Contents

KT&G CORPORATION AND SUBSIDIARIES

Review Report on Consolidated Interim Financial Statements

First quarter of the 32nd Fiscal Year
From January 1, 2018 to March 31, 2018

Deloitte Anjin LLC.

Independent Auditors' Review Report

To the Shareholders and Board of Directors of KT&G CORPORATION

Reviewed financial statements

We have reviewed the accompanying condensed consolidated interim financial statements of KT&G Corporation and subsidiaries expressed in Korean won, which comprise the condensed consolidated interim statements of financial position as of March 31, 2018, and the condensed consolidated interim statements of comprehensive income for the three-month period ended at March 31, 2018, consolidated condensed interim statements of cash flows and condensed consolidated interim statements of changes in equity for the quarters then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility

Management is responsible for the preparation and fair presentation of these condensed consolidated interim financial statements in accordance with Korean International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of condensed consolidated interim financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these condensed consolidated interim financial statements based on our review.

We conducted our review in accordance with the Korean Standards on reviewing the interim and semi-annual financial statements. The review is conducted primarily by analytical procedures and other review procedures as well as questions to treasurers and accountants. In addition, the review is much limited in the range when compared to the full-scale audits that are performed in accordance with auditing standards, and such procedures do not ensure that the auditor will be aware of all significant issues that would have been identified in the audit. Therefore, We do not express my opinion.

Review results

As a result of the review, We have not found any material items that are not fairly stated in terms of materiality in accordance with K-IFRS No. 1034 'Interim Financial Reporting'.

Other matters

KT&G Corporation and subsidiaries's comparative condensed consolidated statements of comprehensive income for the three-month period ended at March 31, 2017, comparative condensed consolidated statements of cash flows and comparative condensed consolidated statements of changes in equity for the quarters then ended were reviewed by KPMG Samjung Accounting Corporation, whose review report dated May 15, 2017 stated that no unfairly-presented item was found in these financial statements, in all material respects, in terms of the K-IFRS No.1034 'Interim Financial Reporting'.

The statements of financial position as of December 31, 2017, the statements of comprehensive income, the statement of changes in equity and the statement of cash flows (not included in this review) for the year ended March 31, 2017 were audited in accordance with the Korean Auditing Standards by the KPMG Samjong Accounting Corporation, which expressed its opinion on the audit report dated February 28, 2018. The accompanying statement of financial position as of December 31, 2017, presented for comparative purposes, does not differ from the above audited statements of financial position with respect to materiality.

10, Gukjegeumyung-ro, Yeongdeungpo-gu, Seoul

Lee Jung Hee, CEO of Anjin Deloitte LLC

May 15, 2018

Notice to Readers

This report is effective as of the review report date (May 15, 2018). Certain subsequent events or circumstances, which may occur between the review report date and the time of reading this report, could have a material impact on the accompanying condensed consolidated financial statements and notes thereto. Accordingly, the readers of the review report should understand that the above review report has not been updated to reflect the impact of such subsequent events or circumstances, if any.

Accompanying Consolidated Interim Financial Statements

KT&G CORPORATION AND SUBSIDIARIES

First quarter of the 32nd Fiscal Year
From January 1, 2018 to March 31, 2018

First quarter of the 31st Fiscal Year
From January 1, 2017 to March 31, 2017

"The consolidated interim financial statements attached have been prepared by our company."
CEO of KT&G Corporation, Baek Bok In

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(Telephone) 080-931-0399

Condensed Consolidated Interim Statements of Financial Position

First quarter of the 32nd Fiscal Year As of March 31, 2018

Full year of the 31st Fiscal Year As of December 31, 2017

KT&G CORPORATION AND SUBSIDIARIES Korean won

Accounts	Notes	As of March 31, 2018	As of December 31, 2017
Assets:			
Current assets:			
Cash and cash equivalents	5,33,34,37	1,099,779,311,573	1,230,175,789,096
Current other financial assets	5,17,33,34,35,37	222,090,144,365	1,563,899,746,161
Current term's profit and loss-Fair value of financial asset	6,33,37	1,646,189,381,254	–
Trade and other receivables	8,33,37	1,078,658,853,033	1,126,906,681,740
Financial derivatives	7,33	6,005,977,646	–
Inventories	9	2,258,209,012,375	2,317,466,486,017
Refund asset	21	673,719,196	–
Accrued tobacco excise and other taxes		248,404,144,156	261,458,634,993
Advance payments	35	65,270,505,346	59,174,970,582
Prepaid expenses		38,024,912,782	26,315,942,164
Total current assets		6,663,305,961,726	6,585,398,250,753
Non-current assets:			
Other long-term financial assets	5,17,33,37	16,347,597,000	6,350,597,000
Long-term deposits in MSA Escrow Fund	10,33,37	532,239,901,288	510,223,375,080
Current term's profit and loss-Fair value of financial asset	6,33,37	178,911,045,579	–
Other comprehensive profit and loss-Fair value of financial asset	11,33,37	278,488,076,635	–
Long-term trade and other receivables	8,33,37	62,455,829,902	63,687,114,014
Available-for-sale financial assets	4,11,33,37	–	471,762,743,361
Investments in associates and joint ventures	12	50,979,411,763	51,030,988,219
Property, plant and equipment	13,17	1,666,269,882,287	1,756,979,126,818
Intangible assets	14,16	85,563,976,262	84,747,974,375
Investment property	15,17	439,218,210,364	330,998,857,548
Refund asset	21	472,062,058	–
Long-term advance payments		69,779,705,697	69,773,731,927
Long-term prepaid expenses		5,150,628,962	5,547,561,711
Deferred income tax assets	30	37,972,531,445	39,405,222,139
Total non-current assets		3,423,848,859,242	3,390,507,292,192
Total assets		10,087,154,820,968	9,975,905,542,945
Equity and liabilities:			
Liabilities:			

Current liabilities:			
Short-term borrowings	17,18,33,34	50,235,114,647	174,656,638,008
Current portion of long-term borrowings	17,18,33,34	4,410,646,400	3,702,326,400
Trade and other payables	19,33	1,024,165,295,319	523,299,592,457
Advance receipts		6,138,183,361	6,823,287,073
Current provision	21	10,687,788,851	2,969,527,177
Income tax payable	30	248,743,120,448	175,149,546,607
Tobacco excise and other taxes payable		883,000,097,575	916,397,793,192
Total current liabilities		2,227,380,246,601	1,802,998,710,914
Non-current liabilities:			
Long-term borrowings	17,18,33,34	99,314,559,200	100,588,590,400
Long-term trade and other receipts	19,33	35,998,233,793	34,436,148,465
Long-term advance receipts		9,917,945,013	10,826,615,063
Net defined benefit liability	20	87,683,889,233	75,782,588,379
Provision	21	8,253,475,607	13,363,453,237
Deferred income tax liabilities	30	119,259,899,880	108,149,068,670
Total non-current liabilities		360,428,002,726	343,146,464,214
Total liabilities		2,587,808,249,327	2,146,145,175,128
Equity			
Ordinary shares	22	954,959,485,000	954,959,485,000
Other capital surplus	22	(29,719,795,353)	(29,719,795,353)
Treasury shares	23	(328,157,286,128)	(328,157,286,128)
Gain on sales of treasury shares	23	513,775,933,891	513,775,933,891
Reserve	24	5,358,855,144,578	4,927,331,928,515
Retained earnings	25	971,456,050,805	1,733,863,414,006
Equity attributable to owners of the parent		7,441,169,532,793	7,772,053,679,931
Non-controlling interests		58,177,038,848	57,706,687,886
Total equity		7,499,346,571,641	7,829,760,367,817
Total liabilities and equity		10,087,154,820,968	9,975,905,542,945

"The accompanying notes are a part of the condensed consolidated interim financial statements."

Condensed Consolidated Interim Statements of Comprehensive Income
From January 1, 2018 to March 31, 2018
From January 1, 2017 to March 31, 2017

KT&G CORPORATION AND SUBSIDIARIES Korean won

Accounts	Notes	For the Three-Month Period Ended March 31, 2018	For the Three-Month Period Ended March 31, 2017
Sales	4,26,37	1,067,590,374,238	1,178,747,511,091
Cost of sales	9,26,27	(433,470,398,353)	(478,122,186,754)
Gross profit		634,119,975,885	700,625,324,337
Selling, general and administrative expenses	16,27	(322,751,601,083)	(305,294,310,419)
Operating profit	4,16,27	311,368,374,802	395,331,013,918
Other income	28	35,896,988,385	16,423,967,191
Other expenses	9,28	(20,333,789,621)	(102,001,813,609)
Finance income	6,29,33	35,594,836,892	22,000,505,963
Cost of finance	6,29,33	(2,669,999,708)	(1,533,314,392)
Net finance income	29	32,924,837,184	20,467,191,571
Share of gain of associates and joint ventures for the quarter	12	–	1,469,156,141
Share of loss of associates and joint ventures for the quarter	12	(51,576,456)	(5,595,754)
Profit before income tax		359,804,834,294	331,683,919,458
Income tax expense	30	(110,436,052,951)	(96,647,665,821)
Profit for the quarter		249,368,781,343	235,036,253,637
Other comprehensive income (loss) after income tax:			
Items that are not reclassified subsequently to profit or loss			
Remeasurements of net defined benefit liability, net of tax	20	(1,066,485,586)	(591,457,603)
Other comprehensive income (loss)-Valuation of profit and loss of fair value of financial asset		(6,929,090,849)	–
Others that can be reclassified subsequently to profit and loss			
Exchange differences on translating foreign operations, net of tax		(9,817,470,948)	(5,051,957,707)
Unrealized net changes in fair value of available-for-sale financial assets, net of tax	33	–	5,085,279,164
Other comprehensive profit after income tax		(17,813,047,383)	(558,136,146)
Total comprehensive income for the quarter		231,555,733,960	234,478,117,491
Profit attributable to:			
Owners of the parent company		248,897,226,618	234,383,106,470
Non-controlling interests		471,554,725	653,147,167
Total		249,368,781,343	235,036,253,637
Other comprehensive profit for the quarter attributable to:			
Owners of the parent company		231,085,382,998	230,885,311,548
Non-controlling interests		470,350,962	3,592,805,943
Total		231,555,733,960	234,478,117,491
Earnings per share:			
Basic and diluted	31	1,971	1,856

“The accompanying notes are a part of the condensed consolidated interim financial statements.”

Condensed Consolidated Interim Statements of Changes in Equity

From January 1, 2018 to March 31, 2018

From January 1, 2017 to March 31, 2017

KT&G CORPORATION AND SUBSIDIARIES — Korean won

Accounts	Ordinary shares	Other capital surplus (deficit)	Treasury shares	Gains on sales of treasury shares	Reserve	Retained earnings	Owners of the parent	Non-controlling interests	Total equity
Balance at January 1, 2017	954,959,485,000	(3,428,862,637)	(328,157,286,128)	513,775,933,891	4,296,522,940,448	1,611,532,365,941	7,045,204,576,515	72,553,715,968	7,117,758,292,483
Total comprehensive income (loss) for the quarter:									
Profit for the quarter	–	–	–	–	–	234,383,106,470	234,383,106,470	653,147,167	235,036,253,637
Other comprehensive income (loss) for the quarter:									
—Re-measurements of net defined benefit liability, net of tax	–	–	–	–	–	(590,159,784)	(590,159,784)	(1,297,819)	(591,457,603)
—Unrealized net changes in fair value of available-for-sale financial assets, net of tax	–	–	–	–	5,085,279,164	–	5,085,279,164	–	5,085,279,164
—Exchange differences on translating foreign operations, net of tax	–	–	–	–	(7,992,914,302)	–	(7,992,914,302)	2,940,956,595	(5,051,957,707)
Sum of other comprehensive profit (loss) for the quarter	–	–	–	–	(2,907,635,138)	(590,159,784)	(3,497,794,922)	2,939,658,776	(558,136,146)
Other comprehensive profit (loss) for the quarter	–	–	–	–	(2,907,635,138)	233,792,946,686	230,885,311,548	3,592,805,943	234,478,117,491
Transactions with owners, recognized directly in equity:									
Dividends	–	–	–	–	–	(454,554,457,200)	(454,554,457,200)	–	(454,554,457,200)
Transfer from reserve for research and human resource development	–	–	–	–	(10,000,000,000)	10,000,000,000	–	–	–
Transfer to unconditional reserve	–	–	–	–	623,914,622,466	(623,914,622,466)	–	–	–
Changes in non-controlling interests and others	–	(26,286,574,854)	–	–	–	–	(26,286,574,854)	(18,866,308,756)	(45,152,883,610)
Total transactions with owners of the parent company	–	(26,286,574,854)	–	–	613,914,622,466	(1,068,469,079,666)	(480,841,032,054)	(18,866,308,756)	(499,707,340,810)
Balance at March 31, 2017	954,959,485,000	(29,715,437,491)	(328,157,286,128)	513,775,933,891	4,907,529,927,776	776,856,232,961	6,795,248,856,009	57,280,213,155	6,852,529,069,164
Balance at January 1, 2018	954,959,485,000	(29,719,795,353)	(328,157,286,128)	513,775,933,891	4,927,331,928,515	1,733,863,414,006	7,772,053,679,931	57,706,687,886	7,829,760,367,817
Effect of change in accounting policy	–	–	–	–	(36,765,729,396)	(20,143,292,740)	(56,909,022,136)	–	(56,909,022,136)
Balance at January 1, 2018 (basic after revision)	954,959,485,000	(29,719,795,353)	(328,157,286,128)	513,775,933,891	4,890,566,199,119	1,713,720,121,266	7,715,144,657,795	57,706,687,886	7,772,851,345,681
Total comprehensive income (loss):									
Profit for the quarter	–	–	–	–	–	248,897,226,618	248,897,226,618	471,554,725	249,368,781,343
Other comprehensive profit (loss) for the quarter:									
—Remeasurements of net defined benefit liability, net of tax	–	–	–	–	–	(1,065,281,823)	(1,065,281,823)	(1,203,763)	(1,066,485,586)
—Other comprehensive profit (loss)-Valuation profit and loss of fair value of financial asset	–	–	–	–	(6,929,090,849)	–	(6,929,090,849)	–	(6,929,090,849)
—Exchange differences on translating foreign operations, net of tax	–	–	–	–	(9,817,470,948)	–	(9,817,470,948)	–	(9,817,470,948)
Sum of other comprehensive profit (loss) for the quarter	–	–	–	–	(16,746,561,797)	(1,065,281,823)	(17,811,843,620)	(1,203,763)	(17,813,047,383)
Total comprehensive profit (loss) for the quarter	–	–	–	–	(16,746,561,797)	247,831,944,795	231,085,382,998	470,350,962	231,555,733,960
Transactions with owners, recognized directly as equity:									
Dividends	–	–	–	–	–	(505,060,508,000)	(505,060,508,000)	–	(505,060,508,000)
Transfer from reserve for research and human resource development	–	–	–	–	(10,000,000,000)	10,000,000,000	–	–	–
Transfer to unconditional reserve	–	–	–	–	495,035,507,256	(495,035,507,256)	–	–	–
Total transactions with owners of the parent company	–	–	–	–	485,035,507,256	(990,096,015,256)	(505,060,508,000)	–	(505,060,508,000)
Balance at March 31, 2018	954,959,485,000	(29,719,795,353)	(328,157,286,128)	513,775,933,891	5,358,855,144,578	971,456,050,805	7,441,169,532,793	58,177,038,848	7,499,346,571,641

“The accompanying notes are a part of the condensed consolidated interim financial statements.”

