Yapı ve Kredi Bankası A.Ş.

Consolidated financial statements at December 31, 2017 together with independent auditor's report

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of Yapı ve Kredi Bankası A.Ş.

Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Yapı ve Kredi Bankası A.Ş. (the "Bank") and its subsidiaries (together the "Group") as at 31 December 2017, and their consolidated financial performance and their consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

What we have audited

The Group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2017;
- the consolidated statement of income for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in shareholder's equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing ("ISA"). 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 believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("IESBA Code") and "Independence Audit by-Law" published by the Public Oversight Accounting and Auditing Standards Authority ("POA"), independent auditing requirements referred to in Article 400 of the Turkish Commercial Code ("TCC"), "Regulation on Independent Audit of Banks" published by the Turkish Banking Regulation and Supervision Agency on the Official Gazette No.29314 dated 2 April 2015 and Communiqué Series: X No: 22 on "Principles Regarding Independent Auditing Standards in the Capital Markets" (collectively referred to as "Turkish Local Independence Rules"). We have fulfilled our other ethical responsibilities in accordance with these requirements.

Our audit approach

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the financial services industry in which the Group operates.

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.

Key audit matter	*How our audit addressed the key audit matter*
Impairment of loans and receivables The Group has net loans and receivables of TL 215,105,383 thousand which represents a significant portion of the Group's total assets in its consolidated financial statements as at 31 December 2017. We focused on this area due to the size of the loans and receivables, level of management's judgement and estimations in determining timing of recognition of impairment and the estimation of the size of any such impairment. Explanations and notes related to the provision for impairment of loans and receivables are presented in Note 9 in the consolidated financial statements.	During our audit we performed the following procedures to support our conclusions: • We assessed and tested the design and operating effectiveness of the relevant controls over the monitoring and identification, which loans and receivables are impaired and the calculation of impairment provisions. • We have carried out a loan review on a selected sample of loans and receivables with the objective of identifying whether the loss event had occurred and whether the provision for impairment was recognized in a timely manner. • We tested individually impaired loans on a sampling basis and checked management's calculations by testing the forecasts of future cash flows, and we assessed the reasonableness of the assumptions and compared estimates to external evidence where available. • Where impairment was calculated on a modelled basis for collectively assessed portfolios, we understood and assessed appropriateness of the methodology and models used to calculate the provision including any changes in parameters and assumptions used in the models. Based on the evidence obtained we concluded that identification of impairment events, the principal assumptions used and the impairment provisions are reasonable.

Key audit matter	*How our audit addressed the key audit matter*
Valuation of pension obligations The Group has booked provision amounting to TL 690,852 thousand for pension fund obligations in the accompanying consolidated financial statements as at 31 December 2017. Explanations on the valuation of pension fund obligations are presented in Note 24 in the consolidated financial statements. Employees of the Bank are members of Yapı ve Kredi Bankası Anonim Şirketi Mensupları Yardım ve Emekli Sandığı (the "Pension Fund") which was established under the Provisional Article 20 of Social Insurance Law No: 506. As disclosed in Note 2.U.(i) "Pension benefits transferable to Social Security Institution ("SSI")", members of the Pension Fund are to be transferred to the Social Security Institution ("SSI"). Following the transfer, the social rights and payments defined in the pension agreement, which will not be covered by SSI, will be covered by the institutions that employ the fund's members. The Council of Ministers is authorized to determine the transfer date. The total obligation of the fund is estimated using separate methods and assumptions for transferrable and non-transferrable benefits. The valuations of the pension obligations requires significant judgement and technical expertise in choosing appropriate assumptions and estimates, such as transferrable social benefits, discount rates, salary increases, and economic and demographic expectations. The Bank's management uses external actuaries for the valuation of the pension fund obligations. During our audit, the above mentioned main assumption and estimates used in calculations of pension fund obligations, the uncertainty of the transfer date, the technical interest rate determined by the law and the significant impact on the Pension Fund's obligation due to the differentiation of these assumptions were taken into consideration, and this area is considered as a key audit matter.	During our audit we performed the following procedures to support our conclusions: • We tested on a sampling basis the accuracy of the employee data supplied by the Bank's management to the external actuarial firm for the purpose of the valuation of the Pension Fund's obligation. In addition, we verified the existence and fair values of the Pension Fund's assets. • We examined whether there are any significant changes in actuarial assumptions used in the calculation, employee benefits provided during the period, plan assets and liabilities and regulations related to valuations and tested significant changes, if any. • We engaged with our actuarial specialists to understand the judgements made in determining key economic assumptions used in the calculation of the liability and we assessed the reasonableness of those assumptions by comparing them to our own independently determined benchmarks and examined whether there were any significant changes in actuarial assumptions used in the calculation. Based on the evidence obtained, we found that the data and assumptions used by management in the actuarial valuations and the fair value of the plan assets are within a range we consider to be reasonable.

Key audit matter	How our audit addressed the key audit matter
Estimated impact of first time application of IFRS 9 The impact of the first application of IFRS 9 on 1 January 2018 equity is presented in Note 2 (A) in the consolidated financial statements. The implementation of IFRS 9 "Financial Instruments" effective from 1 January 2018 introduces significant changes in the classification and measurement as well as the impairment of financial assets. Management assessed the business model to determine whether its financial assets are held to collect, held to collect and sell or other. For the financial assets in every business model, management has performed sample based assessment for each type of product to conclude whether the cash flows from financial instruments fulfil the solely of payment of principal of interest criteria ('SPPI'). The Group has developed new IFRS 9 impairment models for determining the 12-month expected loss (stage 1), the lifetime expected loss (stage 2) and the lifetime expected loss for defaulted financial assets (stage 3), which requires judgements and estimations with regards to • the complexity of the impairment models • the impairment methodology in calculation of expected credit loss • the criteria for determining the stages (1, 2 or 3) for calculating the expected credit losses, and • data quality regarding data fields which has not been part of the financial reporting process before. As this is a major change in the accounting framework of the Group, we considered this estimate as key audit matter.	During our audit we performed the following procedures: • We reviewed of the Bank's documentation regarding the accounting policy choices to determine whether these are in accordance with the requirements of IFRS 9. • We challenged management on their accounting policy choices and judgments and they provided us with reasonable explanations together with evidence supporting their judgments. • With regards to the classification and measurement requirements of IFRS 9 our audit work consisted of the review of the accounting principles defined by the Group; substantive tests on samples of representative contracts; and the assessment of the documentation of the business models. • During our audit work on impairment requirements, we assessed the impairment methodology for compliance with IFRS 9 with the involvement of our internal specialists. We reviewed the operational implementation of the impairment methodologies in the information system and tested data quality checks and IT General Controls for the IFRS 9 impairment calculation tool. Furthermore we tested on a sampling basis, the data used as inputs for impairment calculations. On the basis of the work we carried out, we conclude that, given the inherent estimation uncertainty involved in determining the impact of IFRS 9 on the equity at 1 January 2018, the estimated impact as disclosed in the consolidated financial statements is reasonable.

Other matter

The consolidated financial statements of the Bank and its subsidiaries as at 31 December 2016 were audited by another auditor whose report dated 7 March 2017 expressed an unqualified opinion.

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 ISA 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 ISA, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

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

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

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current 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.

PwC Bağımsız Denetim ve
Serbest Muhasebeci Mali Müşavirlik A.Ş.

Halûk Yalçın, SMMM
Partner

Istanbul, 2 March 2018

Yapı ve Kredi Bankası A.Ş.

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Consolidated statement of financial position as at December 31, 2017
(Amounts expressed in thousands of TL unless otherwise indicated.)

	Note	December 31, 2017	December 31, 2016
Assets			
Cash and balances with central banks	5	42,451,970	33,083,295
Loans and advances to banks	6	5,654,217	3,449,218
Financial assets held for trading			
- Trading securities	7	102,587	43,365
- Derivative financial instruments	7-8	4,109,547	2,986,773
Loans and advances to customers	9	215,105,383	188,980,851
Hedging derivatives	8	1,756,611	1,209,712
Investment securities			
- Available-for-sale	10	12,824,820	12,948,479
- Available-for-sale pledged as collateral	10-35	11,491,326	5,268,827
- Held-to-maturity	10	2,460,983	4,628,032
- Held-to-maturity pledged as collateral	10-35	11,736,083	6,960,858
Investment in associates and joint ventures accounted for using the equity method	11-12	790,411	682,728
Goodwill	13	1,023,528	1,023,528
Other intangible assets	14	702,859	587,422
Property and equipment	15	1,206,103	1,267,706
Deferred income tax assets	22	351,398	94,246
Other assets	16	5,769,821	5,317,893
Total assets		**317,537,647**	**268,532,933**
Liabilities			
Deposits from banks	17	18,676,359	13,811,243
Customer deposits	18	164,133,655	149,550,753
Funds borrowed	19	52,975,912	37,167,753
Debt securities in issue	20	24,452,247	19,308,899
Financial liabilities designated at fair value	21	4,363,503	3,938,694
Derivative financial instruments	8	3,820,705	2,578,679
Current income taxes payable		255,614	33,792
Deferred income tax liabilities	22	16,606	7,892
Hedging derivatives	8	312,778	89,296
Other provisions	23	1,231,170	765,014
Retirement benefit obligations	24	1,091,399	697,516
Other liabilities	25	15,411,523	13,663,912
Total liabilities		**286,741,471**	**241,613,443**
Equity			
Share capital and share premium	27	4,822,259	4,822,259
Other reserves	28	1,672,139	1,195,533
Retained earnings	28	24,301,236	20,901,197
Equity attributable to equity holders of the parent		**30,795,634**	**26,918,989**
Equity attributable to non-controlling interests		542	501
Total equity		**30,796,176**	**26,919,490**
Total liabilities and equity		**317,537,647**	**268,532,933**

The accompanying notes set out on pages 6 to 89 form an integral part of these consolidated financial statements.

Yapı ve Kredi Bankası A.Ş.

Consolidated statement of income for the year ended December 31, 2017
(Amounts expressed in thousands of TL unless otherwise indicated.)

	Note	December 31, 2017	December 31, 2016
Continuing operations			
Interest income	29	24,651,289	19,751,183
Interest expense	29	(15,781,209)	(11,732,216)
Net interest income		**8,870,080**	**8,018,967**
Fee and commission income	30	4,230,804	3,706,435
Fee and commission expense	30	(1,521,262)	(1,309,008)
Net fee and commission income		**2,709,542**	**2,397,427**
Foreign exchange gains, net		152,757	119,905
Net trading, hedging and fair value income	31	18,057	350,457
Gains from investment securities, net		53,274	40,488
Other operating income		125,645	120,506
Operating income		**11,929,355**	**11,047,750**
Impairment losses on loans, investment securities and credit related commitments, net	33	(2,274,076)	(2,362,567)
Provision for retirement benefit obligations, net	24	(176,764)	(24,514)
Other provisions	23	(430,198)	(127,668)
Other operating expenses	32	(4,871,670)	(4,588,092)
Operating profit		**4,176,647**	**3,944,909**
Share of profit/(loss) of associates and joint ventures accounted for using the equity method	11-12	87,612	85,362
Profit before income tax		**4,264,259**	**4,030,271**
Income tax expense	22	(839,270)	(781,936)
Profit for the year		**3,424,989**	**3,248,335**
Attributable to:			
Equity holders of the parent		3,424,910	3,248,269
Non-controlling interest		79	66
		3,424,989	**3,248,335**
Basic and diluted earnings per share attributable to the equity holders of the Parent (expressed in TL per thousand share)	34	7.88	7.47

The accompanying notes set out on pages 6 to 89 form an integral part of these consolidated financial statements.

Yapı ve Kredi Bankası A.Ş.

Consolidated statement of comprehensive income for the year ended December 31, 2017

(Amounts expressed in thousands of TL unless otherwise indicated.)

	Note	December 31, 2017	December 31, 2016
Profit for the year		**3,424,989**	**3,248,335**
Items that are or may be reclassified to profit or loss			
Exchange differences on translation of foreign operations		372,042	326,535
Net gains / (losses) on available-for-sale financial assets			
- Unrealized net gains / (losses) arising during the year, before tax		117,367	42,051
- Net amount reclassified to the statement of income		(39,180)	(236,391)
Net investment hedges			
- Net gains / (losses) arising on hedges recognized in other comprehensive income, before tax	8	(321,859)	(201,497)
Cash flow hedges			
- Net gains / (losses) arising on hedges recognized in other comprehensive income, before tax		871,530	94,574
- Net amount reclassified to the statement of income	8	(272,787)	44,407
Income tax effect	22	**(72,750)**	**28,381**
		654,363	**98,060**
Items that will never be reclassified to profit or loss			
Re-measurement (losses) / gains on defined benefit liability	24	(259,779)	2,120
Income tax effect	22	57,151	(375)
		(202,628)	**1,745**
Other comprehensive income for the year, net of tax		**451,735**	**99,805**
Total comprehensive income for the year		**3,876,724**	**3,348,140**
Total comprehensive income attributable to:			
Equity holders of the parent (total)		3,876,645	3,348,074
Non-controlling interest (total)		79	66

The accompanying notes set out on pages 6 to 89 form an integral part of these consolidated financial statements.

Yapı ve Kredi Bankası A.Ş.

Consolidated statement of changes in equity for the year ended December 31, 2017
(Amounts expressed in thousands of TL unless otherwise indicated.)

		Attributable to equity holders of the parent						
	Note	Share capital	Share premium	Other reserves (Note 28)	Retained earnings (Note 28)	Total	Non-controlling interest	Total equity
Balance at January 1, 2016		**4,286,580**	**535,679**	**999,508**	**17,749,148**	**23,570,915**	**470**	**23,571,385**
Total comprehensive income for the year		-	-	99,805	3,248,269	3,348,074	66	3,348,140
Dividends paid		-	-	-	-	-	(35)	(35)
Transfer to statutory reserves and to retained earnings	28	-	-	96,220	(96,220)	-	-	-
Balance at December 31, 2016		**4,286,580**	**535,679**	**1,195,533**	**20,901,197**	**26,918,989**	**501**	**26,919,490**
Total comprehensive income for the year				**451,735**	**3,424,910**	**3,876,645**	**79**	**3,876,724**
Dividends paid		-	-	-	-	-	(38)	(38)
Transfer to statutory reserves and to retained earnings	28	-	-	24,871	(24,871)	-	-	-
Balance at December 31, 2017		**4,286,580**	**535,679**	**1,672,139**	**24,301,236**	**30,795,634**	**542**	**30,796,176**

The accompanying notes set out on pages 6 to 89 form an integral part of these consolidated financial statements.

Consolidated statement of cash flows for the year ended December 31, 2017

(Amounts expressed in thousands of TL unless otherwise indicated.)

	Note	December 31, 2017	December 31, 2016
Cash flows from operating activities			
Net profit		3,424,989	3,248,335
Adjustments for:			
Unrealized (gain) / loss on financial assets held for trading, net		(292)	283
Allowances for losses on loans, investment securities and credit related commitments	33	2,274,076	2,362,567
Measurement of derivative financial instruments at fair value	8	(204,164)	(961,486)
Share of profit of associates and joint ventures	11-12	(87,612)	(85,362)
Amortization of other intangible assets	32	136,120	124,721
Depreciation of property and equipment	32	204,228	208,820
Reversal of impairment for property and equipment	15	-	(716)
Provision for current and deferred income taxes	22	839,270	781,936
Other provisions	23	430,198	127,668
Provision / (reversal) for retirement benefit obligations	24	176,764	24,514
Other liabilities		30,803	150,859
Unearned commission income	25	7,514	29,543
Dividend income		(10,725)	(6,173)
Interest income, net	29	(8,870,080)	(8,018,967)
Interest paid		(9,125,413)	(11,470,082)
Interest received		22,121,115	18,462,374
Effect of exchange rates on financing activities		5,714,743	4,994,209
Others, net		1,172,622	(1,325,769)
Cash flows from operating profits before changes in operating assets and liabilities		**18,234,156**	**8,647,274**
Changes in operating assets and liabilities:			
Net decrease / (increase) in cash balances with central banks		(3,765,796)	303,681
Net decrease / (increase) in loans and advances to banks		122,324	(160,761)
Net decrease / (increase) in trading securities		(58,930)	30,591
Net decrease / (increase) in loans and advances to customers		(27,436,868)	(27,845,470)
Net (increase) / decrease in other assets		(533,354)	(1,520,682)
Net increase / (decrease) in deposits from banks		4,858,295	(1,586,105)
Net (decrease) / increase in customer deposits		14,586,925	24,287,842
Net increase / (decrease) in other liabilities and provisions		2,354,475	1,153,655
Income taxes paid		(879,020)	(820,041)
Net cash from / (used in) operating activities		**7,482,207**	**2,489,984**
Cash flows from investing activities			
(Purchase of) property and equipment	15	(152,855)	(215,561)
Net book value of property and equipment disposed		29,749	94,580
(Purchase of) intangible assets, net	14	(259,738)	(179,700)
(Purchase of) held-to-maturity securities	10	(3,231,152)	(1,703,125)
Redemption or sale of held-to-maturity securities	10	1,381,405	283,389
(Purchase of) available-for-sale securities	10	(17,733,200)	(14,426,408)
Sale or redemption of available-for-sale securities	10	11,581,249	16,765,939
Disposal of a subsidiary		215,307	-
Dividends received		10,725	6,173
Net (used in) investing activities		**(8,158,510)**	**625,287**
Cash flows from financing activities			
(Repayments of) borrowed funds and debt securities		(16,238,933)	(9,141,606)
Proceeds from borrowed funds and debt securities		23,390,945	10,594,690
Dividend paid		(38)	(37)
Net cash from / (used in) financing activities		**7,151,974**	**1,453,047**
Net increase / (decrease) in cash and cash equivalents		**6,475,671**	**4,568,318**
Effects of foreign exchange rate changes on cash and cash equivalents		1,585,494	1,357,079
Cash and cash equivalents at beginning of year	5	16,161,962	10,236,565
Cash and cash equivalents at end of year	**5**	**24,223,127**	**16,161,962**

The accompanying notes set out on pages 6 to 89 form an integral part of these consolidated financial statements.

1. General information

Yapı ve Kredi Bankası A.Ş. ("YKB", the "Parent Bank" or the "Bank" or together with its subsidiaries it is referred to as "the Group" in these consolidated financial statements) was established with the permission of the Council of Ministers of the Republic of Turkey No. 3/6710 on September 9, 1944 as a private capital commercial bank, authorized to perform all banking, economic, financial and commercial activities which are allowed by Turkish laws. The statute of the Bank has not changed since its incorporation. The Group provides retail, corporate and private banking, credit cards, leasing, factoring and investment management services. The Group has operations in Turkey, the Netherlands, Azerbaijan, Russia and Malta.

The Group's controlling parent with 81.80% of shareholding is Koç Finansal Hizmetler A.Ş. ("KFS"), a joint venture of UniCredit Group ("UCG") and Koç Group. KFS was established as a financial holding company on March 16, 2001 to combine Koç Group financial services companies under one organization. As of October 22, 2002, Koç Group established a strategic partnership with UCG over KFS.

The Bank's shares have been traded on the Istanbul Stock Exchange ("ISE") since 1987. As of December 31, 2017, 18.20% of the shares of the Bank are publicly traded (2016 – 18.20%). The Bank's publicly traded shares are traded on ISE and the representatives of these shares. Global Depository Receipts are quoted on the London Stock Exchange.

At December 31, 2017, the Group has 18,839 employees (2016 - 19,419 employees). The Bank has 865 branches operating in Turkey and 1 branch in overseas (2016 – 935 branches operating in Turkey, 1 branch in overseas) and 17,944 employees (2016 - 18,366 employees).

The Bank is registered in Istanbul, Turkey at the following address: Yapı Kredi Plaza D Blok, Levent 34330, İstanbul, Turkey.

These consolidated financial statements for the year ended December 31, 2017 have been approved for issue by the Board of Directors on March 2, 2018.

2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

A. Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis; except for available-for-sale investments, derivative financial instruments, other financial assets held for trading, financial assets designated as hedged items in qualifying fair value hedge relationships, art objects and paintings in property and equipment which are revalued and financial liabilities designated at fair value which have all been measured at fair value.

The carrying values of recognized assets that are hedged items in fair value hedges, and otherwise carried at amortized cost, are adjusted to record changes in fair value attributable to the risks that are being hedged.

2. Summary of significant accounting policies (continued)

Statement of compliance

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

The Bank maintains its books of accounts and prepares its statutory financial statements in Turkish Lira in accordance with the Banking Act No. 5411 ("Banking Act"), which is effective from November 1, 2005, the Turkish Commercial Code ("TCC"), the Turkish Tax Legislation, the "Regulation on the Principles and Procedures Regarding Banks' Accounting Applications and Safeguarding of Documents" published in the Official Gazette No. 26333 dated November 1, 2006 by the Banking Regulation and Supervision Agency ("BRSA") which refers to "Turkish Accounting Standards" ("TAS") and "Turkish Financial Reporting Standards ("TFRS") issued by the Public Oversight Accounting and Auditing Standards Authority ("POA") and other decrees, notes and explanations related to the accounting and financial reporting principles (all "Turkish Accounting Standards" or "TAS") published by the BRSA. The subsidiaries maintain their books of accounts based on statutory rules and regulations applicable in their jurisdiction. Consolidated financial statements are derived from statutory financial statements with adjustments and reclassifications for the purpose of fair presentation in accordance with IFRS.

Presentation of financial statements

The Group presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the statement of financial position date (current) and more than 12 months after the statement of financial position date (non-current) is presented in Note 4.

Changes in accounting policies and disclosures

The accounting policies adopted in the preparation of the consolidated financial statements as at December 31, 2017 are consistent with those followed in the preparation of the consolidated financial statements of the prior year, except for the adoption of new standards and amendments to standards, including any consequential amendments to other standards summarized below. The effects of these standards and related amendments on the Group's financial position and performance have been disclosed in the related notes.

Standards issued but not yet effective and not early adopted

A number of new standards and amendments to standards are effective for annual periods beginning after January 1, 2018; however, the Group has not applied the following new or amended standards in preparing these consolidated financial statements.

IFRS 9, 'Financial instruments'; will replace IAS 39 Financial Instruments: recognition and measurement, related to the classification and measurement of financial instruments. The new requirements become effective as of January 1, 2018.

IFRS 9 standard sets out the new principles for the classification and measurement of financial instruments, for impairment for credit risk on financial assets and for general hedge accounting. Based on the analysis carried out, it is considered that all requirements of IAS 39 will be maintained for hedge accounting

IFRS 9 will require financial assets to be classified on the basis of two criteria; classification and measurement of financial assets will depend on the business model within which financial assets are managed and their contractual cash flow characteristics whether the cash flows represent "solely payments of principal and interest (SPPI)".

2. Summary of significant accounting policies (continued)

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

The new principles of IFRS 9 for the classification and measurement of financial instruments will not have a material impact on the financials of the Group.

IFRS 9 will introduce a new accounting model for impairment, based on (i) expected losses approach substituting the current approach based on the incurred losses, and (ii) will introduce the concept of "lifetime" expected losses, and consequently an anticipation and a structural increase of the provisioning with particular reference to credit losses. The ECL estimates are required to be unbiased, probability-weighted, and should include supportable information about past events, current conditions, and forecasts of future economic conditions. The ECL should reflect multiple macroeconomic scenarios and include the time value of money. The ECL model applies to all on-balance financial assets accounted for at amortized cost and FVOCI such as loans and debt securities, as well as off-balance items such as certain loan commitments, financial guarantees, and undrawn revolving credit facilities.

These financial assets will be divided into three categories depending on the gradual increase in credit risk observed since their initial recognition. Impairment shall be recognized on outstanding amounts in each category, as follows:

Stage 1:

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

Stage 2:

In the event of a significant increase in credit risk since initial recognition, the financial asset will be transferred to this category. Impairment for credit risk will be determined on the basis of the instrument's lifetime expected credit losses.

Stage 3

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

The Group will recognize an adjustment to opening equity balance for the new requirements as of January 1, 2018 without making any adjustments to the comparative periods. As a result of the related adjustment, net of tax, the negative impact is calculated as approximately TL 2.4 billion.

