

**Türkiye Garanti Bankası Anonim Şirketi  
And Its Affiliates**  
Consolidated Financial Statements  
30 September 2016  
With Report on Review of Interim  
Financial Information Thereon

24 October 2016

This report contains the "Independent Auditors' Review Report" comprising 1 page and; the "Consolidated Financial Statements and Their Explanatory Notes" comprising 81 pages.

**Türkiye Garanti Bankası Anonim Şirketi  
And Its Affiliates**

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To the Board of Directors of  
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## REVIEW REPORT FOR THE INTERIM FINANCIAL INFORMATION

### Introduction

We have reviewed the accompanying consolidated financial statements of Türkiye Garanti Bankası A.Ş. ("the Bank") and its consolidated affiliates (together "the Group"), which comprise the consolidated statement of financial position as at September 30, 2016, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the nine-month period then ended, and a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and fair presentation of this interim financial information in accordance with International Financial Reporting Standards. Our responsibility is to express a conclusion on this interim financial information based on our review.

### Scope of Review

We conducted our review in accordance with International Standard on Review Engagements 2410, Review of Interim Financial Information Performed by the Independent Auditor of the Entity. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

### Basis for Qualified Conclusion

Subsequent to the reversal of TL 42,000 thousands in the current period the accompanying consolidated financial statements include a general reserve amounting to TL 300,000 thousands as of the balance sheet date, provided by the Group management in line with conservatism principle considering the circumstances which may arise from any changes in the economy or market conditions.

### Qualified Conclusion

Based on our review, except for the effect of the matter described in the basis for qualified conclusion paragraph, nothing has come to our attention that causes us to believe that the accompanying interim financial information does not present fairly, in all material respects, the financial position of the Bank and its consolidated affiliates as at September 30, 2016, and of their financial performance and cash flows for the nine-month period then ended in accordance with International Financial Reporting Standards.

*DRT Bağımsız Denetim ve ŞMMM A.Ş.*

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

Istanbul, October 24, 2016

**Türkiye Garanti Bankası AŞ And Its Affiliates**  
**Consolidated Statement of Financial Position**  
**At 30 September 2016**

(Currency: Thousands of Turkish Lira (TL))

	<u>Notes</u>	<u>30 September 2016</u>	<u>31 December 2015</u>
<b>Assets</b>			
Cash and balances with central banks	4	17,713,279	6,802,108
Financial assets at fair value through profit or loss	5	1,088,356	660,193
Loans and advances to banks	6	12,196,236	14,378,087
Loans and advances to customers	7,23	190,272,052	175,681,692
Other assets	9	19,691,541	25,779,200
Investment securities	10,22,23	44,486,351	46,072,823
Investments in equity participations	11	41,386	41,216
Tangible and intangible assets	12	4,640,606	4,376,178
Goodwill, net	13	32,948	32,948
Deferred tax asset	20	879,961	1,013,552
<b>Total Assets</b>		<b><u>291,042,716</u></b>	<b><u>274,837,997</u></b>
<b>Liabilities</b>			
Deposits from banks	14	2,810,994	6,960,181
Deposits from customers	15	164,322,461	149,154,274
Obligations under repurchase agreements and money market fundings	16	18,678,332	16,567,796
Loans and advances from banks and other institutions	17	39,334,000	39,959,934
Bonds payable	18	15,128,623	15,511,597
Subordinated liabilities	19	-	159,792
Current tax liability	20	133,853	376,779
Deferred tax liability	20	37,586	19,512
Other liabilities, accrued expenses and provisions	21	14,859,120	14,122,442
<b>Total Liabilities</b>		<b><u>255,304,969</u></b>	<b><u>242,832,307</u></b>
<b>Equity attributable to owners of the bank</b>			
Share capital	22	5,146,371	5,146,371
Share premium	22	11,880	11,880
Unrealised gains/(losses) on available-for-sale assets	10,22	(132,595)	(283,792)
Hedging reserve	22	(404,796)	(241,097)
Actuarial gain/(loss)	22	(76,718)	(76,718)
Revaluation surplus on tangible assets	22	1,551,066	1,590,481
Translation reserve	22	875,037	696,557
Legal reserves	22	1,274,312	1,229,498
Retained earnings	22	27,235,289	23,705,893
		<b><u>35,479,846</u></b>	<b><u>31,779,073</u></b>
<b>Non-controlling interests</b>	22	<b><u>257,901</u></b>	<b><u>226,617</u></b>
<b>Total Equity</b>		<b><u>35,737,747</u></b>	<b><u>32,005,690</u></b>
<b>Total Liabilities and Equity</b>		<b><u>291,042,716</u></b>	<b><u>274,837,997</u></b>
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The notes on pages 5 to 81 are an integral part of these consolidated financial statements.

**Türkiye Garanti Bankası AŞ And Its Affiliates**  
**Consolidated Statement of Comprehensive Income**  
**For The Nine-Month Period Ended 30 September 2016**  
*(Currency: Thousands of Turkish Lira (TL))*

		1 January 2016- 30 September 2016	1 July 2016- 30 September 2016	Restated 1 January 2015- 30 September 2015	Restated 1 July 2015- 30 September 2015
<b>Statement of Income:</b>					
Interest income:-					
Interest on loans		13,048,811	4,555,684	10,659,772	3,826,917
Interest on securities		2,871,579	963,614	2,520,404	667,746
Interest on deposits at banks		343,856	126,382	198,694	69,792
Interest on lease business		323,937	108,713	293,241	104,849
Others		61,534	20,989	52,610	16,047
		16,649,717	5,775,382	13,724,721	4,685,351
Interest expense:-					
Interest on saving, commercial and public deposits		(4,987,643)	(1,652,695)	(4,155,355)	(1,430,564)
Interest on borrowings, obligations under repurchase agreements, money market and swap fundings		(2,578,373)	(726,325)	(2,194,909)	(1,544,668)
Interest on bonds payable		(809,567)	(282,847)	(707,512)	(261,059)
Interest on bank deposits		(252,458)	(144,577)	(123,363)	(64,118)
Interest on subordinated liabilities		(1,953)	(515)	(4,355)	(1,526)
Others		(16,962)	(2,153)	(11,969)	(1,265)
		(8,646,956)	(2,809,112)	(7,197,463)	(3,303,200)
<b>Net interest income before provisions for loans and other credit risks</b>		<b>8,002,761</b>	<b>2,966,270</b>	<b>6,527,258</b>	<b>1,382,151</b>
<b>Provisions for loans and other credit risks, net</b>	5,6,7,8,10, 21	<b>(1,430,451)</b>	<b>(600,981)</b>	<b>(1,184,531)</b>	<b>(435,490)</b>
<b>Net interest income after provisions for loans and other credit risks</b>		<b>6,572,310</b>	<b>2,365,289</b>	<b>5,342,727</b>	<b>946,661</b>
Fee and commission income		3,113,662	1,075,126	2,704,227	960,198
Fee and commission expense		(772,595)	(266,952)	(686,307)	(257,589)
<b>Net fee and commission income</b>	28	<b>2,341,067</b>	<b>808,174</b>	<b>2,017,920</b>	<b>702,609</b>
Premium income from insurance business		406,652	136,215	340,956	120,397
Gain on sale of assets	33	405,609	23,507	68,838	16,092
Trading gains, net	29	283,959	446,527	-	-
Foreign exchange gains, net		-	(365,084)	357,621	(382,344)
Other operating income	30	119,448	32,606	151,875	43,738
<b>Other operating income</b>		<b>1,215,668</b>	<b>273,771</b>	<b>919,290</b>	<b>(202,117)</b>
<b>Total operating income</b>		<b>10,129,045</b>	<b>3,447,234</b>	<b>8,279,937</b>	<b>1,447,153</b>
Salaries and wages		(1,504,385)	(532,052)	(1,522,157)	(536,311)
Employee benefits	21	(699,702)	(224,268)	(431,614)	(170,821)
Credit card rewards and promotion expenses		(511,285)	(204,457)	(582,307)	(224,304)
Rent expenses		(283,074)	(97,267)	(248,544)	(87,979)
Depreciation and amortization	9, 12	(255,596)	(87,844)	(213,245)	(66,464)
Taxes and duties other than on income		(222,076)	(36,334)	(176,819)	(62,270)
Communication expenses		(152,267)	(51,217)	(141,298)	(47,558)
Impairment losses, net (including general reserve, net)	9,11,12,13,21	(147,595)	(127,912)	(34,925)	4,490
Foreign exchange losses, net		(231)	(231)	-	-
Trading losses, net	29	-	-	(93,902)	1,133,128
Other operating expenses	30	(1,162,393)	(382,626)	(1,269,267)	(461,263)
<b>Total operating expenses</b>		<b>(4,938,604)</b>	<b>(1,744,208)</b>	<b>(4,714,078)</b>	<b>(519,352)</b>
<b>Income before tax</b>		<b>5,190,441</b>	<b>1,703,026</b>	<b>3,565,859</b>	<b>927,801</b>
Taxation charge	20	(1,027,211)	(366,017)	(735,690)	(205,296)
<b>Net income for the period</b>		<b>4,163,230</b>	<b>1,337,009</b>	<b>2,830,169</b>	<b>722,505</b>
<b>Other Comprehensive Income:</b>					
<i>(items that may be reclassified subsequently to statement of income)</i>					
Foreign currency translation differences for foreign operations	22	133,509	120,146	527,458	366,387
Fair value reserves (available-for-sale financial assets):					
Net change in fair values	22	413,739	(4,983)	(779,411)	(374,916)
Net amount transferred to income	22	(214,746)	24,136	(106,079)	(9,238)
Cash flow hedges:					
Effective portion of changes in fair value	22	(32,310)	25,712	(36,109)	(62,950)
Net amount transferred to income	22	(80,657)	(16,468)	61,069	36,958
Net investment hedge for foreign operations	22	(50,620)	(42,306)	(194,245)	(105,785)
Revaluation surplus on tangible assets		(31,878)	(31,878)	-	-
<i>(items that cannot be reclassified subsequently to statement of income)</i>					
Actuarial gain/(loss) related to employee benefits					
Effect of changes in actuarial assumptions	21	-	-	-	-
Change in measurement of plan liabilities arising from passage of time	21	-	-	-	-
<b>Other comprehensive income for the period, net of tax</b>		<b>137,037</b>	<b>74,359</b>	<b>(527,317)</b>	<b>(149,544)</b>
<b>Total Comprehensive Income for the Period</b>		<b>4,300,267</b>	<b>1,411,368</b>	<b>2,302,852</b>	<b>572,961</b>
<b>Net income attributable to:</b>					
Equity holders of the Bank		4,130,722	1,327,119	2,804,803	713,863
Non-controlling interests		32,508	9,890	25,366	8,642
		<b>4,163,230</b>	<b>1,337,009</b>	<b>2,830,169</b>	<b>722,505</b>
<b>Total comprehensive income attributable to:</b>					
Equity holders of the Bank		4,267,773	1,401,492	2,277,496	564,310
Non-controlling interests		32,494	9,876	25,356	8,651
		<b>4,300,267</b>	<b>1,411,368</b>	<b>2,302,852</b>	<b>572,961</b>
<b>Weighted average number of shares with a face value of Kr 1 each</b>	22	<b>420 billions</b>	<b>420 billions</b>	<b>420 billions</b>	<b>420 billions</b>
<b>Basic and diluted earnings per share (full TL amount per TL 1 face value each)</b>		<b>0.984</b>	<b>0.316</b>	<b>0.668</b>	<b>0.170</b>

## Türkiye Garanti Bankası AŞ And Its Affiliates

### Consolidated Statement of Changes in Equity For The Nine-Month Period Ended 30 September 2016

(Currency: Thousands of Turkish Lira (TL))

	Share Capital	Share Premium	Unrealised Gains/(Losses) on Available-for-Sale Assets	Hedging Reserve	Translation Reserve	Legal Reserves	Actuarial Gain/(Loss)	Revaluation Surplus on Tangible Assets	Retained Earnings	Non-Controlling Interests	Total Equity
<b>Restated balances at 31 December 2014</b>	<b>5,146,371</b>	<b>11,880</b>	<b>88,631</b>	<b>(191,244)</b>	<b>367,064</b>	<b>1,182,824</b>	<b>(53,170)</b>	<b>-</b>	<b>20,543,485</b>	<b>193,733</b>	<b>27,289,574</b>
Foreign exchange difference on foreign currency legal reserves	-	-	-	-	-	4,609	-	-	-	-	4,609
Transfer to legal reserves	-	-	-	-	-	41,634	-	-	(41,634)	-	-
Dividends paid	-	-	-	-	-	-	-	-	(567,000)	(1,354)	(568,354)
Net unrealised market value losses from available-for-sale portfolio	-	-	(779,401)	-	-	-	-	-	-	(10)	(779,411)
Net gains on available-for-sale assets transferred to income statement at disposal	-	-	(106,079)	-	-	-	-	-	-	-	(106,079)
Foreign currency translation differences for foreign operations	-	-	(11,985)	-	253,085	-	-	-	-	-	241,100
Net fair value gains from cash flow hedges	-	-	-	154,497	-	-	-	-	-	-	154,497
Net investment hedge for foreign operations	-	-	-	(281,749)	281,749	-	-	-	-	-	-
Net income for the nine-month period	-	-	-	-	-	-	-	-	2,804,803	25,366	2,830,169
<b>Restated Balances at 30 September 2015</b>	<b>5,146,371</b>	<b>11,880</b>	<b>(808,834)</b>	<b>(318,496)</b>	<b>901,898</b>	<b>1,229,067</b>	<b>(53,170)</b>	<b>-</b>	<b>22,739,654</b>	<b>217,735</b>	<b>29,066,105</b>
Foreign exchange difference on foreign currency legal reserves	-	-	-	-	-	(1,734)	-	-	-	-	(1,734)
Transfer to legal reserves	-	-	-	-	-	2,165	-	-	(2,165)	-	-
Net unrealised market value gains from available-for-sale portfolio	-	-	446,901	-	-	-	-	-	-	15	446,916
Net gains on available-for-sale assets transferred to income statement at disposal	-	-	(2,962)	-	-	-	-	-	-	-	(2,962)
Foreign currency translation differences for foreign operations	-	-	81,103	-	(115,546)	-	-	(146)	-	-	(34,589)
Revaluation surplus on tangible and intangible assets	-	-	-	-	-	-	-	1,590,627	-	-	1,590,627
Net fair value losses from cash flow hedges	-	-	-	(107,635)	-	-	-	-	-	-	(107,635)
Net investment hedge for foreign operations	-	-	-	185,034	(89,795)	-	-	-	-	-	95,239
Net change in actuarial gain/(loss) related to employee benefits	-	-	-	-	-	-	(23,548)	-	-	20	(23,528)
Net income for three-month period	-	-	-	-	-	-	-	-	968,404	8,847	977,251
<b>Balances at 31 December 2015</b>	<b>5,146,371</b>	<b>11,880</b>	<b>(283,792)</b>	<b>(241,097)</b>	<b>696,557</b>	<b>1,229,498</b>	<b>(76,718)</b>	<b>1,590,481</b>	<b>23,705,893</b>	<b>226,617</b>	<b>32,005,690</b>
Foreign exchange difference on foreign currency legal reserves	-	-	-	-	-	2,185	-	-	-	-	2,185
Transfer to legal reserves	-	-	-	-	-	42,629	-	-	(42,629)	-	-
Dividends paid	-	-	-	-	-	-	-	-	(567,000)	(1,210)	(568,210)
Net unrealised market value gains/(losses) from available-for-sale portfolio	-	-	413,753	-	-	-	-	-	-	(14)	413,739
Net gains on available-for-sale assets transferred to income statement at disposal	-	-	(214,746)	-	-	-	-	-	-	-	(214,746)
Foreign currency translation differences for foreign operations	-	-	(47,810)	(112)	178,480	-	-	766	-	-	131,324
Revaluation surplus on tangible and intangible assets	-	-	-	-	-	-	-	(40,181)	8,303	-	(31,878)
Net fair value losses from cash flow hedges	-	-	-	(112,967)	-	-	-	-	-	-	(112,967)
Net investment hedge for foreign operations	-	-	-	(50,620)	-	-	-	-	-	-	(50,620)
Net income for the nine-month period	-	-	-	-	-	-	-	-	4,130,722	32,508	4,163,230
<b>Balances at 30 September 2016</b>	<b>5,146,371</b>	<b>11,880</b>	<b>(132,595)</b>	<b>(404,796)</b>	<b>875,037</b>	<b>1,274,312</b>	<b>(76,718)</b>	<b>1,551,066</b>	<b>27,235,289</b>	<b>257,901</b>	<b>35,737,747</b>

**Türkiye Garanti Bankası AŞ And Its Affiliates**  
**Consolidated Statement of Cash Flows**  
**For The Nine-Month Period Ended 30 September 2016**

(Currency: Thousands of Turkish Lira (TL))

	<u>Notes</u>	<b>1 January 2016- 30 September 2016</b>	<b>Restated 1 January 2015- 30 September 2015</b>
<b>Cash flows from operating activities:-</b>			
Interests and commissions received		16,459,281	13,760,645
Interests and commissions paid		(9,415,360)	(8,136,137)
Other operating activities, net		1,592,627	(449,436)
Cash payments to employees and suppliers		<u>(4,248,039)</u>	<u>(4,315,012)</u>
		4,388,509	860,060
<b>(Increase)/decrease in operating assets:-</b>			
Loans and advances to banks		(8,087,205)	(3,018,756)
Balances with central banks		5,971,167	(630,425)
Financial assets at fair value through profit or loss		(427,467)	239,423
Loans and advances to customers		(11,538,203)	(25,647,604)
Consumer loans		(4,963,477)	(5,392,974)
Other assets		(225,896)	(187,184)
<b>Increase/(decrease) in operating liabilities:-</b>			
Deposits from banks		(4,148,684)	2,034,188
Deposits from customers		15,156,480	30,201,996
Obligations under repurchase agreements and money market fundings		2,115,923	2,588,544
Other liabilities		1,060,649	1,747,016
<b>Net cash (outflows)/inflows from operating activities before taxes and duties paid</b>		<b><u>(698,204)</u></b>	<b><u>2,794,284</u></b>
<b>Income taxes and other duties paid</b>		<b><u>(1,374,183)</u></b>	<b><u>(980,994)</u></b>
<b>Net cash (outflows)/inflows from operating activities</b>		<b><u>(2,072,387)</u></b>	<b><u>1,813,290</u></b>
<b>Cash flows from investing activities:-</b>			
Net decrease in investment securities		2,826,517	(1,081,310)
Interest received for investment securities		1,668,601	1,829,456
Dividends received		9,062	5,387
Proceeds from sale of tangible and intangible assets		255,124	169,165
Purchase of tangible and intangible assets		(901,109)	(378,302)
<b>Net cash inflows from investing activities</b>		<b><u>3,858,195</u></b>	<b><u>544,396</u></b>
<b>Cash flows from financing activities:-</b>			
(Decrease)/increase in loans and advances from banks and other institutions, net		(545,736)	2,887,828
Increase in bonds payable, net		(349,090)	1,810,198
(Decrease)/increase in subordinated liabilities, net		(158,355)	28,346
Dividends paid		(568,210)	(568,354)
<b>Net cash (outflows)/inflows from financing activities</b>		<b><u>(1,621,391)</u></b>	<b><u>4,158,018</u></b>
<b>Effect of exchange rate changes</b>		<b><u>273,324</u></b>	<b><u>1,551,067</u></b>
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b><u>437,741</u></b>	<b><u>8,066,771</u></b>
Cash and cash equivalents at the beginning of the period		<u>11,756,386</u>	<u>10,004,218</u>
<b>Cash and cash equivalents at the end of the period</b>	2	<b><u><u>12,194,127</u></u></b>	<b><u><u>18,070,989</u></u></b>

The notes on pages 5 to 81 are an integral part of these consolidated financial statements.

## **Overview of the Bank**

Türkiye Garanti Bankası AŞ (the Bank) is a bank domiciled in Turkey. The consolidated financial statements of the Bank as of and for the nine-month period ended 30 September 2016 comprise the Bank, its affiliates (the Affiliates) and their interest in associates.

### **(a) Brief History**

The foundation of the Bank was approved by the decree of the Council of Ministers numbered 3/4010 dated 11 April 1946 and its “Articles of Association” was published in the official gazette dated 25 April 1946. The Bank provides retail, commercial, corporate and small and medium size enterprises (SME) banking, leasing, insurance, asset management and factoring services through a network of 906 domestic branches, nine foreign branches, three representative offices abroad and 61 offices. In addition to its branches, the Bank has 100% ownership in three banks each of which is located in Amsterdam, Bucharest and Moscow. The Bank and its affiliates in total have 23,425 employees. The Bank’s head office is located at Levent Nispetiye Mahallesi Aytar Caddesi 2 Beşiktaş 34340 Istanbul, Turkey.

### **(b) Ownership**

As of 30 September 2016, group of companies under Banco Bilbao Vizcaya Argentaria SA (“BBVA”) that currently owns 39.90% shares of the Bank, is named the BBVA Group (the Group) and it is the main shareholder.

On 22 March 2011, BBVA had acquired; 78.120.000.000 shares of the Bank owned by GE Capital Corporation at a total nominal value of TL 781,200 thousands representing 18.60% ownership, and 26.418.840.000 shares of the Bank owned by Doğu Holding AŞ at a total nominal value of TL 264,188 thousands representing 6.19% ownership. BBVA, purchasing 24.89% shares of the Bank, had joint control on the Bank’s management together with group of companies under Doğu Holding AŞ (the Doğu Group).

Subsequently, on 7 April 2011, BBVA had acquired 503.160.000 shares at a nominal value of TL 5,032 thousands and increased its ownership in the Bank’s share capital to 25.01%. Accordingly, BBVA and the Doğu Group had mutual control on the Bank’s management.

Finally, in accordance with the terms of the agreement between BBVA and the Doğu Group which was previously disclosed on 19 November 2014, the sale of shares representing 14.89% of the share capital of the Bank with a face value of TL 625,380 thousands and 62.538.000.000 shares by the Doğu Group to BBVA, has been completed on 27 July 2015. Following the acquisition, BBVA’s stake in the Bank has reached to 39.90% and BBVA became the main shareholder. The Bank has moved to “Foreign Deposit Banks” category from “Private Deposit Bank” category by the Banking Regulation and Supervision Agency (the “BRSA”).

Accordingly, as of balance sheet date, the Doğu Group’s interest in the share capital of the Bank is at 10%.

## **Significant accounting policies**

### **(a) Statement of compliance**

The Bank and its Turkish affiliates maintain their books of accounts and prepare their statutory financial statements in Turkish Lira (TL) in accordance with the Accounting Practice Regulations as promulgated by the BRSA; Turkish Accounting Standards promulgated by the Public Oversight Accounting and Auditing Standards Authority; the Turkish Commercial Code; and the Turkish Tax Legislation (collectively, Turkish GAAP); the Bank’s foreign affiliates maintain their books of accounts and prepare their statutory financial statements in accordance with the generally accepted accounting principles and the related legislation applicable in the countries they operate.

The accompanying consolidated financial statements are based on the statutory records with adjustments and reclassifications for the purpose of fair presentation in accordance with International Financial Reporting Standards (“IFRS”). The accompanying consolidated financial statements are authorized for issue by the directors on 24 October 2016.



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

### **(b) Basis of preparation**

The accompanying consolidated financial statements are presented in thousands of TL, which is the Bank's functional currency.

The financial statements are prepared on the historical cost basis as adjusted for the effects of inflation that lasted until 31 December 2005, except that the following assets and liabilities are stated at their fair value if reliable measures are available: derivative financial instruments, instruments at fair value through profit or loss, available-for-sale financial assets and tangible assets held for sale.

The accounting policies set out below have been applied consistently by the Bank and its affiliates to all periods presented in these consolidated financial statements.

### **(c) Use of estimates and judgements**

The preparation of 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 recognized in the period in which the estimates are revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognized in the financial statements are in Notes 7, 9, 10, 12, 13, 17, 18, 20, 21, 23, 24, 25 and 32.

### **(d) Basis of consolidation**

The accompanying consolidated financial statements include the accounts of the parent company, the Bank, its affiliates and associates on the basis set out in sections below. The financial statements of the entities included in the consolidation have been prepared as of the date of the consolidated financial statements.

#### *Affiliates*

Affiliates are the entities controlled by the Bank. The control exists if and only if;

- when the Bank has the power over an affiliate which that power, directly or indirectly, give rights to govern the financial and operating policies of the entity so as to obtain benefits from its activities.
- exposure, or rights, to variable returns from its involvement with the affiliate.
- the ability to use its power over the affiliate to affect the amount of its returns.

The Bank reassesses its control power over its affiliates if there is an indication that there are changes to any of the three elements of control. The financial statements of affiliates are included in the consolidated financial statements from the date that control commences until the date that control ceases.

#### *Associates*

Associates are those entities in which the Bank and its affiliates have significant influence, but not control, over the financial and operating policies. The consolidated financial statements include the Bank and its affiliates' share of the total recognized gains and losses of associates on an equity accounting basis, from the date that significant influence commences until the date that significant influence ceases. When the Bank and its affiliates share of losses exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Bank and its affiliates has incurred obligations in respect of the associate.

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

### *Special purpose entities*

Special purpose entities are entities that are created to accomplish a narrow and well defined objective such as the securitisation of particular assets, or the execution of a specific borrowing or lending transaction. Special purpose entities are consolidated when the substance of the relationship between the Bank and the special purpose entity indicates that the special purpose entity is controlled by the Bank.

### *Transactions eliminated on consolidation*

Intercompany balances and transactions, and any unrealized gains and losses arising from intercompany transactions, are eliminated in the accompanying consolidated financial statements.

Unrealized gains arising from transactions with associates and jointly controlled entities are eliminated to the extent of the Bank and its affiliates' interest in the entity. Unrealized gains arising from transactions with associates are eliminated against the investment in the associate. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

## **(e) Foreign currency**

### *Foreign currency transactions*

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

### *Financial statements of foreign operations*

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

## **(f) Tangible and intangible assets and related depreciation**

### *Owned assets*

The costs of the tangible and intangible assets acquired before 31 December 2005 are restated for the effects of inflation in TL units current at 31 December 2005 pursuant to IAS 29. Such assets acquired after this date are recorded at their historical costs. Accordingly, they are carried at costs, less accumulated depreciation and impairment losses (refer to accounting policy (s)). As of 1 November 2015, changing the existing accounting policy, it has been decided to apply revaluation model for properties recorded under tangible and intangible assets instead of cost model in accordance with IAS 16. Accordingly, for all real estates registered in the ledger, a valuation study was performed by independent expertise firms.

### *Leased assets*

Leases in terms of which the Bank and its affiliates assume substantially all the risks and rewards of ownership are classified as financial leases. Tangible assets acquired by way of financial lease are stated at amounts equal to the lower of their fair values and the present value of the minimum lease payments at inception of the lease, less accumulated

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

depreciation (see below) and impairment losses (refer to accounting policy (s)). Lease liabilities are reduced through repayments of principal, while the finance charge component of the lease payment is charged directly to income.

#### *Internally generated softwares*

As per IAS 38, internally-generated softwares should be recognised as assets if they meet the below listed criterias:

- The technical feasibility of completing the asset so that it will be available for use,
- Availability of the intention to complete and use the asset,
- The ability to use the asset,
- Clarity in probable future economic benefits to be generated from the asset,
- The availability of adequate technical, financial and other resources to complete the development phase and to start using the asset,
- The availability to measure reliably the expenditure attributable to the asset during the development phase.

The directly attributable development costs of asset are included in the the cost of such assets, however the research costs are recognised as expense as incurred.

#### *Subsequent expenditure*

Expenditures incurred to replace a component of a tangible and intangible asset that is accounted for separately, and major inspection and overhaul costs, are capitalized. Other subsequent expenditures are capitalized only when it increases the future economic benefits embodied in the item of such assets. All other expenditures are reflected as expense in the statement of income as incurred.

Expenditures for major renewals and improvement of tangible and intangible assets are capitalized and depreciated over the remaining useful lives of the related assets.

#### *Depreciation*

The estimated useful lives and depreciation rates of tangible and intangible assets are as follows. Depreciation method in use was not changed in the current period.

<i>Tangible and intangible assets</i>	<i>Estimated useful lives (years)</i>	<i>Depreciation Rates (%)</i>
Buildings	50	2
Vaults	50	2
Motor vehicles	5-7	15-20
Other tangible and intangible assets	4-20	5-25

The estimated useful lives, residual values and depreciation methods are reviewed at least once a year, with the effect of any changes in estimate accounted for on a prospective basis.

