive income. 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.

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 in respect of other assets, impairment losses recognised in prior periods is assessed at each reporting date for any indications that the loss has decreased or no longer exists. 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. Significant accounting policies *(continued)*

### 3.19. Deposits and funds borrowed

Deposits are the Bank's main source of debt funding. Deposits of the Bank comprised of the deposits from banks and customers.

Deposits and funds borrowed are initially measured at fair value minus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

### 3.20. Provisions

A provision is recognised if, as a result of a past event, the Group 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 Group 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 Group 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 Group recognises any impairment loss on the assets associated with that contract.

### 3.21. Employee benefits

*Reserve for employee severance indemnity*

Reserve for employee severance indemnity represents the present value of the estimated future probable obligation of the Group arising from the retirement of the employees and calculated in accordance with the Turkish Labour Law. Employment termination benefit is not a funded liability and there is no requirement to fund it. Employment termination benefit is calculated based on the estimation of the present value of the employee's probable future liability arising from the retirement. IAS 19 ("Employee Benefits") requires actuarial valuation methods to be developed to estimate the bank's obligation under defined employee plans. IAS 19 has been revised effective from the annual period beginning after 1 January 2013. In accordance with the revised standard, actuarial gain / loss related to employee benefits shall be recognised in other comprehensive income.

*Short-term employee benefits*

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

## 3. Significant accounting policies *(continued)*

### 3.22. 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 Group's Management Committee (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. Segment results that are reported to the Board of Directors include items directly attributable to that segment as well as those that can be allocated on a reasonable basis.

### 3.23. Classifications

In order to comply with the presentation of the financial statements as of 31 December 2018, reclassifications were made to the balance sheet for the year ended 31 December 2017. This classification includes the reclassification effects of IFRS 9, which is presented under "2.6. Changes in Accounting Policies" section.

### 3.24. 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 financial statements. Events after the reporting period that are not adjusting events are disclosed in the notes when material.

## 4. Operating segments

The Group has four reportable segments, as described below, which are the Group's strategic business units. The strategic business units offer different products and services, and are managed separately based on the Group's management and internal reporting structure. For each of the strategic business units, the chief operating decision maker, the Board of Directors reviews internal management reports on at least a quarterly basis. The following summary describes the operations in each of the Group's reportable segments:

*Retail banking*

Includes loans, deposits and other transactions and balances with retail customers.

*Corporate and commercial banking*

Includes loans, deposits and other transactions and balances with corporate customers.

*Treasury*

Undertakes the Group's funding and centralised risk management activities through borrowings, and investing in liquid assets such as short-term placements and corporate and government debt securities.

*Investment banking*

Includes the Group's trading and corporate finance activities.

Information regarding the results of each reportable segment is included in the following page. Performance is measured based on segment profit before income tax, as included in the internal management reports that are reviewed by the Board of Directors. Segment profit is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate within these industries. Inter-segment pricing is determined on an arm's length basis.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**4. Operating segments** *(continued)*

**Information about operating segments**

| 31 December 2018 | Retail banking | Corporate and commercial banking | Treasury | Investment banking | Others | Total |
|---|---|---|---|---|---|---|
| Net interest income | 289,937 | 459,291 | 124,673 | 18,939 | - | 892,840 |
| Net fee and commission income | 62,017 | 98,242 | 26,667 | 4,051 | - | 190,977 |
| Other income | 40,487 | 64,015 | 17,409 | 2,645 | - | 124,556 |
| Other expenses | (260,015) | (411,117) | (111,806) | (16,985) | - | (799,923) |
| **Profit before taxes** | **132,426** | **210,431** | **56,943** | **8,650** | **-** | **408,450** |

| 31 December 2018 | Retail banking | Corporate and commercial banking | Treasury | Investment banking | Others | Total |
|---|---|---|---|---|---|---|
| Segment assets | 5,463,027 | 8,629,892 | 2,371,126 | 367,234 | 668,417 | 17,499,696 |
| **Total assets** | **5,463,027** | **8,629,892** | **2,371,126** | **367,234** | **668,417** | **17,499,696** |
| Segment liabilities | 4,485,608 | 7,085,872 | 1,946,895 | 301,530 | 1,355,328 | 15,175,233 |
| Equity and non-controlling interests | | | | | 2,324,463 | 2,324,463 |
| **Total liabilities and equity** | **4,485,608** | **7,085,872** | **1,946,895** | **301,530** | **3,679,791** | **17,499,696** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**4. Operating segments** *(continued)*

**Information about operating segments** *(continued)*

| **31 December 2017** | **Retail banking** | **Corporate and commercial banking** | **Treasury** | **Investment banking** | **Others** | **Total** |
|---|---|---|---|---|---|---|
| Net interest income | 197,189 | 312,370 | 84,780 | 12,881 | - | 607,220 |
| Net fee and commission income | 49,826 | 78,929 | 21,422 | 3,255 | - | 153,432 |
| Other income | 19,865 | 31,469 | 8,540 | 1,298 | - | 61,172 |
| Other expenses | (187,468) | (296,970) | (80,595) | (12,247) | - | (577,280) |
| **Profit before taxes** | **79,412** | **125,798** | **34,147** | **5,187** | **-** | **244,544** |

| **31 December 2017** | **Retail banking** | **Corporate and commercial banking** | **Treasury** | **Investment banking** | **Others** | **Total** |
|---|---|---|---|---|---|---|
| Segment assets | 5,687,278 | 8,984,140 | 2,468,458 | 382,309 | 628,051 | 18,150,236 |
| **Total assets** | **5,687,278** | **8,984,140** | **2,468,458** | **382,309** | **628,051** | **18,150,236** |
| Segment liabilities | 4,200,692 | 6,635,794 | 1,823,232 | 282,378 | 3,040,139 | 15,982,235 |
| Equity and non-controlling interests | - | - | - | - | 2,168,001 | 2,168,001 |
| **Total liabilities and equity** | **4,200,692** | **6,635,794** | **1,823,232** | **282,378** | **5,208,140** | **18,150,236** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 5. Cash and cash equivalents

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Cash and cash equivalents | 167,778 | 59,818 |
| Loans and advances to banks (with original maturity of less than 3 months) | 1,508,141 | 1,043,943 |
| Unrestricted balances with the central bank | 590,161 | 511,426 |
| Receivables from reverse repurchase transactions | 273,336 | 109,295 |
| IFRS 9 allowances | 524 | |
| **Total cash and cash equivalents in the consolidated statement of financial position** | **2,539,940** | **1,724,482** |
| Blocked loans and advances to banks and other financial institutions | (7,041) | (19,426) |
| Loans and advances to banks (with original maturity of more than 3 months) | - | (345) |
| Interest accruals on cash and cash equivalents | (8,538) | (35,674) |
| **Cash and cash equivalents in the consolidated statement of cash flows** | **2,524,361** | **1,669,037** |

As at 31 December 2018, deposits with banks amounting to TL 7,041 (31 December 2017: TL 19,426) are blocked at financial institutions for the interest rate swaps and credit default swaps entered into by the Group.

## 6. Balances with central bank

### a) Unrestricted balances with central bank

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Demand deposits-TL | 273,078 | 313,978 |
| Demand deposits-FC | 317,083 | 197,448 |
| **Total** | **590,161** | **511,426** |

### b) Reserve deposits with central bank

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Foreign currency reserve | 701,940 | 1,310,653 |
| **Total** | **701,940** | **1,310,653** |

Reserve deposits are kept as blockage in Central Bank of Turkey (CBRT) for foreign currency liabilities. The banks operating in Turkey keep reserve deposits for Turkish currency and foreign currency liabilities in TL and foreign currencies at the rates of 1.5% - 8.0% and 4.0% - 20.0%, respectively as per the Communiqué no.2005/1 "Reserve Deposits" of the CBRT (31 December 2017: 4.0% - 10.5% and 8.0% - 12.0% respectively). In communiqué, reserve ratio for Turkish Lira liabilities has been changed to between 1.5% and 8.0% according to the maturity of the liabilities and it has been taken into consideration as of the report date.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 7. Financial assets at fair value through profit or loss

As at 31 December 2018, financial assets at fair value through profit or loss comprised the following:

| | 31 December 2018 | |
|---|---|---|
| | **Carrying value** | **Effective interest rate (%)** |
| Eurobonds issued by the Turkish Government | 1,537 | 2.00-8.00 |
| Government bonds in TL | 96 | 5.40-21.96 |
| **Total** | **1,633** | |

**Trading assets**

As at 31 December 2017, trading assets comprised the following:

| | 31 December 2017 | |
|---|---|---|
| | **Carrying value** | **Effective interest rate (%)** |
| Eurobonds issued by the Turkish Government | 807 | 4.24-5.84 |
| Government bonds in TL | 109,565 | 13.04- 14.05 |
| **Total** | **110,372** | |

Debt instruments are given as collateral under repurchase agreements:

| | **31 December 2018** | **31 December 2017** |
|---|---|---|
| Deposited at financial institutions for repurchase transactions | - | 87,659 |

As at 31 December 2018, there are no government securities kept at Istanbul Takas ve Saklama Bankası Anonim Şirketi (Takasbank - Istanbul Clearing and Custody Incorporation) and at Capital Markets Board of Turkey for legal requirements and as a guarantee for stock exchange and money market operations (31 December 2017: TL 8).

## 8. Derivative financial assets / liabilities held for trading purpose

In the ordinary course of business, the Group enters into various types of transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instruments, reference rates or indices. Derivative financial instruments of the Group mainly include foreign currency forwards, cross currency interest rate swaps, foreign currency options and credit default swaps.

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

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 8. Derivative financial assets / liabilities held for trading purpose *(continued)*

The fair value of derivative financial instruments is calculated by using forward exchange rates at the reporting date and option pricing models. In the absence of reliable forward rate estimations in a volatile market, current market rate is considered to be the best estimate of the present value of the forward exchange rates.

| | 31 December 2018 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Fair value assets | Fair value liabilities | Notional amount in Turkish Lira equivalent | Up to 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | 1 to 5 years | More than 5 years |
| ***Derivatives financial instruments held for trading purpose:*** | | | | | | | | | |
| Forward purchase contract | 2,784 | 496 | 401,416 | 375,384 | 10,194 | 2,590 | 13,248 | - | - |
| -Forward sale contract | - | - | 398,844 | 375,356 | 9,304 | 7,767 | 6,417 | - | - |
| Currency swap purchase | 21,166 | 32,832 | 2,133,435 | 1,037,064 | 502,958 | 105,273 | 35,264 | 347,605 | 105,271 |
| Currency swap sale | - | - | 2,156,008 | 1,042,422 | 504,232 | 122,787 | 36,602 | 344,693 | 105,272 |
| Interest swap purchase | - | - | 590,474 | - | - | - | - | 289,344 | 301,130 |
| Interest swap sale | - | - | 590,474 | - | - | - | - | 428,597 | 161,877 |
| Put option purchase | - | - | 194,119 | 50,267 | 130,079 | 2,186 | 11,587 | - | - |
| Put option sale | - | - | 205,651 | 52,392 | 139,486 | 2,186 | 11,587 | - | - |
| **Total** | **23,950** | **33,328** | **6,670,421** | **2,932,885** | **1,296,253** | **242,789** | **114,705** | **1,410,239** | **673,550** |

| | 31 December 2017 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Fair value assets | Fair value liabilities | Notional amount in Turkish Lira equivalent | Up to 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | 1 to 5 years | More than 5 years |
| ***Derivatives financial instruments held for trading purpose:*** | | | | | | | | | |
| Forward purchase contract | 1,116 | 1,288 | 424,376 | 408,341 | 10,623 | 5,412 | - | - | - |
| Forward sale contract | - | - | 430,993 | 414,976 | 10,616 | 5,401 | - | - | - |
| Currency swap purchase | 27,755 | 22,132 | 2,023,645 | 1,247,237 | 417,390 | 62,824 | 85,990 | 210,204 | - |
| Currency swap sale | - | - | 2,021,494 | 1,249,355 | 422,526 | 62,513 | 84,063 | 203,037 | - |
| Interest swap purchase | - | - | 483,953 | - | - | 18,062 | 135,464 | 330,427 | - |
| Interest swap sale | - | - | 483,953 | - | - | 18,062 | 135,464 | 330,427 | - |
| Put option purchase | - | - | 228,934 | 193,609 | 35,325 | - | - | - | - |
| Put option sale | - | - | 228,934 | 193,609 | 35,325 | - | - | - | - |
| **Total** | **28,871** | **23,420** | **6,326,282** | **3,707,127** | **931,805** | **172,274** | **440,981** | **1,074,095** | **-** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 9. Investment securities