IFRS 15, 'Revenue from contracts with customers'; effective from annual periods beginning on or after January 1, 2018. IFRS 15, 'Revenue from contracts with customers' is a converged standard from the IASB and FASB on revenue recognition. The standard will improve the financial reporting of revenue and improve comparability of the top line in financial statements globally.

Amendment to IFRS 15, 'Revenue from contracts with customers', effective from annual periods beginning on or after January 1, 2018. These amendments comprise clarifications of the guidance on identifying performance obligations, accounting for licences of intellectual property and the principal versus agent assessment (gross versus net revenue presentation). New and amended illustrative examples have been added for each of those areas of guidance. The IASB has also included additional practical expedients related to transition to the new revenue standard.

2. Summary of significant accounting policies (continued)

IFRS 16, 'Leases'; effective from annual periods beginning on or after 1 January 2019, this standard replaces the current guidance in IAS 17 and is a farreaching change in accounting by lessees in particular. Under IAS 17, lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a 'right of use asset' for virtually all lease contracts. The IASB has included an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees. For lessors, the accounting stays almost the same. However, as the IASB has updated the guidance on the definition of a lease (as well as the guidance on the combination and separation of contracts), lessors will also be affected by the new standard. At the very least, the new accounting model for lessees is expected to impact negotiations between lessors and lessees. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

B. Consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries for the year ended December 31, 2017. The financial statements of the Bank's subsidiaries (including the structured entity that the Bank consolidates) are prepared for the same reporting period as the Bank, using consistent accounting policies.

(a) Subsidiaries

Subsidiaries including the structured entity 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 that control commences until the date that control ceases.

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

Non-controlling interests are measured at their proportionate share of the acquiree's identifiable net assets at the acquisition date.

Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

Intra-group balances, and any unrealised income and expenses arising from intra-group transactions, are eliminated in the preparation of 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.

(Amounts expressed in thousands of TL unless otherwise indicated.)

2. Summary of significant accounting policies (continued)

The Group does not have significant restrictions on its ability to access or use its assets and settle its liabilities other than those resulting from the supervisory frameworks within which banking subsidiaries operate. The supervisory frameworks require banking subsidiaries to keep certain levels of regulatory capital and liquid assets, limit their exposure to other parts of the Group and comply with other ratios. The carrying amount of banking subsidiaries' assets and liabilities are TL 10,292,450 and TL 8,257,598 respectively (2016: TL 9,226,298 and TL 7,482,421 respectively) before intra-group eliminations.

The list of principal subsidiaries at December 31, 2017 is as follows:

Name of subsidiary	Country of incorporation	Nature of business
Yapı Kredi Finansal Kiralama A.O.	Turkey	Leasing
Yapı Kredi Faktoring A.Ş.	Turkey	Factoring
Yapı Kredi Portföy Yönetimi A.Ş.	Turkey	Portfolio management
Yapı Kredi Yatırım Menkul Değerler A.Ş.	Turkey	Investment management
Yapı Kredi Bank Nederland N.V.	Netherlands	Banking
Stiching Custody Services YKB	Netherlands	Custody services
Yapı Kredi Holding B.V.	Netherlands	Financial holding
Yapı Kredi Azerbaijan	Azerbaijan	Banking
Yapı Kredi Malta	Malta	Banking
Enternasyonel Turizm Yatırım A.Ş. ("Enternasyonel")	Turkey	Investment
Agro-san Kimya Sanayi ve Ticaret A.Ş. ("Agro-San")	Turkey	Agricultural chemicals
Yapı Kredi Kültür Sanat Yayıncılık Tic. ve San. A.Ş.	Turkey	Culture / art publications
Yapı Kredi Diversified Payment Rights Finance Co.	Cayman Islands	Structured entity ("SE")
Yapı Kredi Teknoloji A.Ş.	Turkey	IT Development

	2017		2016	
Name of subsidiary	Control rates (%)	Effective rates (%)	Control rates (%)	Effective rates (%)
Yapı Kredi Finansal Kiralama A.O.	99.99	99.99	99.99	99.99
Yapı Kredi Faktoring A.Ş.	99.96	99.96	99.96	99.96
Yapı Kredi Portföy Yönetimi A.Ş.	99.97	99.95	99.97	99.95
Yapı Kredi Yatırım Menkul Değerler A.Ş.	99.98	99.98	99.98	99.98
Yapı Kredi Bank Nederland N.V.	100.00	100.00	100.00	100.00
Stiching Custody Services YKB	100.00	100.00	100.00	100.00
Yapı Kredi Bank Moscow(1)	-	-	100.00	100.00
Yapı Kredi Holding B.V.	100.00	100.00	100.00	100.00
Yapı Kredi Azerbaijan	100.00	100.00	100.00	100.00
Yapı Kredi Invest LLC(2)	-	-	100.00	100.00
Yapı Kredi Malta	100.00	100.00	-	-
Enternasyonel	99.99	99.96	99.99	99.96
Agro-san	100.00	99.99	100.00	99.99
Yapı Kredi Kültür Sanat Yayıncılık Tic. ve San. A.Ş.	100.00	99.99	100.00	99.99
Yapı Kredi Diversified Payment Rights Finance Co.(3)	-	-	-	-
Yapı Kredi Teknoloji A.Ş.	100.00	100.00	-	-

(1) It is resolved on October 25, 2017 by the Bank's Board of Directors to sell our Group's 100% shares in Yapı Kredi Bank Moscow with Russian Rouble 478,272,000 nominal value to Expobank LLC in Russia for Russian Rouble 3,300,000,000 and to sign the Share Purchase Agreement with Expobank LLC regarding this issue

(2) Yapı Kredi Invest LLC, which is owned by Yapı Kredi Azerbaijan, a subsidiary of the Parent Bank, was liquidated on December 21, 2017

(3) Yapı Kredi Diversified Payment Rights Finance Company is a structured entity established for YKB's securitization transactions as explained in Note 20. It is included in the consolidation although YKB or any of its affiliates does not have any shareholding interest in this company.

(b) Associates

Associates are all entities over which the Group has significant influence but not control. An investment in associates is accounted for using the equity method of accounting and is initially recognized at cost. The Group's investment in associate includes goodwill (net of any accumulated impairment loss) identified on acquisition.

(Amounts expressed in thousands of TL unless otherwise indicated.)

2. Summary of significant accounting policies (continued)

The Group's share of its associates' post-acquisition profits or losses is recognized in the statement of income, and its share of post-acquisition movements in reserves is recognized in the Group's equity. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealized gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies for associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

The details of the associates at December 31, 2017 and 2016 are as follows:

					2017		2016
Name of associate	**Country of incorporation**	**Nature of business**	**Original currency**	**Control rate (%)**	**Effective rate (%)**	**Control rate (%)**	**Effective rate (%)**
Banque de Commerce et de Placements ("Banque de Commerce")	Switzerland	Banking	CHF	30.67	30.67	30.67	30.67
Allianz Yaşam ve Emeklilik A.Ş.	Turkey	Life insurance	TL	20.00	20.00	20.00	20.00

(c) Joint ventures

The joint venture is an entity in whose capital the Group participates and has joint control. The joint venture is a real estate investment trust ("REIT") and operates according to special legislation with permission and license, is established in Turkey and the related joint venture is accounted for using the equity method.

The Group's share of its joint ventures' post-acquisition profits or losses is recognized in the statement of income, and its share of post-acquisition movements in reserves is recognized in the Group's equity. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in a jointly controlled entity equals or exceeds its interest in the joint venture, including any other unsecured receivables, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the joint venture.

Unrealized gains on transactions between the Group and its joint venture are eliminated to the extent of the Group's interest in the joint venture. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of joint venture have been changed where necessary to ensure consistency with the policies adopted by the Group.

The details of the joint venture at December 31, 2017 and 2016 are as follows:

					2017		2016
Name of joint venture	**Country of incorporation**	**Nature of business**	**Original currency**	**Control rate (%)**	**Effective rate (%)**	**Control rate (%)**	**Effective rate (%)**
Yapı Kredi Koray Gayrimenkul Yatırım Ortaklığı A.Ş.	Turkey	REIT	TL	30.45	30.45	30.45	30.45

(d) Fund management

The Group manages and administers open-ended mutual funds. Determining whether the Group controls such a fund usually focuses on the assessment of the aggregate economic interests of the Group in the fund (comprising any carried interests and expected management fees) and the investors' rights to remove the fund manager. As a result, after evaluating the aggregate economic interests in funds and the rights to remove the fund manager, the Group has concluded that it acts as agent for the investors in all cases, and therefore has not consolidated these funds. Information about the Group's fund management is set out in Note 39.

2. Summary of significant accounting policies (continued)

C. Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency").

The consolidated financial statements are presented in TL, which is the Bank's functional and the Group's presentation currency, and all values are rounded to the nearest thousands, except when otherwise indicated.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement, except when deferred in equity as qualifying cash flow and net investment hedges.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

(c) Group companies

The results and financial position of all the group entities that have a functional currency different from the presentation currency (none of which has the currency of a hyperinflationary economy) are translated into the presentation currency as follows:

(i) assets and liabilities for each statement of financial position presented are translated at the exchange rate prevailing at the date of that statement of financial position,

(ii) income and expenses for each statement of income are translated at average exchange rates.

Exchange differences resulting from the different rates applied for the translation of the statement of financial position and the statement of income as well as differences arising from the translation of the portion of the net asset value in foreign entities pertaining to the Group are recognized as "currency translation differences / translation reserves" included in other reserves in equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings designated as hedges of such investments, are presented in equity.

When a foreign operation is sold, such exchange differences are recognized in the income statement as part of the gain or loss on the sale.

2. Summary of significant accounting policies (continued)

D. Related parties

For the purpose of these consolidated financial statements, shareholders, companies controlled by or affiliated with them and other companies within the Koç Group and the UniCredit Group as well as key management personnel are considered and referred to as related parties (Note 38).

E. Due from other banks

Amounts due from other banks are recorded when the Group advances money to counterparty banks with no intention of trading the resulting unquoted non-derivative receivable due on fixed or determinable dates. Amounts due from other banks are carried at amortized cost.

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

This category has two sub-categories: financial assets held for trading and those designated at fair value through profit or loss at inception. Financial assets and financial liabilities are designated at fair value through profit or loss when doing so significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments such as loans and advances to customers or banks and debt securities in issue were carried at amortized cost.

Gains and losses arising from changes in the fair value of derivatives that are managed in conjunction with designated financial assets or financial liabilities are included in ‘net trading, hedging and fair value income and loss.

A financial asset is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives are also categorized as held for trading unless they are designated as hedging instruments.

Financial assets or liabilities at fair value through profit or loss are initially recognized and subsequently re-measured at fair value. All related realized and unrealized fair value gains and losses are included in net trading income. Interest earned or paid whilst holding financial assets or liabilities at fair value through profit or loss is reported as interest income or expense.

All purchases and sales of trading assets that require delivery within the time frame established by regulation or market convention (“regular way” purchases and sales) are recognized at the settlement date, which is the date that the asset is delivered to/by the Group. Any change in fair value of the trading assets to be received during the period between the trade date and the settlement date is recognized in profit or loss.

2. Summary of significant accounting policies (continued)

G. Investment securities

Investment securities are classified into the following two categories: held-to-maturity and available-for-sale assets. Investment securities with fixed maturity, where management has both the intent and the ability to hold to maturity are classified as held-to-maturity. Investment securities intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices, or client's servicing activity are classified as available-for-sale. Management determines the appropriate classification of its investments at the time of the purchase.

Investment securities are initially recognized at fair value which is the cash consideration including transaction costs. Available-for-sale financial assets are subsequently re-measured at fair value. Gains and losses arising from changes in the fair value of securities classified as available-for sale are recognized as other comprehensive income in "revaluation reserve - available-for-sale investments" included in other reserves, until the financial asset is derecognized or impaired at which time the cumulative gain or loss previously recognized in equity is transferred to the income statement.

Held-to-maturity investments are carried at amortized cost using the effective interest method, less any provision for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate.

There are no financial assets that were previously classified as held-to-maturity but cannot be subject to this classification for two years due to a breach of classification principles. In accordance with IAS 39, the sale or reclassification to available-for-sale portfolio of insignificant amount of financial assets, sale or reclassification to available for sale portfolio of financial assets which are close to maturity, or sale or reclassification to available for sale portfolio of assets as a result of significant increase in the risk weights of held to maturity investments used for regulatory risk-based capital purposes will not result in tainting.

Equity securities classified as available-for-sale are carried at fair values except equity securities whose fair value can not be reliably measured, which are measured at cost after deduction for any impairment (Note 10).

Interest earned whilst holding investment securities is reported as interest income. Dividends earned whilst holding available-for-sale financial investments are recognized in the statement of income when the right of the payment has been established.

All purchases and sales of investment securities are recognized at the settlement date, which is the date the asset is delivered to/by the Group. Any change in fair value of the available-for-sale securities to be received during the period between the trade date and the settlement date is recognized in other comprehensive income.

Unsettled transactions are recorded as off statement of financial position commitments until the settlement date.

H. Repurchase and reverse repurchase agreements

Securities sold subject to linked repurchase agreements ("repos") are not derecognized from the statement of financial position as the Group retains substantially all the risks and rewards of ownership. The corresponding cash received is recognized in the consolidated statement of financial position as an asset with a corresponding obligation to return it, including accrued interest as a liability within deposits from banks and customer deposits, reflecting the transaction's economic substance as a loan to the Group. The difference between the sale and repurchase price is treated as interest expense and amortized over the life of repo agreements using the effective interest method.

2. Summary of significant accounting policies (continued)

On the other hand securities purchased under agreements to resell ("reverse repo") are not recognized in the statement of financial position. The amount paid, including accrued interest, is recorded as loans and advances to banks in the statement of financial position. The difference between the purchase and resale prices is recorded in "interest income" and is accrued over the life of the agreement using the effective interest method.

I. Loans and advances to customers

Loans and advances to customers are recorded when the Group advances money to purchase or originate an unquoted non-derivative receivable from a customer due on fixed or determinable dates and has no intention of trading the receivable. Loans and advances to customers are carried at amortized cost, less allowance for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the effective interest rate. The losses arising from impairment are recognized in the income statement in "impairment losses on loans, investment securities and credit related commitments".

The Group holds appropriate collateral for each loan according to its specified risk and the relevant BRSA communiqués. The collateral strategy differentiates between collateral types on the basis of customers' ratings and loan terms. In general, the types of collaterals are cash collaterals, mortgages, guarantees, promissory notes, securities issued by the Turkish Treasury Undersecretariat and Central Bank and pledges on assets.

J. Impairment of financial assets

Financial assets carried at amortized cost

The Group assesses at each statement of financial position date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. Impairment losses are recognized in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of the financial asset and which have an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. If the Group determines that no objective evidence exists that impairment was incurred for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. The primary factors that the Group considers when a financial asset is impaired is its overdue status and realizability of related collateral, if any. The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss has occurred:

- any instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- the borrower experiences a significant financial difficulty as evidenced by borrower's financial information that the bank obtains;
- the borrower considers bankruptcy or a financial reorganization;
- there is adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impact the borrower.

The Group uses a set of obligatory and judgement-based triggers that can lead to a classification as impaired. The final decision on impaired classification is always subject to expert judgement. Obligatory triggers include bankruptcy, financial restructuring and 90 days' past due. Judgement-based triggers include elements such as (but are not limited to) negative equity, regular payment problems, improper use of credit lines, legal action by other creditors. These triggers are complementary to the judgement of an expert.

2. Summary of significant accounting policies (continued)

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

The Group adopted the Incurred But Not Reported ("IBNR") model for performing loans with intrinsic elements such as loss detection period ("LDP") and expert views. IBNR impairments on loans represent the provisions that are provided for the transactions where loss events have already occurred, but have not been reported. In such cases provision is created in such proportion to the exposure that reflects the amount of losses that have been incurred as a result of the past but not reported events.

Impairment losses are always recognized through an allowance account to write down the asset's carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the original effective interest rate of the asset. If the loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account through profit or loss.

Uncollectible assets are written-off against the related impairment loss provision after all the necessary procedures to recover the asset have been completed and the amount of the loss has been determined.

Financial assets classified as available for sale

For available-for-sale financial investments, the Group assesses at each statement of financial position date whether there is objective evidence that an investment is impaired.

In the case of debt instruments classified as available-for-sale, the Bank assesses individually whether there is objective evidence of impairment based on the same criteria as financial assets carried at amortized cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortized cost and the current fair value, less any impairment loss on that investment previously recognized in the income statement. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of 'Interest income'. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to a credit event occurring after the impairment loss was recognized in the income statement, the impairment loss is reversed through the income statement.

2. Summary of significant accounting policies (continued)

In the case of equity investments classified as available-for-sale, objective evidence would also include a ‘significant’ or ‘prolonged’ decline in the fair value of the investment below its cost. Where there is evidence of impairment, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognized in the income statement - is removed from equity and recognized in the income statement. Impairment losses on equity investments are not reversed through the income statement; increases in the fair value after impairment are recognized directly in equity.

K. Derivative financial instruments

Derivatives are initially recognized at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. The fair values of derivative financial instruments that are quoted in active markets are determined from quoted market prices in active markets including recent market transactions. The fair values of financial derivatives that are not quoted in active markets are determined by using valuation techniques, including discounted cash flow models. Where valuation techniques (for example, models) are used to determine fair values, they are validated and periodically reviewed. Fair values of derivatives are carried as assets when positive and as liabilities when negative. The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received). Derivative financial instruments are classified as held for trading and hedging.

Certain derivative transactions, even though providing effective economic hedges under the Group risk management position, do not qualify for hedge accounting under the specific rules in IAS 39, and are therefore treated as derivatives held for trading with fair value gains and losses reported in the income statement.

Certain derivatives embedded in other financial instruments, such as credit linked notes (“CLN”), constant maturity swaps (“CMS”), are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit or loss. These embedded derivatives are separately accounted for at fair value, with changes in fair value recognized in the income statement unless the Group chooses to designate the hybrid contracts at fair value through profit or loss.

Embedded derivatives are separated from the host contract and accounted for as a derivative in accordance with IAS 39, if and only if:

- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract;

- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and

- the hybrid (combined) instrument is not measured at fair value with changes in fair value recognized in profit or loss (i.e. a derivative that is embedded in a financial asset or financial liability at fair value through profit or loss is not separated).

If an embedded derivative is separated, the host contract shall be accounted for under IAS 39 if it is a financial instrument and in accordance with other appropriate standards if it is not a financial instrument.

2. Summary of significant accounting policies (continued)

L. Hedge accounting

The Group makes use of derivative instruments to manage exposures to interest rate and foreign currency risks, including exposures arising from forecast transactions and firm commitments. In order to manage particular risks, the Group applies hedge accounting for transactions that meet the specified criteria. The Group documents at inception of the transaction the relationship between hedging instruments and hedged items, as well as their risk management objectives and the strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the instruments that are used in hedging transactions are highly effective in offsetting changes in values of hedged items.

Net investment hedge

The effective portion of the foreign exchange differences of borrowings that are designated and qualify as net investment hedges are recognized in equity. The gain or loss relating to the ineffective portion is recognized immediately in the income statement. Gains and losses accumulated in equity are included in the income statement when the foreign operation is disposed of.

Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. Effective changes in fair value of interest rate swaps and related hedged items are reflected in “net trading, hedging and fair value income”. Any ineffectiveness is also recorded in “net trading, hedging and fair value income”.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortized to profit or loss over the period to maturity.

Cash flow hedge

For designated and qualifying cash flow hedges, the effective portion of the gain or loss on the hedging instrument is initially recognized directly in equity in the ‘Cash flow hedge’ reserve (hedging reserves are included in other reserves). The ineffective portion of the gain or loss on the hedging instrument is recognized immediately in ‘net trading income’.

When the hedged cash flow affects the income statement, the gain or loss on the hedging instrument is recorded in the corresponding income or expense line of the income statement. When a hedging instrument expires, or is sold, terminated, exercised, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognized when the hedged transaction is ultimately recognized in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

2. Summary of significant accounting policies (continued)

M. Property and equipment

All property and equipment are carried at cost less accumulated depreciation and accumulated impairment if any, except art objects and paintings. The Group adopted a revaluation method for its art objects and paintings in property and equipment in accordance with IAS 16 in 2014.

Depreciation is calculated using the straight-line method to write down the cost of such assets to their residual values over their estimated useful life as follows:

Buildings	50 years
Furniture and fixtures and motor vehicles	5 years
Office equipment	5 years
Leasehold improvements	5 years, or over the period of the lease term if less than 5 years

The residual values and useful lives of the assets are reviewed, and adjusted if appropriate, at each statement of financial position date.

Assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less cost to sell and value in use.

Gains and losses on disposal of property and equipment are determined by comparing net proceeds with the carrying amount and recognized in "other operating income/expense" in the income statement.

Expenses for the repair of property and equipment are charged against income. They are, however, capitalized if they result in an enlargement or substantial improvement of the respective assets.

Leasehold improvements comprise primarily the capitalized branch refurbishment costs.

N. Other intangible assets

(i) Computer software

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortized on the basis of the expected useful lives (not exceeding a period of five years).

(ii) Trademarks and customer relationships related intangibles

Intangible assets such as trademarks and customer relationships related intangibles acquired in a business combination are carried at fair value at the acquisition date. The fair value of an intangible asset reflects market expectations about the probability that the future economic benefits embodied in the asset will flow to the Group. In other words, the effect of probability is reflected in the fair value measurement of the intangible asset. The Group recognizes at the acquisition date separately from goodwill an intangible asset of the acquiree if the asset's fair value can be measured reliably, irrespective of whether the asset had been recognized by the acquiree before the business combination. Those intangible assets are amortized using the straight-line method over their useful lives, which have been assessed as 10 years.

2. Summary of significant accounting policies (continued)

(iii) Other intangible assets

Expenditures to acquire patents, rights and licenses are capitalized and amortized using the straight-line method over their useful lives of 5 years or licencing periods.

O. Accounting for leases

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.

Finance leases:

(i) Group company is the lessor

When assets are sold under a finance lease, the total amount of the lease payments is recognized as a receivable. The difference between the gross receivable and the present value of the receivable is recognized as unearned finance income. Lease income is recognized over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

(ii) Group company is the lessee

Assets acquired under finance lease agreements are capitalized at the inception of the lease at the fair value of the leased asset, which is the amount of cash consideration given for the leased asset. Lease payments are treated as comprising capital and interest elements; the capital element is treated as reducing the capitalized obligation under the lease and the interest element is charged to income. Depreciation on the leased asset is also charged to income on a straight-line basis over the useful life of the asset.

Operating leases:

(i) Group company is the lessor

Leases where the Group does not transfer substantially all the risks and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating operating leases are added to the carrying amount of the leased asset and recognized over the lease term on the same basis as rental income. Contingent rents are recognized as revenue in the period in which they are earned.

ii) Group company is the lessee

Leases which do not transfer to the Group substantially all the risks and benefits incidental to ownership of the leased items are operating leases. Operating lease payments, including prepayments (net of any incentives received from the lessor), are recognized as an expense in the income statement on a straight line basis over the lease term. Contingent rentals payable are recognized as an expense in the period in which they are incurred.

P. Goodwill

The excess of the cost of an acquisition over the fair value of the Group's share of the identifiable assets, liabilities or contingent liabilities of the acquired subsidiary at the date of acquisition of control is recorded as goodwill and represents a payment made by the acquirer in anticipation of future economic benefits from assets that are not capable of being individually identified and separately recognized. The acquirer also recognizes assets that are capable of being individually identified and separately recognized, intangible assets (e.g. credit card brand value, deposit base and customer portfolio) and contingent liabilities at fair value, irrespective of whether the asset had been recognized by the acquiree before the business combination; (if they can be distinguished from goodwill and if the asset's fair value can be measured reliably).

2. Summary of significant accounting policies (continued)

In line with "International Financial Reporting Standard for Business Combinations" ("IFRS 3"), goodwill is not subject to depreciation but is tested annually or more frequently for impairment and carried at cost less accumulated impairment losses, if any, in line with "International Accounting Standard for Impairment on Assets" ("IAS 36").