#### *Investment property*

Land and buildings that are held to earn rentals or for capital appreciation or both rather than for use in production, supply of goods or services, administrative purposes or sale in the ordinary course of business are classified as investment property. As of 1 November 2015, changing the existing accounting policy, it has been decided to apply fair value model for investment properties instead of cost model in accordance with the IAS 40. Accordingly, for all the investment properties registered in the ledger, a valuation study was performed by independent expertise firms. Fair value changes in investment properties were accounted retrospectively in the income statement for the period they occurred.

Investment properties under fair value model are not depreciated.

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

### **(g) Goodwill**

Goodwill arose from business combinations and represents the excess of the total acquisition costs over the share of the Bank and its affiliates in the fair value of the net assets of the acquired companies at the dates of acquisitions. When the excess is negative, it is recognized immediately in income. Goodwill is assessed for indication of impairment at least annually using external and internal sources such as market value, information on any adverse effect on the acquired companies, market interest rates or other market rates of return on investments and carrying value of net assets. If any such indication exists, the recoverable amount of the goodwill is estimated. If the recoverable amount is less than the carrying amount, the carrying amount is reduced to its recoverable amount, and impairment loss is recognized as an expense in income. The losses arising from the impairment of goodwill are not reversed in a subsequent period.

### **(h) Financial instruments**

#### *Classification*

*Financial instruments at fair value through profit or loss* are those instruments that are principally held for the purpose of short-term profit taking. These include investments, certain loans and derivative contracts that are not designated as effective hedging instruments, and liabilities from short-term sales of financial instruments. All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported as trading assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported as trading liabilities.

The Bank classifies certain loans at their origination dates, as financial assets at fair value through profit or loss in compliance with IAS 39. Financial assets at fair value through profit or loss are initially recorded at cost and measured at fair value in subsequent periods.

*Loans and receivables* are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Bank and its affiliates provide money, goods and services directly to a debtor with no intention of trading the receivable. Loans and receivables comprise loans and advances to banks and customers.

*Available-for-sale assets* are financial assets that are not held for trading purposes, provided by the Bank and its affiliates, or held to maturity. Available-for-sale instruments include certain debt and equity investments.

*Held-to-maturity assets* are financial assets with fixed or determinable payments and fixed maturity that the Bank and its affiliates have the positive intent and ability to hold to maturity. These include certain loans and advances to banks and customers and certain debt investments.

#### *Recognition*

Financial assets at fair value through profit or loss and available-for-sale assets are initially recognized on the settlement date at which the Bank and its affiliates become a party to the contractual provisions of the instrument. From this date, any gains and losses arising from changes in fair value of the assets are recognized in income for the financial assets at fair value through profit or loss and in the other comprehensive income for available for-sale assets.

Held-to-maturity instruments, loans and receivables, deposits and subordinated liabilities are recognized in the statement of financial position on the date they are originated.

#### *Measurement*

Financial instruments are initially measured at fair value, including transaction costs.

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

Subsequent to initial recognition all trading instruments and available-for-sale assets are measured at fair value.

All non-trading financial liabilities, loans and receivables and held-to-maturity assets are measured at amortized cost less impairment losses. Amortized cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortized based on the effective interest rate of the instrument.

#### *Fair value measurement principles*

The fair values of financial instruments are based on 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. It is therefore measured with the quoted market prices at the date of the statement of financial position without any deduction for transaction costs. If a quoted market price is not available, fair value of an instrument is estimated using the available market information and the appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to develop the estimated fair value. Accordingly, the estimates made are not necessarily indicative of the amounts that could be realized in the current market.

The fair values of derivatives that are not exchange-traded are estimated at the amounts that the Bank and its affiliates would receive or pay to terminate the contracts at the date of the statement of financial position taking into account current market conditions and the current creditworthiness of the counterparties.

#### *Gains and losses on subsequent measurement*

Gains and losses arising from changes in the fair values of trading financial instruments are recognized in income. Whereas, gains and losses arising from changes in the fair value of cash flow hedges and available-for-sale assets are deferred as a separate component of equity until the hedged transaction impacts earnings or the available-for-sale assets are sold or impaired.

#### *Specific instruments*

*Cash and balances with central banks:* Cash and balances with central banks comprise cash balances on hand, cash deposited with the central banks and other cash items. Money market placements are classified in loans and advances to banks.

*Investments:* Investments held for the purpose of short-term profit taking are classified as trading instruments. Debt investments that the Bank and its affiliates have the intent and ability to hold to maturity are classified as held-to-maturity assets.

*Loans and advances to banks and customers:* Loans and advances provided by the Bank and its affiliates are classified as loans and receivables, and reported net of allowances to reflect the estimated recoverable amounts.

*Financial lease receivables:* Leases where the entire risks and rewards incident to ownership of an asset are substantially transferred to the lessee, are classified as financial leases. A receivable at an amount equal to the present value of the lease payments, including any guaranteed residual value, is recognized. The difference between the gross receivable and the present value of the receivable is unearned finance income and is recognized over the term of the lease using the effective interest rate method. Financial lease receivables are included in loans and advances to customers.

*Factoring receivables:* Factoring receivables are stated at fair value at initial recognition. Subsequent to the initial recognition, factoring transactions are accounted for at amortized costs.

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

### *Derecognition*

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognized when the rights to receive cash flows from the asset have expired; the Bank (and/or its affiliates) retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a ‘pass through’ arrangement; or the Bank (and/or its affiliates) has transferred its rights to receive cash flows from the asset and either has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset. A financial liability is derecognized when it is extinguished.

Available-for-sale assets and assets held for trading that are sold are derecognized and corresponding receivables from the buyer for the payment are recognized as of the date the Bank and its affiliates commit to sell the assets. The specific identification method is used to determine the gain or loss on derecognition.

Held-to-maturity instruments and loans and receivables are derecognized on the dates they are transferred by the Bank and its affiliates.

### **(i) Derivatives held for risk management purposes**

Derivatives held for risk management purposes are measured at fair value in the statement of financial position. The treatment for the changes in their fair value depends on their classification into the following categories:

#### *Cash flow hedge*

When a derivative is designated as a hedge of the variability in cash flows attributable to a particular risk associated with a recognized asset or liability or a highly probable forecast transaction that could affect the income, the effective portion of changes in the fair value of the derivative are recognized directly in other comprehensive income and presented in hedging reserve in equity. The amount recognized in other comprehensive income is removed and included in income in the same period as the hedged cash flows affect the income under the same line item as the hedged item. Any ineffective portion of changes in the fair value of the derivative is recognized immediately in income.

If the derivative expires or is sold, terminated, or exercised, or no longer meets the criteria for cash flow hedge accounting, or the designation is revoked, then hedge accounting is discontinued and the amount recognized in other comprehensive income and presented in the hedging reserve in equity remains there until the forecast transaction affects the income. If the forecast transaction is no longer expected to occur, then hedge accounting is discontinued and the balance in other comprehensive income is recognized immediately in income.

#### *Fair value hedge*

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recognized in income immediately, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The change in the fair value of the hedging instrument and the change in the hedged item attributable to the hedged risk are recognized in income relating to the hedged item.

Hedge accounting is discontinued when the Group revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. The fair value adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to income from that date.

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

### *Net investment hedge*

When a derivative or non-derivative financial liability is designated as a hedge of a net investment in a foreign operation, the effective portion of changes in the fair value of the hedging instrument is recognized directly in the shareholders' equity, in the foreign currency translation reserve. Any ineffective portion of changes in the fair value of the derivative is recognized immediately in income. The amount recognized in the shareholders' equity is removed and included in the income on disposal of the foreign operation.

The foreign currency risk arising from net investments in foreign operations are hedged with long-term foreign currency borrowings and currency translation differences arising from conversion of foreign investments and foreign currency borrowings into TL are accounted for translation reserve and hedging reserve, respectively, in equity.

### *Embedded derivatives*

Derivatives may be embedded in another contractual arrangement (a "host contract"). The Bank and its affiliates account for embedded derivatives separately from the host contract when the host contract is not itself carried at fair value through profit or loss, and the characteristics of the embedded derivatives are not clearly and closely related to the host contract. Separated embedded derivatives are accounted for depending on their classification, and are presented in the statement of financial position together with the host contract.

### **(j) Securities borrowing and lending business**

Investments lent under securities lending arrangements continue to be recognized in the statement of financial position and are measured in accordance with the accounting policy for the related assets as appropriate. Cash collateral received in respect of securities lent is recognized as liabilities to either banks or customers. Investments borrowed under securities borrowing agreements are not recognized in the statement of financial position as the related risks and rewards of such securities are not retained. Borrowed securities are recorded under commitments and contingencies. Cash collateral placements in respect of securities borrowed are recognized under loans and advances to either banks or customers depending on the type of counterparty.

### **(k) Repurchase and resale agreements over investments**

The Bank and its affiliates enter into purchases of investments under agreements to resell (reverse repo) substantially identical investments at a certain date in the future at a fixed price. Investments purchased subject to commitments to resell them at future dates are not recognized. The amounts paid are recognized in loans to either banks or customers. The receivables are shown as collateralized by the underlying security. Investments sold under repurchase agreements (repo) are recognized in the statement of financial position and are measured in accordance with the accounting policy for the related assets as appropriate. The proceeds from the sale of the investments are reported as "obligations under repurchase agreements and money market fundings", a liability account.

Income and expenses arising from the repurchase and resale agreements over investments are recognized on an accrual basis over the period of the transactions and are included in interest income or expense.

### **(l) Items held in trust**

Assets, other than cash deposits, held by the Bank and its affiliates in fiduciary or agency capacities for its customers and government entities are not included in the accompanying consolidated statement of financial position, since such items are not under the ownership of the Bank.

**Significant accounting policies (continued)**

**(m) Financial guarantees**

Financial guarantees are contracts that require the Bank and its affiliates to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognized at their fair value, and the initial fair value is amortised over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortised amount or the present value of any expected payment (when a payment under the guarantee has become probable).

**(n) Employee benefits**

*(i) Defined benefit plan*

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee and his/her dependants will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation.

The Bank has a defined benefit plan (“the Plan”) for its employees namely Türkiye Garanti Bankası Anonim Şirketi Emekli ve Yardım Sandığı Vakfı (“the Fund”). The Fund is a separate legal entity and a foundation recognized by an official decree, providing pension and post-retirement medical benefits to all Bank employees entitled to receive such benefits. This benefit plan is funded through contributions of both by the employees and the employer as required by Social Security Law numbered 506 and these contributions are as follows:

	<i>30 September 2016</i>	
	<i>Employer</i>	<i>Employee</i>
	<u>%</u>	<u>%</u>
Pension contributions	15.5	10.0
Medical benefit contributions	6.0	5.0

This benefit plan is composed of a) the contractual benefits of the employees, which are subject to transfer to Social Security Foundation (“SSF”) (“pension and medical benefits transferable to SSF”) (see Note 21) and b) other excess social rights and payments provided in the existing trust indenture but not transferable to SSF and medical benefits provided by the Bank for its constructive obligation (“excess benefits”).

*a) Pension and medical benefits transferable to SSF*

As discussed in Note 21, the Bank expects to transfer a portion of the obligation of the Fund to SSF. This transfer will be a settlement of that portion of the Fund’s obligation. Final legislation establishing the terms for this transfer was enacted on 8 May 2008. Although the settlement will not be recognized until the transfer is made, the Bank believes that it is more appropriate to measure the obligation as the value of the payment that would need to be made to SSF to settle the obligation at the date of the statement of financial position in accordance with the Temporary Article 20 of the Law No.5754: “Law regarding the changes in Social Insurance and General Health Insurance Law and other laws and regulations” (“New Law”). The pension disclosures set out in Note 21, therefore reflect the actuarial assumptions and mortality tables specified in the New Law, including a discount rate of 9.80%.

The pension benefits transferable to SSF are calculated annually by an independent actuary, who is registered with the Undersecretariat of the Treasury.

*b) Excess benefits not transferable to SSF*

The excess benefits, which are not subject to the transfer, are accounted for in accordance with IAS 19, “Employee Benefits”. The obligation in respect of the retained portion of the defined benefit pension plan is calculated by estimating the amount of future benefit that



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

employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value by using the projected unit credit method, and any unrecognized past service costs and the fair value of any plan assets are deducted.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions were directly charged to income in periods before the year 2013. As per the revised IAS 19, the actuarial gains/losses are recognized under shareholders' equity starting from 1 January 2013.

#### *(ii) Reserve for employee severance indemnity*

Reserve for employee severance indemnity represents the present value of the estimated future probable obligation of the Bank and its affiliates calculated in accordance with the Turkish Labor Law. In accordance with Turkish Labor Law, the Bank and its affiliates are required to make lump-sum payments to each employee whose employment is terminated due to retirement or before the retirement date for reasons other than resignation or misconduct and has completed at least one year of service.

Provision is made for the present value of the liability calculated using the projected unit credit method. All actuarial gains and losses were recognized immediately in income in prior periods. As per the revised IAS 19, the actuarial gains/losses are recognized under shareholders' equity starting from 1 January 2013.

#### *(iii) Short-term employee benefits*

The Bank provided for undiscounted short-term employee benefits earned during the financial periods as per services rendered in compliance with IAS 19.

### **(o) Operating leases**

Leases other than finance leases are classified as operating leases.

#### *As lessor*

Rental income from operating leases is recognized on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognized on a straight-line basis over the lease term.

#### *As lessee*

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognized as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognized as a liability. The aggregate benefit of incentives is recognized as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

### **(p) Taxes on income**

Taxes on income for the period comprise current taxes and deferred taxes. Current taxes on income comprises tax payable on the taxable income for the period, using tax rates enacted or substantively enacted at the reporting date, and; any adjustment in taxes payable for previous years.

Deferred income tax is provided, using the statement of financial position method, on all taxable temporary differences arising between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax

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

is not recognized for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable income or loss, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax liabilities and assets are recognized when it is probable that the future economic benefits resulting from the reversal of temporary differences will flow to or from the Bank and its affiliates. Deferred tax asset is recognized to the extent that it is probable that future taxable profit will be available against which the deferred tax asset can be utilized. Currently, enacted tax rates are used to determine deferred taxes on income.

An individual consolidated affiliate offsets deferred tax asset and deferred tax liability if the deferred tax asset and deferred tax liability relate to income taxes levied by the same taxation authority or where the legal right of offset exists.

Deferred taxes related to fair value remeasurement of available-for-sale assets and cash flow hedges, are charged or credited directly to equity and subsequently recognized in income together with the deferred gains or losses that are realized.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that is no longer probable that sufficient taxable income will be available to allow all or part of the asset to be recovered.

#### **(q) Offsetting**

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, there is a legally enforceable right to set off the amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses from a group of similar transactions.

#### **(r) Earnings per share**

Earnings per share disclosed in the accompanying consolidated statement of comprehensive income are determined by dividing net income by the weighted average number of shares outstanding during the period attributable to the shareholders of the Bank. In Turkey, companies can increase their share capital by making a pro-rata distribution of shares ("Bonus Shares") to existing shareholders from retained earnings. Additionally, considering the fact that the increase in the number of shares issued by way of bonus shares in fact does not require any cash injection by the shareholders; the number of issued shares outstanding before such bonus share issuances is adjusted for the proportionate change in the number of issued shares outstanding as if the event had occurred at the beginning of the earliest period reported.

#### **(s) Impairment**

Financial and non-financial assets are reviewed at each date of the statement of financial position to determine whether there is objective evidence of impairment. If any such indication exists, the asset's recoverable amount is estimated in order to determine the extent of the impairment loss, if any.

#### *Loans and receivables and held-to-maturity instruments*

The recoverable amounts of loans and receivables and held-to-maturity instruments, are calculated as the present values of the expected future cash flows discounted at the instrument's original effective interest rate. Short-term balances are not discounted.

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

Loans and receivables are presented net of specific and portfolio basis allowances for uncollectibility. Specific allowances are made against the carrying amount of loans and receivables that are identified as being impaired based on regular reviews of outstanding balances to reduce these loans and receivable to their recoverable amounts. In assessing the recoverable amounts of the loans and receivables, the estimated future cash flows are discounted to their present value using the loans' original effective interest rates. Portfolio basis allowances are maintained to reduce the carrying amount of portfolios of similar loans and receivables to their estimated recoverable amounts at the date of financial position. The expected cash flows for portfolios of similar assets are estimated based on previous experience and considering the credit rating of the underlying customers and late payments of interest or penalties. Increases in the allowance account are recognized in income. When a loan is known to be uncollectible, all the necessary legal procedures have been completed, and the final loss has been determined, the loan is written off directly. If in a subsequent period, the amount of impairment loss decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down or allowance is reversed through income.

#### *Financial assets remeasured to fair value*

The recoverable amount of an equity instrument is its fair value. The recoverable amount of debt instruments and purchased loans remeasured to fair value is calculated as the present value of the expected future cash flows discounted at the current market rate of interest.

Where an asset remeasured to fair value is impaired, the write-down is recognized in income.

If in a subsequent period, the amount of impairment loss decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through income.

#### **(t) Income and expense recognition**

##### *Interest income and expense*

Interest income and expense is recognized on an accrual basis by taking into account the effective yield of the asset or an applicable floating rate. Interest income and expense includes the amortization of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

##### *Fee and commission*

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

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

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

##### *Net trading income*

Net trading income includes gains and losses arising from disposals of financial assets at fair value through profit or loss, available-for-sale, and from trading derivatives.

##### *Dividend income*

Dividend income is recognized in income when the right to receive payment is established.

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

### *Insurance business*

*Premium income:* For short-term insurance contracts, premiums are recognized as income (earned premiums), net of premium ceded to reinsurer firms, proportionally over the period of coverage. The portion of premium received on in-force contracts that relates to unexpired risks at date of the statement of financial position is recognized as the reserve for unearned premiums that are calculated on a daily pro-rata basis. Premiums are shown before deduction of commissions and deferred acquisition cost, and are gross of any taxes and duties levied on premiums. For long-term insurance contracts, premiums are recognized as income when the premiums are due from the policyholders. Premiums received for long-term insurance contracts with discretionary participation feature (“DPF”), are recognized directly as liabilities.

*Unearned premium reserve:* Unearned premiums are those proportions of the premiums written in a period that relate to the period of risk subsequent to the date of the statement of financial position for all short-term insurance policies. In accordance with the incumbent legislation on the computation of insurance contract liabilities, unearned premium reserve set aside for unexpired risks as at the dates of the statements of financial position, has been computed on a daily pro-rata basis. The change in the provision for unearned premium is recognized in income in the order that income is recognized over the period of risk.

*Claims and provision for “outstanding” claims:* Claims are recognized in the period in which they occur, based on reported claims or on the basis of estimates when not reported. The claims provision is the total estimated ultimate cost of settling all claims arising from events, which have occurred up to the end of the accounting period. Full provision is accounted for outstanding claims, including claim settlements reported at the period-end. Incurred but not reported claims (“IBNR”) are also provided for under the provision for outstanding claims.

*Liability adequacy test:* At each statement of financial position date, asset-liability adequacy tests are performed to ensure the adequacy of the contract liabilities, net of related deferred acquisition costs. In performing these tests, current best estimates of future cash flows are used. Any deficiency is immediately charged to income.

*Income generated from pension business:* Income arising from asset management and other related services offered by the insurance affiliate of the Bank is recognized in the accounting period in which the service is rendered. Fees consist primarily of investment management fees arising from services rendered in conjunction with the issue and management of investment contracts where the insurance company actively manages the consideration received from its customers to fund a return that is based on the investment profile that the customer selected on origination of the instrument. These services comprise the activity of trading financial assets in order to reproduce the contractual services. In all cases, these services comprise an indeterminate number of acts over the life of the individual contracts.

*Mathematical provisions:* Mathematical provisions are the provisions recorded against the liabilities of the insurance affiliate of the Bank to the beneficiaries of long-term life, health and individual accident policies based on actuarial assumptions. Mathematical provisions consist of actuarial mathematical provisions for long term insurance contracts, saving portion of the saving life products classified as investment contracts and related profit sharing reserves.

Actuarial mathematical provisions are calculated as the difference between the net present values of premiums written in return of the risk covered by the insurance affiliate and the liabilities to policyholders for long-term insurance contracts based on the basis of actuarial mortality assumptions as approved by the Republic of Turkey Prime Ministry Undersecretariat of Treasury, which are applicable for Turkish insurance companies.

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

Profit sharing reserves are the reserves provided against income obtained from asset backing saving life insurance contracts. These contracts entitle the beneficiaries of those contracts to a minimum guaranteed crediting rate per annum or, when higher, a bonus rate declared by the insurance affiliate from the eligible surplus available to date.

Mathematical provisions are presented under “other liabilities, accrued expenses and provisions” in the accompanying consolidated financial statements.

**(u) Non-current assets held for sale**

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (disposal group) is available for immediate sale in its present condition.

Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

**(v) Segment reporting**

An operating segment is a component of the Bank and its affiliates that engage in business activities from which it may earn income and incur expenses, including income and expenses that relate to transactions with any of the Bank’s other components. All operating segments’ operating results are reviewed regularly by the management to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

**(y) New standards and interpretations**

**New and revised IFRSs applied with no material effect on the consolidated financial statements**

- IFRS 14 *Regulatory Deferral Accounts*
- Amendments to IFRS 11 *Accounting for Acquisition of Interests in Joint Operations*
- Amendments to IAS 16 and IAS 38 *Clarification of Acceptable Methods of Depreciation and Amortisation*
- Amendments to IAS 27 *Equity Method in Separate Financial Statements*
- Annual Improvements 2012-2014 Cycle *IFRS 5, IFRS 7, IAS 19, IAS 34*
- Amendments to IAS 1 *Disclosure Initiative*
- Amendments to IFRS 10, IFRS 12 and IAS 28 *Investment Entities: Applying the Consolidation Exception*

**New and revised IFRSs in issue but not yet effective**

- Amendments to IFRS 10 and IAS 28 *Sale of Contribution of Assets between an Investor and its Associate or Joint Venture*
- Amendments to IAS 12 *Recognition of Deferred Tax Assets for Unrealized Losses*
- Amendments to IAS 7 *Disclosure Initiative*
- IFRS 9 *Financial Instruments*
- IFRS 15 *Revenue from Contracts with Customers*
- IFRS 16 *Leases*
- Amendments to IFRS 15 *Revenue from Contracts with Customers*
- Amendments to IFRS 2 *Classification and Measurement of Share-Based Payment Transactions*
- Amendments to IFRS 4 Applying IFRS 9 'Financial Instruments' with IFRS 4 'Insurance Contracts'

**Significant accounting policies (continued)**

**(z) Restatements in prior years' consolidated financial statements**

As of 1 November 2015, changing the existing accounting policy, it has been decided to apply fair value model for investment properties instead of cost model in accordance with IAS 40. Accordingly, for all the investment properties registered in the ledger, a valuation study was performed by independent expertise firms. Fair value changes in investment properties were accounted retrospectively in the income statement for the period they occurred.

As of 31 December 2015, changing the existing accounting policy, it has been decided to account for taxation related levies and liabilities in the periods when the events resulting in such liabilities occurred instead of applying accrual basis of accounting as in prior years in accordance with the interpretation of IFRIC 21 "Levies".

As of 31 December 2015, in accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets", provisions are calculated and accounted for fee and commission income recognized in prior years but reimbursed in subsequent periods.

As of 31 December 2015, in accordance with IAS 1 "Presentation of Financial Statements", interest portion of derivative transactions performed for margin management purposes are reclassified from "trading gains/(losses), net" to "interest on borrowings, obligations under repurchase agreements and money market fundings" for a better presentation.

Due to the aforementioned accounting policy changes, the accompanying prior years' consolidated financial statements were restated as per IAS 8.

The effects of the adjusting entries on the prior period's consolidated financial statements are as follows:

<i>1 January - 30 September 2015</i>	<i>Reported</i>	<i>Correction</i>	<i>Restated</i>
Interest on Borrowings, Obligations Under Repurchase Agreements and Money Market and Swap Fundings	(1,402,750)	(792,159)	(2,194,909)
Trading Losses, net	(886,061)	792,159	(93,902)
Foreign Exchange Gains, net	410,163	(52,542)	357,621
Other Operating Expenses	(1,249,174)	(20,093)	(1,269,267)
Taxation Charge	(750,216)	14,526	(735,690)
<b>Net Income for the Period</b>	<b>2,888,278</b>	<b>(58,109)</b>	<b>2,830,169</b>

<i>1 July - 30 September 2015</i>	<i>Reported</i>	<i>Correction</i>	<i>Restated</i>
Interest on Borrowings, Obligations Under Repurchase Agreements and Money Market and Swap Fundings	(506,535)	(1,038,133)	(1,544,668)
Trading Gains, net	94,995	1,038,133	1,133,128
Foreign Exchange Losses, net	(346,039)	(36,305)	(382,344)
Other Operating Income	55,691	(11,953)	43,738
Depreciation and amortization	(87,107)	20,643	(66,464)
Other Operating Expenses	(474,458)	13,195	(461,263)
Taxation Charge	(208,179)	2,883	(205,296)
<b>Net Income for the Period</b>	<b>734,042</b>	<b>(11,537)</b>	<b>722,505</b>

**Index for the notes to the consolidated financial statements:**

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## 1 Segment reporting

The Bank has seven reportable segments from banking and other financial institutions, as described in the business segments part 1.2 below, which are the Bank's strategic business units. The strategic business units offer different products and services, and are managed separately because they require different technology and marketing strategies. For each of the strategic business units, the senior management reviews internal reports regularly. The following summary describes the operations in each of the Bank's reportable segments:

### 1.1 Geographical segments

The Bank and its affiliates operate principally in Turkey, but also have operations in the Netherlands, Romania, Russia, Turkish Republic of Northern Cyprus, Malta, Luxembourg and Germany. Total geographic sector risk concentrations, both on and off balance sheet, are presented in the table below:

	<i>30 September 2016</i>				
	<i><u>Loans and Advances to Customers</u></i>	<i><u>Total Assets</u></i>	<i><u>Total Liabilities</u></i>	<i><u>Non-Cash Loans</u></i>	<i><u>Capital Expenditures</u></i>
Turkey	176,961,386	262,778,427	188,914,976	38,430,231	698,771
England	592,051	7,403,174	14,368,521	485,196	-
Romania	5,061,599	6,391,214	3,856,538	370,510	11,265
Netherlands	2,053,450	4,777,234	5,645,457	127,558	8,557
Malta	1,282,305	1,405,658	363,593	85,932	-
Germany	571,595	1,265,974	9,372,921	219,944	243
USA	452,619	1,184,558	5,946,287	3,610,576	-
Cyprus	571,936	1,084,898	940,991	54,647	-
Luxembourg	331,710	872,885	2,063,042	550	-
France	62,337	540,515	1,254,662	321,656	-
Russia	51,744	470,338	391,376	15,126	194
Switzerland	407,634	448,384	6,469,867	5,093,950	-
Sweden	339,816	342,406	104,968	104,776	-
Belgium	255,613	311,530	647,003	7,623	-
Spain	30,047	241,609	518,272	268,273	-
Singapore	159,561	230,657	642,202	598,414	-
United Arabian Emirates	137,902	142,045	3,176,713	1,681,485	-
Italy	103,391	127,144	650,786	407,736	-
Austria	56,108	73,707	523,291	13,465	-
Ukraine	36,888	36,940	121,063	7,519	-
Canada	28,398	33,813	477,589	86	-
Azerbaijan	29,258	29,276	1,289,465	289	-
China	15,863	16,254	912,373	311,129	-
Japan	149	5,720	150,734	457,977	-
Ireland	1,055	1,062	414,031	1,228	-
Qatar	126	126	228,470	1,012	-
Thailand	4	85	2,525,611	90	-
Others	677,507	827,083	3,334,167	498,308	-
	<u>190,272,052</u>	<u>291,042,716</u>	<u>255,304,969</u>	<u>53,175,286</u>	<u>719,030</u>



**1 Segment reporting (continued)**

	<i>31 December 2015</i>				
	<i>Loans and Advances to Customers</i>	<i>Total Assets</i>	<i>Total Liabilities</i>	<i>Non-Cash Loans</i>	<i>Capital Expenditures</i>
Turkey	163,802,800	244,302,162	175,982,568	35,542,769	866,801
England	885,866	10,162,400	16,984,801	1,365,027	-
Romania	4,590,331	6,061,830	2,990,211	351,800	10,159
Netherlands	1,002,887	4,149,594	6,011,617	324,905	7,170
USA	322,450	1,681,397	6,879,881	3,489,723	-
Malta	1,163,962	1,269,128	437,159	51,503	-
Germany	422,700	1,147,648	8,710,961	100,817	550
Luxembourg	394,451	908,219	2,091,847	520	-
Russia	107,750	821,392	354,008	16,780	118
Switzerland	745,620	779,928	7,420,042	4,289,798	-
France	86,802	563,091	1,924,134	372,976	-
Cyprus	159,850	470,060	806,344	53,598	-
Italy	359,859	374,633	739,145	510,323	-
Belgium	243,311	294,299	690,415	4,380	-
United Arabian Emirates	232,845	238,316	3,032,065	932,869	-
Singapore	156,924	214,445	138,482	26,856	-
Spain	51,246	166,708	388,299	546,365	-
Sweden	133,433	134,780	90,609	106,556	-
Azerbaijan	54,593	54,684	1,166,836	302	-
Ukraine	37,091	37,132	67,722	4,606	-
Austria	18,530	19,045	408,949	69,565	-
Qatar	-	14,265	173,868	474	-
Japan	3,726	8,574	146,354	242,152	-
Ireland	5,852	6,206	569,359	27	-
Canada	2,300	5,090	339,645	637	-
Thailand	-	377	1,146,762	626	-
China	-	32	20,433	296,055	-
Others	696,513	952,562	3,119,791	230,713	-
	<u>175,681,692</u>	<u>274,837,997</u>	<u>242,832,307</u>	<u>48,932,722</u>	<u>884,798</u>

