

Company Registration No. 2643004

Turkish Bank (UK) Limited

Report and Financial Statements

31 December 2018

Turkish Bank (UK) Limited
Report and financial statements 2018

| Contents | Page |
|---|-------------|
| Chairman's Statement | 3 |
| Strategic Report | 5 |
| Directors' Report | 7 |
| Independent Auditor's Report | 10 |
| Statement of Profit or Loss and Other Comprehensive Income | 16 |
| Statement of Financial Position | 17 |
| Statement of Cash Flows | 18 |
| Statement of Changes in Equity | 19 |
| Notes to the accounts | 20 |

Turkish Bank (UK) Limited

Report and financial statements 2018

Officers and professional advisors

Directors

I H Bortecene (Chairman)
S M Bennett
S Betteridge **
J W Heales *
J Gillan
M Arig
M Y Rahmioglu
A A Doherty (appointed 29 December 2017, resigned 31 January 2018)
R W Long (resigned 2 May 2018)

* Chairman of the Audit Committee

** Chairman of the Risk Committee

Registered office

84-86 Borough High Street
London SE1 1LN

Auditor

Mazars LLP
Chartered Accountants
Tower Bridge House,
St Katharine's Way,
London
E1W 1DD

Chairman's Statement

In last year's statement, I had written about the unprecedented change that we had witnessed in the year. This year, we have come to the realisation that this rate of rapid change has become a constant in our lives, with no signs of reducing in the near future. This has led to our new motto in the Turkish Bank Group: 'A quarter equals a year'.

In 2018, the uncertainty over global economic policies, high volatility in the financial markets of developed economies and ongoing geopolitical tensions affected global growth negatively. Political policies, steering away from globalization, and concerns over international trade have been gradually causing a decrease in global growth estimations. The growth rate of the world economy was 3.2% in 2018, but the forecast has been reduced down to 2.9% for 2019.

Gradual monetary tightening, by major central banks, continued in 2018. However, sluggish growth and the increased uncertainty over the global economy led to the expectation that the pace of policy normalization in advanced economies might decelerate going forward.

The uncertainty of Mr. Trump's policies, rising trade wars especially with China, and financial market volatility in the US forced the Fed to adopt a more cautious tone on rate hikes. Despite stronger labour data and higher wage growth, the Fed revised its median projection to one or two rate hikes for 2019, at its December meeting; down from three at the March meeting.

The UK economy expanded 1.3%, year-on-year, in the fourth quarter of 2018. Lower growth in the UK would follow a similar pattern in some of the Eurozone's biggest economies. Forecasts for growth in 2019 are down to 1.2%, from a previous estimate of 1.7%. In 2018, the inflation rate was at 2.1%. The mounting Brexit uncertainty causes the Bank of England to tone down its policy response to rising inflation. The expectation is for the Bank of England to increase interest rates from 0.75% once in 2019, while the asset purchase program of £435 billion is in progress.

The Turkish economy has shown a very volatile pattern in 2018. It grew in the first 2 quarters of 2018, at 7.2% and 5.3% respectively, but it lost momentum towards the second half of the year and the growth rate decreased to 1.6% in the 3rd quarter of the year. The TRY depreciation was due to tighter global liquidity conditions, extensive private sector foreign exchange debt, as well as political and geopolitical risks. The inflation rate has increased mainly due to foreign exchange pass through effect and rising oil prices. The Turkish authorities have since taken steps which have served to soothe the volatility.

The Turkish Republic of Northern Cyprus's (TRNC) estimated growth rate of 2018 is around 5%. The most important contributions to the growth are tourism and trade. Due to the low import to export ratio, the increase in foreign trade of the TRNC implies an increase in the foreign trade deficit. Inflation rate still continues to keep high levels; in parallel with the Turkish Lira depreciation

This year we are approaching Group institutions with a wide-ranging thematic focus, we have been increasingly using this approach to anchor our goals in these fast shifting environments. On our agenda for the whole Group is a focus on improving the cost/income ratio through increased marketing efforts, Digital Transformation and HR. The Group is also focusing on Assets Under Management (AUM) as a key indicator, this is arising from our belief that Digital Wealth Management has a great potential in the future, through Open Banking practices.

Our parent company has had a successful year; high liquidity arising from historically conservative policies combined with TRY interest rate hikes, resulted in a 100% increase in profitability compared to last year. 2018 has also marked the start of our new Managing Director Mr. Erhan Raif. Mr. Raif has been with the Group for over 30 years and has taken over from Mr. Rahmioğlu who will continue serving on the Parents Board with a focus on the insurance arm as well as social responsibility projects. One such exciting project is our Green Bank Project. Turkish Bank Ltd. has made significant strides in adopting green policies that govern its lending practices but perhaps more exciting is the upcoming Solar Energy project aiming to source all the Bank and its subsidiaries energy needs. This will help us achieve a more sustainable business model for our next generations. In addition to this, Turkish Bank Ltd. has become the first ever corporate bond issuer of TRNC, another mile stone that we are proud of. I am also pleased to say that this year has seen enhanced collaboration between Turkish Bank (UK) Ltd (TBUK) and Turkish Bank Ltd. Together they have created a new product to assist UK expats who reside in TRNC, a mirror of our community business in London.

Chairman's Statement (continued)

In order to focus on these important projects, Mr Rahmioglu will be stepping down from the Board of TBUK, to be replaced by Mr Kemal Şahin. Mr Şahin's appointment is part of our continued effort to increase diverse subject matter experts on our Boards, rejuvenating the management team of TBUK; as well as improving synergy across Group organisations. Mr. Şahin's background in Compliance, Financial Crime and Internal Control with over 25 years of experience at top tier international banks around Europe will certainly be beneficial for TBUK.

This year TBUK will be focusing on its cost/income ratio as is the rest of the Group. A lot of preparation has been done to lower the cost level of TBUK, primarily through our investments in technology infrastructure.

Digital transformation program continues to mark our actions. 2018 was the year we completed the first phase of our program after completing the assessment of Group IT infrastructure, Human Capital as well as workflows and processes. With ever decreasing demand for branch services, we see a continuing downtrend in branch numbers across the Group that are being replaced with more sophisticated channels like Video Banking and Whatsapp Banking.

TBUK has kept its network this year, with the relocation of our Mayfair Office from Brook Street to a newly refurbished office space on 20 North Audley Street just 5 minutes away. We believe that this new model of shared offices and co-work spaces will be the way of the future and based on the excellent customer feedback we receive, we will continue to embrace modern work environments in the near future

Whilst Brexit is full speed ahead, we do not anticipate any significant impact to our business but we continue to closely monitor the highly fluid events as they unfold in order to manage any risk that may arise. It is worth noting that UK and Turkey relations are witnessing historically high economic cooperation, a welcome rapprochement between two friendly nations in these challenging times of Brexit.

Looking forward to 2019; TBUK will continue investing in Cyber Security and Operational Resilience. In addition to this, Open Banking is a key strategic area that the Bank is preparing for with the expectation of a possible leapfrogging opportunity. Following our membership to the Payment Schemes, the Bank continues with the momentum in significantly investing in this area.

In the year 2018, we have increased our outreach and engagement with the wider Turkish community in the United Kingdom as a result of which we recently sponsored a major cultural event as part of our efforts in London that gathered over 7000 people from the Turkish community over two days. We also launched a Group wide internal newsletter called "Turkish Times" that is on its third issue already. These are all parts of our effort to increase transparent communication with all our stakeholders.

We are now going into our 45th year in the United Kingdom and our mission remains the same as always; to serve the Turkish-speaking community with dignity, care, diligence, and at the highest standards of Banking.

Hakan Bortecene

Chairman of the Board

April 4, 2019

The Strategic report

For the year ended 31 December 2018

Review of the Year

Profit before tax decreased from £46k to a loss before tax of £246k, driven principally by an increase in non-recurring professional fees due to projects expanded on below.

The Bank joined the Faster Payments and BACs payments schemes successfully at the end of 2017 and the Cheque Clearing Scheme in 2018. These have all resulted in an improved service for our customers. During and following these projects, the Bank took the opportunity to review its processes and governance and upgrade its core banking software and internet services. The costs associated with these, together with other one off external professional fees of £673K were expensed in the year, resulting in an increase in general overheads as the Bank invests for its future.

During 2018 the Bank attracted an increase in deposits, a reflection of the Bank's reputation for strong and conservative management, with high liquidity. This drove Treasury related interest income which, combined with steady interest from the lending portfolio, increased net interest income from £4.6million to £4.9million. Fee income was reduced mainly as a result of a reduction in remittance transfers offset by a slight increase in commission on loans and advances.

Impairment losses for the year remained low at £18k. Total ECL provisions in accordance with IFRS 9 stood at £158k (2017: £135k), 2017 provision includes the IBNR (Incurred But Not Recorded) of £100k; this level of provisioning, against a loan book of £96.3 million, is below the norm for the industry. This reflects the Bank's policy of concentrating on secured lending at cautious margins of collateral and debt serviceability. The Bank continues to monitor its loan book closely to identify cases of financial stress with a view to providing assistance wherever possible.

Total assets increased by £16.8m to £194.4m driven principally through surplus funds being placed with The Bank of England. Total lending decreased slightly to £96.3m, a result of the conservative stance taken by the Bank off the back of some economic challenges in Turkey and lead up to Brexit.

Customer deposits at year end increased by £1.2m (2017: decrease £8mn) to £146.2m (2016: £145mn).

There was an increase in the level of fees received from lending activities. These fee increases were offset by a planned reduction in remittance fee income, hence there was a reduction in total fee income.

During 2017 and 2018, the Bank invested heavily in developing its platform, fully integrating into the UK's payments infrastructure, enhancing its internet banking and upgrading its core banking software. These investments, together with an ongoing focus on improving customer service and driving efficiency put the Bank in a strong position to take advantage of some exciting industry developments, such as the increasing digitalisation of services and Open Banking. The Bank seeks to ensure that it keeps pace with changes in the financial services industry by closely monitoring competition on the High Street and from Fintechs as well as in the wholesale markets.

We look to 2019 knowing that the service enhancements and operating efficiencies we can derive from our investments in the Bank's underlying platform, combined with the continued positive developments in our target market through a steady increase in immigration to the UK, puts us in a strong position to enhance profitability. As always, our focus will be on providing our clients with the quality service to which they are entitled, in line with the Bank's history and values.

Principal risks and uncertainties

The Bank's activities expose it to a number of financial risks including credit risk, interest rate and currency risk, operational risk, reputational risk, liquidity risk and funding risk. The Bank uses only "plain vanilla" currency swaps and does not enter into any exotic contracts. Such swaps are used to hedge the Bank's currency positions and are not used for trading purposes. Risk policies have been disclosed in Note 34 of the financial statements, which also provides greater detail of how risk is managed.

Turkish Bank (UK) Limited

Company Registration No. 2643004

Impact of Brexit

The Bank has undertaken a business wide review on the potential impact of Brexit on its operations. As the Bank does not offer banking services in any other EU or EEA country other than UK, the direct impact is expected to be minimal. Notwithstanding this, the Bank has undertaken comprehensive risk assessments across credit, liquidity and contractual risks in relation the indirect consequences of Brexit, such as house price decline, increased unemployment, a significant depreciation of sterling or other negative economic indicators. Given the conservative approach to lending, the high liquidity and the limited number of customers who have trading relationships with Europe, the impact is expected to be minimal. For example, even when stress testing the lending portfolio to the worst case scenarios, the Bank remains on a sound footing.

Interest rate and currency risk: The Bank's activity exposes it primarily to the financial risk of changes to the interest rate environment and to a lesser extent to foreign currency exchange rate movements. With regard to interest rate risk the Bank has only a very small part of its loan portfolio on fixed interest rates, and the majority is on variable rates, reducing the Bank's exposure to interest rate fluctuations. Money market placements are at fixed rate but these are typically for a short period, up to three months to minimise risks.

Credit risk: The Bank has no significant concentration of credit risk, with lending mainly against UK property and LTV (Loan to Value) which are at the lower end of the UK mortgage market. Regular stress testing of the Bank's collateral security is carried out and the Directors are satisfied with the levels of equity where lending is against freehold and long dated leasehold property which is itself restricted to the UK market.

Liquidity and funding risk: In order to maintain liquidity and funding to ensure that sufficient funds are available for on-going operations and future developments. The Bank has set a cautious risk appetite with a significant proportion of the total assets held in medium-term and short-term money market. The directors believe that the Bank has a strong liquidity and funding position that meets with their Policy guidelines.

The Bank operates a risk management policy and has set quantifiable risk appetite limits and uses financial instruments based on the operations it undertakes. This risk management policy, which includes a description of how financial instruments are used, is disclosed in Note 34 to the financial statements.

Operational Risk can arise from internal or external factors. These include attempted fraud, cyber-attacks, terrorist activities, systems failures and legal risk. The Bank's risk appetite is to mitigate these as far as is practical. Various techniques are used including firewall protection, security controls, back up procedures and recovery plans.

Future developments

The directors aim to maintain the policies that have resulted in the Bank's growth. As stated in the review, the Bank has invested to improve the Bank's internet offering and is also reviewing its product portfolio with the intention to expand the range of products for the benefit of its customers. Other future activities are covered in the Chairman's Report.

Approved by the Board of Directors and signed on behalf of the Board



April 4, 2019

Hakan Bortacene

Directors' report

The Directors present their annual report and the audited financial statements for the year ended 31 December 2018.

Activity Report

The principal activities of Turkish Bank (UK) Limited ("TBUK or the Bank") are twofold namely:

- to provide a superior community banking service to the Turkish-speaking people of London particularly and the UK in general; and
- meet the UK banking needs of Corporate clients and high net worth individuals who are customers of our parent or sister organisations within the Turkish Bank Group.

TBUK is a subsidiary of Turkish Bank Limited and a member of the Turkish Bank Group (Group) headquartered in Istanbul. The Chairman of the Group also performs the role of Chairman of TBUK. TBUK operates within and is guided by the overall strategic objectives of the Group. These focus on providing quality customer service at a competitive price to our clients and to provide a reasonable return on capital to our shareholders. More information regarding TBUK activities can be obtained by accessing the Bank's website at www.turkishbank.co.uk or the Group website at www.turkishbankgroup.com.

Review of the Year

Information regarding the Bank's financial performance and position during the year ended 31 December 2018 is presented in the Strategic Report on page 6.

Principal risks and uncertainties

Information regarding the exposure of credit risk, interest rate and currency risk, liquidity and funding risk are included in the Strategic Report on page 6.

Going Concern

After making enquiries, the Directors have a reasonable expectation that the Bank has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Further details regarding the Bank's accounting policies can be found in the statement of accounting policies in these financial statements on page 20.

| Key performance indicators | 2018 | 2017 |
|---|-------------|-------------|
| (Loss)/Profit before tax as % of equity | (0.90) % | 0.17 % |
| Equity as % of total assets | 14.07 % | 15.00 % |
| General expenses as a % of net income | 104.07 % | 99.21 % |

The Bank recorded a loss driven by exceptional, one-off project related expenses of £673k relating to the investment in the Bank's infrastructure for the future. Equity as a percentage of total assets decreased following the increase in the balance sheet. General expenses as a % of net income increased mainly due to one-off project related costs and a reduction in fee income mentioned above.

Results and dividends

The loss for the year after taxation amounted to £125,000 (2017 – profit £79,000). The Directors do not recommend the payment of a dividend (2017 – £nil)

Prior Year Adjustment

As detailed in Note 2 (b) to these financial statements, a prior year adjustment has been made to correct the calculation of the deferred tax liability on revaluations made to freehold land and properties prior to 2017. The deferred tax liability has been reduced by £587,000 and £636,000 in the opening balances for 2017 and 2018 respectively. This has led to a corresponding increase in net assets at the same time. The Directors confirm that they believe that there has been no breach in regulatory or internal requirements relating to levels of capital.

Turkish Bank (UK) Limited

Company Registration No. 2643004

Political and charitable contributions

The Bank does not make political contributions but does support registered charities that operate in the same community. During the year, the Bank made various charitable contributions totalling £200 (2017 £375).

Directors and their interests

The directors who served during the year were as follows:

I H Bortecene (Chairman)

S M Bennett

S Betteridge **

J W Heales *

J Gillan

M Arig

M Y Rahmioglu

A A Doherty (appointed 29 December 2017, resigned 31 January 2018)

R W Long (resigned 2 May 2018)

* Chairman of the Audit Committee

** Chairman of the Risk Committee

Directors' indemnities

The Bank has made qualifying third-party indemnity provisions for the benefit of its Directors which were made during the year and remain in force at the date of this report.