***Financial assets at fair value through other comprehensive income***

| | 31 December 2018 | |
|---|---|---|
| | Amount | Effective interest rate (%) |
| Eurobonds issued by the Turkish Government | 532,165 | 6.00-8.00 |
| Foreign currency denominated bonds | 212,181 | 0.77-6.00 |
| Equity instruments | 12,346 | - |
| **Total financial assets at FVOCI** | **756,692** | |

The movement of financial assets at fair value through other comprehensive income is as follows:

| | 31 December 2018 |
|---|---|
| **Balance at beginning of period** | **1,236,588** |
| Foreign currency differences on monetary assets | 130,303 |
| Purchases during the period | 49,103 |
| Disposals through sales and redemptions | (166,777) |
| Allowance for impairment | (102) |
| Changes in amortised cost | (34,651) |
| Transfer | (457,772) |
| **Balance at the end of period** | **756,692** |

Carrying value of financial assets at FVOCI given as collateral under repurchase agreements and for other banking transactions under the normal course of the banking operations are as follows:

| | 31 December 2018 |
|---|---|
| Deposited at financial institutions for repurchase transactions | 189,822 |
| Collaterals | 47,930 |
| Other | 518,940 |
| **Total** | **756,692** |

As at 31 December 2018, carrying value of underlying financial assets classified as financial assets at FVOCI collateralised against repurchase agreements is TL 189,822.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**9. Investment securities** *(continued)*

***Available-for-sale financial assets***

| | 31 December 2017 | |
|---|---|---|
| | **Amount** | **Effective interest rate (%)** |
| Eurobonds issued by the Turkish Government | 948,512 | 12.64-13.60 |
| Foreign currency denominated bonds | 278,453 | 4.00-6.00 |
| Equity instruments | 9,623 | - |
| **Total available-for-sale financial assets** | **1,236,588** | |

Carrying value of available-for-sale financial assets given as collateral under repurchase agreements and for other banking transactions under the normal course of the banking operations are as follows:

| | **31 December 2017** |
|---|---|
| Deposited at financial institutions for repurchase transactions | 883,343 |
| Collaterals | 69,263 |
| Other | 283,982 |
| **Total** | **1,236,588** |

As at 31 December 2017, carrying value of underlying financial assets classified as available-for-sale financial assets collateralised against repurchase agreements is TL 883,343.

The movement of available-for-sale financial assets is as follows:

| | **31 December 2017** |
|---|---|
| **Balance at beginning of period** | **1,209,632** |
| Foreign currency differences on monetary assets | 98,228 |
| Purchases during the period | 211,986 |
| Disposals through sales and redemptions | (288,651) |
| Allowance for impairment | (5,746) |
| Changes in amortised cost | 9,697 |
| Stock market valuation changes | 1,442 |
| **Balance at the end of period** | **1,236,588** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**9. Investment securities** *(continued)*

***Financial assets measured at amortised cost***

| | 31 December 2018 | |
|---|---|---|
| | **Amount** | **Effective interest rate (%)** |
| ***Debt instruments:*** | | |
| Foreign currency denominated bonds | 328,138 | 1.03-7.44 |
| Government bonds TL | 233,299 | 18.40-22.61 |
| **Total (*)** | **561,437** | |

(*) Government bonds amounting to TL 467,293 has been transferred from financial assets at fair value through profit or loss to financial assets measured at amortised cost and presented in the table together with the rediscount on the amortized cost.

The movement of financial assets measured at amortised cost is as follows:

| | **31 December 2018** |
|---|---|
| **Balances at beginning of period** | **-** |
| Reclassification from financial assets at fair value through profit or loss (IFRS 9 transition) (Note 2.6) | 467,293 |
| Foreign currency differences on monetary assets | 56,483 |
| Purchases during the period | 89,952 |
| Disposals through sales and redemptions | (57,198) |
| Allowance for impairment | (2,574) |
| Changes in amortised cost | 7,512 |
| IFRS 9 Provisions | (31) |
| **Balances at end of period** | **561,437** |

| | **31 December 2018** |
|---|---|
| Deposited at financial institutions for repurchase transactions | 286,218 |
| Collaterals | 49,698 |
| Other | 225,521 |
| **Total** | **561,437** |

***Held to maturity financial assets***

As of 31 December 2017, there are no held to maturity financial assets of the Bank.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 10. Loans and receivables

| | 31 December 2018 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Amount | | | | Effective interest rate (%) | | |
| | TL | FC | FC indexed | Total | TL | FC | FC indexed |
| Corporate loans | 8,075,465 | 2,927,356 | 234,725 | 11,237,546 | 5.04-60.00 | 0.50-7.50 | 3.60-12.00 |
| Consumer loans | 147,970 | 400 | 1,064 | 149,434 | 4.80-38.40 | 4.50 | 4.80-8.28 |
| Credit cards | 63,347 | 58 | - | 63,405 | 26.04-27.00 | - | - |
| Factoring receivables | 372,373 | - | - | 372,373 | 16.54-52.47 | - | - |
| **Total performing loans** | **8,659,155** | **2,927,814** | **235,789** | **11,822,758** | | | |
| Non-performing loans | - | - | - | 820,950 | - | - | - |
| Allowance for: | | | | | | | |
| Individually impaired loans | - | - | - | (447,054) | - | - | - |
| Collectively impaired loans | - | - | - | (156,148) | - | - | - |
| **Loans and receivables, net** | **-** | **-** | **-** | **12,040,506** | **-** | **-** | **-** |

| | 31 December 2017 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Amount | | | | Effective interest rate (%) | | |
| | TL | FC | FC indexed | Total | TL | FC | FC indexed |
| Corporate loans | 9,005,471 | 2,516,917 | 759,486 | 12,281,874 | 3.60-49.50 | 0.25-7.80 | 3.60-8.76 |
| Consumer loans | 212,950 | 282 | 4,586 | 217,818 | 4.68-21.60 | 3.96-6.36 | 4.68-8.28 |
| Credit cards | 61,570 | 32 | - | 61,602 | 16.80-22.08 | - | - |
| Factoring receivables | 420,194 | - | - | 420,194 | 9.77-41.20 | - | - |
| **Total performing loans** | **9,700,185** | **2,517,231** | **764,072** | **12,981,488** | | | |
| Non-performing loans | - | - | - | 337,057 | - | - | - |
| Allowance for: | | | | | | | |
| Individually impaired loans | - | - | - | (110,081) | - | - | - |
| Collectively impaired loans | - | - | - | (131,074) | - | - | - |
| **Loans and receivables, net** | **-** | **-** | **-** | **13,077,390** | **-** | **-** | **-** |

"Loans and receivables" captions in the statement of financial position include the following:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Loans and receivables measured at amortised cost | 12,203,232 | 12,898,351 |
| Factoring receivables | 372,373 | 420,194 |
| Less impairment loss allowance | 603,202 | 241,155 |
| Loans and receivables at FVTPL(*) | 68,103 | - |
| **Total loans and receivables** | **12,040,506** | **13,077,390** |

(*) Includes the loan provided to a special purpose entity (Levent Yapılandırma Yönetimi A.Ş). This loan is accounted under loans measured at FVTPL based on IFRS 9. The fair value of this loan is determined by the independent valuation company by considering different methodologies (discounted cash flows, peer market multipliers, similar transaction multipliers in the same sector etc.). Valuation techniques considered in the valuation work and any possible changes in the basic assumptions may affect the carrying value of the related asset. Accordingly, the loan is classified as Level 3.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 10. Loans and receivables *(continued)*

The specific allowance for possible loan losses is comprised of amounts for specifically identified as being impaired and non-performing loans and receivables plus a further amount considered adequate to cover the inherent risk of loss present in the lending relationships presently performing in accordance with agreements made with borrowers.

Movements in the reserve for possible loan losses:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| **Reserve at beginning of the period/year** | **241,155** | **239,048** |
| Adjustment from adoption of IFRS 9 | 174,828 | |
| **Adjusted balance at 1 January 2018** | **415,983** | |
| Provision for possible loan losses, net of recoveries | 243,701 | 87,808 |
| Provision for possible loan losses | 333,134 | 159,561 |
| Recoveries | (89,433) | (71,753) |
| **Provision, net of recoveries** | **243,701** | **87,808** |
| Loans written-off during the period/year | (57,086) | (85,701) |
| Foreign currency differences on monetary assets | 604 | - |
| **Reserve at end of the period/year** | **603,202** | **241,155** |

The movement of loss allowances per asset class for loans and receivables as of 31 December 2018 is as follows:

| | 31 December 2018 | | | |
|---|---|---|---|---|
| **Loans and receivables** | **Stage 1** | **Stage 2** | **Stage 3** | **Total** |
| Balances at 31 December 2017 | 131,074 | - | 110,081 | 241,155 |
| Impact of adopting IFRS 9 at 1 January 2018 | (36,554) | 66,195 | 145,187 | 174,828 |
| Balances at 1 January 2018 | 94,520 | 66,195 | 255,268 | 415,983 |
| Additions | 25,732 | 96,384 | 211,018 | 333,134 |
| Disposals | (51,232) | (35,330) | (2,871) | (89,433) |
| Debt sales | - | - | (14,512) | (14,512) |
| Write-offs | - | - | (42,574) | (42,574) |
| Transfer to stage 1 | 5,199 | (5,199) | - | - |
| Transfer to stage 2 | (15,067) | 15,067 | - | - |
| Transfer to stage 3 | - | (40,725) | 40,725 | - |
| Effects of movements in exchange rates | 548 | 56 | - | 604 |
| **Balances at the end of the period** | **59,700** | **96,448** | **447,054** | **603,202** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 10. Loans and receivables *(continued)*

The credit quality analysis of loans and receivables excluding factoring receivables, including related income accruals, is as follows as of 31 December 2018:

| | 31 December 2018 | | |
|---|---|---|---|
| | **Stage 1** | **Stage 2** | **Stage 3** |
| Stage 1 : Low-fair risk | 9,869,648 | - | - |
| Stage 2 : Watch list | - | 1,344,302 | - |
| Stage 3.1: Substandard | - | - | 252,660 |
| Stage 3.2: Doubtful | - | - | 203,197 |
| Stage 3.3: Loss | - | - | 267,885 |
| Total loans | 9,869,648 | 1,344,302 | 723,742 |
| Income accrual on loans | 141,782 | 94,653 | 97,208 |
| Loss allowance | (59,700) | (96,448) | (447,054) |
| **Total carrying amount** | **9,951,730** | **1,342,507** | **373,896** |

## 11. Factoring receivables

As at 31 December 2018 and 2017, short-term and long-term factoring receivables included in the loans and receivables are as follows:

| | **31 December 2018** | **31 December 2017** |
|---|---|---|
| Short-term | 372,373 | 417,986 |
| Long-term | - | 2,208 |
| **Total** | **372,373** | **420,194** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 12. Property and equipment