Total geographic sector risk concentrations of the net income are presented in the table below:

	<i>Nine-month period ended 30 September 2016</i>	<i>Three-month period ended 30 September 2016</i>	<i>Nine-month period ended 30 September 2015</i>	<i>Three-month period ended 30 September 2015</i>
Turkey	3,858,060	1,202,874	2,380,208	648,708
Malta	213,387	87,178	322,746	37,499
Luxembourg	30,902	8,174	38,112	14,684
Netherlands	26,611	16,567	18,011	(2,112)
Romania	15,479	15,774	66,552	16,509
Others	18,791	6,442	4,540	7,217
	<u>4,163,230</u>	<u>1,337,009</u>	<u>2,830,169</u>	<u>722,505</u>

**Türkiye Garanti Bankası AŞ and Its Affiliates**

Notes to Consolidated Financial Statements

As of and for the Nine-Month Period Ended 30 September 2016

(Currency: Thousands of Turkish Lira (TL))

**1 Segment reporting (continued)**

**1.2 Business segments**

The main business segments are banking, leasing, insurance and factoring sectors. Banking segment information is detailed further to retail banking and commercial, corporate and SME banking as these are the major banking activities. Other operations heading under the banking segment include mainly treasury and investment banking activities as well as unallocated income and expense items. The analysis is as follows:

<u>30 September 2016</u>	<u>Retail Banking</u>	<u>Commercial, Corporate &amp; SME Banking</u>	<u>Other Operations</u>	<u>Total Banking</u>	<u>Leasing</u>	<u>Insurance</u>	<u>Factoring</u>	<u>Other Financial</u>	<u>Other Non-Financial</u>	<u>Combined</u>	<u>Eliminations</u>	<u>Total</u>
Operating income	3,848,285	2,937,876	2,404,134	9,190,295	185,856	434,836	52,533	209,219	98,777	10,171,516	(42,471)	10,129,045
Operating expenses	(2,675,640)	(1,382,132)	(422,405)	(4,480,177)	(57,746)	(201,570)	(31,517)	(133,100)	(69,084)	(4,973,194)	34,590	(4,938,604)
<b>Income from operations</b>	<b>1,172,645</b>	<b>1,555,744</b>	<b>1,981,729</b>	<b>4,710,118</b>	<b>128,110</b>	<b>233,266</b>	<b>21,016</b>	<b>76,119</b>	<b>29,693</b>	<b>5,198,322</b>	<b>(7,881)</b>	<b>5,190,441</b>
Taxation charge	-	-	(922,941)	(922,941)	(25,173)	(46,655)	(5,911)	(8,750)	(17,986)	(1,027,416)	205	(1,027,211)
<b>Net income for the period</b>	<b>1,172,645</b>	<b>1,555,744</b>	<b>1,058,788</b>	<b>3,787,177</b>	<b>102,937</b>	<b>186,611</b>	<b>15,105</b>	<b>67,369</b>	<b>11,707</b>	<b>4,170,906</b>	<b>(7,676)</b>	<b>4,163,230</b>
Segment assets	59,573,720	127,191,809	89,892,054	276,657,583	5,583,401	1,622,254	2,278,214	527,583	211,481	286,880,516	(1,432,701)	285,447,815
Investments in equity participations	-	-	431,291	431,291	10,528	275	-	2,645	112	444,851	(403,465)	41,386
Other assets	-	-	4,482,551	4,482,551	105,051	44,130	23,393	23,475	844,301	5,522,901	30,614	5,553,515
<b>Total assets</b>	<b>59,573,720</b>	<b>127,191,809</b>	<b>94,805,896</b>	<b>281,571,425</b>	<b>5,698,980</b>	<b>1,666,659</b>	<b>2,301,607</b>	<b>553,703</b>	<b>1,055,894</b>	<b>292,848,268</b>	<b>(1,805,552)</b>	<b>291,042,716</b>
Segment liabilities	109,600,440	64,090,838	74,330,019	248,021,297	4,694,444	400,701	2,120,740	502,844	920,718	256,660,744	(1,355,775)	255,304,969
Total equity	-	-	33,550,128	33,550,128	1,004,536	1,265,958	180,867	50,859	135,176	36,187,524	(449,777)	35,737,747
<b>Total liabilities and equity</b>	<b>109,600,440</b>	<b>64,090,838</b>	<b>107,880,147</b>	<b>281,571,425</b>	<b>5,698,980</b>	<b>1,666,659</b>	<b>2,301,607</b>	<b>553,703</b>	<b>1,055,894</b>	<b>292,848,268</b>	<b>(1,805,552)</b>	<b>291,042,716</b>

**Türkiye Garanti Bankası AŞ and Its Affiliates**

Notes to Consolidated Financial Statements

As of and for the Nine-Month Period Ended 30 September 2016

(Currency: Thousands of Turkish Lira (TL))

**1 Segment reporting (continued)**

	<i>Retail Banking</i>	<i>Commercial Corporate &amp; SME Banking</i>	<i>Other Operations</i>	<i>Total Banking</i>	<i>Leasing</i>	<i>Insurance</i>	<i>Factoring</i>	<i>Other Financial</i>	<i>Other Non- Financial</i>	<i>Combined</i>	<i>Eliminations</i>	<i>Total</i>
<b><u>30 September 2015</u></b>												
Operating income	2,614,245	2,980,720	1,864,477	7,459,442	173,563	351,238	48,901	109,860	179,468	8,322,472	(42,535)	8,279,937
Operating expenses	(2,730,030)	(1,190,638)	(359,076)	(4,279,744)	(50,444)	(167,765)	(26,975)	(78,678)	(149,315)	(4,752,921)	38,843	(4,714,078)
<b>Income from operations</b>	<b>(115,785)</b>	<b>1,790,082</b>	<b>1,505,401</b>	<b>3,179,698</b>	<b>123,119</b>	<b>183,473</b>	<b>21,926</b>	<b>31,182</b>	<b>30,153</b>	<b>3,569,551</b>	<b>(3,692)</b>	<b>3,565,859</b>
Taxation charge	-	-	(655,365)	(655,365)	(24,510)	(37,020)	(4,403)	(7,161)	(7,334)	(735,793)	103	(735,690)
<b>Net income for the period</b>	<b><u>(115,785)</u></b>	<b><u>1,790,082</u></b>	<b><u>850,036</u></b>	<b><u>2,524,333</u></b>	<b><u>98,609</u></b>	<b><u>146,453</u></b>	<b><u>17,523</u></b>	<b><u>24,021</u></b>	<b><u>22,819</u></b>	<b><u>2,833,758</u></b>	<b><u>(3,589)</u></b>	<b><u>2,830,169</u></b>
<b><u>31 December 2015</u></b>												
Segment assets	54,964,113	116,696,020	89,330,954	260,991,087	5,157,111	1,368,951	2,948,684	409,650	175,382	271,050,865	(1,676,762)	269,374,103
Investments in equity participations	-	-	431,287	431,287	10,490	275	-	2,516	112	444,680	(403,464)	41,216
Other assets	-	-	4,468,275	4,468,275	127,992	38,167	19,470	21,353	716,724	5,391,981	30,697	5,422,678
<b>Total assets</b>	<b><u>54,964,113</u></b>	<b><u>116,696,020</u></b>	<b><u>94,230,516</u></b>	<b><u>265,890,649</u></b>	<b><u>5,295,593</u></b>	<b><u>1,407,393</u></b>	<b><u>2,968,154</u></b>	<b><u>433,519</u></b>	<b><u>892,218</u></b>	<b><u>276,887,526</u></b>	<b><u>(2,049,529)</u></b>	<b><u>274,837,997</u></b>
Segment liabilities	99,097,088	58,183,209	78,507,506	235,787,803	4,361,014	327,959	2,802,410	398,850	759,637	244,437,673	(1,605,366)	242,832,307
Total equity	-	-	30,102,846	30,102,846	934,579	1,079,434	165,744	34,669	132,581	32,449,853	(444,163)	32,005,690
<b>Total liabilities and equity</b>	<b><u>99,097,088</u></b>	<b><u>58,183,209</u></b>	<b><u>108,610,352</u></b>	<b><u>265,890,649</u></b>	<b><u>5,295,593</u></b>	<b><u>1,407,393</u></b>	<b><u>2,968,154</u></b>	<b><u>433,519</u></b>	<b><u>892,218</u></b>	<b><u>276,887,526</u></b>	<b><u>(2,049,529)</u></b>	<b><u>274,837,997</u></b>

## 2 Cash and cash equivalents

Cash and cash equivalents include cash balances on hand, due from banks with original maturity periods of less than three months and other cash items. Cash and cash equivalents as of 30 September 2016 and 2015, included in the accompanying consolidated statements of cash flows are as follows:

	<i>30 September</i> <u>2016</u>	<i>30 September</i> <u>2015</u>
Cash at branches	2,200,992	2,318,650
Unrestricted balances with central banks	5,368,607	10,983,291
Placements at money markets	318,680	152,064
Loans and advances to banks with original maturity periods of less than three months	<u>4,305,848</u>	<u>4,616,984</u>
	<u>12,194,127</u>	<u>18,070,989</u>

## 3 Related party disclosures

For the purpose of this report, the shareholders either controlling or has a significant influence over the Bank, BBVA and Doğu Holding AŞ, respectively, and all their subsidiaries, and their ultimate owners, directors and executive officers and the Bank's unconsolidated affiliates are referred to as related parties. During the course of the business, the Bank has made placements with and granted loans to related parties and also received deposits from them at various terms. The Bank had the following balances outstanding from and transactions with related parties:

### 3.1 Outstanding balances

	<i>30 September</i> <u>2016</u>	<i>31 December</i> <u>2015</u>
<i>Statement of financial position</i>		
Loans and advances to banks	149,835	57,582
Loans and advances to customers	2,214,519	2,194,160
Miscellaneous receivables	1,034	1,220
Deposits from banks	422,277	288,554
Deposits from customers	697,377	613,522
Loans and advances from banks and other institutions	6,727	12,669
Miscellaneous payables	30,634	70,457
<i>Commitments and contingencies</i>		
Non-cash loans	1,329,472	1,267,542
Derivatives	23,901,596	16,416,097

### 3.2 Transactions

	<i>Nine-month period ended</i> <u>30 September 2016</u>	<i>Three-month period ended</i> <u>30 September 2016</u>	<i>Nine-month period ended</i> <u>30 September 2015</u>	<i>Three-month period ended</i> <u>30 September 2015</u>
Interest, fee and commission income	103,016	25,989	96,919	40,386
Interest, fee and commission expenses	5,191	1,177	20,119	12,032
Trading and foreign exchange gains/(losses), net	(478,969)	(333,444)	(8,598)	(38,187)
Other operating income	12,043	2,501	8,193	575
Other operating expenses	41,528	13,161	41,076	8,171

### 3 Related party disclosures (continued)

In the first nine-months of 2016, interest rates applied to foreign currency receivables from and payables to related parties vary within the ranges of 2%-15% and 1%-3% (31 December 2015: 2%-13% and 1%-2%), respectively. The interest rates applied to TL receivables from and payables to related parties vary within the ranges of 3%-20% and 7%-12%, respectively (31 December 2015: 10%-20% and 5%-13%). Various commission rates are applied to transactions involving guarantees and commitments. The pricing in transactions with the related parties is set on an arms-length basis.

No impairment losses or specific allowances have been recorded against balances outstanding during the period with related parties as of 30 September 2016 (30 September 2015: nil).

Key management personnel compensation for the nine-month period ended 30 September 2016 amounted TL 115,034 thousands (30 September 2015: TL 145,141 thousands) on a consolidated basis. Within this total, individual key management expenses of the Bank amounted TL 72,493 thousands (30 September 2015: TL 94,196 thousands) and of its affiliates amounted TL 42,541 thousands (30 September 2015: TL 50,945 thousands).

### 4 Cash and balances with central banks

	<i>30 September</i> <u>2016</u>	<i>31 December</i> <u>2015</u>
Cash at branches	2,200,992	2,199,132
Balances with central banks excluding reserve deposits	<u>15,512,287</u>	<u>4,602,976</u>
	<u>17,713,279</u>	<u>6,802,108</u>

### 5 Financial assets at fair value through profit or loss

	<i>30 September</i> <u>2016</u>				<i>31 December</i> <u>2015</u>
	<u>Face</u> <u>value</u>	<u>Carrying</u> <u>value</u>	<u>Interest rate</u> <u>range %</u>	<u>Latest</u> <u>maturity</u>	<u>Carrying</u> <u>value</u>
<i>Debt and other instruments held at fair value:</i>					
Gold	-	857,736	-	-	244,556
Government bonds in TL	72,724	75,460	3-11	2026	85,525
Investment fund	-	39,189	-	-	32,262
Government bonds indexed to CPI	22,679	29,254	1-4	2025	14,499
Eurobonds	6,778	7,721	3-12	2045	21,973
Bonds issued by financial institutions	6,326	6,528	4-14	2019	36,531
Bonds issued by corporations	6,279	6,338	12-15	2019	3,335
Discounted government bonds in TL	5,864	5,760	8-12	2025	1,519
Government bonds-floating (a)	5,339	<u>5,447</u>	8-11	2020	<u>7,722</u>
		1,033,433			447,922
<i>Loans held at fair value</i>		-			198,118
<i>Equity and other non-fixed income instruments:</i>					
Listed shares		<u>54,923</u>			<u>14,153</u>
Total financial assets at fair value through profit or loss		<u>1,088,356</u>			<u>660,193</u>

(a) The interest rates applied on these securities are floating quarterly based on interest rates of government bond bids of the government.

## 5 Financial assets at fair value through profit or loss (continued)

Income from debt and other instruments held at fair value is reflected in the consolidated statement of income as interest on securities. Gains and losses arising from trading of financial assets at fair value through profit or loss are recorded in net trading gains/(losses).

There is no impairment loss for the financial assets at fair value through profit or loss as of 30 September 2016 (30 September 2015: TL 12 thousands).

As of 30 September 2016, financial assets at fair value through profit or loss amounting to TL 11,265 thousands are blocked against asset management operations and securitizations (31 December 2015: TL 11,930 thousands) (refer to Note 10).

As of 30 September 2016, there are TL 2,025 thousands of securities pledged under repurchase agreements with customers (31 December 2015: TL 8,814 thousands).

## 6 Loans and advances to banks

	<u>30 September 2016</u>			<u>31 December 2015</u>		
	<u>TL</u>	<u>Foreign Currency</u>	<u>Total</u>	<u>TL</u>	<u>Foreign Currency</u>	<u>Total</u>
<i>Loans and advances-demand</i>						
Domestic banks	4,396	9,399	13,795	1,382	3,218	4,600
Foreign banks	<u>6,381</u>	<u>3,047,061</u>	<u>3,053,442</u>	<u>10,671</u>	<u>4,139,860</u>	<u>4,150,531</u>
	<u>10,777</u>	<u>3,056,460</u>	<u>3,067,237</u>	<u>12,053</u>	<u>4,143,078</u>	<u>4,155,131</u>
<i>Loans and advances-time</i>						
Domestic banks	1,004,307	1,604,823	2,609,130	952,644	1,499,003	2,451,647
Foreign banks	<u>47,778</u>	<u>6,103,567</u>	<u>6,151,345</u>	<u>11,905</u>	<u>7,644,493</u>	<u>7,656,398</u>
	<u>1,052,085</u>	<u>7,708,390</u>	<u>8,760,475</u>	<u>964,549</u>	<u>9,143,496</u>	<u>10,108,045</u>
Placements at money markets	<u>19,480</u>	<u>299,200</u>	<u>318,680</u>	<u>18,710</u>	<u>61,650</u>	<u>80,360</u>
Income accrual on loans and advances to banks	<u>28,309</u>	<u>21,535</u>	<u>49,844</u>	<u>15,342</u>	<u>19,209</u>	<u>34,551</u>
Total loans and advances to banks	1,110,651	11,085,585	12,196,236	1,010,654	13,367,433	14,378,087
Less: allowance for uncollectibility	-	-	-	-	-	-
Net loans and advances to banks	<u>1,110,651</u>	<u>11,085,585</u>	<u>12,196,236</u>	<u>1,010,654</u>	<u>13,367,433</u>	<u>14,378,087</u>

As of 30 September 2016, majority of loans and advances-time are short-term with interest rates ranging between 1%-11% per annum for foreign currency time placements and 1%-16% per annum for TL time placements (31 December 2015: 1%-8% and 1%-15%, respectively).

As of 30 September 2016, loans and advances at domestic and foreign banks include blocked accounts of TL 7,060,022 (31 December 2015: TL 7,694,176 thousands) held against securitizations, fundings and insurance business.

## 7 Loans and advances to customers

Outstanding loans and advances to customers are divided between economic sectors and loan types as follows:

	<i>30 September</i> <u>2016</u>	<i>31 December</i> <u>2015</u>
Consumer loans	59,043,571	54,080,094
<i>Mortgage loans</i>	21,759,483	19,341,743
<i>Credit card receivables</i>	16,039,020	14,981,373
<i>Auto loans</i>	1,885,819	1,553,478
<i>General purpose and other consumer loans</i>	19,359,249	18,203,500
Energy	20,662,739	18,866,417
Service sector	14,929,892	14,005,954
Construction	9,895,369	9,008,359
Financial institutions	8,233,400	7,886,038
Food	8,121,761	7,137,335
Transportation and logistics	7,494,823	5,616,571
Textile	7,149,388	6,433,026
Transportation vehicles and sub-industry	5,903,412	7,212,974
Metal and metal products	5,094,457	5,442,433
Tourism	5,026,783	4,919,498
Data processing	4,246,157	4,168,324
Chemistry and chemical products	3,806,157	3,309,528
Durable consumption	2,724,616	2,325,288
Agriculture and stockbreeding	2,278,392	2,177,618
Machinery and equipment	2,205,027	1,971,079
Stone, rock and related products	2,000,451	1,724,809
Mining	1,968,557	1,326,302
Paper and paper products	1,290,222	1,037,931
Electronic, optical and medical equipment	996,862	1,054,627
Plastic products	776,877	787,752
Others	<u>7,261,281</u>	<u>6,390,182</u>
Total performing loans	181,110,194	166,882,139
Financial lease receivables, net of unearned income (Note 8)	5,024,037	4,857,333
Factoring receivables	2,105,125	2,823,833
Income accrual on loans, factoring and lease receivables	2,712,699	2,244,728
Non-performing loans, factoring and lease receivables	6,970,335	6,090,168
Allowance for probable losses from loans, factoring and lease receivables	<u>(7,650,338)</u>	<u>(7,216,509)</u>
Loans and advances to customers	<u>190,272,052</u>	<u>175,681,692</u>

As of 30 September 2016, interest rates on loans granted to customers range between 1%-31% (31 December 2015: 1%-28%) per annum for the foreign currency loans and 1%-37% (31 December 2015: 1%-33%) per annum for the TL loans.

## 7 Loans and advances to customers (continued)

The provision for probable losses is comprised of amounts for specifically identified as being impaired and non-performing loans and advances and a further portfolio-basis amount considered adequate to cover the residual inherent risk of loss present in the lending relationships presently performing in accordance with agreements made with borrowers. The amount of the portfolio basis allowance is TL 2,331,173 thousands (31 December 2015: TL 1,759,922 thousands). Movements in the allowance for probable losses on loans, factoring and lease receivables including the portfolio basis allowances, are as follows:

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Balance at the beginning of the period	7,216,509	5,657,900
Write-offs	(1,152,974)	(433,073)
Recoveries and reversals	(783,167)	(904,159)
Provision for the period	<u>2,369,970</u>	<u>2,895,841</u>
Balance at the end of the period	<u>7,650,338</u>	<u>7,216,509</u>

A part of non-performing receivables of the Bank and its consolidated affiliates amounting to TL 749,828 thousands (30 September 2015: TL 190,861 thousands) was sold for a consideration of TL 74,967 thousands in the current period (30 September 2015: TL 34,568 thousands). Considering the related provision of TL 735,594 thousands (30 September 2015: TL 181,383 thousands) made in the financial statements in the prior periods, a gain of TL 60,707 thousands (30 September 2015: TL 25,067 thousands) is recognized under “gains on sale of assets” in the statement of income. The revenues earned from subsequent collections of the sold receivables in prior period, amounting to TL 84 thousands (30 September 2015: TL 1,767 thousands) is recognized in the income statement under “gains on sale of assets” in the current period.

## 8 Financial lease receivables

The financial leases typically run for a period of one to five years, with transfer of ownership of the leased asset at the end of the lease term. Interest is charged over the period of the lease. The receivables are secured by way of the underlying assets. Loans and advances to customers include the following financial lease receivables:

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Financial lease receivables, net of unearned income (Note 7)	5,024,037	4,857,333
Add: non-performing lease receivables	640,072	346,924
Less: allowance for probable losses on lease receivable	<u>(230,993)</u>	<u>(186,851)</u>
	<u>5,433,116</u>	<u>5,017,406</u>
Income accrual on lease receivables	<u>29,825</u>	<u>28,719</u>
<i>Analysis of net financial lease receivables</i>		
Due within 1 year	2,524,897	2,163,017
Due between 1 and 5 years	3,257,780	3,190,621
Due after 5 years	<u>327,196</u>	<u>365,799</u>
Financial lease receivables, gross	6,109,873	5,719,437
Unearned income	<u>(676,757)</u>	<u>(702,031)</u>
Financial lease receivables, net	<u>5,433,116</u>	<u>5,017,406</u>
<i>Analysis of net financial lease receivables</i>		
Due within 1 year	2,223,819	1,853,824
Due between 1 and 5 years	2,901,476	2,820,654
Due after 5 years	<u>307,821</u>	<u>342,928</u>
Financial lease receivables, net	<u>5,433,116</u>	<u>5,017,406</u>



## 9 Other assets

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Reserve deposits at central banks	15,163,672	21,094,712
Derivative financial assets	1,887,572	2,407,675
Investment properties	537,493	307,095
Tangible assets held for sale	490,659	366,365
Prepaid expenses, insurance claims and similar items	477,430	445,882
Option premium receivables	380,486	500,359
Miscellaneous receivables	363,959	285,235
Prepaid taxes and taxes/funds to be refunded	91,029	86,350
Insurance premium receivables	81,707	81,613
Balances with clearing house	7,914	39,823
Others	209,620	164,091
	<u>19,691,541</u>	<u>25,779,200</u>

### *Reserve deposits at central banks*

Reserve deposits at the Central Bank of Turkey are kept as minimum reserve requirement. These funds are not available for the daily business of the Bank and its affiliates. As required by the Turkish Banking Law, these reserve deposits are calculated on the basis of liabilities in TL, foreign currencies and gold taken at the rates determined by the Central Bank of Turkey. Turkish Lira reserve deposits earn interest monthly starting from November 2014, and quarterly starting from 2015, to be paid by Central Bank of Turkey on the first business day following the end of March, June, September and December. US\$ reserve deposits also earn interest starting from May 2015. The interest rates are calculated by Central Bank of Turkey according to market conditions.

The reserve deposits at the Central Bank of the Netherlands, as required by the Dutch Banking Law, are calculated as 1% on all customer deposits with an original maturity less than 2 years and 1% on bank deposits of non-EU banks with an original maturity less than 2 years. The reserve deposits are not required to be kept under blocked accounts in the Netherlands, therefore, such balances are classified under “cash and balances with central banks” in Note 4.

The banks operating in Romania are obliged to keep minimum reserve requirements in accounts held with Romanian Central Bank (NBR). The reserve requirements are to be held in RON for RON liabilities and in Euro or US\$ for foreign currency liabilities. Currently, in line with stipulations of related legislation in force, the rates for reserve requirements are 8% for RON denominated liabilities with a remaining maturity less than 2 years and 12% for foreign currency denominated liabilities with a remaining maturity less than 2 years excluding Romanian banks’ fundings. The interest rates paid by the NBR to banks for reserve requirements are subject of permanent update, currently the rates are 0.11% for RON reserves 0.06% for Euro reserves and 0.06% for US\$ reserves.

The reserve deposits at the Central Bank of Russia are not available for the daily business, as required by the Russian Banking Law, these reserve deposits are calculated on the basis of RUB and foreign currency liabilities taken at the rates determined by the Central Bank of Russia. In accordance with the current legislation, the reserve deposit rate for liabilities in rubles is 5.00%, rate for liabilities to individuals in foreign currency is 6.00%, and rate for other liabilities in foreign currency is 7.00%.

### *Tangible assets held for sale*

The tangible assets held for sale are comprised of foreclosed real estates acquired by the Bank against its impaired receivables and are intended to be sold shortly. Such assets are required to be disposed of within three years following their acquisitions per the Turkish Banking Law. This three year period can be extended by a legal permission from the regulators. In case of real estates held for sale, this requirement is valid only if the legal limit on the size of the real estate portfolio that a bank can maintain is exceeded. Currently, as the Bank is within this legal limit, it is not subject to the above requirement.

## 9 Other assets (continued)

Impairment losses provided on real estates held for sale were determined based on the appraisals of independent appraisal firms. As of 30 September 2016, real estates held for sale have been impaired by TL 32,212 thousands (31 December 2015: TL 24,302 thousands).

As of 30 September 2016, the rights of repurchase on various tangible assets held for sale amounted to TL 317,722 thousands (31 December 2015: TL 258,845 thousands).

### *Investment properties*

Movements in investment properties are as follows:

	<i>30 September</i> <u>2016</u>	<i>31 December</i> <u>2015</u>
Balance at the beginning of the period	307,095	296,191
Additions	228,791	-
Transfers to tangible assets	-	(18,009)
Fair value changes	-	29,279
Effects of movement in exchange rates	<u>1,607</u>	<u>(366)</u>
Balance at the end of the period	<u>537,493</u>	<u>307,095</u>

The investment properties are held for operational leasing purposes.

## 10 Investment securities

	<i>30 September</i> <u>2016</u>				<i>31 December</i> <u>2015</u>
	<u>Face</u> <u>value</u>	<u>Carrying</u> <u>value</u>	<u>Interest rate</u> <u>range %</u>	<u>Latest</u> <u>maturity</u>	<u>Carrying</u> <u>value</u>
<i>Debt and other instruments available-for-sale:</i>					
Government bonds indexed to CPI	6,018,306	7,778,960	1-4	2025	6,883,939
Government bonds in TL	5,924,083	6,086,708	3-11	2026	5,499,427
Government bonds at floating rates (a)	3,653,339	3,647,804	8-11	2020	6,074,069
Bonds issued by financial institutions	2,560,243	2,626,802	1-15	2027	3,235,670
Bonds issued by foreign governments	1,111,940	1,246,077	1-12	2028	1,246,837
Bonds issued by corporations	973,031	1,023,712	1-15	2028	812,449
Eurobonds	512,081	528,580	3-12	2041	526,266
Discounted government bonds in TL	43,700	43,091	9	2024	128,360
Others		<u>198,089</u>			<u>348,560</u>
Total securities available-for-sale		23,179,823			24,755,577
<i>Debt and other instruments held-to-maturity:</i>					
Government bonds indexed to CPI	6,677,313	7,298,498	1-4	2024	7,298,498
Eurobonds	5,025,315	5,844,940	6-12	2040	5,739,860
Bonds issued by financial institutions	3,142,861	3,082,079	4-6	2022	3,299,190
Government bonds in TL	2,607,531	2,521,608	6-10	2023	2,998,498
Bonds issued by corporations (b)	154,238	150,985	4-8	2021	146,746
Bonds issued by foreign governments	135,325	<u>135,325</u>	1-7	2017	<u>42,267</u>
		19,033,435			19,525,059
Income accrual on held-to-maturity portfolio		<u>2,273,093</u>			<u>1,792,187</u>
Total securities held-to-maturity		<u>21,306,528</u>			<u>21,317,246</u>
Total investment securities		<u>44,486,351</u>			<u>46,072,823</u>

(a) The interest rates applied on these securities are floating quarterly based on interest rates of government bond bids of the government.