Audit Committee

The Bank has an Audit Committee comprising three non-executive directors, all of whom are experienced bankers or Subject Matter Experts in their respective field. The Committee met on five occasions in 2018 (2017: five times).

Risk Committee

The Bank has a Risk Committee comprising three non-executive directors (including two independent directors), and the Chief Executive Officer whom are all experienced bankers or Subject Matter Experts in the respective field, plus members of the executive management. The Committee met on five occasions in 2018 (2017: five times).

Disclosure of information to the auditor

Each of the directors of the Bank holding office at the date of approval of this report confirms that: so far as each of the directors are aware, there is no relevant audit information of which the Bank's auditor is unaware; and so far as each of the directors are aware they have taken all the steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the Bank's auditor is aware of that information. This confirmation is given and shall be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

Auditor

Pursuant to Section 487 of the Companies Act 2006, the auditor will be deemed to be reappointed and Mazars LLP will therefore continue in office.



I H Bortecene
April 4, 2019

84-86 Borough High Street
London SE1 1LN
United Kingdom

Turkish Bank (UK) Limited

Company Registration No. 2643004

The directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with IFRSs as adopted by the EU and applicable law.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Bank and of the profit or loss of the Bank for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Bank's transactions and disclose with reasonable accuracy at any time the financial position of the Bank and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Bank and to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Bank's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board



April 4, 2019

Registered in England. Company No. 2643004

Turkish Bank (UK) Limited
Company Registration No. 2643004

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF TURKISH BANK (UK) LIMITED

Opinion

We have audited the financial statements of Turkish Bank (UK) Limited (the 'Bank') for the year ended 31 December 2018 which comprises of the statement of profit or loss and other comprehensive income, the statement of financial position, the statement of cash flows, the statement of changes in equity, and notes to the financial statements on pages 20 - 71, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

In our opinion, the financial statements:

- give a true and fair view of the state of the Bank's affairs as at 31 December 2018 and its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the Bank in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

The Impact of uncertainties due to the United Kingdom exiting the European Union on our audit

The directors' view on the impact of Brexit is disclosed on page 6.

The terms on which the United Kingdom may withdraw from the European Union, are not clear, and it is therefore not currently possible to evaluate all the potential implications to the Bank's trade, customers, suppliers and the wider economy.

We considered the impact of Brexit on the Bank as part of our audit procedures, applying a standard firm wide approach in response to the uncertainty associated with the Bank's future prospects and performance.

However, no audit should be expected to predict the unknowable factors or all possible implications for the Bank and this is particularly the case in relation to Brexit.

Turkish Bank (UK) Limited

Company Registration No. 2643004

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Bank's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) we identified, including those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

We summarise below the key audit matters in forming our audit opinion above, together with an overview of the principal audit procedures performed to address each matter and, where relevant, key observations arising from those procedures.

These matters, together with our findings, were communicated to those charged with governance through our Audit Completion Report.

| Area of Focus | How our audit addressed the area of focus |
|---|---|
| <p>Credit Risk in relation to loan loss provisions</p> <p>The impairment provision relating to the Bank's loan portfolio requires the directors to make judgements over the ability of the Banks' customers to make future loan repayments.</p> <p>The implementation of IFRS 9 has changed the focus of the impairment provisions from an incurred loss model to an expected loss model. The Bank has developed a model to estimate the expected losses requiring judgement to the input parameters and assumptions as set out in note 4 of the financial statements.</p> | <p>We have assessed the design and tested the operating effectiveness of the key controls operating in the Bank in relation to credit processes. This included reviewing the credit files for all significant watch list loans and a sample of performing loans.</p> <p>In respect of the model used to determine expected credit losses we:</p> <ul style="list-style-type: none"> - Considered the appropriateness of methodology used by management; - Reviewed assumptions used in applying the methodology adopted and assessed for reasonableness; - Tested the completeness of the loan portfolio applied to the model; - Tested the process in place at the Bank to |

Turkish Bank (UK) Limited
Company Registration No. 2643004

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|---|--|
| | <p>allocate loans to the IFRS 9 credit risk stages;</p> <ul style="list-style-type: none"> - Assessed the suitability and relevance the key assumptions applied to determine probability of default and loss given default. <p><i>We found the approach taken in respect of loan loss provisions to be consistent with the requirements of IFRS 9 and judgements made were reasonable.</i></p> |
| <p>Risk of fraud in revenue recognition</p> <p>The financial reporting fraud risk over revenue recognition specifically relates to income recognised on an effective interest method (EIR). The EIR takes in to account transactions costs and fees and points paid or received that are an integral part of the EIR. Fees relating to lending arrangements are deferred based on the expected life of the asset.</p> <p>Judgement is required to determine whether fees are recognised as EIR or recognised when a service has been performed over the expected life.</p> | <p>We assessed the design and tested the operation of the controls in place at the Bank relating to revenue recognition.</p> <p>With respect to EIR calculation, we:</p> <ul style="list-style-type: none"> - Re-performed the EIR calculations; - Verified details to underlying loan agreements; - Assessed the period over which yield adjustments are applied; - Considered the appropriateness of judgement applied in determining the basis of revenue recognition including the expected life of the financial instrument. <p><i>We found that the judgements and estimates applied in determining the basis for revenue recognition were reasonable.</i></p> |

Our application of materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole. Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

| | |
|-----------------------------|------------------|
| Overall materiality | £274,000 |
| How we determined it | 1% of net assets |

Turkish Bank (UK) Limited
Company Registration No. 2643004

| | |
|--|---|
| Rationale for benchmark applied | <p>We have used net assets as the benchmark to calculate materiality.</p> <p>In determining this threshold, we have taken into consideration that the Bank is a Public Interest Entity.</p> <p>The Bank was loss making in 2018 so income statement benchmarks were not considered appropriate as a basis for materiality.</p> <p>Net assets was therefore considered to better reflect more appropriately the size of the Bank's operations. Furthermore, it remains the focus of the regulator and shareholders in terms of capital adequacy.</p> |
| Performance materiality | £191,000 |
| Reporting threshold | £8,000 |

An overview of the scope of our audit

As part of designing our audit, we determined materiality and assessed the risk of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements such as making assumptions on significant accounting estimates.

We gained an understanding of the legal and regulatory framework applicable to the Bank, the structure of the Bank and the industry in which it operates. We considered the risk of acts by the Bank which were contrary to the applicable laws and regulations including fraud. We designed our audit procedures to respond to those identified risks, including non-compliance with laws and regulations (irregularities) that are material to the financial statements.

We focused on laws and regulations that could give rise to a material misstatement in the financial statements, including, but not limited to, the Companies Act 2006. We tailored the scope of our audit to ensure that we performed sufficient work to be able to give an opinion on the financial statements as a whole. We used the outputs of a risk assessment, our understanding of the Bank's accounting processes and controls and its environment and considered qualitative factors in order to ensure that we obtained sufficient coverage across all financial statement line items.

Our tests included, but were not limited to, obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by irregularities including fraud or error, review of minutes of directors' meetings in the year and enquiries of management. As a result of our procedures, we did not identify any Key Audit Matters relating to Irregularities, including fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are discussed under "Key audit matters" within this report.

The primary responsibility for the prevention and detection of irregularities including fraud rests with both Those Charged with Governance and management. As with any audit, there remained a risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal controls.

Turkish Bank (UK) Limited
Company Registration No. 2643004
Other Information

The directors are responsible for the other information. The other information comprises the information included in the Report and Financial Statements other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In light of the knowledge and understanding of the Bank and its environment obtained in the course of the audit, we have not identified material misstatements in the Strategic Report or the Directors' Report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Responsibilities of Directors

As explained more fully in the directors' responsibilities statement set out on page 9 the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

Turkish Bank (UK) Limited
Company Registration No. 2643004

Auditor's responsibilities for the audit of the financial statements

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

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Other matters which we are required to address

Following the recommendation of the audit committee, we were appointed by those charged with governance on 20 September 2018 to audit the financial statements for the year ended 31 December 2018 and subsequent financial periods. The period of total uninterrupted engagement is 1 year.

The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Bank and we remained independent of the Bank in conducting our audit.

Our audit opinion is consistent with the additional report to the audit committee.

Use of the audit report

This report is made solely to the Bank's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's members as a body for our audit work, for this report, or for the opinions we have formed.



Greg Simpson (Senior Statutory Auditor)
for and on behalf of Mazars LLP
Chartered Accountants and Statutory Auditor
Tower Bridge House
St Katharine's Way
London
England
E1W 1DD
April 4, 2019

Turkish Bank (UK) Limited

Statement of Profit or Loss and Other Comprehensive Income For the year ended 31 December 2018

| | | 2018 | 2017 |
|---|--------|----------------|----------------|
| | Notes | £'000 | £'000 |
| Interest income | 8 | 6,166 | 5,786 |
| Interest expense | 8 | (1,275) | (1,217) |
| Net interest income | 8 | 4,891 | 4,569 |
| Fees and commissions receivable | 9 | 1,155 | 1,299 |
| Fees and commissions payable | 9 | (163) | (200) |
| Net fee and commission income | | 992 | 1,099 |
| Net trading income | 10 | 156 | 184 |
| Other operating income | | 4 | 1 |
| Impairment losses on financial instruments | 12, 19 | (18) | (9) |
| Total operating income | | 6,025 | 5,844 |
| Personnel expenses | 11 | (2,722) | (2,828) |
| Premises and equipment | | (607) | (552) |
| Administrative expenses | | (2,299) | (1,890) |
| Depreciation and amortisation | 21,22 | (638) | (517) |
| Other expenses | | (5) | (11) |
| Total operating expenses | | (6,271) | (5,798) |
| (Loss)/Profit before taxation | 13 | (246) | 46 |
| Income tax credit | 14 | 121 | 33 |
| (Loss)/Profit after taxation | | (125) | 79 |
| Other comprehensive income | | | |
| Items that will not be reclassified to profit or loss | | | |
| Equity investments at FVOCI – net change in fair value | 16 | 199 | N/A |
| Deferred tax effect of net change in fair value of equity investments | | (31) | N/A |
| Items that are or may subsequently be classified to profit or loss | | | |
| Available for sale financial assets net change in fair value | | N/A | (60) |
| Revaluation of properties | | - | 1,732 |
| Deferred tax on property revaluation | | - | (245) |
| Total other comprehensive income | | 168 | 1,427 |
| Total comprehensive income | | 43 | 1,506 |

The notes on pages 20 to 71 form an integral part of these financial statements.
All activities relate to continuing operations.

Turkish Bank (UK) Limited

Statement of Financial Position For the year ended 31 December 2018

| | | 2018 | 2017 |
|-------------------------------------|-------|----------------|----------------|
| | | | Restated |
| | Notes | £'000 | £'000 |
| Assets | | | |
| Cash and cash equivalents | 15 | 85,862 | 63,088 |
| Loans and advances to banks | 17 | 1,773 | 1,772 |
| Loans and advances to customers | 18 | 94,480 | 98,532 |
| Investment securities | 20 | 498 | 812 |
| Current taxation assets | 14 | 206 | 151 |
| Property and equipment | 22 | 8,979 | 9,265 |
| Intangible assets | 21 | 1,386 | 1,459 |
| Other assets | 23 | 1,189 | 2,524 |
| Total assets | | 194,373 | 177,603 |
| Liabilities | | | |
| Deposits from banks | 24 | 18,854 | 3,138 |
| Deposits from customers | 25 | 146,164 | 145,009 |
| Deferred tax liabilities | 27 | 374 | 332 |
| Derivative liabilities | 30 | 78 | 50 |
| Other liabilities | 26 | 1,547 | 1,791 |
| Total liabilities | | 167,017 | 150,320 |
| Equity | | | |
| Called up share capital | 28 | 12,000 | 12,000 |
| Retained earnings | | 8,069 | 8,198 |
| Fair value reserve | | 467 | 265 |
| Revaluation reserve | | 6,820 | 6,820 |
| Total equity | | 27,356 | 27,283 |
| Total liabilities and equity | | 194,373 | 177,603 |

The Board of Directors approved these financial statements and authorised for issue on April 4, 2019

Signed on behalf of the Board of Directors



I H Bortecene
Director



S Betteridge
Director

Registered number 2643004

The notes on pages 20 to 71 form an integral part of these financial statements.

Turkish Bank (UK) Limited

Statement of Cash Flows For the year ended 31 December 2018

| | 2018 | 2017 |
|---|---------------|-----------------|
| | £'000 | £'000 |
| Cash flows from operating activities | | |
| (Loss) / Profit after taxation | (125) | 79 |
| Adjustments for:- | | |
| Depreciation of property and equipment | 415 | 375 |
| Amortisation of intangible assets | 223 | 142 |
| Profit from disposal of fixed assets | (3) | - |
| Net interest income | (4,891) | (4,569) |
| Income tax (credit) | (121) | (33) |
| | (4,502) | (4,006) |
| Changes in:- | | |
| Loans and advances to customers | 4,082 | (25,748) |
| Loans and advances to banks | (19) | (68) |
| Other assets | 1,335 | (1,810) |
| Derivative liabilities held for risk management | 28 | 50 |
| Deposits from banks | 15,716 | (666) |
| Deposits from customers | 1,155 | (8,112) |
| Other liabilities | (232) | 128 |
| | 22,065 | (36,226) |
| Interest received | 6,166 | 5,786 |
| Interest paid | (1,275) | (1,217) |
| Income tax received / (paid) | 78 | (140) |
| Net cash flows from operating activities | 22,532 | (35,803) |
| Cash flows from investing activities | | |
| Acquisition of property and equipment | (141) | (372) |
| Acquisition of intangible assets | (150) | (1,000) |
| Proceeds from disposal of fixed assets | 3 | - |
| Acquisition of investment securities | - | (8,902) |
| Proceeds from disposal of investment securities | 546 | 9,029 |
| Net cash used in investing activities | 258 | (1,245) |
| Net increase / (decrease) in cash and cash equivalents | 22,791 | (37,048) |
| Cash and cash equivalents as at 1 January | 63,088 | 100,136 |
| IFRS 9 Adjustment at January 1 2018 | (17) | - |
| Cash and cash equivalents as at 31 December | 85,862 | 63,088 |

The notes on pages 20 to 71 form an integral part of these financial statements.

**Statement of Changes in Equity
For the year ended 31 December 2018**

| | Called up Share capital £'000 | Fair value reserve £'000 | Revaluation reserve £'000 | Retained earnings £'000 | Total £'000 |
|---|--|---|--|--|------------------------|
| Balance as at 1 January 2017 | 12,000 | 325 | 4,746 | 8,119 | 25,190 |
| Impact of prior year adjustment (see note 2) | - | - | 587 | - | 587 |
| Balance as at 1 January 2017 (as restated) | 12,000 | 325 | 5,333 | 8,119 | 25,777 |
| Profit for the year | - | - | - | 79 | 79 |
| Other comprehensive income | - | (60) | - | - | (60) |
| Revaluation of freehold property | - | - | 1,732 | - | 1,732 |
| Net movement in deferred tax on property revaluations | - | - | (245) | - | (245) |
| Balance as at 31 December 2017 Restated | 12,000 | 265 | 6,820 | 8,198 | 27,283 |
| IFRS 9 Adjustments to the 31 December 2017 Balance (see note 16 (v)) | - | 34 | - | (4) | 30 |
| Balance as at 1 January 2018 | 12,000 | 299 | 6,820 | 8,194 | 27,313 |
| Loss for the year | - | - | - | (125) | (125) |
| Other comprehensive income | - | 168 | - | - | 168 |
| Balance as at 31 December 2018 | 12,000 | 467 | 6,820 | 8,069 | 27,356 |

Fair value reserve relates to the gain/loss on the fair valuation of marketable securities which were classified as assets for sale in 2017 and fair value assets through other comprehensive income in 2018. Please see Note 20.

Revaluation reserve relates to the revaluation of freehold land and buildings. Please see Note 22.

The notes on pages 20 to 71 form an integral part of these financial statements.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

1. Reporting Entity

Turkish Bank (UK) Limited (the "Bank") is domiciled in the United Kingdom. The Bank's registered office is 84-86 Borough High Street, London SE1 1LN. The Bank is a regulated Bank, in the retail banking sector.

2. Basis of preparation

a. Basis of preparation

The financial statements have been prepared in accordance with IFRS, as adopted by the EU. They were authorised for issue by the Bank's Board of Directors on April 3, 2019.

These accounts have been prepared on a going concern basis. The Bank invested in becoming a direct member of the BACS and Faster Payments System, and is one of the first niche banks in the UK to achieve this. The Directors consider that this will retain the Bank's competitiveness in its chosen market and are comfortable that the Bank can continue to operate as a going concern. The Bank continues to offer the existing range of services. These financial statements are presented in pounds sterling which is the Bank's functional currency. All amounts have been rounded to the nearest thousand, unless otherwise indicated.

