

## INDEPENDENT AUDITOR'S REPORT

To the General Assembly of Türkiye Halk Bankası A.Ş.

### A) Report on the Audit of the Financial Statements

#### 1) Qualified Opinion

We have audited the financial statements of Türkiye Halk Bankası A.Ş. (“the Bank”), which comprise the balance sheet as at 31 December 2018, and the statement of income, statement of income and expense items accounted for under shareholders’ equity, statement of changes in shareholders’ equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, except for the effect of the matters on the unconsolidated financial statements described in the basis for the qualified opinion paragraph, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with “the Banking Regulation and Supervision Agency (“BRSA”) Accounting and Reporting Regulations” including the regulation on “The Procedures and Principles Regarding Banks’ Accounting Practices and Maintaining Documents” published in the Official Gazette dated 1 November 2006 with No. 26333, and other regulations on accounting records of banks published by the Banking Regulation and Supervision Board and circulars and pronouncements published by the BRSA and provisions of Turkish Financial Reporting Standards (TFRS) for the matters not legislated by the aforementioned regulations.

#### 2) Basis for Qualified Opinion

The accompanying unconsolidated financial statements as at 31 December 2018, include a general reserve amounting to TRY 414.000 thousand, provided by the Bank management in the current period for the possible result of the negative circumstances which may arise from any changes in the economy or market conditions. If such general provision was not provided, as at 31 December 2018, other provisions would decrease by TRY 414.000 thousand and net profit would increase by TRY 414.000 thousand.

The Bank reclassified the government bonds amounting to TRY 18.965.006 thousand, which were previously classified under financial assets at fair value through other comprehensive income according to the business model prepared in accordance with Turkish Financial Reporting Standard (“TFRS”) 9, into financial assets measured at amortised cost and reversed the marketable securities revaluation fund accumulated under other comprehensive income or loss to be reclassified through profit or loss amounting to TRY 2.229.977 thousand on 23 May 2018. The reclassification constitutes a departure from TFRS 9. The government bonds reclassified into financial assets measured at amortised cost amounted to TRY 17.904.805 thousand as at 31 December 2018. If such reclassification were not made, total assets and shareholders’ equity excluding tax effect would be lower by TRY 2.597.814 thousand as at 31 December 2018.

We conducted our audit in accordance with the regulation on “Independent Auditing of Banks” published in the Official Gazette dated 2 April 2015 with No. 29314 and Standards on Independent Auditing (“SIA”) which is a part of Turkish Auditing Standards published by the Public Oversight Accounting and Auditing Standards Authority (“POA”). 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 *Code of Ethics for Independent Auditors* (“Code of Ethics”) published by the POA, together with the ethical requirements that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

**3) Emphasis of Matter**

As detailed in Section 6 Note 1, one of the Bank’s former directors has been convicted and imprisoned for some of the charges by the court in the United States of America (“USA”) of the violation of the USA sanctions involving Iran as of 16 May 2018. The subsequent legal process is not yet completed but ongoing for the defendant former director of the Bank such as appeal and other legal rights following the first phase of the trial.

The Bank is not a trialist or defendant in this case. The respective court in this trial has not issued any administrative or monetary decision against the Bank. The Bank is also closely following this trial by hiring external legal counsel resident in the USA.

Separate from this trial, there is an uncertainty of any negative decisions by the USA authorities against the Bank affecting its financial position, if any. The Bank’s management indicated that there are no enforcement or other actions against the Bank at this stage. No provision has been made in the accompanying financial statements related to this matter. Our conclusion is not modified in respect of this matter.

**4) Key Audit Matters**

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. 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.

Key Audit Matter	How the matter was addressed in the audit
<p><b><i>Impairment of loans in accordance with TFRS 9</i></b></p> <p>Impairment of loans is a key area of judgement for the management. The Bank has the total loans and receivables amounting to TRY 250.623.713 thousands, which comprise 66% of the Bank’s total assets in its unconsolidated financial statements and the total provision for</p>	<p>As part of our audit work, the following procedures were performed:</p> <p>We assessed and tested the design, implementation and operating effectiveness of key controls applied by the Bank with respect to classification of</p>

impairment amounting to TRY 8.450.513 as at 31 December 2018.

As of 1 January 2018, the Bank has started to recognize provisions for impairment in accordance with the TFRS 9 requirements according to the “Regulation on the Procedures and Principles for Classification of Loans by Banks and Provisions to be set aside” published in the Official Gazette dated 22 June 2016 numbered 29750. In this respect, as of 31 December 2017, the method of provisions for impairment as set out in accordance with the related legislation of BRSA as mentioned in the Section 3 Note XXIII of Explanation on Accounting Policies has been changed by applying the expected credit loss model under TFRS 9. The expected credit loss estimates are required to be unbiased, probability-weighted and should include supportable information about past events, current conditions, and forecasts of future economic conditions.