(b) In the prior period, the Bank sold a part of its credit linked notes with a total face value of US\$ 300,000,000 before maturity as per the exceptions set out in IAS39 for the sale or reclassification of securities originally classified under debt and other instruments held-to maturity.

## 10 Investment securities (continued)

Interest income from debt and other fixed or floating instruments is reflected in interest on securities, whereas, gains and losses arising from changes in the fair values of available-for-sale assets are deferred as a separate component of equity.

There are no impairment losses on the investment securities as of 30 September 2016 (31 December 2015: nil).

Government bonds and treasury bills include securities pledged under repurchase agreements with customers amounting to TL 7,383,810 thousands (31 December 2015: TL 16,499,273 thousands).

The following table summarizes securities that were deposited as collateral with respect to various banking, insurance and asset management transactions:

	<u>30 September 2016</u>		<u>31 December 2015</u>	
	<u>Face Value</u>	<u>Carrying value</u>	<u>Face Value</u>	<u>Carrying value</u>
Collateralized to foreign banks	11,203,280	12,473,772	12,719,029	13,936,577
Deposited at central banks for interbank transactions	4,220,466	4,705,399	926,832	1,043,307
Deposited at central banks for repurchase transactions	760,089	878,824	2,562,224	2,684,281
Deposited at Borsa Istanbul	384,800	459,049	6,587,375	7,762,361
Deposited at Clearing Bank (Takasbank)	184,730	187,907	196,283	214,031
Deposited at CBT for foreign currency money market transactions	75,000	128,630	79,800	126,179
Others		19,734		19,292
		<u>18,853,315</u>		<u>25,786,028</u>

## 11 Investments in equity participations

	<u>30 September 2016</u>		<u>31 December 2015</u>	
	<u>Carrying Value</u>	<u>Ownership %</u>	<u>Carrying Value</u>	<u>Ownership %</u>
İstanbul Takas ve Saklama Bankası AŞ	27,636	5.25	27,636	5.25
Others	13,750		13,580	
	<u>41,386</u>		<u>41,216</u>	

The paid-in capital of Garanti Ödeme Sistemleri AŞ was decided to be increased from TL 350 thousands to TL 6,000 thousands at the board of directors meeting held on 13 December 2014. The ownership percentage of the Bank remained the same.

At the Bank's board of directors meeting held on 6 September 2014, it was decided to buy the shares of Garanti Hizmet Yönetimi AŞ and Garanti Ödeme Sistemleri AŞ, included in others above, for a consideration of TL 145 thousands and TL 7 thousands, respectively. The ownership percentage for Garanti Hizmet Yönetimi AŞ increased from 93.40% to 96.40%, and for Garanti Ödeme Sistemleri AŞ from 99.92% to 99.96%.

The board of directors of one of the Bank's consolidated affiliates decided to sell its shares in Garanti Turizm Yatırım ve Ortaklığı AŞ for a consideration of TL 4,028 thousands on 17 September 2014. The sale took place in October 2014.

The shares in Vadeli İşlem ve Opsiyon Borsası AŞ were replaced by the shares of Borsa İstanbul AŞ according to the article 138-6/b of the Capital Market Law no. 6362.

The legal name of İMKB Takasbank AŞ was changed as İstanbul Takas ve Saklama Bankası AŞ in 2013. The paid-in capital of İstanbul Takas ve Saklama Bankası AŞ was decided to be increased from TL 60,000 thousands to TL 420,000 thousands by TL 360,000 thousands of which TL 180,000 thousands was in cash, at the ordinary general meeting held on 29 March 2013. The Bank and its consolidated affiliate participated in this increase by TL 10,539 thousands in cash and also acquired bonus shares of TL 5,135 thousands. The ownership percentage remained the same.

## 11 Investments in equity participations (continued)

At the Bank's board of directors meeting held on 3 June 2009, it was decided to participate in the capital increase of Kredi Garanti Fonu AŞ, included in others above, by TL 4,000 thousands and to subscribe for future capital increases up to TL 4,000 thousands in restructuring of the company to build a three-shareholders structure including the Turkish Union of Chambers and Commodity Exchanges (TOBB), the Small and Medium Size Enterprises Development Organization (KOSGEB) and banks. As per this decision, the Bank has paid TL 2,000 thousands of its capital commitment of TL 4,000 thousands on 15 October 2009 for the capital increase of Kredi Garanti Fonu AŞ decided on 11 September 2009. The remaining balance was paid in two tranches in July 2011 and September 2012, by TL 1,000 thousands each.

Others include "Garanti Konut Finansmanı Danışmanlık Hizmetleri AŞ" which was established as per the decision made during the board of directors meeting of the Bank on 15 September 2007 to provide consultancy and outsourcing services to banks, housing finance and mortgage finance companies. Its legal registration process was completed on 3 October 2007. The Bank owns 100% of the company shares. The share capital of the company amounting TL 750 is fully paid. This company is not consolidated in the accompanying consolidated financial statements as currently it does not have material operations compared to the consolidated performance of the Bank and its affiliates, instead it is recorded under investments in equity participations in "others" above and valued at cost.

İstanbul Takas ve Saklama Bankası AŞ and other equity participations do not have a quoted market price in an active market and other methods of reasonably estimating their values would be inappropriate and impracticable, accordingly they are stated at cost, restated for the effects of inflation in TL units current at 31 December 2005.

There are no impairment losses on investments in equity participations as of 30 September 2016 (31 December 2015: nil). The cumulative provisions for impairment losses on investments in equity participations amounted to TL 85 thousands as of 30 September 2016 (31 December 2015: TL 85 thousands).

## 12 Tangible and intangible assets

Movement in tangible and intangible assets from 1 January to 30 September 2016 is as follows:

	<u>1 January</u>	<u>Additions</u>	<u>Effects of Movement in Exchange Rates</u>	<u>Revaluation Surplus</u>	<u>Disposals and Transfer</u>	<u>30 September</u>
<i>Costs</i>						
Land and buildings	2,444,444	11,261	8,416	(42,970)	59,722	2,480,873
Furniture, fixture, equipments and motor vehicles	2,593,173	472,685	9,607	-	(207,132)	2,868,333
Leasehold improvements	<u>1,045,159</u>	<u>133,268</u>	<u>8,581</u>	<u>-</u>	<u>(6,362)</u>	<u>1,180,646</u>
	6,082,776	617,214	26,604	(42,970)	(153,772)	6,529,852
<i>Less: Accumulated depreciation</i>						
Buildings	4,978	15,558	211	(90)	(265)	20,392
Furniture, fixture, equipments and motor vehicles	1,333,702	187,499	5,894	-	(84,960)	1,442,135
Leasehold improvements	<u>683,349</u>	<u>98,699</u>	<u>6,485</u>	<u>-</u>	<u>(7,495)</u>	<u>781,038</u>
	2,022,029	301,756	12,590	(90)	(92,720)	2,243,565
<i>Construction in progress</i>	<u>371,562</u>	101,816	53	-	(62,930)	<u>410,501</u>
	4,432,309					4,696,788
<i>Impairment in value of tangible and intangible assets</i>	<u>(56,131)</u>					<u>(56,182)</u>
	<u>4,376,178</u>					<u>4,640,606</u>

## 12 Tangible and intangible assets (continued)

Movement in tangible assets and intangible from 1 January to 31 December 2015 is as follows:

	<u>1 January</u>	<u>Additions</u>	<u>Effects of Movement in Exchange Rates</u>	<u>Revaluation Surplus</u>	<u>Depreciation Netted in Revaluation Model</u>	<u>Disposals and Transfer</u>	<u>31 December</u>
<i>Costs</i>							
Land and buildings	1,180,589	27,211	8,167	1,579,189	(359,368)	8,656	2,444,444
Furniture, fixture, equipments and motor vehicles	2,191,693	581,236	13,647	-	-	(193,403)	2,593,173
Leasehold improvements	<u>921,624</u>	<u>128,649</u>	<u>14,298</u>	-	-	<u>(19,412)</u>	<u>1,045,159</u>
	4,293,906	737,096	36,112	1,579,189	(359,368)	(204,159)	6,082,776
<i>Less: Accumulated depreciation</i>							
Buildings	335,922	25,330	1,247	-	(352,577)	(4,944)	4,978
Furniture, fixture, equipments and motor vehicles	1,211,735	208,974	7,220	-	-	(94,227)	1,333,702
Leasehold improvements	<u>579,140</u>	<u>112,533</u>	<u>9,383</u>	-	-	<u>(17,707)</u>	<u>683,349</u>
	2,126,797	346,837	17,850	-	(352,577)	(116,878)	2,022,029
<i>Construction in progress</i>	<u>203,630</u>	147,702	425	28,846	-	(9,041)	<u>371,562</u>
	2,370,739						4,432,309
<i>Impairment in value of tangible and intangible assets</i>	<u>(51,471)</u>						<u>(56,131)</u>
	<u>2,319,268</u>						<u>4,376,178</u>

Depreciation expense of tangible assets for the nine-month period ended 30 September 2016 amounted to TL 301,756 thousands (30 September 2015: TL 253,575 thousands).

As of 30 September 2016, the revaluation model effect, net of deferred tax, for real estates under tangible and intangible assets amounting to TL 1,551,066 thousands were accounted under shareholders' equity (31 December 2015: TL 1,590,481 thousands).

As of 30 September 2016, the net book value of real estates under cost model instead of revaluation model is TL 1,616,367 thousands (31 December 2015: TL 1,096,969 thousands).

In 2015, TL 56,131 thousands was provisioned and TL 51,517 thousands was reversed for land and buildings as per the valuation study performed in accordance with IAS36.

## 13 Goodwill

As of 30 September 2016, goodwill arises from the direct acquisitions of Garanti Yatırım Menkul Kıymetler AŞ, Garanti Finansal Kiralama AŞ, Garanti Emeklilik ve Hayat AŞ and Garanti Faktoring AŞ consisting of the excesses of the total acquisition costs over the fair values of the net assets of these consolidated entities at the dates of their acquisition as follows:

	<u>30 September 2016</u>	<u>31 December 2015</u>
Garanti Yatırım Menkul Kıymetler AŞ	20,984	20,984
Garanti Faktoring AŞ	6,697	6,697
Garanti Finansal Kiralama AŞ	5,233	5,233
Garanti Emeklilik ve Hayat AŞ	<u>34</u>	<u>34</u>
	32,948	32,948
Impairment of goodwill	<u>-</u>	<u>-</u>
	<u>32,948</u>	<u>32,948</u>

Impairment losses when necessary are provided for decrease in the net asset value of the consolidated entities by assessing their internal and external resources.

## 14 Deposits from banks

Deposits from banks comprise the following:

	<i>30 September</i> <u>2016</u>	<i>31 December</i> <u>2015</u>
Payable on demand	1,152,540	1,824,611
Term deposits	<u>1,653,108</u>	<u>5,129,721</u>
	2,805,648	6,954,332
Expense accrual on deposits from banks	<u>5,346</u>	<u>5,849</u>
	<u>2,810,994</u>	<u>6,960,181</u>

Deposits from banks include both TL accounts amounting to TL 672,400 thousands (31 December 2015: TL 1,927,442 thousands) and foreign currency accounts amounting to TL 2,133,248 thousands (31 December 2015: TL 5,026,890 thousands) in total. As of 30 September 2016, interest rates applicable to TL bank deposits and foreign currency bank deposits vary within ranges of 6%-12% and 1%-10% (31 December 2015: 6%-12% and 1%-11%), respectively.

## 15 Deposits from customers

Deposits from customers comprise the following:

	<i>30 September</i> <u>2016</u>			<i>31 December</i> <u>2015</u>
	<u><i>Demand</i></u>	<u><i>Time</i></u>	<u><i>Total</i></u>	<u><i>Total</i></u>
Foreign currency	21,178,848	70,610,075	91,788,923	83,464,399
Saving	8,826,033	42,501,484	51,327,517	46,195,917
Commercial	6,766,942	9,334,988	16,101,930	14,866,494
Public and other	1,290,610	1,814,101	3,104,711	2,853,450
Gold and other precious metals	<u>1,270,486</u>	<u>143,078</u>	<u>1,413,564</u>	<u>1,199,905</u>
	39,332,919	124,403,726	163,736,645	148,580,165
Expense accrual on deposits from customers	<u>17,931</u>	<u>567,885</u>	<u>585,816</u>	<u>574,109</u>
	<u>39,350,850</u>	<u>124,971,611</u>	<u>164,322,461</u>	<u>149,154,274</u>

As of 30 September 2016, interest rates applicable to TL deposits and foreign currency deposits vary within the ranges of 1%-15% and 1%-10% (31 December 2015: 1%-15% and 1%-12%), respectively.

## 16 Obligations under repurchase agreements and money market fundings

The Bank and its affiliates raise funds by selling financial instruments under agreements to repay the funds by repurchasing the instruments at future dates at the same price plus interest at a predetermined rate. Repurchase agreements are commonly used as a tool for short-term financing of interest-bearing assets, depending on the prevailing interest rates.

Obligations under repurchase agreements and money market fundings comprise the following:

	<i>30 September</i> <u>2016</u>	<i>31 December</i> <u>2015</u>
Money market fundings	11,398,866	426,678
Obligations under repurchase agreements	7,262,464	16,127,113
Obligations on securities under reverse repurchase agreements	<u>17,002</u>	<u>14,005</u>
	<u>18,678,332</u>	<u>16,567,796</u>

## 16 Obligations under repurchase agreements and money market fundings (continued)

Assets sold under repurchase agreements are further detailed as follows:

	<u>Carrying value</u>	<u>Fair value of underlying assets</u>	<u>Carrying amount of corresponding liabilities</u>	<u>Range of repurchase dates</u>	<u>Repurchase price</u>
<b>30 September 2016</b>					
Financial assets at fair value through profit or loss	2,025	2,025	2,060	Oct'16	2,061
Investment securities	<u>7,383,810</u>	<u>7,392,034</u>	<u>7,260,404</u>	Oct'16-Feb'25	<u>7,285,861</u>
	<u>7,385,835</u>	<u>7,394,059</u>	<u>7,262,464</u>		<u>7,287,922</u>
<b>31 December 2015</b>					
Financial assets at fair value through profit or loss	8,814	8,814	9,996	Jan'16	9,996
Investment securities	<u>16,499,273</u>	<u>16,492,406</u>	<u>16,117,117</u>	Jan'16-Feb'25	<u>16,288,306</u>
	<u>16,508,087</u>	<u>16,501,220</u>	<u>16,127,113</u>		<u>16,298,302</u>

The proceeds from the sale of securities under repurchase agreements are treated as liabilities and recorded as obligations under repurchase agreements. As of 30 September 2016, the maturities of the obligations varied from one day to 101 months and interest rates varied between 1%-10% (31 December 2015: 1%-14%). In general the carrying values of such assets are more than the corresponding liabilities due to the margins set between the parties, since such funding is raised against assets collateralized.

Expense accrual on obligations under repurchase agreements and money market fundings amounting to TL 14,983 thousands (31 December 2015: TL 20,370 thousands) is included in the carrying amount of corresponding liabilities.

## 17 Loans and advances from banks and other institutions

Loans and advances from banks and other institutions comprise the following:

	<u>30 September 2016</u>	<u>31 December 2015</u>
<u>Short-term borrowings</u>		
Domestic banks	899,634	1,239,704
Foreign banks	<u>12,744,592</u>	<u>12,408,195</u>
	13,644,226	13,647,899
<u>Long-term debts</u>		
Short-term portion	6,532,416	4,879,261
Medium and long-term portion	<u>18,896,181</u>	<u>21,205,296</u>
	25,428,597	26,084,557
Expense accrual on loans and advances from banks and other institutions	<u>261,177</u>	<u>227,478</u>
	<u>39,334,000</u>	<u>39,959,934</u>

As of 30 September 2016, loans and advances from banks and other institutions included various promissory notes amounting to TL 949,162 thousands in total with short-term maturities (31 December 2015: TL 1,244,891 thousands).

## 17 Loans and advances from banks and other institutions (continued)

As of 30 September 2016, short-term borrowings included two one-year-syndicated-loan facilities to be utilized for general trade finance purposes including export and import contracts in two tranches of (i) US\$ 479,325,000 and EUR 814,625,000 with rates of Libor + 0.85% and Euribor + 0.75% per annum with the participation of 42 banks from 15 countries (equivalent of TL 4,168,103 thousands), (ii) US\$ 266,550,000 and EUR 939,500,000 with rates of Libor + 0.75% and Euribor + 0.75% per annum with the participation of 39 banks from 16 countries (equivalent of TL 3,950,574 thousands).

Long-term debts comprise the following:

	30 September 2016				31 December 2015	
	Interest rate%	Latest maturity	Amount in original currency	Short term portion	Medium and long term portion	Medium and long term debts
DPR Future Flow Transaction-XVI	3	2034	US\$ 1 billions	-	2,992,000	2,908,000
DPR Future Flow Transaction-XVII	3	2034	US\$ 550 millions	-	1,645,600	1,599,400
Deutsche Bank AG-II	3	2019	US\$ 500 millions	-	1,496,000	1,454,000
DPR Future Flow Transaction-XVIII	2-3	2019	US\$ 500 millions	-	1,494,769	1,453,662
DPR Future Flow Transaction-XIV	3	2026	US\$ 398 millions	119,680	1,072,135	1,128,752
Bilateral Loan I	2	2017	US\$ 190 millions	-	568,480	552,520
Deutsche Bank AG-I	11-13	2017	TL 568 millions	-	568,150	568,150
ING DIBA	1	2017	US\$ 161 millions	184,299	297,421	289,952
Syndicated Loan	2	2018	US\$ 149 millions	-	445,645	431,874
EIB I	1-4	2022	US\$ 125 millions	66,681	307,035	342,427
DPR Future Flow Transaction-XV	3	2018	US\$ 116 millions	174,533	174,533	296,858
DPR Future Flow Transaction-XV	2	2018	EUR 90 millions	151,025	151,025	249,409
DPR Future Flow Transaction-XIX	2	2027	US\$ 100 millions	7,298	291,851	288,013
DPR Future Flow Transaction-XIX	2	2020	US\$ 90 millions	22,440	246,840	259,384
DPR Future Flow Transaction-IX	1	2018	EUR 69 millions	115,213	115,363	190,353
EIB III	10	2020	TL 219 millions	-	218,513	218,513
EIB II	9	2019	TL 206 millions	-	206,250	206,250
DPR Future Flow Transaction-VIII	1	2017	US\$ 56 millions	167,552	-	122,129
DPR Future Flow Transaction-XII	2	2022	EUR 49 millions	25,118	138,678	148,645
DPR Future Flow Transaction-XII	1	2022	EUR 49 millions	25,118	138,678	148,645
Bilateral Loan II	3	2019	US\$ 50 millions	-	149,600	-
OPIC	3	2019	US\$ 47 millions	43,085	96,941	125,626
EBRD-V	3	2017	US\$ 26 millions	51,291	25,646	49,851
EIB IV	9	2019	TL 69 millions	-	69,093	68,580
DPR Future Flow Transaction-VIII	1	2017	US\$ 16 millions	47,862	-	34,872
DPR Future Flow Transaction-VIII	1	2017	US\$ 16 millions	47,837	-	34,884
EBRD-II	1	2025	US\$ 12 millions	2,112	33,792	34,681
KfW	1	2017	EUR 7 millions	22,378	-	10,559
EBRD-IV	2	2017	EUR 6 millions	19,178	-	18,093
EFSE	4	2017	EUR 5 millions	16,804	-	15,888
Others				<u>5,222,912</u>	<u>5,952,143</u>	<u>7,955,326</u>
				<u>6,532,416</u>	<u>18,896,181</u>	<u>21,205,296</u>

In June 2016, the Bank secured a loan from international credit markets (Bilateral Loan II) in the amount of US\$50 millions with a maturity of three years and one week.

In December 2014, one of the Bank's consolidated affiliates signed a loan agreement with ING Bank (ING DIBA), in the amount of US\$ 125 millions in two equal tranches of one year (Tranche A) and two years (Tranche B) for the refinancing of trade finance loan portfolio. In December 2015, Tranche A of the secured facility was extended for 2 years and increased from US\$ 62.5 millions to US\$ 100 millions bringing the outstanding loan amount to US\$ 162.5 millions at that time.



## **17 Loans and advances from banks and other institutions (continued)**

In November 2015, the Bank secured a loan from international credit markets (Bilateral Loan I) in the amount of US\$ 190 millions with a maturity of two years and one week.

In September 2015, the Bank signed a syndicated loan agreement with 1098 days maturity in the amount of US\$ 150 millions with a rate of Libor + 1.85%.

In July 2015, the Bank completed a DPR Future Flow Transaction (“the DPR Future Flow Transaction XIX”) transaction; US\$ 100 millions with a maturity of 12 years, and US\$ 90 millions with a maturity of 5 years through its future cashflows under the DPR program.

In December 2014, the Bank signed a loan agreement with European Investment Bank (EIB) (EIB IV) in amount of TL 69,093 thousands (equivalent of EUR 25 millions) with a maturity of five years for the financing of small and medium sized enterprises.

In July 2014, the Bank signed a loan agreement with European Investment Bank (EIB) (EIB III) in amount of TL 218,513 thousands (equivalent of EUR 75 millions) with a maturity of six years for the financing of small and medium-sized enterprises.

In May 2014, the Bank completed a DPR Future Flow Transaction (the “DPR Future Flow Transaction XVIII”) transaction; US\$ 500 millions with a maturity of five years through its future cashflows under the DPR program.

In April 2014, the Bank completed a DPR Future Flow Transaction (the “DPR Future Flow Transaction XVII”) transaction; US\$ 550 millions with a maturity of 20 years through its future cashflows under the DPR program.

In December 2013, the Bank completed a DPR Future Flow Transaction (the “DPR Future Flow Transaction XVI”) transaction; US\$ 1 billions with a maturity of 21 years through its future cashflows under the DPR program.

The Bank classified its DPR Future Flow Transactions XVI, XVII and XVIII as financial liability at fair value through profit/loss at the initial recognition. As of 30 September 2016, the positive credit risk change amounting to TL 103,570 thousands is recognized in the statement of income (30 September 2015: TL 633,455 thousands).

In December 2013, the Bank signed a loan agreement with European Investment Bank (EIB) (EIB II) in amount of TL 206,250 thousands (equivalent of EUR 75 millions) with a maturity of six years for the financing of small and medium-sized enterprises.

In October 2013, the Bank completed a DPR Future Flow Transaction (the DPR Future Flow Transaction-XV) transaction, arranged by European Bank for Reconstruction and Development (EBRD), Wells Fargo Bank NA, Raiffeisen Bank International AG and Sumitomo Mitsui Banking Corporation in the amount of US\$ 175 millions and EUR 135 millions both with a maturity of five years.

In August 2013, the Bank signed a loan agreement with Kreditanstalt für Wiederaufbau (KfW) in the amount of EUR 20 millions with a maturity of four years for the financing of small and medium-sized enterprises.

In December 2012, one of the Bank’s consolidated affiliates signed a loan agreement with European Fund for Southeast Europe (EFSE) in the amount of EUR 25 millions with a maturity of five years for the financing of micro and small enterprises.

In November 2012, the Bank signed a loan agreement with EBRD (EBRD-V) in the amount of US\$ 60 millions with a maturity of five years for the financing of the women entrepreneurs.

In August 2012, the Bank completed a DPR Future Flow Transaction (the “DPR Future Flow Transaction-XIV) transaction by issuance of certificates, a tranche of US\$ 400 millions with 14 years maturity, granted directly by Overseas Private Investment Corporation (OPIC) to finance credit needs of SMEs across Turkey.

## **17 Loans and advances from banks and other institutions (continued)**

In December 2011, the Bank signed a credit agreement with EBRD (EBRD-IV) for a loan in the amount of EUR 40 millions with a maturity of five years for financing of small and medium size enterprises in agribusiness.

In June 2011, the Bank completed a DPR Future Flow Transaction (the “DPR Future Flow Transaction-XIII”) transaction, arranged by SMBC Nikko Securities America Inc., WestLB AG and Wells Fargo Securities LLC in the amount of US\$ 225 millions with a maturity of five years and by Standard Chartered Bank in the amount of EUR 50 millions with five years maturity.

In December 2010, the Bank completed a DPR Future Flow Transaction (the “DPR Future Flow Transaction-XII”) transaction, with the involvement of EIB in the amount of EUR 75 millions with 12 years maturity, by EBRD in the amount of EUR 75 millions with 12 years maturity, by West LB in the amount of EUR 100 millions with five years maturity.

In September 2010, the Bank signed a loan agreement with EBRD (EBRD-III) in the amount of EUR 50 millions which consists of 2 tranches for the financing of SMEs. The first tranche in the amount of EUR 20 millions with a maturity of five years has been financed by EBRD while the second tranche in the amount of EUR 30 millions with one year maturity by Standard Chartered Bank.

In June 2010, the Bank drew a second loan tranche worth of US\$ 60,050,000 (equivalent of EUR 50 millions) with a maturity of 12 years, within the EUR 150,000,000 framework agreement signed with EIB (EIB I) on 25 November 2009. The fund will be used for the financing of the investment and working capital needs of SMEs located in Turkey. In December 2009, the Bank had been granted another funding by EIB again for the financing of SME loans in the amount of US\$ 147,680,000 (equivalent of EUR 100 millions) with a maturity of 12 years.

In May 2010, the Bank signed a credit agreement with EBRD (EBRD-II) for a loan in the amount of US\$ 60 millions which consists of two tranches. The loan, which is funded directly by EBRD with the 5-year tranche of US\$ 48 millions and by the Clean Technology Fund which is established by the International Bank for Reconstruction and Development (the World Bank) in consultation with other international financial institutions, developed and developing countries and development partners, with the 15-year tranche of US\$ 12 millions, will be utilized for the financing of the energy efficiency needs of the small sized enterprises.

In December 2009, the Bank signed a credit agreement with OPIC for a facility for the financing of SMEs in the amount of US\$ 100 millions with a maturity of ten years.

In April 2009, the Bank borrowed US\$ 500 millions (Deutsche Bank AG-II) from Deutsche Bank AG, London with a maturity of ten years at 2.7% annual fixed-interest rate through a secured financing transaction. Accordingly, the Bank pledged US\$ 500 millions of cash collateral to Deutsche Bank AG, London at annual US\$ libor floating interest rate.

In August 2008, the Bank completed a DPR Future Flow Transaction (the “DPR Future Flow Transaction-IX”) transaction by issuance of certificates; a tranche of EUR 200 millions with ten years maturity from EIB.

In June 2007, the Bank completed a DPR Future Flow Transaction (the “DPR Future Flow Transaction-VIII”) transaction by issuance of certificates; three tranches of US\$ 550 millions with ten years maturity wrapped by Ambac Assurance Corp., Financial Guaranty Insurance Corp. and XL Capital Assurance and a tranche of US\$ 50 millions with eight years maturity and no financial guarantee.

In January 2007, the Bank borrowed TL 435 millions from Deutsche Bank AG, London with a maturity of ten years at 12.93% annual fixed interest rate through a secured financing transaction. Accordingly, the Bank pledged US\$ 300 millions of cash collateral to Deutsche Bank AG, London. Subsequently, the Bank has entered into two more secured financing transactions with the same counterparty under the same collateral conditions and borrowed in total TL 266 millions in two separate transactions on 28 June and 3 July 2007 with maturity of ten years for each and pledged US\$ 100 millions of cash collateral for each. The funding costs are 11.30% and 11.35%, respectively (Deutsche Bank AG-I). The cash collaterals earn annually US\$ libor floating interest rate.

## 17 Loans and advances from banks and other institutions (continued)

The DPR Future Flow Transaction is a way of securitizing the Bank's payment orders created via SWIFT MT 103 or similar payment orders in terms of US Dollar, Euro and GBP accepted as derived primarily from the Bank's trade finance and other corporate businesses and paid through foreign depository banks.

## 18 Bonds payable

Bonds payable comprise of the following:

	<u>30 September 2016</u>			<u>31 December 2015</u>
	<u>Latest maturity</u>	<u>Interest rate %</u>	<u>Amount</u>	<u>Amount</u>
Bonds payable of US\$ 2,632 millions	2022	0.7-6.4	7,195,407	7,963,319
Bonds payable of TL 5,004 millions	2018	7.5-12.1	4,709,789	4,495,626
Bonds payable of EUR 586 millions	2027	0.5-5.2	1,957,800	1,875,214
Bonds payable of AUD 175 millions	2018	5.6	400,140	370,913
Bonds payable of RON 450 millions	2019	5.5-6.3	337,378	313,252
Bonds payable of JPY 6,100 millions	2017	0.4-1.3	180,109	113,768
Bonds payable of CZK 340 millions	2016	2.4	42,228	39,849
			<u>14,822,851</u>	<u>15,171,941</u>
Expense accrual on bonds payable			<u>305,772</u>	<u>339,656</u>
			<u>15,128,623</u>	<u>15,511,597</u>

The total face value of the bonds and bills issued by the Bank in domestic market amounted to TL 3,432 millions as of 30 September 2016 (31 December 2015: TL 2,880 millions). The issuances are authorized by the Turkish Capital Markets Board.