Condensed Consolidated Interim Statements of Cash Flows

From January 1, 2018 to March 31, 2018

From January 1, 2017 to March 31, 2017

KT&G CORPORATION AND SUBSIDIARIES | Korean won

Accounts	Notes	For the Three-Month Period Ended March 31, 2018	For the Three-Month Period Ended March 31, 2017
Cash flows from operating activities			
Cash generated from operations	36	383,004,783,138	(131,061,039,993)
Income tax paid		(21,549,146,652)	(90,397,412,682)
Net cash provided by operating activities		361,455,636,486	(221,458,452,675)
Cash flows from investing activities	36		
Interest received		2,283,942,913	12,581,841,216
Dividends received		2,513,852,149	2,453,845,496
Proceeds from sale of property, plant and equipment		878,709,211	700,680,752
Proceeds from sales of intangible assets		484,000	1,440,000,000
Current term's profit and loss-Proceeds from fair value of financial assets		6,573,920,518	–
Other comprehensive profit and loss-Proceeds from fair value of financial assets		90,000	–
Collection of loans		3,577,351,647	3,629,100,837
Withdrawal of guarantee deposits		9,584,156,263	9,209,259,620
Acquisition of property, plant and equipment		(59,351,012,716)	(89,378,559,187)
Acquisition of intangible assets		(1,941,166,624)	(1,743,836,816)
Acquisition of investments in associates and joint ventures		–	(42,091,811,555)
Acquisition of available-for-sale financial assets		–	(5,380,000,000)
Other comprehensive profit and loss-Acquisition of fair value of financial assets		(450,000,000)	–
Increase in loans		(21,330,000)	(29,772,225)
Payments of guarantee deposits		(14,160,128,321)	(14,495,173,483)
Payments of long-term deposits in MSA Escrow Fund		(15,193,216,594)	(19,708,798,616)
Increase in other financial assets, net		(302,270,028,733)	751,592,031,481
Changes in consolidation		–	(5,856,678,366)
Net cash used in investing activities		(367,974,376,287)	602,922,129,154
Cash flows from financing activities	36		
Proceeds from borrowings		168,168,807,230	145,112,838,462
Increase in deposits received		1,926,071,000	4,167,462,400
Payments of share issuance cost		–	(22,990,233)
Interest paid		(833,845,174)	(1,573,494,145)
Payments of borrowings		(288,664,710,211)	(262,096,265,344)
Decrease in deposits received		(4,442,649,323)	(601,471,794)
Net cash used in financing activities		(123,846,326,478)	(115,013,920,654)
Net increase in cash and cash equivalents		(130,365,066,279)	266,449,755,825
Cash and cash equivalents at January 1		1,230,175,789,096	850,786,228,377
Effect of exchange rate fluctuation on cash held		(31,411,244)	2,430,955,608
Cash and cash equivalents at March 31		1,099,779,311,573	1,119,666,939,810

"The accompanying notes are a part of the condensed consolidated interim financial statements."

Notes

From January 1, 2018 to March 31, 2018
From January 1, 2017 to March 31, 2017
KT&G CORPORATION AND SUBSIDIARIES

1. Organization and Description of Business

(1) Description of the Controlling Company

KT&G Corporation (the "Parent Company"), which is engaged in manufacturing and selling tobaccos, was established on April 1, 1987, as Korea Monopoly Corporation, a wholly owned enterprise of the Korean government, pursuant to the Korea Monopoly Corporation Act in order to secure financing and to promote and develop, through efficient management, the monopoly business of red ginseng and tobacco.

On April 1, 1989, the Parent Company changed its name to Korea Tobacco and Ginseng Corporation pursuant to the Korea Tobacco and Ginseng Corporation Act. Also, pursuant to the Act on Management Reform and Privatization of Public Enterprises, proclaimed on August 28, 1997, and enforced on October 1, 1997, the Parent Company was excluded from the application of the Act for the Management of Government Invested Enterprises. Accordingly, the Parent Company became an entity existing and operating under the Commercial Act of Korea. The Korean government sold 28,650,000 shares of the Parent Company to the public during 1999, and the Parent Company listed its shares on the Korea Exchange on October 8, 1999. On December 27, 2002, the Parent Company changed its name again to KT&G Corporation from Korea Tobacco and Ginseng Corporation.

As of March 31, 2018, the Parent Company has three manufacturing plants, including the Shintanjin plant, and 14 local headquarters and 123 branches for the sale of tobacco throughout the country. Also, the Parent Company has the Gimcheon plant for fabrication of leaf tobacco and the Cheonan printing plant for the manufacturing of packaging material. The headquarters of the Parent Company is located at 71, Beotkkot-gil, Daedeok-gu, Daejeon.

Pursuant to the Korean government's privatization program and management reorganization plan, on December 28, 1998, the shareholders approved a plan to separate the Parent Company into two companies by setting up a subsidiary for its red ginseng business segment effective January 1, 1999. The separation into a wholly owned subsidiary, Korea Ginseng Corporation, was accomplished by the Parent Company's contribution of the assets and liabilities in the red ginseng business segment.

On October 17, 2002, and October 31, 2001, the Parent Company listed 35,816,658 and 45,400,000 Global Depositary Receipts ("GDRs"), respectively, (each GDR representing the right to receive one-half share of an ordinary share of the Parent Company) on the Luxembourg Stock Exchange pursuant to the Korean government's privatization program. Also, on June 25, 2009, the listing market of the Parent Company's GDR was changed from the BdL market to the Euro MTF in the Luxembourg Stock Exchange.

The ownership of the Parent Company's issued ordinary shares as of the end of the current term is held as follows

Type	Number of shares	Percentage of ownership
National Pension Service	13,191,374	9.61%
Industrial Bank of Korea	9,510,485	6.93%
Employee Share Ownership Association	2,927,745	2.13%
Treasury shares	11,027,370	8.03%
Others	100,635,523	73.30%
Total	137,292,497	100.00%

(2) Consolidated Subsidiaries

The list of consolidated subsidiaries as of March 31, 2018, is as below.

Next most senior partner	Subsidiary	Principal operation	Percentage of ownership	Reporting date	Location
The Parent Company	Korea Ginseng Corporation	Manufacturing and selling ginseng	100.00%	2018.03.31	Korea
	Yungjin Pharm. Co., Ltd.	Manufacturing and selling pharmaceuticals	52.45%	2018.03.31	Korea
	Tae-a Industry Co., Ltd.	Manufacturing tobacco materials	100.00%	2018.03.31	Korea
	KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	Manufacturing and selling tobaccos	99.99%	2018.03.31	Turkey
	Korea Tabacos do Brasil Ltda.	Processing leaf tobaccos	99.99%	2018.03.31	Brazil
	KT&G Pars	Manufacturing and selling tobaccos	99.99%	2018.03.31	Iran
	KT&G Rus L.L.C.	Manufacturing and selling tobaccos	100.00%	2018.03.31	Russia
	KT&G USA Corporation	Selling tobaccos	100.00%	2018.03.31	USA
	Cosmocos Co., Ltd (former, Somang Cosmetics Co., Ltd)	Manufacturing and selling cosmetics	98.56%	2018.03.31	Korea
	Renzoluc Pte., Ltd. (*)	Holding company	100.00%	2018.03.31	Singapore
	KGC Yebon Corporation	Manufacturing and selling medical herbs	100.00%	2018.03.31	Korea
	PT KT&G Indonesia	Selling tobaccos	99.99%	2018.03.31	Indonesia
	Sang Stay, Inc.	Hotel	100.00%	2018.03.31	Korea
	KT&G Global Rus L.L.C.	Selling tobaccos	100.00%	2018.03.31	Russia
Renzoluc Pte., Ltd.	PT Trisakti Purwosari Makmur	Manufacturing and selling tobaccos	99.99%	2018.03.31	Indonesia
	PT Mandiri Maha Mulia	Manufacturing and selling tobaccos	99.98%	2018.03.31	Indonesia
PT Trisakti Purwosari Makmur	PT Sentosa Ababi Purwosari	Manufacturing and selling tobaccos	100.00%	2018.03.31	Indonesia
	PT Purindo Ilufa	Manufacturing and selling tobaccos	100.00%	2018.03.31	Indonesia
	PT Nusantara Indag Makmur	Selling tobaccos	100.00%	2018.03.31	Indonesia
Korea Ginseng Corporation	KGC Life & Gin Co., Ltd	Manufacturing and selling cosmetics	100.00%	2018.03.31	Korea
	Cheong Kwan Jang Taiwan Corporation	Selling ginseng	100.00%	2018.03.31	Taiwan
	Korean Red Ginseng Corp., Inc.	Selling ginseng	100.00%	2018.03.31	USA
	Korea Ginseng (China) Corp.	Selling ginseng	100.00%	2018.03.31	China

	Korea Ginseng Corporation Japan	Selling ginseng	100.00%	2018.03.31	Japan
	PT CKJ Indonesia	Selling ginseng	99.88%	2018.03.31	Indonesia
	Jilin Hanzheng Ginseng Co., Ltd	Selling ginseng	100.00%	2018.03.31	China
Cosmoscos Co., Ltd	K&I HK Co., Ltd.	Selling cosmetics	100.00%	2018.03.31	Hong Kong
	K&I China Co., Ltd.	Selling cosmetics	100.00%	2018.03.31	China

(*) KT&G Corporation's percentage of ownership, shown above, excludes redeemable convertible preferred shares. As of the end of the current term, KT&G Corporation's percentage of ownership would be 88.60% if preferred shares are included.

For the previous term, the Parent Company made a capital contribution in kind to Cosmoscos Co., Ltd. by transferring its interest in K&I HK Co., Ltd. and K&I China Co., Ltd., increasing its ownership from 98.49% to 98.56%.

For the previous term, the Parent Company acquired additional shares of PT Sentosa Ababi Purwosari, PT Trisakti Purwosari Makmur and PT Mandiri Maha Mulia and its ownership interest increased to 100.00%, 99.99% and 99.98% from 99.8%, 60.17% and 66.47%, respectively.

(3) Summary of Subsidiaries' Financial Information
Financial information of subsidiaries as of the end of the current term is as below.

In millions of Korean won					
Subsidiary	Total assets	Total liabilities	Revenue	Net profit (loss)	Total comprehensive income (loss)
Korea Ginseng Corporation	1,931,624	290,391	393,407	68,834	68,624
Yungjin Pharm Co., Ltd.	200,341	79,606	48,027	1,088	1,086
Tae-a Industry Co., Ltd.	13,211	1,699	3,538	(7)	(17)
KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	37,953	38,220	2,394	(2,351)	(2,360)
Korea Tabacos do Brasil Ltda.	2,615	6	–	–	–
KT&G Pars	16,828	56,534	–	(3,525)	(3,902)
KT&G Rus L.L.C.	167,086	86,471	10,796	1,254	1,324
KT&G USA Corporation	57,239	43,969	19,574	(4,642)	(4,699)
Cosmoscos Co., Ltd.	65,813	27,012	18,984	(2,633)	(2,633)
Renzoluc Pte., Ltd.	126,107	27,175	–	(205)	(2,120)
KGC Yebon Corporation	60,254	12,983	3,297	98	101
PT KT&G Indonesia	48,914	62,935	21,742	1,943	2,214
SangSang Stay Inc.	6,636	2,020	4,358	(1,394)	(1,394)
KT&G Global Rus L.L.C.	89,519	99,020	7,523	806	786
PT Trisakti Purwosari Makmur, etc.	115,763	6,004	1,537	2,080	10,370
PT Sentosa Ababi Purwosari	55,630	55,022	7,064	(321)	(332)
PT Purindo Ilufa	11,368	15,174	2,068	(237)	(163)
PT Mandiri Maha Mulia	52,690	39,227	8,492	(164)	(425)
PT Nusantara Indag Makmur	248	46	–	(309)	–
KGC Life & Gin Co., Ltd.	28,796	8,273	10,629	620	618

Cheong Kwan Jang Taiwan Corporation	14,206	10,968	7,702	1,077	1,120
Korean Red Ginseng Corp., Inc.	19,355	16,720	4,665	(931)	(798)
Korea Ginseng (China) Corp.	22,150	9,353	10,417	412	855
Korea Ginseng Corporation Japan	6,042	4,545	4,219	113	186
PT CKJ Indonesia	–	–	–	–	75
Jilin Hanzheng Ginseng Co., Ltd.	57,503	154	2,459	(1,322)	754
K&I HK Co., Ltd.	294	29	–	(32)	(35)
K&I China Co., Ltd.	1,779	873	641	(270)	(230)

(4) Changes in Consolidated Group
During the previous term, K-Q Hongkong I, Limited was under liquidation.

During the previous term, KT&G Life Sciences Corporation, a subsidiary of the Parent Company, was merged into Yungjin Pharm. Co., Ltd. as of January 13, 2017.

During the previous term, PT Trisakti Purwosari Makmur, PT Mandiri Maha Mulia, PT Sentosa Ababi Purwosari and PT Purindo Ilufa respectively acquired 97%, 1%, 1%, 1% shares of PT Nusantara Indag Makmur. This has led to PT Nusantara Indag Makmur to become a reporting entity as part of the consolidated group.

2. Basis of Preparation

(1) Statement of Compliance
The consolidated interim financial statements of the Parent Company are consolidated interim financial statements prepared in accordance with Korean International Financial Reporting Standard ("K-IFRS") No. 1034 'Interim Financial Reporting.'

The consolidated interim financial statements of the Parent Company were authorized for issue by the board of directors on May 10, 2018.

(2) Basis of Measurement
The consolidated interim financial statements have been prepared on the historical cost basis, except for the following material items in the statements of financial position

- Derivatives measured at fair value
- Available-for-sale financial assets measured at fair value
- Liabilities for defined benefit plans recognized at the net of the total present value of defined benefit obligations less the fair value of plan assets

(3) Functional and Presentation Currency
The Group's consolidated interim financial statements are being prepared in Korean won, the key currency of economic environment for operating activities.

(4) Use of Estimates and Judgments
The preparation of the consolidated interim financial statements in conformity with K-IFRS requires

management to make judgments, estimates and assumptions that affect the application of accounting policies and the magnitude of assets, liabilities, income and expenses. Actual results may differ from these estimates if estimates and assumptions that are based on the management's best judgment at the end of the Interim reporting period differ from the actual environment.

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

Management's assessment of the application of, and estimates of, the Group's accounting policies used in the consolidated interim financial statements is based on the same accounting policies and assumptions used in the annual financial statements for that year ended December 31.

3. Significant Accounting Policies

The accounting policies, except for the application of the amendment standard effective from January 1, 2018, set out below have been applied consistently to all periods presented in these interim financial statements.

- K-IFRS No. 1102 'Share-based Payments' (Amendments)

The amendments include the following as key contents 1) the accounting for the effects of vesting conditions and non-vesting conditions in measuring the fair value of cash-settled share-based payment transactions shall address the same approach as that applied to the accounting for equity-settled share-based payment transactions; 2) when an entity makes equity-settled share-based payments to its employees net of income tax withholdings without net settlement characteristics, then the gross payment amounts shall be classified as the equity-settled if classified as such; and 3) if the terms of the cash-settled share-based payment transaction are changed to equity-settled, the existing liabilities are eliminated while new measurements are recognized, at the fair value of the equity instruments granted, at the date of the modification. The difference between the carrying amount of the eliminated amount of liabilities and the recognized amount of the equity is immediately recognized in profit or loss. The amendments have no significant impact on the consolidated interim financial statements of the Group.

- K-IFRS No. 1040 'Investment property' (amended)

The amendment clarifies that a real estate shall be reclassified as investment property if the real estate is supported by the observable evidence that a change in use has occurred based on the assessment of whether the real estate meets or fails to meet the definition of the investment property. The amendments also clarify that the circumstances that are not listed in K-IFRS No. 1040 can be the evidence of changes in use as well and change of use is possible for a real estate under construction, that is, the change in use is not limited to the finished or completed asset. The amendments have no significant impact on the consolidated interim financial statements of the Group.

- The Interpretation No. 2122 'Advance Payment or Receipt of Considerations in Foreign Currency' (enacted)

The interpretation explains how to determine the transaction date for the applicable exchange rate when the related assets, costs, or revenues (or a portion thereof) are initially recognized by eliminating non-monetary assets or non-monetary liabilities (e.g., non-refundable deposits or deferred revenue) arising from advanced payment or receipt of a consideration in foreign currency.

The interpretation stipulates that the transaction date is the first day of recognizing the non-monetary assets or non-monetary liabilities, either as an advanced payment or receipt of the consideration that is made. The interpretation also stipulates that the transaction date for each advanced payment or receipt must be determined separately if the payment or receipt is made several times.

The Group applies consistent method with the interpretation with regard to payment or receipt of advance consideration made in foreign currency; so, the Group does not expect the enactments to have a significant impact on the consolidated interim financial statements.

- K-IFRS No. 1109 'Financial Instruments' (enacted)

The Group applied the amendments to K-IFRS No. 1109 and the related amendments to other standards for the first time from the current quarter on January 1, 2018 as the date of initial application. K-IFRS No. 1109 introduced new rules for 1) classification and measurement of financial assets and financial liabilities, 2) impairment of financial assets, and 3) hedge accounting.

The Group has adopted a method that does not restate the prior period when applying it for the first time and did not reclassify the comparative financial statements, accordingly.

The key details of the new regulation are as follows, and the impact on the consolidated interim financial statements of the Group is explained in Note 37.

(1) Classification and measurement of financial instruments

All financial assets included in the scope of K-IFRS No. 1109 are subsequently measured at amortized cost or fair value based on the business model for the management of financial assets and the nature of the contractual cash flows.