Movements of property and equipment as at and for the year ended 31 December 2018 and 2017 are as follows:

| | Buildings | Motor vehicles | Furniture, office equipment and leasehold improvements | Total |
|---|---|---|---|---|
| **Cost** | | | | |
| Opening balance, 1 January 2017 | 118,814 | 7,511 | 102,609 | 228,934 |
| Additions | 617 | - | 15,488 | 16,105 |
| Disposals | - | (1,687) | (873) | (2,560) |
| Effect of movements in exchange rates | - | - | 82 | 82 |
| Revaluation | 76,372 | - | - | 76,372 |
| **Closing balance, 31 December 2017** | **195,803** | **5,824** | **117,306** | **318,933** |
| Opening balance, 1 January 2018 | 195,803 | 5,824 | 117,306 | 318,933 |
| Additions | - | - | 2,241 | 2,241 |
| Disposals | - | (1,543) | (41,191) | (42,734) |
| Effect of movements in exchange rates | - | - | 248 | 248 |
| Revaluation | 3,420 | - | - | 3,420 |
| Impairment | (14,805) | - | - | (14,805) |
| **Closing balance, 31 December 2018** | **184,418** | **4,281** | **78,604** | **267,303** |
| **Accumulated depreciation:** | | | | |
| Opening balance, 1 January 2017 | 3,998 | 7,341 | 84,435 | 95,774 |
| Additions | 1,744 | 175 | 8,454 | 10,373 |
| Disposals | - | (1,777) | (687) | (2,464) |
| Revaluation | (3,785) | - | - | (3,785) |
| **Closing balance, 31 December 2017** | **1,957** | **5,739** | **92,202** | **99,898** |
| Opening balance, 1 January 2018 | 1,957 | 5,739 | 92,202 | 99,898 |
| Additions | 1,781 | 27 | 7,993 | 9,801 |
| Disposals | - | (1,543) | (41,191) | (42,734) |
| Revaluation | (1,742) | - | - | (1,742) |
| **Closing balance, 31 December 2018** | **1,996** | **4,223** | **59,004** | **65,223** |
| **Net carrying value** | | | | |
| 1 January 2017 | 114,816 | 170 | 18,174 | 133,160 |
| 31 December 2017 | 193,846 | 85 | 25,104 | 219,035 |
| 31 December 2018 | 182,422 | 58 | 19,600 | 202,080 |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 13. Intangible assets

Movements of intangible assets as at and for the year ended 31 December 2018 and 2017 are as follows:

| | Software | Other intangibles | Total |
|---|---|---|---|
| **Cost** | | | |
| Opening balance, 1 January 2017 | 22,261 | 1,356 | 23,617 |
| Additions | 3,651 | - | 3,651 |
| Disposals | - | - | - |
| Effect of movements in exchange rates | 50 | - | 50 |
| **Closing balance, 31 December 2017** | **25,962** | **1,356** | **27,318** |
| Opening balance, 1 January 2018 | 25,962 | 1,356 | 27,318 |
| Additions | 6,425 | - | 6,425 |
| Disposals | (14,347) | - | (14,347) |
| **Closing balance, 31 December 2018** | **18,040** | **1,356** | **19,396** |
| **Accumulated amortisation:** | | | |
| Opening balance, 1 January 2017 | 15,299 | 1,356 | 16,655 |
| Additions | 2,648 | - | 2,648 |
| Disposals | - | - | - |
| **Closing balance, 31 December 2017** | **17,947** | **1,356** | **19,303** |
| Opening balance, 1 January 2018 | 17,947 | 1,356 | 19,303 |
| Additions | 4,136 | - | 4,136 |
| Disposals | (13,835) | - | (13,835) |
| **Closing balance, 31 December 2018** | **8,248** | **1,356** | **9,604** |
| **Net carrying value** | | | |
| 1 January 2017 | 6,962 | - | 6,962 |
| 31 December 2017 | 8,015 | - | 8,015 |
| 31 December 2018 | 9,792 | - | 9,792 |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 14. Other assets

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Transfer cheques | 359,312 | 321,486 |
| Assets held for sale | 200,063 | 41,100 |
| Collateral for leveraged operations(1) | 22,915 | 23,872 |
| Prepaid expenses | 5,885 | 7,588 |
| Credit card payments | 1,372 | 3,872 |
| Advances given | 42 | 509 |
| Other | 18,824 | 11,000 |
| **Total** | **608,413** | **409,427** |

(1) Collateral for leveraged operations are composed of the colleterals given for transactions, which take place through Anadolu Yatırım Menkul Kıymetler AŞ.

### *Assets held for sale*

An asset (or a disposal group) classified as asset held for sale is measured at lower of the carrying amount and fair value less costs to sell. An asset (or a disposal group) is regarded as asset held for sale only when the sale is highly probable and the asset (disposal group) is available for immediate sale in its present condition. For a highly probable sale, there must be a valid plan prepared by the management for the sale of asset including identification of possible buyers and completion of sale process. Furthermore, the asset should be actively marketed at a price consistent with its fair value.

As at 31 December 2018, TL 200,063 (31 December 2017: TL 41,100) of the other assets is comprised of foreclosed real estates acquired by the Bank against its impaired receivables.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 15. Deposits

### Deposits from banks

| | 31 December 2018 | | | | 31 December 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Amount | | Effective interest rate (%) | | Amount | | Effective interest rate (%) | |
| | TL | FC | TL | FC | TL | FC | TL | FC |
| Demand | 3 | 287 | - | - | 3 | 6,407 | - | - |
| Time | 80,934 | 63,138 | 22.00-22.50 | 2.3 | 265,905 | 94,010 | 14.00-14.75 | 0.39-3.05 |
| **Total** | **80,937** | **63,425** | | | **265,908** | **100,417** | | |

### Deposits from customers

| | 31 December 2018 | | | | 31 December 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Amount | | Effective interest rate (%) | | Amount | | Effective interest rate (%) | |
| | TL | FC | TL | FC | TL | FC | TL | FC |
| ***Saving:*** | | | | | | | | |
| Demand | 55,099 | 839,689 | - | - | 54,968 | 716,360 | - | - |
| Time | 5,459,399 | 4,268,665 | 6.00-31.00 | 0.10-8.00 | 5,187,113 | 3,017,447 | 5.00-14.86 | 0.39-4.27 |
| | **5,514,498** | **5,108,354** | | | **5,242,081** | **3,733,807** | | |
| ***Commercial and other deposits:*** | | | | | | | | |
| Demand | 210,277 | 259,862 | - | - | 242,989 | 239,923 | - | - |
| Time | 1,305,380 | 327,754 | 6.50-28.75 | 1.00-2.50 | 2,079,097 | 1,442,228 | 2.00-15.70 | 1.00-3.25 |
| | **1,515,657** | **587,616** | | | **2,322,086** | **1,682,151** | | |
| **Total** | **7,030,155** | **5,695,970** | | | **7,564,167** | **5,415,958** | | |

### Other money market deposits

| | 31 December 2018 | | | | 31 December 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Amount | | Effective interest rate (%) | | Amount | | Effective interest rate (%) | |
| | TL | FC | TL | FC | TL | FC | TL | FC |
| ***Obligations under repurchase agreements:*** | | | | | | | | |
| Due to banks | - | 337,550 | - | 0.25-3.80 | 275,289 | 551,747 | 12.75 | 2.35-2.53 |
| Other | 20,011 | 360,776 | 17.00 | 0.05-3.90 | 14,290 | 379,441 | 13.10-13.20 | 0.05-2.65 |
| **Total** | **20,011** | **698,326** | | | **289,579** | **931,188** | | |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 15. Deposits *(continued)*

### Other money market deposits *(continued)*

As at 31 December 2018, there is no carrying values of underlying financial assets at fair value through profit or loss collateralised against repurchase agreements (31 December 2017: TL 87,659). There is no financial asset measured at amortised cost collateralised against repurchase agreements (31 December 2017: None) and carrying values of underlying financial assets at FVOCI collateralised against repurchase agreements amounts to TL 189,822 (31 December 2017: TL 883,343).

## 16. Funds borrowed

| | 31 December 2018 | | | | 31 December 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Amount | | Effective interest rate (%) | | Amount | | Effective interest rate (%) | |
| | TL | FC | TL | FC | TL | FC | TL | FC |
| Short-term(*) | 251,910 | 246,585 | 6.59-29.50 | 0.50-6.39 | 349,163 | 224,190 | 6.34-6.84 | 0.25-2.95 |
| Medium/long term(*) | - | 224,441 | - | 0.53-4.02 | | 228,309 | - | 0.54-3.75 |
| **Total** | **251,910** | **471,026** | | | **349,163** | **452,499** | | |

(*) Borrowings are presented considering their original maturities.

Repayment plans of funds borrowed are as follows:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| 2018 | - | - |
| 2019 | 527,919 | 709,700 |
| 2020 | 20,267 | 1,607 |
| 2021 | 174,750 | 90,355 |
| **Total** | **722,936** | **801,662** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 17. Other liabilities and provisions

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Transfer orders | 469,923 | 347,342 |
| General reserve(*) | 50,000 | - |
| Assignment fee | 40,828 | 9,434 |
| Taxes other than on income | 39,794 | 36,468 |
| Reserve for employee severance indemnity and vacation | 34,567 | 18,896 |
| *- Employee severance indemnity* | *23,047* | *9,267* |
| *- Vacation pay liability* | *11,520* | *9,629* |
| Collections from guarantee cheques | 34,545 | 21,190 |
| Other various provisions | 30,891 | 32,302 |
| Collateral for leveraged operations | 25,893 | 24,962 |
| Payables due from credit cards | 19,124 | 27,821 |
| Other | 49,028 | 46,242 |
| **Total** | **794,593** | **564,657** |

(*) As of 31 December 2018, general reserves amounting to TL 50,000 are provided by the Bank considering the circumstances which may arise from any changes in economy or market conditions.

The movement of employee severance indemnity is as follows:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Net liability at the beginning of the year | 9,267 | 8,093 |
| Payments during the period | (6,791) | (3,680) |
| Actuarial losses | 10,086 | 93 |
| Changes during the period | 10,485 | 4,761 |
| **Total** | **23,047** | **9,267** |

IAS 19 requires that all actuarial gains and losses to be recognised immediately in other comprehensive income in accordance with the change in IAS 19.

The movement of vacation pay liability is as follows:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Total provision at the beginning of the year | 9,629 | 8,755 |
| Paid during the year | (1,585) | (1,528) |
| Total expense recognised in the profit or loss | 3,476 | 2,402 |
| **Total** | **11,520** | **9,629** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 18. Income taxes

Major components of income tax expense:

| | 2018 | 2017 |
|---|---|---|
| ***Current income taxes:*** | | |
| Current income tax charge | (55,998) | (69,399) |
| ***Deferred taxes:*** | | |
| Relating to origination and reversal of temporary differences | (43,268) | 20,928 |
| **Income tax expense** | **(99,266)** | **(48,471)** |

The current income tax charges and prepaid taxes are detailed below:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Current income tax charge | 55,998 | 69,399 |
| Advance taxes | (20,446) | (46,554) |
| **Current tax liability** | **35,552** | **22,845** |

The Bank is subject to Turkish corporate taxes. Provision is made in the accompanying consolidated financial statements for the estimated charge based on the Group's results for the years and periods. Turkish tax legislation does not permit a parent company and its subsidiary to file a consolidated tax return. Therefore, provisions for taxes, as reflected in the accompanying consolidated financial statements, have been calculated on a separate-entity basis.

As at 31 December 2018 and 2017, deferred tax assets and liabilities are attributable to the following items:

| | 31 December 2018 | | 31 December 2017 | |
|---|---|---|---|---|
| | Deferred tax Assets/ (Liabilities) | | Deferred tax Assets/ (Liabilities) | |
| | Asset | Liability | Asset | Liability |
| Valuation difference of derivative financial instruments | 671 | (435) | 2,731 | (8) |
| Differences in the measurement of the debt securities | - | (7,867) | - | (3,986) |
| Personnel bonuses | 2,562 | - | 2,641 | - |
| Reserve for employee severance indemnity and vacation | 4,932 | - | 3,684 | - |
| Valuation of financial assets at FVOCI | 17,408 | - | | |
| Valuation of AFS securities | | | 4,695 | - |
| Loan loss provisions | 33,226 | - | 15,120 | |
| Revaluation of property and equipment | - | (7,036) | - | (8,016) |
| Other | 10,376 | - | 8,699 | (2,591) |
| **Total deferred tax assets/(liabilities)** | **69,175** | **(15,338)** | **37,570** | **(14,601)** |
| Offsetting | (15,338) | 15,338 | (14,601) | 14,601 |
| **Deferred tax assets/(liabilities)** | **53,837** | **-** | **22,969** | **-** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**18. Income taxes** *(continued)*

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| **Deferred tax asset / (liability) at 1 January** | **22,969** | **17,592** |
| Deferred tax recognised in profit or loss | (43,268) | 20,928 |
| Deferred tax recognised in equity | 31,869 | (15,551) |
| IFRS 9 effect | 42,267 | |
| **Deferred tax asset / (liability) at 31 December** | **53,837** | **22,969** |

The Group has offset the deferred tax assets and deferred tax liabilities on an entity by entity basis based on the legally enforceable right to set off the recognised amounts such as offsetting current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority.