Q. Business combinations

Business combinations are accounted for using the purchase method. Transaction costs directly attributable to the acquisition form part of the acquisition costs. The non-controlling interest is measured as the proportionate share of the acquiree's identifiable net assets.

Business combinations achieved in stages are accounted for as separate steps. Any additional acquired share of interest does not affect previously recognized goodwill.

A business combination involving entities under common control of KFS is a business combination in which all of the combining entities are ultimately controlled by KFS both before and after the business combination, and that control is not transitory. In that respect, the Group considers legal mergers arising between entities ultimately controlled by KFS as business combinations under common control. On the other hand, business combinations involving entities under common control are scoped out of IFRS 3 and there is no other guidance on how to account for such transactions in current IFRS literature.

As there is an absence of a standard or an interpretation that specifically applies to business combinations involving entities under common control, the Bank management, in accordance with IAS 8, uses its judgment and developed and applied an accounting policy that the management believes results in information that is relevant to the economic decision-making needs of users and reflected the economic substance of transactions and not merely their legal form. In making its judgment in accordance with IAS 8, management considered US GAAP as a framework with a similar conceptual framework and applied pooling of interest method applicable under US GAAP in accounting for the business combinations involving entities under common control of KFS.

Since business combinations involving entities under the common control of KFS result in a single combined entity, a single uniform set of accounting policies is adopted. Therefore, the combined entity recognizes the assets, liabilities and equity of the combining entities at their existing carrying amounts adjusted only as a result of conforming the combining entities' accounting policies and applying those policies to all periods presented. There is no recognition of any new goodwill or negative goodwill. Similarly, the effects of all transactions between the combining entities, whether occurring before or after the merger, are eliminated in preparing the financial statements of the combined entity.

Expenditures incurred in relation to legal mergers are recognized as expenses in the period in which they are incurred.

2. Summary of significant accounting policies (continued)

R. Impairment of non-financial assets

At each reporting date, the Group evaluates whether there is any impairment indication on the asset. When an indication of impairment exists, the Group estimates the recoverable values of such assets. Impairment exists if the carrying value of an asset or a cash generating unit is greater than its recoverable amount which is the higher of value in use or fair value less costs to sell. Value in use is the present value of the future cash flows expected to be derived from an asset or cash-generating unit. An impairment loss is recognized immediately in the consolidated statement of income. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash flows from other assets or group of assets. An impairment loss recognized in prior periods for an asset (excluding goodwill) is reversed if the subsequent increase in the asset's recoverable amount is caused by a specific event since the last impairment loss was recognized. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized as income in the consolidated financial statements.

Impairment losses relating to goodwill cannot be reversed in future periods.

S. Financial liabilities

Financial liabilities including deposits from banks, customer deposits and other borrowed funds are recognized initially at cost. Subsequently, financial liabilities are stated at amortized cost, using the effective interest rate, except for financial liabilities designated at fair value. Amortized cost is calculated by taking into account any discount or premium on the issue and costs that are an integral part of the effective interest rate.

T. Income taxes

(i) Current income tax

Income tax payable (receivable) is calculated on the basis of the applicable tax law in the respective jurisdiction and is recognized as an expense (income) for the period except to the extent that current tax relates to items that are charged or credited in other comprehensive income or directly to equity. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the statement of financial position date.

Taxes other than on income are recorded within operating expenses (Note 32).

(ii) Deferred income taxes

Deferred income tax is provided in full, using the liability method, on all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the date of the statement of financial position and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

The principal temporary differences arise from measurement of financial assets and liabilities at fair value, provision for loan impairment, provision for employment termination benefits and unused investment allowances.

(Amounts expressed in thousands of TL unless otherwise indicated.)

2. Summary of significant accounting policies (continued)

Deferred income tax liabilities and assets are recognized when it is probable that the future economic benefit resulting from the reversal of temporary differences will flow to or from the Group. Deferred income tax assets resulting from temporary differences, carry forward of unused tax losses and unused tax credits are recognized to the extent that it is probable that future taxable profit will be available against which the deferred income tax asset can be utilized (Note 22).

Deferred income tax is provided on temporary differences arising from investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the difference will not reverse in the foreseeable future.

Deferred tax related to fair value re-measurement of available-for-sale investments and cash flow hedges, which are recognized in other comprehensive income, is also recognized in the other comprehensive income and subsequently in the consolidated income statement together with the deferred gain or loss.

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

U. Retirement benefit obligations

(i) Pension benefits transferable to Social Security Institution ("SSI")

Yapı ve Kredi Bankası Anonim Şirketi Mensupları Yardım ve Emekli Sandığı Vakfı ("the Fund") is a separate legal entity and a foundation recognized by an official decree, providing all qualified YKB employees with pension and post-retirement benefits. This scheme is funded through payments of both the employees and the employer as required by SSI Law Numbered 506 and are as follows:

	2017		2016	
	Employer (%)	**Employee (%)**	**Employer (%)**	**Employee (%)**
Retirement benefit contributions	11	9	11	9
Medical benefit contributions	7.5	5	7.5	5

The New Law was published in the Official Gazette dated May 8, 2008, numbered 26870. With the new law, the banks' pension funds would be transferred to SSI within three years from the date of publication of the decree and this period could be extended for a maximum of two years on the decision of the Council of Ministers. The transfer period was extended for another two years with the decision of the Council of Ministers No. 2011/1559 published in the Official Gazette dated April 9, 2011. According to the "Amendment of Social Insurance and General Health Insurance Law No, 6283" published in the Official Gazette dated March 8, 2012, the Council of Ministers was authorized to increase the two-year extension period mentioned above to four years. According to the decision of The Council of Ministers dated February 24, 2014, the transfer date was set as May 2015. The Council of Ministers was authorized to determine the transfer date of pension funds in accordance with the last amendment in the first paragraph of the 20th provisional article of Law No. 5510 implemented by the Law No. 6645 on Amendment of the Occupational Health and Safety Law and Other Laws and Decree Laws published in the Official Gazette dated April 23, 2015 and numbered 29335.

The Group's obligation in respect of the Fund has been determined as the value of the payment that would need to be made to SSI to settle the obligation at the statement of financial position date in accordance with Temporary Article 20 of the "Law regarding the changes in Social Insurance and General Health Insurance Law and other related laws and regulations" ("New Law") (Note 24). The pension disclosures set out in Note 24 therefore reflect actuarial parameters and results in accordance with the New Law provisions.

2. Summary of significant accounting policies (continued)

The pension benefits transferable to SSI are defined benefit plans and are calculated annually by an independent actuary who is registered by the Undersecretariat of Treasury.

(ii) Defined contribution plans

The Bank's subsidiaries in Turkey pay contributions to publicly administered SSI on a mandatory basis. Foreign subsidiaries contribute to the related government body for the pension scheme of its employees in the country they are domiciled. The Group has no further payment obligations once the contributions have been paid. The contributions are recognized as employee benefit expense when they are due.

(iii) Reserve for employment termination benefits

Provision for employment termination benefits represents the present value of the estimated total provision of the future probable obligation of the Group arising from the retirement of employees calculated in accordance with the Turkish Labour Law. In accordance with existing social legislation and Turkish Labour Law in Turkey, the Group is required to make lump-sum termination indemnities to each employee whose employment is terminated due to retirement or for reasons other than resignation or misconduct and who has completed at least one year of service. Provision is made for the present value of the defined benefit obligation calculated using the projected unit credit method. All actuarial gains and losses stem from the re-measurements of defined benefit obligation and are recognized immediately in the other comprehensive income.

V. Provisions, contingent assets and contingent liabilities

Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made.

Where the effect of the time value of money is material, provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation.

Possible assets or obligations that arise from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group are not included in the consolidated financial statements and are treated as contingent assets or liabilities.

Uncertain tax positions

The Group's uncertain tax positions are reassessed by management at every statement of financial position date. Liabilities are recorded for income tax positions that are determined by management as more likely than not to result in additional taxes being levied if the positions were to be challenged by the tax authorities. The assessment is based on the interpretation of tax laws that have been enacted or substantively enacted by the statement of financial position date and any known court or other rulings on such issues. Liabilities for penalties, interest and taxes other than on income are recognized based on management's best estimate of the expenditure required to settle the obligations at the statement of financial position date.

2. Summary of significant accounting policies (continued)

W. Interest income and expense

Interest income and expense are recognized in the income statement using the effective interest method.

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses.

The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, incremental costs that are directly attributable to the instrument and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognized using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

X. Fee and commission income and expense

Fees and commissions are generally recognized in the income statement on an accrual basis over the life of the transaction to which they refer. Commission income and fees for certain banking services such as import and export-related services, clearing, brokerage and custody services are recorded as income at the time of effecting the transactions to which they relate.

Portfolio and other management, advisory and service fees are recognized based on the applicable service contracts.

Y. Share capital

(i) Share issue costs

Incremental costs directly attributable to the issue of new shares or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

(ii) Share premium

When shares are issued, the excess of contributions received over the nominal value of the shares issued is recorded as share premium in equity.

(iii) Dividends on ordinary shares

Dividends on ordinary shares are recognized in equity in the period in which they are approved by the Company’s shareholders. Dividends for the year that are declared after the statement of financial position date are dealt with in the subsequent events note.

Z. Acceptances

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers, if the latter fails to meet their obligation. Acceptances are accounted for as off-statement of financial position transactions.

2. Summary of significant accounting policies (continued)

AA. Other credit related commitments

In the normal course of business, the Group enters into other credit related commitments including loan commitments, letters of credit and guarantees. These are reported as off-statement of financial position items at their notional amounts and are assessed using the same criteria as originated loans (Note 2.I). Specific provisions are therefore established when losses are considered probable and recorded as other provisions. The provision for credit related commitments also covers losses from the collective assessment where the commitments are grouped using the internal models developed by the Group stemming from the classification of credit related commitments into risk rating classes based on the observation of a series of parameters related to the borrower and/or to the utilization of the loan.

Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.

Financial guarantees are initially recognized in the financial statements at fair value on the date the guarantee was given. The fair value of a financial guarantee at the time of signature is zero because all guarantees are agreed on arm's length terms and the value of the premium agreed corresponds to the value of the guarantee obligation. Subsequent to initial recognition, the Group's liabilities under such guarantees are measured at the higher of the initial amount, less amortization of fees recognized in accordance with IAS 18, and the best estimate of the amount required to settle the guarantee. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the judgement of management. The fee income earned is recognized on a straight-line basis over the life of the guarantee. Any increase in the liability relating to guarantees is reported in the consolidated income statement within "impairment losses on loans, investment securities and credit related commitments".

AB. Offsetting

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a current legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

AC. Cash and cash equivalents

Cash and cash equivalents comprise balances with original maturities less than 90 days including cash and balances with central banks excluding reserve requirements and loans and advances to banks (Note 5).

AD. Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker is the person or group that allocates resources to and assesses the performance of the operating segments of an entity. All transactions between business segments are conducted on an arm's length basis, with intra-segment revenue and costs being eliminated in head office. Income and expenses directly associated with each segment are included in determining business segment performance.

In accordance with IFRS 8, the Group has the following business segments: Retail banking, Corporate and commercial banking, Private banking and wealth management, foreign operations, domestic operations, treasury asset liability management and other.

2. Summary of significant accounting policies (continued)

AE. Earnings per share

Earnings per share disclosed in the consolidated income statement are determined by dividing net income by the weighted average number of shares outstanding during the year concerned in Note 34.

AF. Dividends on ordinary shares

Dividends on ordinary shares are recognized as a liability and deducted from equity when they are approved by the Bank's shareholders.

AG. Comparatives

Comparative figures are reclassified, where necessary, to conform to changes in presentation of the December 31, 2017 consolidated financial statements.

3. Critical accounting estimates and judgements in applying accounting policies

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. These disclosures supplement the commentary significant accounting policies (Note 2) and financial risk management (Note 4).

Critical accounting judgements made in applying the Group's accounting policies include:

Financial asset and liability classification: The Group's accounting policies provide scope for assets and liabilities to be designated on inception into different accounting categories in certain circumstances:

In classifying financial assets and liabilities as "trading", "held-to-maturity" and "available-for-sale assets" the Group has determined that it meets the descriptions set out in accounting policy Note 2F and Note 2G.

Finance leases and derecognition of financial assets: Management applies judgement to determine if substantially all the significant risks and rewards of ownership of financial assets and lease assets are transferred to counterparties, in particular which risks and rewards are the most significant and what constitutes substantially all risks and rewards.

The key assumptions concerning the future and other key sources of estimation uncertainty that may be a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Impairment of available for-sale investments

The Group reviews its debt securities classified as available-for-sale investments at each statement of financial position date to assess whether they are impaired. This requires similar judgement as applied to the individual assessment of loans and advances.

3. Critical accounting estimates and judgements in applying accounting policies (continued)

The Group also determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement the Group evaluates, among other factors, the volatility in share price and duration and extent to which the fair value of an investment is less than its cost. In addition, objective evidence of impairment may be deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational or financing cash flows.

Impairment losses on loans and advances

The methodology and assumptions used for estimating both the amount and timing of future cash flows from a portfolio of loans are reviewed regularly to reduce any differences between loss estimates and actual loss experience. The Group calculates collective (IBNR) provision with intrinsic elements such as loss confirmation periods, probability of default and loss given defaults along with expert views.

Fair value of derivatives

Where valuation techniques (for example, models) are used to determine fair values, they are validated and periodically reviewed. To the extent practical, models use only observable data, however areas such as credit risk (both own and counterparty), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect reported fair values. However, the effect of the changes in assumptions about these factors is insignificant as at December 31, 2017.

Tax legislation

Turkish tax legislation is subject to varying interpretations as disclosed in Note 22.

Pension fund

The Group determines the present value of funded benefit obligations in accordance with the New Law by using several critical actuarial assumptions, including the discount rate, mortality rate, and medical costs defined by the Law as disclosed in Note 24. This approach recognizes the obligations of the Group to make payments to SSI in respect of the benefits which will be transferred to SSI rather than an obligation to make benefit payments to individuals.

Deferred income tax asset recognition

Deferred income tax assets are recorded to the extent that realization of the related tax benefit is probable. The future taxable profits and the amount of tax benefits that are probable in the future are based on medium term business plans prepared by management and extrapolated results thereafter. The business plans are based on management expectations that are believed to be reasonable under the circumstances.

Goodwill

Recoverable amount of goodwill was estimated based on value in use calculation as disclosed in Note 13.

With specific reference to future cash flow projections used in the impairment test of goodwill, it should be noted that the parameters and information used are significantly influenced by the macro-economic market situation and realization of business plans, which may change.

4. Financial risk management

The Group's risk management functions are independent from the commercial operations along with committees such as Executive Committee and the other individual risk committees covering credit, market and operational risks and are an integral part of ensuring the Group's fulfilment of requirements stipulated by the Banking Law in a manner consistent with shareholders' risk appetites. The risk management function is responsible for: (1) maximizing returns on invested capital and maintaining sustainable growth of profitability (2) monitoring trends in risk exposures and communicating irregularities promptly to senior management (3) monitoring asset and liability profiles for rebalancing actions on a timely basis (4) identifying and classifying the risk structures of products, processes and services (5) developing and validating the credit rating/scoring models and (6) ensuring compliance with Basel requirements and Banking Law.

A. Credit risk

Credit risk is the risk that the Group will incur a loss because its customers or counterparties fail to discharge their contractual obligations. Credit risk arises mainly from commercial and consumer loans and advances, credit cards and loan commitments arising from such lending activities, but can also arise from credit enhancement provided, such as financial guarantees, letters of credit, endorsements and acceptances.

The Group is also exposed to other credit risks arising from investments in debt securities and other exposures arising from its trading activities ('trading exposures'), including non-equity trading portfolio assets, derivatives, reverse repos and settlement balances with market counterparties.

The Group makes available to its customers guarantees which may require that the Group makes payments on their behalf and enter into commitments to extend credit lines to secure their liquidity needs. Letters of credit and guarantees (including standby letters of credit) commit the Group to make payments on behalf of customers in the event of a specific act, generally related to the import or export of goods. Such commitments expose the Group to similar risks to loans and are mitigated by the same control processes and policies.

The Group manages credit risk through the following implementations:

(a) establishment of credit risk policy involving credit risk strategies, implementation of credit policy guidelines, definition of the optimum composition of the overall loan portfolio, credit risk budget and identification of risk positions within legal and group wide limitations;

(b) development, enhancement and maintenance of rating and scoring models (probability of default ("PD"), exposure at default ("EAD") and loss given default ("LGD")) models for all segments for measuring, monitoring and controlling credit risk;

(c) monitoring and measuring the evolution of credit risk for all segments, (i.e. by industry, sector, geographical area etc.), presentation of the strategic credit risk related reports to senior management, including evolution of loan provisioning and comparison with peer banks;

(d) obtaining continuity of operative methodologies (e.g. borrower evaluation, loan and collateral classifications, monitoring and recovery principles) for credit processes (underwriting, monitoring and work-out) and related tools (including testing of new functionalities);

(e) evaluation of new credit products, changes to existing ones and monitoring them to ensure the risk profile is compatible with the risk appetite and reputational risk of the Bank (e.g. on the basis of minimum requirements in terms of granting, monitoring, work-out procedures, pilot phase definition, regular performance measurement, sustainable and sound introduction and growth criteria, etc.);

(f) preparation of credit risk budget in line with predefined lending targets;

(g) calculation of Cost of Risk and related provisions by segments to better assess the riskiness of the loan portfolio for maintaining asset quality;

(h) execution of provisioning methodologies in line with BRSA and IFRS principles.

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

Credit policies reflect general credit risk principles to be followed throughout the Group's lending activities and the related strategies and goals, as well as shareholders' risk appetites. The credit policy guideline is prepared by the Group's credit risk management department and approved by the Board of Directors.

Parent Bank rating system:

The strategy of the Bank is to develop rating/scoring models (both application and behavioural) in house. For this aim, a credit rating model development unit has been established and all models since 2009 have been developed internally. In parallel to this, a separate validation team is responsible for initial and ongoing validation of the models.

30 different rating models (including sub-models) developed internally are in use for different clients.

For corporate & commercial clients, integrated with the underwriting process, the Bank's internal application rating model calculates ratings and assigns a probability of default for each borrower, classifying them under a scale of 9 grades examining both quantitative (statement of financial position, income and cash flow analysis, collateral value) and qualitative information (management assessment, competitive position, sector performance and environmental factors). The outcomes of the grading system reflect the riskiness of each rated customer.

A separate rating model is used for the customers operating in construction industry.

The Bank's rating tool concentration by risk classes as of December 31, 2017 and 2016 is as follows:

		Concentration level (%)	
	Rating class (1)	**2017**	**2016**
Above average	1-4	46.5	45.2
Average	5+ - 6	46.9	44.3
Below average	7+ - 9	6.6	10.5

(1) For corporate and commercial clients that are rated individually only.

Application rating model used for SME clients has 6 sub-segments to measure the risk level of SME clients during the underwriting process.

Behavioural rating models for SME and commercial clients are used for monitoring the performance of existing portfolio on a monthly basis.

On the private individual side, scoring models are also used throughout the granting, limit management and monitoring/collection processes for consumer loans and credit cards segment.

The above-mentioned methodologies and processes dedicated to different market segments (usage of different credit evaluation tools per segments) gives the Bank the ability to measure, manage and monitor credit risk in a more accurate way.

Taking into consideration the scoring models, the Group classifies its credit portfolio into the following groups as at December 31, 2017 and 2016:

	December 31, 2017		**December 31, 2016**	
Group's rating	**% of Loans and advances**	**Provision coverage %**	**% of Loans and advances**	**Provision coverage %**
1. Performing loans	93.09	0.41	92.21	0.50
2. Watch-listed	2.64	4.12	3.28	4.16
3. Legal follow-up	4.27	75.07	4.51	74.43
	100.00	**3.69**	**100.00**	**3.96**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

The details of the loans and advances past due but not impaired (the Group defines this group as loans with a past due days between 30 to 90 days) which are classified under performing loans (including past due watch-listed loans) are as follows;

	December 31, 2017			
	Past due between 30 – 60 days	**Past due between 60 – 90 days**	**Total**	**December 31, 2016 Total**
Corporate	502,034	3,540,118	4,042,152	4,580,073
Consumer	704,553	348,705	1,053,258	1,396,737
Credit cards	162,536	202,262	364,798	478,427
Leasing	6,502	2,875	9,377	10,407
Factoring	11,741	2,887	14,628	19,258
	1,387,366	**4,096,847**	**5,484,213**	**6,484,902**

The watch list category is defined as clients with payments past due 30 to 90 days and clients which are considered by the monitoring department on the basis of subjective criteria, to require close monitoring.

Loans and advances rescheduled:

Restructuring activities include extended and/or rescheduled payment arrangements, approved external management plans, arrangement of terms of loan such as modification and deferral of payments, interest rate, foreign exchange (“FX”) type, collateral structure, or additional loans etc, there can also be alternatives of granting additional loans or sale of collateral, sale of debts, and sale of companies.

Restructuring may be applied for watch-listed loans (classification as watch is not based on past due days) or loans in nonperforming loan accounts, If restructuring is applied for a watch-listed loan, that loan will be classified to performing loan accounts but its terms (FX rate, payment dates, interest rate etc) may be changed.

On the other hand, if restructuring is applied for loans in non-performing loan accounts that loan will continue to stay at least 6 more months in non-performing loan accounts and it may be transferred to specified “restructured loan accounts” when both of the following conditions are met: after at least 15% collection of the loan amount and staying at least 6 months in nonperforming loan accounts, If an additional loan was granted during restructuring, then at least 15% collection requirement becomes at least 20% of total (existing + additional loan). As of December 31, 2017, the total amount of restructured loans included in legal follow up during the year was TL 391,266 (2016 - TL 528,332).

Restructuring policies and practices are consistent with the requirements of the BRSA.

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

Maximum exposure to credit risk

	December 31, 2017	December 31, 2016
Credit risk exposures relating to assets on-statement of financial position:		
Loans and advances to banks	5,654,217	3,449,218
Loans and advances to customers		
- Credit cards	24,651,478	22,814,646
- Consumer	34,878,810	31,655,980
- Corporate	141,481,380	123,363,847
- Leasing	10,260,673	8,262,225
- Factoring	3,833,042	2,884,153
Financial assets held for trading:		
- Securities	102,587	43,365
- Derivative financial instruments	4,109,547	2,986,773
Hedging derivatives	1,756,611	1,209,712
Investment securities		
- Available-for-sale	24,316,146	18,217,306
- Held-to-maturity	14,197,066	11,588,890
Other assets	4,919,955	4,607,967
Credit risk exposures relating to off-statement of financial position items:		
Credit related commitments	71,827,637	61,985,401
Other	7,023,778	6,469,083

The above table represents a worst case scenario of credit risk exposure in the absence of any collateral or credit enhancements.

The main types of collateral obtained are as follows:

- For securities lending and reverse repurchase transactions, cash or securities
- For commercial lending, mortgages over real estate properties, cash, guarantee letters, securities, pledges or guarantees
- For retail lending, mortgages over residential properties or pledges on vehicles

Management monitors the market value of collateral and requests additional collateral in accordance with the underlying agreement when necessary.

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

Industry sectors

The Group uses the Central Bank of Republic of Turkey (CBRT) definitions for economic sectors in order to be able to make comparisons with banking sector wide figures. These definitions are also in line with NACE (European Classification of Economic Activities) classifications which are used within the EU. Through the credit policy, the Board of Directors sets the sectoral limits on lending, and these limits can only be altered by a decision from the Board of Directors. The sector concentration is accordingly monitored and reported on a regular basis. Particular attention is given to some sectors which are considered as “low performers” in terms of high non-performing loan (“NPL”) levels. Macroeconomic conditions, NPL levels, expectations about sectors and UCG group policies are taken into consideration in setting and altering the limits. Sectoral classification is defined in terms of the borrower’s activity area, not based on collateral.