The Bank exercises significant decisions using judgement, interpretation and assumptions over calculating loan impairments. These judgements, interpretations and assumptions are key in the development of the financial models built to measure the expected credit losses on loans.

There is a potential risk of impairment losses/provisions provided/will be provided may not meet the requirements of the TFRS 9. Failure in determining the loans and receivables that are impaired and not recording the adequate provision for these impaired loans is the aforementioned risk. Accordingly, impairment of loans is considered as a key audit matter.

Related explanations relating to the impairment of loans and receivables are presented in Section 5 Note I.5.

loans and determination and calculation of impairments. Our information system experts have also participated to perform these procedures.

We have read and analysed the relevant contract terms to assess management’s accounting policy and classification of the instrument for selected samples.

We have performed loan review procedures on selected samples of loans and receivables with the objective of identifying whether the loss event had occurred and whether the provision for impairment has been recognized in a timely manner within the framework of the provisions of the relevant legislation.

We have tested relevant inputs and assumption used by the management in each stage of the expected credit loss calculation by considering whether the inputs and assumptions appear reasonable, the relationship between the assumptions and whether the assumptions are interdependent and internally consistent, whether the assumptions appropriately reflect current market information and collections, and whether the assumptions appear reasonable when considered collectively with other assumptions, including those for the same accounting estimates and those for other accounting estimates.

We have tested historical loss data to validate the completeness and accuracy of key parameters.

We have tested whether the model is applied to appropriate groupings of assets which share credit risk characteristics and whether the historical loss rates were incurred under economic conditions representative of those that may exist during the assets’ exposure periods.

We tested the application of the model to the relevant inputs and the mathematical

	<p>integrity of each stage of the expected credit loss calculation.</p> <p>Based on our discussions with the Bank management, we evaluated whether the key assumptions and other judgements underlying the estimations of impairments were reasonable.</p> <p>Our specialists are involved in all procedures related to models and assumptions.</p> <p>We have reviewed disclosures made within the TFRS 9 framework in the financial statements of the Bank with respect to loans and receivables and related impairment provisions.</p>
<p><b>Key Audit Matter</b></p>	<p><b>How the matter was addressed in the audit</b></p>
<p><i><b>First time adaptation of TFRS 9 Financial Instruments Standard</b></i></p> <p>As of 1 January 2018, the Bank started to recognize provisions for impairment in accordance with the TFRS 9 requirements according to the “Regulation on the Procedures and Principles for Classification of Loans by Banks and Provisions to be set aside” published in the Official Gazette dated 22 June 2016 numbered 29750. TFRS 9 standard introduced significant changes in accounting policies and required adjustments to be made to the amounts previously recognized in accordance with the transition rules.</p> <p>For the first time adoption of TFRS 9, the Bank included more significant estimates and judgments in determining the business model and the cash flows characteristics of contracts. Since the Bank had a fundamental change in its financial reporting framework and had an impact on many significant financial statement line-items, the first time adoption of TFRS 9 has been considered as a key audit matter.</p> <p>Explanations on the equity effects of TFRS 9 transition are disclosed in Section 3 Note VI.</p>	<p>Our audit work included the following procedures:</p> <p>The Bank's IFRS 9 policy of the classification of financial assets and financial liabilities has been read and compared with the requirements of TFRS 9.</p> <p>The Bank's contractual cash flows tests for its financial instruments have been reviewed, its criteria and results have been evaluated.</p> <p>The appropriateness of the opening balance adjustments and the disclosures presented were checked.</p> <p>The procedures applied for the expected credit losses are set out in the key audit matter related to the “Impairment of loans in accordance with TFRS 9” above.</p>