The Bank's consolidated affiliates issue short-term bills with total outstanding face value amounting to TL 822,109 thousands and latest maturity date of August 2017.

In July 2014, the Bank issued EUR 500 millions, fixed-rate notes with a maturity date of 8 July 2019 and a coupon rate of 3.375% in the international markets.

In June 2014, one of the Bank's consolidated affiliates issued fixed-rate notes with a total face value of RON 300,000 thousands, a maturity date of 15 May 2019 and a coupon rate of 5.47%.

In April 2014, the Bank issued US\$ 750 million, fixed rate notes with a maturity date of 17 October 2019 and a coupon rate of 4.75% in the international markets.

In April 2013, the Bank established a Global Medium Term Notes (GMTN) program in order to issue bonds and other borrowing instruments in any currency with different series and maturities. In this regard, since May 2013 the Bank issues bills in US\$, EUR, CHF, RON, CZK, JPY and AUD with latest maturity in April 2027.

In March 2013, the Bank issued TL 750 million 5-year fixed-rate notes with a maturity date of 7 March 2018 and a coupon rate of 7.375% in the international markets.

In September 2012, the Bank issued US\$ 750 million 10-year fixed-rate notes with a maturity date of 13 September 2022 and a coupon rate of 5.25% and US\$ 600 million 5-year fixed-rate notes with a maturity date of 13 September 2017 and a coupon rate of 4.00% in the international markets.

In April 2011, the Bank issued US\$ 500 million 10-year fixed-rate notes with a maturity date of 20 April 2021 and a coupon rate of 6.25% and US\$ 300 million 5-year floating-rate notes with a maturity date of 20 April 2016 and a coupon rate of 3-month libor + 2.50% in the international markets.

The Bank and/or its consolidated affiliates repurchased some of the Group's own Turkish Lira securities with a total face value of TL 114,590 thousands (31 December 2015: TL 162,821 thousands) and foreign currency securities with a total face value of TL 618,536 thousands (31 December 2015: TL 638,989 thousands), and netted off such securities in the accompanying consolidated financial statements as of 30 September 2016.

## 18 Bonds payable (continued)

The Bank classified certain securities amounting to TL 15,959 thousands and RON 34,500,000 as financial liability at fair value through profit/loss at the initial recognition. As of 30 September 2016, the accumulated negative credit risk changes and the negative and positive credit risk changes recognised in the statement of income amounted to TL 71 thousands and TL 2,354 thousands, and TL 71 thousands and TL 427 thousands, respectively. The carrying value of the related financial liability amounted to TL 16,261 thousands and TL 30,108 thousands, and the related current period losses and gains amounted to TL 275 thousands and TL 578 thousands, respectively.

## 19 Subordinated liabilities

Subordinated liabilities comprised of the following as of 31 December 2015:

	<u>31 December 2015</u>		
	<u>Latest</u>	<u>Interest rate %</u>	<u>Amount</u>
	<u>maturity</u>		
Subordinated debt of EUR 50 millions	2021	euribor+3.5	158,355
Expense accrual on subordinated liabilities			<u>1,437</u>
			<u>159,792</u>

On 23 February 2009, the Bank had obtained a 12-year subordinated loan of EUR 50 millions due in March 2021 from Proparco (Societe de Promotion et de Participation pour la Cooperation Economique SA) a company of the French Development Agency Group, with an interest of euribor+3.5% and a repayment option for the Bank at the end of the seventh year. Following the approval of the BRSA, total amount of the debt has been repaid on 31 March 2016, by exercising the call option.

## 20 Taxation

In Turkey, corporate income tax is levied at the rate of 20% on the statutory corporate income tax base, which is determined by modifying accounting income for certain exclusions and allowances for tax purposes.

Dividends paid to the resident institutions and the institutions working through local offices or representatives in Turkey are not subject to withholding tax. As per the decisions no. 2009/14593 and 2009/14594 of the Council of Ministers published in the Official Gazette no. 27130 dated 3 February 2009, certain duty rates included in the articles no. 15 and 30 of the new Corporate Tax Law no. 5520 are revised. Accordingly, the withholding tax rate on the dividend payments other than the ones paid to the nonresident institutions generating income in Turkey through their operations or permanent representatives and the resident institutions, is 15%. In applying the withholding tax rates on dividend payments to the nonresident institutions and the individuals, the withholding tax rates covered in the related Double Tax Treaty Agreements are taken into account. Appropriation of the retained earnings to capital is not considered as profit distribution and therefore is not subject to withholding tax.

Under the Turkish taxation system, tax losses can be carried forward to offset against future taxable income for up to five years. Tax losses cannot be carried back to offset profits from prior years. There is no procedure for a final and definite agreement on tax assessments. Companies file their tax returns within four months following the end of the accounting year to which they relate. Tax returns and accounting records are open for five years from the beginning of the year that follows the date of filing during which time the tax authorities have the right to audit the tax returns, and the related accounting records on which they are based, and may issue re-assessments based on their findings.

In Turkey, the tax legislation does not permit a parent company and its affiliates to file a consolidated tax return. Therefore, the taxation charge, as reflected in the accompanying consolidated financial statements, represents the total amount of the taxation charge of each affiliate.

## **20 Taxation (continued)**

### *Tax applications for foreign branches*

#### *NORTHERN CYPRUS*

According to the Corporate Tax Law of the Turkish Republic of Northern Cyprus no.41/1976 as amended, the corporate earnings (including foreign corporations) are subject to a 10% corporate tax and 15% income tax. This tax is calculated based on the income that the taxpayers earn in an accounting period. Tax base is determined by modifying accounting income for certain exclusions and allowances for tax purposes. The corporations cannot benefit from the rights of offsetting losses, investment incentives and amortisation unless they prepare and have certified their statements of financial position, statements of comprehensive income and accounting records used for tax calculations by an auditor authorized by the Ministry of Finance. In cases where it is revealed that the earnings of a corporation were not subject to taxation in prior years or the tax paid on such earnings are understated, additional taxes can be charged in the next 12 years following that the related taxation period. The corporate tax returns are filed in the tax administration office in April after following the end of the accounting year to which they relate. The corporate taxes are paid in two equal installments in May and October.

#### *MALTA*

The corporate earnings are subject to a 35% corporate tax. This rate is determined by modifying accounting income for certain exclusions and allowances for tax purposes. The earnings of the foreign corporations' branches in Malta are also subject to the same tax rate that the resident corporations in Malta are subject to. The earnings of such branches that are transferred to their head offices are not subject to an additional tax. The taxes payable is calculated by the obligating firm and the calculation is shown at the tax declaration form that is due till the following year's September and the payment is done till this date.

#### *LUXEMBOURG*

The corporate earnings are subject to a 21% corporate tax. This rate is determined by modifying accounting income for certain exclusions and allowances for tax purposes. An additional 7% of the calculated corporate income tax is paid as a contribution to unemployment insurance fund. 3% of the taxable income is paid as municipality tax addition to corporate tax, the municipalities have the right to increase this rate up to 200-350%. The municipality commerce tax, which the Bank's Luxembourg branch subject to currently is applied as 7.50% of taxable income. The tax returns do not include any tax amounts to be paid. The tax calculations are done by the tax office and the amounts to be paid are declared to corporates through official letters called Note. The amounts and the payment dates of prepaid taxes are determined and declared by the tax office at the beginning of the taxation period. The corporations whose head offices are outside Luxembourg, are allowed to transfer the rest of their net income after tax following the allocation of 5% of it for legal reserves, to their head offices.

### *Tax applications for foreign affiliates*

#### *THE NETHERLANDS*

In the Netherlands, corporate income tax is levied at the rate of 20% for tax profits up to EUR 200,000 and 25% for the excess part over this amount on the worldwide income of resident companies, which is determined by modifying accounting income for certain exclusions and allowances for tax purposes for the related year. A unilateral decree for the avoidance of double taxation provides relief for resident companies from Dutch tax on income, such as foreign business profits derived through a permanent establishment abroad, if no tax treaty applies. There is an additional dividend tax of 5% computed only on the amounts of dividend distribution at the time of such payments. Under the Dutch taxation system, tax losses can be carried forward for nine years to offset against future taxable income. Tax losses can be carried back to one prior year. Companies must file their tax returns within nine

## 20 Taxation (continued)

months following the end of the tax year to which they relate, unless the company applies for an extension (normally an additional nine months). Tax returns are open for five years from the date of final assessment of the tax return during which time the tax authorities have the right to audit tax returns, and the related accounting records on which they are based, and may issue re-assessments based on their findings. The corporate income tax rate for the Germany branch is 30%.

### RUSSIA

The applicable corporate tax rate in Russia is 20% (2% federal and 18% regional). The taxation system in the Russian Federation is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open for a longer period.

### ROMANIA

The applicable corporate tax rate in Romania is 16%. The taxation system in Romania is continuously developing and is subject to varying interpretations and constant changes, which may become rarely retroactive. In Romania, tax periods remain open for tax audits for seven years. Tax losses can be carried forward to offset against future taxable income for seven years.

The total provision for taxes on income is different than the amount computed by applying the Turkish statutory tax rate to income before provision for taxes as shown in the following reconciliation:

	<i>30 September</i>		<i>30 September</i>	
	<u>2016</u>	<u>%</u>	<u>2015</u>	<u>%</u>
Taxes on income per statutory tax rate	1,038,088	20.00	713,173	20.00
Disallowable expenses	14,879	0.29	53,643	1.50
Income items exempt from tax or subject to different tax rates	(29,386)	(0.57)	(2,861)	(0.08)
General reserve	8,400	0.16	7,000	0.20
Others	<u>(4,770)</u>	<u>(0.09)</u>	<u>(35,265)</u>	<u>(0.99)</u>
Taxation charge	<u>1,027,211</u>	<u>19.79</u>	<u>735,690</u>	<u>20.63</u>

The taxation charge is comprised of the following:

	<i>For the nine-month period ended</i>	
	<i>30 September</i>	<i>30 September</i>
	<u>2016</u>	<u>2015</u>
Current taxes	900,522	434,403
Deferred taxes	<u>126,689</u>	<u>301,287</u>
Taxation charge	<u>1,027,211</u>	<u>735,690</u>

The movement of current tax liability is as follows:

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Balance at the beginning of the period	376,779	450,209
Current period taxation charge	900,522	832,787
Less: Advance taxes paid during the period	<u>(1,143,448)</u>	<u>(906,217)</u>
Current tax liability	<u>133,853</u>	<u>376,779</u>

In accordance with the related regulation for prepaid taxes on income, such advance payments during the year are being deducted from the final tax liability for the period. Accordingly, the taxation charge on income is not equal to the final tax liability appearing on the statement of financial position.

## 20 Taxation (continued)

Deferred tax assets and liabilities are as follows:

	<i>30 September</i> <u>2016</u>	<i>31 December</i> <u>2015</u>
Total deferred tax assets	1,131,117	1,235,869
Off-setted amount	<u>(251,156)</u>	<u>(222,317)</u>
Deferred tax assets per financial statements	<u>879,961</u>	<u>1,013,552</u>
Total deferred tax liabilities	288,742	241,829
Off-setted amount	<u>(251,156)</u>	<u>(222,317)</u>
Deferred tax liabilities per financial statements	<u>37,586</u>	<u>19,512</u>
Net deferred tax assets	<u>842,375</u>	<u>994,040</u>

Movements in deferred tax assets and liabilities are detailed in the table below:

	<i>Opening</i> <i>balance</i>	<i>Recognized in</i> <i>income</i> <i>statement</i>	<i>Effects of</i> <i>movement in</i> <i>exchange rates</i>	<i>Recognized</i> <i>in equity</i>	<i>Closing</i> <i>balance</i>
<b><u>30 September 2016</u></b>					
Impairment losses on loans	599,828	(13,885)	63	-	586,006
Discount on loans and advances to customers	81,090	811	-	-	81,901
Reserve for employee severance indemnity	58,303	9,579	(22)	-	67,860
Short-term employee benefits	49,743	27,865	413	-	78,021
Tax losses carried forward	43,601	(18,118)	2,774	-	28,257
Valuation difference on financial assets and liabilities	98,117	(70,604)	(1,455)	(27,701)	(1,643)
Revaluation surplus on real estates	(27,620)	1,039	(204)	1,679	(25,106)
Impairment of equity participations, tangible and intangible assets	14,361	445	-	-	14,806
Accruals on credit card rewards	17,362	1,728	-	-	19,090
Pro-rata basis depreciation expenses	(58,726)	(10,304)	(230)	-	(69,260)
Prepaid expenses and promotions	(1)	-	-	-	(1)
Others, net	<u>117,982</u>	<u>(55,245)</u>	<u>(293)</u>	<u>-</u>	<u>62,444</u>
Net deferred tax assets	<u>994,040</u>	<u>(126,689)</u>	<u>1,046</u>	<u>(26,022)</u>	<u>842,375</u>

	<i>Opening</i> <i>balance</i>	<i>Recognized in</i> <i>income</i> <i>statement</i>	<i>Effects of</i> <i>movement in</i> <i>exchange rates</i>	<i>Recognized</i> <i>in equity</i>	<i>Closing</i> <i>balance</i>
<b><u>31 December 2015</u></b>					
Impairment losses on loans	488,751	110,869	208	-	599,828
Discount on loans and advances to customers	71,386	9,704	-	-	81,090
Reserve for employee severance indemnity	49,772	2,644	-	5,887	58,303
Short-term employee benefits	51,699	(2,054)	98	-	49,743
Tax losses carried forward	44,863	(5,132)	3,870	-	43,601
Valuation difference on financial assets and liabilities	170,297	(258,412)	(2,355)	188,587	98,117
Revaluation surplus on real estates	(11,219)	(1,825)	(6)	(14,570)	(27,620)
Impairment of equity participations, tangible and intangible assets	11,944	2,417	-	-	14,361
Accruals on credit card rewards	16,487	875	-	-	17,362
Tax exemption for leasing business	1,202	(1,202)	-	-	-
Pro-rata basis depreciation expenses	(41,254)	(17,908)	436	-	(58,726)
Prepaid expenses and promotions	(17)	16	-	-	(1)
Others, net	<u>54,447</u>	<u>38,886</u>	<u>416</u>	<u>24,233</u>	<u>117,982</u>
Net deferred tax assets	<u>908,358</u>	<u>(121,122)</u>	<u>2,667</u>	<u>204,137</u>	<u>994,040</u>

## 20 Taxation (continued)

### *Transfer pricing*

The article no.13 of the Corporate Tax Law describes the issue of transfer pricing under the title of “Disguised Profit Distribution by Way of Transfer Pricing”. “The General Communiqué on Disguised Profit Distribution by Way of Transfer Pricing” published at 18 November 2007, explains the application related issues on this topic.

According to this communiqué, if the taxpayers conduct transactions like purchase and sale of goods or services with the related parties where the prices are not determined according to the arm’s length principle, then it will be concluded that there is a disguised profit distribution by way of transfer pricing. Such disguised profit distributions will not be deducted from the corporate tax base for tax purposes.

As stated in the “7.1 Annual Documentation” section of this communiqué, the taxpayers are required to fill out the “Transfer Pricing, Controlled Foreign Entities and Thin Capitalization” form for the purchase and sale of goods or services conducted with their related parties in a taxation period, attach these forms to their corporate tax returns and submit to the tax offices.

## 21 Other liabilities, accrued expenses and provisions

The principal components of other liabilities, accrued expenses and provisions are as follows:

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Blocked accounts against expenditures of card holders	7,854,259	6,943,869
Derivative financial liabilities	2,326,814	2,873,548
Miscellaneous payables	492,989	354,050
Expense accruals	455,214	468,803
Cheques at clearing house	409,039	-
Short-term employee benefits	401,245	263,691
Reserve for employee severance indemnity	359,010	311,132
Option premium payables	349,828	499,070
General reserve	300,000	342,000
Insurance business related provisions	291,477	251,285
Withholding taxes	284,000	326,345
Provision for non-cash loans	282,937	254,221
Transfer orders	253,750	180,809
Advances received	131,613	93,540
Unearned income	107,498	102,269
Payables to suppliers relating to financial lease activities	90,036	112,976
Blocked accounts	34,344	39,561
Payables to insurance and reinsurance companies relating to insurance business	31,938	21,096
Cash guarantees obtained	17,080	213,184
Others	386,049	470,993
	<u>14,859,120</u>	<u>14,122,442</u>

As of 30 September 2016, other liabilities, accrued expenses and provision include a general reserve amounting to TL 300,000 thousands (31 December 2015: TL 342,000 thousands) provided by the Bank in line with conservatism principle considering the circumstances which may arise from any changes in economy or market conditions under the name of general reserve.



## **21 Other liabilities, accrued expenses and provisions (continued)**

### *Recognized liability for defined benefit obligations*

#### *(i) Defined benefit plan*

As a result of the changes in legislation described below, the Bank will transfer a substantial portion of its pension liability under the Plan to SSF. This transfer, which will be a settlement of the Bank's obligation in respect of the pension and medical benefits transferable to SSF, was originally set to be within three years from the enactment of the New Law in May 2008, however, has been postponed for two years as per the decision of the Council of Ministers published on 9 April 2011 as further explained below. The actual date of the transfer has not been specified yet. However, in the financial statements for the year ended 31 December 2007, the Bank has modified the accounting required by IAS 19 Employee Benefits as the Bank believes that it is more appropriate to measure the obligation, in respect of the benefits that will be transferred to SSF, at the expected transfer amount prior to the date on which the transfer and settlement will occur. The expected transfer amount is calculated based on the methodology and actuarial assumptions (discount rate and mortality tables) prescribed in the New Law. As such, this calculation measures the liability to be transferred at the expected settlement amount i.e., the expected value of the payment to be made to SSF to assume that obligation.

The obligation with respect to excess benefits is accounted for as a defined benefit plan under IAS 19.

#### a) Pension and medical benefits transferable to SSF

As per the provisional Article no.23 of the Turkish Banking Law no.5411 as approved by the Turkish Parliament on 19 October 2005, pension funds which are in essence similar to foundations are required to be transferred directly to SSF within a period of three years. In accordance with the Banking Law, the actuarial calculation of the liability (if any) on the transfer should be performed regarding the methodology and parameters determined by the commission established by Ministry of Labor and Social Security. Accordingly, the Bank calculated the pension benefits transferable to SSF in accordance with the Decree published by the Council of Ministers in the Official Gazette no. 26377 dated 15 December 2006 ("Decree") for the purpose of determining the principles and procedures to be applied during the transfer of funds. However the said Article was vetoed by the President and at 2 November 2005 the President initiated a lawsuit before the Turkish Constitutional Court in order to rescind certain paragraphs of the provisional article no.23.

The Bank obtained an actuarial report regarding its obligations at 31 December 2006. This report, which was dated 12 February 2007, is from an actuary, who is registered with the Undersecretariat of the Treasury regarding this Fund in accordance with the Decree. Based on this Decree, the actuarial statement of financial position of the Fund has been prepared using a discount rate of 10.24% and the CSO 1980 mortality table. Based on the actuarial report, the assets of the plan exceeded the amount that would be required to be paid to transfer the obligation at 31 December 2006. In accordance with the existing legislation at 31 December 2006, the pension and medical benefits within the social security limits were subject to transfer and the banks were not required to provide any excess social rights and payments.

On 22 March 2007, the Turkish Constitutional Court reached a verdict with regards to the suspension of the execution of the first paragraph of provisional article no.23 of the Turkish Banking Law, which requires the transfer of pension funds to SSF, until the decision regarding the cancellation thereof is published in the Official Gazette. The Constitutional Court stated in its reasoned ruling published in the Official Gazette numbered 26731, dated 15 December 2007 that the reason behind this cancellation was the possible loss of antecedent rights of the members of pension funds. Following the publication of the verdict, the Grand National Assembly of Republic of Turkey ("Turkish Parliament") worked on the new legal arrangements by taking the cancellation reasoning into account. At 17 April 2008, the

## 21 Other liabilities, accrued expenses and provisions (continued)

New Law has been accepted by the Turkish Parliament and the New Law has been enacted at 8 May 2008 following its publication in the Official Gazette no. 26870. In accordance with the New Law, members of the funds established in accordance with the Social Security Law should be transferred to SSF within three years following its enactment date. The transfers are to take place within the three-year period starting from 1 January 2008. Subsequently, the transfer of the contributors and the persons receiving monthly or regular income and their right-holders from such funds established for employees of the banks, insurance and reinsurance companies, trade chambers, stock markets and unions that are part of these organizations subject to the provisional Article no. 20 of the Social Security Law no.506 to the SSF, has been postponed for two years. The decision was made by the Council of Ministers on 14 March 2011 and published in the Official Gazette no. 27900 dated 9 April 2011 as per the decision of the Council of Ministers, numbered 2011/1559, and as per the letter no. 150 of the Ministry of Labor and Social Security dated 24 February 2011 and according to the provisional Article no. 20 of the Social Security and Public Health Insurance Law no.5510.

On 19 June 2008, the main opposition party Cumhuriyet Halk Partisi (“CHP”) applied to the Constitutional Court for the cancellation of various articles of the Law including the first paragraph of the provisional Article no. 20. At the meeting of the Constitutional Court on 30 March 2011, it was decided that the Article no. 73 and the first paragraph of the provisional Article no. 20 added to the law no. 5510 are not contradictory to the Constitutional Law, and accordingly the dismissal of the cancellation request was denied with the majority of votes.

Before the completion of two-years period set by the Council of Ministers on 14 March 2011 as explained above, as per the Article no. 51 of the law no. 6645, published in the Official Gazette no. 29335 dated 23 April 2015, the Article no. 20 of the law no. 5510 was amended giving the Council of Ministers the authority to determine the date of transfer without defining any timeline.

The Bank obtained an actuarial report dated 7 December 2015 from an independent actuary reflecting the principles and procedures on determining the application of transfer transactions in accordance with the New Law. The actuarial statement of financial position of the Fund has been prepared using a discount rate of 9.80% and the CSO 1980 mortality table, and the assets of the plan exceed the amount that would be required to be paid to transfer the obligation at 31 December 2015.

The Bank’s obligation in respect of the pension and medical benefits transferable to SSF has been determined as the value of the payment that would need to be made to SSF to settle the obligation at the date of the statement of financial position in accordance with the related article of the New Law.

The pension disclosures set out below therefore reflect the methodology and actuarial assumptions specified in the New Law. This calculation measures the benefit obligation at the expected transfer amount i.e., the estimated amount the Bank will pay to SSF to assume this portion of the obligation.

The pension benefits are calculated annually. As per the calculation as of 31 December 2015, the present value of funded obligations amounted to TL 114,487 thousands and the fair value of the planned assets amounted to TL 2,522,836 thousands.

	<b><i>31 December</i></b>
	<b><u>2015</u></b>
Present value of funded obligations	
- Pension benefits transferable to SSF (obligation measured at the expected transfer amount)	(608,796)
- Medical benefits transferable to SSF (obligation measured at the expected transfer amount)	528,011
- General administrative expenses	<u>(33,702)</u>
	(114,487)
Fair value of plan assets	<u>2,522,836</u>
Asset surplus in the plan (*)	<u>2,408,349</u>

(\*) Asset surplus in this plan will be used to cover the excess benefits not transferable to SSF.

## 21 Other liabilities, accrued expenses and provisions (continued)

Plan assets consisted of the following:

	<i>31 December</i>
	<u>2015</u>
Cash and due from banks	532,000
Securities	1,893,501
Land and buildings	96,845
Other	490
	<u>2,522,836</u>

b) Excess benefits not transferable to SSF

The other social rights and payments representing benefits in excess of social security limits are not subject to transfer to SSF. Therefore these excess benefits are accounted for as an ongoing defined benefit plan.

Asset surplus/(shortage) on present value of defined benefit obligation is as follows:

	<i>31 December</i>
	<u>2015</u>
Present value of defined benefit obligations	
- Pension	(592,937)
- Health	(478,453)
Fair value of plan assets (*)	<u>2,408,349</u>
Asset surplus over present value of defined benefit obligation	<u>1,336,959</u>

(\*) Plan assets are composed of asset surplus in the plan explained in paragraph a).

As per the actuarial calculation performed as of 31 December 2015 as detailed above, the asset surplus over the fair value of the plan assets to be used for the payment of the obligations also fully covered the benefits not transferable and still a surplus of TL 1,336,959 thousands remains. However, the Bank's management, acting prudently, did not consider the health premium surplus amounting to TL 528,011 thousands as stated above and resulted from the present value of medical benefits and health premiums transferable to SSF. However, despite this treatment there was no excess obligation that needed to be provided against as of 31 December 2015.

	<i>31 December</i>
	<u>2015</u>
Asset surplus over present value of defined benefit obligation	1,336,959
Net present value of medical benefits and health premiums transferable to SSF	<u>(528,011)</u>
Present value of asset surplus/(defined benefit obligation)	<u>808,948</u>

Expenses recognized regarding this benefit plan in the accompanying consolidated statement of income for the first nine-months of 2016 and 2015 are as follows:

	<i>30 September</i>	<i>30 September</i>
	<u>2016</u>	<u>2015</u>
Total contribution payment	203,716	168,561
Provision for unfunded liability	-	-
	<u>203,716</u>	<u>168,561</u>

## 21 Other liabilities, accrued expenses and provisions (continued)

Principal actuarial assumptions used were as follows:

	<b>31 December</b>
	<b>2015</b>
	<b>%</b>
Discount rates <sup>(*)</sup>	10.30
Inflation rates <sup>(*)</sup>	7.10
Future real salary increase rates	1.5
Medical cost trend rates	40% above inflation
Future pension increase rates <sup>(*)</sup>	7.10

<sup>(\*)</sup> The above mentioned rates are effective rates, whereas the rates applied for the calculation differ according to the employees' years in service.

Assumptions regarding future mortality are based on published statistics and mortality tables. The average life expectancy of an individual retiring at age 60 is 17 for males, and at age 58 for females is 23.

The sensitivity analysis of defined benefit obligation of excess liabilities were as follow as of 31 December 2015:

<b>% change in defined benefit obligation</b>			
<b><u>Assumption change</u></b>	<b><u>Pension Benefits</u></b>	<b><u>Medical Benefits</u></b>	<b><u>Overall</u></b>
	<b>%</b>	<b>%</b>	<b>%</b>
Discount rate +1%	(14.0)	(17.5)	(15.6)
Discount rate -1%	18.1	22.8	20.2
Medical inflation +10% of CPI		15.3	6.8
Medical inflation -10% of CPI		(13.1)	(5.9)

### *Short-term employee benefits*

Movement in the provision for short-term employee benefits are as follows:

	<b>30 September</b>	<b>31 December</b>
	<b>2016</b>	<b>2015</b>
Balance, beginning of the period	263,691	283,112
Payments	(117,277)	(364,568)
Provision for the period, net	<u>254,831</u>	<u>345,147</u>
Balance, end of the period	<u>401,245</u>	<u>263,691</u>

### *Insurance business related provisions*

Insurance business related provisions are detailed in the table below:

	<b>30 September</b>	<b>31 December</b>
	<b>2016</b>	<b>2015</b>
Reserve for unearned premiums, net	82,883	89,118
<i>Gross</i>	108,535	112,548
<i>Reinsurers' share</i>	(25,652)	(23,430)
Provision for claims, net	24,397	25,723
<i>Gross</i>	33,886	34,980
<i>Reinsurers' share</i>	(9,489)	(9,257)
Life mathematical reserves	<u>184,197</u>	<u>136,444</u>
	<u>291,477</u>	<u>251,285</u>

## 21 Other liabilities, accrued expenses and provisions (continued)

### *Reserve for employee severance indemnity*

Movement in the reserve for employee severance indemnity is as follows:

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Balance, beginning of the period	311,132	268,544
Payments	(25,990)	(19,540)
Provision for the period	73,868	59,870
Actuarial gain/loss	-	2,258
Balance, end of the period	<u>359,010</u>	<u>311,132</u>

The computation of the liabilities is based upon the retirement pay ceiling announced by the government. The ceiling amounts applicable for each year of employment are full TL 4,297.21 and full TL 3,828.37 as of 30 September 2016 and 31 December 2015, respectively.