	Financial institutions	Manufacturing	Real estate	Wholesale and retail trade	Public sector	Other industries	Individuals	Total
Loans and advances to banks	5,654,217	-	-	-	-	-		5,654,217
Loans and advances to customers	5,570,189	39,829,034	3,314,131	12,640,344	1,781,807	92,268,357	59,701,521	215,105,383
Trading securities - debt securities			-	-	56,980	-	-	56,980
Derivative financial instruments	1,699,742	2,090,344	-	-	190	1,933	317,338	4,109,547
Hedging derivatives	1,756,611	-	-	-		-	-	1,756,611
Investment securities - debt securities	2,752,311	-	-		35,760,901	-	-	38,513,212
Other assets	2,889,449	-	-	-	208	2,875,843	4,321	5,769,821
As of December 31, 2017	**20,322,519**	**41,919,378**	**3,314,131**	**12,640,344**	**37,600,086**	**95,146,133**	**60,023,180**	**270,965,771**
As of December 31, 2016	**16,805,189**	**27,329,742**	**891,382**	**6,065,879**	**28,823,595**	**107,268,000**	**44,603,569**	**231,787,356**

	Financial institutions	Manufacturing	Real estate	Wholesale and retail trade	Public sector	Other industries	Individuals	Total
Letter of guarantees	4,784,929	23,477,423	1,442,307	4,366,623	-	26,228,243	226	60,299,751
Letter of credits	513,380	8,760,697	20,000	1,764,313	-	469,496	-	11,527,886
Acceptance credits	-	174,128	-	21,500	-	17,057	-	212,685
Other commitments and contingencies	272,783	4,152,875	-	476,977	-	1,908,458	-	6,811,093
As of December 31, 2017	**5,571,092**	**36,565,123**	**1,462,307**	**6,629,413**	**-**	**28,623,254**	**226**	**78,851,415**
As of December 31, 2016	**4,481,450**	**33,362,053**	**578,686**	**5,322,829**	**-**	**24,709,466**	**-**	**68,454,484**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

Geographical sectors

Geographical concentrations of total assets:

	Turkey	Italy	Other EU	Other	Total
Cash and balances with central banks	41,973,580	-	227,545	250,845	42,451,970
Loans and advances to banks	2,720,343	452,228	894,779	1,586,867	5,654,217
Financial assets held for trading	1,164,753	-	934,408	2,112,973	4,212,134
-Trading securities	102,587	-	-	-	102,587
-Derivative financial instruments	1,062,166	-	934,408	2,112,973	4,109,547
Hedging derivatives	1	-	207,723	1,548,887	1,756,611
Loans and advances to customers, net					
- Credit cards	24,591,786	-	-	59,692	24,651,478
- Consumer	34,794,566	-	-	84,244	34,878,810
- Corporate	133,426,476	523,373	3,946,729	3,584,802	141,481,380
- Leasing	10,001,003	-	115,481	144,189	10,260,673
- Factoring	3,833,042	-	-	-	3,833,042
Investment securities					
- Available-for-sale	23,967,131	-	25,404	323,611	24,316,146
- Held-to-maturity	13,192,237	54,669	894,326	55,834	14,197,066
Investment in associates and joint ventures	261,027	-	-	529,384	790,411
Goodwill	1,023,528				1,023,528
Other intangible assets	684,074	-	1,142	17,643	702,859
Property and equipment	1,190,792	-	2,272	13,039	1,206,103
Deferred income tax assets	351,398	-	-	-	351,398
Other assets	5,166,810	29,814	138,913	434,284	5,769,821
As of December 31, 2017	**298,342,547**	**1,060,084**	**7,388,722**	**10,746,294**	**317,537,647**
As of December 31, 2016	**255,505,992**	**267,395**	**8,065,418**	**4,694,128**	**268,532,933**
Letter of guarantees	45,537,167	1,225,029	2,156,704	11,380,851	60,299,751
Letter of credits	413,156	240,529	2,481,999	8,392,202	11,527,886
Acceptance credits	3,854	12,360	74,482	121,989	212,685
Other commitments and contingencies	4,395,744	-	1,345,584	1,069,765	6,811,093
As of December 31, 2017	**50,349,921**	**1,477,918**	**6,058,769**	**20,964,807**	**78,851,415**
As of December 31, 2016	**60,725,045**	**1,243,923**	**1,274,902**	**5,210,614**	**68,454,484**

4. Financial risk management (continued)

B. Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchange rates and equity prices. As a commercial group, the focus is serving the financial needs of the customers, thereby generating exposure to interest rate, and foreign exchange risk.

The Market Risk Policy of the Group identifies risk-management guidelines. According to the Market Risk Policy, market risk is managed depending on the treatment of the banking book and trading book. The banking book consists of all assets and liabilities arising from commercial activities and is sensitive to interest rate and foreign exchange movements. The trading book, on the other hand, includes the positions held for trading, client servicing purposes or for market making operations.

The Group trades mainly in FX and securities, within predefined limits. Risk limits are set on intra-day and end of day positions as well as Value-at-Risk, monitored on a daily basis.

The banking book interest rate risk is measured through the economic value sensitivity method, which implies the potential change in fair value of the interest rate positions resulting from a parallel upward/downward shift of the yield curve. The overall sensitivity is required to be within 20% of the Core Tier 1 Capital, as also outlined in Basel II. Interest rate swaps are utilized to mitigate the banking book interest rate risk resulting from repricing and maturity mismatches. Besides Economic Value Sensitivity, an overall Value at Risk, covering all statement of financial position items and Basis Point Value (“BPV”) methods are used to measure the structural interest rate risk.

As part of the management of market risk, the Group undertakes various hedging strategies with hedge accounting applied (Note 8). The Group also uses derivative financial instruments such as forwards, swaps, futures and options in the foreign exchange and capital markets. These transactions are considered as effective economic hedges under the Group’s risk management policies. However, since they do not qualify for hedge accounting under the specific provisions of IAS 39, they are treated as derivatives held for trading.

The major measurement techniques used to measure and control market risk are outlined below.

(a) Value-at-risk

The Group applies a VaR methodology to its trading portfolios, to estimate the market risk of positions held and the maximum losses expected, based upon a number of assumptions for various changes in market conditions. The VaR limits are set by the Board of Directors and revised every year according to the budget and strategic plan of the Group. VaR limit compliance is monitored by Risk Management on a daily basis.

VaR is a statistically based estimate of the potential loss on the current portfolio from adverse market movements. It expresses the “maximum” amount the Group might lose, but only to a certain level of confidence (99%). There is therefore a specified statistical probability (1%) that actual loss could be greater than the VaR estimate. The VaR model of the Group assumes a one-day “holding period” until positions can be closed. The Group’s assessment of past movements is based on data for the past 500 days. The Group applies these historical changes in rates, prices, indices, etc. directly to its current positions - a method known as historical simulation. Actual outcomes are monitored regularly to test the validity of the assumptions and parameters/factors used in the VaR calculation (back testing). The use of this approach does not prevent losses outside of these limits in the event of more significant market movements.

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

As VaR constitutes an integral part of the Group's market-risk control regime, VaR limits are established annually for all trading portfolio operations. For investment positions, such as available for sale or held-to-maturity portfolios, risk appetite limits are also applied (VaR/Nominal Positions). Actual exposure against limits, together with a consolidated group-wide VaR, is reviewed daily by Risk Management. Average VaR for the trading portfolio of the Group for the twelve months period is TL 5,342 in 2017.

The quality of the VaR model is continuously monitored by back-testing the VaR results for trading books. All back-testing exceptions are investigated, and results are reported to the monthly Executive Committee ("ExCo") meetings.

Group total VaR includes securities, fx position, loans, deposits, debt securities issued and derivatives which are sensitive to fluctuations in interest rates, FX, equity prices and commodity prices on and off the bank's balance sheet and the trading VaR takes into account the securities portfolio held for trading, fx position and derivatives performed for trading purposes.

Trading portfolio VaR by risk type	**12 months to reporting date (2017)**		
	Average	**High**	**Low**
Foreign exchange risk	5,736	11,818	1,487
Interest rate risk of trading securities	2,526	4,996	1,335
Equities risk	1,547	5,508	211
Total VaR	**5,342**	**9,589**	**2,685**

	12 months to reporting date (2016)		
	Average	**High**	**Low**
Foreign exchange risk	2,538	5,983	344
Interest rate risk of trading securities	3,057	7,450	710
Equities risk	1,215	2,823	25
Total VaR	**2,508**	**5,593**	**651**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

(b) Stress tests

Stress tests provide an indication of the potential size of losses that could arise in extreme conditions. The stress tests carried out by Risk Management, also included in the market risk policy of the Group, include: FX and interest rate stress testing, where stress movements are applied to the FX position and to the banking book. The results of the stress tests are reviewed by ExCo.

i) Foreign exchange risk

Foreign exchange exposure is the result of the mismatch of foreign currency denominated assets and liabilities (including foreign currency indexed ones) together with exposures resulting from off-balance sheet foreign exchange derivative instruments. The Group takes an exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows.

The limits are set by the Board of Directors on the level of exposure in aggregate for both overnight and intra-day positions, which are monitored on a daily basis.

The table below summarizes the Group's assets and liabilities at carrying amounts, categorized by currency. The off-balance sheet gap represents the difference between the notional amounts of purchased and sold foreign currency derivative financial instruments.

December 31, 2017

				Foreign currency
	USD	**EUR**	**Other**	**Total**
Assets				
Cash and balances with central banks	18,596,857	11,061,491	5,197,921	34,856,269
Loans and advances to banks	2,317,496	3,152,939	97,684	5,568,119
Financial assets held for trading				
- Trading securities	27,786	2,610	-	30,396
- Derivative financial instruments	384,670	133,043	78	517,791
Loans and advances to customers	44,461,584	44,099,681	1,367,850	89,929,115
Hedging derivatives	119,641	49,028	-	168,669
Investment securities				
- Available-for-sale	2,201,127	737,775	72,507	3,011,409
- Held-to-maturity	6,293,547	1,131,782	1	7,425,330
Investment in associates and joint ventures	-	-	529,384	529,384
Property and equipment	-	2,272	13,038	15,310
Deferred income tax assets	-	-	-	-
Other assets	974,964	1,746,483	399,684	3,121,131
Total assets	**75,377,672**	**62,117,104**	**7,678,147**	**145,172,923**
Liabilities				
Deposits from banks	5,094,399	1,782,796	79,547	6,956,742
Customer deposits	57,090,475	31,308,283	2,769,866	91,168,624
Funds borrowed	19,918,484	22,978,476	242,173	43,139,133
Debt securities in issue	19,372,565	1,100,496	96,669	20,569,730
Financial liabilities designated at fair value	4,363,503	-	-	4,363,503
Derivative financial instruments	211,703	71,301	24	283,028
Current income taxes payable	-	7,627	3,789	11,416
Deferred income tax liabilities	-	271	6,882	7,153
Hedging derivatives	-	12,443	-	12,443
Other provisions	-	253	-	253
Retirement benefit obligations				
Other liabilities	755,854	2,159,622	26,004	2,941,480
Total liabilities	**106,806,983**	**59,421,568**	**3,224,954**	**169,453,505**
Net balance sheet position	**(31,429,311)**	**2,695,536**	**4,453,193**	**(24,280,582)**
Off-balance sheet derivative instruments net notional position	**31,509,469**	**(2,502,851)**	**(3,782,174)**	**25,224,444**
Net foreign currency position	**80,158**	**192,685**	**671,019**	**943,862**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

December 31, 2016

	USD	EUR	Other	Foreign currency Total
Assets				
Cash and balances with central banks	12,058,587	6,964,891	5,008,378	24,031,856
Loans and advances to banks	962,258	2,339,578	103,993	3,405,829
Financial assets held for trading				
- Trading securities	16,400	1,425	-	17,825
- Derivative financial instruments	277,751	115,196	62	393,009
Loans and advances to customers	45,618,318	37,564,363	1,444,578	84,627,259
Hedging derivatives	88,593	24,511	-	113,104
Investment securities				
- Available-for-sale	2,251,867	700,325	21,317	2,973,509
- Held-to-maturity	5,889,209	868,012	2	6,757,223
Investment in associates and joint ventures	-	-	437,143	437,143
Property and equipment	-	2,363	32,328	34,691
Deferred income tax assets	-	-	-	-
Other assets	1,233,193	1,530,339	220,750	2,984,282
Total assets	**68,396,176**	**50,111,003**	**7,268,551**	**125,775,730**
Liabilities				
Deposits from banks	3,044,682	1,388,883	60,406	4,493,971
Customer deposits	43,731,650	24,214,215	2,389,788	70,335,653
Funds borrowed	13,537,887	18,958,930	372,278	32,869,095
Debt securities in issue	14,526,320	487,387	304,310	15,318,017
Financial liabilities designated at fair value	3,938,694	-	-	3,938,694
Derivative financial instruments	209,704	153,519	26,521	389,744
Current income taxes payable	-	4,188	-	4,188
Deferred income tax liabilities	-	263	7,629	7,892
Hedging derivatives	4,200	18,832	1	23,033
Other provisions	-	208	91	299
Retirement benefit obligations	-	-	-	-
Other liabilities	863,587	1,614,500	7,612	2,485,699
Total liabilities	**79,856,724**	**46,840,925**	**3,168,636**	**129,866,285**
Net balance sheet position	**(11,460,548)**	**3,270,078**	**4,099,915**	**(4,090,555)**
Off-balance sheet derivative instruments net notional position	**11,314,635**	**(3,142,494)**	**(3,490,796)**	**4,681,345**
Net foreign currency position	**(145,913)**	**127,584**	**609,119**	**590,790**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

At December 31, 2017, assets and liabilities denominated in foreign currency were translated into TL using a foreign exchange rate of TL 3.7719 = USD 1, and TL 4.5155 = EUR 1 (2016 - TL 3.5192 = USD 1, and TL 3.7099 = EUR 1).

For the purpose of calculating currency risks, foreign currency indexed loans and securities have been reported in this table in the relevant currency of indexation.

Currency risk sensitivity:

The table below represents the sensitivity of the Parent Bank to a 15% change of currency exchange rates (USD and EUR). A 15% change is the assumption of parity change that may be faced in a possible fluctuation used in the Parent Bank's stress test scenarios.

	December 31, 2017	December 31, 2016
Change in currency exchange rate	**Profit/loss effect [1]**	**Profit/loss effect [1]**
(+) 15%	(78,072)	(55,076)
(-) 15%	78,072	55,076

(1) Excluding tax effect.

ii) Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest rate risk limits are set in terms of an economic value sensitivity limit and Basis Point Value ("BPV") limit. Economic value sensitivity analysis is performed according to a scenario of 2% shift in FX yield curve and 4% shift in TL yield curve. The resulting profit/loss should not exceed 20% (Sensitivity Limit) of the Bank's Tier 1 + Tier 2 Capital. The BPV limit restricts maximum interest rate risk position by currency and time buckets. BPV is applied for the banking book and represents the sensitivity of the banking book to 1 bp change in interest rates.

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

The table below summarizes the Group's exposure to interest rate risk at December 31, 2017 and 2016. Included in the table are the Group's assets and liabilities in carrying amounts classified in terms of periods remaining to contractual repricing dates.

December 31, 2017	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Non-interest Bearing	Total
Assets						
Cash and balances with central banks	24,310,693	-	-	-	18,141,277	42,451,970
Loans and advances to banks	4,008,328	378,192	-	-	1,267,697	5,654,217
Financial assets held for trading						
- Trading securities	7,808	3,889	12,871	39,577	38,442	102,587
- Derivative financial instruments	2,727,387	729,100	443,836	209,224	-	4,109,547
Hedging derivatives	566,758	25,328	1,030,302	134,223	-	1,756,611
Loans and advances to customers	68,613,285	67,472,920	65,378,677	12,634,067	1,006,434	215,105,383
Investment securities						
- Available-for-sale	7,417,136	6,552,573	7,178,172	2,921,472	246,793	24,316,146
- Held-to-maturity	2,891,220	2,551,131	1,166,133	7,588,582	-	14,197,066
Investment in associates and joint ventures	-	-	-	-	790,411	790,411
Goodwill	-	-	-	-	1,023,528	1,023,528
Other intangible assets	-	-	-	-	702,859	702,859
Property and equipment	-	-	-	-	1,206,103	1,206,103
Deferred income tax assets	-	-	-	-	351,398	351,398
Other assets		-	-	-	5,769,821	5,769,821
Total assets	**110,542,615**	**77,713,133**	**75,209,991**	**23,527,145**	**30,544,763**	**317,537,647**
Liabilities						
Deposits from banks	17,316,185	542,842	180,656	-	636,676	18,676,359
Customer deposits	122,350,087	8,851,426	1,495,220	168,085	31,268,837	164,133,655
Funds borrowed	33,050,373	11,278,956	6,888,737	1,757,846	-	52,975,912
Debt securities in issue	6,169,772	3,623,472	7,399,208	7,259,795	-	24,452,247
Financial liabilities designated at fair value	4,363,503	-	-	-	-	4,363,503
Derivative financial instruments	1,854,785	979,499	793,936	192,485	-	3,820,705
Current income taxes payable	-	-	-	-	255,614	255,614
Deferred income tax liabilities	-	-	-	-	16,606	16,606
Hedging derivatives	188,841	3,039	113,966	6,932	-	312,778
Other provisions	-	-	-	-	1,231,170	1,231,170
Retirement benefit obligations	-	-	-	-	1,091,399	1,091,399
Other liabilities	-	-	131	2	15,411,390	15,411,523
Total liabilities	**185,293,546**	**25,279,234**	**16,871,854**	**9,385,145**	**49,911,692**	**286,741,471**
Net interest repricing gap (on balance)	**(74,750,931)**	**52,433,899**	**58,338,137**	**14,142,000**	**(19,366,929)**	**30,796,176**
Off-balance sheet derivative instruments net notional position	36,374,419	(3,383,971)	(27,300,898)	(7,175,587)	-	(1,486,037)
Net interest repricing gap (net position)	**(38,376,512)**	**49,049,928**	**31,037,239**	**6,966,413**	**(19,366,929)**	**29,310,139**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

December 31, 2016	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Non-interest bearing	Total
Assets						
Cash and balances with central banks	18,716,507	55,603	-	-	14,311,185	33,083,295
Loans and advances to banks	1,909,371	202,417	1,083	-	1,336,347	3,449,218
Financial assets held for trading						
- Trading securities	856	10,914	6,179	18,781	6,635	43,365
- Derivative financial instruments	1,872,312	420,684	423,567	270,210	-	2,986,773
Hedging derivatives	1,169,122	456	40,134	-	-	1,209,712
Loans and advances to customers	62,956,520	55,692,196	44,570,284	21,580,392	4,181,459	188,980,851
Investment securities						
- Available-for-sale	6,504,246	5,798,470	3,475,043	2,236,164	203,383	18,217,306
- Held-to-maturity	879,676	1,505,914	1,645,515	7,557,785	-	11,588,890
Investment in associates and joint ventures	-	-	-	-	682,728	682,728
Goodwill	-	-	-	-	1,023,528	1,023,528
Other intangible assets	-	-	-	-	587,422	587,422
Property and equipment	-	-	-	-	1,267,706	1,267,706
Deferred income tax assets	-	-	-	-	94,246	94,246
Other assets	89,480	-	-	-	5,228,413	5,317,893
Total assets	**94,098,090**	**63,686,654**	**50,161,805**	**31,663,332**	**28,923,052**	**268,532,933**
Liabilities						
Deposits from banks	12,501,077	696,516	-	-	613,650	13,811,243
Customer deposits	113,004,146	8,862,812	981,506	133,683	26,568,606	149,550,753
Funds borrowed	24,338,842	10,240,290	1,853,121	735,500	-	37,167,753
Debt securities in issue	7,289,311	6,452,217	5,530,026	37,345	-	19,308,899
Financial liabilities designated at fair value	-	-	-	3,938,694	-	3,938,694
Derivative financial instruments	880,670	589,609	903,948	204,452	-	2,578,679
Current income taxes payable	-	-	-	-	33,792	33,792
Deferred income tax liabilities	-	-	-	-	7,892	7,892
Hedging derivatives	88,157	631	508	-	-	89,296
Other provisions	-	-	-	-	765,014	765,014
Retirement benefit obligations	-	-	-	-	697,516	697,516
Other liabilities	591	7,696	1,112	-	13,654,513	13,663,912
Total liabilities	**158,102,794**	**26,849,771**	**9,270,221**	**5,049,674**	**42,340,983**	**241,613,443**
Net interest repricing gap (on balance)	**(64,004,704)**	**36,836,883**	**40,891,584**	**26,613,658**	**(13,417,931)**	**26,919,490**
Off-balance sheet derivative instruments net notional position	27,267,765	(2,350,770)	(16,392,589)	(8,159,895)	-	364,511
Net interest repricing gap (net position)	**(36,736,939)**	**34,486,113**	**24,498,995**	**18,453,763**	**(13,417,931)**	**27,284,001**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

Interest rate sensitivity analysis:

The sensitivity analysis regarding the effect of interest rate fluctuations on the financial statements is performed for all interest earning assets and interest bearing liabilities.

Interest rate risk resulting from banking books comprise of repricing risk, yield curve risk, and basis risk.

Interest rate risk is measured and monitored monthly by market risk management. Duration analysis, gap analysis, basis points value analysis, scenario analysis and simulation of net interest income are performed and reported monthly to Asset Liability Management function of the Executive Committee.

Interest sensitivity is measured most appropriately using the duration distribution map for every type of product. Investment decisions are done by taking into account the interest rate measurements. The maturity and interest risk for products with uncertain maturities is effectively measured using behavioral analysis.

Economic value differences resulting from interest rate fluctuations of the Bank as of December 31, 2017 and 2016 are presented in the table below.

	December 31, 2017		
Currency	**Applied shock (+/- x basis points)**	**Gains/ Losses**	**Gains/ Regulatory Equity-Losses/ Regulatory Equity**
TL	(+)500 bp	(3,185,735)	(8.80)%
TL	(-)400 bp	3,039,566	8.40%
EUR	(+)200 bp	(38,967)	(0.11)%
EUR	(-)200 bp	(1,774)	-
USD	(+)200 bp	(14,025)	(0.04)%
USD	(-)200 bp	177,156	0.49%
Total (for negative shock)		**3,214,948**	8.88%
Total (for positive shock)		**(3,238,727)**	(8.95)%

	December 31, 2016		
Currency	**Applied shock (+/- x basis points)**	**Gains/ Losses**	**Gains/ Regulatory Equity-Losses/ Regulatory Equity**
TL	(+)500 bp	(2,513,657)	(7.72)%
TL	(-)400 bp	2,503,767	7.69%
EUR	(+)200 bp	(232,786)	(0.71)%
EUR	(-)200 bp	232,057	0.71%
USD	(+)200 bp	(134,829)	(0.41)%
USD	(-)200 bp	286,728	0.88%
Total (for negative shock)		**3,022,552**	9.28%
Total (for positive shock)		**(2,881,272)**	(8.85)%

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

The table below summarises weighted average interest rates for financial instruments by major currencies outstanding at December 31, 2017 and 2016 based on yearly contractual rates.

	December 31, 2017			December 31, 2016		
	USD (%)	EUR (%)	TL (%)	USD (%)	EUR (%)	TL (%)
Assets						
Cash and balances with central banks	1.50	-	9.98	0.49	-	3.31
Loans and advances to banks	1.61	1.92	12.36	0.45	1.36	11.14
Financial assets held for trading	5.36	2.59	12.32	3.69	3.06	9.92
Investment securities	-	-	14.03			
- Available-for-sale	5.32	4.02	13.05	5.46	4.31	9.59
- Held-to-maturity	5.35	1.67	13.35	5.40	2.97	9.46
Loans and advances to customers	6.43	4.33	14.15	5.90	4.27	13.18
Liabilities						
Deposits from banks	3.26	1.55	13.36	1.62	0.87	10.58
Customer deposits	3.41	1.59	13.42	2.87	1.55	10.74
Debt securities in issue	4.66	1.77	14.00	4.45	2.14	8.00
Funds borrowed	3.17	1.48	13.22	2.49	1.21	8.95

C. Liquidity risk

Liquidity risk is defined as the risk of unexpected loss occurring or the Group having difficulties in raising funds while meeting maturing liabilities. Liquidity management is daily monitored by the Bank under Treasury Management, Risk Management and Capital Management. The liquidity policy of the Group is approved by the Bank’s Board of Directors. Treasury Management is responsible for carrying out transactions which are appropriate to Bank’s policy, monitoring of liquidity position and submitting necessary reports to executives. Capital management contributes to determining strategies and operating actions for the management of the liquidity position in addition to preparing funding plans and contingency plans for the Bank in cooperation with Treasury Management. Liquidity risk is evaluated with liquidity gap analysis, liquidity stress tests and supplementary precautions/measurements. Liquidity Gap analysis is performed for two different periods as short-term and long-term. Going concern scenario and structural positions are reported monthly. This reporting constitutes the basis of monitoring and management of liquidity position.