-Debt instruments that are held under a business model with the aim to receive contractual cash flows and have contractual cash flows that consist of principal and interest on principal balance alone are subsequently measured at their amortized cost (financial assets at amortized cost).

-Debt instruments that are held under a business model with the aim of both the receipt and sale of the contractual cash flows and have contractual cash flows that consist of principal and interest on principal balance alone are subsequently recognized at their fair value (financial assets at fair value through other comprehensive income).

-All other debt instruments and equity instruments other than the above specified are subsequently measured at fair value and are recognized in profit or loss (financial assets at fair value through profit or loss).

Notwithstanding the details described above, K-IFRS 1109 permits an entity to make an irrevocable election as follows at the time of initial recognition

- For the investment in equity instruments that are not short-term trading items and that are not contingent consideration recognized by the acquirer in a business combination applying K-IFRS No. 1103, the Group may elect to present subsequent changes in its fair value in other comprehensive income.

- When accounting discrepancies can be eliminated or significantly reduced if designated as items at fair value through profit or loss, debt instruments that meet the requirements of financial assets measured at amortized cost or financial assets measured at fair value through other comprehensive income can be designated as items at fair value through profit or loss.

Of the debt instruments that meet the requirements of financial assets measured at amortized cost or financial assets measured at fair value through other comprehensive income in the current period, there is no debt instrument designated as items at fair value through profit or loss.

If the debt instrument measured at fair value through other comprehensive income (or loss) is removed, the cumulative gain or loss recognized in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment. On the other hand, for equity instruments designated as items at fair value through other comprehensive income (or loss), cumulative gains or losses previously recognized in other comprehensive income are not subsequently reclassified to profit or loss. The debt instruments measured at amortized cost or at fair value through other comprehensive income (or loss) subsequently are subject to the impairment provisions.

Management has reviewed and assessed the financial assets held by the Group based on the facts and circumstances that existed at the date of initial application and determined that there will be the following impacts with respect to the classification and measurement of the Group's financial assets as a result of the initial application of K-IFRS No. 1109

- Among the debt instruments classified as available-for-sale financial assets in accordance with K-IFRS No. 1039, the debt instruments that are held under a business model with the aim of both the receipt and sale of the contractual cash flows and have contractual cash flows that consist of principal and interest on principal balance alone are classified as financial assets at fair value through other comprehensive income (loss). Changes in the fair value of these debt instruments are recognized as accumulated gain or loss (unrealized) until they are eliminated or reclassified.

- Investments in equity instruments classified as available-for-sale financial assets in accordance with K-IFRS No. 1039 and measured at fair value at the end of each reporting period (neither short-term trading nor contingent consideration arising from a business combination) are designated as items at fair value through other comprehensive income (or loss). Changes in the fair value of these equity instruments are continuously recognized as accumulated gain or loss (unrealized).

Among the held-to-maturity investments that are measured at amortized cost or financial assets that are classified as loans and receivables in accordance with K-IFRS No. 1039, debt instruments that are held under a business model with the aim to receive contractual cash flows and have contractual cash flows that consist of principal and interest on principal balance alone are subsequently measured at their amortized cost after K-IFRS No. 1109.

- Financial assets that are classified as financial assets at fair value through profit or loss in accordance with K-IFRS No. 1039 are also measured in the statement of income as items at fair value through profit or loss under K-IFRS No. 1109.

Other reclassifications of financial assets do not affect the Group's financial position, profit or loss, other comprehensive income or total comprehensive income.

(2) Impairment of financial assets

The Group accounts for the expected credit loss and changes in financial assets at the end of the reporting date, to reflect changes in the credit risk of the financial assets that may occur after the date of the initial recognition, in accordance with the expected credit loss model under the K-IFRS No.1109 unlike K-IFRS No.1039 with respect to the impairment of financial assets. That is, it does not necessarily mean that a credit event should occur before you recognize credit losses.

The Group recognizes the expected credit loss for the following as a loss reserve i) debt instruments that are subsequently measured at amortized cost or at fair value through other comprehensive income (or loss); ii) lease receivables; iii) contract assets; and, iv) loan agreements and financial guarantee contracts subject to the impairment provisions of K-IFRS No. 1109. In particular, if the credit risk of a financial instrument increases significantly after initial recognition, or if credit is impaired when the financial asset is acquired, the loss provision is measured at the amount equal to the lifetime-expected credit loss over the period. In addition, K-IFRS No. 1109 provides a simplified method of measuring the allowance for losses on trade receivables, contract assets and lease receivables under certain circumstances. The Group applies the simplified method for trade receivables and contract assets.

In accordance with K-IFRS No. 1109, management of the Group determined the credit risk at the date of initial recognition of the financial instruments and reviewed and assessed impairment losses on financial assets, contractual assets and financial guarantee contracts held by the Group at the date of initial application using reasonable and supportive information that is available without undue cost or effort in comparison to the credit risk of the first application date (January 1, 2018).

(3) Classification and measurement of financial instruments

One of the major changes related to the classification and measurement of financial liabilities as a result of the adoption of K-IFRS No. 1109 is the way of accounting for the change in the fair value of the financial liabilities designated as ‘items at fair value through profit or loss’ attributable to the change in the issuer's credit risk. Except where accounting inconsistency in profit or loss is caused or enlarged when the effect of the change in the credit risk of the financial liabilities designated as items at fair value through profit or loss is recognized in other comprehensive income (or loss), changes in fair value attributable to changes in credit risk of related financial liabilities are recognized in other comprehensive income. Changes in fair value attributable to changes in credit risk of related financial liabilities are not subsequently reclassified to profit or loss, but are replaced with retained earnings when the financial liabilities are eliminated. In accordance with K-IFRS No. 1039, all the amount of changes in fair value of financial liabilities designated as financial liabilities at fair value through profit or loss has been presented in profit or loss.

Except for the above, the adoption of K-IFRS No. 1109 has no significant impact on the classification and measurement of the Group’s financial liabilities.

(4) General hedge accounting

The new general hedge accounting model maintains three types of hedge accounting. However, more flexibility is being introduced in the types of transactions eligible for hedge accounting with the expansion in risk factors of non-financial items and the types of hedging instruments that are appropriate for hedge

accounting. In addition, the related regulations on appraisal of hedging effectiveness were generally revised and replaced by the "economic relationship" principle between the hedged items and the hedging instrument. Retrospective assessment of the hedging effectiveness is no longer required. Additional disclosure requirements have been introduced regarding the Group’s risk management activities.
In accordance with the transitional provisions of K-IFRS No. 1109 for hedge accounting, the Group adopted the hedge accounting provisions of K-IFRS No. 1109 prospectively from January 1, 2018, but the Group does not have any transaction subject to the hedge accounting as of the end of the quarter.

- K-IFRS No. 1115 'Revenue from contracts with customers’ (enacted)

The Group applied K-IFRS No. 1115, 'Revenue from contracts with customers' for the first time in the current quarter reporting and adopted a retrospective application, according to the transitional provisions of K-IFRS No. 1115, to recognize the cumulative effect of the initial application of the K-IFRS on January 1, 2018, the date of initial application. In addition, the Group applied K-IFRS No. 1115 retroactively only to those contracts that had not been completed on the date of initial application, but did not apply the retroactive restatement for any contract changes made prior to the first application date using a practical simplified approach.

Accordingly, the comparative financial statements have not been reclassified in line with the transitional provisions of K-IFRS No. 1115 and the cumulative effects of the first application are retroactively applied to January 1, 2018, to be recognized in retained earnings. Details of the accounting policies and the financial impact of adopting the K-IFRS No. 1115 are explained in Note 37.

- 2014-2016 Annual Improvements to K-IFRS

This annual improvements include certain amendments to K-IFRS No. 1101 'First-time adoption of Korean International Financial Reporting Standards’ and K-IFRS No. 1028 'Investments in associates and joint ventures.' In accordance with K-IFRS No. 1028, it is clarified that a venture capital investment organization or a similar entity may individually select each of the associates and joint ventures as items at fair value through profit or loss, and such a choice must be made when initially recognizing an investment in a joint venture or an associate. In addition, when a company which is not an investment company applies the equity method to its associate or joint venture which is an investment company, it is allowed to apply the same fair value measurement the associates as the investment company applied to its subsidiaries. It is also clarified that the choice can be made on the individual basis for each individual associate, the investment company.

Since the Group does not adopt K-IFRS to date and is not a venture capital investment organization, the amendment does not have any effect on the consolidated financial statements.

The significant accounting policies applied by the Group for the preparation of consolidated interim financial statements in accordance with K-IFRS are as follows.

(1) Operating Segments

Operating segments are determined based on the internal reportings that are reviewed periodically by the chief operating decision maker in order to make decisions about allocating resources to the segments and to assess performance. As mentioned in Note 4, there are four reporting segments in the Group and each segment is the strategic operating unit of the Group. Segment information that is reported to the CEO includes items that directly belong to segments and items that can reasonably be allocated.

(2) Basis of Consolidation

① Business combination
Acquisitions of businesses are accounted for using the acquisition method other than the combination with regard to business entity or business under the same domination.

The consideration transferred in a business combination is measured at fair value just like generally measuring the identifiable net assets acquired at fair value. In case the business combination leads to goodwill, impairment test is conducted annually, and in case there is a difference in the bargain purchase, it is immediately recognized as the current term's profit or loss. Acquisition-related costs are generally recognized as expenses in the period in which cost has incurred and service has been received, excluding the issuance cost of debt security and equity security recognized in accordance with K-IFRS 1032 and K-IFRS 1039.

The consideration transferred does not include amount related to settlement of the previous relationship, and the settlement amount of the previous relationship is generally recognized as the current term's profit and loss.

The contingent consideration is measured at its acquisition-date fair value. Contingent consideration that is classified as equity is not remeasured and its subsequent settlement is accounted for within equity. In case contingent consideration is not classified as equity, the subsequent accounting for changes in the fair value of the contingent consideration is recognized as the current term's profit or loss.

In case the acquirer's share-based payment awards exchanged for awards held by the acquiree's employees, all or a portion of the market-based measure of the acquirer's replacement awards is included in measuring the consideration transferred in the business combination. As for the portion of a replacement award that is part of the consideration transferred for the acquiree and the portion that is a remuneration for post-combination service, the market-based measure of the replacement award for the acquiree and the replacement award attributable to pre-combination service are compared.

② Non-controlling interests
Non-controlling interests are measured at their proportionate share of the acquiree's identifiable net assets at the acquisition date.

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

③ Subsidiaries
Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date on which control ceases.

④ Loss of control
When the Group loses control over a subsidiary, it derecognizes the assets and liabilities of the subsidiary and any related non-controlling interests and other components of equity. Any resulting gain or loss is recognized in profit or loss. Any interest retained in the former subsidiary is measured at fair value when

control is lost.

⑤ Interests in equity-accounted investees
The Group's interests in equity-accounted investees comprise interests in associates and joint ventures.

Associates are those entities in which the Group has significant influence, but not control or joint control, over the financial and operating policies. A joint venture is an arrangement in which the Group has joint control, whereby the Group has rights to the net assets of the arrangement, rather than rights to its assets and obligations for its liabilities.

Interests in associates and joint venture are accounted for using the equity method. They are initially recognized at cost, which includes transaction costs. Subsequent to initial recognition, the consolidated financial statements include the Group's share of the profit or loss and other comprehensive income of equity-accounted investees until the date on which significant influence or joint control ceases.

⑥ Transactions eliminated on consolidation
Intragroup balances and transactions, and any unrealized income and expenses arising from intragroup transactions, are eliminated. Unrealized gains arising from transactions with equity-accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

⑦ Acquisitions from entities under common control
The assets and liabilities acquired under business combinations under common control are recognized at the carrying amounts recognized previously in the consolidated financial statements of the ultimate parent. The difference between consideration transferred and carrying amounts of net assets acquired is recognized as part of share premium.

(3) Joint Arrangements
A joint arrangement is an arrangement of two or more parties that have joint control. Joint control is a contractually agreed sharing of control of an arrangement that exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

Joint arrangements are classified into two types - joint operations and joint ventures. A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement (i.e., joint operators) have rights to the assets, and obligations for the liabilities, relating to the arrangement. A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement (i.e., joint ventures) have rights to the net assets of the arrangement.

The Group determines the type of joint arrangement in which it is involved by considering its rights and obligations arising from the arrangement. The Group assesses its rights and obligations by considering the structure and legal form of the arrangement; the terms agreed by the parties in the contractual arrangement; and, when relevant, other facts and circumstances.

If the Group is a joint operator, it recognizes and measures the assets and liabilities (and recognizes the related revenues and expenses) in relation to its interest in the arrangement in accordance with relevant K-IFRSs applicable to the particular assets, liabilities, revenues and expenses.

If the Group is a joint venturer, it recognizes its interest in a joint venture as an investment and accounts for that investment using the equity method in accordance with K-IFRS No. 1028 Investments in Associates and Joint Ventures, unless an investment or a portion of an investment in the joint venture meets the criteria to be classified as held for sale.

(4) Property, Plant and Equipment

All property, plant and equipment are stated at historical cost, less depreciation and accumulated impairment loss. Historical cost includes expenditures directly attributable to the acquisition of items.

Subsequent costs are included in an asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the consolidated interim statement of comprehensive income during the financial period in which they are incurred.

Property, plant and equipment, except for land and other tangible fixed assets, constituting trees and others, are depreciated on a straight-line basis over estimated useful lives that appropriately reflect the pattern in which an asset's future economic benefits are expected to be consumed.

The estimated useful lives of the Group's assets are as follows

Type	Useful life (years)
Buildings	10–60
Structures	5–40
Machinery	5–20
Vehicles	4–10
Tools	4–5
Furniture and fixtures	2–5

The assets' residual values and useful lives are reviewed and adjusted, if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized in other income and expense in the consolidated interim statement of comprehensive income.

(5) Borrowing Costs

The Group capitalizes borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. Other borrowing costs are recognized in expense as incurred. A qualifying asset is an asset that requires a substantial period of time to get ready for its intended use or sale. Financial assets and inventories that are manufactured or otherwise produced over a short period of time are not qualifying assets. Assets that are ready for their intended use or sale when acquired are not qualifying assets.

To the extent that the Group borrows funds specifically for the purpose of obtaining a qualifying asset, the Group determines the amount of borrowing costs eligible for capitalization as the actual borrowing costs incurred on that borrowing during the period, less any investment income on the temporary investment of those borrowings. The Group immediately recognizes other borrowing costs as an expense. To the extent that the Group borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the Group determines the amount of borrowing costs eligible for capitalization by applying a capitalization rate to the expenditures on that asset. The capitalization rate is the weighted average of the borrowing costs applicable to the borrowings of the Group that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs that the Group capitalizes during a period does not exceed the amount of borrowing costs incurred during that period.

(6) Government Grants
Government grants are not recognized, unless there is a reasonable assurance that the Group will comply with the grant's conditions and that the grant will be received.

Government grants that are intended to compensate the Group for expenses incurred are recognized as other income in profit or loss over the periods in which the Group recognizes the related costs as expenses.

(7) Intangible Assets except for Goodwill
Intangible assets are measured initially at cost and subsequently are carried at cost, less accumulated amortization and accumulated impairment losses. Intangible assets consist of industrial property rights, facility usage rights and intangible assets under development. Intangible assets are amortized on a straight-line basis over the estimated useful lives of intangible assets from the date that they are available for use. The residual value of intangible assets is assumed to be zero. However, as there are no foreseeable limits to the periods over which some of industrial property rights and facility usage rights are expected to be available for use, these intangible assets are regarded as having indefinite useful lives and not amortized.

Type	Useful lives (years)
Industrial property rights	5–20 or indefinite
Facility usage rights	Indefinite
Other intangible assets	3–14 or indefinite
Intangible assets under development	Indefinite

Amortization periods and amortization methods for intangible assets with finite useful lives are reviewed at the end of each reporting period. The useful lives of intangible assets that are not being amortized are reviewed at the end of each reporting period to determine whether events and circumstances continue to support indefinite useful life assessment for those assets. The change is accounted for as a change in an accounting estimate.

(8) Investment Property
Property held for the purpose of earning rentals or benefiting from capital appreciation is classified as investment property. Investment property is initially measured at its cost. Transaction costs are included in the initial measurement. Subsequently, investment property is carried at depreciated cost, less any accumulated impairment losses.

Subsequent costs are recognized in the carrying amount of investment property at cost or, if appropriate, as separate items if it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing are recognized in profit or loss as incurred.