The principal actuarial assumptions for the Bank and its consolidated affiliates are as follows:

	<i>30 September</i>	<i>31 December</i>
	<u>2016 (*)</u>	<u>2015 (*)</u>
	<u>%</u>	<u>%</u>
Discount rates	2.99	2.99
Interest rates	10.30	10.30
Expected rates of salary increases	8.60	8.60
Inflation rates	7.10	7.10

(\*) *The above mentioned rates are effective rates, whereas the rates applied for the calculation differ according to the employees' years in service.*

### *Provision for non-cash loans*

Movement in the provision for non-cash loans are as follows:

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Balance, beginning of the period	254,221	249,272
(Reversal)/provision for the period, net	28,716	4,949
Balance, end of the period	<u>282,937</u>	<u>254,221</u>

## 22 Equity

### *Share capital*

The authorized nominal share capital of the Bank amounted to TL 4,200,000 thousands as of 30 September 2016.

*Unrealised gains from changes in fair value of available-for-sale assets are detailed as follows:*

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Balance at the beginning of the period	(283,792)	88,631
Net unrealised (losses)/gains from changes in fair value	502,156	(410,897)
Related deferred and current income taxes	(88,403)	78,397
Net gains transferred to the statement of comprehensive income on disposal	(235,104)	(138,349)
Related deferred and current income taxes	20,358	29,308
Effect of movements in foreign exchange rates	(47,810)	69,118
Balance at the end of the period	<u>(132,595)</u>	<u>(283,792)</u>

## 22 Equity (continued)

### *Hedging reserve*

The hedging reserve comprises the effective portions of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred (see Note 26.4 for the details) and of the cumulative change in the net investment hedge performed in order to hedge the foreign currency risk arising from net investments in foreign operations with long-term foreign currency borrowings.

### *Translation reserve*

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations into the functional currency of the Bank which is TL and of the cumulative change in the net investment hedge performed in order to hedge the foreign currency risk arising from net investments in foreign operations with long-term foreign currency borrowings.

### *Legal reserves*

As per the decisions made at the annual general assemblies of the Bank and its affiliates, 5% of the prior year's net income is allocated to legal reserves. The reserves include legal reserves amounting to TL 1,274,312 thousands (31 December 2015: TL 1,229,498 thousands) in total.

For the Bank and its Turkish affiliates, the legal reserves are generated by annual appropriations amounting to 5% of the statutory income until such reserves reach 20% of paid-in share capital (first legal reserves). Without limit, a further 10% of dividend distributions in excess of 5% of paid-in share capital appropriated to generate the legal reserves (second legal reserves). The legal reserves are restricted and are not available for distribution as dividends unless they exceed 50% of the share capital.

The Bank's affiliate in Russia allocates legal reserves upto 15% of its authorized capital. To achieve required level, the affiliate annually allocates 5% of its statutory net income. The reserves of the Russian affiliate is intended to cover losses, repayment of bonds, repurchase of shares if no other asset is available, and cannot be used for any other purposes.

The Bank's affiliates in Romania also allocate legal reserves in accordance with the requirements of statutory laws and regulations applicable for each entity. According to the relevant legislation, legal reserves include annual allocations of 5% of the statutory income before tax. According to the relevant legislation, the legal reserve cannot exceed 20% of the share capital.

The Bank's affiliate in the Netherlands is not subject to any legal reserve requirements.

### *Non-controlling interests*

As of 30 September 2016, net non-controlling interests amount to TL 257,901 thousands (31 December 2015: TL 226,617 thousands). Non-controlling interests are detailed as follows:

	<b>30 September</b>	<b>31 December</b>
	<b><u>2016</u></b>	<b><u>2015</u></b>
Capital	55,219	55,219
Retained earnings and other reserves	170,174	137,185
Net income for the period	<u>32,508</u>	<u>34,213</u>
	<u>257,901</u>	<u>226,617</u>

## 23 Fair value information

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.

The estimated fair values of financial instruments have been determined using available market information by the Bank, and where it exists, appropriate valuation methodologies. However, judgment is necessary required to interpret market data to determine the estimated fair value. While management uses available market information in estimating the fair values of financial instruments, the market information may not be fully reflective of the value that could be realized in the current circumstances.

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

Fair value of loans and advances to customers is TL 191,788,727 thousands (31 December 2015: TL 177,074,949 thousands), whereas the carrying amount is TL 190,272,052 thousands (31 December 2015: TL 175,681,692 thousands) in the accompanying consolidated statement of financial position as of 30 September 2016.

Fair value of investment securities is TL 45,122,757 thousands (31 December 2015: TL 46,223,017 thousands), whereas the carrying amount is TL 44,486,351 thousands (31 December 2015: TL 46,072,823 thousands) in the accompanying consolidated statement of financial position as of 30 September 2016.

The table below analyses financial instruments carried at fair value, by valuation method:

<b><u>30 September 2016</u></b>	<b><u>Level 1</u></b>	<b><u>Level 2</u></b>	<b><u>Level 3</u></b>	<b><u>Total</u></b>
Financial assets at fair value through profit or loss	1,086,523	1,833	-	1,088,356
Derivative financial assets	664	1,886,908	-	1,887,572
Debt and other instruments available-for-sale	<u>18,728,264</u>	<u>3,752,458</u>	<u>699,101</u>	<u>23,179,823</u>
Financial Assets at Fair Value	<u>19,815,451</u>	<u>5,641,199</u>	<u>699,101</u>	<u>26,155,751</u>
Loans and advances from banks and other institutions	-	5,753,134	-	5,753,134
Derivative financial liabilities	<u>1,371</u>	<u>2,325,443</u>	-	<u>2,326,814</u>
Financial Liabilities at Fair Value	<u>1,371</u>	<u>8,078,577</u>	-	<u>8,079,948</u>
<b><u>31 December 2015</u></b>	<b><u>Level 1</u></b>	<b><u>Level 2</u></b>	<b><u>Level 3</u></b>	<b><u>Total</u></b>
Financial assets at fair value through profit or loss	430,753	229,440	-	660,193
Derivative financial assets	285	2,407,390	-	2,407,675
Debt and other instruments available-for-sale	<u>18,457,705</u>	<u>5,724,174</u>	<u>573,698</u>	<u>24,755,577</u>
Financial Assets at Fair Value	<u>18,888,743</u>	<u>8,361,004</u>	<u>573,698</u>	<u>27,823,445</u>
Loans and advances from banks and other institutions	-	5,688,704	-	5,688,704
Derivative financial liabilities	<u>3,617</u>	<u>2,869,931</u>	-	<u>2,873,548</u>
Financial Liabilities at Fair Value	<u>3,617</u>	<u>8,558,635</u>	-	<u>8,562,252</u>

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

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

Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs)

## 24 Commitments and contingencies

In the ordinary course of business, the Bank and its affiliates undertake various commitments and incur certain contingent liabilities that are not presented in the accompanying consolidated financial statements, including letters of guarantee, acceptance credits and letters of credit. Commitments and contingent liabilities comprise the following:

	<i>30 September</i> <u>2016</u>	<i>31 December</i> <u>2015</u>
Letters of guarantee	35,952,809	32,709,109
Letters of credit	15,009,375	14,576,338
Acceptance credits	2,079,835	1,538,069
Other guarantees and endorsements	<u>133,267</u>	<u>109,206</u>
	<u>53,175,286</u>	<u>48,932,722</u>

As of 30 September 2016;

- Commitment for unpaid capital of affiliated companies amounts to TL 4,774 thousands (31 December 2015: TL 5,297 thousands).
- Commitments for unused credit limits and promotions of credit cards, cheques and loans to customers, commitments for loan granting and other irrevocable commitments amount to TL 44,212,002 thousands (31 December 2015: TL 45,969,931 thousands) in total.
- Commitments for the derivative transactions carried out on behalf of customers in the Turkish Derivatives Exchange amount to TL 1,066,860 thousands (31 December 2015: TL 793,989 thousands) in total.

As of 30 September 2016, the securities acquired under security borrowing transactions include shares with total market and carrying values of TL 31,036 thousands (31 December 2015: TL 45,473 thousands).

## 25 Derivative financial instruments

As of 30 September 2016, commitment for purchase and sale of foreign currencies under spot, forwards, swaps, future rate agreements, options and forward agreements for gold trading amounts to TL 150,449,692 thousands (31 December 2015: TL 132,069,129 thousands), approximately 84% of which are due within a year.

The following tables summarize the notional amounts of the forward, swap, futures and options contracts, with details of remaining periods to maturity. Foreign currency amounts are translated at rates ruling at the date of the statement of financial position. Monetary items denominated in foreign currencies are economically hedged using foreign currency derivative contracts. All gains and losses on foreign currency contracts are recognized in the statement of income, except for contracts of cash flow hedges as stated above.



**25 Derivative financial instruments (continued)**

<b>30 September 2016</b>	<i>Notional amount with remaining life of</i>					<b>Total</b>
	<b><u>Up to 1 month</u></b>	<b><u>1 to 3 months</u></b>	<b><u>3 to 6 months</u></b>	<b><u>6 to 12 months</u></b>	<b><u>Over 1 year</u></b>	
<b><u>Interest Rate Derivatives</u></b>						
Interest rate swaps (*)	7	43	533	9,926	1,186,933	1,197,442
<i>Purchases</i>	4	24	128	7,198	494,705	502,059
<i>Sales</i>	3	19	405	2,728	692,228	695,383
Interest rate options	-	2,416,392	-	-	5,323,320	7,739,712
<i>Purchases</i>	-	1,208,196	-	-	2,661,660	3,869,856
<i>Sales</i>	-	1,208,196	-	-	2,661,660	3,869,856
Interest rate futures	-	17,952	-	-	-	17,952
<i>Purchases</i>	-	-	-	-	-	-
<i>Sales</i>	-	17,952	-	-	-	17,952
<b><u>Other Derivatives</u></b>						
Securities, shares and index options	116,119	31,877	56,525	-	-	204,521
<i>Purchases</i>	69,751	29,870	29,994	-	-	129,615
<i>Sales</i>	46,368	2,007	26,531	-	-	74,906
Other forward contracts	229,890	158,708	130,609	36,197	-	555,404
<i>Purchases</i>	215,510	85,959	86,255	20,912	-	408,636
<i>Sales</i>	14,380	72,749	44,354	15,285	-	146,768
Other future contracts	34,659	60,487	4,425	-	-	99,571
<i>Purchases</i>	25,037	699	-	-	-	25,736
<i>Sales</i>	9,622	59,788	4,425	-	-	73,835
Other swap contracts	-	756,295	7,055	12,536	11,049,057	11,824,943
<i>Purchases</i>	-	-	-	-	5,041,519	5,041,519
<i>Sales</i>	-	756,295	7,055	12,536	6,007,538	6,783,424
<b><u>Currency Derivatives</u></b>						
Spot exchange contracts	3,402,216	-	-	-	-	3,402,216
<i>Purchases</i>	689,295	-	-	-	-	689,295
<i>Sales</i>	2,712,921	-	-	-	-	2,712,921
Forward exchange contracts	7,524,862	2,809,903	1,447,226	1,227,942	679,244	13,689,177
<i>Purchases</i>	3,631,876	1,388,036	701,166	489,417	256,841	6,467,336
<i>Sales</i>	3,892,986	1,421,867	746,060	738,525	422,403	7,221,841
Currency/cross currency swaps	47,030,300	13,217,068	6,292,468	8,780,188	4,359,095	79,679,119
<i>Purchases</i>	23,049,418	6,189,458	3,166,125	4,679,782	2,869,922	39,954,705
<i>Sales</i>	23,980,882	7,027,610	3,126,343	4,100,406	1,489,173	39,724,414
Options	6,518,156	11,149,224	6,975,054	5,787,178	1,414,505	31,844,117
<i>Purchases</i>	3,302,365	4,205,200	2,740,917	2,621,605	942,520	13,812,607
<i>Sales</i>	3,215,791	6,944,024	4,234,137	3,165,573	471,985	18,031,510
Foreign currency futures	188,128	7,390	-	-	-	195,518
<i>Purchases</i>	299	3,722	-	-	-	4,021
<i>Sales</i>	187,829	3,668	-	-	-	191,497
Subtotal Purchases	30,983,555	13,111,164	6,724,585	7,818,914	12,267,167	70,905,385
Subtotal Sales	34,060,782	17,514,175	8,189,310	8,035,053	11,744,987	79,544,307
Total of Transactions	<u>65,044,337</u>	<u>30,625,339</u>	<u>14,913,895</u>	<u>15,853,967</u>	<u>24,012,154</u>	<u>150,449,692</u>

(\*) In case of interest rate swaps, the amounts presented in the table above are the marked-to-market values of such transactions.

**25 Derivative financial instruments (continued)**

<b><u>31 December 2015</u></b>	<i>Notional amount with remaining life of</i>					<b><u>Total</u></b>
	<b><u>Up to 1 month</u></b>	<b><u>1 to 3 months</u></b>	<b><u>3 to 6 months</u></b>	<b><u>6 to 12 months</u></b>	<b><u>Over 1 year</u></b>	
<b><u>Interest Rate Derivatives</u></b>						
Interest rate options	-	-	102,930	2,280,312	3,877,250	6,260,492
<i>Purchases</i>	-	-	51,465	1,140,156	1,938,625	3,130,246
<i>Sales</i>	-	-	51,465	1,140,156	1,938,625	3,130,246
Interest rate swaps (*)	-	4,096	11,264	10,141	675,587	701,088
<i>Purchases</i>	-	4,096	11,264	10,070	381,019	406,449
<i>Sales</i>	-	-	-	71	294,568	294,639
Interest rate futures	-	-	-	-	-	-
<i>Purchases</i>	-	-	-	-	-	-
<i>Sales</i>	-	-	-	-	-	-
<b><u>Other Derivatives</u></b>						
Securities, shares and index options	22,440	14,154	-	-	46,546	83,140
<i>Purchases</i>	11,909	10,362	-	-	23,273	45,544
<i>Sales</i>	10,531	3,792	-	-	23,273	37,596
Other forward contracts	140,082	333,368	319,350	531,798	-	1,324,598
<i>Purchases</i>	121,906	296,211	247,483	365,185	-	1,030,785
<i>Sales</i>	18,176	37,157	71,867	166,613	-	293,813
Other future contracts	-	10,050	106,089	170,708	-	286,847
<i>Purchases</i>	-	2,450	-	-	-	2,450
<i>Sales</i>	-	7,600	106,089	170,708	-	284,397
Other swap contracts	118,545	-	-	-	10,652,114	10,770,659
<i>Purchases</i>	118,545	-	-	-	4,798,200	4,916,745
<i>Sales</i>	-	-	-	-	5,853,914	5,853,914
<b><u>Currency Derivatives</u></b>						
Spot exchange contracts	1,634,258	-	-	-	-	1,634,258
<i>Purchases</i>	74,243	-	-	-	-	74,243
<i>Sales</i>	1,560,015	-	-	-	-	1,560,015
Forward exchange contracts	6,382,940	4,156,264	2,197,044	2,378,497	1,364,279	16,479,024
<i>Purchases</i>	3,363,106	2,531,173	1,102,542	1,218,629	718,135	8,933,585
<i>Sales</i>	3,019,834	1,625,091	1,094,502	1,159,868	646,144	7,545,439
Currency/cross currency swaps	31,216,686	4,902,106	6,066,843	5,465,597	4,267,356	51,918,588
<i>Purchases</i>	17,471,004	3,615,102	3,691,734	3,844,558	2,892,910	31,515,308
<i>Sales</i>	13,745,682	1,287,004	2,375,109	1,621,039	1,374,446	20,403,280
Options	8,131,932	10,212,011	6,133,226	14,511,987	3,614,252	42,603,408
<i>Purchases</i>	3,148,483	4,291,510	2,845,755	8,779,015	2,065,545	21,130,308
<i>Sales</i>	4,983,449	5,920,501	3,287,471	5,732,972	1,548,707	21,473,100
Foreign currency futures	-	3,117	-	3,910	-	7,027
<i>Purchases</i>	-	3,117	-	345	-	3,462
<i>Sales</i>	-	-	-	3,565	-	3,565
Subtotal Purchases	24,309,196	10,754,021	7,950,243	15,357,958	12,817,707	71,189,125
Subtotal Sales	23,337,687	8,881,145	6,986,503	9,994,992	11,679,677	60,880,004
Total of Transactions	<u>47,646,883</u>	<u>19,635,166</u>	<u>14,936,746</u>	<u>25,352,950</u>	<u>24,497,384</u>	<u>132,069,129</u>

(\*) In case of interest rate swaps, the amounts presented in the table above are the marked-to-market values of such transactions.

## **26 Financial risk management disclosures**

This section provides details of the Bank and its affiliates' exposure to risk and describes the methods used by management to control risk. The most important types of financial risk to which the Bank and its affiliates are exposed, are credit risk, liquidity risk, market risk and operational risk.

The nature of the risks and the approach to managing risk differs fundamentally between the trading and non-trading portfolios; section 26.2 contains risk management information related to the trading portfolio and section 26.3 deals with the non-trading portfolio.

### ***Risk management framework***

The Bank's Risk Management Strategy is established as part of a maintainable long term, value adding growth strategy. This strategy involves optimal allocation of economic capital to business lines considering the risk-return balance by measuring risks with the methods in compliance with its activities and national regulations and international standards.

The Bank determines the necessary approaches in order to update, revise, apply and manage its policies set for the proper assessment and management of risks considering changes in conditions.

The top management is responsible of managing, developing the risk management strategies, policies and application principles approved by the board of directors, reporting of major risks that the Bank is facing to the board of directors, assessment of internal control, internal audit and risk reports of departments and either eliminating risks, deficiencies or defects identified in these departments or taking the necessary precautions to prevent those, and participating in determination of risk limits.

The risk management activities are structured under the responsibility of the Bank's board of directors. Risk Committee, with its all members from board of directors, supervises corporate risk management policy and practices, manages the various risks present in the Bank activities, as well as capital adequacy, planning and liquidity adequacy. The risks such as corporate risk management policy and application review, capital adequacy, planning and liquidity coverage are at the responsibility of risk management composed of the members of board. The top management is responsible to the board of directors for monitoring and managing of risks. Besides, the following departments participate in monitoring of risks, independent from the departments having operational activities; Internal Control, Risk Management, Compliance and Internal Audit.

The risks are evaluated on a continuously developing structure that is managed by internationally accepted applications and in compliance with the Bank's policies and procedures and the international and local regulations.

The risks are also managed through risk mitigations using hedging transactions beside measurement, limitation and capital allocation techniques. The data of the Bank and the market are regularly monitored for better risk monitoring and management. As part of limitation of risks, internal limits are also set beside the legal limits. The possible changes in economic conditions and the risks that can be faced under extraordinary conditions are taken into consideration.

In order to ensure the compliance with the rules altered pursuant to the relevant articles of the Turkish Banking Law No. 5411 and of Regulation on Internal Systems and Internal Capital Adequacy Assessment Process of Banks published in the Official Gazette dated 11 July 2014, the Bank periodically reviews the current written policies and implementation procedures regarding management of each risk encountered in its activities. The Bank also conducts internal capital adequacy assessment process (ICAAP) within the scope of the same regulation on both consolidated and bank-only basis. The main target of this process is to maintain the Bank's capital adequacy, considering the Bank's strategies, credit growth expectations, assets and liabilities structure, future funding sources and liquidity, dividend policy and possible fluctuations in capital requirement due to economic cycle, by being compatible with its risk profile and risk appetite.

In this scope, possible internal capital requirement is assessed as of every year-end for following 3 years, in line with current capital structure, in the frame of the Bank's activities and risks exposed, and the Bank's future target and strategies. This assessment includes market, credit, operational risks, which are directly related with regulatory capital adequacy ratio, and also interest rate risk in banking book, liquidity risk, reputation risk, concentration risk, strategic risk, and country and transfer risk.

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

### *Audit Committee*

The audit committee consists of two members of the board of directors who do not have any executive functions. The audit committee, which was established to assist the board of directors in its auditing and supervising activities, is responsible for:

- Monitoring the effectiveness and adequacy of the Bank's internal control, risk management and internal audit systems, operation of these systems and accounting and reporting systems in accordance with applicable regulations and the integrity of resulting information;
- Performing the preliminary studies required for the election of independent audit firms and regularly monitoring their activities;
- Ensuring that the internal audit functions of consolidated organizations are performed in a consolidated and coordinated manner.

### *Liquidity Risk Management Committee*

- Determining the excess liquidity that the Bank holds in foreign currencies;
- Periodically monitoring the liquidity report and early-warning signals;
- Determining the stress level of the Bank; monitoring internal and external factors that might affect the Bank's liquidity in case of a liquidity crisis;
- Ensuring that the action plan aligned with the Contingency Funding Plan is properly implemented;
- Determining measures required by the Bank's customer confidence, cost of funding and key liquidity increasing strategies, and ensuring internal communication and coordination with regard to the implementation of committee decisions.

### *Other Committees*

Market, credit and operational sub-risk committees have been established in order to facilitate exchange of information and views with the relevant units of the Bank and to promote the use of risk management and internal audit systems within the Bank.

### **26.1 Derivative financial instruments**

The Bank and its affiliates enter into a variety of derivative financial instruments for hedging and risk management purposes. This note describes the derivatives used. Further details of the objectives and strategies in the use of derivatives are set out in the sections of this note on non-trading activities. Details of the nature and terms of derivative instruments outstanding at the dates of the statements of financial position are set out in Note 25. Derivative financial instruments used include swaps, futures, forwards, options and other similar types of contracts whose value changes in response to changes in interest rates, foreign exchange rates and gold prices. Derivatives are individually negotiated over-the-counter contracts. A description of the main types of derivative instruments used is set out below:

#### *Swaps*

Swaps are over-the-counter agreements to exchange future cash flows based upon agreed notional amounts. Most commonly used swaps are currency swaps. The Bank and its affiliates are subject to credit risk arising from the respective counterparties' failure to perform. Market risk arises from the possibility of unfavorable movements in market rates relative to the contractual rates of the contract.

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

### *Futures and forwards*

Futures and forward contracts are commitments to either purchase or sell a designated financial instrument, currency, commodity or an index at a specified future date for a specified price and may be settled in cash or another financial asset. Futures are standardized exchange-traded contracts whereas forwards are individually traded over-the-counter contracts. Initial margin requirements for futures are met in cash or other instruments, and changes in the future contract values are settled daily. Therefore credit risk is limited to the net positive change in the market value for a single day. Futures contracts have little credit risk because the counterparties are clearing houses. Forward contracts result in credit exposure to the counterparty. Futures and forward contracts both result in exposure to market risk based on changes in market prices relative to contracted amounts.

### *Options*

Options are derivative financial instruments that give the buyer, in exchange for a premium payment, the right, but not the obligation, to either purchase from (call option) or sell (put option) to the writer a specified underlying at a specified price on or before a specified date. The Bank enters into foreign exchange, bond, equity index, interest rate options, not only vanilla options but also exotic options. Foreign currency options provide protection against rising or falling currency rates. The Bank as a buyer of over-the-counter options is subject to market risk and credit risk since the counterparty is obliged to make payments under the terms of the contract if the Bank exercises the option. As the writer of over-the-counter options, the Bank is subject to market risk only since it is obliged to make payments if the option is exercised.

### **26.2 Trading activities**

The Bank and its affiliates maintain active trading positions in non-derivative financial instruments. Most of the trading activities are customer driven. In anticipation of customer demand, an inventory of capital market instruments is carried and access to market liquidity is maintained by quoting bid and offer prices to and trading with other market makers. Positions are also taken in the interest rate, foreign exchange, debt and equity markets based on expectations of future market conditions. These activities constitute the proprietary trading business and enable the Bank and its affiliates to provide customers with capital market products at competitive prices. As trading strategies depend on both market-making and proprietary positions, given the relationships between instruments and markets, those are managed in concert to maximize net trading income. Trading activities are managed by type of risk involved and on the basis of the categories of trading instruments held.

#### *Counterparty credit risk*

The Bank and its affiliates' counterparty credit exposure at the date of the statement of financial position from financial instruments held or issued for trading purposes is represented by the fair value of instruments with a positive fair value at that date, as recorded on the statement of financial position. Notional amounts disclosed in the notes to the financial statements do not represent the amounts to be exchanged by the parties to derivatives and do not measure the exposure to credit or market risks. The amounts to be exchanged are based on the terms of the derivatives.

The risk that counterparties to trading instruments might default on their obligations is monitored on an ongoing basis. In monitoring credit risk exposure, consideration is given to trading instruments with a positive fair value and to the volatility of the fair value of trading instruments. To manage the level of credit risk, the Bank and its affiliates deal with counterparties of good credit standing, enter into master netting agreements whenever possible, and when appropriate, obtain collateral. Master netting agreements provide for the net settlement of contracts with the same counterparty in the event of default.

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

### *Market risk*

Market Risk is defined as the losses that the trading portfolio of the Bank may incur due to the risks caused by market price changes (interest rate, equities, foreign exchange and commodity prices), the correlations between market prices and the uncertainty in the volatility levels.

All trading instruments are subject to market risk. The instruments are recognized at fair value, and all changes in market conditions directly affect net trading income.

The Bank and its affiliates manage its use of trading instruments in response to changing market conditions.

The board of directors monitors the effectiveness of risk management systems through audit committee, related other committees and top management, and in the light of various risk reports and the assessments made by the audit committee.

The risk policies and application procedures have been approved by the board of directors and regularly revisited. The market risk is also managed by risk mitigations through hedging transactions beside measuring the risks in compliance with the international standards, limiting such risk and allocating capital accordingly.

Market risks arising from trading portfolios are measured by the Bank as per “standard” and “value at risk (VaR)” methods. The measurements as per the standard method are performed on a monthly basis, and taken into consideration in the calculation of capital adequacy. Whereas, the measurements as per VaR method are performed on a daily basis. The Bank takes the historical VaR results as the basis for the internal management of market risk and limit setting. In the VaR calculation, one year historical market data set is used, and 99% confidence interval and one-day holding period (10 days for regulatory capital calculation) are taken into account. In order to test the reliability of the VaR model, back tests are performed. Stress tests and scenario analysis are also applied in order to reflect the effects of prospective severe market fluctuations in the VaR calculations. Beside the VaR limits, the limits on transaction, trader, position, stop-loss approved by the board of directors for trading portfolio are also applied for limiting the market risk.

The capital requirement for general market risk and specific risks is calculated using the standard method defined by the “Regulation on Measurement and Assessment of Capital Adequacy Ratios of Banks” as set out by the BRSA and reported monthly on a bank-only basis and quarterly on a consolidated basis.

### **26.3 Non-trading activities**

Below is a discussion of the various risks the Bank and its affiliates are exposed to as a result of its non-trading activities and the approach taken to manage those risks.

#### *Liquidity risk*

Liquidity risk is defined as the risk that the Bank may not be able to fulfil its payment obligations in a timely manner due to the lack of available cash or cash inflows in quality and in quantity to cover the cash outflows in a complete and timely manner due to imbalances in the cash flows of the Bank and its affiliates.

Liquidity Risk is managed by Asset and Liability Management Department (ALMD) and Asset and Liability Committee (ALCO) in line with risk management policies and risk appetite approved by the board of directors in order to take the necessary measures in a timely and correct manner against possible liquidity shortages that may result from market conditions and balance sheet structure. Under stressed conditions, liquidity risk is managed within the Contingency Funding Plan framework.

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

The board of directors reviews the liquidity risk management strategy, policy and practices, and approves the liquidity strategy and policies within the framework of risk management strategy and policies, ensures the effective of practice of policies and integrations with Bank's risk management strategy. It determines the basic metrics in liquidity risk measurement and monitoring. It establishes risk appetite of the Bank in liquidity risk management and identifies the risk limits in accordance with the risk appetite and reviews it regularly.

ALCO takes necessary decisions which will be executed by related departments by assessing the liquidity risk that the Bank is exposed to and considering the Bank's strategy and conditions of competition and pursues the implementations.

ALMD, performs daily liquidity management by ensuring compliance with regulatory and internal liquidity limits and monitoring related early warning indicators in case of probable liquidity squeezes. The medium and long term liquidity and funding management is performed by ALMD in accordance with ALCO decisions.

Risk Management Department defines the Bank's liquidity risk, measures and monitors the risks with liquidity risk measurement methods that are in compliance with international standards, presents measurement results periodically to related departments, committees and senior management. Risk Management Department coordinates related parties in order to ensure compliance of risk management process in accordance with the Bank's risk profile, operation environment and strategic plan with regulations. Risk Management Department analyses, develops and revises relevant liquidity risk measurement methods and models in accordance with changing market conditions and the Bank's structure. Risk Management Department reviews assumptions and parameters used in liquidity risk analysis.

The liquidity risk analysis and the important early warning signals are reported monthly to related senior management. Additionally, analysis and monitored internal ratios related to liquidity risk are presented in ALCO report. Internal liquidity metrics are monitored with limit and alert levels approved by the board of directors and reported regularly to related parties.