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Deferred tax assets | 53,837 | 25,403 |
| Deferred tax liabilities | - | (2,434) |
| **Total** | **53,837** | **22,969** |

A reconciliation of income tax expense applicable to profit from operating activities before income taxes at the statutory income tax rate to income tax expense at the Group's effective income tax rate for the year ended 31 December 2018 and 2017 were as follows:

| | 2018 | 2017 |
|---|---|---|
| **Net profit from ordinary activities before income taxes and non-controlling interest** | **408,450** | **244,544** |
| Taxes on income per statutory tax rate | 82,466 | 48,909 |
| Disallowable expenses | 543 | 2,325 |
| Current-year losses for which no deferred tax asset is recognised | 11,000 | - |
| Effect of income not subject to tax | 5,257 | (2,763) |
| **Income tax expense** | **99,266** | **48,471** |

For the year ended 31 December 2018, the effective tax rate is 24.3% (2017: 19.8%).

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 19. Capital and reserves

### Share capital

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Number of common shares, TL 0.01 (in full TL), par value authorised, issued and outstanding 60,000 millions | 600,000 | 600,000 |

As at 31 December 2018 and 2017, the authorised nominal share capital of the Bank amounted to TL 600,000.

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

| | 31 December 2018 | | 31 December 2017 | |
|---|---|---|---|---|
| | Amount | % | Amount | % |
| Habaş Sınai ve Tıbbi Gazlar İstihsal Endüstrisi AŞ | 419,867 | 69.98 | 419,867 | 69.98 |
| Mehmet Rüştü Başaran | 163,895 | 27.32 | 163,895 | 27.32 |
| Other shareholders | 16,238 | 2.70 | 16,238 | 2.70 |
| **Nominal value** | **600,000** | **100.00** | **600,000** | **100.00** |
| Restatement effect per IAS 29 | 2,619 | | 2,619 | |
| **Total** | **602,619** | | **602,619** | |

### Translation reserve

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

### Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of financial assets at FVOCI until the investment is derecognised or impaired.

As at 31 December 2018, after deduction of related tax effect, amounted to TL 59,656 loss (31 December 2017: TL 9,346 loss) recognised under equity as gains/losses.

*(Amounts expressed in thousands of Turkish Lira (“TL”) unless otherwise stated.)*

## 19. Capital and reserves *(continued)*

### Other reserves and legal reserves

Other reserves consist of the revaluation of property and equipment which is amounted to TL 63,275, actuarial difference which is amounted to TL 14,507 loss and others which are amounted to TL 60 (31 December 2017: Revaluation of property and equipment which is amounted to TL 72,141, actuarial difference which is amounted to TL 6,440 loss and others which are amounted to TL 309).

The legal reserves consist of first and second legal reserves in accordance with the Turkish Commercial Code and amounted to TL 81,945 (31 December 2017: TL 72,757). 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.

### Non-controlling interests

As at 31 December 2018, non-controlling interests amount to TL 3,465 (31 December 2017: TL 2,811).

## 20. Related parties

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. The Group is controlled by Habaş Sınai ve Tıbbi Gazlar İstihsal Endüstrisi AŞ which owns 69.98% (31 December 2017: 69.98%) of ordinary shares, and included in Habaş Group of companies. For the purpose of these consolidated financial statements, shareholders and Habaş Group companies are referred to as related parties. Related parties also include individuals that are principal owners and management and members of the Group’s Board of Directors and their families. In the course of conducting its banking business, the Group conducted various business transactions with related parties on commercial terms.

The following significant balances exist and transactions have been entered into with related parties:

### Outstanding balances

| | 31 December 2018 | 31 December 2017 |
|---|---:|---:|
| Cash loans | 84,109 | 2,067 |
| Non-cash loans | 89,600 | 87,195 |
| Deposits taken | 238,911 | 185,305 |

### Transactions

| | 2018 | 2017 |
|---|---:|---:|
| Interest income | 6,623 | 8,289 |
| Interest expense | 7,522 | 6,346 |
| Other operating income | - | - |

### Directors’ remuneration

For the year ended 31 December 2018, the key management and the members of the Board of Directors received remuneration and fees amounting to TL 26,697 (31 December 2017: TL 23,772).

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 21. Interest income / expenses

| | 2018 | 2017 |
|---|---|---|
| Interest on loans and receivables | 2,372,196 | 1,530,791 |
| Interest on marketable securities | 71,971 | 70,675 |
| *Financial assets at FVTPL* | *6,401* | |
| *Trading assets* | | *8,956* |
| *Financial assets at FVOCI* | *33,433* | |
| *Available-for-sale financial assets* | | *61,719* |
| *Financial assets measured at amortized cost* | *32,137* | |
| Interest on loans and advances to banks and other financial institutions | 48,882 | 23,974 |
| Interest on other money market placements | 11,446 | 10,652 |
| Other interest income | 20,459 | 8,309 |
| **Total interest income** | **2,524,954** | **1,644,401** |

| | 2018 | 2017 |
|---|---|---|
| Interest on deposits | 1,542,630 | 950,547 |
| Interest on funds borrowed | 69,046 | 49,313 |
| Interest on other money market deposits | 18,138 | 32,669 |
| Other interest expenses | 2,300 | 4,652 |
| **Total interest expenses** | **1,632,114** | **1,037,181** |

## 22. Fee and commission income / expenses

| | 2018 | 2017 |
|---|---|---|
| From non-cash loans | 42,831 | 32,891 |
| Other | 182,044 | 141,103 |
| *From cash loans* | *121,277* | *103,517* |
| *From individual loan application* | *10,220* | *5,893* |
| *Other* | *50,547* | *31,693* |
| **Fee and commission income** | **224,875** | **173,994** |

| | 2018 | 2017 |
|---|---|---|
| Securities commissions | 11,828 | 1,473 |
| Credit card exchange commissions | 4,792 | 2,896 |
| EFT commissions | 3,720 | 2,358 |
| Credit card commissions | 3,034 | 3,678 |
| Credit bureau commissions | 2,336 | 2,524 |
| Istanbul stock exchange commissions | 1,844 | 1,730 |
| ATM commissions | 1,085 | 1,010 |
| Foreign correspondents commissions | 675 | 1,848 |
| Other | 4,584 | 3,045 |
| **Fee and commission expenses** | **33,898** | **20,562** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 23. Salaries and employee benefits

| | 2018 | 2017 |
|---|---|---|
| ***Staff costs:*** | | |
| Wages and salaries | 187,987 | 172,829 |
| Cost of defined contribution plan (employer's share of social security premiums) | 29,453 | 26,913 |
| Other fringe benefits | 29,438 | 42,589 |
| Provision for employee termination benefits and unused vacation accruals | 26,102 | 6,263 |
| **Total** | **272,980** | **248,594** |

The average number of employees during the years is:

| | 2018 | 2017 |
|---|---|---|
| The Bank | 1,644 | 1,817 |
| Subsidiaries | 168 | 183 |
| **Total** | **1,812** | **2,000** |

## 24. Other expenses

| | 2018 | 2017 |
|---|---|---|
| General reserve provision(*) | 50,000 | - |
| Operating lease charges | 29,272 | 25,188 |
| Energy costs | 9,249 | 3,661 |
| Communication expenses | 8,808 | 8,167 |
| Saving Deposit Insurance Fund Premium | 8,697 | 9,227 |
| Maintenance expenses | 8,512 | 6,658 |
| Expertise expenses | 5,447 | 3,111 |
| Advertising expenses | 4,506 | 1,213 |
| Transportation expenses | 3,699 | 3,517 |
| Chartered accountants | 3,384 | 1,630 |
| Cleaning service expenses | 3,344 | 3,110 |
| BRSA participation fee | 1,868 | 3,060 |
| Office supplies | 1,419 | 2,810 |
| Other | 22,791 | 32,542 |
| **Total** | **160,996** | **103,894** |

(*) As of 31 December 2018, general reserves amounting to TL 50,000 are provided by the Bank considering the circumstances which may arise from any changes in economy or market conditions.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 25. Commitments and contingencies

In the ordinary course of business activities, the Bank and its subsidiaries undertake various commitments and incur certain contingent liabilities that are not presented in the consolidated financial statements. Commitments and contingent liabilities comprise the following:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Letters of guarantee | 2,923,356 | 3,199,553 |
| Letters of credit | 457,186 | 594,787 |
| Acceptance credits | 11,811 | 11,371 |
| Other guarantees | 314,912 | 106,919 |
| **Total non-cash loans** | **3,707,265** | **3,912,630** |
| Credit card limit commitments | 117,331 | 113,761 |
| Other commitments | 447,142 | 520,845 |
| **Total** | **4,271,738** | **4,547,236** |

### Litigations

In the normal course of its operations, the Group faces with legal disputes, claims and complaints. The necessary provision, if any, for those cases are provided based on management estimates and professional advice.

As of 31 December 2018, there are 200 cases against the Group which have a probability to result against the Group with respect to information received from Law Departments of the Group. The total amount of these cases is TL 1,800 and provision amount for these cases is TL 12,634.

## 26. Financial risk management

### (a) Introduction and overview

This note presents information about the Group's exposure to each of the below risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risks
- operational risks

*Risk management framework*

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board of Directors monitors the effectiveness of the risk management system through the audit committee. Consequently, the Risk Management Department, which carries out the risk management activities and works independently from executive activities, report directly to the Board of Directors.

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 Group, 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 risks are measured with the internationally accepted methodologies in compliance with local and international regulations, the Bank's structure, policy and procedures. They are effectively managed and assessed in a continuously growing manner. At the same time, studies for compliance with the international banking applications, such as Basel III, are carried out.

*Audit Committee:* The Audit Committee consists of two members of the Board of Directors who do not have any executive functions. The Audit Committee, established to assist the Board of Directors in its auditing and supervising activities, is responsible for:

- The supervision of the efficiency and effectiveness of the internal control, risk management and internal audit systems of the Bank, functioning of these systems as well as accounting and reporting systems within the framework of related procedures, and the integrity of information generated;
- The preliminary assessment on the selection process of independent audit firms and the systematic monitoring of the activities of these companies;
- The maintenance and coordination of the internal audit functions of corporations subject to consolidated internal audits.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

### (b) Credit risk

Credit risk is most simply defined as the potential that a bank borrower or counterparty will fail to meet its obligations in accordance with agreed terms. Credit risk is defined as the probability of loss if the customer or counterparty fails to meet its obligations partially or completely on the terms set. Credit risk is considered in depth covering the counterparty risks arising from not only from future or option contracts but also credit risks originating from the transactions in Banking Law.

**Exposure to credit risk**

| | Loans and receivables to customers | | Other assets | |
|---|---|---|---|---|
| | **2018** | **2017** | **2018** | **2017** |
| Impaired | 817,736 | 332,938 | 3,214 | 4,119 |
| Individual allowance for impairment | (443,840) | (105,962) | (3,214) | (4,119) |
| **Carrying amount** | **373,896** | **226,976** | **-** | **-** |
| Past due but not impaired | 197,160 | 726,998 | - | - |
| **Carrying amount** | **197,160** | **726,998** | **-** | **-** |
| Neither past due nor impaired | 11,120,538 | 11,900,243 | - | - |
| Loans with renegotiated terms | 505,060 | 354,247 | - | - |
| **Carrying amount** | **11,625,598** | **12,254,490** | **-** | **-** |
| Collective allowance for impairment | (156,148) | (131,074) | - | - |
| **Total carrying amount** | **12,040,506** | **13,077,390** | **-** | **-** |

**Impaired loans and receivables**

Impaired loans and receivables are loans and receivables for which the Group determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan agreements.

**Past due but not impaired loans**

Loans and receivables where contractual interest or principal payments are past due but the Group believes that impairment is not appropriate on the basis of the level of security / collateral available and / or the stage of collection of amounts owed to the Group.

**Loans with renegotiated terms**

Loans with renegotiated terms are loans that have been restructured due to temporary deterioration in the borrower's financial position and where the Group has made concessions that it would not otherwise consider. Once the loan is restructured it remains in this category independent of satisfactory performance after restructuring.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(b) Credit risk** *(continued)*

**Write-off policy**

The Group writes off a loan / security balance (and any related allowances for impairment losses) when Group determines that the loans / securities are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower / 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 and the completion of the legal procedure. For smaller balance standardised loans, charge off decisions generally are based on a product specific past due status.