The Bank has undertaken a business wide review on the potential impact of Brexit on its operations. As the Bank does not offer banking services in any other EU or EEA country other than UK, the direct impact is expected to be minimal. Notwithstanding this, the Bank has undertaken comprehensive risk assessments across credit, liquidity and contractual risks in relation the indirect consequences of Brexit, such as house price decline, increased unemployment, a significant depreciation of sterling or other negative economic indicators. Given the conservative approach to lending, the high liquidity and the limited number of customers who have trading relationships with Europe, the impact is expected to be minimal. For example, even when stress testing the lending portfolio to the worst case scenarios, the Bank remains on a sound footing.

b. Prior year adjustment

During the preparation of these financial statements it was identified that indexation allowance was not taken into account in the calculation of the deferred tax liability on the revaluation of freehold land and properties which occurred prior to 1 January 2018. This has been corrected retrospectively and certain comparative figures in the financial statements have been adjusted. The effect of the adjustment is set out below:

| £'000 | Reported | Adjustment | Adjusted |
|-----------------------------------|----------|------------|----------|
| Impact at 1 January 2017 | | | |
| Deferred tax liability | 620 | (587) | 33 |
| Revaluation reserve | 4,746 | 587 | 5,333 |
| Impact at 31 December 2017 | | | |
| Deferred tax liability | 968 | (636) | 332 |
| Revaluation reserve | 6,184 | 636 | 6,820 |

3. Change in accounting policies

The Bank has initially adopted IFRS 9 and IFRS 15 from 1 January 2018. A number of other new standards are also effective from 1 January 2018 but they do not have a material effect on the Bank's financial statements.

Due to the transition method chosen by the Bank in applying IFRS 9, comparative information throughout these financial statements has not been restated to reflect its requirements.

The adoption of IFRS 15 did not impact the timing or amount of fee and commission income from contracts with customers and the related assets and liabilities recognised by the Bank. Accordingly, the impact on the comparative information is limited to new disclosure requirements.

The effect of initially applying these standards is mainly attributed to the following:

- A small increase in impairment losses recognised on financial assets (see Note 16 and 19)
- additional disclosures related to IFRS 9 (see Notes 6, 16 and 19)
- additional disclosures related to IFRS 15 (see Note 9)

Notes to the accounts

For the year ended 31 December 2018

Except for the changes below, the Bank has consistently applied the accounting policies as set out in Note 6 below to all periods presented in these consolidated financial statements.

IFRS 9 Financial Instruments

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard removes the previous IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

For an explanation of how the Bank classifies financial liabilities under IFRS 9, see Note 16.

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments. Under IFRS 9, credit losses are recognised earlier than under IAS 39. For an explanation of how the Bank applies the impairment requirements of IFRS 9, see Note 19.

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively. The Bank used the exemption not to restate comparative periods.

Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.

The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.

- The determination of the business model within which a financial asset is held.
- The designation and revocation of previous designations of certain financial assets and financial liabilities as measured at FVTPL.
- The designation of certain investments in equity instruments not held for trading as FVOCI.

For more information and details on the changes and implications resulting from the adoption of IFRS 9, see Notes 6, 16 and 19.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaced IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations.

The Bank initially applied IFRS 15 on 1 January 2018 retrospectively in accordance with IAS 8 without any practical expedients. The timing or amount of the Bank's fee and commission income from contracts with customers was not impacted by the adoption of IFRS 15. The impact of IFRS 15 was limited to the new disclosure requirements (Note 9).

Notes to the accounts

For the year ended 31 December 2018

4. Use of judgements and estimates

In preparing these financial statements, management has made judgements, estimates and assumptions that effect the application of the Bank's 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 estimates are recognised prospectively. Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ending 31 December 2018 are included in the notes:

Note 6 and Note 16: classification of financial assets: assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are SPPI on the principal amount outstanding.

Note 19: establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining methodology for incorporating forward-looking information into measurement of ECL and selection and approval of models used to measure ECL.

Note 19: impairment of financial instruments: determining inputs into the ECL measurement model, including incorporation of forward-looking information, estimates of probability of default and loss given default.

Note 19: impairment of financial instruments: key assumptions used in estimating recoverable cash flows.

Note 14: recognition of deferred tax assets.

Notes 12 and 19: recognition and measurement of provisions and contingencies; key assumptions about the likelihood and magnitude of an outflow of resources.

Note 6 and 9: recognition and deferral of loan administration commissions based on the expected life of the loans and advances to customers and banks.

5. Measurement of fair values

A number of the Bank's accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities.

The Bank has an established control framework with respect to the measurement of fair values.

Significant valuation issues are reported to the Bank's Audit Committee.

When measuring the fair value of an asset or liability the Bank uses observable market data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly (derived from prices)
- Level 3: inputs for the asset or liability that are not based on observable market data.

If the inputs used to measure the fair value of an asset or liability fall into different levels of the fair value hierarchy then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

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

Notes to the accounts For the year ended 31 December 2018

6. Accounting Policies

a. Revenue recognition

(i) Interest income

Policy applicable from 1 January 2018

Effective interest rate

Interest income and expense are recognised in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

The gross carrying amount of the financial asset; or

The amortised cost of the financial liability.

When calculating the effective interest rate for financial instruments other than purchased or originated credit-impaired assets, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not ECL. For purchased or originated credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including ECL.

The calculation of the effective interest rate includes transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

Amortised cost and gross carrying amount

The 'amortised cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance (or impairment allowance before 1 January 2018).

The 'gross carrying amount of a financial asset' is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

Interest income on financial assets classified as loans and receivables or available for sale is calculated using the standard accruals method which is the same as the effective interest rate method for performing loans. If the Bank were to make provisions on loans it would apply the effective interest method to every such loan individually; i.e. the rate that discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. For the recognition and spreading of loan administration fees please see Note 6 a. (ii)

Calculation of interest income and expense

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortised cost of the liability. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest. However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortised cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

Presentation

Interest income calculated using the effective interest method presented in the statement of profit or loss and OCI includes:

- interest on financial assets and financial liabilities measured at amortised cost;
- interest on debt instruments measured at FVOCI;

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

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

- financial liabilities measured at amortised cost; and

Interest income and expense on other financial assets and financial liabilities at FVTPL are presented in net income from other financial instruments at FVTPL.

Policy applicable before 1 January 2018

Interest income on financial assets classified as loans and receivables or available for sale is calculated using the standard accruals method which is the same as the effective interest rate method for performing loans. If the Bank were to make provisions on loans it would apply the effective interest method to every such loan individually; i.e. the rate that discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

(ii) Rendering of services and commissions

Fees that are an integral part of generating an involvement with a resulting financial instrument together with the related direct costs, are deferred and recognised as part of the effective interest rate.

If a specific lending arrangement is entered into, the administration fee received is deferred based on the expected life of the asset. If the commitment expires without making the loan, the fee is recognised as revenue on expiry. If it is unlikely that a specific lending arrangement will be entered into, the commitment fee is recognised as revenue on a time proportion basis over the commitment period.

Fees earned for banking services provided are recognised as revenue as the services are provided.

Fee and commission income from contracts with customers is measured based on the consideration specified in a contract with a customer. The Bank recognises revenue when it transfers control over a service to a customer.

The Bank provides banking services to retail and corporate customers, including account management, provision of overdraft facilities, foreign currency transactions, and servicing fees. Fees for ongoing account management are charged to the customer's account on a monthly basis. The Bank sets the rates separately for retail and corporate banking customers in each jurisdiction on an annual basis. Transaction-based fees for interchange, foreign currency transactions and overdrafts are charged to the customer's account when the transaction takes place. Servicing fees are charged on a monthly basis and are based on fixed rates reviewed annually by the Bank. Revenue from account service and servicing fees is recognised over time as the services are provided. Revenue related to transactions is recognised at the point in time when the transaction takes place. Fees earned for banking services provided are recognised as revenue as the services are provided.

(iii) Trading income

Trading income relate to foreign exchange commissions earned from customer transactions and are recognised as income at the point transactions are realised.

b. Financial assets and financial liabilities

(i) Recognition and initial measurement

The Bank initially recognises loans and advances, deposits, debt securities issued and subordinated liabilities on the date on which they are originated. All other financial instruments (including regular-way purchases and sales of financial assets) are recognised on the trade date, which is the date on which the Bank becomes a party to the contractual provisions of the instrument.

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

(ii) Classification

Financial assets – Policy applicable from 1 January 2018

On initial recognition, a financial asset is classified as measured at: amortised cost, FVOCI or FVTPL.

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

- The asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI).

Notes to the accounts

For the year ended 31 December 2018

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

- The asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are SPPI.

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

All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Business model assessment

The Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management.

The information considered includes:

- The stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and its strategy for how those risks are managed;
- how managers of the business are compensated (e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected); and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessment of whether contractual cash flows are solely payments of principal and interest (SPPI)

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are SPPI, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse loans); and
- features that modify consideration of the time value of money (e.g. periodical reset of interest rates).

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Non-recourse loans

In some cases, loans made by the Bank that are secured by collateral of the borrower limit the Bank's claim to cash flows of the underlying collateral (non-recourse loans). The Bank applies judgment in assessing whether the non-recourse loans meet the SPPI criterion. The Bank typically considers the following information when making this judgement:

- whether the contractual arrangement specifically defines the amounts and dates of the cash payments of the loan;
- the fair value of the collateral relative to the amount of the secured financial asset;
- the ability and willingness of the borrower to make contractual payments, notwithstanding a decline in the value of collateral;
- whether the borrower is an individual or a substantive operating entity or is a special-purpose entity;
- the Bank's risk of loss on the asset relative to a full-recourse loan;
- the extent to which the collateral represents all or a substantial portion of the borrower's assets; and
- whether the Bank will benefit from any upside from the underlying assets.

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets.

Financial assets – Policy applicable before 1 January 2018

The Bank classified its financial assets into one of the following categories:

- loans and receivables;
- held-to-maturity;
- available-for-sale; and
- at FVTPL, and within this category as:
 - o held-for-trading; or
 - o designated as at FVTPL.

Financial liabilities

The Bank classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortised cost or FVTPL.

(iii) Derecognition

Financial assets

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of the consideration received (including any new asset obtained less any new liability assumed) and any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

From 1 January 2018 any cumulative gain/loss recognised in OCI in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability.

Financial liabilities

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

Notes to the accounts

For the year ended 31 December 2018

(iv) Modifications of financial assets and financial liabilities

Policy applicable from 1 January 2018

Financial assets

If the terms of a financial asset are modified, then the Bank evaluates whether the cash flows of the modified asset are substantially different.

If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised (see (iii)) and a new financial asset is recognised at fair value plus any eligible transaction costs. Any fees received as part of the modification are accounted for as follows:

- fees that are considered in determining the fair value of the new asset and fees that represent reimbursement of eligible transaction costs are included in the initial measurement of the asset; and
- other fees are included in profit or loss as part of the gain or loss on derecognition.

If cash flows are modified when the borrower is in financial difficulties, then the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different terms.

If the modification of a financial asset measured at amortised cost or FVOCI does not result in derecognition of the financial asset, and then the Bank first recalculates the gross carrying amount of the financial asset using the original effective interest rate of the asset and recognises the resulting adjustment as a modification gain or loss in profit or loss. For floating-rate financial assets, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs or fees incurred and fees received as part of the modification adjust the gross carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset.

If such a modification is carried out because of financial difficulties of the borrower, then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income calculated using the effective interest rate method.

Financial liabilities

The Bank derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in profit or loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit or loss. For floating-rate financial liabilities, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

Notes to the accounts

For the year ended 31 December 2018

Policy applicable before 1 January 2018

Financial assets

If the terms of a financial asset were modified, then the Bank evaluated whether the cash flows of the modified asset were substantially different. If the cash flows were substantially different, then the contractual rights to cash flows from the original financial asset were deemed to have expired. In this case, the original financial asset was derecognised (see (iii)) and a new financial asset was recognised at fair value.

If the terms of a financial asset were modified because of financial difficulties of the borrower and the asset was not derecognised, then impairment of the asset was measured using the pre-modification interest rate (see (vii)).

Financial liabilities

The Bank derecognised a financial liability when its terms were modified and the cash flows of the modified liability were substantially different. In this case, a new financial liability based on the modified terms was recognised at fair value. The difference between the carrying amount of the financial liability extinguished and consideration paid was recognised in profit or loss.

Consideration paid included non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability. If the modification of a financial liability was not accounted for as derecognition, then any costs and fees incurred were recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

(v) Offsetting

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

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

(vi) Fair value measurement

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

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

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

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

The fair value of a financial liability with a demand feature (e.g. a demand deposit) is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

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

Notes to the accounts

For the year ended 31 December 2018

(vii) Impairment of financial assets

Policy applicable from 1 January 2018

The Bank recognises loss allowances for ECL on the following financial instruments that are not measured at FVTPL:

- financial assets that are debt instruments;
- lease receivables;
- financial guarantee contracts issued; and
- loan commitments issued.

No impairment loss is recognised on equity investments.

The Bank measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments (other than lease receivables) on which credit risk has not increased significantly since their initial recognition

The Bank considers a debt investment security to have low credit risk when its credit risk rating is equivalent to the globally understood definition of 'investment grade'. The Bank does not apply the low credit risk exemption to any other financial instruments.

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Financial instruments for which a 12-month ECL is recognised are referred to as 'Stage 1 financial instruments'.

Life-time ECL are the ECL that result from all possible default events over the expected life of the financial instrument. Financial instruments for which a lifetime ECL is recognised but which are not credit-impaired are referred to as 'Stage 2 financial instruments'.

Measurement of ECL

ECL is a probability-weighted estimate of credit losses. They are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive);
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn loan commitments: as the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI, and finance lease receivables are credit-impaired (referred to as 'Stage 3 financial assets'). A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

Notes to the accounts

For the year ended 31 December 2018

A loan that has been renegotiated due to a deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment. In addition, a retail loan that is overdue for 90 days or more is considered credit-impaired even when the regulatory definition of default is different.

In making an assessment of whether an investment in sovereign debt is credit-impaired, the Bank considers the following factors.

- The market's assessment of creditworthiness as reflected in the bond yields.
- The rating agencies' assessments of creditworthiness.
- The country's ability to access the capital markets for new debt issuance.
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.
- The international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision;
- where a financial instrument includes both a drawn and an undrawn component, and the Bank cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Bank presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

Recoveries of amounts previously written off are included in 'impairment losses on financial instruments' in the statement of profit or loss and OCI.

Financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank's procedures for recovery of amounts due.

Policy applicable before 1 January 2018

If there is objective evidence that an impairment loss on financial assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through use of an allowance account. The amount of the loss is recognised in the profit or loss account. Each impaired asset is assessed on its merits and the work out strategy and estimate of cash flows considered recoverable are independently approved by the Credit Committee. Impairment losses on available for sale securities are recognised through profit and loss.

A collective component of the total allowance is established for:-

- groups of homogeneous loans that are not considered individually significant; and
- groups of assets that are individually significant but that were not found to be individually impaired (Loss Incurred But Not Reported).

Notes to the accounts

For the year ended 31 December 2018

The collective allowance for groups of homogeneous loans is established using statistical methods or for small portfolios a formula approach based on historical loss experience. Management applies judgement to ensure that the estimate of loss arrived at on the basis of historical information is appropriately adjusted to reflect the economic conditions and product mix at the reporting date. Loss rates are bench marked against actual loss experience.

The IBNR allowance covers credit losses inherent in portfolios of loans and advances, when there is objective evidence to suggest that they contain impaired items but the individual impaired items cannot yet be identified.

In assessing the need for collective impairment management considers factors such as credit quality, portfolio size, concentrations and economic factors. To estimate the required allowance, assumptions are made to define how inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the allowance depends on the assumptions and parameters used in determining the collective allowance.

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

The Bank writes off a loan or an investment debt security, either partially or in full, and any related allowance for impairment losses, when Bank Credit determines that there is no realistic prospect of recovery.

(viii) Designation at fair value through profit or loss

Financial assets

At initial recognition, the Bank has designated certain financial assets as at FVTPL because this designation eliminates or significantly reduces an accounting mismatch, which would otherwise arise.

Before 1 January 2018, the Bank also designated certain financial assets as at FVTPL because the assets were managed, evaluated and reported internally on a fair value basis.