Investment property, except for land, is depreciated on a straight-line basis over 10–60 years as estimated useful lives.

Depreciation methods, useful lives and residual values are reviewed at the end of each reporting date and adjusted, if appropriate. The change is accounted for as a change in an accounting estimate.

(9) Non-Current Assets Held for Sale

Non-current assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale, rather than through continuous use, are classified as held for sale. In order to be classified as held for sale, an asset (or a disposal group) must be available for immediate sale in its present condition and its sale must be highly probable. The assets or disposal groups that are classified as non-current assets held for sale are measured at the lower of their carrying amount or fair value, less cost to sell. The Group recognizes an impairment loss for any initial or subsequent write-down of the asset (or the disposal group) to fair value, less costs to sell, and a gain for any subsequent increase in fair value, less costs to sell, up to the cumulative impairment loss previously recognized in accordance with K-IFRS No. 1039 'Financial instrument: Recognition and measurement.'

A non-current asset that is classified as held for sale or part of a disposal group classified as held for sale is not depreciated (or amortized).

(10) Inventories

Inventories are measured at the lower of cost or net realizable value. The cost of inventories comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

The cost of inventories is determined as below.

Type	Determination method of unit cost price
Merchandise, finished goods, byproducts and work in progress	Weighted-average method
Processed tobacco leaf and tobacco leaf in raw material	Weighted-average method
Raw materials (excluding processed tobacco leaf and tobacco leaf in raw material) and supplies	Moving-average method
All other inventories	Specific identification method

When inventories are sold, the carrying amount of those inventories is recognized as an expense in the period in which the related revenue is recognized. The amount of any write-down of inventories to net realizable value and all losses of inventories are recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realizable value, is recognized as a reduction in the amount of inventories and recognized as an expense in the period in which the reversal occurs.

Tobacco leaf inventories that have an operating cycle that exceeds 12 months are classified as current assets, consistent with recognized industry practice. The estimated amounts of inventories in current assets, which are not expected to be realized within 12 months are ₩296,632 million and ₩317,640 million, respectively, as of December 31, 2017 and 2016.

(11) Impairment of Non-Financial Assets
The carrying amounts of the Group's non-financial assets, other than inventories, deferred tax assets, assets arising from employee benefits and non-current assets held for sale, are reviewed at the end of the reporting period to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill and intangible assets that have indefinite useful lives or that are not yet available for use, irrespective of whether there is any indication of impairment, are tested for impairment annually by comparing their recoverable amount to their carrying amount.

The Group estimates the recoverable amount of an individual asset. If it is impossible to measure the individual recoverable amount of an asset, then the Group estimates the recoverable amount of cash-generating unit ("CGU"). A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value, less costs to sell. The value in use is estimated by applying a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU for which estimated future cash flows have not been adjusted to the estimated future cash flows expected to be generated by the asset or CGU.
An impairment loss is recognized if the carrying amount of an asset or a CGU exceeds its recoverable amount. Impairment losses are recognized in profit or loss.
Except for impairment losses in respect of goodwill, which are never reversed, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(12) Financial Assets

- Classifications
From January 1, 2018, the Group classifies financial assets in the following measurement scope
- Financial assets measured at fair value (recognizes changes in fair value through other comprehensive income or current term's profit or loss)
- Financial assets measured at amortized cost

The classification of financial assets will be driven by the Group's business model for managing the financial assets and contractual terms of cash flow. The profit or loss of financial assets measured at fair value is recognized as current term's profit or loss or other comprehensive income. Investment with regard to debt instruments is recognized as current term's profit or loss or other comprehensive income depending on the business model of the relevant asset. The Group only reclassifies debt instruments in case the business model that manages financial assets is changed. The entity can make an irrevocable election to present in other comprehensive income for changes in the fair value of an investment in an equity instrument that is not held for trading. Changes in fair value of investment with regard to undesignated equity instruments are recognized as current term's profit and loss.

- Measurement
Financial assets are initially measured at fair value and in the event they are not current term's profit and loss-financial assets measured at fair value, transaction costs that are directly attributable to the acquisition of financial assets or issuance of financial liabilities are added to the fair value. The transaction costs of

current term’s profit and loss-financial assets measured at fair value are recognized as current term’s profit and loss.
If the host contract is determined in a hybrid contract, an entity classifies the entire hybrid contract as a financial asset rather than separating the embedded derivative from the host contract.

① Debt instruments
The subsequent measurement of financial assets is based on the entity’s business model for managing the financial assets and contractual cash flow characteristics of the financial assets. The Group classifies debt instruments into the following three scopes

(A) Amortized cost
Under the business model whose objective is to hold financial assets in order to collect contractual cash flows, assets that are comprised of solely principal and interest are measured at amortized cost. As financial assets are measured at amortized cost, the profit or loss of financial assets that are not subject to hedge is recognized as current term’s profit or loss when the relevant financial asset is eliminated or impaired. The interest income of financial assets recognized in accordance with the effective interest method is included in the financial income.

(B) Financial assets measured at fair value through other comprehensive income
Under the business model whose objective is to hold financial assets in order to collect contractual cash flows and to sell the financial assets, the financial assets that are comprised of solely principal and interest are measured at fair value through other comprehensive income. Other than impaired loss (reversal), interest income and foreign exchange loss, the profit or loss of financial assets measured at fair value through other comprehensive income is recognized as other comprehensive income. When eliminating the financial assets, the accumulated amount of other comprehensive income recognized is reclassified as current term’s profit and loss in equity. The interest income of the financial assets recognized in accordance with the effective interest method is included in the finance income. The foreign exchange loss is expressed as other income or other expense, and the impaired loss is expressed as other expense.

(C) Financial assets measured at fair value through current term’s profit and loss
Debt instruments that are not financial assets measured at amortized cost or measured at fair value through other comprehensive income are measured at fair value through current term’s profit and loss. The profit and loss of debt instruments measured at fair value through current term’s profit and loss in which hedge has not been applied are recognized as current term’s profit and loss and are expressed as finance income and finance expense, respectively, in the consolidated interim statement of income.

② Equity instruments
The Group subsequently measures investment with regard to all equity instruments as fair value. With regard to equity instruments that have opted to express changes in fair value as other comprehensive income, the amount recognized as other comprehensive income is not reclassified as current term’s profit and loss even when the relevant equity instrument is eliminated. The dividend income with regard to such equity instruments is recognized as finance income and current term’s profit and loss when the dividend rights of the Group are confirmed.

- Impairment
The Group evaluates the expected credit loss with regard to debt instruments measured at amortized cost or measured at fair value through other comprehensive income based on the future prospect information.

Impairment method is determined depending on the extent of significant increase in the credit risk. However, with regard to trade receivables, a simplified approach that recognizes the expected credit loss over the entire period from the initial recognition point of debt is applied.

(13) Derivatives
Derivatives are initially recognized at the date the derivative contract is entered into and are subsequently remeasured to their fair value at the end of each reporting period. The resulting gain or loss arising from the changes in fair value of derivatives is recognized as current term's profit or loss.

(14) Cash and Cash Equivalents
Cash and cash equivalents comprise cash balances and call deposits with maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value and are used by the Group in the management of its short-term commitments. Equity investments are excluded from cash equivalents, unless they are, in substance, cash equivalents, for example, in the case of preferred shares when they have a short maturity with a specified redemption date.

(15) Employee Benefits

① Short-term employee benefits
Short-term employee benefits are employee benefits that are due to be settled within 12 months after the end of the period in which the employees render the related service. When an employee has rendered service to the Group during an accounting period, the Group recognizes the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.

② Other long-term employee benefits
As for other long-term employee benefits that are not due to be settled within 12 months after the end of the period in which the employees rendered the related service, the future benefits acquired in return for the services provided in the current term and the past period are discounted as current value. Changes following remeasurements are recognized as current term's profit and loss that have incurred in the period.

③ Retirement benefits: defined contribution plans
When an employee has rendered service to the Group during a period, the Group recognizes the contribution payable to a defined contribution plan in exchange for that service as a liability (accrued expense) after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the end of the reporting period, the Group recognizes that excess as an asset (prepaid expense) to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

④ Retirement benefits: defined benefit plans
The calculation of defined benefit obligations is performed annually by a qualified actuary using the projected unit credit method. When the calculation results in a potential asset for the Group, the recognized asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. To calculate the present value of economic benefits, consideration is given to any applicable minimum funding requirements. Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognized immediately in other comprehensive income. The Group determines the net interest expense (income) on the net defined benefit

liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments.

Net interest expense and other expenses related to defined benefit plans are recognized in profit or loss. When the benefits of a plan are changed or when a plan is curtailed, the resulting change in benefit that relates to past service or the gain or loss on curtailment is recognized immediately in profit or loss. The Group recognizes gains and losses on the settlement of a defined benefit plan when the settlement occurs.

⑤ Termination benefits

Termination benefits are expensed at the earlier of when the Group can no longer withdraw the offer of those benefits and when the Group recognizes costs for a restructuring. If benefits are not expected to be settled wholly within 12 months of the end of the reporting period, then they are discounted.

(16) Provisions

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

The risks and uncertainties that inevitably surround many events and circumstances are taken into account in reaching the best estimate of a provision. Where the effect of the time value of money is material, provisions are determined at the present value of the expected future cash flows. Where some or all of the expenditures required to settle a provision are expected to be reimbursed by another party, the reimbursement shall be recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The reimbursement shall be treated as a separate asset.

Provisions are reviewed at the end of each reporting period and adjusted to reflect the current best estimates. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision is reversed.

(17) Equity Capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issuance of ordinary shares and share options are recognized as a deduction from equity, net of any tax effects.

When the Group repurchases its share capital, the amount of the consideration paid is recognized as a deduction from equity and classified as treasury shares. The profits or losses from the purchase, disposal, reissue or retirement of treasury shares are not recognized as current profits or losses. If the Group acquires and retains treasury shares, the consideration paid or received is directly recognized in equity.

(18) Revenue Recognition

The Group’s revenue categories consist of revenue from goods sold, services and other income.

① Sales of goods

Revenue from sale of goods is measured at the fair value of the consideration received or receivable. Revenue from the sale of goods is recognized when the Group has transferred to the buyer the significant risks and rewards of ownership of the goods, the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group and the costs incurred or to be incurred in respect of the transaction can be measured reliably.

The Group allows returns under the contract that supplies goods to customers, so the revenue from customers may change. The Group recognizes revenue when it can reasonably anticipate a return allowed to customers and only to the extent that it is highly probably that a significant reversal in the amount of cumulative revenue recognized will not subsequently occur. If reasonable estimates are not possible, it shall be offset as refund liability.

② Rendering of services

Revenue from rendering of services is recognized by reference to the stage of completion of the transaction at the end of the reporting period when the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group, the stage of completion of the transaction at the end of the reporting period can be measured reliably and the costs incurred for the transaction and the costs to complete the transaction can be measured reliably. When the outcome of the transaction involving the rendering of services cannot be estimated reliably, revenue is recognized only to the extent of the expenses recognized that are recoverable.

The Group provides logistics services according to the contract signed with customers. The Group controls the logistics service before transferring to the customer so that it belongs to 'oneself' and revenue is recognized as total amount.

③ Construction of real estate for residence

The Group constructs and sells real estate for residence according to a long-term contract with customers. Such contract is signed before the construction of real estate for residence begins. According to the contract conditions, transferring the real estate to another customer is restricted and the Group has the right to claim for enforceable payment with regard to work performed. Therefore, revenue incurred from real estate for residence is recognized based on the percentage-of-completion method (in other words, in proportion to the cost incurred with regard to the work performed until the point compared to expected cost). The management personnel using the percentage-of-completion method has judged it to be an appropriate method for measuring the progress rate until the completion of the execution duty under K-IFRS 1115.

The Group has the right to make claims to the customer with regard to the construction of real estate for residence in accordance with the achievement of milestone related to a series of work. Upon reaching a certain milestone, the customer sends the relevant work specification signed by a third evaluator and the invoice related to the milestone consideration is issued. Contract assets recognized with regard to all work executed previously are reclassified as receivables at the point the claim is made to the customer. If the payment amount following the milestone exceeds the revenue recognized until then in accordance with the percentage-of-completion method, the Group recognizes the said difference as contract liability. The difference between the revenue recognition point and the milestone payment point under the percentage-of-completion method is below one year at all times, so there is no significant finance element in the contract with customers.

The Group pays sales commission in relation to the sales contract of real estate for residence. When the Group estimates that such incremental cost would be recovered, the incremental cost is capitalized and amortized over the period in which the real estate for residence is transferred to the customer.

④ Lease of real estate, etc.

The profit from lease of investment property and others is recognized as flat rate standard over the period of lease.

(19) Finance Income and Finance Cost

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income and investment income on long-term deposits in MSA Escrow Fund. Interest income is recognized as it accrues in profit or loss, using the effective interest method. Dividend income is recognized in profit or loss on the date the Group's right to receive payment is established.

Finance cost is interest expense on borrowings and unwinding of the discount on trade and other payables, which is recognized in profit or loss using the effective interest method.

(20) Income Taxes

Income tax expense comprises current and deferred taxes. Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination or items recognized directly in equity or in other comprehensive income.

① Current tax

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, using tax rates enacted or substantively enacted at the end of the reporting period and any adjustment to tax payable in respect of previous years. The taxable profit is different from the accounting profit for the period since the taxable profit is calculated excluding the temporary differences, which will be taxable or deductible in determining taxable profit (tax loss) of future periods and non-taxable or non-deductible items from the accounting profit.

② Deferred tax

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the Group expects at the end of the reporting period to recover or settle the carrying amount of its assets and liabilities.

The Group recognizes a deferred tax asset for all deductible temporary differences to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilized.

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

Deferred tax assets and liabilities are offset only if there is a legally enforceable right to offset the related current tax liabilities and assets, they relate to income taxes levied by the same tax authority and they intend to settle current tax liabilities and assets on a net basis.

(21) Foreign Currencies

① Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of the Group at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated to the functional currency using the reporting date's exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date the fair value was determined.

Foreign currency differences arising on retranslation are recognized in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments, a financial liability designated as a hedge of the net investment in a foreign operation or qualifying cash flow hedges that are recognized in other comprehensive income. Non-monetary items that are measured in terms of a historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

② Foreign operations

If the presentation currency of the Group is different from a foreign operation's functional currency, the financial statements of the foreign operation are translated into the presentation currency using the following methods

The assets and liabilities of foreign operations, whose functional currency is not the currency of a hyperinflationary economy, are translated to presentation currency at exchange rates at the reporting date. The income and expenses of foreign operations are translated to functional currency at exchange rates at the dates of the transactions. Foreign currency differences are recognized in other comprehensive income.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition of that foreign operation are treated as assets and liabilities of the foreign operation. Thus, they are expressed in the functional currency of the foreign operation and translated at the closing rate.

Foreign exchange gains or losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely to occur in the foreseeable future and which, in substance, is considered to form part of the net investment in the foreign operation, are recognized in other comprehensive income in the translation reserve. On the partial disposal of a subsidiary that includes a foreign operation, the entity reattributes the proportionate share of the cumulative amount of the exchange differences recognized in other comprehensive income to the non-controlling interests in that foreign operation. In any other partial disposal of a foreign operation, the entity reclassifies to profit or loss only the proportionate share of the cumulative amount of the exchange differences recognized in other comprehensive income.

③ Conversion of net investment with regard to foreign operations

Foreign exchange gains or losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely to occur in the foreseeable future and which in substance is considered to form part of the net investment in the foreign operation, are recognized in other comprehensive income in the translation reserve and is reclassified as current term's profit or loss at the disposal point of the relevant net investment.

(22) Earnings per Share

The Group presents basic and diluted earnings per share ("EPS") data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Parent Company by the weighted-average number of ordinary shares outstanding during the period, adjusted for own shares held. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted-average number of ordinary shares outstanding, adjusted for own shares held, for the effects of all dilutive potential ordinary shares.

(23) Emission Rights
The Group accounts for greenhouse gases emission right and the relevant liability as below, pursuant to the Act on Allocation and Trading of Greenhouse Gas Emission that became effective in 2015.

① Greenhouse Gases Emission Right
Greenhouse Gases Emission Right consists of emission allowances that are allocated from the government free of charge or purchased from the market. The cost includes any directly attributable costs incurred during the normal course of business. Emission rights held for the purpose of performing the obligation are classified as intangible assets and are initially measured at cost and after initial recognition are carried at cost, less accumulated impairment losses. Emission rights held for short-swing profits are classified as current assets and are measured at fair value with any changes in fair value recognized as profit or loss in the respective reporting period.