The Bank has written off the non-performing loans from the loan portfolio as of 31 December 2018 and subtracted which is amounted to TL 42,574. The Parent Bank's subsidiary Anadolu Faktoring A.Ş. sold the non-performing loans from the loan portfolio in 30 November 2018, subtracted which is amounted to TL 14,512.

**Collateral policy**

The Group holds collateral against loans and receivables to customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over loans and advances to banks, except when securities are held as part of reverse repurchase and securities borrowing activity. Collateral usually is not held against investment securities, and no such collateral was held at 31 December 2018 or 2017.

The breakdown of performing cash and non-cash loans and receivables to customers by type of collateral is as follows:

| **Cash loans** | **31 December 2018** | **31 December 2017** |
|---|---|---|
| Secured loans: | | |
| Secured by cash collateral | 279,969 | 238,093 |
| *Secured by mortgages* | *2,898,290* | *3,697,054* |
| *Secured by government institutions or government securities* | *581,824* | - |
| *Guarantees issued by financial institutions* | *29,608* | *24,661* |
| *Other collateral (pledge on assets, corporate and personal guarantees, promissory notes)* | *3,871,895* | *7,437,049* |
| Unsecured loans | 3,788,799 | 1,164,437 |
| **Total performing loans and receivables** | **11,450,385** | **12,561,294** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(b) Credit risk** *(continued)*

**Collateral policy** *(continued)*

| **Non-cash loans** | **31 December 2018** | **31 December 2017** |
|---|---|---|
| Secured loans: | | |
| *Secured by mortgages* | *166,555* | *197,130* |
| *Secured by cash collateral* | *122,022* | *83,865* |
| *Guarantees issued by financial institutions* | *2,915* | - |
| *Other collateral (pledge on assets, corporate and personal guarantees, promissory notes)* | *295,392* | *3,101,836* |
| Unsecured loans | 3,120,381 | 529,799 |
| **Total non-cash loans** | **3,707,265** | **3,912,630** |

An estimate of the fair value of collaterals held against non-performing loans and receivables is as follows:

| | **31 December 2018** | **31 December 2017** |
|---|---|---|
| Mortgages | 444,466 | 184,788 |
| Pledge on automobile | 6,076 | 2,030 |
| **Total** | **450,542** | **186,818** |

**Sectorial and geographical concentration of impaired loans**

The Bank and its subsidiaries monitor concentrations of credit risk by sector and by geographic location. An analysis of concentrations of non-performing loans is shown below:

| | **31 December 2018** | **31 December 2017** |
|---|---|---|
| Service sector | 280,635 | 82,614 |
| Construction | 244,853 | 70,828 |
| Agriculture and stockbreeding | 129,704 | 56,574 |
| Textile | 30,600 | 30,125 |
| Consumer loans | 18,414 | 15,719 |
| Food | 4,514 | 11,911 |
| Metal and metal products | 9,884 | 8,233 |
| Durable consumption | 17,523 | 7,254 |
| Others | 84,823 | 53,799 |
| **Total non-performing loans and receivables** | **820,950** | **337,057** |

| | **31 December 2018** | **31 December 2017** |
|---|---|---|
| Turkey | 820,950 | 337,057 |
| United States of America | - | - |
| **Total non-performing loans and receivables** | **820,950** | **337,057** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

## (b) Credit risk *(continued)*

### Sectorial break down of cash and non-cash loans

| | 31 December 2018 | | | | 31 December 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Cash | Cash (%) | Non cash | Non cash (%) | Cash | Cash (%) | Non-cash | Non-cash (%) |
| **Agriculture** | **1,041,995** | **8.65** | **27,556** | **1.00** | **1,230,166** | **9.41** | **16,127** | **0.41** |
| *Farming and stockbreeding* | *1,015,234* | *8.43* | *13,873* | *0.50* | *1,181,461* | *9.04* | *11,266* | *0.29* |
| *Forestry* | *6,087* | *0.05* | *7,017* | *0.25* | *10,788* | *0.08* | *2,756* | *0.07* |
| *Fishing* | *20,674* | *0.17* | *6,666* | *0.25* | *37,917* | *0.29* | *2,105* | *0.05* |
| **Industry** | **3,259,685** | **27.06** | **844,422** | **23.00** | **3,359,630** | **25.69** | **880,513** | **22.50** |
| *Mining and quarrying* | *99,655* | *0.83* | *6,735* | *1.00* | *137,239* | *1.05* | *3,444* | *0.09* |
| *Manufacturing* | *2,959,100* | *24.56* | *786,627* | *21.00* | *2,560,762* | *19.58* | *720,139* | *18.40* |
| *Electricity, gas, water* | *200,930* | *1.67* | *51,060* | *1.00* | *661,629* | *5.06* | *156,930* | *4.01* |
| **Construction** | **1,928,394** | **16.01** | **1,013,415** | **27.00** | **2,442,985** | **18.68** | **1,162,085** | **29.70** |
| **Services** | **5,630,950** | **46.74** | **1,794,042** | **48.00** | **5,695,053** | **43.55** | **1,827,471** | **46.71** |
| *Wholesale and retail trade* | *2,775,006* | *23.04* | *618,831* | *17.00* | *2,944,000* | *22.52* | *588,507* | *15.04* |
| *Hotel and restaurant services* | *106,548* | *0.88* | *32,573* | *1.00* | *400,281* | *3.06* | *30,221* | *0.77* |
| *Transportation and communication* | *611,745* | *5.08* | *96,249* | *2.00* | *578,061* | *4.42* | *120,025* | *3.07* |
| *Financial institution* | *1,428,825* | *11.86* | *901,275* | *24.00* | *1,100,468* | *8.42* | *845,650* | *21.61* |
| *Real estate and rent services* | *115,286* | *0.96* | *2,405* | - | *64,588* | *0.49* | *4,281* | *0.11* |
| *Professional services* | *107,282* | *0.89* | *34,778* | *1.00* | *160,124* | *1.22* | *112,513* | *2.88* |
| *Educational services* | *207,425* | *1.72* | *48,255* | *1.00* | *206,488* | *1.58* | *75,446* | *1.93* |
| *Health and social services* | *278,833* | *2.31* | *59,676* | *2.00* | *241,043* | *1.84* | *50,828* | *1.30* |
| **Consumer loans** | **15,323** | **0.13** | **-** | **-** | **215,822** | **1.65** | **-** | **-** |
| **Credit card** | **63,405** | **0.53** | **-** | **-** | **61,590** | **0.47** | **-** | **-** |
| **Others** | **100,754** | **0.88** | **27,830** | **1.00** | **72,144** | **0.55** | **26,434** | **0.68** |
| **Total** | **12,040,506** | **100.00** | **3,707,265** | **100.00** | **13,077,390** | **100.00** | **3,912,630** | **100.00** |

**26. Financial risk management *(continued)***

**(c) Liquidity risk**

In order to avoid the liquidity risk, the Group diversifies funding resources as customer deposits and foreign borrowings, considers the maturity mismatch between assets and liabilities and maintains liquid assets to guarantee sufficient liquidity during market fluctuations.

While the Group short term liquidity need is met mainly with deposits, its long term liquidity is provided through foreign funding sources such as syndication and securitization transactions. There are no significant idle liquidity resources.

**Liquidity coverage ratio**

The Bank makes use of liquidity stress tests in the internal measurement of liquidity risk. In liquidity gap analysis and liquidity stress scenarios, the Bank’s compensation level of net cash outflows which are more likely to happen in short term are presented. Measurements regarding liquidity risk are performed by Risk Management Department and measurement results are reported regularly to performer units responsible of management of the related risk and top management and the Board of Directors.

Liquidity risk may occur as a result of funding long-term assets with short-term resources. Utmost care is taken to maintain the consistency between the maturities of assets and liabilities; strategies are used to acquire funds over longer terms. In order to avoid adversely affecting the Bank's liquidity risk profile on the funding side of concentrations that may occur, deposit and non-deposit debt concentration limits are used in an active way.

Liquidity risk exposure of the bank, depending on the basic strategy of the Bank is consistent with the resulting risk appetite with risk capacity determined within the limits anticipated by the legislation is a key priority.

The Bank, against a reduction in the huge levels may occur in liquidity sources it is essential to have adequate levels free liquid assets that can be sold in any case or pledged. The level of liquidity buffer consisting of liquid assets in question, expressed in liquidity risk limits are determined by the Board of Directors and is set in accordance with the Bank’s liquidity risk tolerance. The Bank's Asset Liability Committee (ALCO) is responsible for determination of the required funding sources and maturities, revising the liquidity situation to determine the appropriate level of liquidity, within the limits approved by the Board of Directors.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(c) Liquidity risk** *(continued)*

**Liquidity coverage ratio** *(continued)*

| | | Total Unweighted Value (average)(*) | | Total Weighted Value (average)(*) | |
|---|---|---|---|---|---|
| **Current Period** | | **TL+FC** | **FC** | **TL+FC** | **FC** |
| **HIGH QUALITY LIQUIDITY ASSETS** | | | | | |
| 1 | High Quality Liquidity Assets | | | 2,911,110 | 2,367,761 |
| **CASH OUTFLOWS** | | | | | |
| 2 | Retail and Small Business Customers' Deposits | 10,654,664 | 4,761,955 | 909,536 | 391,753 |
| 3 | Stable Deposits | 3,118,590 | 1,688,856 | 155,929 | 84,443 |
| 4 | Less Stable Deposits | 7,536,074 | 3,073,099 | 753,607 | 307,310 |
| 5 | Unsecured Fundings besides retail and small business customers' deposits | 3,706,898 | 1,845,041 | 2,118,831 | 1,000,513 |
| 6 | Operational Deposits | - | - | - | - |
| 7 | Non-Operational Deposits | 3,191,563 | 1,675,088 | 1,612,762 | 830,560 |
| 8 | Other unsecured fundings | 515,335 | 169,953 | 506,069 | 169,953 |
| 9 | Secured Fundings | | | 37,466 | 37,466 |
| 10 | Other Cash Outflows | 102,429 | 146,929 | 102,430 | 146,929 |
| 11 | Derivatives cash outflows and collateral outflows | 102,429 | 146,929 | 102,430 | 146,929 |
| 12 | Obligation related to structured financial products | - | - | - | - |
| 13 | Commitments related to debts to financial markets and other off-balance sheet obligations | - | - | - | - |
| 14 | Other revocable off-balance sheet commitments and contractual obligations | 96,389 | 96,389 | 4,819 | 4,819 |
| 15 | Other irrevocable or conditionally revocable off-balance sheet obligations | 3,832,914 | 1,263,333 | 382,299 | 212,239 |
| **16** | **TOTAL CASH OUTFLOWS** | | | **3,555,381** | **1,793,719** |
| **CASH INFLOWS** | | | | | |
| 17 | Secured Lending | 70,481 | - | - | - |
| 18 | Unsecured Lending | 2,453,516 | 1,496,173 | 1,947,775 | 1,381,674 |
| 19 | Other Cash Inflows | 36,455 | 143,613 | 36,455 | 143,614 |
| 20 | **TOTAL CASH INFLOWS** | **2,560,452** | **1,639,786** | **1,984,230** | **1,525,288** |
| | | | | **Total Adjusted Value** | |
| 21 | **TOTAL HQLA STOCK** | | | **2,911,110** | **2,367,761** |
| 22 | **TOTAL NET CASH OUTFLOW** | | | **1,571,151** | **462,486** |
| 23 | **LIQUIDITY COVERAGE RATIO (%)** | | | **185.29** | **511.96** |

(*) It is the average calculated for the last three months of the consolidated liquidity coverage, calculated by taking a monthly simple arithmetic mean.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