Financial liabilities

The Bank has designated certain financial liabilities as at FVTPL in either of the following circumstances:

- the liabilities are managed, evaluated and reported internally on a fair value basis; or
- the designation eliminates or significantly reduces an accounting mismatch that would otherwise arise.

c. Loans and advances

Policy applicable from 1 January 2018

'Loans and advances' captions in the statement of financial position include:

- loans and advances measured at amortised cost; they are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;

Policy applicable before 1 January 2018

Loans and receivables are measured at initial recognition at fair value based on transaction costs and are subsequently measured at amortised cost using the effective interest rate method. Appropriate allowances for estimated irrecoverable amounts are recognised in the profit and loss account.

The effective interest rate method is a method of calculating the amortised cost of a financial asset and of allocating interest income over a relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts thought the expected life of the financial asset, or, where appropriate, a shorter period.

Notes to the accounts

For the year ended 31 December 2018

d. Investment securities

Policy applicable from 1 January 2018

The 'investment securities' caption in the statement of financial position includes:

- debt investment securities measured at amortised cost; these are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;
- debt securities measured at FVOCI; and
- equity investment securities designated as at FVOCI.

For debt securities measured at FVOCI, gains and losses are recognised in OCI, except for the following, which are recognised in profit or loss in the same manner as for financial assets measured at amortised cost:

- interest revenue using the effective interest method;
- ECL and reversals; and
- foreign exchange gains and losses.

When debt security measured at FVOCI is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss.

The Bank elects to present in OCI changes in the fair value of certain investments in equity instruments that are not held for trading. The election is made on an instrument-by-instrument basis on initial recognition and is irrevocable. Gains and losses on such equity instruments are never reclassified to profit or loss and no impairment is recognised in profit or loss.

Dividends are recognised in profit or loss unless they clearly represent a recovery of part of the cost of the investment, in which case they are recognised in OCI. Cumulative gains and losses recognised in OCI are transferred to retained earnings on disposal of an investment.

Policy applicable before 1 January 2018

Investments in debt securities are classified as available-for-sale or held-to-maturity. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Available-for-sale investments are measured at subsequent reporting dates at fair value. For available-for-sale investments, gains and losses arising from changes in fair value are recognised directly in equity until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the profit or loss for the period. Foreign exchange gains and losses, interest recognised under the effective interest rate method and impairment losses are taken to the profit and loss account. Impairment losses recognised in profit or loss for debt instruments classified as available-for-sale are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition of the impairment loss.

Investments with fixed or determinable payments and fixed maturity dates that the Bank has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are measured at amortised cost using the effective interest method less any impairment, with revenue recognised on an effective yield basis.

e. Credit Risk

For the definition of credit risk and information on how credit risk is managed by the Bank see Note 34.

f. Pension schemes

Contributions to a defined contribution scheme are charged to profit or loss so as to reflect the amounts payable to the pension schemes in respect of the accounting period.

g. Foreign currency translation

Transactions in foreign currencies are recorded at the rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the mid-day rates of exchange ruling at the reporting date. All differences arising are taken to profit or loss.

Notes to the accounts

For the year ended 31 December 2018

h. Derivatives

Derivative contracts consist of foreign currency swap contracts, which are outstanding at the reporting date. Derivatives are measured at fair value, with changes in the fair value recognised in the profit and loss account. The Bank does not use derivative financial instruments for speculative or trading purposes. The Bank has not designated any of the derivative contracts in hedging relationships for hedge accounting purposes.

The Bank's investment securities are stated at fair market value. The best evidence of fair value is a quoted price in an actively traded market. If the market for a financial instrument is not active, or the financial instruments are traded infrequently and have little price transparency or the fair value is less objective, and requires varying degrees of judgment, the Bank uses valuation techniques to arrive at the fair value as set out in Note 5 above.

The valuation techniques employ observable market data to calculate fair values, including comparisons with similar financial instruments for which market observable prices exist. When valuing instruments by reference to comparable instruments, management takes into account the maturity, structure and rating of the instrument with which the position held is being compared.

i. Depreciation

Depreciation is provided on all property and equipment, except freehold land, at rates calculated to write off the cost, less estimated residual value, of each asset evenly over its expected useful life, as follows:

| | |
|------------------------------------|---------------------|
| Freehold buildings | Over 50 years |
| Short leasehold land and buildings | Over the lease term |
| Fixtures, fittings and equipment | 5% to 20% |
| Assets under finance lease | 20% |
| Motor vehicle | 20% |

j. Current and deferred taxation

Current tax including UK corporation tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the reporting.

Deferred taxation is provided in full on timing differences that result in an obligation at the reporting date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included within the financial statements. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

k. Leasing and hire purchase commitments

Assets held under finance leases, which are leases where substantially all the risks and rewards of ownership of the asset have passed to the Bank, and hire purchase contracts are capitalised in the balance sheet and are depreciated over the shorter of the lease term and their useful lives. The capital elements of future obligations under the leases and hire purchase contracts are included as liabilities in the balance sheet, while the interest elements are charged to profit or loss over the period of the lease to produce a constant rate of charge on the balance of capital repayments outstanding. Rentals under operating leases are charged to profit or loss account on a straight-line basis over the term of the lease.

l. Intangible assets – Software licences and software purchased

Software licences are included at cost and amortised in equal annual instalments over a period of five years which is their estimated useful economic life. These software licences amortizations coincide with hardware depreciation over a period of five years. Provision is made for any impairment loss. Costs relating to the core banking system, and external costs relating to self-developed software are amortised over ten years.

Notes to the accounts

For the year ended 31 December 2018

m. Property revaluations

The accounting policy for freehold land and buildings is to revalue to market value. Revaluations are performed with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the reporting date. The last professional valuation was undertaken by London's Surveyors & Valuers Ltd, a chartered surveyor external to the Bank, in December 2017 which resulted in a net surplus of £1,732,000. Valuations were made on the basis of open market value for existing use. The directors are satisfied that the aggregate fair value of those assets at the time in question is not less than the aggregate amount at which they are or being stated in the Bank's account.

n. Financial guarantees and loan commitments

'Financial guarantees' are contracts that require the Bank to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. 'Loan commitments' are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan at a below-market interest rate are initially measured at fair value. Subsequently, they are measured as follows:

- from 1 January 2018: at the higher of the loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15; and
- before 1 January 2018: at the higher of the amount representing the initial fair value amortised over the life of the guarantee or the commitment and the present value of any expected payment to settle the liability when a payment under the contract has become probable.

The Bank has issued no loan commitments that are measured at FVTPL. For other loan commitments:

- from 1 January 2018: the Bank recognises a loss allowance;
- before 1 January 2018: the Bank recognised a provision in accordance with IAS 37 if the contract was considered to be onerous.

o. Segment analysis

The Bank has produced segmental analysis based on geographical sectors and reportable business sectors as described in Note 7.

p. Cash and cash equivalents

Cash and cash equivalents' include notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of three months or less from the date of acquisition that are subject to an insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

q. Standards Issued but not yet adopted

A number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2018 and earlier application is permitted; however, the Bank has not early adopted them in preparing these consolidated financial statements.

(i) IFRS 16 Leases

The Bank is required to adopt IFRS 16 Leases from 1 January 2019. The Bank has assessed the estimated impact that the initial application of IFRS 16 will have on its financial statements, as described below. The actual impact of adopting the standard on 1 January 2019 may change because:

- the Bank has not finalised the testing and assessment of controls over its new IT systems; and
- the new accounting policies are subject to change until the Bank presents its first financial statements that include the date of initial application.

Notes to the accounts

For the year ended 31 December 2018

IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases.

IFRS 16 replaces existing leases guidance, including IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease.

Leases in which the Bank is a lessee

Adoption of the standard is not expected to have a significant impact however, this assessment made by the Bank is preliminary as not all transition work requirements have been finalised and therefore may be subject to adjustment. The actual impact of applying IFRS 16 on the financial statements in the period of initial application will depend on future economic conditions, the development of the Bank's lease portfolio, the Bank's assessment of whether it will exercise any lease renewal options and the extent to which the Bank chooses to use practical expedients and recognition exemptions.

The Bank will recognise new assets and liabilities for its operating leases of branch and office premises. The nature of expenses related to these leases will now change because IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities.

Previously, the Bank recognised operating lease expense on a straight-line basis over the term of the lease, and recognised assets and liabilities only to the extent that there was a timing difference between actual lease payments and the expense recognised.

As at 31 December 2018, the Bank's future minimum lease payments under non-cancellable operating leases amounted to €221 thousand, on an undiscounted basis, which the Bank estimates it will recognise as additional lease liabilities.

No significant impact is expected for the Bank's finance leases.

Transition

The Bank plans to apply IFRS 16 initially on 1 January 2019, using a modified retrospective approach. Therefore, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2019, with no restatement of comparative information.

The Bank plans to apply the practical expedient to grandfather the definition of a lease on transition. This means that it will apply IFRS 16 to all contracts entered into before 1 January 2019 and identified as leases in accordance with IAS 17 and IFRIC 4.

(ii) Other standards

The following amended standards are not expected to have a significant impact on the Bank's financial statements.

Annual Improvements to IFRS Standards 2015–2017 Cycle – various standards

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

Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)

IFRIC 23 Uncertainty over Income Tax Treatments

Amendments to References to Conceptual Framework in IFRS Standards

IFRS 17 Insurance Contracts.

**Notes to the accounts
For the year ended 31 December 2018**

7. Segmental analysis

The Bank's profit and loss and balance sheet is analysed by business sector below:

| | Retail banking £'000 | Treasury £'000 | Central £'000 | Total £'000 |
|---|-------------------------------------|---------------------------|--------------------------|------------------------|
| 2018 | | | | |
| Net interest income | 3,575 | 1,067 | 249 | 4,891 |
| Net fee and commission income | 832 | 97 | 63 | 992 |
| Net trading income | - | 156 | - | 156 |
| Other operating income | 1 | - | 3 | 4 |
| Total segment revenues | 4,408 | 1,320 | 315 | 6,043 |
| Impairment losses | (18) | - | - | (18) |
| Operating expenses | (2,314) | (230) | (3,727) | (6,271) |
| Segment profit (loss) before tax | 2,076 | 1,090 | (3,412) | (246) |
| Segment assets | 92,688 | 90,507 | 11,178 | 194,373 |
| Segment liabilities | 146,552 | 19,327 | 1,138 | 167,017 |
| 2017 (Restated) | | | | |
| Net interest income | 4,321 | (13) | 261 | 4,569 |
| Net fee and commission income | 1,042 | 129 | (72) | 1,099 |
| Net trading income | - | 184 | - | 184 |
| Other operating income | (2) | 3 | - | 1 |
| Total segment revenues | 5,361 | 303 | 189 | 5,853 |
| Impairment losses | (9) | - | - | (9) |
| Operating expenses | (1,915) | (685) | (3,198) | (5,798) |
| Segment profit (loss) before tax | 3,437 | (382) | (3,009) | 46 |
| Segment assets | 99,684 | 68,864 | 9,055 | 177,603 |
| Segment liabilities | 145,916 | 3,756 | 648 | 150,320 |

In the classifications above, Retail Banking is defined as the Bank's customer based business, Treasury is the money market, foreign exchange and financial instrument business, and Central is the remaining revenue and overheads relating to the shareholders equity and central operating costs.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Sector analysis continued

The Bank's profit and loss account can be analysed by geographic region as follows:

Geographic analysis

| | UK £'000 | Rest of Europe £'000 | Total £'000 |
|---|----------------|----------------------------|----------------|
| 2018 | | | |
| Net interest income | 2,496 | 2,395 | 4,891 |
| Net fee and commission income | 540 | 452 | 992 |
| Net trading income | 156 | - | 156 |
| Other operating income | 3 | 1 | 4 |
| Total segment revenues | 3,195 | 2,848 | 6,043 |
| Impairment losses | (18) | - | (18) |
| Operating expenses | (5,912) | (359) | (6,271) |
| Segment profit (loss) before tax | (2,735) | 2,489 | (246) |
| Segment assets | 119,606 | 74,767 | 194,373 |
| Segment liabilities | 52,876 | 114,141 | 167,017 |
| 2017 (Restated) | | | |
| Net interest income | 2,532 | 2,037 | 4,569 |
| Net fee and commission income | 634 | 465 | 1,099 |
| Net trading income | 184 | - | 184 |
| Other operating income | 1 | - | 1 |
| Total segment revenues | 3,351 | 2,502 | 5,853 |
| Impairment losses | (9) | - | (9) |
| Operating expenses | (5,455) | (343) | (5,798) |
| Segment profit (loss) before tax | (2,113) | 2,159 | 46 |
| Segment assets | 96,019 | 81,584 | 177,603 |
| Segment liabilities | 57,898 | 92,422 | 150,320 |

Europe excluding UK is mainly Turkey and the Turkish Republic of Northern Cyprus.

Turkish Bank (UK) Limited

Notes to the accounts For the year ended 31 December 2018

8. Net interest income

| | 2018 £'000 | 2017 £'000 |
|---------------------------------|----------------|----------------|
| Interest income | | |
| Cash and cash equivalents | 1,036 | 452 |
| Loans and advances to banks | 17 | 18 |
| Loans and advances to customers | 4,983 | 4,947 |
| Debt Securities | 130 | 369 |
| Total interest income | 6,166 | 5,786 |
| Interest expense | | |
| Deposits from banks | (12) | (2) |
| Deposits from customers | (1,263) | (1,215) |
| Total interest expense | (1,275) | (1,217) |
| Net interest income | 4,891 | 4,569 |

9. Net fee and commission income

| | 2018 £'000 | 2017 £'000 |
|--|---------------|---------------|
| Major Service Lines | | |
| Remittances | 347 | 459 |
| Account charges | 375 | 429 |
| Commission on Loans and Advances | 433 | 411 |
| Total fee and commission income from contracts with customers | 1,155 | 1,299 |
| Fee and commission expense | (163) | (200) |
| Net fee and commission income | 992 | 1,099 |

Net fee and commission income was all derived from retail banking customer fees for both 2018 and 2017.

10. Net trading income

Net trading income was all from foreign exchange trading for both 2018 and 2017

Turkish Bank (UK) Limited

Notes to the accounts For the year ended 31 December 2018

11. Personnel expenses

| | 2018 £'000 | 2017 £'000 |
|---|---------------|---------------|
| Personnel expenses during the year (including directors) | | |
| Wages and salaries | 2,167 | 2,268 |
| Social security costs | 231 | 255 |
| Pension costs | 97 | 85 |
| Other staff costs | 227 | 220 |
| | <u>2,722</u> | <u>2,828</u> |

The average monthly number of employees during the year was made up as follows:

| | 2018 No. | 2017 No. |
|-------------------------------|-------------|-------------|
| Commercial banking activities | <u>82</u> | <u>82</u> |

Directors' remuneration during the year consisted of:

| | 2018 £'000 | 2017 £'000 |
|------------|---------------|---------------|
| Emoluments | <u>294</u> | <u>266</u> |

The emoluments of the highest paid director were £111,000 (2017: £112,000).

The Bank operates a stakeholder pension arrangement, whereby the staff contribute, and the Bank makes a contribution with reference to current National Insurance rates.

12. Impairment losses on cash equivalents, loans and advances

| | 2018 £'000 | 2017 £'000 |
|--------------------------------|---------------|---------------|
| Impairment charge for the year | (18) | (16) |
| Recoveries | - | 7 |
| Net impairment charge | <u>(18)</u> | <u>(9)</u> |

13. Profit on ordinary activities before taxation

| | 2018 £'000 | 2017 £'000 |
|-------------------------------------|---------------|---------------|
| Profit is stated after charging: | | |
| Foreign currency gains | (151) | (184) |
| Operating lease rentals | | |
| Land and buildings | 214 | 203 |
| Depreciation and amortisation | | |
| Property and equipment | 414 | 375 |
| Intangible fixed assets | 223 | 142 |
| Fees payable to the Bank's auditor | | |
| Audit of the Bank's annual accounts | 110 | 112 |
| | <u>810</u> | <u>648</u> |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

14. Income taxes

| | 2018 £'000 | 2017 £'000 |
|---|---------------|---------------|
| Tax paid in respect of current year | - | 80 |
| Tax recoverable in respect of prior years | 206 | 79 |
| United Kingdom corporation tax at 19.00% (2017: 19.25%) based on taxable profit | - | (8) |
| Current taxation asset | 206 | 151 |
| United Kingdom corporation tax at 19.00% (2017: 19.25%) based on taxable profit | - | (8) |
| Adjustment in respect of prior years | 134 | 87 |
| Total current tax | 134 | 79 |
| Deferred tax | | |
| Current year movement | (13) | (54) |
| Prior year adjustment | - | 8 |
| Current year tax credit | 121 | 33 |

Deferred tax has been calculated at 17% as this is the enacted rate for the period when the timing difference is expected to reverse.