The Group derecognizes an emission right asset when the emission allowance is unusable, disposed or submitted to the government in which the future economic benefits are no longer expected to be probable.

② Emission liability
Emission liability is a present obligation of submitting emission rights to the government with regard to emission of greenhouse gas. Emission liability is recognized when it is probable that outflows of resources will be required to settle the obligation and the costs required to perform the obligation are reliably estimable. Emission liability is an amount of estimated obligations for emission rights to be submitted to the government for the performing period. The emission liability is measured based on the expected quantity of emission for the performing period in excess of emission allowance in possession and the unit price for such emission rights in the market at the end of the reporting period.

(24) Current Arrangement of Consolidated Interim Financial Statements
The Group has changed the order of current arrangement of consolidated interim financial statements in order to provide reliable information suitable to the objective. In order to conveniently compare the consolidated interim financial statements in the previous term and the consolidated interim financial statements of the current term, they were expressed in the order of current arrangement method. Such reclassification does not affect the net profit and loss or the net asset reported in the previous-term net asset.

(25) New Standards and Interpretations Not Yet Adopted
The following new standards and interpretations have been enacted or announced and issued for annual periods beginning after January 1, 2018, but the Group has not early adopted the following new standards in preparing these consolidated interim financial statements.

- K-IFRS No. 1116 'Lease'
K-IFRS No. 1116 'Lease' published on May 22, 2017, is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. It replaces existing lease standards, including K-IFRS No. 1017 'Lease,' K-IFRS No. 2104 'Determining whether a commitment includes a lease,' K-IFRS No. 2015

‘Operating lease: incentive’ and K-IFRS No. 2027 ‘Assessment of the substance of the transaction, including lease in legal form.’

At the time of contract, the Group determines whether the contract is a lease or whether the contract includes a lease, and identifies whether the contract is a lease or whether the contract includes a lease, in accordance with this standard at the date of initial application. However, the Group may not rejudge all contracts by applying the simplified method for contracts before the first application date.

The lessee and the lessor must account for each lease element in the lease contract separately from the non-lease element (called "non-lease element") in the lease contract or the contract including lease. The lessee must recognize a lease asset representing the right to use an underlying asset and a lease liability representing an obligation to pay the lease payments. However, short-term leases (leases with lease period less than 12 months) and small leases are subject to the exemption provisions of the standard. In addition, the lessee can use the simplified method as a method of accounting for each lease element and related non-lease element as one lease element instead of separating the non-lease element from the lease element. The accounting for lessor did not change significantly with the accounting of the current K-IFRS No. 1017.

The lessee can apply either the retrospective application for the past reporting period or retrospective application to recognize the cumulative effect of the initial application at the date of initial application, in accordance with K-IFRS No. 1008 ‘Accounting Policies, Changes in Accounting Estimates and Errors.’ The Group plans to apply K-IFRS No. 1116 initially on January 1, 2019. The actual impact of adopting those new standards will vary the lease asset that the Group holds and economic conditions at that time, as well as accounting and judgements that the Group will make in the future. The Group did not assess the potential impact on selected policy and its consolidated interim financial statements resulting from the application of this new standard and expects to disclose additional quantitative information before it adopts the standard in 2018.

The Group is analyzing the financial effects of the first adoption of K-IFRS No. 1116 on the 2018 consolidated interim financial statements based on present situation and information obtained as of March 31, 2018, but it is difficult to provide a rational estimated figure with regard to the financial impact until the Group completes such analysis.

4. Operating Segments

(1) The Group's operating segments are summarized as follows

Operating segments	Principal operation
Tobacco	Manufacturing and selling tobaccos
Ginseng	Manufacturing and selling red ginseng
Real estate	Selling and renting real estate
Others	Manufacturing and selling pharmaceuticals, cosmetics and others

(2) Segment information on sales and operating profit for the current quarter and previous quarter is as below.

① For the three-month period ended March 31, 2018

In millions of Korean won							
Type	Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Total segment sales	604,733	420,328	14,430	126,358	1,165,849	(98,259)	1,067,590
Less: Intersegment sales	44,287	27,241	2,832	23,899	98,259	(98,259)	–
External sales	560,446	393,087	11,598	102,459	1,067,590	–	1,067,590
Operating profit	200,041	91,216	5,139	4,500	300,896	10,472	311,368

② For the three-month period ended March 31, 2017

In millions of Korean won							
Type	Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Total segment sales	740,094	360,497	33,549	124,722	1,258,862	(80,114)	1,178,748
Less: Intersegment sales	39,987	22,493	3,152	14,482	80,114	(80,114)	–
External sales	700,107	338,004	30,397	110,240	1,178,748	–	1,178,748
Operating profit	309,144	77,072	25,446	(9,761)	401,901	(6,570)	395,331

(3) The Group obtains revenue by transferring goods and services over a period or at a point in the main business subsidiaries as follows. The categories of main business subsidiaries are consistent with the revenue disclosure information per reporting segment in accordance with K-IFRS No. 1108.

In millions of Korean won			
Type		For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Revenue recognized at a point			
Manufacturing and sales of tobacco	Wholesale and retail, etc.	389,695	428,529
	Special (duty-free, etc.)	50,442	53,576
	Agent	119,290	218,002
Manufacturing and sales of red ginseng, etc.	Direct sales	355,661	310,029
	Consignment	–	3,082
	Agent	37,426	24,893
Sales and rental of real estate	Rental	11,598	10,537
Others	Wholesale and retail, etc.	12,798	–
	Direct sales	82,519	99,435
	Special (duty-free, etc.)	966	–
	Agent	1,566	1,561
Subtotal		1,061,961	1,149,644
Revenue recognized over a period			
Manufacturing and sales of tobacco	Transportation, etc.	1,019	–
Sales and rental of real estate	Sales	–	19,860
Others	Direct sales	4,420	9,227
	Technology service	190	17
Subtotal		5,629	29,104
Total		1,067,590	1,178,748

(4) Segment information on assets and liabilities as of the end of current quarter and end of previous term was as follows

① As of March 31, 2018

In millions of Korean won							
Type	Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Assets:							
Segment assets	5,087,748	1,992,330	454,292	246,343	7,780,713	(1,900,714)	5,879,999
Investments in associates and joint ventures	–	–	47,774	3,205	50,979	–	50,979
Subtotal	5,087,748	1,992,330	502,066	249,548	7,831,692	(1,900,714)	5,930,978
Unallocated assets							4,156,177
Total assets							10,087,155
Acquisition of non-current assets	55,203	5,576	–	1,187	61,966	(673)	61,293
Liabilities:							
Segment liabilities	1,639,393	146,463	–	93,517	1,879,373	(353,086)	1,526,287
Unallocated liabilities							1,061,521
Total liabilities							2,587,808

② As of December 31, 2017

In millions of Korean won							
Type	Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Assets:							
Segment assets	3,849,835	1,950,480	280,899	244,782	6,325,996	(362,806)	5,963,190
Investments in associates and joint ventures	–	–	47,865	3,166	51,031	–	51,031
Subtotal	3,849,835	1,950,480	328,764	247,948	6,377,027	(362,806)	6,014,221
Unallocated assets							3,961,685
Total assets							9,975,906
Acquisition of non-current assets	267,151	45,160	–	14,935	327,246	(2,523)	324,723
Liabilities:							
Segment liabilities	1,646,316	150,207	–	82,398	1,878,921	(327,617)	1,551,304
Unallocated liabilities							594,841
Total liabilities							2,146,145

Cash and cash equivalents, available-for-sale financial assets, deferred tax assets and others are included in the unallocated assets, and in unallocated liabilities, borrowings, deferred tax liabilities and others are included.

(5) Geographical information determined by customer's location as of the current term and previous term is as follows

In millions of Korean won						
Type	For the three-month period ended March 31, 2018			For the three-month period ended March 31, 2017		
	Korea	Overseas	Total	Korea	Overseas	Total
Sales	985,701	81,889	1,067,590	1,094,524	84,224	1,178,748
Non-current assets	3,274,558	149,291	3,423,849	3,144,956	133,415	3,278,371

In the non-current assets above, deferred tax assets have been excluded, and in case of overseas, the sales or non-current assets that belong to a particular country were not important, so they were not classified and expressed per country.

(6) Revenues from major customers, which amount to more than 10% of the details of the Group's consolidated total revenues as of the current quarter and previous quarter are as follows

In millions of Korean won			
Segment	Major customer	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Tobacco	Alokozay International Limited	6,258	122,711

5. Cash and Cash Equivalents and Other Financial Assets

(1) Cash and cash equivalents as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Cash on hand	25,894	36,955
Demand deposits	219,353	186,874
Specific money in trust	854,532	1,006,347
Total	1,099,779	1,230,176

(2) Current other financial assets as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won				
Type	As of March 31, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Time deposits	112,752	6,340	113,811	6,340
Certificates of deposits	31,280	–	31,286	–
Special money trusts	78,000	10,000	1,418,803	–
Security deposits for checking accounts	58	8	–	11
Total	222,090	16,348	1,563,900	6,351

(3) Financial assets restricted in use as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won			
Type		As of March 31, 2018	As of December 31, 2017
Long-term other financial assets	Security deposits for checking accounts	8	11
Short-term other financial assets	Security deposits for checking accounts	58	–
Long-term other financial assets	Business performance bond	6,340	6,340
Short-term other financial assets	ACH(Automated Clearing House) transaction collateral	1,280	1,287
Total		7,686	7,638

6. Financial assets at fair value through profit or loss

As explained in Note 3, the Group applied K-IFRS No. 1109 ‘ Financial Instruments’, from the beginning of the year. Please refer to Note 37 for the effect of these accounting policies and changes on financial asset classification and financial statements.

(1) Financial assets at fair value through profit or loss

In millions of Korean won				
Item	As of March 31, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Special money trust	1,646,189	–	1,320,000	–
Beneficiary certificate of real estate	–	178,911	–	184,169
Total	1,646,189	178,911	1,320,000	184,169

(*) The above financial assets were classified as other financial assets and available-for-sale financial assets at the end of the previous fiscal year, respectively. The figures above do not include the effect of changes in retained earnings caused by changes in accounting policies.

(2) Amounts recognized in profit or loss

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Unrealized net changes in fair value related to the measurements at fair value through profit or loss(*)	14,217	–
Gains or losses on disposals related to the measurements at fair value through profit or loss(*)	7,762	–
Total	21,979	–

(*)Include profit or loss of money trust recognized in cash and cash equivalents

7. Derivative Financial Assets

(1) Derivative financial assets as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Currency forward	6,006	–

(2) Changes in derivative financial assets for the three-month periods ended March 31, 2018 and 2017 are as follows.

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Beginning balance	–	–
Valuation profit and loss	6,006	–
Balance at end	6,006	–
Statement of financial position:		
Current	6,006	–
Non-current	–	–
Total	6,006	–

8. Trade and Other Receivables

(1) Trade and other receivables as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won				
Type	As of March 31, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Loans to employees	16,818	33,339	17,100	36,021
Loans	862	688	949	880
Other receivables	22,353	–	17,371	–
Guarantee deposits	47,939	28,429	45,225	26,786
Accrued income	4,483	–	7,875	–
Trade receivables	986,204	–	1,038,387	–
Total	1,078,659	62,456	1,126,907	63,687

(2) Trade and other receivables and allowance for doubtful accounts as of March 31, 2018 and December 31, 2017 are as follows

In millions of Korean won				
Type	As of March 31, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Gross trade and other receivables	1,172,935	62,456	1,154,696	63,687
Allowances:				
Loans	–	–	–	–
Other receivables	(99)	–	(2,189)	–
Trade receivables	(94,177)	–	(25,600)	–
Total allowances	(94,276)	–	(27,789)	–
Net trade and other receivables	1,078,659	62,456	1,126,907	63,687

(3) Changes in allowance for trade and other receivables for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Type	For the Three-Month Period Ended March 31, 2018	For the Three-Month Period Ended March 31, 2017
Beginning balance	27,789	31,590
Change in accounting policy	69,258	–
Impairment loss (reversal)	(418)	57
Elimination	(5,317)	–
Net exchange difference, etc.	2,964	(492)
Ending balance	94,276	31,155

Impairment loss (reversal of impairment loss) on trade and other receivables is included as part of selling, general and administrative expenses and other expense (income) in the separate statements of comprehensive income.

(4) Details of trade and other receivables that are measured at amortized cost using effective interest rate as of the end of current term and end of previous term are as follows

In millions of Korean won						
Type	As of March 31, 2018			As of December 31, 2017		
	Effective interest rate	Current	Non-current	Effective interest rate	Current	Non-current
Loans to employees	2.66%–5.68%	16,818	33,339	2.45%–5.68%	17,100	36,021
Loans	1.93%	30	238	1.93%	–	237
Guarantee deposits	1.49%–5.68%	47,939	28,429	1.49%–3.52%	43,569	25,279
Total		64,787	62,006		60,669	61,537

9. Inventories

(1) Inventories as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won						
Type	As of March 31, 2018			As of December 31, 2017		
	Acquisition cost	Net of loss on write-down of inventories	Carrying amount	Acquisition cost	Net of loss on write-down of inventories	Carrying amount
Merchandize	57,362	(1,140)	56,222	38,790	(1,104)	37,686
Finished goods	720,048	(3,796)	716,252	679,882	(3,165)	676,717
Work in progress	610,974	(542)	610,432	701,976	(1,142)	700,834
Raw materials	814,752	(1,254)	813,498	821,992	(1,158)	820,834
Supplies	26,627	–	26,627	24,637	–	24,637
Byproducts	6,613	–	6,613	6,168	–	6,168
Buildings under construction	2,894	–	2,894	–	–	–
Sites for construction of real estate	7,922	–	7,922	–	–	–
Goods in transit	17,749	–	17,749	50,590	–	50,590
Total	2,264,941	(6,732)	2,258,209	2,324,035	(6,569)	2,317,466

(2) The amount of loss on valuation and disposals of inventories recognized as an expense for the three-month periods ended March 31, 2018 and 2017 were as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Cost of sales:		
Loss of write-down of inventories	743	412
Loss on retirement of inventories	2,057	1,155
Other expenses:		
Loss on retirement of inventories	520	1,591
Foreign currency translation exchange differences	(580)	57
Total	2,740	3,215

10. Long-Term Deposits In Msa Escrow Fund

Long-term deposits in MSA Escrow Fund as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Demand deposits	1,936	1,921
T-Note	530,304	508,302
Total	532,240	510,223

As discussed in Note 35 to the separate financial statements, long-term deposits in MSA Escrow Fund are deposited to the U.S. government related to the export of tobacco to the United States. For the years ended March 31, 2018 and 2017, ₩15,146 million and ₩19,709 million, respectively, were paid into long-term deposits in MSA Escrow Fund.

11. Financial assets at fair value through other comprehensive income

(1) Financial assets at fair value through other comprehensive income as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Available-for-sale equity instruments		
—YTN Co., Ltd.	17,514	17,557
—Oscotech Inc.	13,966	8,686
—Shinhan Financial Group Co., Ltd.	183,182	198,013
—Rexahn Pharmaceuticals, Inc.	1,034	1,382
—U&I Corporation	12,466	12,079
Listed	228,162	237,717
Unlisted (*)	50,326	234,046
Total	278,488	471,763

(*) In the prior year, the Group classified unlisted equity instruments as available-for-sale financial assets for the purpose of holding them in the long-run. The figures did not include the effect of changes in assets caused by changes in accounting policies. Of the unlisted equity instruments classified as available-for-sale financial instruments, ₩ 184,169 million were reclassified to financial assets at fair value through profit or loss in accordance with the application of KIFRS No. 1109.

At the disposal of the above equity instruments, the related accumulated other comprehensive income or expense is reclassified to retained earnings and is not reclassified to profit or loss.