### (c) Liquidity risk *(continued)*

**Liquidity coverage ratio** *(continued)*

| Prior Period | | Total Unweighted Value (average) (*) | | Total Weighted Value (average) (*) | |
|---|---|---|---|---|---|
| | | TL+FC | FC | TL+FC | FC |
| **HIGH QUALITY LIQUIDITY ASSETS** | | | | | |
| 1 | High Quality Liquidity Assets | | | 2,488,406 | 2,032,479 |
| **CASH OUTFLOWS** | | | | | |
| 2 | Retail and Small Business Customers' Deposits | 9,232,009 | 3,848,706 | 840,538 | 367,399 |
| 3 | Stable Deposits | 1,653,256 | 349,435 | 82,663 | 17,472 |
| 4 | Less Stable Deposits | 7,578,753 | 3,499,271 | 757,875 | 349,927 |
| 5 | Unsecured fundings besides retail and small business customers' deposits | 4,914,465 | 1,740,452 | 2,741,337 | 878,198 |
| 6 | Operational Deposits | 33,750 | 33,750 | 8,438 | 8,438 |
| 7 | Non-Operational Deposits | 3,895,839 | 1,617,091 | 1,757,826 | 780,149 |
| 8 | Other unsecured fundings | 984,876 | 89,611 | 975,073 | 89,611 |
| 9 | Secured Fundings | | | 33,054 | 33,054 |
| 10 | Other Cash Outflows | 10,496 | 223,889 | 10,496 | 223,889 |
| 11 | Derivatives cash outflows and collateral outflows | 10,496 | 223,889 | 10,496 | 223,889 |
| 12 | Obligation related to structured financial products | - | - | - | - |
| 13 | Commitments related to debts to financial markets and other off-balance sheet obligations | - | - | - | - |
| 14 | Other revocable off-balance sheet commitments and contractual obligations | 7,582 | 7,582 | 379 | 379 |
| 15 | Other irrevocable or conditionally revocable off-balance sheet obligations | 3,968,906 | 1,174,650 | 429,165 | 183,498 |
| **16** | **TOTAL CASH OUTFLOWS** | | | **4,054,969** | **1,686,417** |
| **CASH INFLOWS** | | | | | |
| 17 | Secured Lending | 73,358 | - | - | - |
| 18 | Unsecured Lending | 1,991,096 | 895,971 | 1,628,633 | 800,092 |
| 19 | Other Cash Inflows | 35,819 | 257,153 | 35,819 | 257,153 |
| 20 | **TOTAL CASH INFLOWS** | **2,100,273** | **1,153,124** | **1,664,453** | **1,057,245** |
| | | | | **Total Adjusted Value** | |
| 21 | **TOTAL HQLA STOCK** | | | **2,488,406** | **2,032,479** |
| 22 | **TOTAL NET CASH OUTFLOW** | | | **2,390,516** | **629,172** |
| 23 | **LIQUIDITY COVERAGE RATIO (%)** | | | **104.09** | **323.04** |

(*) It is the average calculated for the last three months of the consolidated liquidity coverage, calculated by taking a monthly simple arithmetic mean.

| | **Current period** | | **Perior period** | |
|---|---|---|---|---|
| | TL+FC | FC | TL+FC | FC |
| **Lowest** | **128.67** | **344.96** | **99.35** | **312.56** |
| **related month** | 29 November 2018 | 31 December 2018 | 31 October 2017 | 31 December 2017 |
| **Highest** | **241.98** | **711.86** | **111.60** | **330.33** |
| **related month** | 2 November 2018 | 1 November 2018 | 31 December 2017 | 30 November 2017 |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

### (c) Liquidity risk *(continued)*

**Liquidity coverage ratio** *(continued)*

Liquidity coverage ratio aims to ensure banks maintain adequate levels of high quality liquid assets against net cash outflows. High quality liquid assets are mainly cash and cash equivalents, reserve requirements maintained at CBRT and marketable securities that are not subject to repurchase agreements or not given as collateral. 67% of the Bank's high quality assets are cash & cash equivalents and reserve requirements maintained at CBRT; 27% are marketable securities and %6 are cash. Besides, time deposits, derivatives, loans up to 1 month and non-cash loans are balance sheet accounts that are significant on the ratio. 78% of cash outflows are unsecured funding, 2% are secured funding and 20% are off-balance items.

*Residual contractual maturities of monetary liabilities*

| 31 December 2018 | Carrying amount | Gross nominal outflow | Demand | Less than one month | 1-3 months | 3 months to 1 year | 1-5 years | More than 5 years |
|---|---|---|---|---|---|---|---|---|
| Deposits from banks | 144,362 | 145,538 | 290 | 63,612 | 81,636 | - | - | - |
| Deposits from customers | 12,726,125 | 13,609,973 | 1,272,053 | 5,859,666 | 5,098,015 | 875,078 | 466,891 | 38,270 |
| Obligations under repurchase agreements | 380,786 | 382,431 | - | 84,859 | 152,287 | 113,937 | 31,348 | - |
| Funds borrowed | 722,936 | 730,048 | - | 346,025 | 41,169 | 145,707 | 197,147 | - |
| **Total** | **13,974,209** | **14,867,990** | **1,272,343** | **6,354,162** | **5,373,107** | **1,134,722** | **695,386** | **38,270** |

| 31 December 2017 | Carrying amount | Gross nominal outflow | Demand | Less than one month | 1-3 months | 3 months to 1 year | 1-5 years | More than 5 years |
|---|---|---|---|---|---|---|---|---|
| Deposits from banks | 366,325 | 368,585 | 6,410 | - | 287,704 | 74,471 | - | - |
| Deposits from customers | 12,980,125 | 13,493,842 | 1,256,339 | 824,293 | 9,901,080 | 1,005,668 | 368,662 | 137,800 |
| Obligations under repurchase agreements | 827,036 | 882,688 | - | 297,460 | 331,473 | 230,265 | 23,490 | - |
| Funds borrowed | 801,662 | 805,865 | - | 312,747 | 231,386 | 170,542 | 91,190 | - |
| **Total** | **14,975,148** | **15,550,980** | **1,262,749** | **1,434,500** | **10,751,643** | **1,480,946** | **483,342** | **137,800** |

The previous table shows the undiscounted cash flows on the Group's monetary liabilities on the basis of their earliest possible contractual maturity. The Group's expected cash flows on these instruments vary significantly from this analysis.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

### (c) Liquidity risk *(continued)*

The table below analyses contractual maturities of derivative transactions:

| | 31 December 2018 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Fair value assets** | **Fair value liabilities** | **Notional amount in Turkish Lira equivalent** | **Up to 1 month** | **1 to 3 months** | **3 to 6 months** | **6 to 12 months** | **1 to 5 years** | **More than 5 years** |
| ***Derivatives financial instruments held for trading purpose:*** | | | | | | | | | |
| Forward purchase contract | 2,784 | 496 | 401,416 | 388,969 | 8,322 | 2,697 | 1,428 | - | - |
| Forward sale contract | - | - | 398,844 | 386,828 | 8,125 | 3,299 | 592 | - | - |
| Currency swap purchase | 21,166 | 32,832 | 2,133,435 | 1,292,258 | 326,587 | 32,552 | 221,981 | 260,057 | - |
| Currency swap sale | - | - | 2,156,008 | 1,297,913 | 328,638 | 33,947 | 232,110 | 263,400 | - |
| Interest swap purchase | - | - | 590,474 | - | - | - | 60,280 | 389,415 | 140,779 |
| Interest swap sale | - | - | 590,474 | - | - | - | 60,280 | 389,415 | 140,779 |
| Put option purchase | - | - | 194,119 | 174,021 | 16,864 | 3,234 | - | - | - |
| Put option sale | - | - | 205,651 | 185,444 | 16,973 | 3,234 | - | - | - |
| **Total** | **23,950** | **33,328** | **6,670,421** | **3,725,433** | **705,509** | **78,963** | **576,671** | **1,302,287** | **281,558** |

| | 31 December 2017 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Fair value assets** | **Fair value liabilities** | **Notional amount in Turkish Lira equivalent** | **Up to 1 month** | **1 to 3 months** | **3 to 6 months** | **6 to 12 months** | **1 to 5 years** | **More than 5 years** |
| ***Derivatives financial instruments held for trading purpose:*** | | | | | | | | | |
| Forward purchase contract | 1,116 | 1,288 | 424,376 | 408,341 | 10,623 | 5,412 | - | - | - |
| Forward sale contract | - | - | 430,993 | 414,976 | 10,616 | 5,401 | - | - | - |
| Currency swap purchase | 27,755 | 22,132 | 2,023,645 | 1,279,264 | 216,887 | 3,268 | 233,121 | 214,043 | 77,062 |
| Currency swap sale | - | - | 2,021,494 | 1,252,063 | 250,703 | 24,160 | 212,558 | 178,009 | 104,001 |
| Interest swap purchase | - | - | 483,953 | - | - | - | - | 442,550 | 41,403 |
| Interest swap sale | - | - | 483,953 | - | - | - | - | 370,271 | 113,682 |
| Put option purchase | - | - | 228,934 | 193,612 | 35,322 | - | - | - | - |
| Put option sale | - | - | 228,934 | 193,612 | 35,322 | - | - | - | - |
| **Total** | **28,871** | **23,420** | **6,326,282** | **3,741,868** | **559,473** | **38,241** | **445,679** | **1,204,873** | **336,148** |

### *Non-cash loans*

| **31 December 2018** | **Demand** | **Less than one month** | **1-3 months** | **3 months to 1 year** | **1-5 years** | **More than 5 years** | **Total** |
|---|---|---|---|---|---|---|---|
| Non-cash loans | - | 1,355,524 | 61,036 | 1,064,111 | 1,024,230 | 202,364 | **3,707,265** |

| **31 December 2017** | **Demand** | **Less than one month** | **1-3 months** | **3 months to 1 year** | **1-5 years** | **More than 5 years** | **Total** |
|---|---|---|---|---|---|---|---|
| Non-cash loans | - | 1,430,614 | 64,417 | 1,123,058 | 1,080,967 | 213,574 | **3,912,630** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

## (d) Market risk

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads will affect the Group'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 optimizing the return on risk.

### Management of market risk

The Group separates its exposure to market risk between trading and non-trading portfolios. Trading portfolios mainly are held by the Treasury Department, and include positions arising from market making and proprietary position taking, together with financial assets and liabilities that are managed on a fair value basis.

### Exposure to market risk – trading portfolios

The market risk arising from trading portfolio is monitored, measured and reported using Standardised Approach according to the legal legislation. The monthly market risk report and the weekly currency risk reports prepared using Standardised Approach are reported to BRSA.

The principal tool used to measure and control market risk exposure within the Bank's trading portfolios is Value at Risk (VaR). The VaR of a trading portfolio is the estimated loss that will arise on the portfolio over a specified period of time (holding period) from an adverse market movement with a specified probability (confidence level). The VaR model used by the Group is based upon a 99 percent confidence level and assumes a 1 day holding period. The VaR model used is based mainly on Monte Carlo simulation. Taking account of market data from the previous 252 days, and observed relationships between different markets and prices, the model generates a wide range of plausible future scenarios and stress tests for market price movements. The VaR model used is based on and Monte Carlo simulation with using with Nelson Siegel method for yield curve and GARCH method for volatility. The VaR analysis of the Bank are not reported outside and used only by the top management.