The current tax charge for the year can be reconciled to the standard rate of corporation tax at 19.00% (2017: 19.25%) as explained below:

| | 2018 £'000 | 2017 £'000 |
|--|---------------|---------------|
| (Loss)/ Profit on ordinary activities before tax | (246) | 46 |
| Tax at 19.00% (2017: 19.25%) thereon | 47 | (9) |
| Expenses not deductible for tax purposes | (5) | (3) |
| Depreciation lower/(in excess) of capital allowances | (42) | 9 |
| Prior period adjustment | 134 | 87 |
| Reversal of timing differences | - | (5) |
| Total current tax | 134 | 79 |
| Deferred tax: | | |
| Current year movement | (13) | (54) |
| Prior period adjustment | - | 8 |
| Income tax credit for the year | 121 | 33 |

15. Cash and cash equivalents

| | 2018 £'000 | 2017 £'000 |
|---|---------------|---------------|
| Cash and cash equivalents are comprised of the following: | | |
| Cash | 768 | 775 |
| Deposits at the Bank of England | 54,981 | 21,682 |
| On demand | 17,320 | 4,210 |
| Within three months | 12,814 | 36,421 |
| Loss allowance (Under IFRS9) | (21) | N/A |
| | 85,862 | 63,088 |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Included within cash and cash equivalents is an amount of £2,745,987 in respect of Group companies (2017: £5,064,000). The interest received from Group companies during the year was £37,359 (2017: £27,079).

Geographical analysis of cash and cash equivalents is as follows:

| | 2018 £'000 | 2017 £'000 |
|--|---------------|---------------|
| UK | | |
| - Cash | 768 | 775 |
| - Deposits with Bank of England | 54,981 | 21,682 |
| - On current account | 2,859 | 2,599 |
| - On deposit account in money market lending | 2,917 | 886 |
| Outside UK: | | |
| - On current account | 14,461 | 1,611 |
| - Money Market Lending | 9,876 | 35,535 |
| | 85,862 | 63,088 |

By Credit Rating

| | | |
|--------------|---------------|---------------|
| Cash | 768 | 775 |
| AA- to AA+ | 72,294 | 25,890 |
| A- to A+ | 880 | 883 |
| BB | - | 30,477 |
| B | 9,175 | - |
| Not rated | 2,745 | 5,063 |
| Total | 85,862 | 63,088 |

16. Financial assets and financial liabilities

See accounting policies in Note 6.

(i) The following table provides reconciliation between line items in the statement of financial position and categories of financial instruments.

31 December 2018 £'000

| Financial Assets | Note | Mandatorily at FVTPL | Designated as at FVTPL | FVOCI- debt instruments | FVOCI- equity instruments | Amortised Cost | Total carrying amount |
|---------------------------------|------|-------------------------|------------------------------|-------------------------------|---------------------------------|-------------------|-----------------------------|
| Cash and cash equivalents | 15 | - | - | - | - | 85,862 | 85,862 |
| Loans and advances to banks | 17 | - | - | - | - | 1,773 | 1,773 |
| Loans and advances to customers | 18 | - | - | - | - | 94,480 | 94,480 |
| Investment securities – debt | 20 | - | - | - | - | - | - |
| Investment securities – equity | 20 | - | - | - | 498 | - | 498 |
| Total financial assets | | - | - | - | 498 | 182,115 | 182,613 |

| Financial Liabilities | Note | | | | | | |
|------------------------------------|------|----|---|---|---|---------|---------|
| Deposits from banks | 24 | - | - | - | - | 18,854 | 18,854 |
| Deposits from customers | 25 | - | - | - | - | 146,164 | 146,164 |
| Derivative Liabilities | 30 | 78 | - | - | - | - | 78 |
| Total financial liabilities | | 78 | - | - | - | 165,018 | 165,096 |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

31 December 2017 £'000

| Financial Assets | Note | Trading | Designated as at FVTPL | Held-to- maturity | Available- for-sale | Loans and receivables | Other Amortised Cost | Total carrying amount |
|---------------------------------|------|---------|------------------------------|----------------------|------------------------|--------------------------|----------------------------|-----------------------------|
| Cash and cash equivalents | 15 | - | - | - | - | 63,088 | - | 63,088 |
| Loans and advances to banks | 17 | - | - | - | - | 1,772 | - | 1,772 |
| Loans and advances to customers | 18 | - | - | - | - | 98,532 | - | 98,532 |
| Investment securities – debt | 20 | - | - | - | 512 | - | - | 512 |
| Investment securities –equity | 20 | - | - | - | 300 | - | - | 300 |
| Total financial assets | | - | - | - | 812 | 163,392 | - | 164,204 |

| Financial Liabilities | Note | | | | | | | |
|------------------------------------|------|---|----|---|---|---|---------|---------|
| Deposits from banks | 24 | - | - | - | - | - | 3,138 | 3,138 |
| Deposits from customers | 25 | - | - | - | - | - | 145,009 | 145,009 |
| Derivative Liabilities | 30 | - | 50 | - | - | - | - | 50 |
| Total financial liabilities | | - | 50 | - | - | - | 148,147 | 148,197 |

(ii) The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Bank's financial assets and financial liabilities as at 1 January 2018.

| Financial Assets | Note | Original classification under IAS 39 | New classification under IFRS 9 | Original carrying amount under IAS 39 | New carrying amount under IFRS 9 |
|---------------------------------|------|---|---------------------------------------|---|--|
| Cash and cash equivalents | 15 | Loans and receivables | Amortised cost | 63,088 | 63,071 |
| Loans and advances to banks | 17 | Loans and receivables | Amortised cost | 1,772 | 1,754 |
| Loans and advances to customers | 18 | Loans and receivables | Amortised cost | 98,532 | 98,561 |
| Investment securities – debt | 20 | Available-for-sale | Amortised cost | 512 | 546 |
| Investment securities –equity | 20 | Available-for-sale | FVOCI | 300 | 300 |
| Total financial assets | | | | 164,204 | 164,232 |

| Financial Liabilities | Note | Original classification under IAS 39 | New classification under IFRS 9 | Original carrying amount under IAS 39 | New carrying amount under IFRS 9 |
|------------------------------------|------|---|---------------------------------------|---|--|
| Deposits from banks | 24 | Amortised cost | Amortised cost | 3,138 | 3,138 |
| Deposits from customers | 25 | Amortised cost | Amortised cost | 145,009 | 145,009 |
| Derivative Liabilities | 30 | FVTPL | FVTPL | 50 | 50 |
| Total financial liabilities | | | | 148,197 | 148,197 |

Certain debt securities are held by the Bank Central Treasury in a separate portfolio for long-term yield. These securities may be sold, but such sales are not expected to be more than infrequent. The Bank considers that these securities are held within a business model whose objective is to hold assets to collect the contractual cash flows. These assets are classified as measured at amortised cost under IFRS 9.

Certain equity investments held by the Bank for strategic purposes have been designated under IFRS 9 as at FVOCI. Before the adoption of IFRS 9, these securities were measured at cost because their fair value was not considered to be reliably measureable. IFRS 9 has removed this cost exception.

Notes to the accounts
For the year ended 31 December 2018

(iii) The following table reconciles the carrying amounts under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on 1 January 2018.

| | IAS 39 carrying amount 31 December 2017 | Reclassification | Remeasurement IFRS 9 carrying amount | IFRS 9 carrying amount 1 January 2018 |
|----------------------------------|---|------------------|--|---|
| Financial assets | | | | |
| Amortised cost | | | | |
| Cash and cash equivalents: | | | | |
| Opening balance | 63,088 | - | - | 63,088 |
| Remeasurement | - | - | (17) | (17) |
| Closing balance | 63,088 | - | (17) | 63,071 |
| Loans and advances to banks: | | | | |
| Opening balance | 1,772 | - | - | 1,772 |
| Remeasurement | - | - | (18) | (18) |
| Closing balance | 1,772 | - | (18) | 1,754 |
| Loans and advances to customers: | | | | |
| Opening balance | 98,532 | - | - | 98,532 |
| Remeasurement | - | - | 29 | 29 |
| Closing balance | 98,532 | - | 29 | 98,561 |
| Investment securities: | | | | |
| Opening balance | - | - | - | - |
| From available-for-sale | - | 512 | - | 512 |
| Remeasurement | - | - | 34 | 34 |
| Closing balance | - | 512 | 34 | 546 |
| Other assets | - | | | |
| Total amortised cost | 163,392 | 512 | 28 | 163,932 |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

| | IAS 39 carrying amount 31 December 2017 | Reclassification | Remeasurement IFRS 9 carrying amount | IFRS 9 carrying amount 1 January 2018 |
|---------------------------|---|------------------|--|---|
| Available-for-sale | | | | |
| Investment securities: | | | | |
| Opening balance | 812 | - | - | 812 |
| To FVOCI – equity | - | (300) | - | (300) |
| To FVOCI – debt | - | - | - | - |
| To FVTPL | - | - | - | - |
| To amortised cost | - | (512) | - | (512) |
| Closing balance | 812 | (812) | - | - |
| FVOCI – debt | | | | |
| Investment securities: | - | - | - | - |
| Opening balance | - | - | - | - |
| From available-for-sale | - | - | - | - |
| Closing balance | - | - | - | - |
| FVOCI – equity | | | | |
| Investment securities: | | | | |
| Opening balance | - | - | - | - |
| From available-for-sale | 300 | - | - | 300 |
| Closing balance | 300 | - | - | 300 |
| Total FVOCI | 300 | - | - | 300 |

(iv) The following table shows the effects of the reclassification of financial assets and financial liabilities from IAS 39 categories into the amortised cost category under IFRS 9.

| | 2018 |
|---|------|
| From available-for-sale financial assets under IAS 39 | |
| Fair value at 31 December 2018 | |
| Fair value loss that would have been recognised during the year ended | |
| 31 December 2018 in OCI if the financial assets had not been reclassified | 34 |

Turkish Bank (UK) Limited

Notes to the accounts For the year ended 31 December 2018

(v) The following table summarises the impact of transition to IFRS 9 on the opening balance of retained earnings

| | 2018 |
|--|-------|
| Liability credit reserve | |
| Closing balance under IAS 39 (31 December 2017) | - |
| Change of credit risk for financial liabilities designated as at FVTPL | - |
| Related tax | - |
| Opening balance under IFRS 9 (1 January 2018) | - |
| Fair value reserve | |
| Closing balance under IAS 39 (31 December 2017) | 265 |
| Reclassification of investment securities (debt) from available-for-sale to amortised cost | 34 |
| Reclassification of investment securities (debt and equity) from available-for-sale to FVTPL | - |
| Reclassification of investment securities (equity) measured at cost from available-for sale to FVOCI | - |
| Recognition of expected credit losses under IFRS 9 for debt financial assets at FVOCI | - |
| Related tax | - |
| Opening balance under IFRS 9 (1 January 2018) | 299 |
| Retained earnings | |
| Closing balance under IAS 39 (31 December 2017) | 8,198 |
| Reclassifications under IFRS 9 (net of tax) | - |
| Recognition of expected credit losses under IFRS 9 (including lease receivables, loan commitments and financial guarantee contracts) | (5) |
| Related tax | 1 |
| Opening balance under IFRS 9 (1 January 2018) | 8,194 |

(vi) The following table reconciles the closing impairment allowance for financial assets under IAS 39 and provisions for loan commitments and financial guarantee contracts under IAS 37 Provisions, Contingent Liabilities and Contingent Assets as at 31 December 2017; to the opening ECL allowance determined under IFRS 9 as at 1 January 2018.

| | 31 December 2017 (IAS 39/IAS 37) | Reclassification | Remeasurement | 1 January 2018 (IFRS 9) |
|--|--|------------------|---------------|-------------------------------|
| Loans and receivables and held-to-maturity securities under IAS 39/financial assets at amortised cost under IFRS 9 (includes cash and cash equivalents, loans and advances to banks and loans and advances to customers) | 135 | - | (10) | 125 |
| Loan commitments and financial guarantee contracts issued | - | - | 15 | 15 |
| Total | 135 | - | 5 | 140 |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

17. Loans and advances to banks

| | 2018 £'000 | 2017 £'000 |
|---|---------------|---------------|
| Loan to a Turkish bank original maturity less than 1 year | 1,795 | 1,772 |
| Loss allowance | (22) | - |
| | <u>1,773</u> | <u>1,772</u> |

18. Loans and advances to customers

| | 2018 £'000 | 2017 £'000 |
|-----------------------------------|---------------|---------------|
| Loans are repayable as follows: | | |
| On demand | 5,468 | 5,023 |
| Within three months | 2,932 | 1,925 |
| Between three months and one year | 8,729 | 7,745 |
| Between one and five years | 56,119 | 63,083 |
| Five years or more | 21,346 | 20,891 |
| ECL Allowance | | |
| Specific | (35) | (35) |
| Collective | (79) | (100) |
| | <u>94,480</u> | <u>98,532</u> |

Loans and advances are classified as non-performing if repayments are not made within 30 days of the due date. Non-performing loans and advances totalled £4,362,093 at the year-end (2017: £2,739,002).

Loans and advances to customers includes £ 4,316,602 (2017: £ 2,703,288) which has been in the watch list but no provision was made against them. The following information is given in respect of the nature and type of loans and advances to customers:

2018

| | Fixed Rate Loan £'000 | | Floating Rate Loan £'000 | | Total £'000 |
|---------------|--------------------------|--------------|-----------------------------|------------|----------------|
| | Secured | Unsecured | Secured | Unsecured | |
| Overdraft | - | - | 5,275 | 146 | 5,421 |
| Fixed term | | | | | |
| - Retail | 3,265 | - | 71,608 | 107 | 74,980 |
| - Corporation | 900 | 3,185 | 10,104 | 4 | 14,193 |
| | <u>4,165</u> | <u>3,185</u> | <u>86,987</u> | <u>257</u> | <u>94,594</u> |
| ECL Allowance | - | (30) | - | (84) | (114) |
| | <u>4,165</u> | <u>3,155</u> | <u>86,987</u> | <u>173</u> | <u>94,480</u> |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

| | Fixed Rate Loan | | 2017 Floating Rate Loan | | Total |
|---------------|-----------------|-----------|----------------------------|-----------|--------|
| | £'000 | | £'000 | | £'000 |
| | Secured | Unsecured | Secured | Unsecured | |
| Overdraft | - | - | 4,788 | 235 | 5,023 |
| Fixed term | | | | | |
| - Retail | 1,944 | - | 76,514 | 978 | 79,436 |
| - Corporation | 272 | 2,962 | 10,974 | - | 14,208 |
| | 2,216 | 2,962 | 92,276 | 1,213 | 98,667 |
| ECL Allowance | - | (15) | - | (120) | (135) |
| | 2,216 | 2,130 | 92,276 | 1,093 | 98,532 |

The following information is given in respect of origin and currency of loans and advances.

| | 2018 £'000 | | | | 2017 £'000 | | | |
|----------|---------------|-------|------|--------|---------------|-------|------|--------|
| | GBP | USD | EURO | Total | GBP | USD | EURO | Total |
| UK | 52,231 | - | - | 52,231 | 51,529 | - | - | 51,529 |
| Non UK | | | | | | | | |
| - Turkey | 36,320 | 4,630 | - | 40,950 | 39,443 | 4,284 | 909 | 44,636 |
| - Others | 1,299 | - | - | 1,299 | 2,367 | - | - | 2,367 |
| Total | 89,850 | 4,630 | - | 94,480 | 93,343 | 4,284 | 909 | 98,532 |

19. Provisions for impairment losses

The following table shows reconciliations from the opening to the closing balance of the loss allowance. Comparative amounts for 2017 represent the allowance account for credit losses and reflect the measurement basis under IAS 39.

| Loss allowance | 2018 | | | | 2017 | | |
|--------------------------------------|---------|---------|---------|-------|------------|------------|-------|
| | Stage 1 | Stage 2 | Stage 3 | Total | Individual | Collective | Total |
| Balance at 1 January | 100 | - | 35 | 135 | 26 | 100 | 126 |
| Net re-measurement of loss allowance | 5 | - | - | 5 | - | - | - |
| Increase in loss allowance | 8 | - | 10 | 18 | 9 | - | 9 |
| Balance at 31 December | 112 | - | 45 | 158 | 35 | 100 | 135 |

In 2017, In accordance with IAS39 an Incurred but not Reported ("IBNR") provision has been made in order to reflect losses incurred but not yet identified. The provision as at 31 December 2017 was £100,000.

Inputs, assumptions and techniques used for estimating impairment

See accounting policy in Note 6

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables;

- probability of default (PD);
- loss given default (LGD); and
- exposure at default (EAD).