(2) Changes in other comprehensive income (loss)-financial assets measured at fair value for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Beginning balance	471,763	386,596
Change in accounting policy	(184,169)	–
Acquisition	450	–
Change in fair value	(9,556)	7,262
Transfer	–	(2,054)
Ending balance	278,488	391,804
Statement of financial position:		
Current	–	–
Non-current	278,488	391,804
Total	278,488	391,804

12. Investments in associates and joint ventures

(1) Investments in associates as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won							
Company	Location	Principal operation	Date of statement of financial statements used	As of March 31, 2018		As of December 31, 2017	
				Percentage of ownership	Carrying amount	Percentage of ownership	Carrying amount
Lite Pharm Tech, Inc.	Korea	Manufacturing medical supplies	March 31	20.24%	3,206	20.24%	3,166
JR REIT V Co., Ltd.	Korea	Renting of real estate	March 31	34.63%	5,241	34.63%	5,202
JR REIT VIII Co., Ltd.	Korea	Renting of real estate	March 31	21.74%	9,218	21.74%	9,187
JR REIT X Co., Ltd.	Korea	Renting of real estate	March 31	28.79%	8,542	28.79%	8,471
JR REIT XIII Co., Ltd.	Korea	Renting of real estate	March 31	27.03%	4,813	27.03%	4,805
KORAMCO Private REIT 50 Fund (*1)	Korea	Renting of real estate	March 31	84.21%	16,019	84.21%	16,168
KB Gimpo Logistics CR REIT Co., Ltd. (*2)	Korea	Renting of real estate	March 31	12.00%	3,003	12.00%	3,032
Yong In Jung Sim Co., Ltd.	Korea	Developing real estate	March 31	22.22%	937	22.22%	1,000
LSK Global Pharma Services Co., Ltd.	Korea	Researching and developing medicine	March 31	23.15%	-	23.15%	-

Cosmo Tobacco Co., Ltd.	Mongolia	Manufacturing and sales of tobacco	March 31	40.00%	-	40.00%	-
Total					50,979		51,031

(*1) KORAMCO Private REIT 50 Fund is classified as a joint venture since decisions about the significant financial and operating policy of the investee cannot be made without unanimous consent of the parties that control the arrangement collectively.

(*2) KB Gimpo Logistics CR REIT Co., Ltd is classified as a joint venture since decisions about the significant financial and operating policy of the investee cannot be made without unanimous consent of the parties, holding 12% shares each, as the voting power of 76% shares held by the collective investment business entity is not entitled to have an impact on a resolution of the investee by the Financial Investment Services and Capital Markets Act.

In the previous term, the Group made an investment of ₩1,000 million in Yong In Jung Sim Co., Ltd.
In the previous term, the Group recognized ₩7,319 million of gain on sale of investments in associates and joint ventures as KVG REIT 1 Co., Ltd. was liquidated.

(2) Financial information of associates and joint ventures, which represents 100% of the entities' balances as of the end of current quarter and end of previous term, is summarized as follows

① As of March 31, 2018

A. Summarized financial information

In millions of Korean won				
Company	Total assets	Total liabilities	Revenue	Total comprehensive income (loss)
Lite Pharm Tech, Inc.	18,944	3,106	3,014	144
JR REIT V Co., Ltd.	30,427	15,291	349	113
JR REIT VIII Co., Ltd.	108,351	65,951	1,214	139
JR REIT X Co., Ltd.	85,546	55,877	1,086	245
JR REIT XIII Co., Ltd.	46,969	29,164	372	30
KORAMCO Private REIT 50 Fund (*1)	46,911	27,889	800	110
KB Gimpo Logistics CR REIT Co., Ltd. (*2)	61,726	36,696	1,053	145
Yong In Jung Sim Co., Ltd.	4,220	–	–	(280)
LSK Global Pharma Services Co., Ltd.	9,885	10,506	8,935	2,603
Cosmo Tobacco Co., Ltd.	–	–	–	–

B. Additional financial information about joint ventures

In millions of Korean won								
Company	Cash and cash equivalents	Current financial liabilities	Non-current financial liabilities	Depre-ciation	Amortization	Interest income	Interest cost	Income tax expense
KB Gimpo Logistics CR REIT Co., Ltd.	482	35,598	992	230	–	3	359	–
KORAMCO Private REIT 50 Fund	366	27,054	754	175	–	2	273	–

② As of December 31, 2017

A. Summarized financial information

In millions of Korean won				
Company	Total assets	Total liabilities	Revenue	Total comprehensive income (loss)
Lite Pharm Tech, Inc.	19,775	4,134	13,689	130
KVG REIT I Co., Ltd.	–	–	12,825	10,044
JR REIT V Co., Ltd.	30,769	15,746	2,409	1,252
JR REIT VIII Co., Ltd.	107,087	64,826	6,920	2,337
JR REIT X Co., Ltd.	85,345	55,921	4,337	809
JR REIT XIII Co., Ltd.	46,898	29,123	1,772	248
KORAMCO Private REIT 50 Fund	46,337	27,137	3,010	831
KB Gimpo Logistics CR REIT Co., Ltd.	60,969	35,706	3,960	1,093
Yong In Jung Sim Co., Ltd.	4,500	–	–	–
LSK Global Pharma Services Co., Ltd.	9,112	10,831	349	106
Cosmo Tobacco Co., Ltd.	–	–	–	–

B. Additional financial information about joint ventures

In millions of Korean won								
Company	Cash and cash equivalents	Current financial liabilities	Non-current financial liabilities	Depre-ciation	Amortization	Interest income	Interest cost	Income tax expense
KB Gimpo Logistics CR REIT Co., Ltd.	759	35,325	381	999	–	3	1,276	–
KORAMCO Private REIT 50 Fund	577	26,847	290	759	–	2	970	–

(3) Changes in investments in associates and joint ventures for the current quarter and previous term are as follows

① As of March 31, 2018

In millions of Korean won			
Company	Beginning balance	Share of gain (loss)	Ending balance
Lite Pharm Tech, Inc.	3,166	40	3,206
JR REIT V Co., Ltd.	5,202	40	5,242
JR REIT VIII Co., Ltd.	9,187	30	9,217
JR REIT X Co., Ltd.	8,471	71	8,542
JR REIT XIII Co., Ltd.	4,805	8	4,813
KORAMCO Private REIT 50 Fund	16,168	(150)	16,018
KB Gimpo Logistics CR REIT Co., Ltd.	3,032	(29)	3,003
Yong In Jung Sim Co., Ltd.	1,000	(62)	938
LSK Global Pharma Services Co., Ltd.	–	–	–
Cosmo Tobacco Co., Ltd.	–	–	–
Total	51,031	(52)	50,979

② As of December 31, 2017

In millions of Korean won						
Company	Beginning balance	Acquisition	Disposal	Share of gain (loss)	Dividends	Ending balance
Lite Pharm Tech, Inc.	3,001	–	–	165	–	3,166
KVG REIT I Co., Ltd.	6,426	–	(6,860)	2,980	(2,546)	–
JR REIT V Co., Ltd.	5,420	–	–	761	(979)	5,202
JR REIT VIII Co., Ltd.	9,555	–	–	512	(880)	9,187
JR REIT X Co., Ltd.	8,697	–	–	315	(541)	8,471
JR REIT XIII Co., Ltd.	4,742	–	–	63	–	4,805
KORAMCO Private REIT 50 Fund	15,692	–	–	723	(247)	16,168
KB Gimpo Logistics CR REIT Co., Ltd.	2,943	–	–	198	(109)	3,032
Yong In Jung Sim Co., Ltd.	–	1,000	–	–	–	1,000
LSK Global Pharma Services Co., Ltd.	–	–	–	–	–	–
Cosmo Tobacco Co., Ltd.	–	–	–	–	–	–
Total	56,476	1,000	(6,860)	5,717	(5,302)	51,031

(4) Reconciliation of the summarized financial information presented to the carrying amount of the Group’s interest in associates and joint ventures as of the end of current quarter and end of previous term is summarized as follows

① As of March 31, 2018

In millions of Korean won					
Company	Net assets	Percentage of ownership	Share of net assets	Share of loss not recognized	Carrying amount
Lite Pharm Tech, Inc.	15,838	20.24%	3,206	–	3,206
JR REIT V Co., Ltd.	15,136	34.63%	5,241	–	5,241
JR REIT VIII Co., Ltd.	42,400	21.74%	9,218	–	9,218
JR REIT X Co., Ltd.	29,669	28.79%	8,542	–	8,542
JR REIT XIII Co., Ltd.	17,805	27.03%	4,813	–	4,813
KORAMCO Private REIT 50 Fund	19,022	84.21%	16,019	–	16,019
KB Gimpo Logistics CR REIT Co., Ltd.	25,030	12.00%	3,003	–	3,003
Yong In Jung Sim Co., Ltd.	4,220	22.22%	937	–	937
LSK Global Pharma Services Co., Ltd.	(621)	23.15%	(144)	144	–
Cosmo Tobacco Co., Ltd.	–	40.00%	–	–	–
Total					50,979

② As of December 31, 2017

In millions of Korean won					
Company	Net assets	Percentage of ownership	Share of net assets	Share of loss not recognized	Carrying amount
Lite Pharm Tech, Inc.	15,641	20.24%	3,166	–	3,166
JR REIT V Co., Ltd.	15,023	34.63%	5,202	–	5,202
JR REIT VIII Co., Ltd.	42,261	21.74%	9,187	–	9,187
JR REIT X Co., Ltd.	29,424	28.79%	8,471	–	8,471
JR REIT XIII Co., Ltd.	17,775	27.03%	4,805	–	4,805
KORAMCO Private REIT 50 Fund	19,200	84.21%	16,168	–	16,168
KB Gimpo Logistics CR REIT Co., Ltd.	25,263	12.00%	3,032	–	3,032
Yong In Jung Sim Co., Ltd.	4,500	22.22%	1,000	–	1,000
LSK Global Pharma Services Co., Ltd.	(1,719)	23.15%	(398)	398	–
Cosmo Tobacco Co., Ltd.	–	40.00%	–	–	–
Total					51,031

13. Property, Plant And Equipment

(1) Details of property, plant and equipment as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won						
Type	As of March 31, 2018			As of December 31, 2017		
	Acquisition cost	Accumulated depreciation and impairment	Carrying amount	Acquisition cost	Accumulated depreciation and impairment	Carrying amount
Land	600,031	–	600,031	667,291	–	667,291
Buildings	1,000,342	(467,614)	532,728	992,706	(457,583)	535,123
Structures	74,299	(45,692)	28,607	74,031	(45,121)	28,910
Machinery	1,328,118	(1,015,912)	312,206	1,314,043	(1,001,641)	312,402
Vehicles	11,544	(8,885)	2,659	11,247	(8,405)	2,842
Tools	66,869	(55,734)	11,135	66,357	(54,541)	11,816
Furniture and fixtures	232,763	(168,136)	64,627	227,245	(160,989)	66,256
Others	1,819	–	1,819	1,829	–	1,829
Construction in progress	112,458	–	112,458	130,510	–	130,510
Total	3,428,243	(1,761,973)	1,666,270	3,485,259	(1,728,280)	1,756,979

(2) Changes in property, plant and equipment for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won							
Type	Beginning balance	Acquisition	Disposal	Depreciation	Transfer of construction in progress	Net exchange difference and others (*)	Ending balance
Land	667,291	711	–	–	14,021	(81,992)	600,031
Buildings	535,123	486	(155)	(9,041)	4,034	2,281	532,728
Structures	28,910	53	–	(783)	369	58	28,607
Machinery	312,402	4,048	407	(15,825)	10,175	999	312,206
Vehicles	2,842	107	(29)	(217)	–	(44)	2,659
Tools	11,816	809	(129)	(1,414)	–	53	11,135
Furniture and fixtures	66,256	5,015	(315)	(7,440)	968	143	64,627
Others	1,829	–	–	–	–	(10)	1,819
Construction in progress	130,510	52,285	(134)	–	(29,567)	(40,636)	112,458
Total	1,756,979	63,514	(355)	(34,720)	–	(119,148)	1,666,270

(*) For the current quarter, land, buildings, structures and construction in progress transferred to investment property were of ₩110,884 million.

(3) Changes in property, plant and equipment for the previous quarter are as follows

In millions of Korean won							
Type	Beginning balance	Acquisition	Disposal	Depreciation	Transfer of construction in progress	Net exchange difference and others (*)	Ending balance
Land	541,980	3	–	–	–	(377)	541,606
Buildings	538,708	647	(370)	(8,992)	7,011	(2,204)	534,800
Structures	30,398	204	(108)	(820)	188	(133)	29,729
Machinery	331,145	4,149	(579)	(17,218)	9,314	(1,261)	325,550
Vehicles	2,415	222	(3)	(215)	294	(105)	2,608
Tools	11,370	429	(35)	(1,243)	–	(33)	10,488
Furniture and fixtures	62,698	6,580	52	(6,883)	227	(136)	62,538
Others	1,907	9	–	–	–	–	1,916
Construction in progress	85,908	74,428	–	–	(17,034)	(958)	142,344
Total	1,606,529	86,671	(1,043)	(35,371)	–	(5,207)	1,651,579

(*) For the previous quarter, land, buildings and structures transferred to investment property include ₩391 million.

14. Intangible Assets

(1) Details of intangible assets as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won						
Type	As of March 31, 2018			As of December 31, 2017		
	Acquisition cost	Accumulated depreciation and impairment	Carrying amount	Acquisition cost	Accumulated depreciation and impairment	Carrying amount
Goodwill	91,189	(85,472)	5,717	91,189	(85,472)	5,717
Industrial property rights	50,716	(38,390)	12,326	50,506	(38,193)	12,313
Facility usage rights	36,350	(1,113)	35,237	35,506	(1,113)	34,393
Other intangible assets	115,938	(85,019)	30,919	115,903	(84,424)	31,479
Intangible assets under development	3,275	(1,910)	1,365	2,756	(1,910)	846
Total	297,468	(211,904)	85,564	295,860	(211,112)	84,748

(2) Changes in intangible assets for the three-month periods ended March 31, 2018 and 2017 are as follows

A. For the three-month period ended March 31, 2018

In millions of Korean won							
Type	Beginning balance	Acquisition	Disposal	Depreciation	Transfer of construction in progress	Net exchange difference and others	Ending balance
Goodwill	5,717	–	–	–	–	–	5,717
Industrial property rights	12,313	127	(6)	(197)	89	–	12,326
Facility usage rights	34,393	844	–	–	–	–	35,237
Other intangible assets	31,479	175	–	(972)	–	237	30,919
Intangible assets under development	846	608	–	–	(89)	–	1,365
Total	84,748	1,754	(6)	(1,169)	–	237	85,564

B. For the three-month period ended March 31, 2017

In millions of Korean won						
Type	Beginning balance	Acquisition	Disposal	Depreciation	Net exchange difference and others	Ending balance
Goodwill	15,061	–	–	–	–	15,061
Industrial property rights	11,681	189	–	(190)	(2)	11,678
Facility usage rights	32,349	65	(917)	–	–	31,497
Other intangible assets	41,748	257	–	(1,134)	(520)	40,351
Intangible assets under development	4,090	–	–	–	–	4,090
Total	104,929	511	(917)	(1,324)	(522)	102,677

For the previous term, the Group recognized ₩15,662 million of impairment losses on goodwill and other intangible assets under development since the carrying amounts exceeded their recoverable amounts.

(4) Research and development expenditures recognized as expenses for the three-month periods ended March 31, 2018 and 2017 were as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Cost of sales	10	455
Selling, general and administrative expenses	8,508	7,620
Total	8,518	8,075

15. Investment property

(1) Details of investment property as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won						
Type	As of March 31, 2018			As of December 31, 2017		
	Acquisition cost	Accumulated depreciation and impairment	Carrying amount	Acquisition cost	Accumulated depreciation and impairment	Carrying amount
Land	203,838	–	203,838	129,105	–	129,105
Buildings	279,336	(82,188)	197,148	283,041	(81,147)	201,894
Assets in construction	38,232	–	38,232	–	–	–
Total	521,406	(82,188)	439,218	412,146	(81,147)	330,999

(2) Changes in investment property for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won								
Type	For the three-month period ended March 31, 2018				For the three-month period ended March 31, 2017			
	Land	Buildings	Assets in construction	Total	Land	Buildings	Assets in construction	Total
Beginning balance	129,106	201,893	–	330,999	129,655	211,925	–	341,580
Depreciation	–	(2,665)	–	(2,665)	–	(2,750)	–	(2,750)
Transfer from (to) property, plant and equipment	74,732	(2,080)	38,232	110,884	247	144	–	391
Ending balance	203,838	197,148	38,232	439,218	129,902	209,319	–	339,221

(3) Details of profit or loss recognized related to the investment property for the three-month periods ended March 31, 2018 and 2017 are summarized as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Rental income	11,859	11,069
Direct operating expense	(2,748)	(2,750)
Total	9,111	8,319

(4) The carrying amount and the fair value of investment property as of March 31, 2018 and December 31, 2017 were as follows

In millions of Korean won				
Type	As of March 31, 2018		As of December 31, 2017	
	Fair value	Carrying amount	Fair value	Carrying amount
Land	738,166	203,838	751,251	129,105
Buildings	288,775	197,148	293,756	201,894
Assets in construction	38,232	38,232	–	–
Total	1,065,173	439,218	1,045,007	330,999

The fair value of investment property was determined based on the yield capitalization method by external, independent values. The fair value measurement for all of the investment properties has been categorized as Level 3 fair value based on the inputs to the valuation techniques used.