Key Audit Matter	How the matter was addressed in the audit
<p><b><i>Valuation of Pension Fund Obligations</i></b></p> <p>Defined benefit pension plan that the Bank provides to its employees is managed by Türkiye Halk Bankası AŞ Emekli Sandığı Vakfı and T.C. Ziraat Bankası ve T. Halk Bankası Çalışanları Emekli Sandığı Vakfı (“Plan”) which were established by the 20th provisional article of the Social Security Law numbered 506 (the “Law”).</p> <p>As disclosed in the Section III Note XVI to the unconsolidated financial statements, the Plan is composed of benefits which are subject to transfer to the Social Security Foundation (“SSF”) as per the Social Security Law no.5510 provisional article 20, and other social rights and pension benefits provided by the Bank that are not transferable to the SSF. The Council of Ministers has been authorized to determine the transfer date. Following the transfer, the funds and the institutions that employ the funds’ members will cover the non-transferable social rights and pension benefits provided under the Plan even if it is included in foundation voucher.</p> <p>As of 31 December 2018, the Bank’s transferrable liabilities are calculated by an independent actuary using the actuarial assumptions regulated by the Law, and in accordance with the Decision of the Council of Ministers announced in the Official Gazette dated 15 December 2006 and No.26377. The valuation of the Plan liabilities requires judgment in determining appropriate assumptions such as defining the transferrable social benefits, discount rates, salary increases, inflation levels, demographic assumptions, and the impact of changes in the Plan. Management uses expert opinion of the independent actuary in assessing uncertainties related to these underlying assumptions and estimates.</p> <p>As described in Section V Note II.9.f considering the subjectivity of key judgments and assumptions, plus the uncertainty around</p>	<p>Our audit work included the following procedures:</p> <p>We involved external experts (actuary) in our audit team to evaluate the assumptions used in the calculation of the pension obligations and the appropriateness of the estimates.</p> <p>It has been tested whether the plan assets meet plan obligations in accordance with the methods and assumptions used.</p> <p>In addition, reconciliations and tests were carried out through sampling of the accuracy of the data provided to the Bank’s actuary.</p> <p>We have assessed whether there is a significant change in the actuarial assumptions, methods, legal regulations and legislation used in the calculations and whether the assumptions are reasonable.</p>

<p>the transfer date and basis of the transfer calculation given the fact that the technical interest rate is prescribed under the Law, we considered this as a key audit matter.</p>	
<p><b>Key Audit Matter</b></p>	<p><b>How the matter was addressed in the audit</b></p>
<p><b><i>Information Technologies Audit</i></b></p> <p>The Bank and its finance functions are dependent on the IT-infrastructure for the continuity of its operations, and the demand for technology-enabled business services is rapidly growing in the Bank and its subsidiaries. Controls over reliability and continuity of the electronic data processing are within the scope of the information systems internal controls audit. The reliance on information systems within the Bank means that the controls over access rights, continuity of systems, privacy and integrity of the electronic data are critical and found to be key area of focus as part of our risk based scoping.</p>	<p>Procedures within the context of our information technology audit work:</p> <p>We identified and tested the Banks' controls over information systems as part of our audit procedures.</p> <p>Information generation comprise all layers of information systems including applications, networks, transmission systems and database. The information systems controls tested are categorized in the following areas:</p> <ul style="list-style-type: none"> <li>• Manage security</li> <li>• Manage changes</li> <li>• Manage operations</li> </ul> <p>We selected high-risk areas as, database logging and change management control activities, to prevent and detect whether accesses to financial data had been identified in a timely manner.</p> <p>We tested the accesses and logging controls underlying all applications that have direct or indirect impacts on financial data generation.</p> <p>Automated controls and integration controls are tested to underly and detect changes and accesses in the process of financial data generation.</p> <p>We also tested the appropriateness and accuracy of the information produced by the entity and information used in controls reports as inputs to our controls and outputs generated by the IT components.</p>

	Finally, we understood and tested the controls over database, network, application and operating system layers of applications.
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## **5) Responsibilities of Management and Those Charged with Governance for the Financial Statements**

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the BRSA Accounting and Reporting Regulations, and for such internal control as management determines 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, management is 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 management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

## **6) Auditor's Responsibilities for the Audit of the Financial Statements**

Responsibilities of independent auditors in an independent audit are as follows:

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 the regulation on "Independent Auditing of Banks" published in the Official Gazette dated 2 April 2015 with No. 29314 and SIA 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.

As part of an audit in accordance with the regulation on "Independent Auditing of Banks" published in the Official Gazette dated 2 April 2015 with No. 29314 and SIA, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

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

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor’s report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

## **B) Report on Other Legal and Regulatory Requirements**

In accordance with paragraph four of the Article 402 of the Turkish Commercial Code No. 6102 (“TCC”), nothing has come to our attention that may cause us to believe that the Bank’s set of accounts for the period 1 January-31 December 2018 does not comply with the TCC and the provisions of the Bank’s articles of association in relation to financial reporting.

In accordance with paragraph four of the Article 402 of the TCC, the Board of Directors provided us all the required information and documentation with respect to our audit.

The engagement partner on the audit resulting in this independent auditor’s report is Hasan Kılıç.

## **Additional Paragraph for English Translation**

The effect of the differences between the accounting principles summarized in Section 3 and the accounting principles generally accepted in countries in which the accompanying financial



statements are to be distributed and International Financial Reporting Standards (“IFRS”) have not been quantified and reflected in the accompanying financial statements. The accounting principles used in the preparation of the accompanying financial statements differ materially from IFRS. Accordingly, the accompanying financial statements are not intended to present the Bank’s financial position and results of its operations in accordance with accounting principles generally accepted in such countries of users of the financial statements and IFRS.

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

Hasan Kılıç  
Partner

İstanbul, 14 February 2019