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

ECL for exposures in Stage 1 is calculated by multiplying the 12-month PD by LGD and EAD. Lifetime ECL is calculated by multiplying the lifetime PD by LGD and EAD.

LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset. For loans secured by retail property, LTV ratios are a key parameter in determining LGD. LGD estimates are recalibrated for different economic scenarios and, for real estate lending, to reflect possible changes in property prices.

EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract and arising from amortisation. The EAD of a financial asset is its gross carrying amount at the time of default. For lending commitments, the EADs are potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts.

As described above, and subject to using a maximum of a 12-month PD for Stage 1 financial assets, the Bank measures ECL considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for credit risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment or guarantee.

For portfolios in respect of which the Bank has limited historical data, external benchmark information such as Moody's Default Rates and Loss Recovery Rates are used to supplement the internally available data. The portfolios for which external benchmark information represents a significant input into measurement of PD and ECL are as follows.

- Corporate Loans
- Loans to Banks
- Money Market Deposits to Banks

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort.

The Bank has not experienced significant losses in the past and has a very highly collateralised loan portfolio with very low loan to value. Loans with less than 30 days overdue are classified as Stage 1, 30-90 days are classified as Stage 2 and over 90 days are classified as Stage 3. The methodology of estimating the PD's and LGD is provided below.

Accounts that are in excess of agreed limits are discussed at the monthly core lending meetings and escalated to the Credit Committee if appropriate. Provision is made on the advice of Credit Committee if an exposure is deemed to be at risk of non-recovery. All the provisions are approved by the Board of Directors.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

20. Investment securities

| | 2018 | | | 2017 | | |
|----------------------------------|-----------------------|------------------------|------------|----------------------------|------------------------|------------|
| | Share in Visa Inc. | Floating rate bonds | Total | Share in Visa Europe | Floating rate bonds | Total |
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| Share in Visa Inc. / Visa Europe | 498 | - | 498 | 300 | - | 300 |
| Corporate bonds | - | - | - | - | 512 | 512 |
| | <u>498</u> | <u>-</u> | <u>498</u> | <u>300</u> | <u>512</u> | <u>812</u> |

Investment in securities will mature as follows:

| | 2018 £'000 | 2017 £'000 |
|----------------------------|---------------|---------------|
| Repayable: | | |
| 3 to 12 months | - | 512 |
| Between one and five years | - | - |
| Five years or more | 498 | 300 |
| | <u>498</u> | <u>812</u> |

During 2016 there was a reorganisation of the Visa network which included the sale of Visa Europe to Visa Inc. As a result in 2016 the Bank realised £975k through profit or loss of which Euro 1,040k was received during the year. In addition the Bank received 743 preference shares valued at £325k which were treated as Available for Sale in 2017 and FVOCI in 2018 following implementation of IFRS 9. The bank revalues these shares through other comprehensive income.

The debt securities comprise corporate bonds and are held as available for sale in 2017 reclassified as Amortised Cost in 2018 following implementation of IFRS 9.

The above balance includes debt securities of £0.00 which are due to mature in less than one year (2017: £512,000).

Analysis by currency of origin is as follows:

| Origin of investment securities | 2018 | | | | 2017 | | | |
|------------------------------------|----------|------------|----------|------------|----------|------------|------------|------------|
| | GBP | USD | TRY | Total | GBP | USD | TRY | Total |
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| Europe | - | - | - | - | - | - | - | - |
| Turkey | - | - | - | - | - | - | 512 | 512 |
| USA | - | 498 | - | 498 | - | 300 | - | 300 |
| Total | <u>-</u> | <u>498</u> | <u>-</u> | <u>498</u> | <u>-</u> | <u>300</u> | <u>512</u> | <u>812</u> |

Turkish Bank (UK) Limited

Notes to the accounts For the year ended 31 December 2018

21. Intangible fixed assets

| | Computer Software £'000 |
|-----------------------|--|
| Cost | |
| At 1 January 2018 | 3,405 |
| Additions | 150 |
| Disposals | - |
| At 31 December 2018 | <u>3,555</u> |
| Amortisation | |
| At 1 January 2018 | 1946 |
| Charge for the year | 223 |
| Disposals | - |
| At 31 December 2018 | <u>2,169</u> |
| Net book value | |
| At 31 December 2018 | <u>1,386</u> |
| At 31 December 2017 | <u>1,459</u> |

The intangible fixed assets comprise software purchased, and external costs relating to developed systems. The additions represent the costs incurred in the project to join the BACS and Faster Payments systems. These project costs as well as the licence for the core banking system are being amortised over 10 years, other software is amortised over 5 years. The values above represent amortised historic cost and have not been adjusted to fair value.

22. Property and Equipment

| | Freehold land and buildings £'000 | Lease hold land and building £'000 | Lease equipment £'000 | Fixtures, fittings and equipment £'000 | Total £'000 |
|-------------------------|--|---|--------------------------------------|---|------------------------|
| Cost/Revaluation | | | | | |
| At 1 January 2018 | 8520 | 653 | 386 | 2,721 | 12,280 |
| Additions | - | - | 69 | 72 | 141 |
| Disposals | - | - | (55) | (12) | (67) |
| At 31 December 2018 | <u>8,520</u> | <u>653</u> | <u>400</u> | <u>2,781</u> | <u>12,354</u> |
| Depreciation | | | | | |
| At 1 January 2018 | - | 653 | 92 | 2,270 | 3,015 |
| Charge for the year | 167 | - | 87 | 161 | 415 |
| Disposals | - | - | (43) | (12) | (55) |
| At 31 December 2018 | <u>167</u> | <u>653</u> | <u>136</u> | <u>2,419</u> | <u>3,375</u> |
| Net book value | | | | | |
| At 31 December 2018 | <u>8,353</u> | <u>-</u> | <u>264</u> | <u>362</u> | <u>8,979</u> |
| At 31 December 2017 | <u>8,520</u> | <u>-</u> | <u>294</u> | <u>451</u> | <u>9,265</u> |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

The land and buildings are occupied by the Bank for its own activities. The properties were revalued by an independent surveyor in December 2017 resulting in a valuation increase of £1,880,000 (2016: £NIL). The carrying value of freehold buildings if they were carried at historical cost would be £ 1,537,000 (net of depreciation). Freehold land and buildings were revalued to fair value as at December 2017. The board considers that the fair value is not less than the carrying value. It is intended to next revalue these assets as at 31 December 2020.

23. Other assets

| | 2018 £'000 | 2017 £'000 |
|-----------------------------------|---------------|---------------|
| Bonds sold awaiting settlement | - | 1,145 |
| Items in the course of collection | 206 | 430 |
| Prepayments | 453 | 392 |
| Other assets | 530 | 557 |
| | <u>1,189</u> | <u>2,524</u> |

24. Deposits from banks

| | 2018 £'000 | 2017 £'000 |
|---|---------------|---------------|
| Deposits from banks are repayable as follows: | | |
| On demand | | |
| - Group | 18,043 | 2,180 |
| - Other | 811 | 958 |
| | <u>18,854</u> | <u>3,138</u> |

The interest paid to Group companies during the year was £ 10,821 (2017: £1,897). All bank deposits mature the next day.

Geographical analysis of deposit by banks is as follows:

| | 2018 £'000 | 2017 £'000 |
|--------------------|---------------|---------------|
| In UK: | | |
| On current account | - | - |
| Outside UK: | | |
| On current account | 18,854 | 3,138 |
| | <u>18,854</u> | <u>3,138</u> |

25. Deposits from customers

| | 2018 £'000 | 2017 £'000 |
|---|----------------|----------------|
| Customer deposits are repayable as follows: | | |
| On demand | 82,831 | 84,685 |
| Within three months | 31,344 | 26,622 |
| Between three months and one year | 28,095 | 27,801 |
| Between one year and five years | 3,894 | 5,901 |
| | <u>146,164</u> | <u>145,009</u> |

The balance includes customers' deposits of £142 million (2017: £139 million) which are due to mature in less than one year.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

The following information is given in respect of the nature and type of customer deposits:

| | 2018 £'000 | | | 2017 £'000 | | |
|-----------------|------------------------|---------------------------|----------------|------------------------|---------------------------|----------------|
| | Fixed rate interest | Floating rate interest | Total | Fixed rate interest | Floating rate interest | Total |
| Current account | - | 40,789 | 40,789 | - | 44,814 | 44,814 |
| Deposit account | - | 40,805 | 40,805 | - | 38,029 | 38,029 |
| Fixed deposit | 64,570 | - | 64,570 | 62,166 | - | 62,166 |
| | <u>64,570</u> | <u>81,594</u> | <u>146,164</u> | <u>62,166</u> | <u>82,843</u> | <u>145,009</u> |

The following information is given in respect of currency and origin of customer deposits:

| | 2018 £'000 | | | | | 2017 £'000 | | | | |
|--------|------------------|---------------|---------------|--------------|----------------|----------------|---------------|---------------|--------------|----------------|
| | GBP £'000 | USD £'000 | EUR £'000 | TRY £'000 | Total £'000 | GBP £'000 | USD £'000 | EUR £'000 | TRY £'000 | Total £'000 |
| UK | 46,147 | 3,651 | 735 | 343 | 50,876 | 43,436 | 2,622 | 1,645 | 525 | 48,228 |
| Turkey | 27,415 | 23,403 | 6,102 | 5 | 56,925 | 37,768 | 26,318 | 4,765 | 2,072 | 70,923 |
| TRNC | 28,353 | 4,022 | 5,202 | 60 | 37,637 | 19,596 | 1,936 | 3,624 | 98 | 25,254 |
| Others | 242 | 458 | 24 | - | 724 | 442 | 147 | 10 | 5 | 604 |
| Total | <u>1,102,158</u> | <u>31,535</u> | <u>12,063</u> | <u>408</u> | <u>146,164</u> | <u>101,242</u> | <u>31,023</u> | <u>10,044</u> | <u>2,700</u> | <u>145,009</u> |

TRNC is the Turkish Republic of Northern Cyprus

26. Other liabilities

| | 2018 £'000 | 2017 £'000 |
|---|---------------|---------------|
| Amounts owed to Group companies | 25 | 14 |
| Other taxes and social security costs | 59 | 64 |
| Deferred income | 905 | 632 |
| Items in the course of transmission | 11 | 53 |
| Obligations under finance lease and hire purchase | 284 | 301 |
| Other liabilities | 263 | 727 |
| | <u>1,547</u> | <u>1,791</u> |
| | 2018 £'000 | 2017 £'000 |
| Obligations under finance lease and hire purchase | | |
| Under one year | 72 | 69 |
| 1-5 Years | 212 | 231 |
| Total | <u>284</u> | <u>301</u> |

Turkish Bank (UK) Limited

Notes to the accounts For the year ended 31 December 2018

27. Deferred tax liabilities

| £'000 | Revaluation of land and buildings | Fair valuation of Visa shares | Other short term timing differences | Total |
|---|---|--|--|-------|
| Originally reported at 31.12.2016 | 611 | - | 9 | 620 |
| Restatement impact at 1 January 2017 | (587) | - | - | (587) |
| As restated at 01.01.2017 | 24 | - | 9 | 33 |
| Charge (credit) to income | - | - | 54 | 54 |
| Charge (credit) to comprehensive income | 245 | - | - | 245 |
| At 31.12.2017 | 269 | - | 63 | 332 |
| IFRS 9 adjustment at 1.1.2018 | - | - | (1) | (1) |
| Charge (credit) to income | (28) | - | 41 | 13 |
| Charge (credit) to comprehensive income | | 30 | | 30 |
| At 31.12.2018 | 241 | 30 | 103 | 374 |

Deferred Tax has been calculated at 17% of the timing difference

28. Called up share capital

| | Called up, allotted and fully paid | |
|---------------------------------------|---------------------------------------|---------------|
| | 2018 £'000 | 2017 £'000 |
| 12,000,000 Ordinary shares of £1 each | 12,000 | 12,000 |

All shares have the same rights. There are no restrictions on the distribution of dividends and the repayment of capital subject to regulatory capital adequacy restrictions.

29. Commitments

The amounts shown below are intended to provide an indication of the volume of business transacted and not of the underlying credit or other risks.

| | 2018 £'000 | 2017 £'000 |
|--|---------------|---------------|
| Formal standby facilities, credit lines and other commitments to lend: | | |
| One year and over | - | - |
| Less than one year | 5,066 | 4,385 |
| | 5,066 | 4,385 |

There are annual commitments under non-cancellable operating leases as follows:

| | Land and buildings | |
|--------------------------------|-----------------------|---------------|
| | 2018 £'000 | 2017 £'000 |
| Operating leases which expire: | | |
| Within one year | 168 | 202 |
| Between two and five years | 103 | 243 |
| More than five years | - | - |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

30. Assets and liabilities in foreign currencies

The aggregate amounts of assets and liabilities denominated in foreign currencies were as follows:

| | 2018 £'000 | 2017 £'000 |
|-------------|---------------|---------------|
| Assets | 33,209 | 44,963 |
| Liabilities | 49,649 | 45,842 |

There were open foreign exchange swaps as at 31 December 2018 with net value £78,014 (2017: £49,706).

31. Transactions with directors and managers

As at 31 December 2018 £30,655 was outstanding by way of loans to managers of the Bank (or persons connected with them) (2017: £9,564). During the year, £3,828 (2017: £24,170) was paid back and £34,483 drawn by the managers (or persons connected to them) (2017: £9,564). There were transactions with parties related to directors for £58,908 (2017: £73,660). The transactions with related parties are on standard commercial terms.

32. Ultimate parent company

The ultimate parent and controlling company is Ozyol Holding A.S., which is incorporated in Turkey, registered address:- Macka Polat Apartmani, 10 V Alaaddin Yavasca Sokak, Istanbul. The parent company of the largest and smallest groups of which the Bank is a member and for which consolidated accounts are prepared is Turkish Bank Limited, incorporated in Cyprus, registered address 92 Girne Cad, Lefkosa, Cyprus. Copies of its financial statements can be obtained from 84-86 Borough High Street, London SE1 1LN.

33. Related party transactions

Transactions with senior managers and staff are described in note 24. The only other related party transactions are described below. All the transactions below were at "arm's length" prices:

| | 2018 £'000 | 2017 £'000 |
|--|---------------|---------------|
| Placements with group companies | 2,746 | 6,230 |
| Deposits from group companies | 18,043 | 1,013 |
| Purchase of loans from group companies | - | 9,300 |
| Interest received from group companies | 37 | 27 |
| Interest paid to group companies | 11 | 2 |

A number of loans were sold to the parent bank during 2016, the parent bank's regulator noted that the collateral remained in the name of the UK bank, and was proposing a higher than anticipated risk weighting, so the bank repurchased the loans in 2017. No profit or loss was made on the sale or the repurchase.

34. Risk management framework

Risk taking is central to banking activity. The Bank evaluates business opportunities in terms of a prudent risk-reward relationship. The risks that the Bank takes on are managed within an established control environment, within its financial resources and credit competence.

The diversity of our business requires us to identify measure and manage risks effectively. At TBUK, the risk is managed through an organisational structure including risk management and the monitoring of processes that are closely aligned with the activities of the Bank and in line with the guidelines given by the Regulators.

The following key principles form part of TBUK's approach to risk management:

The Board, through its subcommittee, the Risk Committee, (Chaired by a Non-Executive Director) oversees risk management, and sets the framework and risk appetite. The Risk Committee overviews all risks and controls and in particular the Risk Management System operated by the Bank and is also responsible for monitoring emerging risks and keeping the Board advised. It also is the Committee that takes the lead on the Recovery and Resolution Plan

Notes to the accounts

For the year ended 31 December 2018

(RRP), Individual Capital Adequacy Assessment Process (ICAAP) and Individual Liquidity Adequacy Assessment Process (ILAAP) plus associated risk documents. The risk appetite sets out detailed tolerance limits within which the business operates, and this is supported by Bank Policies. All Policies are approved by the Board and subject to review at least once each calendar year.

The Audit Committee (Chaired by a Non-Executive Director) reports to the Board and is responsible for ensuring that the controls set out by the Board and Risk Committee and by various policies are carried out in practice and remain effective. The Internal Audit function reports direct to the Audit Committee and the external auditor is invited to all meetings of the Audit Committee, which meets at least quarterly.