16. Non-Current Assets Held For Sale

Changes in non-current assets held for sale for the current quarter and previous term are as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Beginning balance	–	21,165
Transfer from property, plant and equipment	–	–
Transfer from investment property	–	–
Disposal	–	(21,165)
Ending balance	–	–

The Group has sold the land and building in Pyeongtaek City, Gyeonggi-do, accounted for non-current assets held for sale in the previous term and has recognized ₩283 million as gain on sale of property, plant and equipment.

However, the Group decided to use the fragrance capsule business facility, which was classified as a non-current asset held for sale during the previous term, as a research facility. As the non-current asset held for sale is held by a subsidiary, the consolidated interim financial statements are restated for the period when the asset was classified as non-current asset held for sale as follows

(1) Consolidated statement of financial position as of the end of previous quarter

In millions of Korean won		
Type	Before restatement	After restatement
Non-current assets	3,278,371	3,282,898
Machinery	1,332,879	1,338,858
Accumulated depreciation	(1,011,856)	(1,013,308)
Non-current assets held for sale	26,315	21,165
Total assets	9,275,713	9,275,090
Retained earnings	777,479	776,856
Total equity	6,853,152	6,852,529

(2) Consolidated statement of comprehensive income (loss) for the previous quarter

In millions of Korean won		
Type	Before restatement	After restatement
Selling, general and administrative expenses	305,170	305,295
Depreciation	10,533	10,658
Operating profit	395,456	395,331
Profit before income tax	331,808	331,683
Profit for the quarter	235,161	235,036

17. Pledged Assets

Assets pledged as collateral as of March 31, 2018 and December 31, 2017 are summarized as follows

(1) As of March 31, 2018

In millions of Korean won					
Type	Carrying amount	Type	Received amount	Collateralized amount	Holder
Investment property	146,374	Leasehold deposits received	11,183	11,830	Metlife Insurance Korea Co., Ltd., etc.
Property, plant and equipment; investment property; etc.	67,832	Current long-term borrowings	2,166	65,000	Kookmin Bank
		Long-term borrowings	9,750		Kookmin Bank
Property, plant and equipment	172,888	Investment subsidy	3,488	4,186	Wonju-si
		Investment subsidy	–	660	Chungju-si
		Short-term borrowings	10,800	15,500	Korea Development Bank (“KDB”)
		Right to collateral security and lease	3,104	3,493	Korea Workers’ Compensation & Welfare Service etc.
		Short-term borrowings	10,000	24,000	KEB Hana Bank
Other financial assets	1,280	ACH pledged	–	1,280	Bank of Oklahoma
	6,340	Performance bond	–	6,340	Korea Land & Housing Corporation
Total	394,714		50,491	132,289	

(2) As of December 31, 2017

In millions of Korean won					
Type	Carrying amount	Reason for providing collateral	Received amount	Collateralized amount	Holder
Investment property	148,810	Leasehold deposits received	12,982	13,889	Metlife Insurance Korea Co., Ltd., etc.
Property, plant and equipment and investment property	79,800	Short-term borrowings	14,666	76,138	KEB Hana Bank, etc.
		Long-term borrowings	10,292	12,862	KEB Hana Bank, etc.
Property, plant and equipment	154,359	Investment subsidy	–	4,189	Wonju-si
		Investment subsidy	–	660	Chungju-si
		Long-term and short-term borrowings	10,800	15,500	KDB
		Right to collateral security and lease	3,104	3,493	Korea Workers’ Compensation & Welfare Service etc.
Other financial assets	1,287	ACH pledged	–	1,287	Bank of Oklahoma
	6,340	Performance bond	–	6,340	Korea Land & Housing Corporation
Total	390,596		51,844	134,358	

18. Short-term borrowings

(1) Short-term borrowings as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won				
Type	Lender	Annual interest rate	As of March 31, 2018	As of December 31, 2017
Borrowings	KEB Hana Bank	3.48%–3.85%	10,000	12,500
	KEB Hana Bank Bahrain	2.50%	5,868	5,881
	KDB	3.02%	1,500	100,237
	Korea Agro-Fisheries & Food Trade	1.00%	15,000	15,000
	Kookmin Bank	–	–	9,249
	The Export-Import Bank of Korea	–	–	10,000
	Woori Bank	–	–	200
	Subtotal		32,368	153,067
Customer credit contracts (*)	Nonghyup Bank, etc.	5.92%, etc.	17,867	21,590
Total			50,235	174,657

(*) The Group has entered into a customer credit contract with Nonghyup Bank, etc. The financial institutions pay trade receivables on behalf of customers, and the Group has provided guarantees to the financial institutions for customers.

(2) Long-term borrowings as of the end of current quarter and end of previous term are summarized as follows

In millions of Korean won					
Type	Lender	Maturity	Annual interest rate	As of March 31, 2018	As of December 31, 2017
Borrowings	Nonghyup Bank	2018.12.31–2022.12.31	–	47,168	47,193
	Kookmin Bank	2023.09.11	2.4%–3.0%	11,917	12,458
	KDB	2021.08.19	2.33%–2.90%	8,500	8,500
	KDB	2021.11.10	3.44%	800	800
Redeemable convertible preferred shares (*1)				35,340	35,340
Total				103,725	104,291
Consolidated interim statements of financial position:					
Current				4,410	3,702
Non-current				99,315	100,589
Total				103,725	104,291

(*1) Details of convertible bonds and preferred shares as of the end of current quarter are summarized as follows

Issuing company	Renzoluc Pte, Ltd.
Issue date	September 14, 2012
Issued value	35,340 million
Carrying amount	35,340 million
Maturity	The convertible instrument will mature 10 years from the date of establishment of QCP 2011 Corporate Partnership Private Equipment Fund (“PEF”).
Convertible rights to ordinary share	The instrument can be converted into 6,978,948 ordinary shares at any time after five years from the issue date.
Repayment claim right	Payable on demand from 270 days prior to the expiration of the PEF

(3) As discussed in Note 17 to the consolidated interim financial statements, the Group provided collateral for the above borrowings.

19. Trade and other payables

Trade and other payables as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won				
Type	As of March 31, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Leasehold deposits received	21,680	12,686	23,189	9,406
Trade payables	96,291	–	63,083	–
Withholdings	194,662	–	165,364	–
Accrued expenses	141,736	17,923	202,729	17,532
Other payables	64,735	5,389	68,935	7,498
Accrued dividends	505,061	–	–	–
Total	1,024,165	35,998	523,300	34,436

20. Retirement Benefits Plan

(1) Details of profit or loss recognized related to retirement benefits for the three-month periods ended March 31, 2018 and 2017 were as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Defined benefit plans:		
Current service cost	10,815	11,300
Net interest on net defined benefit liability	457	747
Subtotal	11,272	12,047
Defined contribution plan:		
Contributions recognized as expense	2,486	2,241
Other long-term employee benefits:		
Current service cost	538	–
Total	14,296	14,288

The Group recognized termination benefits amounting to ₩2,510 million and ₩689 million as an expense for the current quarter and previous quarter, respectively.

(2) Net defined benefit liability as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Present value of defined benefit obligations	432,661	427,161
Fair value of plan assets	(344,977)	(351,378)
Net defined benefit liabilities	87,684	75,783

21. Refund liabilities

(1) Refund liabilities as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won									
Type	As of March 31, 2018					As of December 31, 2017			
	Beginning	Change in accounting policy	Increases	Decreases	End	Beginning	Increases	Decreases	End
Provision for refund	8,473	1,333	971	–	10,777	4,704	4,800	(1,031)	8,473
Provision for site restoration	3,363	–	232	–	3,595	–	3,363	–	3,363
Provision for others	4,497	–	21	–	4,518	–	4,497	–	4,497
Ending amount	16,333	1,333	1,224	–	18,890	4,704	12,660	(1,031)	16,333

(2) In the case of returnable sales, the Group estimates the amount of return capability expected at the time of sale and deducts the expected amount of return from sales and cost of sales to establish a debt to cover the returns. In addition, the refund assets as of the end of current quarter are as follows

In millions of Korean won	
Type	Amount
Refund assets	1,146

(3) The Group estimates the best amount of future expected restoration costs of retained assets as of the end of current term. The Group has recognized restoration costs in the acquisition cost of property, plant and equipment, which is expected to be used at the end of the lease term.

(4) The Group has entered into a contract with Iran Tobacco Company to produce more than certain number of tobacco each year, and the amount expected to be below the certain number of tobacco to be produced by Iran Tobacco Company in accordance with the agreement is set as other provision.

22. Share capital

(1) Details of share capital as of March 31, 2018 and December 31, 2017 were as follows

Type	As of March 31, 2018	As of December 31, 2017
Authorized	800,000,000 shares	800,000,000 shares
Amount per share	₩5,000	₩5,000
Issued	137,292,497 shares	137,292,497 shares
Share capital	₩954,959 million	₩954,959 million

The Parent Company has 53,699,400 shares of treasury shares reacquired and retired in prior years. Accordingly, as of December 31, 2017, the Parent Company's ordinary share differs from the aggregate par value of issued shares by ₩268,497 million.

(2) Changes in other capital surplus for the current quarter and previous term are as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Beginning balance	(29,720)	(3,429)
Acquisition of non-controlling interests	–	(26,291)
Ending balance	(29,720)	(29,720)

For the previous term, the Parent Company acquired additional shares of PT Sentosa Ababi Purwosari, PT Trisakti Purwosari Makmur and PT Mandiri Maha Mulia, and following such acquisition, changes in the amount of shares related to such acquisition have been offset as other capital surplus.

23. Treasury shares

Treasury shares as of March 31, 2018 and December 31, 2017 are summarized as follows

Type	As of March 31, 2018	As of December 31, 2017
Number of treasury shares	11,027,370 shares	11,027,370 shares
Treasury shares	₩(328,157) million	₩(328,157) million
Profit from sales of treasury shares	₩513,776 million	₩513,776 million

24. Reserves

(1) Reserves as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Other comprehensive income (loss)-Financial assets measured at fair value–net change in fair value (Previous term: Available-for-sale financial assets-net change in fair value)	(35,965)	7,730
Foreign operations-Foreign currency translation differences	(101,536)	(91,719)
Legal reserve	603,145	603,145
Voluntary reserve	4,893,211	4,408,176
Total	5,358,855	4,927,332

(2) Other comprehensive income (loss) as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Other comprehensive income (loss)-net change in fair value before tax	(50,178)	10,662
Tax effect	14,213	(2,932)
Other comprehensive income (loss)-net change in fair value after tax	(35,965)	7,730

(3) The Korean Commercial Act requires the Company to appropriate a legal reserve in an amount equal to at least 10% of cash dividends for each accounting period until the reserve equals 50% of stated capital. The legal reserve may be used to reduce a deficit or may be transferred to ordinary shares in connection with a free issue of shares.

(4) Voluntary reserve as of March 31, 2018, and December 31, 2017, is summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Reserve for business rationalization	12,851	12,851
Reserve for research and human resource development	–	10,000
Reserve for business expansion	698,881	698,881
Unconditional reserve	4,181,479	3,686,444
Total	4,893,211	4,408,176

① Reserve for business rationalization

Until December 10, 2002, under the Restriction of Special Taxation Act, investment tax credits were allowed for certain investments. The Parent Company was, however, required to appropriate from retained earnings the amount of tax benefits received and transfer such amount into a reserve for business rationalization.

Effective December 11, 2002, the Parent Company was no longer required to establish a reserve for business rationalization despite tax benefits received for certain investments, and consequently, the existing balance is now regarded as a voluntary reserve.

② Reserve for research and human resource development

According to the Restriction of Special Taxation Act, certain taxable deductions are required to be transferred from retained earnings to reserve for research and human resource development. This reserve may be used for each purpose and their remaining amounts could be reclassified as a voluntary reserve.

③ Reserve for business expansion and other reserves

The Parent Company appropriated reserves without specific purposes. Those reserves can be used for other purposes upon a resolution at the general meeting of shareholders.

25. Retained earnings

Changes in retained earnings for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Beginning balance	1,733,863	1,611,532
Change in accounting policy	(20,144)	–
Dividends	(505,061)	(454,554)
Transfer from reserve for research and human resource development	10,000	10,000
Accumulation of unconditional reserve	(495,036)	(623,915)
Profit for the quarter	249,369	235,036
—Less: Non-controlling interests	(470)	(653)
Remeasurements of net defined benefit liability (net of tax)	(1,066)	(591)
—Less: Non-controlling interests	1	1
Ending balance	971,456	776,856

26. Revenue from Real Estate Sales

Changes in balance of contract amount for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Construction	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Beginning balance	–	133,491
Contract increase	–	–
Revenue recognition	–	(19,860)
Ending balance	–	113,631

27. Operating profit

(1) Details of expenses classified by nature incurred for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Changes in inventories	59,257	144,038
Raw materials and consumables purchased	237,310	190,240
Employee benefits	151,473	134,203
Retirement and termination benefits	16,268	14,977
Depreciation	37,385	38,121
Amortization	1,169	1,324
Employee welfare	17,271	15,977
Advertising	57,047	61,458
Commissions	102,693	91,134
Other expenses	76,349	91,945
Total	756,222	783,417

(2) Details in selling, general and administrative expenses for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Salaries	102,165	90,040
Retirement and termination benefits	10,909	9,877
Employee welfare	12,233	10,698
Travel	4,076	3,600
Communications	1,404	1,228
Utilities	3,140	2,572
Taxes and dues	2,270	2,624
Supplies	1,056	912
Rent	7,239	6,530
Depreciation	11,186	10,658
Amortization	947	1,118
Repairs and maintenance	1,116	617
Vehicles	1,693	1,443
Insurance	1,170	669
Commissions	82,539	77,551
Freight and custody	11,303	12,951

Conferences	1,037	1,261
Advertising	57,020	61,435
Training	1,155	1,276
Prizes and rewards	806	331
Cooperation	198	234
Research and development	8,508	7,620
Impairment loss (reversal of impairment loss) on trade receivables	(418)	50
Total	322,752	305,295

28. Other Income and Expenses

(1) Details of other income for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Foreign currency transaction gain	2,875	3,986
Foreign currency translation gain	3,383	6,239
Gain on sale of property, plant and equipment	474	121
Gain on sale of intangible assets	–	685
Gain in fair value from derivatives	6,006	–
Gain from derivative transactions	824	–
Others	22,335	5,393
Total	35,897	16,424

(2) Details of other expenses for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Foreign currency transaction loss	1,996	15,837
Foreign currency translation loss	12,136	81,274
Impairment loss on other receivables	–	7
Donations	2,030	2,095
Loss on sale of property, plant and equipment	347	306
Loss on sale of intangible assets	6	162
Loss on sale of investments in joint ventures	–	1,794
Others	3,819	527
Total	20,334	102,002

29. Net Finance Income

(1) Details of net finance income for the three-month periods ended March 31, 2018 and 2017 are as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Finance income:		
Interest income	3,857	11,601
Dividend income	8,452	7,803
Investment income on long-term deposits in MSA Escrow Fund	–	2,043
Current term’s income-Gain on fair value of financial assets	15,524	–
Current terms’ income-Gain on fair value on sale of financial assets	7,762	–
Gain on sale of available-for-sale financial assets	–	554
Sum of finance income	35,595	22,001
Finance cost:		
Interest expense	(1,363)	(1,533)
Current term’s income-Loss on fair value of financial assets	(1,307)	–
Sum of finance cost	(2,670)	(1,533)
Net finance income	32,925	20,468

(2) Details of interest income included in finance income for the years ended March 31, 2018 and 2017 were as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Deposits	1,083	10,792
Current term’s income-Fair value of financial assets	417	7
Trade and other receivables	602	802
Long-term deposits	1,755	–
Total	3,857	11,601

(3) Details of interest income included in finance income for the years ended March 31, 2018 and 2017 were as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Borrowings	831	687
Trade and other receivables	398	846
Others	134	–
Total	1,363	1,533

30. Income tax expense

(1) The income tax was calculated by adjusting the adjustments recognized in the current quarter and previous quarter with regard to the current term's income tax in the past period in the current term's income tax expenses, deferred income tax expenses (revenue) arising from the occurrence and dissolution of temporary differences and income tax expenses (revenue) related to items recognized as other than current term's profit and loss. The average effective tax rate of the current quarter and previous quarter was 30.69% and 29.13%, respectively.