Decentralized management approach is adopted in the Bank's liquidity management. Each subsidiary controlled by the Bank performs daily, medium and long term liquidity management independently from the Bank by the authorities in each subsidiary responsible for managing liquidity risk. In addition, within the scope of consolidated risk management, liquidity and funding risk of each subsidiary in control are monitored via the liquidity risk management methods identified by the Bank by considering the operations, risk profile and regulations of the related subsidiary. Also, in increasing market volatility and liquidity deficit environments, cash flows of especially financial subsidiaries are monitored with the Bank's cash flow on a consolidated basis.

The Bank's funding management is carried out in compliance with the ALCO decisions. Funding and placement strategies are developed by assessing liquidity of the Bank.

In liquidity risk management actions that will be taken and procedures are determined by considering normal economic conditions and stress conditions.

Diversification of assets and liabilities is assured so as to be able to continuously meet the obligations, also taking into account the relevant currencies. Funding sources are monitored actively during identification of concentration risk related to funding. The Bank's funding base of customer deposits, interbank and other borrowing transactions are diversified in order to prevent the concentration of a particular funding source. Factors that could trigger the sudden and significant run off in funds or impair the accessibility of the funding sources are analyzed. Additionally, securities which are eligible as collateral at CBRT issued by Republic of Turkey Treasury and have active secondary market are comprised in the Bank's assets.

## 26 Financial risk management disclosures (continued)

In the context of TL and foreign currencies liquidity management, the cash flows regarding assets and liabilities are monitored and the required liquidity in future periods is forecasted. In cash flow analysis, stress is applied to items that affect the liquidity by volume and rate of change from a liquidity management point of view.

Liquidity risk exposed by the Bank is managed by establishing risk appetite, risk mitigation according to the liquidity and funding policies (diversification of funding sources, holding high quality liquid assets reserve) and effective control environment and closely monitoring by limits. For those risks that cannot be reduced, the adoption of the current level of risk, reduction or termination of the activities that cause the risk is considered.

In liquidity risk stress testing framework, the level of the Bank's ability to cover cash outflows in liquidity crisis scenario based on the Bank's current cash flow structure, by high quality liquid assets is calculated. Scenario analysis are performed by assessing changing balance sheet structure, liquidity requirements and market conditions.

The results of liquidity risk stress testing are taken into consideration in the assessment of liquidity adequacy and identification of strategy, policy and procedures regarding liquidity risk and contingency funding plan is prepared within this framework.

There exists "Liquidity Risk Management Contingency Funding Plan" in the Bank including mechanisms to prevent increase in liquidity risk during normal and liquidity crisis scenarios for different conditions and levels. Available liquidity sources are determined by considering the liquidity squeezes. Within the framework of this plan, the Bank monitors liquidity risk in terms of early warning indicators, stress levels determined according to probable scenarios and severity of the crisis and possible actions that can be taken in each stress level. In determination of the stress level in the plan, early warning indicators are taken into consideration.

The table below presents the last three months' consolidated liquidity ratios in accordance with the BRSA regulations:

<b>Period</b>	<b>TL+FC</b>	<b>FC</b>
31 July 2016	124.76%	175.23%
31 August 2016	128.96%	136.58%
30 September 2016	119.10%	135.48%

### *Exposure to liquidity risk*

Liquidity Coverage Ratio (LCR), aims for the banks having the ability to cover 30 days of liquidity needs with their own cash and high quality liquid assets that are easy to convert to cash during liquidity shortages in the markets. With that perspective and according to "Regulation for Banks' Liquidity Coverage Ratio Calculations" terms LCR ratio is calculated by having high quality liquid assets divided by net cash outflows. After a transition period that will end by 1 January 2019, in both bank-only and consolidated basis, LCR ratio should be at least 80% for foreign currency and 100% for total.

The Bank's banking affiliate in the Netherlands is subject to liquidity coverage ratio requirements as per the rules of Capital Requirement Regulation. In addition, the Dutch Central Bank applies a national liquidity regulation, where the bank is required to have a positive liquidity gap in stress test scenario.

The Bank's banking affiliate in Russia is subject to three levels of liquidity requirement; instant liquidity of minimum 15%, current liquidity of minimum 50% and long-term liquidity of maximum 120%.

The Bank's banking affiliate in Romania calculates the liquidity ratio as a ratio of effective liquidity in local currency equivalent to necessary liquidity in local currency equivalent for several individual time buckets (<1 month, 1-3 months, 3-6 months, 6-12 months, >1 year) and each ratio for each bucket should be >1.



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The following table provides an analysis of monetary assets and monetary liabilities of the consolidated entities into relevant maturity groupings based on the remaining periods to repayment:

	<b>30 September 2016</b>							
	<i>Demand Accounts</i>	<i>Up to 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Over 5 year</i>	<i>Undistributed</i>	<i>Total</i>
<b>MONETARY ASSETS</b>								
<b>Turkish Lira</b>								
Cash and balances with central banks	1,795,441	-	-	-	-	-	-	1,795,441
Financial assets at fair value through profit or loss	94,112	49	2,191	27,738	66,421	26,938	-	217,449
Loans and advances to banks	10,952	392,919	370,794	333,987	1,999	-	-	1,110,651
Loans and advances to customers	223,058	27,943,459	13,535,523	26,158,966	32,605,410	7,393,805	506,049	108,366,270
Derivative financial assets	-	375,108	238,350	326,416	300,415	141,412	-	1,381,701
Other assets	34,904	442,035	24,553	34,051	12,330	2,287	1,538,894	2,089,054
Investment securities	35,170	103	216,319	508,192	14,662,072	14,839,616	-	30,261,472
Deferred tax asset	-	-	-	-	-	-	871,103	871,103
Total Turkish Lira monetary assets	2,193,637	29,153,673	14,387,730	27,389,350	47,648,647	22,404,058	2,916,046	146,093,141
<b>Foreign Currency</b>								
Cash and balances with central banks	5,774,158	10,143,680	-	-	-	-	-	15,917,838
Financial assets at fair value through profit or loss	857,736	-	-	218	6,369	6,584	-	870,907
Loans and advances to banks	3,059,494	1,991,129	610,565	2,309,239	3,115,158	-	-	11,085,585
Loans and advances to customers	171,109	5,321,937	6,318,106	18,816,050	34,580,887	15,322,115	1,375,578	81,905,782
Derivative financial assets	-	7,039	1,573	23,679	121,831	351,749	-	505,871
Other assets	164,897	15,408,402	29,294	17,797	36,625	14,696	43,204	15,714,915
Investment securities	162,918	117,660	-	231,109	4,695,653	9,017,539	-	14,224,879
Deferred tax asset	-	-	-	-	-	-	8,858	8,858
Total foreign currency monetary assets	10,190,312	32,989,847	6,959,538	21,398,092	42,556,523	24,712,683	1,427,640	140,234,635
Total Monetary Assets	12,383,949	62,143,520	21,347,268	48,787,442	90,205,170	47,116,741	4,343,686	286,327,776
<b>MONETARY LIABILITIES</b>								
<b>Turkish Lira</b>								
Deposits	17,459,367	41,051,885	11,353,260	1,649,453	10,527	-	-	71,524,492
Obligations under repurchase agreements and money market fundings	-	17,974,934	141,898	-	-	-	-	18,116,832
Loans and advances from banks and other institutions	-	634,374	41,370	1,707,116	494,940	-	-	2,877,800
Bonds payable	-	119,113	1,324,944	2,657,531	637,421	-	-	4,739,009
Subordinated liabilities	-	-	-	-	-	-	-	-
Derivative financial liabilities	-	220,379	266,393	410,794	249,748	255,078	-	1,402,392
Other liabilities, accrued expenses and provisions	623,394	8,501,485	230,488	40,426	-	-	1,773,754	11,169,547
Total Turkish Lira monetary liabilities	18,082,761	68,502,170	13,358,353	6,465,320	1,392,636	255,078	1,773,754	109,830,072
<b>Foreign Currency</b>								
Deposits	23,044,830	41,702,556	15,312,939	13,668,526	1,866,410	13,702	-	95,608,963
Obligations under repurchase agreements and money market fundings	81	-	453,509	-	67,122	40,788	-	561,500
Loans and advances from banks and other institutions	-	928,707	5,652,802	11,105,631	13,395,546	5,373,514	-	36,456,200
Bonds payable	-	60,295	23,775	2,040,946	6,461,556	1,803,042	-	10,389,614
Subordinated liabilities	-	-	-	-	-	-	-	-
Derivative financial liabilities	-	20,089	13,154	54,701	372,034	464,444	-	924,422
Other liabilities, accrued expenses and provisions	849,881	339,746	211,563	78,336	1,225	1,938	51,509	1,534,198
Total foreign currency monetary liabilities	23,894,792	43,051,393	21,667,742	26,948,140	22,163,893	7,697,428	51,509	145,474,897
Total Monetary Liabilities	41,977,553	111,553,563	35,026,095	33,413,460	23,556,529	7,952,506	1,825,263	255,304,969

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	<b>31 December 2015</b>						
<b>Demand Accounts</b>	<b>Up to 1 month</b>	<b>1 to 3 months</b>	<b>3 to 12 months</b>	<b>1 to 5 years</b>	<b>Over 5 year</b>	<b>Undistributed</b>	<b>Total</b>
<b>MONETARY ASSETS</b>							
<b>Turkish Lira</b>							
Cash and balances with central banks	2,232,969	-	-	-	-	-	2,232,969
Financial assets at fair value through profit or loss	46,415	4,290	18,813	20,186	255,335	15,683	360,722
Loans and advances to banks	12,090	359,053	255,374	384,137	-	-	1,010,654
Loans and advances to customers	177,200	25,586,430	10,772,947	24,310,309	29,024,574	(134,282)	96,093,175
Derivative financial assets	-	357,444	208,887	805,277	532,557	-	2,061,315
Other assets	61,285	330,050	23,510	27,295	9,859	3,127	1,603,251
Investment securities	36,661	545,535	92,089	3,564,412	12,161,308	14,891,514	31,291,519
Deferred tax asset	-	-	-	-	-	973,920	973,920
<b>Total Turkish Lira monetary assets</b>	<b>2,566,620</b>	<b>27,182,802</b>	<b>11,371,620</b>	<b>29,111,616</b>	<b>41,983,633</b>	<b>21,423,471</b>	<b>135,627,525</b>
<b>Foreign Currency</b>							
Cash and balances with central banks	4,121,492	447,647	-	-	-	-	4,569,139
Financial assets at fair value through profit or loss	244,556	-	6,304	144	26,983	21,484	299,471
Loans and advances to banks	4,145,901	3,218,509	537,176	1,003,214	4,462,633	-	13,367,433
Loans and advances to customers	106,043	5,764,896	5,790,213	19,319,191	33,513,594	13,942,402	79,588,517
Derivative financial assets	-	2,149	2,215	24,992	138,006	178,998	346,360
Other assets	134,012	21,513,617	14,848	18,706	16,617	13,877	21,768,274
Investment securities	311,899	42,336	18,437	305,102	4,240,385	9,863,145	14,781,304
Deferred tax asset	-	-	-	-	-	39,632	39,632
<b>Total foreign currency monetary assets</b>	<b>9,063,903</b>	<b>30,989,154</b>	<b>6,369,193</b>	<b>20,671,349</b>	<b>42,398,218</b>	<b>24,019,906</b>	<b>134,760,130</b>
<b>Total Monetary Assets</b>	<b>11,630,523</b>	<b>58,171,956</b>	<b>17,740,813</b>	<b>49,782,965</b>	<b>84,381,851</b>	<b>45,443,377</b>	<b>270,387,655</b>
<b>MONETARY LIABILITIES</b>							
<b>Turkish Lira</b>							
Deposits	14,634,342	38,696,247	11,784,139	1,028,267	45,880	-	66,188,875
Obligations under repurchase agreements and money market fundings	-	12,969,582	2,349	-	-	-	12,971,931
Loans and advances from banks and other institutions	-	746,972	583,489	545,485	1,771,884	-	3,647,830
Bonds payable	-	338,130	1,309,030	2,170,048	722,975	-	4,540,183
Subordinated liabilities	-	-	-	-	-	-	-
Derivative financial liabilities	-	408,125	265,148	1,186,464	426,513	75,316	2,361,566
Other liabilities, accrued expenses and provisions	191,300	7,502,967	459,492	12,870	583	-	9,878,064
<b>Total Turkish Lira monetary liabilities</b>	<b>14,825,642</b>	<b>60,662,023</b>	<b>14,403,647</b>	<b>4,943,134</b>	<b>2,967,835</b>	<b>75,316</b>	<b>99,588,449</b>
<b>Foreign Currency</b>							
Deposits	23,704,722	36,108,674	14,475,645	14,248,616	1,371,869	16,054	89,925,580
Obligations under repurchase agreements and money market fundings	-	616,969	219,109	2,530,104	190,167	39,516	3,595,865
Loans and advances from banks and other institutions	-	1,519,935	1,346,699	13,981,234	14,027,900	5,436,336	36,312,104
Bonds payable	-	-	58,391	1,194,078	6,418,318	3,300,627	10,971,414
Subordinated liabilities	-	-	14,406	14,396	116,594	14,396	159,792
Derivative financial liabilities	-	8,521	15,481	62,608	259,021	166,351	511,982
Other liabilities, accrued expenses and provisions	1,161,410	313,412	161,122	37,272	921	658	1,767,121
<b>Total foreign currency monetary liabilities</b>	<b>24,866,132</b>	<b>38,567,511</b>	<b>16,290,853</b>	<b>32,068,308</b>	<b>22,384,790</b>	<b>8,973,938</b>	<b>143,243,858</b>
<b>Total Monetary Liabilities</b>	<b>39,691,774</b>	<b>99,229,534</b>	<b>30,694,500</b>	<b>37,011,442</b>	<b>25,352,625</b>	<b>9,049,254</b>	<b>242,832,307</b>

## 26 Financial risk management disclosures (continued)

### *Contractual maturity analysis of liabilities according to remaining maturities*

The remaining maturities table of the contractual liabilities includes the undiscounted future cash outflows for the principal amounts of the Bank and its financial affiliates' financial liabilities as per their earliest likely contractual maturities.

#### **30 September 2016**

	<b><i>Carrying Value</i></b>	<b><i>Nominal Principal Outflows</i></b>	<b><i>Demand</i></b>	<b><i>Up to 1 Month</i></b>	<b><i>1 to 3 Months</i></b>	<b><i>3 to 12 Months</i></b>	<b><i>1 to 5 Years</i></b>	<b><i>Over 5 Years</i></b>
Deposits	167,133,455	166,542,293	40,485,463	82,447,456	26,556,904	15,180,013	1,858,846	13,611
Obligations under repurchase agreements and money market fundings	18,678,332	18,663,349	81	17,963,851	591,676	-	67,122	40,619
Loans and advances from banks and other Institutions	39,334,000	39,072,823	-	1,498,620	5,816,449	12,861,577	13,664,850	5,231,327
Bonds payable	15,128,623	14,822,851	-	174,149	1,332,221	4,683,526	6,837,117	1,795,838
Subordinated liabilities	-	-	-	-	-	-	-	-
<b>Total Monetary Liabilities</b>	<b><u>240,274,410</u></b>	<b><u>239,101,316</u></b>	<b><u>40,485,544</u></b>	<b><u>102,084,076</u></b>	<b><u>34,297,250</u></b>	<b><u>32,725,116</u></b>	<b><u>22,427,935</u></b>	<b><u>7,081,395</u></b>

#### **31 December 2015**

	<b><i>Carrying Value</i></b>	<b><i>Nominal Principal Outflows</i></b>	<b><i>Demand</i></b>	<b><i>Up to 1 Month</i></b>	<b><i>1 to 3 Months</i></b>	<b><i>3 to 12 Months</i></b>	<b><i>1 to 5 Years</i></b>	<b><i>Over 5 Years</i></b>
Deposits	156,114,455	155,534,497	38,311,491	74,518,267	26,125,705	15,158,334	1,404,773	15,927
Obligations under repurchase agreements and money market fundings	16,567,796	16,547,426	-	13,576,686	221,241	2,520,164	190,025	39,310
Loans and advances from banks and other institutions	39,959,934	39,732,456	-	2,201,943	1,843,153	14,482,064	15,795,528	5,409,768
Bonds payable	15,511,597	15,171,939	-	331,132	1,353,146	3,343,310	7,026,530	3,117,821
Subordinated liabilities	<u>159,792</u>	<u>158,355</u>	-	-	<u>14,396</u>	<u>14,396</u>	<u>115,167</u>	<u>14,396</u>
<b>Total Monetary Liabilities</b>	<b><u>228,313,574</u></b>	<b><u>227,144,673</u></b>	<b><u>38,311,491</u></b>	<b><u>90,628,028</u></b>	<b><u>29,557,641</u></b>	<b><u>35,518,268</u></b>	<b><u>24,532,023</u></b>	<b><u>8,597,222</u></b>

### *Market risk*

**Interest rate risk:** The Bank and its affiliates' operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets (including investments) and interest-bearing liabilities mature or reprice at different times or in differing amounts. In the case of floating rate assets and liabilities, the Bank and its affiliates are also exposed to basis risk, which is the difference in repricing characteristics of the various floating rate indices, such as the deposit rate and libor and different types of interest. Treasury activities are aimed at optimizing net interest income, given market interest rate levels consistent with the Bank's business strategies.

In general, as common in current economic environment, the consolidated financial statements are liability sensitive because its interest-earning assets have a longer duration and reprice slightly less frequently than interest-bearing liabilities. This means that in rising interest rate environments, margins earned will narrow as liabilities reprice. However, the actual effect will depend on a number of factors, including the extent to which repayments are made earlier or later than the contracted dates and variations in interest rate sensitivity within repricing periods and among currencies.

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

Interest rate derivatives are primarily used to bridge the mismatch in the repricing of assets and liabilities. This is done in accordance with the guidelines established by the Bank's asset-liability management committee.

Some assets have no defined maturities or interest rate sensitivities and are not readily matched with specific liabilities. Those assets are funded through liability pools based on the assets' estimated maturities and repricing characteristics.

Part of the Bank's return on financial instruments is obtained from controlled mismatching of the dates on which interest receivable on assets and interest payable on liabilities are next reset to market rates or, if earlier, the dates on which the instruments mature.

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The following table provides an analysis of interest rate sensitivity of monetary assets and liabilities of the consolidated entities into relevant maturity groupings:

	<b>30 September 2016</b>						
	<b>Up to 1 month</b>	<b>1 to 3 months</b>	<b>3 to 12 months</b>	<b>1 to 5 years</b>	<b>Over 5 year</b>	<b>Non-Interest Bearing</b>	<b>Total</b>
<b>MONETARY ASSETS</b>							
Cash and balances with central banks	14,450,256	-	-	-	-	3,263,023	17,713,279
Financial assets at fair value through profit or loss	5,680	3,558	52,369	41,388	32,922	952,439	1,088,356
Loans and advances to banks	3,854,959	2,556,685	2,492,396	46,363	272,049	2,973,784	12,196,236
Loans and advances to customers	44,599,823	33,258,916	50,349,847	47,022,794	12,809,619	2,231,053	190,272,052
Other assets	9,871,300	174	-	14,939	2,287	9,802,841	19,691,541
Investment securities	4,269,919	6,970,865	10,891,245	7,668,340	10,517,115	4,168,867	44,486,351
Deferred tax asset	-	-	-	-	-	879,961	879,961
Total Monetary Assets	<u>77,051,937</u>	<u>42,790,198</u>	<u>63,785,857</u>	<u>54,793,824</u>	<u>23,633,992</u>	<u>24,271,968</u>	<u>286,327,776</u>
<b>MONETARY LIABILITIES</b>							
Deposits	88,387,225	26,567,664	15,249,745	1,780,437	5,665	35,142,719	167,133,455
Obligations under repurchase agreements and money market fundings	17,963,852	591,676	-	67,122	40,620	15,062	18,678,332
Loans and advances from banks and other institutions	12,514,427	16,599,414	5,298,579	4,497,642	149,380	274,558	39,334,000
Bonds payable	204,069	1,398,045	4,683,527	6,741,373	1,795,836	305,773	15,128,623
Subordinated liabilities	-	-	-	-	-	-	-
Other liabilities, accrued expenses and provisions	-	-	-	-	-	15,030,559	15,030,559
Total Monetary Liabilities	<u>119,069,573</u>	<u>45,156,799</u>	<u>25,231,851</u>	<u>13,086,574</u>	<u>1,991,501</u>	<u>50,768,671</u>	<u>255,304,969</u>
	<b>31 December 2015</b>						
	<b>Up to 1 month</b>	<b>1 to 3 months</b>	<b>3 to 12 months</b>	<b>1 to 5 years</b>	<b>Over 5 year</b>	<b>Non-Interest Bearing</b>	<b>Total</b>
<b>MONETARY ASSETS</b>							
Cash and balances with central banks	2,099,364	-	-	-	-	4,702,744	6,802,108
Financial assets at fair value through profit or loss	13,237	31,597	226,676	64,627	34,920	289,136	660,193
Loans and advances to banks	5,595,450	2,455,707	2,493,892	8,924	-	3,824,114	14,378,087
Loans and advances to customers	42,364,614	24,499,855	51,195,710	44,622,908	11,780,806	1,217,799	175,681,692
Other assets	805,963	-	-	-	3,126	24,970,111	25,779,200
Investment securities	1,943,865	10,146,778	11,090,909	8,686,541	11,076,840	3,127,890	46,072,823
Deferred tax asset	-	-	-	-	-	1,013,552	1,013,552
Total Monetary Assets	<u>52,822,493</u>	<u>37,133,937</u>	<u>65,007,187</u>	<u>53,383,000</u>	<u>22,895,692</u>	<u>39,145,346</u>	<u>270,387,655</u>
<b>MONETARY LIABILITIES</b>							
Deposits	80,169,766	26,191,936	15,265,914	1,221,025	5,862	33,259,952	156,114,455
Obligations under repurchase agreements and money market fundings	13,576,686	221,241	2,520,164	190,025	39,310	20,370	16,567,796
Loans and advances from banks and other institutions	14,543,784	14,504,579	4,782,467	5,715,968	185,658	227,478	39,959,934
Bonds payable	1,272,460	1,431,663	2,416,522	6,933,473	3,117,821	339,658	15,511,597
Subordinated liabilities	-	-	158,355	-	-	1,437	159,792
Other liabilities, accrued expenses and provisions	-	-	-	-	-	14,518,733	14,518,733
Total Monetary Liabilities	<u>109,562,696</u>	<u>42,349,419</u>	<u>25,143,422</u>	<u>14,060,491</u>	<u>3,348,651</u>	<u>48,367,628</u>	<u>242,832,307</u>

## 26 Financial risk management disclosures (continued)

The following table indicates the effective interest rates by major currencies for the major components of the consolidated statement of financial position for the first nine-months of 2016 and the year 2015:

	<i>30 September 2016</i>			
	<i>US\$</i> <i>%</i>	<i>EUR</i> <i>%</i>	<i>TL</i> <i>%</i>	<i>Other</i> <i>Currencies</i> <i>%</i>
<i>Assets</i>				
Loans and advances to banks	1-3	1-2	1-16	1-11
Debt and other fixed or floating income instruments	3-12	1-5	7-15	6-15
Loans and advances to customers	1-11	1-13	1-37	1-31
<i>Liabilities</i>				
<i>Deposits:</i>				
- Foreign currency deposits	1-4	1-8	-	1-10
- Bank deposits	1-2	1-3	1-12	1-9
- Saving deposits	-	-	6-11	-
- Commercial deposits	-	-	7-15	-
- Public and other deposits	-	-	10	-
Obligations under repurchase agreements and money market fundings	2-3	-	6-11	1
Loans and advances from banks and other institutions	1-4	1-5	10-14	1-4
Bonds payable	1-5	1-3	1-12	1-5
	<i>31 December 2015</i>			
	<i>US\$</i> <i>%</i>	<i>EUR</i> <i>%</i>	<i>TL</i> <i>%</i>	<i>Other</i> <i>Currencies</i> <i>%</i>
<i>Assets</i>				
Loans and advances to banks	1-8	1-2	1-15	1
Debt and other fixed or floating income instruments	1-12	1-6	1-15	3-16
Loans and advances to customers	1-7	1-14	1-33	1-28
<i>Liabilities</i>				
<i>Deposits:</i>				
- Foreign currency deposits	1-4	1-9	-	1-12
- Bank deposits	1-2	1-2	6-12	1-11
- Saving deposits	-	-	7-11	-
- Commercial deposits	-	-	8-15	-
- Public and other deposits	-	-	11	-
Obligations under repurchase agreements and money market fundings	1-3	1	6-14	1-12
Loans and advances from banks and other institutions	1-6	1-6	1-16	1-12
Bonds payable	1-6	1-5	8-12	1-6

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

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

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

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

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

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

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

### *Currency risk*

The Bank and its affiliates are exposed to currency risk through transactions in foreign currencies and through its investment in foreign operations. The Bank and its affiliates' main foreign operations are in the Netherlands, Russia and Romania. The measurement currencies of its operations are Euro, US Dollars and Romanian Leu. As the currency in which the Bank presents its consolidated financial statements is TL, the consolidated financial statements are affected by currency exchange rate fluctuations against TL. The Bank finances a significant proportion of its net investment in foreign operations with borrowings in the same currencies as the relevant measurement currencies to mitigate its currency risk. Currency swaps are also used to match the currency of some of its other borrowings to the measurement currencies involved. The foreign currency exchange risk of the Bank is managed through transaction, trader, position and stop-loss limits approved by the board of directors for the trading portfolio beside the foreign currency net position standard ratio and the VaR limit. The Bank and its affiliates' transactional exposures give rise to foreign currency gains and losses that are recognized in the statement of income. These exposures comprise the monetary assets and monetary liabilities that are not denominated in the measurement currency of the Bank involved.

## 26 Financial risk management disclosures (continued)

These exposures are as follows:

	<b>30 September 2016</b>			<b>Total</b>
	<b>US\$</b>	<b>EUR</b>	<b>Other Currencies</b>	
<i>Assets</i>				
Cash and balances with central banks	2,831,961	12,841,378	244,499	15,917,838
Financial assets at fair value through profit or loss	12,156	1,015	857,736	870,907
Loans and advances to banks	7,671,846	3,065,152	348,587	11,085,585
Loans and advances to customers	43,898,110	35,119,014	2,888,658	81,905,782
Other assets	9,914,951	4,005,715	2,300,120	16,220,786
Investment securities	11,722,557	2,434,451	67,871	14,224,879
Investments in equity participations	-	806	531	1,337
Tangible and intangible assets	188	87,671	93,472	181,331
Deferred tax asset	-	-	8,858	8,858
<b>Total Assets</b>	<b>76,051,769</b>	<b>57,555,202</b>	<b>6,810,332</b>	<b>140,417,303</b>
<i>Liabilities</i>				
Deposits	56,089,157	32,899,702	6,620,104	95,608,963
Obligations under repurchase agreements and money market fundings	189,427	67,122	304,951	561,500
Loans and advances from banks and other institutions	24,645,513	11,565,292	245,395	36,456,200
Current and deferred tax liability	-	20,691	2,975	23,666
Bonds payable	7,416,314	1,974,624	998,676	10,389,614
Other liabilities, accrued expenses and provisions	1,903,832	403,204	127,918	2,434,954
<b>Total Liabilities</b>	<b>90,244,243</b>	<b>46,930,635</b>	<b>8,300,019</b>	<b>145,474,897</b>
<b>Net Statement of Financial Position</b>	<b>(14,192,474)</b>	<b>10,624,567</b>	<b>(1,489,687)</b>	<b>(5,057,594)</b>
<b>Net Off Balance Sheet Position</b>	<b>13,934,836</b>	<b>(12,012,222)</b>	<b>3,034,904</b>	<b>4,957,518</b>
<b>Net Long/(Short) Position</b>	<b>(257,638)</b>	<b>(1,387,655)</b>	<b>1,545,217</b>	<b>(100,076)</b>
<b>31 December 2015</b>				
	<b>US\$</b>	<b>EUR</b>	<b>Other Currencies</b>	<b>Total</b>
<b>Total Assets</b>	<b>84,165,368</b>	<b>42,524,127</b>	<b>8,240,541</b>	<b>134,930,036</b>
<b>Total Liabilities</b>	<b>91,320,718</b>	<b>44,319,606</b>	<b>7,603,534</b>	<b>143,243,858</b>
<b>Net Statement of Financial Position</b>	<b>(7,155,350)</b>	<b>(1,795,479)</b>	<b>637,007</b>	<b>(8,313,822)</b>
<b>Net Off Balance Sheet Position</b>	<b>7,542,704</b>	<b>2,060,338</b>	<b>(122,494)</b>	<b>9,480,548</b>
<b>Net Long/(Short) Position</b>	<b>387,354</b>	<b>264,859</b>	<b>514,513</b>	<b>1,166,726</b>

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

The short positions in the statement of financial position shown in the table above are hedged by currency swaps, forward contracts and other derivatives entered into to manage these currency exposures. In respect of monetary assets and liabilities in foreign currencies that are not economically hedged, the Bank and its affiliates ensure that their net exposures are kept to an acceptable level by buying and selling foreign currencies at spot rates when considered appropriate.