The Bank functions as a central funding institution in its relations with its subsidiaries. Intra-group liquidity management and funding strategies are limited to related legal boundaries.

The Bank issues an annual funding plan in order to sustain funding in a consistent and balanced way. Funding plans have to be updated at least annually and approved by the Executive Committee since they comply with the budgeting process and risk appetite frameworks. The primary purpose of the funding plan is to provide a reliable balance between assets and liabilities.

Both short-term liquidity and long-term (structural) liquidity measurement and reporting for all types of currencies are periodically made for the Bank and its subsidiaries. There are limits which are predetermined and approved by the Board of Directors on the basis of all currencies for each period.

The Bank mainly uses derivative transactions for managing liquidity risk and monitors cash inflow and outflow periods in the framework of funding plan, balancing the distribution among currencies.

The Bank aims to reduce the risks to the lowest level if required via measuring possible risks in liquidity with stress tests. Stress tests make it possible for the Bank to reinterpret the analysis of its liquidity position according to scenarios depending on possible cases and tail risks except for crisis situations. The bank applies weekly liquidity stress tests consisting of different scenarios and maturity segments (maximum 60 days).

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

"Liquidity Contingency Plan" is applied if the Bank needs more liquidity than its daily liquidity need because of possible financial events in future. Duties and responsibilities are defined in detail in the aforementioned plan.

Cash, effective money, cheques, CBRT reserves and debt instruments issued by Treasury of the Republic of Turkey are treated as high quality liquid assets.

Cash outflows from derivative transactions in liquidity coverage ratio calculation are based on inclusion of net cash flows with maturity of 30 days in the calculation. Additionally, transactions having a margin possibility are included in the liquidity coverage ratio calculation by taking the largest amount according to absolute value of net margin flows realized in the last 24 months in respect of 30 day periods or for liability into consideration as cash outflow.

Secured funding consists of repo and secured loan transactions. A large part of securities which are subjects of aforementioned guaranteed funding transactions consist of Sovereign Bonds issued by Treasury of the Republic of Turkey and transactions carried out both in the CBRT market and the interbank market.

The Bank manages all the transactions made by its foreign branches and partnerships within the framework of central bank, markets and related legislation of the country in which the institutions are located. Legal lending limits and high limit transactions are closely monitored in this framework.

The following table presents the cash flows payable by the Group under non-derivative financial liabilities by remaining contractual maturities at the statement of financial position date. The amounts disclosed in the table are the contractual undiscounted cash flows, whereas the Group manages the inherent liquidity risk based on expected undiscounted cash inflows.

December 31, 2017 (1)

	Demand	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
Liabilities						
Deposits from banks	636,676	17,316,188	723,493	5	-	18,676,362
Customer deposits	31,268,837	122,350,431	8,854,821	1,498,071	168,085	164,140,245
Funds borrowed	-	10,006,807	24,990,609	14,476,519	3,515,868	52,989,803
Debt securities in issue	-	2,688,638	3,600,160	13,462,996	4,747,978	24,499,772
Financial liabilities designated at fair value	-	-	-	1,167,408	3,384,690	4,552,098
Total liabilities	**31,905,513**	**152,362,064**	**38,169,083**	**30,604,999**	**11,816,621**	**264,858,280**

(1) Maturities of non-cash loans are presented in Note 36.

December 31, 2016 (1)

	Demand	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
Liabilities						
Deposits from banks	613,650	12,279,872	899,303	336,087	-	14,128,912
Customer deposits	26,568,606	115,649,679	10,394,976	737,892	133,707	153,484,860
Funds borrowed	631,321	3,895,532	20,356,226	9,978,398	7,012,611	41,874,088
Debt securities in issue	-	4,945,960	1,528,104	7,433,015	6,977,915	20,884,994
Financial liabilities designated at fair value	-	-	-	-	4,111,709	4,111,709
Total liabilities	**27,813,577**	**136,771,043**	**33,178,609**	**18,485,392**	**18,235,942**	**234,484,563**

(1) Maturities of non-cash loans are presented in Note 36.

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

The following table represents the outstanding derivative cash flows of the Group on undiscounted contractual maturity basis:

Derivatives settled on a gross basis

December 31, 2017	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Derivatives held for trading:						
Foreign exchange derivatives:						
- Outflow	73,786,086	46,817,805	23,276,455	6,625,121	1,030,178	151,535,645
- Inflow	75,846,160	51,253,705	24,738,200	6,463,673	846,696	159,148,434
Interest rate derivatives:						
- Outflow	669,560	594,136	9,158,103	8,232,749	1,830,085	20,484,633
- Inflow	750,102	690,492	9,262,990	8,234,663	1,929,969	20,868,216
Derivatives held for hedging:						
Interest rate derivatives:						
- Outflow	-	298	161,701	8,339,702	1,203,938	9,705,639
- Inflow	-	479	185,790	10,018,496	1,393,891	11,598,656
Total cash outflow	**74,455,646**	**47,412,239**	**32,596,259**	**23,197,572**	**4,064,201**	**181,725,917**
Total cash inflow	**76,596,262**	**51,944,676**	**34,186,980**	**24,716,832**	**4,170,556**	**191,615,306**

December 31, 2016	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Derivatives held for trading:						
Foreign exchange derivatives:						
- Outflow	37,966,130	11,712,061	7,618,486	4,998,165	1,119,622	63,414,464
- Inflow	37,239,353	12,515,376	7,694,496	4,988,083	897,480	63,334,788
Interest rate derivatives:						
- Outflow	1,036,566	1,220,093	2,297,963	4,501,645	1,099,360	10,155,627
- Inflow	1,152,652	1,263,626	2,175,157	4,910,633	1,212,872	10,714,940
Derivatives held for hedging:						
Interest rate derivatives:						
- Outflow	-	798	244,986	5,358,265	1,430,802	7,034,851
- Inflow	-	987	436,900	6,189,067	1,848,103	8,475,057
Total cash outflow	**39,002,696**	**12,932,952**	**10,161,435**	**14,858,075**	**3,649,784**	**80,604,942**
Total cash inflow	**38,392,005**	**13,779,989**	**10,306,553**	**16,087,783**	**3,958,455**	**82,524,785**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

D. Operational risk

Operational risk is defined as the risk of losses due to errors, infringements, interruptions, damages caused by internal processes or personnel or systems or caused by external events. Legal and compliance risk is a sub-category of operational risk: it is the risk to earnings from violations or noncompliance with laws, rules, regulations, agreements, prescribed practices or ethical standards. The Operational Risk Management department ("ORM") monitors the Group's operational risk exposure in accordance with standards and policies, collects operational risk data in a web-based database, performs the risk indicators' identification, the scenario analysis assessment, Business Continuity Management and assures the quality of data gathered in accordance with Basel II standards, proposes insurance hedging on operational risks and prepares risk mitigation plans. ORM performs second level controls and, manages and measures the Group's operational risks.

For regulatory purposes and consideration in the statutory capital adequacy ratio, on a consolidated basis, the Group calculates the amount subject to operational risk with the basic indicator method in accordance with Section 3 of the " Regulation Regarding Measurement and Evaluation of Banks' Capital Adequacy Ratio" published in the Official Gazette No. 28337 dated June 28, 2012, namely "The Calculation of the Amount Subject to Operational Risk", based on the gross income of the Group for the years ended 2016, 2015 and 2014. As of December 31, 2017, the total amount subject to operational risk is calculated as TL 18,068,782 (2016 - TL 14,338,007) and the amount of the related capital requirement is TL 1,445,503 (2016 - TL 1,147,041).

E. Capital management

Banks in Turkey are required to comply with capital adequacy guidelines promulgated by the BRSA, which are based upon the standards established by the Bank of International Settlements ("BIS"). These guidelines require banks to maintain adequate levels of regulatory capital against risk-bearing assets and off-statement of financial position exposures.

A bank's capital adequacy ratio is calculated by taking the aggregate of its Tier I capital (which comprises paid-in capital, reserves, retained earnings and profit for the current periods minus period loss (if any) its Tier II capital (which comprises general loan and free reserves, revaluation funds and subordinated loans obtained) and its Tier III capital (which comprises certain qualified subordinated loans in accordance with regulatory guidelines) minus deductions (which comprises participations to financial institutions, negative differences between fair and book values of subsidiaries, subordinated loans extended, goodwill and capitalized costs), and dividing this aggregate by risk weighted assets, which reflect both credit risk and market risk. In accordance with these guidelines, banks must maintain a total capital adequacy ratio of a minimum of 12%.

The Group's regulatory capital adequacy position on a consolidated basis at December 31, 2017 and 2016 was as follows:

	December 31, 2017	**December 31, 2016**
Tier I capital	26,637,913	23,388,409
Tier II capital	9,633,807	9,315,485
Deductions	(139,084)	(219,529)
Total regulatory capital	36,132,636	32,484,365
Risk-weighted assets (including market and operational risk)	270,278,292	246,436,668
Capital adequacy ratio (%)	**13.37**	**13.18**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

F. Fair value of financial instruments

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

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

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

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

The Group did not recognise any transfers between levels of the fair value hierarchy during the year.

The following is a description of the determination of fair value for financial instruments which are recorded at fair value using valuation techniques. These incorporate the Group's estimate of assumptions that a market participant would make when valuing the instruments.

Set out below is a comparison, by class, of the carrying amounts and fair values of the Bank's financial instruments that are not carried at fair value in the financial statements.

	December31, 2017		December31, 2016	
	Carrying value	**Fair value**	**Carrying value**	**Fair value**
Financial assets:				
Loans and advances to banks	5,654,217	5,657,535	3,449,218	3,450,512
Investment securities (held-to-maturity)	14,197,066	13,929,233	11,588,890	10,981,828
Loans and advances to customers	215,105,383	223,141,049	188,980,851	196,517,296
Financial liabilities:				
Deposits from banks	18,676,359	18,689,753	13,811,243	13,824,168
Customer deposits	164,133,655	165,068,710	149,550,753	150,432,741
Funds borrowed	52,975,912	53,016,145	37,167,753	37,188,838
Debt securities in issue	24,452,247	24,545,288	19,308,899	19,391,711

The estimated fair values of financial instruments have been determined by the Group using available market information and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to develop the estimated fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Group could realize in a current market exchange.

4. Financial risk management (continued)

The fair value of overnight deposits is considered to approximate their carrying amounts. The estimated fair value of interest bearing placements is based on discounted cash flows using prevailing money market interest rates at the statement of financial position date with similar credit risk and remaining maturity.

Loans and advances to customers

Loans and advances to customers are net of allowances for impairment. The estimated fair value of loans and advances to customers represent the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates with similar currency and remaining maturity to determine their fair value. The credit risk is not considered when calculating the fair value of loans and advances to customers as in line with the pricing of such loans.

Investment securities

Fair value for held-to-maturity securities is based on market prices or prices prevailing at the statement of financial position date announced by the BIST.

Customer deposits, deposits from banks, funds borrowed and debt securities in issue

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand.

The estimated fair value of other borrowings without quoted market price is based on discounted cash flows using money market interest rates prevailing at the statement of financial position date with similar credit risk, currency and remaining maturity. The fair value of debt securities in issue is considered to approximate its carrying amount.

Derivatives

Derivative products valued using a valuation technique with market observable inputs are mainly interest rate swaps, currency swaps and forward foreign exchange contracts. The most frequently applied valuation techniques include forward pricing and swap models, using present value calculations. The models incorporate various inputs including the credit quality of counterparties, foreign exchange spot and forward rates and interest rate curves.

Financial investments - available-for-sale

Available-for-sale financial assets valued using a valuation technique or pricing models primarily consist of unquoted equities and debt securities.

These assets are valued using models which sometimes only incorporate data observable in the market and at other times use both observable and non-observable data. The non-observable inputs to the models include assumptions regarding the future financial performance of the investee, its risk profile, and economic assumptions regarding the industry and geographical jurisdiction in which the investee operates.

Other liabilities designated at fair value through profit or loss

For unquoted notes issued, a discounted cash flow model is used based on a current interest rate yield curve appropriate for the remaining term to maturity adjusted for market liquidity and own credit spreads.

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

Determination of fair value and fair value hierarchy:

IFRS 7 requires classification of line items at fair value presented in the financial statements according to defined levels. These levels depend on the observability of data used during fair value calculations. Classification for fair value is as below:

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

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

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

Assets and liabilities measured at fair value

December 31, 2017	Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit and loss				
Financial assets held for trading				
- Debt securities	56,980	-	-	56,980
- Equity securities	45,607	-	-	45,607
- Derivatives	-	4,109,547	-	4,109,547
Hedging derivatives	-	1,756,611	-	1,756,611
Available-for-sale financial assets				
- Investments securities - debt	22,338,660	1,815,229	-	24,153,889
- Investments securities - equity	96,006	66,251	-	162,257
Total assets	**22,537,253**	**7,747,638**	**-**	**30,284,891**
Financial liabilities at fair value through profit or loss				
- Derivatives	-	3,820,705	-	3,820,705
- Financial Liabilities designated at fair value	-	4,363,503	-	4,363,503
Hedging derivatives	-	312,778	-	312,778
Total liabilities	**-**	**8,496,986**	**-**	**8,496,986**

(Amounts expressed in thousands of TL unless otherwise indicated.)

4. Financial risk management (continued)

December 31, 2016	Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit and loss				
Financial assets held for trading				
- Debt securities	36,713	-	-	36,713
- Equity securities	6,652	-	-	6,652
- Derivatives	-	2,986,773	-	2,986,773
Hedging derivatives	-	1,209,712	-	1,209,712
Available-for-sale financial assets				
- Investments securities - debt	16,052,373	2,053,629	-	18,106,002
- Investments securities - equity	60,849	50,455	-	111,304
Total assets	**16,156,587**	**6,300,569**	**-**	**22,457,156**
Financial liabilities at fair value through profit or loss				
- Derivatives	-	2,578,679	-	2,578,679
- Financial Liabilities designated at fair value	-	3,938,694	-	3,938,694
Hedging derivatives	-	89,296	-	89,296
Total liabilities	**-**	**6,606,669**	**-**	**6,606,669**

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

In the current year, there was no transfer between Level 1 and Level 2.

The fair value amounts of the Bank’s financial instruments disclosed in this note that are not carried at fair value in the financial statements are categorised in Level 2 in the fair value hierarchy except investment securities (held-to-maturity) which are categorised in Level 1.

G. Custody activities

The Group provides custody services to third parties. Those assets that are held in a custody capacity are not included in these consolidated financial statements. The fiduciary capacity of the Group is as follows:

	December 31, 2017	December 31, 2016
Investment securities held in custody	9,282,477	7,522,109
Cheques received for collection	17,432,784	15,989,409
Commercial notes received for collection	5,279,251	5,162,899
	31,994,512	**28,674,417**

(Amounts expressed in thousands of TL unless otherwise indicated.)

5. Cash and cash equivalents for the purpose of presentation in the consolidated statement of cash flows

For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances with less than three months maturity from the date of acquisition:

	December 31, 2017	December 31, 2016
Cash and cash equivalents	2,562,063	2,701,613
Balances with central banks	39,889,907	30,381,682
Reserve deposits with central banks (-)	(23,877,428)	(20,067,325)
Loans and advances to banks (with original maturity less than 90 days) (+)	5,269,737	2,943,042
Other cash equivalents (+)	378,848	202,950
Total cash and cash equivalents at cash flow statement	**24,223,127**	**16,161,962**

The Bank keeps TL, USD, EUR and Gold reserve deposits for its TL and FX liabilities at the Central Bank Accounts in accordance with the legislation of the Central Bank numbered 2005/1, “Decree on Reserve Deposits”.

Foreign reserve requirements:

Reserve requirements of De Nederlandsche Bank and the Central Bank of Malta are determined in relation to the reserve base of each institution, which are defined in relation to elements of its balance sheet. A reserve ratio of 0% shall apply to deposits with an agreed maturity over two years or deposits redeemable at notice over 2 years, or repos and debt securities issued with an original maturity over two years. A reserve ratio of 1% shall apply to all other liabilities included in the reserve base. Credit institutions established in the euro area may deduct a uniform lump-sum allowance from its reserve requirement. As specified in the European Central Bank Regulation on minimum reserves, the lump-sum allowance amounts to EUR 100,000.

Reserve requirements of the National Bank of Azerbaijan represent reserve deposits equivalent to 0.5% (for AZN liabilities), 1.0% (for foreign currency liabilities) of the statutory balances of customer accounts, due to banks and other funds borrowed.

(Amounts expressed in thousands of TL unless otherwise indicated.)

6. Loans and advances to banks

	December 31, 2017			December 31, 2016		
	Domestic	**Foreign**	**Total**	**Domestic**	**Foreign**	**Total**
TL:						
Nostro / demand deposits	4,190	7	4,197	2,448	13	2,461
Time deposits	64,169	13,517	77,686	39,876	800	40,676
Interbank money market and reverse repo	4,215	-	4,215	252	-	252
	72,574	**13,524**	**86,098**	**42,576**	**813**	**43,389**
Foreign currency:						
Nostro/ demand deposits	30,510	1,274,099	1,304,609	23,835	1,400,310	1,424,145
Time deposits	1,804,469	1,646,251	3,450,720	1,697,437	284,247	1,981,684
Interbank money market and reverse repo	812,790	-	812,790	-	-	-
	2,647,769	**2,920,350**	**5,568,119**	**1,721,272**	**1,684,557**	**3,405,829**
Total loans and advances to banks	**2,720,343**	**2,933,874**	**5,654,217**	**1,763,848**	**1,685,370**	**3,449,218**

7. Financial assets held for trading

	December 31, 2017	**December 31, 2016**
Government bonds and treasury bills	56,980	36,713
Total debt securities	**56,980**	**36,713**
Equity securities – listed	45,607	6,652
Total equity securities	**45,607**	**6,652**
Total securities	**102,587**	**43,365**
Derivative financial instruments	4,109,547	2,986,773
Total financial assets held for trading	**4,212,134**	**3,030,138**

Government bonds and treasury bills are discount and coupon securities issued by the Government of the Republic of Turkey.

8. Derivative financial instruments and hedging activities

The Group utilizes the following derivative instruments with the general purpose of minimising market risk carried by balance sheet instruments and/or meeting customer demand:

"Currency forwards" represent commitments to purchase or sell foreign and domestic currency, including undelivered spot transactions. Forwards are customized contracts transacted in the over-the-counter (OTC) market. The Group has credit exposure to the counterparties of forward contracts.

"Currency and interest rate swaps" are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or interest rates. Currency swaps involve the exchange of the principal as well. The Group's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligation. This risk is monitored on an ongoing basis with reference to the current fair value and the liquidity of the market. To control the level of risk taken, the Group assesses counterparties using the same techniques as for its lending activities.

"Options" are contractual agreements that convey the right to the buyer and the obligation to the writer to buy or sell an asset at a specified price either at a fixed future date or at any time within a specified period. A major part of the Group's option book activity stems from clients' needs; therefore to meet client demands the Group actively runs an option book on the residual open positions which are not fully covered. The Group is exposed to credit risk on purchased options only, and only to the extent of their carrying amount, which is their fair value.

"Interest rate cap and floor arrangements" provide the purchaser with the right to receive interest rate differential payments on a notional amount when the indexed rate is in excess of the specified cap rate and limits the benefit of reductions in interest rates if it occurs.

Credit derivatives are capital market tools designed to transfer credit risk from one party to another.

As of December 31, 2017, the Bank's credit derivatives portfolio is composed of "credit linked notes" (embedded derivatives are separated from host contract in line with IAS 39 and recorded as credit default swaps). Credit default swaps are contracts, in which the seller commits to pay the contract value to the buyer in case of certain credit risk events in return for the premium paid by the buyer for the contract. Credit linked notes are valued monthly.

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognized on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments, and therefore, do not indicate the Group's exposure to credit or price risks. Derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in foreign exchange rates and interest rates relative to their terms.

(Amounts expressed in thousands of TL unless otherwise indicated.)

8. Derivative financial instruments and hedging activities (continued)

December 31, 2017

	Contract/ notional amount (aggregate of buy and sell)	Assets	Fair values Liabilities
Derivatives held for trading			
Foreign exchange derivatives:			
Currency forwards	26,814,743	396,773	132,547
Currency swaps	203,863,781	2,375,930	2,394,042
Over the counter ("OTC") currency options	23,957,338	193,006	198,930
Total OTC foreign exchange derivatives	**254,635,862**	**2,965,709**	**2,725,519**
Interest rate derivatives:			
Interest rate swaps	54,129,790	321,291	219,065
Cross-currency interest rate swaps	17,809,770	726,811	866,889
OTC interest rate options	2,121,644	971	8,961
Total OTC interest rate derivatives	**74,061,204**	**1,049,073**	**1,094,915**
Other derivatives	**21,267,164**	**94,765**	**271**
Total derivative assets/ liabilities held for trading	**349,964,230**	**4,109,547**	**3,820,705**
Derivatives used for hedging			
Derivatives designated as fair value hedges:			
Cross-currency interest rate swaps	3,295,553	68,216	205,211
Derivatives designated as cash flow hedges:			
Interest rate swaps and cross currency interest rate swaps	70,586,749	1,688,395	107,567
Total derivative assets/ liabilities used for hedging	**73,882,302**	**1,756,611**	**312,778**
Total recognized derivative assets/ liabilities	**423,846,532**	**5,866,158**	**4,133,483**
Current		2,895,900	2,697,382
Non-current		2,970,258	1,436,101
Total recognized derivative assets/ liabilities	**423,846,532**	**5,866,158**	**4,133,483**

(Amounts expressed in thousands of TL unless otherwise indicated.)

8. Derivative financial instruments and hedging activities (continued)

December 31, 2016

	Contract/ notional amount (aggregate of buy and sell)	Assets	Fair values Liabilities
Derivatives held for trading			
Foreign exchange derivatives:			
Currency forwards	15,273,549	339,654	195,859
Currency swaps	92,020,096	1,280,801	1,219,902
Over the counter ("OTC") currency options	17,590,138	116,930	120,103
Total OTC foreign exchange derivatives	**124,883,783**	**1,737,385**	**1,535,864**
Interest rate derivatives:			
Interest rate swaps	47,580,058	337,089	220,099
Cross-currency interest rate swaps	13,076,180	905,910	718,859
OTC interest rate options	1,671,894	4,401	5,368
Total OTC interest rate derivatives	**62,328,132**	**1,247,400**	**944,326**
Other derivatives	**18,267,410**	**1,988**	**98,489**
Total derivative assets/ liabilities held for trading	**205,479,325**	**2,986,773**	**2,578,679**
Derivatives used for hedging			
Derivatives designated as fair value hedges:			
Cross-currency interest rate swaps	2,658,411	246,295	50,457
Derivatives designated as cash flow hedges:			
Interest rate swaps	50,014,021	963,417	38,839
Total derivative assets/ liabilities used for hedging	**52,672,432**	**1,209,712**	**89,296**
Total recognized derivative assets/ liabilities	**258,151,757**	**4,196,485**	**2,667,975**
Current		1,969,924	2,207,260
Non-current		2,226,561	460,715
Total recognized derivative assets/ liabilities	**258,151,757**	**4,196,485**	**2,667,975**

Fair value hedges

Starting from March 1, 2009 and July 28, 2015 for marketable securities, the Group has hedged the possible fair value effects of changes in market interest rates on part of its fixed interest TL mortgage, car loan portfolios and marketable securities and fair value effects of changes in foreign exchange rates on part of its foreign currency denominated funding and marketable securities by using cross-currency interest rate swaps. The net carrying value of hedging derivatives at December 31, 2017 is a liability amounting to TL 204,859 (2016 - asset TL 195,838). At December 31, 2017, the marked to market difference of the hedging derivatives is TL 4,381 gain (2016 - TL 29,485 gain), the fair value difference of the hedged items is asset TL 23,425 (2016 – asset TL 4,334) and their changes in the fair value for the year amounts to asset TL 19,091 (2016 - asset TL 14,710).