The consolidated value at market risk as of 31 December 2018 calculated as per the statutory consolidated financial statements prepared for the BRSA reporting purposes within the scope of "Regulation on Measurement and Assessment of Capital Adequacy Ratios of Banks" published in Official Gazette no. 28337 dated 28 June 2012 based on the Basel II requirements effective from 1 July 2012 is as follows:

| | | **RWA** |
|---|---|---|
| 1 | Indirect (Cash) Products | |
| 2 | Interest Rate Risk ( general and specific ) | 967,800 |
| 3 | Stock risk (general and specific) | 14,900 |
| 4 | Currency risk | 35,263 |
| | Commodity risk | - |
| 5 | Options | |
| 6 | Simplified Approach | - |
| 7 | Delta-Plus Method | 312 |
| 8 | Scenario Approach | - |
| 9 | Securitization | - |
| | **Total** | **1,018,275** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

## (d) Market risk *(continued)*

### 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 in its day-to-day monitoring activities. A summary of the Group's interest rate gap position is as follows:

| 31 December 2018 | Less than one month | 1-3 months | 3-12 months | 1 -5 years | Over 5 year | Non-Interest | Carrying amount |
|---|---|---|---|---|---|---|---|
| Cash and balances with the Central Bank | 2 | 273,029 | - | - | - | 1,186,848 | **1,459,879** |
| Loans and advances to banks and other financial institutions | 1,317,041 | 28,697 | - | - | - | 162,403 | **1,508,141** |
| Receivables from reverse repurchase transactions | 200,137 | 6,300 | 23,196 | 25,492 | - | 18,211 | **273,336** |
| Financial assets at fair value through profit or loss | - | - | 115 | 1,038 | 48 | - | **1,633** |
| Financial assets at FVOCI | - | - | 58,834 | 257,753 | 427,861 | 12,244 | **756,692** |
| Loans and receivables | 3,923,064 | 2,548,092 | 4,418,647 | 766,735 | 15,710 | 368,258 | **12,040,506** |
| Financial assets measured at amortised cost | 23,874 | 16,089 | 127,367 | 340,223 | 53,884 | - | **561,437** |
| Other assets | 30,524 | - | 2,561 | - | 232 | 864,755 | **898,072** |
| **Total assets** | **5,494,642** | **2,872,207** | **4,630,720** | **1,391,241** | **498,167** | **2,612,719** | **17,499,696** |
| Deposits from banks | 63,155 | 80,917 | - | - | - | 290 | **144,362** |
| Deposits from customers | 8,100,233 | 2,896,431 | 684,671 | 416,072 | 32,431 | 596,287 | **12,726,125** |
| Obligations under repurchase agreements and interbank money market borrowings | 278,341 | 294,263 | 113,194 | 31,303 | - | 1,236 | **718,337** |
| Funds borrowed | 343,867 | 40,951 | 143,102 | 195,016 | - | - | **722,936** |
| Other liabilities, provisions and equity | 8,055 | 526 | - | 712 | 439 | 3,178,204 | **3,187,936** |
| **Total liabilities** | **8,793,651** | **3,313,088** | **940,967** | **643,103** | **32,870** | **3,776,017** | **17,499,696** |
| **Net** | **(3,299,009)** | **(440,881)** | **3,689,753** | **748,138** | **465,297** | **(1,163,298)** | **-** |

| 31 December 2017 | Less than one month | 1-3 months | 3-12 months | 1 -5 years | Over 5 year | Non-Interest | Carrying amount |
|---|---|---|---|---|---|---|---|
| Cash and balances with the Central Bank | - | 313,906 | - | - | - | 1,567,991 | **1,881,897** |
| Loans and advances to banks and other financial institutions | 927,704 | 29,765 | 1,557 | - | - | 84,917 | **1,043,943** |
| Receivables from reverse repurchase transactions | 54,187 | 22,643 | 25,488 | 5,426 | - | 1,551 | **109,295** |
| Trading assets (including derivative assets) | 1,609 | 149 | 94,430 | 15,337 | 691 | 27,027 | **139,243** |
| Available for sale | - | 26,128 | 66,277 | 661,866 | 482,157 | 160 | **1,236,588** |
| Loans and receivables | 4,779,740 | 1,839,096 | 3,369,809 | 2,929,344 | 63,499 | 95,902 | **13,077,390** |
| Investment securities | - | - | - | - | - | - | **-** |
| Other assets | 23,872 | 107 | 4,380 | 214 | - | 633,307 | **661,880** |
| **Total assets** | **5,787,112** | **2,231,794** | **3,561,941** | **3,612,187** | **546,347** | **2,410,855** | **18,150,236** |
| Deposits from banks | 285,997 | 73,918 | - | - | - | 6,410 | **366,325** |
| Deposits from customers | 7,755,239 | 3,268,982 | 460,216 | 217,092 | 22,257 | 1,256,339 | **12,980,125** |
| Obligations under repurchase agreements and interbank money market borrowings | 394,067 | 662,302 | 21,571 | 23,451 | - | 119,376 | **1,220,767** |
| Funds borrowed | 335,930 | 81,504 | 292,264 | 91,964 | - | - | **801,662** |
| Other liabilities, provisions and equity | 13,940 | 1,332 | 695 | 605 | - | 2,764,785 | **2,781,357** |
| **Total liabilities** | **8,785,173** | **4,088,038** | **774,746** | **333,112** | **22,257** | **4,146,910** | **18,150,236** |
| **Net** | **(2,998,061)** | **(1,856,244)** | **2,787,195** | **3,279,075** | **524,090** | **(1,736,055)** | **-** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

### (d) Market risk *(continued)*

The following table indicates the effective interest rates by major currencies for the major components of the consolidated statement of financial position for 2018 and 2017:

| 31 December 2018 | Euro % | USD % | JPY % | TL % |
|---|---|---|---|---|
| Cash and balances with Central Bank | - | 2.00 | - | 13.00 |
| Financial assets at fair value through profit or loss | 3.73 | 6.98 | - | 21.33 |
| Money market placements | 0.43 | 3.79 | - | 21.32 |
| Financial assets at FVOCI | 1.04 | 6.32 | - | - |
| Loans and receivables to customers | 1.97 | 2.81 | 2.23 | 27.73 |
| Financial assets measured at amortised cost | - | - | - | - |
| | | | | |
| Deposits from banks | - | 2.17 | - | 21.81 |
| Deposits from customers | 1.99 | 4.51 | - | 22.91 |
| Obligations under repurchase agreements | 0.21 | 3.45 | - | 20.00 |
| Funds borrowed | 0.69 | 4.48 | - | 23.64 |

| 31 December 2017 | Euro % | USD % | JPY % | TL % |
|---|---|---|---|---|
| Cash and balances with Central Bank | - | 1.50 | - | 4.00 |
| Financial assets at fair value through profit or loss | 2.30 | 5.53 | - | 13.79 |
| Money market placements | - | - | - | - |
| Available for sale | 4.26 | 4.98 | - | 12.89 |
| Loans and receivables to customers | 3.58 | 4.98 | 8.28 | 17.58 |
| Investment securities | - | - | - | - |
| | | | | |
| Deposits from banks | 0.54 | 3.05 | - | 14.50 |
| Deposits from customers | 2.03 | 4.27 | - | 4.86 |
| Obligations under repurchase agreements | 0.70 | 2.12 | - | 12.71 |
| Funds borrowed | 1.48 | 3.56 | - | 6.72 |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(d) Market risk** *(continued)*

**Interest rate sensitivity of the trading and non-trading portfolios**

Interest rate risk in the banking book is evaluated considering the repricing risk, yield curve risk, basis risk and optionality, measured in compliance with the international standards and managed by risk mitigation through limits and hedging.

The interest rate sensitivity of assets, liabilities and off balance-sheet items are evaluated at the weekly Asset-Liability Committee meetings considering also the market developments.

The measurement process of interest rate risk resulting from banking book is established and managed by the Bank on a bank-only basis to include the interest rate positions defined as banking book and to consider the relevant repricing and maturity data.

Duration gaps, gaps by maturity buckets and sensitivity analysis are used in monitoring of repricing risk resulting from maturity mismatch. The duration gap and sensitivity analysis are carried out every two weeks period.

In the duration gap analysis, the present values of interest-rate-sensitive asset and liability items are calculated using yield curves developed from market interest rates. In case of instruments with no maturities assigned, the maturity is determined as per interest rate fixing periods and customer behaviours. Such results are supported by sensitivity and scenario analysis applied periodically for possible instabilities in the markets.

The interest rate risk resulted from banking book is measured legally as per the "Regulation on Measurement and Evaluation of Interest Rate Risk Resulted from Banking Book as per Standard Shock Method" published in the Official Gazette no. 28034 dated 23 August 2011, and the legal limit as per this measurement is monitored and reported monthly. The capital level is maintained considering the interest rate risk resulted from the banking book.

The interest rate risk on the interest-rate-sensitive financial instruments of the trading portfolio is evaluated as part of the market risk.

As of 31 December 2018, the economic value differences resulted from interest rate instabilities calculated on a bank-only basis for the banking book according to the relevant legislation as per the standard shock method are as follows;

| Type of currency | Shocks applied (+/- basis points) | Gains/losses | Gains/equity-Losses/equity |
|---|---|---|---|
| TL | (+) 500 bps | (121,453) | (4.8) % |
| TL | (-) 400 bps | 107,905 | 4.3% |
| USD | (+) 200 bps | (7,359) | (0.3) % |
| USD | (-) 200 bps | (493) | (0.0)% |
| EUR | (+) 200 bps | (5,229) | (0.2) % |
| EUR | (-) 200 bps | 5,687 | 0.2% |
| **Total (of negative shocks)** | | **113,099** | **4.50%** |
| **Total (of positive shocks)** | | **(134,041)** | **(5.30)%** |

## 26. Financial risk management *(continued)*

### (d) Market risk *(continued)*

**Currency risk**

Currency risk arises when an entity's equity is under threat as a result of exchange rate fluctuations. Naturally, a bank doing business in multiple currencies would be exposed to currency risk unless these risks are properly hedged. Any sizeable transaction that would be causing currency risk is immediately hedged with a banking counterpart, or else smaller transactions are gathered until they form a sizeable amount for hedging.

Foreign exchange gains and losses arising from foreign currency transactions are recorded at transaction dates. At the end of the periods, foreign currency assets and liabilities evaluated with the Bank's spot purchase rates and the differences are recorded as foreign exchange gain or loss in profit or loss except for foreign exchange gain/loss arising from the conversion of the net investments in subsidiaries in foreign countries into TL.

The Bank takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board of Directors sets limit on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily. The Group's exposure to foreign currency exchange rate risk at 31 December 2018 and 2017, on the basis of the Group's assets and liabilities at carrying amounts, categorised by currency, is shown in the following table.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(d) Market risk** *(continued)*

**Currency risk** *(continued)*

| **As at 31 December 2018** | **USD** | **Euro** | **Other currencies** | **Total** |
|---|---|---|---|---|
| **Assets:** | | | | |
| Cash and balances with the Central Bank | 684,937 | 208,718 | 236,643 | 1,130,298 |
| Loans and advances to banks and other financial institutions | 523,802 | 935,672 | 19,866 | 1,479,340 |
| Receivables from reverse repo transactions | 11,628 | 61,571 | - | 73,199 |
| Financial assets at FVOCI | 642,690 | 109,047 | - | 751,737 |
| Financial assets at FVTPL | 550 | 987 | - | 1,537 |
| Financial assets measured at amortised cost | 127,504 | 203,208 | - | 330,712 |
| Loans and receivables | 1,437,752 | 1,672,311 | 32,947 | 3,143,010 |
| Other assets | 12,079 | 4,096 | 1,177 | 17,352 |
| **Total assets** | **3,440,942** | **3,195,610** | **290,633** | **6,927,185** |
| **Liabilities:** | | | | |
| Deposits from other banks | 63,384 | 36 | 5 | 63,425 |
| Deposits from customers | 3,341,291 | 2,305,771 | 48,908 | 5,695,970 |
| Other money market deposits | 284,166 | 397,607 | 16,553 | 698,326 |
| Funds borrowed | 119,888 | 351,138 | - | 471,026 |
| Other liabilities and provisions | 19,580 | 9,802 | 49 | 29,431 |
| **Total liabilities** | **3,828,309** | **3,064,354** | **65,515** | **6,958,178** |
| **Net position on the consolidated statement of financial position** | **(387,367)** | **131,256** | **225,118** | **(30,993)** |
| **Off-balance sheet position:** | | | | |
| Net notional amount of derivatives | 333,744 | (113,289) | (226,111) | (5,656) |
| **Net position** | **(53,623)** | **17,967** | **(993)** | **(36,649)** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(d) Market risk** *(continued)*

**Currency risk** *(continued)*

| **As at 31 December 2017** | **USD** | **Euro** | **Other currencies** | **Total** |
|---|---|---|---|---|
| **Assets:** | | | | |
| Cash and balances with the Central Bank | 1,009,727 | 145,809 | 378,724 | 1,534,260 |
| Loans and advances to banks and other financial institutions | 536,039 | 430,966 | 27,037 | 994,042 |
| Receivables from reverse repo transactions | 10,072 | 99,223 | - | 109,295 |
| Available for sale | 738,645 | 274,959 | - | 1,013,604 |
| Financial assets at fair value through profit or loss | 460 | 347 | - | 807 |
| Investment securities | - | - | - | - |
| Loans and receivables | 1,290,508 | 1,958,505 | 32,290 | 3,281,303 |
| Other assets | 18,248 | 3,621 | 1,892 | 23,761 |
| **Total assets** | **3,603,699** | **2,913,430** | **439,943** | **6,957,072** |
| **Liabilities:** | | | | |
| Deposits from other banks | 94,938 | 5,475 | 4 | 100,417 |
| Deposits from customers | 3,388,252 | 1,969,951 | 57,755 | 5,415,958 |
| Other money market deposits | 476,127 | 409,229 | 45,832 | 931,188 |
| Funds borrowed | 234,202 | 218,297 | - | 452,499 |
| Other liabilities and provisions | 28,457 | 10,835 | 38 | 39,330 |
| **Total liabilities** | **4,221,976** | **2,613,787** | **103,629** | **6,939,392** |
| **Net position on the consolidated statement of financial position** | **(618,277)** | **299,643** | **336,314** | **17,680** |
| **Off-balance sheet position:** | | | | |
| Net notional amount of derivatives | 629,745 | (212,032) | (337,995) | 79,718 |
| **Net position** | **11,468** | **87,611** | **(1,681)** | **97,398** |

For the purposes of the evaluation of the table above, the figures represent the TL equivalent of the related hard currencies.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(d) Market risk** *(continued)*

**Exposure to currency risk sensitivity analysis**

A 10 percent devaluation of the TL against the following currencies as at 31 December 2018 and 2017 would have increased/(decreased) equity and profit or loss (without tax effects) by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant.

| | 31 December 2018 | | 31 December 2017 | |
|---|---|---|---|---|
| | Profit or loss | Equity(*) | Profit or loss | Equity(*) |
| USD | 2,135 | (5,362) | 1,785 | 1,147 |
| EUR | 1,996 | 1,797 | 9,735 | 8,761 |
| Other currencies | (99) | (99) | (168) | (168) |
| **Total, net** | **4,032** | **(3,664)** | **11,352** | **9,740** |

(*) Equity effect also includes profit or loss effect of 10% devaluation of TL against related currencies.