## 26 Financial risk management disclosures (continued)

### *Credit risk*

The Bank and its affiliates are subject to credit risk through the trading, lending, hedging and investing activities and the guarantees issued for their customers as well as in cases where they act as intermediaries on behalf of customers or other third parties.

The Bank and its affiliates' primary exposures to credit risk arise through its loans and advances. The amount of credit exposure in this regard is represented by the carrying amounts of these assets on the statement of financial position. The Bank developed a statistical-based internal risk rating model for its credit portfolio of corporate/commercial/medium-size companies. This internal risk rating model has been in use for customer credibility assessment since 2003 and is currently being reviewed and updated. Risk rating has become a requirement for loan applications, and ratings are used both to determine credit authorization limits and in credit assessment process.

The concentration table of the cash and non-cash loans for the Bank according to the risk rating system for its customers defined as corporate, commercial and small-size enterprises is presented below:

	<i>30 September</i>	<i>31 December</i>
	<i>2016</i>	<i>2015</i>
	<u>%</u>	<u>%</u>
Above Average	40	40
Average	48	50
Below Average	<u>12</u>	<u>10</u>
	100	100

Concentrations based on industries and groups are also monitored. Application scorecards are used during loan granting process for retail and credit card portfolios. Behavioural scorecards are also used for these portfolios.

The Bank and its affiliates are exposed to credit risk on various other financial assets, including derivative instruments used for hedging and debt investments. The current credit exposure in respect of these instruments is equal to the carrying amount of these assets in the statement of financial position. In addition, the Bank and its affiliates are exposed to off balance sheet credit risk through guarantees issued (Note 24).

The risk that counterparties to both derivative and other instruments might default on their obligations is monitored on an ongoing basis. To manage the level of credit risk, the Bank and its affiliates deal with counterparties of good credit standing, enter into master netting agreements whenever possible, and when appropriate, obtain collateral.

Concentrations of credit risk (whether on or off balance sheet) that arise from financial instruments exist for groups of counterparties when they have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions.

## 26 Financial risk management disclosures (continued)

### *Exposure to credit risk*

	<i>Loans and advances to customers</i>	
	<u>30 September 2016</u>	<u>31 December 2015</u>
Individually impaired	6,970,335	6,090,168
Allowance for impairment	(5,319,165)	(5,456,587)
Carrying amount	<u>1,651,170</u>	<u>633,581</u>
Portfolio basis allowance	(2,331,173)	(1,759,922)
Loans under follow-up but not impaired	<u>4,890,252</u>	<u>4,182,192</u>
Carrying amount	<u>4,890,252</u>	<u>4,182,192</u>
Neither past due nor impaired	178,154,353	165,579,230
Loans with renegotiated terms	<u>7,907,450</u>	<u>7,046,611</u>
Carrying amount	<u>186,061,803</u>	<u>172,625,841</u>
Total carrying amount	<u>190,272,052</u>	<u>175,681,692</u>

### *Impaired loans*

Impaired loans are loans for which the Bank determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan agreement due to lack of assets, high debtness ratio, insufficient working capital and/or equity of the customer.

### *Sectoral and geographical concentration of impaired loans*

The Bank and its affiliates monitor concentrations of credit risk by sector and by geographic location.

An analysis of concentrations of non-performing loans and lease receivables is shown below:

	<u>30 September 2016</u>	<u>31 December 2015</u>
Consumer loans	2,744,398	2,671,683
Construction	506,862	325,767
Transportation and logistics	454,563	201,586
Service sector	396,365	335,607
Transportation vehicles and sub-industries	363,175	201,704
Textile	321,786	298,488
Metal and metal products	308,979	293,942
Food	278,304	244,694
Energy	267,381	237,241
Agriculture and stockbreeding	209,290	218,503
Tourism	146,110	164,772
Chemistry and chemical products	100,824	95,774
Paper and paper products	87,647	83,405
Durable consumption	83,276	94,638
Others	<u>701,375</u>	<u>622,364</u>
Total non-performing loans, factoring and lease receivables	<u>6,970,335</u>	<u>6,090,168</u>

## 26 Financial risk management disclosures (continued)

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Turkey	5,750,336	4,683,987
Romania	610,868	804,845
Malta	236,121	99,856
Ukraine	109,181	106,375
Switzerland	89,828	88,084
England	68,034	85,514
Cyprus	26,896	27,510
Russia	17,378	37,418
Others	<u>61,693</u>	<u>156,579</u>
Total non-performing loans, factoring and lease receivables	<u>6,970,335</u>	<u>6,090,168</u>

### *Past due but not impaired loans*

These are loans where contractual interest or principal payments are past due but the Bank believes that individual impairment is not appropriate on the basis of the level of collateral available and the customer's current activities, assets and financial position.

### *Renegotiated loans*

Loans are generally renegotiated either as part of the on-going banking relationship with a creditworthy customer or in response to a borrower's financial difficulties. In the latter case, renegotiation encompasses not only revisions to the terms of a loan such as a maturity extension, a payment moratorium, a concessionary rate of interest but also the restructuring of all or part of the exposure.

### *Allowances for impairment*

The Bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a portfolio-basis loan loss allowance established for groups of homogeneous assets in respect of losses that have been incurred but have not been identified on loans subject to individual assessment for impairment.

### *Write-off policy*

The Bank writes off a receivable balance (and any related allowances for impairment losses) when it is determined that the receivable is uncollectible based on the evidence of insolvency issued by the court. In cases where any possible collections are negligible comparing to the prospective expenses and costs, such receivables are written off by the decision of the board of directors.

### *Collateral policy*

The Bank's policy is to require suitable collateral to be provided by certain customers prior to the disbursement of approved loans. The Bank and its affiliates currently hold collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets and guarantees. Collateral generally is not held over loans and advances to banks, except when securities are held as part of reverse repurchase and securities borrowing activity. Collateral usually is not held against investment securities, and no such collateral was held at 30 September 2016 or 31 December 2015.

As part of its statutory capital adequacy calculations, and as per the legislation revised accounting to the Basel II requirements and effective from 1 July 2012, the Bank applies credit risk mitigation

## 26 Financial risk management disclosures (continued)

according to the comprehensive method that includes risk mitigation calculations considering the volatility-adjusted values of financial collaterals in compliance with the relevant local legislation. In the credit risk mitigation, cash and cash equivalent items and high-credit-quality debt instruments are used. The volatility adjustments regarding the receivables, collaterals and currency mismatch of the collaterals are made as per the standard volatility-adjustment approach defined in the relevant regulation. In cases where there are maturity mismatches resulted from shorter remaining life of collateral than of receivables, the value of collateral is considered as the volatility-adjusted value.

The fair value of collateral held against non-performing loans and receivables, is presented below, as per the collateral type, up to the outstanding total amount of exposures:

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Mortgages	1,618,434	1,178,270
Pledge assets	525,492	505,952
Promissory notes	500,769	693,470
Cash collateral	18,508	17,416
Unsecured	<u>4,307,132</u>	<u>3,695,060</u>
	<u>6,970,335</u>	<u>6,090,168</u>

The amounts reflected in the tables above represent the maximum accounting loss that would be recognized at the date of the statement of financial position if counterparties failed completely to perform as contracted and any collateral or security proved to be of no value.

### *Operational risks*

Operational risk expresses the probability of loss that may arise from the overlook of faults and inconsistency with the established rules due to the deficiencies in the Bank and its affiliates' internal controls, manner of the management and the personnel that are not in coherence with time and conditions, deficiencies in the bank management, faults and problems in information technology systems and disasters such as earthquake, fire, flood or terror attacks.

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

Currently, the value at operational risk is calculated according to the basic indicator approach as per the Article 23 of "Regulation on Measurement and Assessment of Capital Adequacy Ratios of Banks" as pronounced by the BRSA.

The annual gross income is defined as net interest income plus net non-interest income reduced by realised gains/losses from the sale of securities available-for-sale and held-to-maturity, non-recurring gains and income derived from insurance claims. The result is added to risk weighted assets in the capital adequacy calculation.

### *Capital management – regulatory capital*

The BRSA sets and monitors capital requirements for the Bank as a whole. The parent company and individual banking operations are directly supervised by their local regulators. In implementing current capital requirements, the BRSA requires the banks to maintain a prescribed ratio of

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

minimum 8% of total capital to total value at credit, market and operational risks. The Bank and its affiliates' consolidated regulatory capital is analysed into two tiers:

- Tier 1 capital, which includes paid-in capital, share premium, legal reserves, retained earnings, other comprehensive income, translation reserve and non-controlling interests after deductions for goodwill and certain cost items.
- Tier 2 capital, which includes qualifying subordinated liabilities and general provisions.

The BRSA also requires the banks to maintain prescribed ratios of minimum 6% and 4.5% of Tier 1 and Tier 2 capital, respectively, to total value at credit, market and operational risks starting from 1 January 2014.

Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures. The Bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognized and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position. There have been no material changes in the Bank's management of capital during the period.

Starting from 1 July 2012, the capital adequacy ratio is calculated within the scope of the "Regulation on Measurement and Assessment of Capital Adequacy Ratios of Banks (the "Regulation")", "Regulation on Credit Risk Mitigation Techniques" and "Regulation on Calculation of Risk Weighted Amounts for Securitisations" published in the Official Gazette no.28337 dated 28 June 2012 and the "Regulation on Equities of Banks" published in the Official Gazette no.26333 dated 1 November 2006 but later revised in the Official Gazette no.28756 dated 5 September 2013. The Bank's process of internal capital requirements is assessed under the regulation on the "Internal Systems and Internal Capital Adequacy Assessment Processes of Banks" published in the Official Gazette no. 29057 dated 11 July 2014. In calculation of capital adequacy ratio, the data prepared from accounting records in compliance with the current legislation are used. Such accounting data is included in the calculation of credit and market risks subsequent to their designation as "trading book" and "banking book" according to the Regulation. The items classified as trading book and the items deducted from the equity are not included in the calculation of credit risk. In the calculation of risk weighted assets, the assets subject to amortisation or impairment, are taken into account on a net basis after being reduced by the related amortisations and provisions.

In the calculation of the value at credit risk for the non-cash loans and commitments and the receivables from counterparties in such transactions are weighted after netting with specific provisions that are classified under liabilities and calculated based on the "Regulation on Identification of and Provision against Non-Performing Loans and Other Receivables". The net amounts are then multiplied by the rates stated in the Article 5 of the Regulation, reduced as per the "Regulation on Credit Risk Mitigation Techniques" and then included in the relevant exposure category defined in the article 6 of the Regulation and weighted as per Appendix-1 of the Regulation.

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

## 26 Financial risk management disclosures (continued)

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

The Bank’s and its affiliates’ regulatory capital positions on consolidated basis as of 30 September 2016 and 31 December 2015, are as follows:

	<i>30 September</i>	<i>31 December</i>
	<u>2016</u>	<u>2015</u>
Tier 1 capital	34,197,954	30,968,875
Tier 2 capital	2,750,801	2,817,785
Deductions from capital	<u>(129,908)</u>	<u>(1,120,150)</u>
Total regulatory capital	36,818,847	32,666,510
Value at credit, market and operational risks	246,251,829	241,514,612
<u>Capital ratios (%)</u>		
Total regulatory capital expressed as a percentage of total value at credit, market and operational risks	14.95	13.53
Total tier 1 capital expressed as a percentage of total value at credit, market and operational risks	13.89	12.82

### 26.4 Hedging

Due to the Bank and its affiliates’ overall interest rate risk position and funding structure, its risk management policies require that it should minimize its exposure to changes in foreign currency rates and manage interest rate, credit risk and market price risk exposure within certain guidelines. Derivative financial instruments are used to manage the potential earnings impact of interest rate and foreign currency movements. Several types of derivative financial instrument are used for this purpose, including interest rate swaps and currency swaps, options, financial futures, forward contracts and other derivatives. The purpose of the hedging activities is to protect the Bank and its affiliates from the risk that the net cash inflows will be adversely affected by changes in interest or exchange rates, credit ratings or market prices. The Bank and its affiliates enter into transactions to ensure that it is economically hedged in accordance with risk management policies. In the accompanying consolidated financial statements, hedge accounting is applied for the cases where hedge accounting relationship is evidenced.

From time to time, the Bank enters into various interest rate swap transactions in order to hedge its certain cash flow or fair value exposures on floating/fixed rate assets and liabilities, through converting its floating/fixed rate income/payments into fixed/floating rate income/payments.

In this respect, the Bank applied fair value hedge accounting for the fixed rate eurobonds issued in 2011 with a total face value of USD 500,000,000, maturity of 10 years and maturity date of 20 April 2021 which were priced at 6.375% originally and had a coupon rate of 6.25%, by designating interest rate swaps with the same face value amount and conditions. In June 2012, the Bank ceased to apply hedge accounting and accordingly fair value calculations for these bonds. The accumulated fair value differences incurred starting from the date of hedge accounting up to the date on which it was ceased, are amortized as per the effective interest-rate method in compliance with IAS 39.

The Bank also applied fair value hedge accounting for its fixed-rate loans with a total principal of TL 2,958,521 thousands, USD 1,100,660,941 and EUR 156,885,339 and for its bonds with a total face value of TL 1,405,000 thousands and USD 265,400,000 and fixed-rate coupons by designating interest rate swaps with the same face values and terms. Accordingly, in the current period, gains of TL 194,800 thousands and TL 52,396 thousands (30 September 2015: a gain of TL 113,103 thousands and a loss of TL 57,422 thousands resulting from outstanding transactions at that date)

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

resulted from the related fair value calculations for the hedged loans and bonds were accounted for under trading income/losses in the income statement, respectively.

In addition; the Bank also entered into cross currency swap agreements in order to hedge its fixed-rate bonds issued for a total principal value of AUD 175,000,000 and RON 85,500,000 with the same face values and terms. Accordingly, in the current period, a loss of TL 15,716 thousands (30 September 2015: total loss of TL 16,797 thousands resulting from outstanding transactions at that date) resulted from the fair value changes of the securities issued and funds borrowed subject to hedge accounting were accounted for under trading income/losses in the income statement.

The Bank applied cash flow hedge accounting for its funds borrowed amounting to USD 83,818,378 and EUR 42,105,266, securitization borrowings amounting to USD 116,666,668 and EUR 166,663,165 by designating cross currency swaps with the same face values and terms, and eurobonds with a total nominal value of USD 10,000,000, the collateralised borrowings amounting to TL 500,000 thousands and USD 250,000,000, borrowings amounting to USD 650,000,000, securitizations amounting to USD 500,000,000 and deposits amounting to USD 300,000,000 by designating interest rate swaps with the same face values and terms. Accordingly, in the current period, a gain of TL 18,461 thousands and a loss of TL 68,137 thousands (30 September 2015: gains of TL 93,893 thousands and TL a loss of 12,121 thousands resulting from outstanding transactions at that date) resulting from cross currency and interest rate swap agreements were recognised under shareholders' equity.

One of the Bank's consolidated affiliates associated its contractual operational lease receivables (contractual future cash flows) denominated in EUR with its EUR denominated borrowings and other foreign currency borrowings converted to EUR currency through swap transactions and applied cash flow hedge accounting. The foreign currency exposures in operational lease receivables are hedged and accordingly the effective portion of foreign currency gains/losses of non-derivative hedging instruments designated for hedges of future cash flows are recognised directly in equity and any ineffective portion is recognised immediately in income. As of 30 September 2016, a negative amount of TL 32,069 thousands (net of deferred taxes) was recognised under shareholders' equity as the hedging reserve (30 September 2015: TL 46,755 thousands).

One of the Bank's consolidated affiliate enters into interest rate swap agreements in order to hedge the change in fair values of its fixed rate financial instruments due to fluctuations in market interest rates. In this respect, the affiliate applied fair value hedge accounting for fixed rate eurobonds with a total face value of USD 240,193,000 and EUR 145,000,000 by designating interest rate swaps with the same face values and terms. Accordingly, in the current period, net gains of TL 18,206 thousands (30 September 2015: -) resulting from the related fair value calculations for the hedged bonds were accounted for under trading income/losses in the income statement.

One of the Bank's consolidated affiliate enters into interest rate agreements in order to hedge the change in cash flows of floating rate financial instruments due to fluctuations in market interest rates. In this respect, the affiliate applied cash flow hedge accounting for its funds borrowed amounting to USD 319,807,000 by designating interest rate swaps with the same face values and terms. Accordingly, in the current period, a net loss of TL 500 thousands (30 September 2015: -) resulting from interest rate swap agreements were recognised under shareholders' equity.

One of the Bank's consolidated affiliate enters into foreign currency derivative contracts to hedge the foreign currency risk of its expected future cash flows. In this respect, the affiliate applied cash flow hedge accounting for its loans granted in Turkish Lira by designating swaps with the same face value amount and similar terms; TL 255,000,000 sell and USD 80,076,154 buy, USD 80,076,154 sell and EUR 69,829,075 buy TL 715,000,000 sell and EUR 207,889,067 buy, CHF 5,487,510 sell and EUR 5,022,622 buy, RON 45,000,000 sell and EUR 9,838,216 buy. Accordingly, in the current period, losses of TL 2,891 thousands (30 September 2015:-) resulting from currency derivative contracts were recognized under shareholder's equity.

## 27 Affiliates, associates and special purpose entities

The table below sets out the consolidated affiliates, associates and special purpose entities of the Bank and its shareholding interests in these entities:

	<b>30 September</b>	<b>31 December</b>
	<b>2016</b>	<b>2015</b>
<b><i>Consolidated entities</i></b>		
Garanti Bank International NV	100.00	100.00
Garanti Holding BV	100.00	100.00
Garanti Bank Moscow	100.00	100.00
Garanti Portföy Yönetimi AŞ	100.00	100.00
Garanti Yatırım Menkul Kıymetler AŞ	100.00	100.00
Garanti Bilişim Teknolojisi ve Tic. AŞ	100.00	100.00
Garanti Filo Yönetimi Hizmetleri AŞ	100.00	100.00
G Netherlands BV	100.00	100.00
Garanti Bank SA	100.00	100.00
Motoractive IFN SA	100.00	100.00
Ralfi IFN SA	100.00	100.00
Garanti Finansal Kiralama AŞ	100.00	100.00
Garanti Emeklilik ve Hayat AŞ	84.91	84.91
Garanti Faktoring AŞ	81.84	81.84
Garanti Yatırım Ortaklığı AŞ	3.30	3.30
Garanti Diversified Payment Rights Finance Company (a)	-	-
RPV Company (a)	-	-

(a) *Garanti Diversified Payment Rights Finance Company and RPV Company, are special purpose entities established for the Bank's securitization transactions, as explained in Note 17, and consolidated in the accompanying consolidated financial statements. The Bank or any of its affiliates do not have any shareholding interests in these companies.*

## 28 Net fee and commission income

	<i>Nine-month period ended</i>	<i>Three-month period ended</i>	<i>Nine-month period ended</i>	<i>Three-month period ended</i>
	<b>30 September 2016</b>	<b>30 September 2016</b>	<b>30 September 2015</b>	<b>30 September 2015</b>
<i>Fee and commission income:*</i>				
Credit cards fees	1,892,683	688,375	1,634,123	565,533
Retail banking	407,547	117,479	372,845	150,565
SME banking	321,044	102,610	301,191	105,869
Commercial banking	239,973	80,891	220,395	75,965
Corporate banking	29,653	11,207	49,667	20,170
Others	<u>222,762</u>	<u>74,564</u>	<u>126,006</u>	<u>42,096</u>
Total fee and commission income	<u>3,113,662</u>	<u>1,075,126</u>	<u>2,704,227</u>	<u>960,198</u>
<i>Fee and commission expense:</i>				
Credit cards fees	606,858	210,617	552,874	208,175
Retail banking	38,760	14,668	23,700	7,879
Commercial banking	9,747	3,718	2,530	885
SME banking	3,699	1,575	2,505	905
Corporate banking	177	86	141	52
Others	<u>113,354</u>	<u>36,288</u>	<u>104,557</u>	<u>39,693</u>
Total fee and commission expense	<u>772,595</u>	<u>266,952</u>	<u>686,307</u>	<u>257,589</u>
Net fee and commission income	<u>2,341,067</u>	<u>808,174</u>	<u>2,017,920</u>	<u>702,609</u>

(\*Includes cancellations/repayments, by the Bank in the current period, of fees and commissions income recognized in prior years in the amount of TL 95,642 thousands (30 September 2015: TL 199,828 thousands) as per the decision of the Turkish Competition Board or the related courts.



## 29 Trading gains/(losses)

Gains and losses from derivative financial instruments and changes in fair value of other trading instruments are reflected in net trading gains/(losses) including the effective portion of fair value hedges, whereas, gains and losses arising from changes in the effective portion of the fair value of cash flow hedges are reflected as a separate component of equity. Net gains/(losses) from trading of financial assets is detailed in the table below:

	<i>Nine-month period ended 30 September 2016</i>	<i>Three-month period ended 30 September 2016</i>	<i>Nine-month period ended 30 September 2015</i>	<i>Three-month period ended 30 September 2015</i>
Fixed/floating securities	218,948	107,093	804,023	499,628
Derivative transactions	<u>65,011</u>	<u>339,434</u>	(897,925)	<u>633,500</u>
Trading gains/(losses), net	<u>283,959</u>	<u>446,527</u>	<u>(93,902)</u>	<u>1,133,128</u>

## 30 Other operating income

	<i>Nine-month period ended 30 September 2016</i>	<i>Three-month period ended 30 September 2016</i>	<i>Nine-month period ended 30 September 2015</i>	<i>Three-month period ended 30 September 2015</i>
<i>Other operating income:</i>				
Net sales from Garanti Technology	29,437	5,709	31,709	11,741
Net sales from Garanti Fleet <sup>(*)</sup>	36,529	11,510	75,466	23,465
Dividend income	9,066	4	5,387	-
Rent income from real estate (including investment property)	8,530	2,710	7,508	2,630
Cheque booklet charge	6,340	2,053	6,172	1,945
Others	<u>29,546</u>	<u>10,620</u>	<u>25,633</u>	<u>3,957</u>
Total operating income	<u>119,448</u>	<u>32,606</u>	<u>151,875</u>	<u>43,738</u>

<sup>(\*)</sup> Depreciation expenses of the fleet portfolio are netted-off with the net sales of Garanti Fleet;

	<i>Nine-month period ended 30 September 2016</i>	<i>Three-month period ended 30 September 2016</i>	<i>Nine-month period ended 30 September 2015</i>	<i>Three-month period ended 30 September 2015</i>
Net sales	92,943	37,782	118,670	44,108
Less: Depreciation	<u>(56,414)</u>	<u>(26,272)</u>	<u>(43,204)</u>	<u>(20,643)</u>
Net sales after depreciation	<u>36,529</u>	<u>11,510</u>	<u>75,466</u>	<u>23,465</u>

## 31 Other operating expenses

	<i>Nine-month period ended 30 September 2016</i>	<i>Three-month period ended 30 September 2016</i>	<i>Nine-month period ended 30 September 2015</i>	<i>Three-month period ended 30 September 2015</i>
Saving deposits insurance fund	171,015	57,187	145,324	50,889
Computer usage expenses	141,162	49,165	110,072	41,032
Advertising expenses	126,742	38,950	86,186	27,404
Claim losses from insurance business	94,834	31,737	61,839	25,727
Utility expenses	76,774	27,620	67,316	20,101
Repair and maintenance expenses	45,987	15,853	60,182	33,041
Research and development expenses	25,655	8,590	21,010	10,507
Stationary expenses	19,874	5,960	20,568	7,672
Insurance related expenses	14,872	5,827	38,223	16,187
Others <sup>(*)</sup>	<u>445,478</u>	<u>141,737</u>	<u>658,547</u>	<u>228,703</u>
	<u>1,162,393</u>	<u>382,626</u>	<u>1,269,267</u>	<u>461,263</u>

<sup>(\*)</sup> Includes lawsuit, execution and other legal expenses borne by the Bank in the current period, of fees and commissions income recognized in prior years but reimbursed, in the amount of TL46,393 thousands (30 September 2015: TL 37,097 thousands), as per the decision of the Turkish Competition Board or the related courts.

## **32 Use of estimates and judgements**

Management discussed with the Audit Committee the development, selection and disclosure of the Bank's critical accounting policies and estimates, and the application of these policies and estimates. These disclosures supplement the commentary on financial risk management (see Note 26).

### *Key sources of estimation uncertainty*

#### Allowances for credit losses

Assets accounted for at amortized cost are evaluated for impairment on a basis described in Note 7.

The specific counterparty component of the total allowances for impairment applies to claims evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgement about a counterparty's financial situation and the net realisable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the credit risk function.

Portfolio-basis assessed impairment allowances cover credit losses inherent in portfolios of claims with similar economic characteristics when there is objective evidence to suggest that they contain impaired claims, but the individual impaired items cannot yet be identified. A component of portfolio-basis assessed allowances relates to country risks. In assessing the need for collective loan loss allowances, management considers factors such as credit quality, portfolio size, concentrations, and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the specific allowances depends on the estimated future cash flows for specific counterparties and the assumptions and inputs to the impairment used in determining collective allowances.

#### Determining fair values

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques as described in significant accounting policies section and Note 23. For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgement depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

### *Critical accounting judgements in applying the Bank's accounting policies*

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

#### Financial asset and liability classification

The Bank and its affiliates' accounting policies provide scope for assets and liabilities to be designated on inception into different accounting categories in certain circumstances:

- In classifying financial assets or liabilities as "trading", the Bank has determined that it meets the description of trading assets and liabilities set out in accounting policy (h) *Financial instruments*.
- In designating financial assets or liabilities at fair value through profit or loss, the Bank has determined that it has met one of the criteria for this designation set out in accounting policy (h) *Financial instruments*.
- In classifying financial assets as held-to-maturity, the Bank has determined that it has both the positive intention and ability to hold the assets until their maturity date as required by accounting policy (h) *Financial instruments*.

## 32 Use of estimates and judgements (continued)

### Securitized assets

In applying its policies on securitized financial assets, the Bank has considered both the degree of transfer of risks and rewards on assets transferred to another entity and the degree of control exercised by the Bank over the other entity:

- When the Bank, in substance, controls the entity to which financial assets have been transferred, the entity is included in these consolidated financial statements and the transferred assets are recognized in the Bank's consolidated statement of financial position.
- When the Bank has transferred financial assets to another entity, but has not transferred substantially all of the risk and rewards relating to the transferred assets, the assets are recognized in the Bank's consolidated statement of financial position.
- When the Bank transfers substantially all the risks and rewards relating to the transferred assets to an entity that it does not control, the assets have been derecognized from the Bank's consolidated statement of financial position.

Details of the Bank's securitization activities are given in Note 17.

### Control over investments

As a bank, regardless of the nature of its involvement with an entity, is required to determine whether it is a parent by assessing whether it controls the entity, the Bank also reassesses whether or not it controls an investment when facts and circumstances indicate that there are changes to one or more of the following three elements of control:

- power over the investee;
- exposure, or rights, to variable returns from involvement with the investee; and
- the ability to use power over the investee to affect the amount of its returns.

## 33 Significant events

- As per the decision made at the annual general assembly of shareholders of the Bank on 31 March 2016, the statutory net income of 2015 was distributed as follows;

<b>2015 INCOME DISTRIBUTION TABLE</b>	
<b>2015 Net Income</b>	<b>3,406,507</b>
A – I. Legal reserve (Turkish Commercial Code 519/1) at 5%	-
Undistributable funds	4,723
B – First dividend at 5% of the paid-in capital	210,000
C – Extraordinary reserves at 5% after above deductions	159,826
D – Second dividend to the shareholders	357,000
E – Extraordinary reserves	2,639,258
F – II. Legal reserve (Turkish Commercial Code 519/2)	35,700

- As of 21 June 2016, the acquisition of Visa Europe Ltd. by Visa Inc. has been completed. In acquisition, the Bank and a consolidated financial affiliate have sold their two shares in Visa Europe Ltd. with a nominal of EUR 10.00 for a consideration of EUR 61,376,433 in cash and 22.284 in "C Type Visa Inc." shares. The income generated from the sale share is recognized under gain on sale of assets in other operating income.

### **34 Subsequent event**

The Bank has entered into a share purchase agreement with Sovcombank, a bank operating in Russia, for the sale of 1729 shares representing 99.94% of the share capital of GarantiBank Moscow AO, a consolidated subsidiary, together with one share held by Garanti Bilişim Teknolojisi ve Ticaret AŞ, on 10 October 2016. Share transfers under the agreement will be completed after obtaining the necessary regulatory approvals. Parties agreed on a purchase price of USD 40,455,201 subject to certain adjustments for the period until the completion of the share transfer procedures.

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