There are then various committees at functional level to oversee the implementation of risk management and associated policies. The principal committees are:

- Executive Committee (EXCO) – responsible for day to day management of the business under the direction of the Managing Director.
- Assets and Liabilities Committee (ALCO), which manages the market and liquidity risks, and now reports direct to the Board (through the Risk Committee on certain issues such as the RRP). ALCO is responsible for the RRP and also the contingency Funding Plan (CFP) and its members have direct responsibility for the ICAAP and ILAAP.
- Management Risk Committee – day to day responsibility for risk reporting to the Risk Committee. This involves all management taking a role in the Risk Management System overseen by the Risk and Compliance Officer and deals with all risks issues not covered by the Conduct Risk Committee.
- The Conduct Risk Committee deals with risk matters of a conduct nature (e.g. Anti-Money Laundering, Treating Customers Fairly, product risk) and this aligns with the principles of the Financial Conduct Authority.
- Credit Committee – dealing specifically with all matters of credit risk.

The Business Development Committee is responsible for developing business, marketing and product development.

Credit Risk Management

Credit risk, with its closely associated concentration risk, is the risk of loss due to the failure of a borrower to meet its credit obligations in accordance with agreed contract terms.

Credit risk makes up the largest part of the Bank's risks exposure. The Bank's credit process is guided by a well-established credit policy, rules and guidelines aim to maintain a well-diversified portfolio of credit risk which produces a reliable and consistent return. The Credit Committee is responsible for controlling credit risk and implementing the Credit Policies as authorised by the Board. All decisions require unanimous agreement at each level of lending authority as prescribed by the Board.

The Bank has a system of checks and balances in place around the extension of credit that are:

- an independent credit management function;
- multiple credit approvers; and
- an independent audit and risk review function.

The Credit Risk Policy reflects TBUK's tolerance for risk, i.e. credit risk appetite and the level of expected return. This, as a minimum, reflects TBUK's strategy to grant credit based on various products, economic sectors, client segments and target markets giving due consideration to risks specific to each target market, and the impact of concentration risk.

Salient features of our Risk approval process are delineated below:

- every extension of credit to any counterparty requires unanimous approval by the pre-defined level of authority sanctioned by the Board;
- all business Banks must apply consistent standards in arriving at their credit decisions;
- every material change to a credit facility requires approval at the appropriate, pre-defined level; and
- credit approval authority is assigned to individuals according to their qualifications and experience.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

The Bank uses risk rating systems to supplement the credit risk measurement procedure. This process previously only applied to exposures exceeding a certain threshold, but during 2016 was expanded to cover all exposures. Risk rating of counterparties is considered an essential requirement of the credit approval process.

Stress testing on the credit portfolio is performed quarterly and more often if required.

The disbursement, administration and monitoring of credit facilities are managed by the Central Credit Unit (CCU). CCU is also responsible for collateral/documents management.

The Bank monitors its credit portfolio on a continuing basis. Procedures are in place to identify, at an early stage, credit exposures for which there may be a risk of loss. The objective of this early warning system is to address potential problems while various options may still be available. Early detection of problem loans is a tenet of our credit culture and is intended to ensure that greater attention is paid to such exposure. The Credit Committee also takes responsibility for monitoring non-performing loans and managing loan recovery.

The following table sets out information about the credit quality of financial assets measured at amortised cost, FVOCI debt investments (2018) and available-for-sale debt assets (2017). Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts. For loan commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranteed, respectively.

| | 2018 | | | | 2017 |
|---|---------|---------|---------|--------|--------|
| | Stage 1 | Stage 2 | Stage 3 | Total | Total |
| Loans and advances to banks at amortised cost | 1,795 | - | - | 1,795 | 1,772 |
| Loss allowance | (22) | - | - | (22) | - |
| Carrying amount | 1,773 | - | - | 1,773 | 1,772 |
| Loans and advances to customers at amortised cost | 90,232 | - | 4,362 | 94,594 | 98,532 |
| Loss allowance | (49) | - | (45) | (94) | (135) |
| Carrying amount | 90,183 | - | 4,317 | 94,500 | 98,397 |
| Debt investment securities at amortised cost (2017: available-for-sale) | - | - | - | - | 512 |
| Loss allowance | - | - | - | - | - |
| Carrying amount | - | - | - | - | 512 |
| Debt investment securities at FVOCI (2017: available-for-sale) | 498 | - | - | 498 | 300 |
| Loss allowance | - | - | - | - | - |
| Carrying amount | 498 | - | - | 498 | 300 |
| Off balance sheet Loan commitments | 5,066 | - | - | 5,066 | 4,385 |
| Loss allowance | (20) | - | - | (20) | - |
| Carrying amount | 5,046 | - | - | 5,046 | 4,385 |

The Bank also monitors, as part of its credit risk assessment, its concentration risk in various sectors.

The Bank's maximum exposure to credit risk at the year-end is £184 million (2017: £167 million). Credit risk exposure of £90 million (2017: £81 million) is secured against the first charge on properties and lien on customers' deposits.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Collateral in the form of cash, freehold or bank guarantees are accepted by the Bank as credit risk mitigating factors.

| Total Collateral held as at 31 December: | 2018 | 2017 |
|---|----------------|----------------|
| | £'000 | £'000 |
| Cash | 1,514 | 300 |
| Freehold | 189,749 | 196,819 |
| Guarantees | 630 | 190 |
| Total | 196,108 | 197,309 |

All collateral is held by the Bank in its original form until the debt has been repaid. The Bank holds collateral and is permitted to sell in the event of default by the owner. Collateral of freehold properties is valued by independent professional values on inception of a loan.

All the above collateral is held against the loans and advances to customers as follows:-

| | 2018 | 2018 | 2017 | 2017 |
|-------------------------------|--------------|-------------------|--------------|-------------------|
| | Loans | Collateral | Loans | Collateral |
| | £'000 | £'000 | £'000 | £'000 |
| Loans & advances to customers | 94,480 | 196,108 | 98,532 | 197,309 |

The collateral value in the above table excludes the value of such collateral which the Bank may accept to manage its risks more effectively such as second charge on assets, other liens and corporate guarantees and related support undertakings from the borrower Bank entities.

Mortgages: The loan to value ratio of lending secured against property is as follows:-

| LTV Ratio | 2018 | 2017 |
|------------------|---------------|---------------|
| | £'000 | £'000 |
| Less than 50% | 36,550 | 36,106 |
| 51-70% | 51,846 | 57,971 |
| 71-90% | 1,574 | - |
| Over 90% | - | - |
| Total | 89,970 | 94,077 |

Note the above table shows the maximum facility amount and is greater than the actual exposure mortgages.

Turkish Bank (UK) Limited

Notes to the accounts For the year ended 31 December 2018

Debt Securities – External Ratings

The issuers of the available for sale securities have ratings as follows:-

| | 2018 | 2017 |
|-----------------|------------|------------|
| | £'000 | £'000 |
| Corporate Bonds | | |
| A+ | 498 | 300 |
| BBB/BBB+ | - | - |
| BB | - | 512 |
| Unrated | - | - |
| | <hr/> | <hr/> |
| Total | 498 | 812 |
| | <hr/> | <hr/> |

Internal credit rating

The Bank assigns internal credit ratings to each of its counterparties. The rating structure is kept under regular review to ensure that the ratings are appropriate.

Industry distribution of credit exposures

Analysis of financial assets by industry distribution as at 31 December:

| | 2018 | 2017 |
|--|---------------|---------------|
| | £'000 | £'000 |
| Real Estate | 8,626 | 9,361 |
| Hotels & Restaurants | 3,849 | 4,418 |
| Retail & Wholesale | 4,127 | 3,932 |
| Construction | 3,453 | 2,962 |
| Service Providers | 772 | 1,488 |
| Financial | - | 452 |
| Individuals & Individual trusts | 73,766 | 76,049 |
| Recreational, Cultural, Sport Activities | - | 5 |
| | <hr/> | <hr/> |
| Total | 94,594 | 98,667 |
| Provision for impairment losses | (114) | (135) |
| | <hr/> | <hr/> |
| Total | 94,480 | 98,532 |
| | <hr/> | <hr/> |

The Bank's policy on forbearance is to consider each loan on a case by case basis. All such cases are discussed and approved by the Credit Committee. During the year no credit or interest was foregone.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

| | 2018 | | | | |
|---------------------------------|---------------------|---------------------------------------|-----------------------------------|--------------------------|------------------------|
| | Cash equivalents | Loans and advances to customers | Loans and advances to banks | Investment securities | Lending commitments |
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| Maximum exposure to credit risk | 30,314 | 94,594 | 1,795 | 498 | 5,066 |
| At amortised cost | | | | | |
| Performing | 30,314 | 90,232 | 1,795 | 498 | 5,066 |
| Watch list | - | 4,327 | - | - | - |
| Impaired | - | 35 | - | - | - |
| Total Gross amount | 30,314 | 98,594 | 1,795 | 498 | 5,066 |
| Impairment provisions | (21) | (94) | (22) | - | (20) |
| Net carrying amount | 30,293 | 94,500 | 1,773 | 498 | 5,046 |

| | 2017 | | | | |
|---------------------------------|---------------------|---------------------------------------|-----------------------------------|--------------------------|------------------------|
| | Cash equivalents | Loans and advances to customers | Loans and advances to banks | Investment securities | Lending commitments |
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| Maximum exposure to credit risk | 40,631 | 98,532 | 1,772 | 812 | 4,385 |
| At amortised cost | | | | | |
| Low | 40,631 | 95,929 | 1,772 | 812 | 4,385 |
| Watch list | - | 2,703 | - | - | - |
| Impaired | - | 35 | - | - | - |
| Total Gross amount | 40,631 | 98,667 | 1,772 | 812 | 4,385 |
| Impairment provisions | - | (135) | - | - | - |
| Net carrying amount | 40,631 | 98,532 | 1,772 | 812 | 4,385 |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Encumbered Assets

The Bank has no encumbered assets and has not pledged any of its assets as collateral.

ICAAP (Internal Capital Adequacy Assessment Process)

The ICAAP is managed by ALCO and presented to the Risk Committee then Board for challenge and approval. The ICAAP process identifies the risks that are involved in the business and the amount of capital that should be held against each of the risks. As an outcome from this process the Bank has determined that it should hold additional capital for the following risks:

- Credit Risk (including concentration risk)
- Market Risk
- Operational Risk (including Systems and Controls; Personnel and Reputational)
- Currency and FX Risk
- Interest Rate Risk

The Bank also has liquidity risk but does not hold capital against this. These risks are discussed further in this section

Credit Risk

The Bank has established limits for Cross Border Transfer Risk (CBTR) based on the ratings assigned by internationally recognised rating agencies. CBTR arises from exposure to counterparties in countries other than the country where exposure is located. The Bank defines transfer risk as arising where an otherwise solvent and willing debtor is unable to meet its obligation due to the imposition of Governmental or regulatory controls restricting its ability to perform under its obligation towards its foreign liabilities.

Market Risk

It is the risk of loss due to adverse movements in market rates or prices, such as foreign exchange rates, interest rates and market prices. The Bank only operates positions housed in its Banking book within strict Board approved guidelines. Currently Market Risk reporting is made to the Regulator on the "Standard Method" base. Derivative transactions currently permitted include foreign currency, Forward Rate Agreements. At present the Bank is only dealing in Foreign Exchange Currency Swaps on a very limited scale and purely to reduce its foreign exchange exposure. Valuation and accounting policies in line with IFRS have been formulated and are operative. There was a notional amount outstanding at the year-end of £ 16,798,048 with a book value of £78,000 (book value £78,000 31 December 2017).

Currency and Foreign Exchange Risk

The Bank's assets are typically funded in the same currency as that of the business transacted to minimise foreign exchange exposure. However, the Bank does incur small open positions in various currencies resulting from the trade related transactions handled by the Bank.

Foreign Exchange risks are controlled and monitored through the limits monitored by ALCO and notified to the PRA. The regulatory limit for foreign exchange is relatively small compared to the size of the Bank; hence the risk generated through foreign exchange activities is not significant and therefore sensitivity analysis has not been presented. End of the day positions are marked to market according to the IFRS and sensitivity is conducted in line with the internal market risk policy of the Bank. The intra-day positions are managed by Treasury.

| Currency of denomination | Net currency | Net currency |
|--------------------------|--------------|--------------|
| | position | position |
| | 2018 | 2017 |
| | £'000 | £'000 |
| US Dollar | 286 | 289 |
| Euro | 5 | - |
| Turkish Lira | (7) | (1,208) |
| Total | 284 | (919) |

Notes to the accounts

For the year ended 31 December 2018

The above table sets out those currency exposures that the Bank has at the year end. The amounts shown in the table take into account the effect of any currency swaps and forward contracts entered into to manage these currency exposures and are consistent with the position throughout the year. The disclosures include all monetary assets and liabilities including short-term debtors and creditors. Those assets and liabilities denominated in sterling have been excluded.

For the purposes of the net currency disclosure above, sterling has been used as the Bank's functional currency.

The Bank enters into short-term foreign exchange currency swap transactions for funding purposes. These currency swap transactions are utilised purely for economic hedging purposes. The Bank does not apply hedge accounting

Interest Rate Risk

Interest rate risk is the risk that an investment value will change due to a change in the absolute level of interest rates i.e. the spread between two rates, in the shape of the yield curve, or in any other interest rate relationship.

A substantial part of the Bank's assets and liabilities are subject to floating rates hence are re-priced simultaneously. However, the Bank is exposed to interest rate risk as a result of mismatches on a relatively small portion of its assets and liabilities. The major portion related to this risk is reflected in the banking book owing to the retail activities and investments. The overall potential impact of the mismatches on the earnings in the short-term and economic value of the portfolio in the longer term is not material and is being managed within the tolerance limits approved by the Board.

Exposure to interest rate movements arise where there is an imbalance between rate sensitive assets and liabilities. The tables on pages 69 and 70 reflect management's estimate of the interest rate sensitivity gap for the Bank as at 31 December 2018, and 31 December 2017. Assets and liabilities are included at the earliest date at which the applicable interest rate can change

Liquidity Risk Management

Liquidity Risk is the risk that the Bank will be unable to meet its cash flow obligations as they become due because of an inability to liquidate assets, or to obtain adequate funding.

The ALCO has the responsibility for the formulation of overall strategy and oversight of the asset/liability management function.

The Bank follows a comprehensive liquidity risk management policy duly approved by ALCO and Board. The policy stipulates maintenance of various ratios, funding preferences and evaluation of Bank's liquidity under normal and crisis situation (stress testing). To comply with the policy, the Bank has also conducted a behavioural study on its core deposits to evaluate their stickiness, which may not reflect in their maturity profile. Such evaluation forms part of the liquidity management process to project realistically the reliance on such funding sources. As a result of close monitoring and strict policies towards reliance on core deposits, the Bank has been able to avoid concentration / reliance on volatile deposits in its books.

Liquidity risk

The Bank is regulated in the United Kingdom by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA), which, from time-to time, sets required liquidity mismatch parameters. The Bank manages the liquidity structure of its assets, liabilities and commitments so that cash flows are appropriately balanced to ensure that all funding obligations are met when due and the required mismatch parameters are not exceeded. The policy of the Bank is to match to maturity as far as is practicable and the Treasury Department will not take on large exposures or placements that cannot easily be matched in the market as to currency or maturity.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Maturity analysis of assets and liabilities

The table below shows the remaining contractual maturities for assets and liabilities. For both 2018 and 2017 the contractual amounts are a reasonable approximation to the fair values.

| £'000 | Carrying amount | Demand | Less than 3 months | 3 months to 1 year | 1-5 years | Over 5 years |
|-------------------------------------|--------------------|----------------|-----------------------|-----------------------|---------------|-----------------|
| 31 December 2018 | | | | | | |
| Cash and cash equivalents | 85,862 | 73,069 | 12,793 | | | |
| Loans and advances to banks | 1,773 | - | - | 1,773 | - | - |
| Loans and advances to customers | 94,480 | 5,422 | 2,911 | 8,709 | 56,090 | 21,348 |
| Investment securities | 498 | - | - | - | - | 498 |
| Other assets | 11,760 | - | 1,189 | 206 | 1,386 | 8,979 |
| Total assets | 194,373 | 78,491 | 16,893 | 10,688 | 57,476 | 30,825 |
| Derivative liabilities | 78 | - | 78 | - | - | - |
| Deposits from banks | 18,854 | 18,854 | - | - | - | - |
| Deposits from customers | 146,164 | 82,831 | 31,344 | 28,095 | 3,894 | - |
| Other liabilities | 1,921 | - | 373 | - | 1,174 | 374 |
| Equity | 27,356 | | | | | 27,356 |
| Total liabilities and equity | 194,373 | 101,685 | 31,795 | 28,095 | 5,068 | 27,730 |

Notes to the accounts
For the year ended 31 December 2018

| £'000 | Carrying amount | Demand | Less than 3 months | 3 months to 1 year | 1-5 years | Over 5 years |
|-------------------------------------|----------------------------|---------------|-------------------------------|-------------------------------|------------------|-------------------------|
| 31 December 2017 (restated) | | | | | | |
| Cash and cash equivalents | 63,088 | 28,849 | 34,239 | - | - | - |
| Loans and advances to banks | 1,772 | - | - | 1,772 | - | - |
| Loans and advances to customers | 98,532 | 4,989 | 1,825 | 7,745 | 63,082 | 20,891 |
| Debt securities | 812 | - | - | 512 | - | 300 |
| Other assets | 13,399 | - | 2,496 | 71 | 853 | 9,979 |
| | 177,603 | 33,838 | 38,560 | 10,100 | 63,935 | 31,170 |
| Total assets | | | | | | |
| Derivative liabilities | 50 | - | 50 | - | - | - |
| Deposits from banks | 3,138 | 3,138 | - | - | - | - |
| Deposits from customers | 145,009 | 84,685 | 26,623 | 27,800 | 5,901 | - |
| Other liabilities | 2,759 | - | 908 | 128 | 822 | 901 |
| Equity | 26,647 | - | - | - | - | 26,647 |
| | 177,603 | 87,823 | 27,581 | 27,928 | 6,723 | 27,548 |
| Total liabilities and equity | | | | | | |

Operational Risk

Operational Risk controls are incorporated in the Temenos (Globus T24) system that allows an overall control of transactions centrally by Compliance Unit. The Board has approved the Operational Risk Policy. It has been further enhanced by the introduction over the last two years of a dedicated Risk Management System (in Globus T24) which records and assesses individual risks to ensure they are properly monitored and controlled.