(Amounts expressed in thousands of TL unless otherwise indicated.)

8. Derivative financial instruments and hedging activities (continued)

Cash flow hedges

The Group is exposed to variability in future interest cash flows on non-trading assets and liabilities which bear interest at a variable rate. The Group uses interest rate swaps as cash flow hedges of these interest rate risks.

In order to hedge its cash flow risk from liabilities, the Group started to apply cash flow hedge accounting from January 1, 2010 onwards. The hedging instruments are USD, EUR and TL interest rate swaps and cross currency swaps with floating receive, fixed pay legs, and the hedged item is the cash outflows due to variable interest payments subject to repricing USD, EUR and TL customer deposits, repos and borrowings.

Net loss on cash flow hedges reclassified to the statement of income

The net loss on cash flow hedges reclassified to the statement of income during the twelve month period ended December 31, 2017 was as follows:

	December 31, 2017	**December 31, 2016**
Net interest income /expense	272,787	(44,407)
Taxation	60,013	8,881

During 2017, a gain of TL 6,987 (2016 - TL 5,290 gain) was recognized in the statement of income due to hedge ineffectiveness from cash flow hedges.

As of December 31, 2017 the net accumulated gain arising from cash flow hedges recognized under equity, net of reclassification to statement of income and net of tax, is TL 836,691 (2016 – TL 379,149 loss).

Net investment hedges

The Group hedges part of the currency translation risk of net investments in foreign operations through foreign currency borrowings.

The Group's Euro denominated borrowing is designated as a hedge of the net investment in certain of the Group's EUR denominated subsidiaries. The total amount of the borrowing designated as a hedge of the net investment at December 31, 2017 is EUR 410 million (2016 - EUR 386 million). The foreign exchange loss of TL 718,766 (December 31, 2016 - TL 473,112 loss), net of tax, on translation of the borrowing to TL at the statement of financial position date is recognized in "hedging reserves" in equity.

No ineffectiveness from hedges of net investments in foreign operations was recognized in profit or loss during the period (2016 - None).

(Amounts expressed in thousands of TL unless otherwise indicated.)

9. Loans and advances to customers

December 31, 2017

	Corporate	Consumer	Credit cards	Leasing	Factoring	Total
Performing loans	136,714,452	33,559,109	23,999,186	9,986,409	3,664,159	207,923,315
Watch listed loans	4,194,521	967,131	356,255	202,260	170,878	5,891,045
Loans under legal follow - up	6,313,080	1,637,933	1,128,584	340,768	110,676	9,531,041
Gross	**147,222,053**	**36,164,173**	**25,484,025**	**10,529,437**	**3,945,713**	**223,345,401**
Specific allowance for impairment	(5,167,100)	(1,108,429)	(799,470)	(219,774)	(102,546)	(7,397,319)
Collective allowance for impairment	(573,573)	(176,934)	(33,077)	(48,990)	(10,125)	(842,699)
Total allowance for impairment	**(5,740,673)**	**(1,285,363)**	**(832,547)**	**(268,764)**	**(112,671)**	**(8,240,018)**
Net	**141,481,380**	**34,878,810**	**24,651,478**	**10,260,673**	**3,833,042**	**215,105,383**

December 31, 2016

	Corporate	Consumer	Credit cards	Leasing	Factoring	Total
Performing loans	118,698,015	29,912,146	21,780,057	7,966,725	2,709,393	181,066,336
Watch listed loans	4,369,279	1,165,790	466,554	279,550	174,064	6,455,237
Loans under legal follow - up	4,934,745	2,181,464	1,648,934	335,655	141,420	9,242,218
Gross	**128,002,039**	**33,259,400**	**23,895,545**	**8,581,930**	**3,024,877**	**196,763,791**
Specific allowance for impairment	(3,915,130)	(1,429,889)	(1,036,735)	(280,296)	(130,598)	(6,792,648)
Collective allowance for impairment	(723,062)	(173,531)	(44,164)	(39,409)	(10,126)	(990,292)
Total allowance for impairment	**(4,638,192)**	**(1,603,420)**	**(1,080,899)**	**(319,705)**	**(140,724)**	**(7,782,940)**
Net	**123,363,847**	**31,655,980**	**22,814,646**	**8,262,225**	**2,884,153**	**188,980,851**

Loans amounting to TL 1,016,716 (at amortized cost) included in the performing loans and advances to consumers have been designated as hedged items in fair value hedges as of December 31, 2017 (2016 - TL 163,861). Those loans have been hedged with interest rate swaps as part of a documented interest rate risk management strategy. The carrying values of such loans that are hedged items in fair value hedges, and otherwise carried at amortized cost, are adjusted to record changes in fair value attributable to the risks that are being hedged.

Fair value of collateral:

Collateral mainly comprises the following: cash funds, deposits, mortgages of real estate at the land registry and mortgages of real estate built on allocated land, export documents, guarantees, and acceptances and pledge on vehicles.

December 31, 2017

	Corporate	Consumer	Leasing	Total
Watch listed loans	8,283,959	988,733	336,250	9,608,942
Loans under legal follow - up	1,157,265	94,729	341,611	1,593,605
Total	**9,441,224**	**1,083,462**	**677,861**	**11,202,547**

(Amounts expressed in thousands of TL unless otherwise indicated.)

9. Loans and advances to customers (continued)

December 31, 2016

	Corporate	Consumer	Leasing	Total
Watch listed loans	8,309,903	998,699	279,550	9,588,152
Loans under legal follow - up	1,173,649	100,758	335,655	1,610,062
Total	**9,483,552**	**1,099,457**	**615,205**	**11,198,214**

Reconciliation of impairment allowance account for losses on loans and advances by class is as follows:

						December 31, 2017
	Corporate	**Consumer**	**Credit cards**	**Leasing**	**Factoring**	**Total**
At January 1	**4,638,192**	**1,603,420**	**1,080,899**	**319,705**	**140,724**	**7,782,940**
Provision for loan impairment	1,669,687	453,908	332,963	82,962	24,249	2,563,769
Amounts recovered during the year	(294,026)	(5,449)	(2,782)	(24,170)	(298)	(326,725)
Loans written off during the year as uncollectible (-) (1), (2)	(290,340)	(775,502)	(579,312)	(109,733)	(52,004)	(1,806,891)
Exchange differences	17,160	8,986	779	-	-	26,925
At December 31	**5,740,673**	**1,285,363**	**832,547**	**268,764**	**112,671**	**8,240,018**

						December 31, 2016
	Corporate	**Consumer**	**Credit cards**	**Leasing**	**Factoring**	**Total**
At January 1	**3,118,983**	**1,144,241**	**731,987**	**276,807**	**115,088**	**5,387,106**
Provision for loan impairment	1,659,568	589,705	405,970	57,262	26,873	2,739,378
Amounts recovered during the year	(149,981)	(134,352)	(57,565)	(14,364)	(906)	(357,168)
Loans written off during the year as uncollectible (-) (1)	(111)	(498)	(4)	-	(331)	(944)
Exchange differences	9,733	4,324	511	-	-	14,568
At December 31	**4,638,192**	**1,603,420**	**1,080,899**	**319,705**	**140,724**	**7,782,940**

(1) Includes the effect of provision releases due to sales from loans under legal follow – up.
(2) Includes the effect of the sale of a subsidiary amounting to TL 16,663 in total.

(Amounts expressed in thousands of TL unless otherwise indicated.)

9. Loans and advances to customers (continued)

The calculation of net investment in direct finance leases is as follows:

	December 31, 2017	December 31, 2016
Gross investment in direct finance leases	12,158,132	9,786,865
Unearned finance income	(1,875,090)	(1,529,623)
	10,283,042	**8,257,242**
Interest accrual on receivables	213,117	120,146
Receivables from outstanding lease payments	33,278	204,542
Provision for impaired lease receivables	(268,764)	(319,705)
Net investment in direct finance leases	**10,260,673**	**8,262,225**

Lease payments receivable consists of rentals over the terms of leases. The rentals according to maturity are as follows:

	December 31, 2017	December 31, 2016
Less than 1 year	4,044,078	2,798,694
More than 1 year but not later than 5 years	6,924,141	5,736,824
Later than 5 years	893,280	960,830
Less: unearned finance income	(1,875,090)	(1,529,623)
Investment in performing lease receivables	**9,986,409**	**7,966,725**

(Amounts expressed in thousands of TL unless otherwise indicated.)

10. Investment securities

(i) Securities available-for-sale

	December 31, 2017	December 31, 2016
Debt securities - at fair value:		
Government bonds and treasury bills	14,016,100	10,796,625
Eurobonds	1,534,189	1,602,741
Government and corporate bonds and treasury bills sold under repurchase agreements	6,937,612	3,651,723
Eurobonds sold under repurchase agreements	-	-
Other	1,665,988	2,054,913
Equity securities - at fair value:		
Listed	96,006	60,849
Unlisted	66,251	50,455
Total securities available-for-sale	**24,316,146**	**18,217,306**
Current	1,596,015	973,154
Non-current	22,720,131	17,244,152

Government bonds, treasury bills and Eurobonds are discount and coupon securities issued by the Government of the Republic of Turkey. Other securities mainly represent A and B type open-ended mutual funds incorporated in Turkey managed by the Group and credit linked notes and other bonds issued by domestic and foreign financial institutions.

Net loss from changes in the fair value of available-for-sale investment securities, net of tax is TL 334,822 loss (2016 - TL 178,462 net loss). There are no impairments recognized for available-for-sale debt securities.

The movement in available-for-sale securities during the years is as follows:

	December 31, 2017	December 31, 2016
At January 1	**18,217,306**	**22,703,163**
Additions	17,733,200	14,426,408
Disposals / redemption	(11,581,249)	(16,765,939)
Sale of a subsidiary	(21,196)	-
Transfer(1)	-	(1,960,740)
Changes in fair value	(36,899)	(194,340)
Exchange differences on monetary assets	4,984	8,754
At December 31	**24,316,146**	**18,217,306**

(1) On July 18, 2016, the Group classified some of its government debt securities from available-for-sale to held-to-maturity portfolio with a nominal amount of TL 1,970,607. The fair value of the aforementioned securities as of July 18, 2016 is TL 2,008,079 and has 8 years maturity in average.

(Amounts expressed in thousands of TL unless otherwise indicated.)

10. Investment securities (continued)

(ii) Securities held-to-maturity

	December 31, 2017	December 31, 2016
Debt securities - at amortized cost - listed:		
Government bonds and treasury bills	5,076,365	3,829,504
Eurobonds	6,021,237	3,969,341
Government bonds and treasury bills sold under repurchase agreements	2,002,802	1,099,964
Eurobonds sold under repurchase agreement	737,714	1,890,245
Foreign government bonds	358,948	799,836
Total securities held-to-maturity	**14,197,066**	**11,588,890**
Current	1,232,399	1,127,845
Non-current	12,964,667	10,461,045

The movement in held-to-maturity securities during the years is as follows:

	December 31, 2017	December 31, 2016
At January 1	**11,588,890**	**7,108,809**
Additions	3,231,152	1,703,125
Redemptions	(1,381,405)	(283,389)
Transfer(2)	-	1,960,740
Other(1)	758,429	1,099,605
At December 31	**14,197,066**	**11,588,890**

(1) Includes the effect of exchange differences, impairment and changes in interest income accruals.

(2) On July 18, 2016, the Group classified some of its government debt securities from available-for-sale to held-to-maturity portfolio with a nominal amount of TL 1,970,607. The fair value of the aforementioned securities as of July 18, 2016 is TL 2,008,079 and has 8 years maturity in average.

11. Investment in associate

	December 31, 2017	December 31, 2016
At January 1	**664,614**	**545,225**
Share of results	87,340	88,099
Dividends paid	(37,487)	(7,645)
Exchange difference	57,558	38,935
At December 31	**772,025**	**664,614**

(Amounts expressed in thousands of TL unless otherwise indicated.)

12. Investment in joint venture valued at net equity

As at December 31, 2017, the Group has one investment in a jointly controlled entity,

	December 31, 2017	December 31, 2016
At January 1	**18,114**	**20,851**
Share of results	272	(2,737)
At December 31	**18,386**	**18,114**

The information about the jointly controlled entity is given below as of December 31, 2017:

	The Parent Bank's shareholding percentage	Group's shareholding percentage	Total assets	Shareholders' equity	Current assets	Non-current assets	Long term debts	Income	Expense
Yapı Kredi Koray Gayrimenkul Yatırım Ortaklığı A.Ş.	30.45	30.45	89,512	69,561	29,967	59,545	8,646	58,265	(55,985)
Total	**30.45**	**30.45**	**89,512**	**69,561**	**29,967**	**59,545**	**8,646**	**58,265**	**(55,985)**

13. Goodwill

	December 31, 2017	December 31, 2016
At January 1	**1,023,528**	**1,023,528**
Impairment charge	-	-
At December 31	**1,023,528**	**1,023,528**

Goodwill is reviewed annually for impairment, or more frequently when there are indications that impairment may have occurred. A +0.25/-0.25% change in discount rate and +1/-1% change in growth rate used in the valuation model does not result in impairment.

The recoverable amount of goodwill has been determined based on value in use calculations, using cash flow projections based on IFRS financial budgets approved by management and on strategic plans covering a five year period. The calculation of value in use ("VIU") is most sensitive to interest margin, discount rates, market share, projected growth rates and local economic indicators.

Discount rates used in the calculations reflect the current market assessment of the Bank's operations. The method for determining the pre-tax discount rate is to first calculate the VIU using post tax cash flows and discount rates, then solving the pre-tax discount rate which gives the same VIU as in the post- tax calculation. The pre-tax discount rate is assumed to be 16% and terminal value is calculated with a long term growth rate of 4%.

Based on the analysis performed, management believes that there is no indication for an impairment for goodwill at December 31, 2017 (2016 - None).

14. Other intangible assets

	December 31, 2017	December 31, 2016
Cost	1,241,289	1,064,686
Accumulated amortization	(538,430)	(477,264)
Net book value	**702,859**	**587,422**

(Amounts expressed in thousands of TL unless otherwise indicated.)

14. Other intangible assets (continued)

Movements of other intangible assets were as follows:

December 31, 2017	Rights and licenses	Software	Trademarks and customer relationships related intangibles	Total
Cost				
At January 1	**385,002**	**516,600**	**163,084**	**1,064,686**
Additions	163,186	96,552	-	259,738
Disposals	(30,247)	(52,566)	-	(82,813)
Sale of a subsidiary	-	(633)		(633)
Transfers	(69,451)	69,451	-	-
Translation differences	(222)	533	-	311
At December 31	**448,268**	**629,937**	**163,084**	**1,241,289**
Accumulated amortization				
At January 1	**(66,689)**	**(247,491)**	**(163,084)**	**(477,264)**
Amortization charge (Note 32)	(27,955)	(108,165)	-	(136,120)
Disposals	30,094	42,480	-	72,574
Sale of a subsidiary	-	588		588
Transfers	69,451	(69,451)	-	-
Translation differences	689	1,103	-	1,792
At December 31	**5,590**	**(380,936)**	**(163,084)**	**(538,430)**
Net book value at December 31	**453,858**	**249,001**	**-**	**702,859**

December 31, 2016	Rights and licenses	Software	Trademarks and customer relationships related intangibles	Total
Cost				
At January 1	**325,337**	**456,923**	**163,084**	**945,344**
Additions	122,113	57,587	-	179,700
Disposals	(18,834)	(41,654)	-	(60,488)
Transfers	(44,001)	44,001	-	-
Translation differences	387	(257)	-	130
At December 31	**385,002**	**516,600**	**163,084**	**1,064,686**
Accumulated amortization				
At January 1	**(60,667)**	**(192,682)**	**(163,084)**	**(416,433)**
Amortization charge (Note 32)	(27,574)	(97,147)	-	(124,721)
Disposals	18,682	41,578	-	60,260
Transfers	-	-	-	-
Translation differences	2,870	760	-	3,630
At December 31	**(66,689)**	**(247,491)**	**(163,084)**	**(477,264)**
Net book value at December 31	**318,313**	**269,109**	**-**	**587,422**

The Group assigned a consultancy firm for the valuation of intangible assets determined as a credit card trademark, customer base and relationship that could be measured reliably and for which the future economic benefit is embodied in the asset during the merger of the Bank with Koçbank. In line with the report dated February 13, 2006 the Group recognized TL 163,084 of intangible assets in its consolidated financial statements. Identified intangible assets are amortized using the straight-line method over their useful lives, which have been assessed as 10 years.

(Amounts expressed in thousands of TL unless otherwise indicated.)

15. Property and equipment

	December 31, 2017	December 31, 2016
Cost	3,963,120	4,005,753
Accumulated depreciation and impairment	(2,757,017)	(2,738,047)
Net book value	**1,206,103**	**1,267,706**

December 31, 2017	Land and buildings	Office equipment	Furniture and fixtures, vehicles and other	Leasehold improvements	Total
Cost					
At January 1	**2,420,789**	**934,312**	**432,850**	**217,802**	**4,005,753**
Additions	24,012	90,239	19,221	19,383	152,855
Disposals	(11,015)	(54,786)	(54,871)	(37,672)	(158,344)
Sale of a subsidiary	(17,290)	(1,390)	(1,084)	-	(19,764)
Transfers	-	(24,623)	24,703	(80)	-
Translation difference	-	4,323	498	2,858	7,679
At December 31	**2,416,496**	**948,075**	**421,317**	**202,291**	**3,988,179**
Accumulated depreciation and impairment					
At January 1	**(1,739,488)**	**(626,473)**	**(274,157)**	**(97,929)**	**(2,738,047)**
Depreciation charge (Note 32)	(24,135)	(107,792)	(32,809)	(39,492)	(204,228)
Disposals	10,006	54,691	54,580	36,250	155,527
Sale of a subsidiary	9,037	690	827	-	10,554
Transfers	-	24,623	(24,703)	80	-
Reversal of impairment	-	-	-	-	-
Translation difference	-	(3,234)	(824)	(1,824)	(5,882)
At December 31	**(1,744,580)**	**(657,495)**	**(277,086)**	**(102,915)**	**(2,782,076)**
Net book value at December 31	**671,916**	**290,580**	**144,231**	**99,376**	**1,206,103**

December 31, 2016	Land and buildings	Office equipment	Furniture and fixtures, vehicles and other	Leasehold improvements	Total
Cost					
At January 1	**2,363,058**	**901,608**	**418,620**	**230,720**	**3,914,006**
Additions	72,123	108,559	14,701	20,178	215,561
Disposals	(5,591)	(30,142)	(49,695)	(32,128)	(117,556)
Transfers	-	(47,599)	49,879	(2,280)	-
Translation difference	(8,801)	1,886	(655)	1,312	(6,258)
At December 31	**2,420,789**	**934,312**	**432,850**	**217,802**	**4,005,753**
Accumulated depreciation and impairment					
At January 1	**(1,716,644)**	**(585,437)**	**(250,267)**	**(80,607)**	**(2,632,955)**
Depreciation charge (Note 32)	(24,639)	(108,834)	(32,761)	(42,586)	(208,820)
Disposals	4,451	25,250	49,695	22,825	102,221
Transfers	-	47,599	(49,879)	2,280	-
Reversal of impairment	-	-	211	505	716
Translation difference	(2,656)	(5,051)	8,844	(346)	791
At December 31	**(1,739,488)**	**(626,473)**	**(274,157)**	**(97,929)**	**(2,738,047)**
Net book value at December 31	**681,301**	**307,839**	**158,693**	**119,873**	**1,267,706**

At December 31, 2017, total impairment provision on property and equipment of the Parent Bank amounts to TL 239,865 (2016 - TL 239,865).

(Amounts expressed in thousands of TL unless otherwise indicated.)

16. Other assets

	December 31, 2017	December 31, 2016
Collateral given	2,172,956	1,946,017
Prepaid expenses	849,898	709,926
Advances given	610,115	515,089
Miscellaneous receivable	61,758	364,648
Gold stocks	378,848	202,950
Assets held for sale, net	221,923	182,079
Other(1)	1,474,323	1,397,184
	5,769,821	**5,317,893**
Current	5,509,710	5,120,708
Non-current	260,111	197,185

(1) Other line item mainly consists of receivables from clearing houses related with interbank, credit card, payments for credit card settlements and cheque transactions.

Assets held for sale represent mainly foreclosed assets received against uncollectible loans and advances to customers, to be sold as required by the Turkish Banking Law. These assets mainly consist of real-estate. The Group's policy is to dispose of these assets within five years in accordance with Turkish Banking Law, Movements in assets held for resale during the years, were as follows:

	2017	2016
Cost		
At January 1	**188,297**	**177,244**
Additions	154,214	98,410
Disposals	(116,211)	(86,974)
Translation differences	504	(383)
At December 31	**226,804**	**188,297**
Impairment		
At January 1	**(6,218)**	**(8,126)**
Reversal of impairment for the year, net (1)	1,337	1,908
At December 31	**(4,881)**	**(6,218)**
Net book amount at December 31	**221,923**	**182,079**

(1) Includes translation differences

(Amounts expressed in thousands of TL unless otherwise indicated.)

17. Deposits from banks

	December 31, 2017			December 31, 2016		
	Demand	**Term**	**Total**	**Demand**	**Term**	**Total**
Foreign currency:						
Domestic banks	428,475	4,152,685	4,581,160	413,004	380,625	793,629
Foreign banks	86,722	1,665,784	1,752,506	63,453	1,657,210	1,720,663
Funds deposited under repurchase agreements	-	623,076	623,076	-	1,979,688	1,979,688
	515,197	**6,441,545**	**6,956,742**	**476,457**	**4,017,523**	**4,493,980**
TL:						
Domestic banks	49,210	2,960,283	3,009,493	19,063	5,482,975	5,502,038
Foreign banks	72,269	17,861	90,130	118,130	37,665	155,795
Funds deposited under repurchase agreements	-	8,619,994	8,619,994	-	3,659,430	3,659,430
	121,479	**11,598,138**	**11,719,617**	**137,193**	**9,180,070**	**9,317,263**
	636,676	**18,039,683**	**18,676,359**	**613,650**	**13,197,593**	**13,811,243**
Current	636,676	17,971,932	18,608,608	613,650	13,110,540	13,724,190
Non-current	-	67,751	67,751	-	87,053	87,053

18. Customer deposits

	December 31, 2017			December 31, 2016		
	Demand	**Term**	**Total**	**Demand**	**Term**	**Total**
Foreign currency deposits:						
Saving deposits	7,409,640	29,464,159	36,873,799	5,259,160	22,684,150	27,943,310
Commercial deposits	9,195,187	45,099,638	54,294,825	8,033,767	34,358,576	42,392,343
	16,604,827	**74,563,797**	**91,168,624**	**13,292,927**	**57,042,726**	**70,335,653**
TL deposits:						
Saving deposits	6,797,877	39,309,952	46,107,829	6,145,162	34,938,530	41,083,692
Commercial deposits	7,615,855	18,801,413	26,417,268	6,899,733	30,362,121	37,261,854
Funds deposited under repurchase agreements	-	183,311	183,311	-	634,683	634,683
Public sector deposits	250,278	6,345	256,623	230,784	4,087	234,871
	14,664,010	**58,301,021**	**72,965,031**	**13,275,679**	**65,939,421**	**79,215,100**
	31,268,837	**132,864,818**	**164,133,655**	**26,568,606**	**122,982,147**	**149,550,753**
Current	31,268,837	131,532,360	162,801,197	26,568,606	121,883,978	148,452,584
Non-current	-	1,332,458	1,332,458	-	1,098,169	1,098,169

(Amounts expressed in thousands of TL unless otherwise indicated.)