**Fair value information**

The estimated fair values of financial instruments have been determined using available market information by the Group, and where it exists, appropriate valuation methodologies. However, during financial crisis, judgment is necessary requirement to interpret market data to determine the estimated fair value.

Management has estimated that the fair value of certain financial assets and liabilities are not materially different than their recorded values except for those of loans and advances to customers and investment securities. These financial assets and liabilities include loans and advances to banks, obligations under repurchase agreements, deposits from banks, and other short-term assets and liabilities that are of a contractual nature. Management believes that the carrying amount of these particular financial assets and liabilities approximates their fair value, partially due to the fact that it is practice to renegotiate interest rates to reflect current market conditions.

Fair values and carrying amounts of loans and receivables and financial assets measured at amortised cost as follows:

| | 31 December 2018 | | 31 December 2017 | |
|---|---|---|---|---|
| | Carrying amount | Fair value | Carrying amount | Fair value |
| Loans and receivables | 12,040,506 | 11,965,692 | 13,077,390 | 12,789,297 |
| Financial assets measured at amortised cost | 561,437 | 536,282 | - | - |

Fair values of financial assets measured at amortised cost are determined as Level 1 and fair values of loans and receivables are determined as Level 2.

Fair values of financial assets measured at amortised cost are derived from market prices or in case of absence of such prices they are derived from prices of other marketable securities, whose interest rate, maturity date and other conditions are similar to securities held.

Fair value of long-term fixed interest rate loans are calculated by discounting cash flows with current market interest rates. For the loans with floating interest rate and short term loans with fixed interest rate, carrying value also represents fair value.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

## 26. Financial risk management *(continued)*

### (d) Market risk *(continued)*

**Fair value information** *(continued)*

*IFRS 7 – Financial Instruments* requires the classification of fair value measurements into a fair value hierarchy by reference to the observability and significance of the inputs used in measuring fair value of financial instruments measured at fair value to be disclosed. This classification basically relies on whether the relevant inputs are observable or not.

**Classification of fair value measurement**

Observable inputs refer to the use of market data obtained from independent sources, whereas unobservable inputs refer to the use of predictions and assumptions about the market made by the Bank. This distinction brings about a fair value measurement classification generally as follows:

Level 1: Fair value measurements using quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2: Fair value measurements using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices).

Level 3: Fair value measurements using inputs for the assets or liability that are not based on observable market data (unobservable inputs).

Classification requires using observable market data if possible.

| | 31 December 2018 | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| Financial assets at fair value through profit or loss: | | | | |
| Financial assets at fair value: | | | | |
| Debt instruments | 1,633 | - | - | 1,633 |
| Loans at fair value through profit or loss | - | - | 68,103 | 68,103 |
| Equity securities | - | - | - | - |
| Derivative financial assets held for trading | - | 23,950 | - | 23,950 |
| Financial assets at FVOCI | | | | |
| Debt instruments issued by Turkish government | 744,346 | - | - | 744,346 |
| Equity securities | - | 7,289 | 5,057 | 12,346 |
| **Total financial assets** | **745,979** | **31,239** | **73,160** | **850,378** |
| Financial liabilities at fair value through profit or loss: | | | | |
| Derivative financial liabilities held for trading | - | 33,328 | - | 33,328 |
| **Total financial liabilities** | **-** | **33,328** | **-** | **33,328** |

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(d) Market risk** *(continued)*

**Classification of fair value measurement** *(continued)*

| | 31 December 2017 | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| Financial assets at fair value through profit or loss: | | | | |
| Financial assets at fair value: | | | | |
| Debt instruments | 110,372 | - | - | 110,372 |
| Equity securities | - | - | - | - |
| Derivative financial assets held for trading | - | 28,871 | - | 28,871 |
| Financial assets available for sale | | | | |
| Debt instruments issued by Turkish government | 1,226,965 | - | - | 1,226,965 |
| Equity securities | - | 4,566 | 5,057 | 9,623 |
| **Total financial assets** | **1,337,337** | **33,437** | **5,057** | **1,375,831** |
| Financial liabilities at fair value through profit or loss: | | | | |
| Derivative financial liabilities held for trading | - | 23,420 | - | 23,420 |
| **Total financial liabilities** | **-** | **23,420** | **-** | **23,420** |

Apart from financial assets and financial liabilities, as of 31 December 2018, the Group carries the real estates at fair value under property and equipment. Level 3 inputs are used to determine fair value of property and equipment.

As of 31 December 2018, the revaluation model effect, net of deferred tax, for real estates under property and equipment amounting to TL 63,275 was accounted under shareholders' equity (2017: TL 72,141).

As of 31 December 2018, if the real estates were accounted based on cost model instead of revaluation model, the net carrying value would be TL 112,258 (2017: TL 114,221).

**Level 3 fair value measurements**

The following table shows a reconciliation from the beginning balances to the ending balances for fair value measurements in Level 3 of the fair value hierarchy.

| | **Loans at fair value through profit or loss** | **Equity securities at FVOCI** | **Total** |
|---|---|---|---|
| Balance at 1 January 2018 | - | 5,057 | 5,057 |
| Transfers into Level 3(*) | 68,103 | - | 68,103 |
| **Balance at 31 December 2018** | **68,103** | **5,057** | **73,160** |

(*) Loans and receivables include the loan granted to the special purpose entity amounting to TL 68,103. The fair value of this loan is determined by the independent valuation company by considering different methodologies (discounted cash flows, peer market multipliers, similar transaction multipliers in the same sector etc.). Valuation techniques considered in the valuation work and any possible changes in the basic assumptions may affect the carrying value of the related asset. Accordingly, the loan is classified as Level 3.

| | **Loans at fair value through profit or loss** | **Available-for-sale equity securities** | **Total** |
|---|---|---|---|
| Balance at 1 January 2017 | - | 5,057 | 5,057 |
| Transfers into Level 3 | - | - | - |
| **Balance at 31 December 2017** | **-** | **5,057** | **5,057** |

## 26. Financial risk management (*continued)*

### (e) 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 the 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 context, appropriate monitoring methodology is developed for each control area that covers all operational risks and control frequencies are determined.

The data and amount of operational losses, the Bank exposed to during its activities is collected and analysed regularly by Risk Management Department and reported to Board of Directors, Auditing Committee and senior management.

The Group calculated the value at operational risk in accordance with the "Computation of Value of Operational Risk" of the circular "Regulation Regarding Measurement and Assessment of Capital Adequacy Ratios of Banks" published in the Official Gazette dated 1 November 2007, using gross profit of the last three years 2015, 2016 and 2017. Value at operational risk is amounting to TL 1,303,008 (31 December 2017: TL 1,161,604).

### (f) Capital management – regulatory capital

The BRSA sets and monitors capital requirements for the Bank as a whole. The parent company and individual banking operations are directly supervised by their local regulators. In implementing current capital requirements, the BRSA requires the banks to maintain a prescribed ratio of minimum 8% of total capital to total value at credit, market and operational risks. The Bank and its affiliates' consolidated regulatory capital is analysed into two tiers:

- Tier 1 capital, which includes paid-in capital, share premium, legal reserves, retained earnings, translation reserve and non-controlling interests after deductions for goodwill and certain cost items.
- Tier 2 capital, which includes qualifying subordinated liabilities, general provisions and the element of the fair value reserve relating to unrealised gain/(loss) on assets classified as financial assets at fair value through other comprehensive income.

Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures. The Bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Bank and its individually regulated operations have complied with externally imposed capital requirements throughout the year. There have been no material changes in the Bank's management of capital during the period.

## 26. Financial risk management *(continued)*

### (f) Capital management – regulatory capital *(continued)*

The capital adequacy ratio is calculated within the scope of the "Regulation on Measurement and Assessment of Capital Adequacy Ratios of Banks (the "Regulation")", "Regulation on Credit Risk Mitigation Techniques" and "Regulation on Calculation of Risk Weighted Amounts for Securitisations" published in the Official Gazette no.29511 dated 23 October 2015 and the "Regulation on Equities of Banks" published in the Official Gazette no.28756 dated 5 September 2013. In calculation of capital adequacy ratio, the data prepared from accounting records in compliance with the current legislation are used. Such accounting data is included in the calculation of credit and market risks subsequent to their designation as "trading book" and "banking book" according to the Regulation. The items classified as trading book and the items deducted from the equity are not included in the calculation of credit risk. In the calculation of risk weighted assets, the assets subject to amortisation or impairment, are taken into account on a net basis after being reduced by the related amortisations and provisions. In the calculation of the value at credit risk for the non-cash loans and commitments and the receivables from counterparties in such transactions are weighted after netting with specific provisions that are classified under liabilities and calculated based on the "Regulation on Identification of and Provision against Non-Performing Loans and Other Receivables". The net amounts are then multiplied by the rates stated in the Article 5 of the Regulation, reduced as per the "Regulation on Credit Risk Mitigation Techniques" and then included in the relevant exposure category defined in the article 6 of the Regulation and weighted as per Appendix-1 of the Regulation.

In the calculation of the value at credit risk for the derivative financial instruments and the credit derivatives classified in banking book, the receivables from counterparties are multiplied by the rates stated in the Appendix-2 of the Regulation, reduced as per the "Regulation on Credit Risk Mitigation Techniques" and then included in the relevant exposure category defined in the article 6 of the Regulation and weighted as per Appendix-1 of the Regulation.

As per the article 5 of the Regulation, the "counterparty credit risk" is calculated for repurchase transactions, securities and commodities borrowing agreements.

*(Amounts expressed in thousands of Turkish Lira ("TL") unless otherwise stated.)*

**26. Financial risk management** *(continued)*

**(f) Capital management – regulatory capital** *(continued)*

The Bank's and its subsidiaries' regulatory capital positions on a consolidated basis as of 31 December 2018 and 2017 are as follows:

| | **31 December 2018** | **31 December 2017** |
|---|---|---|
| Tier 1 capital | 2,410,638 | 2,104,785 |
| Tier 2 capital | 118,567 | 109,377 |
| Deductions from capital | (701) | (1,315) |
| **Total regulatory capital** | **2,528,504** | **2,212,847** |
| Risk-weighted assets | 15,696,636 | 15,448,185 |
| Value at market risk | 1,018,275 | 1,236,738 |
| Operational risk | 1,303,008 | 1,161,604 |
| Capital ratios | | |
| Total regulatory capital expressed as a percentage of total risk-weighted assets, value at market risk and operational risk | 16.11% | 14.32% |
| Total tier 1 capital expressed as a percentage of risk-weighted assets, value at market risk and operational risk | 15.36% | 13.62% |

**27. Events after the reporting period**

The Bomonti branch of the Parent Bank commenced its operations on 2 May 2019.

As of 23 May 2019, the Parent Bank applied to the Capital Markets Board with the decision of the Board of Directors dated 4 February 2019 and numbered 2019/24 for the issuance of debt instruments up to TL 600,000 for domestic sale in accordance with the capital market legislation.