The policy covers the core governing principles for operational risk management and provides guidelines to identify, control, monitor measure and report operational risk in a consistent manner across the Bank. The online authorisations level based control infrastructure is one of the main tools that prevent Operational Risk losses. In addition, Internal Control Unit is able to perform "Transaction Based Control" with the new software (T24). Operational losses and near misses are monitored and assessed. The Board of Director's risk appetite is to keep Operational risk at the minimal level possible within the Bank's business model. The Bank's assessment and control of all Operational risks, which include diverse areas such as cyber-attacks, fraud, human error is the responsibility of the Risk Management committee which reports to the Board of Directors.

Operational Risk is now calculated according to the "Basic Indicator Approach".

Risk monitoring process is performed at both transaction and portfolio levels.

Monitoring at transaction levels is a function of the managers of business units where transactions are actually carried out, which is described as Local Monitoring. In cases where the managers originate business themselves exercising their discretionary authorities, monitoring is performed by their immediate line managers.

Monitoring at portfolio levels is carried out by Head Office committees, under the overview of the Risk and Compliance Manager, or by the Managing Director depending on the nature of risks involved and described as Central Monitoring. Information required for monitoring at a portfolio level is provided by the relative Head Office department manager using information gleaned from appropriate Management reports.

Monitoring of financial risks also covers related operational, statutory and regulatory risks.

Operational risk also includes any risks arising from Systems and Controls failures, Reputational Risk and Key Personnel Risk, all of which are managed through the Risk Management System.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

35. Financial instruments

The Bank maintains a proprietary investment portfolio whereby capital funds are invested in fixed and floating interest rate Corporate Bonds. Additionally, the Bank has financial assets in the form of cash, loans and advances to banks and loans and advances to customers. The Bank also has financial liabilities in the form of deposits by banks and customer accounts and derivatives.

The Bank does not assume in the normal course of business any significant foreign exchange exposures. The Bank is exposed to movements in interest rates and manages this exposure on a continuous basis within limits set by the Board. Short-term foreign exchange currency swaps are utilised, where cost-efficient, as a funding mechanism, principally to convert sterling capital funds to US dollars. The Bank does not utilise derivatives to assume any form of credit or market risk. The Bank utilises derivatives for economic hedging purposes.

The directors of the Bank have established policies relating to large exposures, interest rate gaps, foreign exchange exposure, liquidity management and credit provisioning. In addition, the Bank operates within limits set by the directors relating to country exposure, credit exposure and risk asset maturities. These policies and limits are reviewed on a regular basis, and any amendment to these policies and limits require the consent of the Board of Directors.

Levelling disclosure

There were no transfers of assets between levels during 2018 or 2017 and no significant changes in valuation techniques. The Bank has not separately disclosed the fair values for financial instruments such as loans and advances and customer accounts because carrying amounts are a reasonable approximation to fair value.

| | Level 1 £'000 | Level 2 £0 | Level 3 £'000 | Total £'000 |
|--|------------------|------------------|------------------|----------------|
| 31-Dec-18 | | | | |
| Financial Assets | | | | |
| Equity Instruments FVOCI | - | - | 498 | 498 |
| Financial Liabilities | | | | |
| Derivative liabilities | - | (78) | - | (78) |
| | | | | |
| | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 | Total £'000 |
| 31-Dec-17 | | | | |
| Financial Assets | | | | |
| Marketable securities available for sale | - | 512 | 300 | 812 |
| Financial Liabilities | | | | |
| Derivative liabilities | - | (50) | - | (50) |

There were no transfers of assets between levels during 2018 or 2017 and no significant changes in valuation techniques. The Bank has not separately disclosed the fair values for financial instruments such as loans and advances and customer accounts because carrying amounts are a reasonable approximation to fair value.

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Derivative financial instruments:

At the reporting date the Bank had derivative assets and liabilities from foreign currency swap contracts. The total notional amount of outstanding forward foreign exchange contracts that the Bank has committed is as below.

| | Notional amount £'000 | 2018 | Fair value |
|---------------------------------|-----------------------------|--------|-------------|
| | | Assets | Liabilities |
| | | £'000 | £'000 |
| Foreign currency swap contracts | 16,798 | - | (78) |
| | | | |
| | Notional Amount £'000 | 2017 | Fair value |
| | | Assets | Liabilities |
| | | £'000 | £'000 |
| Foreign currency swap contracts | 1,862 | - | (50) |

The foreign currency swaps as at 31 December 2018 were due to mature in less than three months (2017 due to mature less than three months). The swaps were over the counter short term swaps with a non-connected third party.

No collateral was given or received in respect of the swap. The cash flows associated with the swap are that on maturity, the Bank will exchange currency amounts equivalent to the notional amount above with the contracted counterparty.

Capital risk management

The Bank's lead regulator is the Prudential Regulatory Authority "PRA". The PRA sets and monitors capital requirements for the bank. The Bank's regulatory capital requirements are based on Basel III.

The Bank's policy in respect of capital adequacy is to maintain a strong capital base so as to retain investor, creditor and market confidence. During the years ended 31 December 2018 and 2017 capital has been maintained at a level above minimum PRA requirements. Such levels have been established by reference to an Internal Capital Adequacy Assessment Process ("ICAAP") assessment. The Bank's capital resources consist of Share Capital, retained earnings, and other reserves.

The Bank holds their cash with a number of reputable financial institutions. All cash and cash equivalents are short-term, highly liquid investments that are readily convertible into known amounts of cash.

The Bank's regulatory capital position was as follows:

| | 2018 | 2017 |
|--------------------------|---------|---------|
| | £'000 | £'000 |
| Share capital | 12,000 | 12,000 |
| Retained earnings | 8,069 | 8,198 |
| fair value reserve | 467 | 265 |
| Revaluation reserve | 6,820 | 6,184 |
| Less intangible assets | (1,386) | (1,459) |
| Total regulatory capital | 25,970 | 25,188 |

Note the figures above include changes in fair value and Revaluation reserves, as it has been audited. The actual capital returns submitted would have excluded these items at the time of submission.

Notes to the accounts

For the year ended 31 December 2018

The information in the table below does not form part of the audited financial statements.

| | 2018 | 2017 |
|---|---------------|----------------|
| | £'000 | £'000 |
| Capital surplus taking into account buffers | 7,145 | 3,326 |
| Risk weighted assets are: | | |
| | 2018 | 2017 |
| | £'000 | £'000 |
| Credit Risk | 87,558 | 103,983 |
| Operational Risk | 10,975 | 10,338 |
| FX Risk | - | 111 |
| Total risk weighted assets | 98,533 | 114,432 |

The Bank's main risk is credit risk arising from its loans to customers and placements in the money market. The Bank's main mitigation of credit risk is to secure the lending against real estate. The Bank does not use any risk models for regulatory risk, it adopts the standardised approach to determine risk weighted assets.

Notes to the accounts

For the year ended 31 December 2018

Analysis of financial assets and liabilities by measurement basis 2018

| | Loans and receivables | Fair value assets through OCI | Financial assets/ liabilities at amortised cost | Derivatives at fair value through profit & loss | Total |
|-------------------------------------|----------------------------------|--|--|--|--------------|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| Assets | | | | | |
| Cash and cash equivalents | - | - | 85,862 | - | 85,862 |
| Loans and advances to banks | - | - | 1,773 | - | 1,773 |
| Loans and advances to customers | - | - | 94,480 | - | 94,480 |
| Investment securities-OCI | - | 498 | - | - | 498 |
| Other assets | - | - | - | - | - |
| Total financial assets | - | 498 | 182,115 | - | 182,613 |
| Total non-financial assets | | | | | 11,760 |
| Total assets | | | | | 194,373 |
| Liabilities | | | | | |
| Deposits by banks | - | - | 18,854 | - | 18,854 |
| Customer accounts | - | - | 146,164 | - | 146,164 |
| Derivative liabilities | - | - | - | 78 | 78 |
| Other liabilities | - | - | 1,547 | - | 1,547 |
| Deferred tax liabilities | - | - | 374 | - | 374 |
| Total financial liabilities | - | - | 166,939 | 78 | 167,017 |
| Equity | | | | | 27,356 |
| Total liabilities and equity | | | | | 194,373 |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Analysis of financial assets and liabilities by measurement basis 2017

| | Loans and receivables £'000 | Available for sale £'000 | Financial assets/ liabilities at amortised cost £'000 | Derivatives at fair value through profit & loss £'000 | Total £'000 |
|--|-----------------------------------|--------------------------------|--|---|----------------|
| Assets | | | | | |
| Cash and cash equivalents | 63,088 | - | - | - | 63,088 |
| Loans and advances to banks | 1,772 | - | - | - | 1,772 |
| Loans and advances to customers | 98,532 | - | - | - | 98,532 |
| Investment securities- available for sale | - | 812 | - | - | 812 |
| Other assets | - | - | - | - | - |
| Total financial assets | 163,392 | 812 | - | - | 164,204 |
| Total non-financial assets | | | | | 13,399 |
| Total assets | | | | | 177,603 |
| Liabilities | | | | | |
| Deposits by banks | - | - | 3,138 | - | 3,138 |
| Customer accounts | - | - | 145,009 | - | 145,009 |
| Derivative liabilities | - | - | - | 50 | 50 |
| Other liabilities | - | - | 1,791 | - | 1,791 |
| Deferred tax liabilities | - | - | 332 | - | 332 |
| Total financial liabilities | - | - | 150,270 | 50 | 150,320 |
| Equity | | | | | 27,283 |
| Total liabilities and equity | | | | | 177,603 |

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Interest rate sensitivity gap analysis 2018

| | Less than 3 months £'000 | 3-6 months £'000 | 6-12 months £'000 | 1-5 years £'000 | More than 5 years £'000 | Non- interest bearing £'000 | Total £'000 |
|---------------------------------|--------------------------------|------------------------|-------------------------|--------------------|----------------------------------|--------------------------------------|----------------|
| Assets | | | | | | | |
| Cash and cash equivalents | 85,115 | - | - | - | - | 747 | 85,862 |
| Loans and advances to banks | - | - | 1,795 | - | - | (22) | 1,773 |
| Loans and advances to customers | 8,399 | 2,626 | 6,103 | 56,119 | 21,347 | (114) | 94,480 |
| Investment securities | - | - | - | - | - | 498 | 498 |
| Other assets | - | - | - | - | - | 11,760 | 11,760 |
| | <u>93,514</u> | <u>2,626</u> | <u>7,898</u> | <u>56,119</u> | <u>21,347</u> | <u>12,869</u> | <u>194,373</u> |
| Liabilities | | | | | | | |
| Deposits by banks | 18,854 | - | - | - | - | - | 18,854 |
| Customer accounts | 114,175 | 12,367 | 15,728 | 3,894 | - | - | 146,164 |
| Other liabilities | - | - | - | - | - | 1,999 | 1,999 |
| Shareholders' funds | - | - | - | - | - | 27,356 | 27,356 |
| | <u>133,029</u> | <u>12,367</u> | <u>15,728</u> | <u>3,894</u> | <u>-</u> | <u>29,355</u> | <u>194,373</u> |
| Interest rate sensitivity gap | (39,515) | (9,741) | (7,830) | 52,225 | 21,347 | (16,486) | - |
| Cumulative gap | (39,515) | (49,256) | (57,086) | (4,861) | 16,486 | - | - |

The table above provides only an indication of the sensitivity of the Bank's earnings to movements in interest rates and is consistent with the position throughout 2018.

Other assets are classified as non-interest bearing in the above table and have contractual maturities of less than three months.

The Bank had no outstanding financial guarantee contracts at the year-end (2017: £0).

Turkish Bank (UK) Limited

Notes to the accounts

For the year ended 31 December 2018

Interest rate sensitivity gap analysis 2017 (restated)

| | Less than 3 months £'000 | 3-6 months £'000 | 6-12 months £'000 | 1-5 years £'000 | More than 5 years £'000 | Non- interest bearing £'000 | Total £'000 |
|---------------------------------|-----------------------------------|---------------------|-------------------------|--------------------|----------------------------------|--------------------------------------|----------------|
| Assets | | | | | | | |
| Cash and cash equivalents | 62,313 | - | - | - | - | 775 | 63,088 |
| Loans and advances to banks | - | - | 1,772 | - | - | - | 1,772 |
| Loans and advances to customers | 64,088 | 11,648 | 22,931 | - | - | (135) | 98,532 |
| Investment securities | - | - | 500 | - | - | 312 | 812 |
| Other assets | - | - | - | - | - | 13,399 | 13,399 |
| | <u>126,401</u> | <u>11,648</u> | <u>25,203</u> | <u>-</u> | <u>-</u> | <u>14,351</u> | <u>177,603</u> |
| Liabilities | | | | | | | |
| Deposits by banks | 3,138 | - | - | - | - | - | 3,138 |
| Customer accounts | 111,358 | 13,384 | 14,022 | 6,245 | - | - | 145,009 |
| Derivative liabilities | - | - | - | - | - | - | - |
| Other liabilities | - | - | - | - | - | 2,173 | 2,173 |
| Shareholders' funds | - | - | - | - | - | 27,283 | 27,283 |
| | <u>114,496</u> | <u>13,384</u> | <u>14,022</u> | <u>6,245</u> | <u>-</u> | <u>29,456</u> | <u>177,603</u> |
| Interest rate sensitivity gap | 11,905 | (1,736) | 11,181 | (6,245) | - | (15,105) | - |
| Cumulative gap | 11,905 | 10,169 | 21,350 | 15,105 | 15,105 | - | - |

The table above provides only an indication of the sensitivity of the Bank's earnings to movements in interest rates and is consistent with the position throughout 2017.

Other liabilities are classified as non-interest bearing in the above table and have contractual maturities of less than three months.

A liability (negative) gap position exists when liabilities re-price more quickly than assets during a given period and tends to benefit net interest income in a declining interest rate environment. An asset (positive) gap position exists when assets reprice more quickly than liabilities during a given period and tends to benefit interest income in a rising interest rate environment. The Bank's off balance sheet items carry no interest rate risk. Loans and advances to customers are shown net of provisions totalling £114,000 (2017: £135,000).

The weighted average interest rates are as follows: 1.19% (2017: 0.95%) for the loans and advances to banks; 4.85% (2017: 4.86%) for the loans and advances to customers; 9.38% (2017: 10.04%) for the debt securities; 0.08% (2017: 0.07%) for the deposits by banks; and 1.27% (2017: 1.20%) for the customer accounts.

Interest rate sensitivity analysis

The sensitivity analysis has been determined based on the exposure to interest rate fluctuation for both derivative and non-derivative instruments at the balance sheet date. At reporting date, if interest rate had been 200 basis points higher/lower and all other variables were held constant the Bank's net profit would decrease/increase by £330,000. As at 31 December 2017 the average impact of 200 basis point movement in interest rates was £302,000. However, management believes that Bank interest rate risk is limited since the majority of customers' deposits are repriced within three months as per the terms of their issue.

Notes to the accounts

For the year ended 31 December 2018

36. Post Balance Sheet Events

Please see Note 2. (a) for the evaluation of Brexit on the Bank, which is expected to be insignificant. There are no other significant post balance sheet events.