19. Funds borrowed

	December 31, 2017	December 31, 2016
Foreign institutions and banks		
Syndication loans	10,662,245	8,765,744
Subordinated debt	3,996,100	3,727,751
Other	28,320,390	18,579,223
Total foreign	**42,978,735**	**31,072,718**
Domestic institutions and banks		
Domestic banks	3,367,418	3,163,807
Interbank money market and Settlement Custody Bank	6,629,759	2,931,228
Total domestic	**9,997,177**	**6,095,035**
	52,975,912	**37,167,753**
Current	34,984,313	24,990,528
Non-current	17,991,599	12,177,225

The Parent Bank had early repaid its borrowing for USD 585 million on January 9, 2013 the Bank has received from Unicredit Bank Austria AG on February 22, 2012 with an interest rate of 3 months Libor + 8.30% and received another subordinated borrowing from the same counterparty for USD 585 million with 10 years of maturity (payable after 5 years) and 5.5% fixed interest rate. The Parent Bank incurred an early payment fee for TL 57 million with respect to early closing of this subordinated loan. On January 30, 2015, relevant articles of this agreement have been amended in accordance with Article 8 of the Regulation Regarding Equity of Banks, which is the relevant legislation in force issued by the BRSA. In addition, the interest rate in the credit agreement has been updated as 5.70%.

The Parent Bank obtained a subordinated loan on December 18, 2013 amounting to USD 470 million, with 10 years maturity and a repayment option at the end of 5 years. The interest rate is determined as 6.35% for the first 5 years and midswap+4.68% for the remaining 5 years. The loan was obtained from Unicredit Bank Austria AG. On January 30, 2015, relevant articles of this agreement have been amended in accordance with Article 8 of the Regulation on Own Fund of Banks. In addition, the interest rate has been amended to 6.55% fixed for the first 5 years and Midswap+4.88% for the remaining 5 years.

(Amounts expressed in thousands of TL unless otherwise indicated.)

20. Debt securities in issue

	December 31, 2017	December 31, 2016
Securitization borrowings	8,278,912	6,564,507
Subordinated debt	5,722,705	5,340,142
Bills	1,320,191	1,486,456
Bonds	9,130,439	5,917,794
	24,452,247	**19,308,899**
Current	5,893,650	5,837,213
Non-current	18,558,597	13,471,686
	24,452,247	**19,308,899**

On November 29, 2012, the Parent Bank issued a Basel II compliant 10 year bullet subordinated note for an amount of USD 1 billion. The note has a 5.5% coupon and was counted towards capital at 19% as of December 31, 2017.

On March 8, 2016, the Parent Bank launched a Basel III compliant subordinated note transaction with a 10 year 1 day maturity and an early payment option at the end of the 5th year for an amount of USD 500 million. The note has an 8.5% coupon. If the notes are not redeemed at the fifth year, the coupon will be reset as 5 year mid-swap + 7.40% for the remaining 5 years.

21. Financial Liabilities Designated at Fair Value

The Group classified some of its debt securities issued as financial liabilities designated at fair value in order to eliminate the accounting mismatch at initial recognition in accordance with IAS 39 paragraph 9. As of December 31, 2017, the total amount of financial liabilities designated at fair value through profit/loss is TL 4,363,503 (December 31, 2016-TL 3,938,694) and the fair value loss is TL 216,465 (December 31, 2016-TL 19,783 gain) recognized in the income statement as income.

The nominal amounts of the total return swaps which are closely related to debt securities issued as financial liabilities designated at fair value as of December 31, 2017 are TL 4,618,063 (December 31, 2016: TL 4,033,003) for buy legs and TL 4,618,063 (December 31, 2016: TL 4,033,003) for sell legs with a fair value differences amounting to asset TL 92,985 (December 31, 2016: liability TL 97,052). The mentioned total return swaps have 10 years maturity in average.

(Amounts expressed in thousands of TL unless otherwise indicated.)

22. Taxation

	December 31, 2017	December 31, 2016
Current tax expense	(1,100,842)	(658,037)
Deferred tax expense	261,572	(123,899)
Income tax expense	**(839,270)**	**(781,936)**

Turkish tax legislation does not permit a parent company and its subsidiaries to file a consolidated tax return. Therefore, provisions for taxes, as reflected in these consolidated financial statements, have been calculated on a separate-entity basis.

Corporation tax is payable at the rate of 20% on the total income of entities in Turkey after adjusting for certain disallowable expenses, exempt income and investment and other allowances. Laws No. 7061 has been published in the Official Gazette dated December 5, 2017 and increased the corporate income tax rate for all companies from 20% to 22% for the 2018, 2019 and 2020 fiscal years. According to the recent change, the increased rate will be applied on the first temporary tax period of 2018.

No further tax is payable unless profit is distributed. Dividends paid to non-resident corporations, which have a place of business in Turkey, or resident corporations are not subject to withholding tax. Otherwise, dividends paid are subject to withholding tax at the rate of 15%.

Corporations are required to pay advance corporate tax quarterly on their corporate income. Advance tax is declared by the 14th and paid by the 17th day of the second month following each calendar quarter end. Advance tax paid by corporations for the current period is credited against the annual corporation tax calculated on the annual corporate income in the following year. Despite the offset, if there is temporary prepaid tax remaining, this balance can be refunded or used to offset any other financial liabilities to the government.

Capital gains derived from the sale of equity shares and immovable properties held for at least two years is tax exempt, if such gains are added to paid-in capital or kept in a special fund for 5 years in accordance with 5/1-e of Corporate Tax Law. 75% exemption rate applied over the income derived by corporate taxpayers from the sales of equity shares. 75% exemption rate applied over the income derived by corporate taxpayers from the sales of immovable property has been reduced to 50% in accordance with the Law No. 7061 effective from December 5, 2017.

Under the Turkish taxation system, tax losses can be carried forward for offset against future taxable income for up to 5 years. Tax losses cannot be carried back to offset profits from previous periods.

(Amounts expressed in thousands of TL unless otherwise indicated.)

22. Taxation (continued)

In Turkey, there is no procedure for a final and definitive agreement on tax assessments. Corporations file their tax returns by the 25th day of the fourth month following the close of the financial year to which they relate. Tax returns are open for 5 years from the beginning of the year that follows the date of filing during which the tax authorities have the right to audit tax returns, and the related accounting records on which they are based, and if they find any corrections then the tax amount to be paid might be changed as well.

Reconciliation between the theoretical tax amount that would arise using the basic tax rate of the Parent Bank and the actual taxation charge for the year is stated below:

	December 31, 2017	December 31, 2016
Profit before income taxes	**4,264,259**	**4,030,271**
Theoretical income tax at the applicable tax rate of 20%	852,852	806,054
Effect of different tax rates in other countries	76,203	6,061
Tax effect of items which are not deductible or assessable for taxation purposes:		
- Income exempt from taxation	(136,557)	(34,859)
- Non-deductible expenses for tax purposes	(34,314)	(31,933)
Other	81,086	36,613
Income tax expense	**839,270**	**781,936**

(Amounts expressed in thousands of TL unless otherwise indicated.)

22. Taxation (continued)

Deferred income taxes

For all domestic subsidiaries and the Parent Bank, deferred income taxes are calculated on temporary differences that are expected to be realized or settled under the liability method using a principal tax rate of 22% at December 31, 2017 (2016 - 20%). According to Law No 7061 income tax rate will be 22% for years 2018, 2019 and 2020.

For foreign subsidiaries deferred income taxes are calculated on all temporary differences under the liability method before the exemptions using the principal tax rates at December 31, 2017 and 2016 which are as follows:

	Tax rate (%)	
Country of incorporation	**December 31, 2017**	**December 31, 2016**
Netherlands	25.00	25.00
Azerbaijan	20.00	20.00
Malta	35.00	35.00

The deferred income tax assets and liabilities represent the tax effect of temporary differences arising due to the different treatment of certain items of income and expenses included in the financial statements compared to the local tax return in accordance with the applicable tax law plus any available tax loss carried forward from previous years.

The temporary differences giving rise to the deferred income tax assets and deferred income tax liabilities are as follows:

	Cumulative Temporary Differences		Deferred Tax Asset/Liability	
	December 31, 2017	**December 31, 2016**	**December 31, 2017**	**December 31, 2016**
Impairment on assets	360,496	363,910	54,489	38,714
Allowance for loan impairment	1,057,004	1,015,922	232,191	203,143
Pension benefits transferable to the Social Security Institution (“SSI”) (Note 24)	690,852	568,006	151,987	113,601
Reserve for employment termination benefits (Note 24)	400,547	129,510	88,814	26,388
Revaluation of derivative instruments at fair value	4,168,192	2,711,672	925,946	542,334
Valuation differences on investment securities	80,221	59,754	17,649	11,951
Other	1,889,587	1,251,350	424,718	250,270
Deferred income tax assets	**8,646,899**	**6,100,124**	**1,895,794**	**1,186,401**
Difference between carrying value and tax base of property and equipment	688,098	698,636	108,077	81,975
Valuation differences on investment securities	478,942	522,134	105,507	104,545
Revaluation of derivative instruments at fair value	5,906,527	4,266,432	1,291,356	853,286
Other	267,196	295,149	56,062	60,241
Deferred income tax liabilities	**7,340,763**	**5,782,351**	**1,561,002**	**1,100,047**
Deferred income tax assets, net (1)	**1,306,136**	**317,773**	**334,792**	**86,354**

(1) Includes TL 16,606 deferred tax liabilities as of December 31, 2017 (December 31, 2016 – TL 7,892 liabilities).

(Amounts expressed in thousands of TL unless otherwise indicated.)

22. Taxation (continued)

The movements of net deferred income taxes during the years were as follows:

	December 31, 2017	December 31, 2016
Balance at January 1	**86,354**	**182,930**
(Charge) / credit for the year, net	261,572	(123,899)
Available-for-sale revaluation reserve	(7,753)	15,878
Net investment hedge	76,205	40,299
Cash flow hedge	(141,202)	(27,796)
Re-measurement gains on defined benefit liability	57,151	(375)
Other	2,465	(683)
Balance at December 31	**334,792**	**86,354**

There are no deductible temporary differences for which no deferred tax asset is recognized in the statement of financial position (2016 - None).

Income tax effects relating to components of other comprehensive income

	December 31, 2017			December 31, 2016		
	Before tax amount	Tax (expense) benefit	Net-of tax amount	Before tax amount	Tax (expense) benefit	Net-of tax amount
Foreign currency translation differences	372,042	-	372,042	326,535	-	326,535
Fair value gains on available-for- sale financial assets (including translation difference)	78,187	(7,753)	70,434	(194,340)	15,878	(178,462)
Net investment hedge	(321,859)	76,205	(245,654)	(201,497)	40,299	(161,198)
Cash flow hedge	598,743	(141,202)	457,541	138,981	(27,796)	111,185
Re-measurement gains on defined benefit liability	(259,779)	57,151	(202,628)	2,120	(375)	1,745
Revaluation of art object and paintings	-	-	-	-	-	-
Other comprehensive income for the year (net presentation)	**467,334**	**(15,599)**	**451,735**	**71,799**	**28,006**	**99,805**

(Amounts expressed in thousands of TL unless otherwise indicated.)

23. Other provisions

	December 31, 2017	December 31, 2016
Provision for losses on credit related commitments	428,196	391,204
Tax and other legal provisions	170,953	138,852
Provision on export commitment estimated liability	46,973	45,690
Other	585,048	189,268
	1,231,170	**765,014**
Current	-	-
Non-current	1,231,170	765,014

Credit related commitments provision

The Group management has estimated losses that may arise from credit related commitments and has recognized a provision of TL 428,196 (2016 - TL 391,204).

Tax and other legal provisions

The Group has recorded a provision of TL 101,228 (2016 - TL 75,955) for litigation and has accounted for it in the financial statements under the “Other provisions” account. Except for the cases where provisions are recorded, management considers that negative results in ongoing litigations resulting in cash outflows is not probable.

The Group also recorded a total provision of TL 69,725 (2016 - TL 62,897) against potential tax risks in the form of possible tax duties and penalties in the consolidated financial statements for the year ended December 31, 2017.

Export commitment provision

The Group management has estimated losses that may arise from export loans to customers under legal follow-up where they do not have the ability to fulfill their export commitments and have recognized a provision of TL 46,973 (2016 - TL 45,690).

Movement in other provisions is as follows:

	Provision for credit related commitments	Tax and other legal provisions	Export commitment provisions	Other	2017 Total	2016 Total
At January 1	**391,204**	**138,852**	**45,690**	**189,268**	**765,014**	**713,469**
Provision charged	56,972	32,662	1,756	395,780	487,170	152,094
Provision used / released	(19,940)	(561)	(473)	-	(20,974)	(100,611)
Translation difference	(40)	-	-	-	(40)	62
Balance at December 31	**428,196**	**170,953**	**46,973**	**585,048**	**1,231,170**	**765,014**

(Amounts expressed in thousands of TL unless otherwise indicated.)

24. Retirement benefit obligations

	December 31, 2017	December 31, 2016
Statement of financial position obligations for:		
- Post employment benefits (pension and medical) transferable to SSI	690,852	568,006
- Reserve for employment termination benefits	400,547	129,510
	1,091,399	**697,516**
Income statement (charge) / credit for:		
- Post employment benefits (pension and medical) transferable to SSI	(122,846)	6,243
- Reserve for employment termination benefits	(53,918)	(30,757)
	(176,764)	**(24,514)**

Income statement charge for retirement benefit obligations has been recognized as a separate line item in the income statement for the years ended December 31, 2017 and 2016.

(i) Post-employment benefits (pension and medical) transferable to SSI

The Parent Bank’s personnel are members of the Yapı ve Kredi Bankası Anonim Şirketi Mensupları Yardım ve Emekli Sandığı Vakfı (“the Fund”) which was established in accordance with the 20th temporary article of the Social Security Law No. 506. The technical financial statements of the Fund are audited in accordance with the Article 38 of the Insurance Supervision Law and the “Regulation Regarding the Actuaries” by a registered independent actuary.

Temporary article 23 paragraph one of the Banking Act published in the Official Gazette No 25983 dated November 1, 2005 stated that foundations like the Fund are to be transferred to the Social Security Institution (“SSI”) within three years beginning from the publication date of the article.

The article of the Law related to the transfer was cancelled (pursuant to the application by the President on November 2, 2005) by the decision of Constitutional Court (decision no: E.2005/39, K. 2007/33 dated March 22, 2007) published in the Official Gazette No. 26479 dated March 31, 2007, and the effect of the legal article was suspended from the date of the publication of the decision.

The reasoning of the Constitutional Court regarding the abrogation of the corresponding article was published in the Official Gazette dated December 15, 2007, No 26372. With the publication of the reasoning of the decision, the Grand National Assembly of Turkey (“GNAT”) started to work on new legal arrangements regarding the transfer of fund members to SSI and the related articles of the “Law Regarding the Changes in Social Insurance and General Health Insurance Law and Other Related Laws and Regulations” No 5754 (“the New Law”) regulating the transfer of the funds were approved by the GNAT on April 17, 2008. The New Law was published in the Official Gazette No. 26870 dated May 8, 2008. With the new law, the banks’ pension funds will be transferred to SSI within three years from the date of publication of the decree and this period can be extended for a maximum of two years on the decision of the Council of Ministers. The transfer period was extended for another two years with the decision of the Council of Ministers No. 2011/1559 published in the Official Gazette dated April 9, 2011. According to the “Amendment of Social Insurance and General Health Insurance Law No. 6283” published in the Official Gazette dated March 8, 2012, the Council of Ministers was authorized to increase the two-year extension period mentioned above to four years. According to the decision of The Council of Ministers February 24, 2014, the transfer date was set as May 2015. The Council of Ministers was authorized to determine the transfer date of pension funds in accordance with the last amendment in the first paragraph of the 20th provisional article of Law No.5510 implemented by the Law No. 6645 on Amendment of the Occupational Health and Safety Law and Other Laws and Decree Laws published in the Official Gazette dated April 23, 2015 and numbered 29335.

(Amounts expressed in thousands of TL unless otherwise indicated.)

24. Retirement benefit obligations (continued)

A commission (whose members are the representatives of the SSI, the Ministry of Finance, Turkish Treasury, State Planning Organization, BRSA, Saving Deposit Insurance Fund ("SDIF"), one member representing the Fund and one member representing the Fund members) is in charge of the calculation of the value of the payment that would need to be made to SSI to settle the obligation a technical interest rate of 9.8% by law is used taking into consideration income and expenses by insurance branches of the funds and the excess of salaries and income paid by the funds over the salaries and income to be paid in accordance with the SSI arrangements which should not be less than SSI arrangements, related to the members of the Fund as of the date of the transfer including the members who have left the scheme.

In accordance with the New Law, after the transfer to SSI, any social rights and payments to Fund members and their beneficiaries which are not provided although they are included in the Fund Title Deed will continue to be provided by the Fund and the employers of the Fund members.

The Parent Bank accounts for a provision for the technical deficit based on the report prepared by a registered actuary in accordance with the rates determined by the New Law.

The actuarial statement of financial position of the Fund has been prepared in accordance with a technical interest rate of 9.80% and CSO 1980 mortality table and reflects a technical deficit of TL 690,852 on December 31, 2017 (2016 - TL 568,006).

The Group's obligation in respect of the post-employment pension and medical benefits transferable to SSI has been determined as the value of the payment that would need to be made to SSI to settle the obligation at the statement of financial position date in accordance with the related article of the New Law and other related laws and regulations. The pension disclosures set out below therefore reflect the actuarial parameters and results in accordance with the New Law provisions.

The amounts recognized in the statement of financial position are determined as follows:

	December 31, 2017	**December 31, 2016**
Present value of funded obligations	2,371,855	1,964,448
- Pension benefits transferable to SSI	2,402,317	*1,882,467*
- Post-employment medical benefits transferable to SSI	(30,462)	*81,981*
Fair value of plan assets	(1,681,003)	(1,396,442)
Liability in the statement of financial position	**690,852**	**568,006**

The principal actuarial assumptions used were as follows:

	December 31, 2017	**December 31, 2016**
	(%)	**(%)**
Discount rate		
- Pension benefits transferable to SSI	9.80	9.80
- Post-employment medical benefits transferable to SSI	9.80	9.80

The sensitivity analysis of defined benefit obligation of excess liabilities is as follows:

% change in defined benefit obligation	
	%
Discount rate +1%	(16.6)
Discount rate -1%	22.1
Price inflation +1%	32.6
Price inflation -1%	(22.3)

(Amounts expressed in thousands of TL unless otherwise indicated.)

24. Retirement benefit obligations (continued)

Mortality rate

The average life expectancy in years of a pensioner is defined according to CSO 1980 mortality table.

Plan assets are as follows:

	December 31, 2017		December 31, 2016	
Bank placements	574,905	34%	831,034	60%
Government bonds and treasury bills	723,510	43%	233,858	17%
Property and equipment	261,258	16%	223,150	16%
Other	121,330	7%	108,400	7%
	1,681,003	**100%**	**1,396,442**	**100%**

The fair value of the property and equipment occupied by the Group is TL 261,258 (2016 - TL 223,150).

(ii) Reserve for employment termination benefits

The movement in the reserve for employee termination benefits is as follows:

	December 31, 2017	December 31, 2016
Balance at January 1	**129,510**	**141,388**
Interest costs	6,411	6,504
Actuarial gains and losses	259,779	(2,120)
Annual charge	47,507	24,253
Paid during the year	(41,923)	(40,431)
Translation difference	(737)	(84)
Balance at December 31	**400,547**	**129,510**

Under the Turkish Labour Law, the Parent and its domestic subsidiaries are required to pay termination benefits to each employee who has completed at least one year of service and whose employment is terminated without due cause, is called up for military service, dies or who retires after completing 25 years of service (20 years for women) and achieves the retirement age (63 for women and 64 for men). Since the legislation was changed on September 8, 1999, there are certain transitional provisions relating to length of service prior to retirement. The amount payable consists of one month’s salary limited to the annual ceiling for each year of service.

(Amounts expressed in thousands of TL unless otherwise indicated.)

24. Retirement benefit obligations (continued)

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

IFRS requires actuarial valuation methods to be developed to estimate the enterprise's obligation under defined benefit plans. In the consolidated financial statements, the Group reflected a liability calculated using the projected unit credit method and based upon the factors derived using their experience of personnel terminating their services and being eligible to receive employment termination benefits. The provision has been calculated by estimating the present value of the future probable obligation of the Group arising from the retirement of the employees.

Accordingly the following financial and demographical actuarial assumptions were used in the calculations of the provision:

	December 31, 2017	December 31, 2016
Discount rate (%)	4.95	4.50
The probability of retirement (%)	93.79	93.63

Additionally, the principal actuarial assumption is that the maximum liability will increase in line with inflation. Thus, the discount rate applied represents the expected real rate after adjusting for the effects of future inflation. As the annual ceiling is revised semi-annually, the ceiling of full TL 5,001.76 effective from January 1, 2018 (January 1, 2017 - full TL 4,426.16) has been taken into consideration in calculating the reserve for employment termination benefits of the Parent and its domestic subsidiaries.

25. Other liabilities

	December 31, 2017	December 31, 2016
Credit card payables	8,555,137	7,115,087
Miscellaneous payables to customers	2,528,305	2,474,234
Clearing accounts(1)	699,831	659,991
Blocked accounts	664,986	585,909
Unearned income	302,010	300,146
Taxes other than on income and withholdings	333,487	260,166
Import deposit and transfer orders	351,969	254,120
Premium and bonuses payable to personnel	263,588	238,757
Provision for unused annual vacation	183,832	171,811
Advances taken	149,068	55,438
Saving Deposits Insurance Fund payable	53,041	45,734
Other	1,326,269	1,502,519
Total	**15,411,523**	**13,663,912**
Current	15,411,106	13,663,600
Non-current	417	312

(1) Clearing accounts mainly consist of payables from clearing houses related to interbank, credit card and cheque transactions. The account balance is settled on a daily basis and arises based on the number of transactions the day before the reporting date.

(Amounts expressed in thousands of TL unless otherwise indicated.)

26. Acquisitions and mergers

(i) Mergers, transfers and acquisitions in the year 2017 and 2016

None.

27. Share capital and share premium

The historic amount of share capital of the Bank consists of 434,705,128.40 (2016 - 434,705,128.40) authorized shares with a nominal value of TL 0,01 each. The Company's authorized capital amounts to TL 4,347,051 (2016 - TL 4,347,051).

The issued and fully paid-in share capital and share premium are as follows:

		December 31, 2017		December 31, 2016
Shareholders	**Participation rate (%)**		**Participation rate (%)**	
Koç Finansal Hizmetler A.Ş.	81.80	3,555,712	81.80	3,555,712
Other	18.20	791,339	18.20	791,339
Historical share capital	**100.00**	**4,347,051**	**100.00**	**4,347,051**
Adjustment to share capital		(60,471)		(60,471)
Share premium		535,679		535,679
Total share capital and share premium		**4,822,259**		**4,822,259**

Transfer of the 59.47% of the shares of Yapı Kredi Faktoring A.Ş. with a nominal value of TL 9,992, 73.10% of the shares of Yapı Kredi Finansal Kiralama A.O. with a nominal value of TL 285,048 and 99.80% of the shares of Yapı Kredi Bank Azerbaijan with a nominal value of AZN 6,336,200 (full); all formerly owned by KFS were completed as of October 31, 2007. As a part of this share exchange the Bank's capital was increased by TL 277,601 through increasing the shareholding of KFS. Besides, the differences between the nominal values of the shares issued by the Bank and the fair values of the shares transferred to the Bank amounting to TL 495,852 has been recorded in equity as "Share Premium".

(Amounts expressed in thousands of TL unless otherwise indicated.)

28. Retained earnings and other reserves

	December 31, 2017	December 31, 2016
Statutory reserve	869,435	844,564
Translation reserves	1,204,968	832,926
Revaluation reserve - available-for-sale investments	(350,263)	(420,697)
Hedging reserves	107,386	(104,501)
Re-measurement gains on defined benefit liability	(192,080)	10,548
Revaluation of art objects and paintings	32,693	32,693
Total other reserves	**1,672,139**	**1,195,533**
Retained earnings	**24,301,236**	**20,901,197**

Movements in other reserves were as follows:

	Statutory reserves	Revaluation reserves	Translation reserves	Hedging reserves	Actuarial gains	Revaluation of fixed assets	Total
At January 1, 2017	**844,564**	**(420,697)**	**832,926**	**(104,501)**	**10,548**	**32,693**	**1,195,533**
Net change in available-for-sale investments, net of tax	-	70,434	-	-	-	-	70,434
Gains / (losses) on hedges of a net investment in a foreign operation	-	-	-	(245,654)	-	-	(245,654)
Gains / (losses) on cash flow hedges	-	-	-	457,541	-	-	457,541
Currency translation differences	-	-	372,042	-	-	-	372,042
Re-measurement gains on defined benefit liability, net of tax	-	-	-	-	(202,628)	-	(202,628)
Transfer to statutory reserves	24,871	-		-	-	-	24,871
At December 31, 2017	**869,435**	**(350,263)**	**1,204,968**	**107,386**	**(192,080)**	**32,693**	**1,672,139**

	Statutory reserves	Revaluation reserves	Translation reserves	Hedging reserves	Actuarial gains	Revaluation of fixed assets	Total
At January 1, 2016	**751,537**	**(242,235)**	**506,391**	**(54,488)**	**5,610**	**32,693**	**999,508**
Net change in available-for-sale investments, net of tax	-	(178,462)	-	-	-	-	(178,462)
Gains / (losses) on hedges of a net investment in a foreign operation	-	-	-	(161,198)	-	-	(161,198)
Gains / (losses) on cash flow hedges	-	-	-	111,185	-	-	111,185
Currency translation differences	-	-	326,535	-	-	-	326,535
Re-measurement gains on defined benefit liability, net of tax	-	-	-	-	4,938	-	4,938
Transfer to statutory reserves	93,027		-	-	-	-	93,027
At December 31, 2016	**844,564**	**(420,697)**	**832,926**	**(104,501)**	**10,548**	**32,693**	**1,195,533**

(Amounts expressed in thousands of TL unless otherwise indicated.)

28. Retained earnings and other reserves (continued)

Retained earnings as per the statutory financial statements other than statutory reserves are available for distribution, subject to the statutory reserve requirement referred to below.

Under the Turkish Commercial Code, the Group is required to create the following statutory reserves from appropriation of earnings, which are available for distribution only in the event of liquidation or losses:

a) First statutory reserve, appropriated at the rate of 5% of net income, until the total reserve is equal to 20% of issued and fully paid-in share capital.

b) Second statutory reserve, appropriated at the rate of at least 10% of distribution in excess of 5% of issued and fully paid-in share capital, without limit. It may be used to absorb losses.

After deducting taxes and setting aside the statutory reserves as discussed above, the remaining balance of statutory net profit is available for distribution to shareholders.

29. Net interest income

	December 31, 2017	December 31, 2016
Interest income on:		
Loans and advances:		
- to banks	524,589	161,091
- to customers	18,280,176	15,876,626
Trading and investment securities	3,302,783	2,279,900
Derivative financial instruments	1,622,991	773,887
Financial leases	661,125	517,228
Reserve deposits	233,964	118,632
Other	25,661	23,819
Total interest income	**24,651,289**	**19,751,183**
Interest expense on:		
Due to customers	(9,467,867)	(7,709,100)
Funds borrowed	(1,686,514)	(1,065,679)
Securities issued	(1,232,656)	(968,296)
Derivative financial instruments	(2,338,872)	(843,105)
Repurchase agreements	(304,989)	(579,234)
Deposits from banks	(170,462)	(157,950)
Other	(579,849)	(408,852)
Total interest expense	**(15,781,209)**	**(11,732,216)**
Net interest income	**8,870,080**	**8,018,967**

(Amounts expressed in thousands of TL unless otherwise indicated.)

30. Net fee and commission income

	December 31, 2017	December 31, 2016
Fee and commission income on:		
Credit/debit cards	1,920,164	1,708,997
Banking services	1,114,363	992,810
Insurance products	262,587	192,809
Assets under management	194,050	167,628
Loans		
- Credit related commitments	566,001	513,595
- Loans and advances	15,447	11,047
Brokerage	87,481	58,764
Factoring	20,454	18,272
Other	50,257	42,513
Total fee and commission income	**4,230,804**	**3,706,435**
Fee and commission expense on:		
Credit/debit cards	(805,139)	(658,819)
Payroll charity	(311,054)	(233,869)
Brokerage	(27,713)	(23,498)
Other	(377,356)	(392,822)
Total fee and commission expense	**(1,521,262)**	**(1,309,008)**
Net fee and commission income	**2,709,542**	**2,397,427**

31. Net trading, hedging and fair value income and net gains / losses from investment securities

	December 31, 2017	December 31, 2016
Foreign exchange:		
- Transaction gains less losses on derivatives and securities	(278,273)	1,378,705
Interest rate instruments	296,597	(1,028,968)
Credit derivatives	(267)	720
	18,057	**350,457**

Foreign exchange net trading income includes gains and losses from spot and forward contracts, options, futures and translated foreign currency assets and liabilities. Interest rate instruments include the results of making markets in government securities, money market instruments, interest rate and cross currency interest rate swaps, options, hedge items and other derivatives.

(Amounts expressed in thousands of TL unless otherwise indicated.)

32. Other operating expenses

	December 31, 2017	December 31, 2016
Staff costs	**(2,568,696)**	**(2,316,008)**
Depreciation on property and equipment (Note 15)	(204,228)	(208,820)
Amortization of intangible assets (Note 14)	(136,120)	(124,721)
Depreciation and amortization	**(340,348)**	**(333,541)**
Rent expenses	(321,569)	(307,994)
Payment to Saving Deposit Insurance Fund	(242,902)	(176,119)
Communication expenses	(147,903)	(154,303)
Audit and consultancy fees	(124,437)	(147,853)
Sundry taxes and duties	(129,464)	(126,465)
Marketing and advertisement costs	(142,297)	(114,068)
Repair and maintenance expenses	(114,276)	(103,256)
Utilities expenses	(59,763)	(51,241)
Charities	(13,084)	(13,500)
Other	(666,931)	(743,744)
General and administrative expenses	**(1,962,626)**	**(1,938,543)**
Total	**(4,871,670)**	**(4,588,092)**

33. Impairment losses on loans, investment securities and credit related commitments

	December 31, 2017	December 31, 2016
Impairment losses on loans and receivables (Note 9)	(2,237,044)	(2,382,210)
Impairment losses on credit related commitments (Note 23)	(37,032)	19,643
	(2,274,076)	**(2,362,567)**

(Amounts expressed in thousands of TL unless otherwise indicated.)

34. Earnings per share

Earnings per share disclosed in the consolidated statements of income is determined by dividing the net income attributable to the equity holders of the Parent by the weighted average number of ordinary shares outstanding during the period concerned.

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

The Bank has not issued any shares attributable to transfers to share capital from retained earnings during the year ended December 31, 2017 (2016 - none).

The earnings attributable to basic shares for each period are as follows

	December 31, 2017	December 31, 2016
Profit attributable to equity holders of the Parent	3,424,910	3,248,269
Weighted average number of ordinary shares in issue (thousand) (1 Kr each)	434,705,128	434,705,128
Basic and diluted earnings per share (expressed in TL, full amount per thousand share)	**7.88**	**7.47**

(Amounts expressed in thousands of TL unless otherwise indicated.)

35. Assets pledged and restricted

The Group has the following assets pledged as collateral:

	December 31, 2017		December 31, 2016	
	Assets	Related liability	Assets	Related liability
Investment securities (Note 10)	23,227,409	14,356,090	12,229,685	10,663,792
Other assets pledged (1)	1,354,011	-	1,586,505	-
Total	**24,581,420**	**14,356,090**	**13,816,190**	**10,663,792**

(1) Other assets pledged represent collateral given to the counter parties of the derivative transactions and additional collateral given in relation to funds obtained under repurchase agreements.

Available-for-sale, held-to-maturity and trading securities whose total carrying amount is TL 10,965,391 as of December 31, 2017 (2016 - TL 7,882,529) are pledged to banks and other financial institutions against borrowed funds and funds obtained under repurchase agreements and total return swap transactions. The total amount of funds obtained under repurchase agreements and total return swaps is TL 14,356,090 as of December 31, 2017 (2016 - TL 10,663,792). In accordance with the terms of the agreements with these financial institutions ("transferees"), the Bank provides this collateral (debt instruments as given above) to the transferees and the transferees have the right to sell or re-pledge the collaterals until the expiry date of the agreements.

Securities are also pledged to regulatory authorities for legal requirements and other financial institutions as a guarantee for stock exchange and money market operations. These are mainly the CBRT, Istanbul Stock Exchange (ISE) Settlement and Custody Bank and other financial institutions and amount to TL 12,262,018 (2016 - TL 4,347,157).

As of December 31, 2017, the Group's reserve deposits, including those at foreign central banks, amount to TL 34,653,676 (2016 - TL 27,864,220). There is also TL 240,327 (2016 - TL 119,931) of blocked deposits held in foreign bank accounts.

The Group does not have any financial assets and liabilities that are offset in the financial statements or subject to an enforceable master netting agreement or similar agreements. In addition, the Group and its counterparties do not intend to settle on a net basis or to realize assets and settle liabilities simultaneously.

The Group receives and gives collateral in the form of cash and marketable securities in respect of the above transactions summarized in the above table.

36. Commitments and contingent liabilities

In the normal course of its activities, the Group undertakes various commitments and incurs certain contingent liabilities that are not presented in these financial statements, including letters of guarantee, acceptances and letters of credit. The following is a summary of significant commitments and contingent liabilities.

Legal proceedings

Due to the nature of its business, the Group is involved in a number of claims and legal proceedings, arising in the ordinary course of business. The Group recognizes provisions for such matters when, in the opinion of management and its professional advisors, it is probable that a payment will be made by the Group, and the amount can be reliably estimated (Note 23).

(Amounts expressed in thousands of TL unless otherwise indicated.)

36. Commitments and contingent liabilities (continued)

In respect of further claims asserted against the Group, which according to the principles outlined above, have not been provided for, it is the opinion of the management and its professional advisors that such claims are either without merit, can be successfully defended or will not have a material adverse effect on the Group's financial position.

Credit related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as and if required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Group on behalf of a customer authorizing a third party to draw drafts on the Group up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods to which they relate and therefore have significantly less risk.

Cash requirements under guarantees and standby letters of credit are considerably less than the amount of the commitment.

The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

As of December 31, 2017 the Group's commitments for unused credit card limits amounted to TL 33,700,364 (2016 - TL 29,878,711).

The table below shows the contractual expiry by maturity of the Group's contingent liabilities and commitments. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down. For issued financial guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.

December 31, 2017(1)	Indefinite	Not later than 1 year	1-5 years	Over 5 years	Total
Letter of credits	-	8,072,995	3,452,609	2,282	11,527,886
Letter of guarantees	22,859,931	11,426,328	20,933,980	5,079,512	60,299,751
Acceptance credits		187,776	22,021	2,888	212,685
Other commitments	613,499	1,103,309	1,127,480	3,966,805	6,811,093
Total	**23,473,430**	**20,790,408**	**25,536,090**	**9,051,487**	**78,851,415**

December 31, 2016(1)	Indefinite	Not later than 1 year	1-5 years	Over 5 years	Total
Letter of credits	-	6,654,515	2,532,433	6,222	9,193,170
Letter of guarantees	21,464,214	9,410,155	18,179,733	3,738,129	52,792,231
Acceptance credits	-	168,491	24,902	2,373	195,766
Other commitments	341,794	551,945	2,178,223	3,201,355	6,273,317
Total	**21,806,008**	**16,785,106**	**22,915,291**	**6,948,079**	**68,454,484**

(1) Based on original maturities.

37. Segment analysis

The Group carries out its banking operations through three main business units: (1) Retail Banking (including credit cards and SME banking), (2) Corporate and Commercial Banking (3) Private Banking and Wealth Management.

The Group's Retail Banking activities include card payment systems, SME (small medium size enterprises) banking and individual banking. Retail Banking products and services offered to customers include card payment systems, consumer loans (including general purpose loans, auto loans, mortgages), commercial installment loans, SME loans, time and demand deposits, gold banking, investment accounts, life and non-life insurance products and payroll services. Card payment systems cover the management of products, services, campaigns for member merchants as well as the sales and activities for a variety of customer types. Crystal, Play, Adios and Taksitçi are the other card brands providing services for the different segments within the World brand, shopping and marketing platform of the Bank. The Bank also offers debit card and a prepaid card named World Hediye Card.

Corporate and Commercial Banking segment is organized into three subgroups: Corporate Banking for large-scale companies, Commercial Banking for medium-sized enterprises and Multinational Companies Banking for multinational companies. Corporate and Commercial Banking, has a product range of working capital finance, trade finance, project finance, domestic and international non-cash loans such as letters of credit and letters of guarantee, cash management and internet banking.

Through its Private Banking and Wealth Management activities, the Bank serves high net worth customers and delivers investment products to this customer segment. Among the products and services offered to Private Banking customers are time deposit products, capital guaranteed funds, mutual funds, Type A Type B funds, derivative products such as forwards, futures and options in domestic futures exchange (VOB) and international markets, personal loans, foreign exchange, gold and equity trading, pension plans, insurance products and 7/24 safe deposit boxes and e-banking services. Also, personal art advisory, inheritance advisory, real estate advisory, tax advisory and philanthropic advisory are offered within the Private Banking and Wealth Management activities.

The Group's widespread branch network and alternative distribution channels including ATMs, telephone banking, internet banking and mobile banking are utilized to serve customers in all segments. Foreign operations include the Group's banking transactions in the Netherlands, Azerbaijan, Russia and Malta. Treasury, Asset – Liability Management and other operations, mainly consist of treasury management's results, operations of supporting business units and other unallocated transactions.

The below table is prepared in accordance with the Management Information System (MIS) data of the Group.

(Amounts expressed in thousands of TL unless otherwise indicated.)

37. Segment analysis (continued)

The Group's management manages segment performance based on IFRS consolidated figures.

December 31, 2017	Retail banking	Corporate banking Commercial banking	Private banking wealth management	Foreign operations	Domestic operations	Treasury, asset liability man, & Other(1)	Eliminations(2)	Group
Segment revenue	4,579,996	3,191,097	283,198	306,686	741,203	2,783,071	44,104	11,929,355
Segment expenses	(4,482,210)	(1,105,333)	(111,165)	(124,772)	(273,595)	(1,662,891)	7,258	(7,752,708)
Segment result	97,786	2,085,764	172,033	181,914	467,608	1,120,180	51,362	4,176,647
Operating profit	**97,786**	**2,085,764**	**172,033**	**181,914**	**467,608**	**1,120,180**	**51,362**	**4,176,647**
Share of results of associates and joint ventures	-	-	-	-	-	87,612	-	87,612
Profit before tax	**97,786**	**2,085,764**	**172,033**	**181,914**	**467,608**	**1,207,792**	**51,362**	**4,264,259**
Income tax expense(4)	-	-	-	-	-	(839,270)	-	(839,270)
Profit for the year	**97,786**	**2,085,764**	**172,033**	**181,914**	**467,608**	**368,522**	**51,362**	**3,424,989**
December 31, 2017								
Segment assets(3)	81,615,765	102,324,599	205,198	10,301,937	20,009,244	105,416,027	(3,125,534)	316,747,236
Associates and joint ventures	-	-	-	-	-	790,411	-	790,411
Total assets	**81,615,765**	**102,324,599**	**205,198**	**10,301,937**	**20,009,244**	**106,206,438**	**(3,125,534)**	**317,537,647**
Segment liabilities(3)	74,240,206	61,810,968	30,541,901	8,257,860	17,503,365	128,773,313	(3,589,966)	317,537,647
Total liabilities	**74,240,206**	**61,810,968**	**30,541,901**	**8,257,860**	**17,503,365**	**128,773,313**	**(3,589,966)**	**317,537,647**

(1) Other segment liabilities also include the equity.
(2) Consolidation adjustments include transactions with subsidiaries and investments consolidated and other consolidated adjustments in these financial statements.
(3) Segment asset and liabilities figures are prepared according to Management Information Systems (MIS) data.
(4) Income tax expenses have not been distributed based on operating segments and have been presented under "Treasury, asset liability management and other".

December 31, 2016	Retail banking	Corporate banking Commercial banking	Private banking wealth management	Foreign operations	Domestic operations	Treasury, asset liability man, & Other(1)	Eliminations(2)	Group
Segment revenue	4,352,372	2,806,216	236,421	257,663	632,382	2,700,788	61,908	11,047,750
Segment expenses	(4,331,137)	(1,020,631)	(102,516)	(119,531)	(233,476)	(1,302,518)	6,968	(7,102,841)
Segment result	21,235	1,785,585	133,905	138,132	398,906	1,398,270	68,876	3,944,909
Operating profit	**21,235**	**1,785,585**	**133,905**	**138,132**	**398,906**	**1,398,270**	**68,876**	**3,944,909**
Share of results of associates and joint ventures	-	-	-	-	-	85,362	-	85,362
Profit before tax	**21,235**	**1,785,585**	**133,905**	**138,132**	**398,906**	**1,483,632**	**68,876**	**4,030,271**
Income tax expense(4)	-	-	-	-	-	(781,936)	-	(781,936)
Profit for the year	**21,235**	**1,785,585**	**133,905**	**138,132**	**398,906**	**701,696**	**68,876**	**3,248,335**
December 31, 2016								
Segment assets(3)	68,420,767	87,360,696	156,652	9,235,035	16,804,261	89,217,723	(3,344,929)	267,850,205
Associates and joint ventures	-	-	-	-	-	682,728	-	682,728
Total assets	**68,420,767**	**87,360,696**	**156,652**	**9,235,035**	**16,804,261**	**89,900,451**	**(3,344,929)**	**268,532,933**
Segment liabilities(3)	61,218,411	55,827,497	32,536,775	7,482,674	14,577,348	100,686,053	(3,795,825)	268,532,933
Total liabilities	**61,218,411**	**55,827,497**	**32,536,775**	**7,482,674**	**14,577,348**	**100,686,053**	**(3,795,825)**	**268,532,933**

(1) Other segment liabilities also include the equity.
(2) Consolidation adjustments include transactions with subsidiaries and investments consolidated and other consolidated adjustments in these financial statements.
(3) Segment asset and liabilities figures are prepared according to Management Information Systems (MIS) data.
(4) Income tax expenses have not been distributed based on operating segments and have been presented under "Treasury, asset liability management and other".

(Amounts expressed in thousands of TL unless otherwise indicated.)

38. Related party transactions

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 or operational decisions, The Group is controlled by Koç Group and UCG, owning 50% of the ordinary shares each of KFS.

A number of transactions were entered into with related parties in the normal course of business.

(i) Balances with related parties:

	December 31, 2017			
	Parent	**Other(1)**	**Key management**	**Total**
Loans and advances to customers, net	146,696	2,759,670	79	2,906,445
Trading and investment securities	-	196,127	-	196,127
Derivative financial instruments	-	235	-	235
Loans and advances to banks	70,873	11,161	-	82,034
Other assets	-	840	-	840
Total assets	**217,569**	**2,968,033**	**79**	**3,185,681**
Customer deposits	13,273,046	9,923,386	181,550	23,377,982
Funds borrowed	27,580,765	89,128	-	27,669,893
Derivative financial instruments	6,384	6,420	-	12,804
Other liabilities	216	528	-	744
Deposits from banks	636,279	133,970	-	770,249
Total liabilities	**41,496,690**	**10,153,432**	**181,550**	**51,831,672**
Commitment under derivative instruments	4,585,782	3,974,124	-	8,559,906
Credit related commitments	1,358,830	3,088,681	-	4,447,511
Total commitments and contingent liabilities	**5,944,612**	**7,062,805**	**-**	**13,007,417**

	December 31, 2016			
	Parent	**Other(1)**	**Key management**	**Total**
Loans and advances to customers, net	460,887	2,808,226	59	3,269,172
Trading and investment securities	-	240,124	-	240,124
Derivative financial instruments	2,028	504	-	2,532
Loans and advances to banks	58,557	35,256	-	93,813
Other assets	5	1,296	-	1,301
Total assets	**521,477**	**3,085,406**	**59**	**3,606,942**
Customer deposits	11,536,318	7,241,686	218,528	18,996,532
Funds borrowed	18,958,940	301,269	-	19,260,209
Derivative financial instruments	23,293	11	-	23,304
Other liabilities	198	668	-	866
Deposits from banks	633,580	173,284	-	806,864
Total liabilities	**31,152,329**	**7,716,918**	**218,528**	**39,087,775**
Commitment under derivative instruments	8,532,884	802,512	-	9,335,396
Credit related commitments	1,158,561	2,595,229	-	3,753,790
Total commitments and contingent liabilities	**9,691,445**	**3,397,741**	**-**	**13,089,186**

(1) Other consists of entities with joint control or significant influence over entities, associates and joint ventures in which they are joint-venturer or related parties.

(Amounts expressed in thousands of TL unless otherwise indicated.)

38. Related party transactions (continued)

(ii) Transactions with related parties:

	December 31, 2017			
	Parent	**Other(1)**	**Key management**	**Total**
Interest income on loans and advances to customers	9,516	325,574	1	335,091
Fee and commission income	17,055	44,718		61,773
Interest income on financial leases	206	23,730	-	23,936
Interest income on loans and advances to banks	-	-	-	-
Total interest and fee income	**26,777**	**394,022**	**1**	**420,800**
Interest expense on deposits	(1,339,514)	(782,800)	(4,048)	(2,126,362)
Interest expense on funds borrowed	(119,300)	(68,066)	-	(187,366)
Other operating expense	(3,702)	(6,039)	-	(9,741)
Fee and commission expense	-	(128)	-	(128)
Total interest and fee expense	**(1,462,516)**	**(857,033)**	**(4,048)**	**(2,323,597)**

	December 31, 2016			
	Parent	**Other(1)**	**Key management**	**Total**
Interest income on loans and advances to customers	4,981	247,470	2	252,453
Fee and commission income	16,138	36,401	-	52,539
Interest income on financial leases	-	17,558	-	17,558
Interest income on loans and advances to banks	-	432	-	432
Total interest and fee income	**21,119**	**301,861**	**2**	**322,982**
Interest expense on deposits	(1,021,951)	(567,540)	(4)	(1,589,495)
Interest expense on funds borrowed	(85,425)	(70,965)	-	(156,390)
Other operating expense	(5,557)	(5,813)	-	(11,370)
Fee and commission expense	-	(308)	-	(308)
Total interest and fee expense	**(1,112,933)**	**(644,626)**	**(4)**	**(1,757,563)**

(1) Other consists of entities with joint control or significant influence over entities, associates and joint ventures in which they are a joint-venturer or related parties.

Salaries and other benefits paid to the Group’s key management approximately amount to TL 77,215 as of December 31, 2017 (2016 - TL 56,454).

A significant part of the related party balances and transactions are with related parties other than the parent or associate or joint venture; mainly comprising Koç Group and UCG entities.

39. Assets under management

At December 31, 2017, the Group managed 33 mutual funds (2016 - 35) with total fund value of TL 9,544,251 (2016 - TL 7,365,523) and 25 private pension funds (2016 - 21) with total fund value of TL 10,395,795 (2016 - TL 8,008,952), which were established under Capital Markets Board of Turkey (“CMB”) regulations.

40. Subsequent events

It has been decided by Board of Directors resolution to sell non-performing loans which is comprised of consumer loans, commercial loans and credit cards under follow-up amounting to TL 503,404 to Hayat Varlık Yönetim A.Ş and Istanbul Varlık Yönetim A.Ş for a total amount of TL 26,455 as of February 28, 2018.