(2) In case the tax revenue in the period in which temporary differences are to be deducted is expected to be sufficient, the Group may recognize it as deferred income tax assets, and in case the tax revenue expected in the future is changed, the said deferred income tax assets may change.

31. EPS

Changes in EPS for the three-month periods ended March 31, 2018 and 2017 are as follows

Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Profit for the period attributable to owners of the Parent Company	₩248,897 million	₩234,383 million
Weighted-average number of ordinary shares outstanding	126,265,127 shares	126,265,127 shares
Basic and diluted EPS	₩1,971	₩1,856

The weighted-average number of ordinary shares outstanding is the number of ordinary shares outstanding at the beginning of the period, adjusted by the number of ordinary shares bought back or issued during the period multiplied by a time-weighted factor.

32. Transactions and Balances with Related Parties

(1) Details of parent and subsidiary relationships and related companies as of March 31, 2018 and December 31, 2017 were as follows

Type	As of March 31, 2018	As of December 31, 2017
Associates	Cosmo Tobacco Co., Ltd.	Cosmo Tobacco Co., Ltd.
	Lite Pharm Tech, Inc.	Lite Pharm Tech, Inc.
	–	KVG REIT 1 Co., Ltd.
	JR REIT V Co., Ltd.	JR REIT V Co., Ltd.
	JR REIT VIII Co., Ltd.	JR REIT VIII Co., Ltd.
	LSK Global Pharma Services Co., Ltd.	LSK Global Pharma Services Co., Ltd.
	JR REIT X Co., Ltd.	JR REIT X Co., Ltd.
	JR REIT XIII Co., Ltd.	JR REIT XIII Co., Ltd.
	Yong In Jung Sim Co., Ltd.	Yong In Jung Sim Co., Ltd.
Joint ventures	KB Gimpo Logistics CR REIT Co., Ltd.	KB Gimpo Logistics CR REIT Co., Ltd.
	KORAMCO Private REIT 50 Fund	KORAMCO Private REIT 50 Fund

(2) Significant transactions that occurred in the normal course of business with related companies for the three-month periods ended March 31, 2018 and 2017 are summarized as follows

In millions of Korean won					
Type	Company	For the three-month period ended March 31, 2018		For the three-month period ended March 31, 2017	
		Sales and other income	Trade and other expenses	Sales and other income	Trade and other expenses
Associates and joint ventures	KVG REIT 1 Co., Ltd.	–	–	375	–
	KB Gimpo Logistics CR REIT Co., Ltd.	45	–	–	–
	KORAMCO Private REIT 50 Fund	220	–	–	–
Total		265	–	375	–

(3) Account balances with related companies as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won			
Type	Company	As of March 31, 2018	As of December 31, 2017
		Loans etc.	Loans etc.
Associates	LSK Global Pharma Services Co., Ltd.	1,200	1,500
	JR REIT V Co., Ltd.	–	242
	JR REIT VIII Co., Ltd.	212	212
	JR REIT XIII Co., Ltd.	145	145
	KB Gimpo Logistics CR REIT Co., Ltd.	101	60
	KORAMCO Private REIT 50 Fund	204	–
Total		1,862	2,159

(4) Details of financial transactions with related parties for the three-month periods ended March 31, 2018 and December 31, 2017 were as follows

In millions of Korean won					
Type	Company	As of March 31, 2018	As of December 31, 2017		
		Capital increase	Increase	Loans collection	Capital increase
Associates	LSK Global Pharma Services Co., Ltd.	300	–	2,054	554
	Yong In Jung Sim Co., Ltd.	–	1,000	–	–
Total		300	1,000	2,054	554

(5) There is no guarantee provided by or to related parties.

(6) Details of key management personnel compensation for the three-month periods ended March 31, 2018 and 2017 are summarized as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Short-term employee benefits	6,970	7,038
Retirement benefits	1,319	1,026
Total	8,289	8,064

33. Risk Management and Fair Value of Financial Instruments

(a) Overview

The Group has exposure to the following risks from its use of financial instruments

- Market risk
- Credit risk
- Liquidity risk

This note presents information about the Group's exposure to each of the above risks and the Group's objectives, policies and processes for measuring and managing risk, including quantitative disclosures.

(b) Risk Management Framework

The purpose of managing financial risks is to identify the potential risk factors that may affect the Group's financial performance and minimize, eliminate and avoid it to the extent that is acceptable. One of the principal responsibilities of the treasury department is to manage the financial risks arising from the Group's underlying operations. The treasury department monitors and manages the financial risk arising from the Group's underlying operations in accordance with the risk management policies and procedures authorized by the board of directors. Also, the treasury department provides an internal report analyzing the nature and exposure level of financial risks to the Risk Management Committee of the Group. The Risk Management Committee prepares the overall strategy for financial risk management and evaluates the effectiveness of the financial risk management strategy. In addition, the Parent Company's audit committee consistently observes the compliance of the risk management policy and procedure and reviews the risk exposure limit of the Group. The Group applied the same financial risk management strategy that was applied in the previous period.

(c) Management of Financial Risks

(1) Market risk

Market risk is the risk that changes in market prices – such as foreign exchange rates, interest rates and equity prices – will affect the Company's income or the value of its financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

① Currency risk

The Group has exposure to the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates arising from the export and import of tobacco. The Group's management has measured the currency risk internally and regularly, and has entered into foreign currency forward contracts to hedge foreign currency risk, if necessary.

The carrying amounts of monetary assets and liabilities denominated in a currency other than the functional currency as of March 31, 2018 and December 31, 2017 were as follows

In millions of Korean won				
Type	As of March 31, 2018		As of December 31, 2017	
	Assets	Liabilities	Assets	Liabilities
USD	1,176,685	10,700	960,406	55,438
EUR	33,528	8,294	1,718	5,241
JPY, etc.	47,792	156	10,043	1
Total	1,258,005	19,150	972,167	60,680

As of March 31, 2018 and December 31, 2017, the effects of a 10% weakening or strengthening of functional currency against foreign currencies on profit or loss were as follows

In millions of Korean won				
Type	As of March 31, 2018		As of December 31, 2017	
	10% weakening	10% strengthening	10% weakening	10% strengthening
Increase (decrease) in profit before tax	123,886	(123,886)	91,149	(91,149)

② Equity price risk

The Group has exposure to equity price risk, which arises from listed available-for-sale equity instruments. The Group's management has monitored the proportion of equity instruments in its investment portfolio based on market indices. Material investments within the portfolio are managed on an individual basis, and all buy and sell decisions are approved by the Group's management.

As of March 31, 2018 and December 31, 2017, the effects of a 5% fluctuation in the price index of stocks on comprehensive income were as follows

In millions of Korean won				
Type	As of March 31, 2018		As of December 31, 2017	
	5% increase	5% decrease	5% increase	5% decrease
Increase (decrease) in comprehensive income (loss) before tax	1,836	(1,836)	6,040	(6,040)

③ Interest rate risk

The Group has exposure to the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group's management has monitored the level of interest rates regularly and has maintained the balance of borrowings at variable rates and fixed rates. As of March 31, 2018, there is no significant effect on cash flows or the fair value of financial liabilities from the interest rate fluctuation, considering the amounts of interest bearing liabilities.

(2) Credit risk

The Group has exposure to the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The Group has transacted with customers with high credit ratings to manage credit risk, and has implemented and operated policies and procedures for credit enhancements of the financial assets. Counterparty credit risk is managed by evaluating its credit rating and limiting the aggregate amount and duration of exposure before sales commence, and the Group has been provided collateral and guarantees. The credit ratings of all counterparties and the level of collateral and guarantees are reviewed regularly. Analysis of financial assets past due has been reported interim and appropriate measures have been taken to secure the Group's assets.

The carrying amount of financial assets is maximum exposure to credit risk. The maximum exposure to credit risk as of March 31, 2018 and December 31, 2017 is as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Cash and cash equivalents (excluding cash on hand) (*)	216,353	1,193,221
Other financial assets	238,438	1,570,250
Current term’s income-Financial assets at fair value (*)	2,682,632	–
Trade and other receivables	1,141,115	1,190,594
Derivatives	6,006	–
Long-term deposits in MSA Escrow Fund	532,240	510,223
Total	4,816,784	4,464,288

(*) Special trust fund for the cash equivalents for the end of current quarter is included in the current term’s income-financial assets at fair value

(3) Liquidity risk

The Group has exposure to the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. The Group’s management has established short-term and long-term financial management plans to manage the liquidity risk and analyzed cash outflows occurred and cash outflows budgeted so as to match the maturity structure of financial assets and financial liabilities. The Group’s management determines whether or not the financial liabilities are repayable with the operating cash flows and cash inflows from financial assets.

The contractual maturity analysis with a residual contractual maturity of financial liabilities as of March 31, 2018 and December 31, 2017 is as follows

In millions of Korean won						
Type	Carrying amount	Contractual cash flows	Residual contractual maturity			
			Within 3 months	Between 3 months and 1 year	Between 1 year and 5 years	Beyond 5 years
End of current quarter:						
Long-term borrowings	99,315	99,706	–	–	99,706	–
Current portion of long-term borrowings	4,411	4,693	2,166	2,527	–	–
Short-term borrowings	50,235	56,541	7,196	49,345	–	–
Trade and other payables	865,501	866,237	753,055	87,005	26,164	13
Total	1,019,462	1,027,177	762,417	138,877	125,870	13
End of previous term:						
Long-term borrowings	100,589	103,057	362	1,080	87,157	14,458
Current portion of long-term borrowings	3,702	3,753	560	3,193	–	–
Short-term borrowings	174,657	181,003	22,623	158,380	–	–
Trade and other payables	374,840	375,733	330,629	28,750	16,069	285
Total	653,788	663,546	354,174	191,403	103,226	14,743

The above financial liabilities are presented at the nominal value of undiscounted future cash flows as of the earliest period at which the Group can be required to pay.

(4) The carrying amounts of each category of financial assets and liabilities as of March 31, 2018 and December 31, 2017 are summarized as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Financial assets:		
Available-for-sale financial assets	–	471,763
Current term's income-Financial assets at fair value (*)	2,682,632	–
Other comprehensive income (loss)-Financial assets at fair value	278,488	–
Derivatives	6,006	–
Financial assets measured at amortized cost		
—Cash and cash equivalents (*)	242,247	1,230,176
—Other financial assets	238,438	1,570,250
—Trade and other receivables	1,141,115	1,190,594
—Long-term deposits in MSA Escrow Fund	532,240	510,223

Subtotal	2,154,040	4,501,243
Total financial assets	5,121,166	4,973,006
Financial liabilities:		
Financial liabilities measured at amortized cost		
—Long-term borrowings	99,315	100,589
—Current portion of long-term borrowings	4,411	3,702
—Short-term borrowings	50,235	174,657
—Trade and other payables	865,501	374,840
Total financial liabilities	1,019,462	653,788

(*) Special trust fund for the cash equivalents for the end of current quarter is included in the current term's income-financial assets at fair value

(5) The fair value measurements classified by fair value hierarchy as of March 31, 2018 and December 31, 2017 were as follows

In millions of Korean won				
Type	Carrying amount	Fair value		
		Level 1	Level 2	Level 3
End of current quarter:				
Current term's income-Financial assets at fair value	2,682,632	–	2,503,721	178,911
Other comprehensive income (loss)-Financial assets at fair value	278,488	228,161	–	50,327
Derivative assets	6,006	–	6,006	–
Total	2,967,126	228,161	2,509,727	229,238
End of previous term:				
Available-for-sale financial assets	421,886	237,717	–	184,169

(*) Special trust fund for the cash equivalents for the end of current quarter is included in the current term's income-financial assets at fair value

There is no transfer between fair value hierarchy levels of recurring fair value measurements during this quarter and the previous year.

The fair value measurements for available-for-sale equity instruments in real estate trust fund has been measured using the adjusted net asset method, DCF(discounted cash flow) and option-pricing model and categorized as a Level 3 fair value based on the inputs to the valuation techniques used. Changes in fair value classified as Level 3 for the three-month period ended March 31, 2018 and for the year ended March 31, 2017 were as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Beginning balance (*)	234,046	132,956
Acquisition	450	70,946
Disposal	(5,239)	(22,798)
Changes in fair value	(19)	3,065
Ending balance	229,238	184,169

(*) Available-for-sale financial assets measured using the cost method, in the financial statements as of December 31, 2017, are classified as financial assets at fair value through other comprehensive income in the financial statements as of March 31, 2018, with the effect of ₩ 49,722 million included.

(6) Details of finance income (costs) by categories for the for the three-month period ended March 31, 2018 and for the year ended March 31, 2017 as follows

① For the three-month ended March 31, 2018

In millions of Korean won						
Type	Profit or loss-Financial assets at fair value	Other comprehensive income (loss)-Financial assets at fair value	Derivative asset	Financial assets measured at amortized cost	Financial liabilities measured at amortized cost	Total
Profit or loss:						
Interest income	–	–	–	3,857	–	3,857
Dividend income	–	8,185	–	–	–	8,185
Gain and loss on valuation	14,217	–	6,006	–	–	20,223
Gain on sale of available-for-sale financial assets	7,762	–	824	–	–	8,586
Interest expense	–	–	–	–	(1,363)	(1,363)
Impairment loss on available-for-sale financial assets	–	–	–	418	–	418
Total	21,979	8,185	6,830	4,275	(1,363)	39,906
Comprehensive income (loss) before tax:						
Net change in fair value	–	(9,556)	–	–	–	(9,556)
Total	–	(9,556)	–	–	–	(9,556)

② For the three-month period ended March 31, 2017

In millions of Korean won				
Type	Available-for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
profit or loss:				
Interest income	7	11,594	–	11,601
Dividend income	7,803	–	–	7,803
Investment profit on long-term deposits in MSA Escrow Fund	–	2,043	–	2,043
Gain on sale of available-for-sale financial assets	554	–	–	554
Interest expense	–	–	(1,533)	(1,533)
Total	8,364	13,637	(1,533)	20,468
Comprehensive income (loss) before tax:				
Net change in fair value	7,262	–	–	7,262
Reclassification due to disposal	(554)	–	–	(554)

34. Capital Management

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The board of directors seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position.

The Group monitors capital using equity and net debt by deducting cash and cash equivalents and current financial instruments from borrowings. The Group applied the same capital management strategy that was applied in the previous year. The Group's capital structure as of March 31, 2018 and December 31, 2017 is as follows

In millions of Korean won		
Type	As of March 31, 2018	As of December 31, 2017
Net debt	153,960	278,948
Less: Cash and cash equivalents	(1,099,779)	(1,230,176)
Less: Current other financial assets	(1,868,280)	(1,563,900)
Net equity (net asset)	(2,814,099)	(2,515,128)
Total equity	7,499,347	7,829,760

35. Contingent Liabilities and Commitments

(1) Payment of long-term deposits (MSA Escrow Fund)
Each year the Group deposits a proportion of sales of tobacco products in the United States in accordance with the MSA (Tobacco Master Settlement Agreement) under the Escrow Statute of the U.S. government. The MSA Escrow Funds are maintained to pay the medical expenses of tobacco purchasers who have suffered health effects as a result of smoking. The unused portion of this fund will be refunded to the Group 25 years from the date of each annual funding. The Group recorded as long-term deposits the amounts paid into the MSA Escrow Funds of state governments in the United States against potential litigation and damages related to the export of tobacco to the United States.

(2) As of March 31, 2018, the Group's pending litigations are as follows.

In millions of Korean won				
Type	Suit parties	Case contents	Progress	Litigation value
Lawsuits in which the Group is involved as a plaintiff:				
Seoul Central District Court	Lee Young Geun and one other	Compensation for damages	First trial in progress	1,200
Seoul Eastern District Court	Han Jae Geuk and four others	Compensation for damages	First trial in progress	3,338
Daejeon District Court	Superintendent of North Daejeon Tax Office	Claim for cancellation of corporate tax disposition and others	Partially won first trial/second trial in progress	3,440
Seoul Central District Court	Tong Yang Moolsan and two others	Compensation for damages	First trial in progress	222
Seoul Central District Court	Kim Moo Seok and four others	Compensation for damages	First trial in progress	4,774

Seoul Central District Court	Seol Young Geon, CEO of Cell Co., Ltd. and four others	Compensation for damages	First trial in progress	1,543
Seoul Central District Court	Uniontech and three others	Compensation for damages	First trial in progress	4,958
Seoul Central District Court	LBC Soft Co., Ltd.	Eviction lawsuit	First trial in progress	148
Seoul Central District Court	IT&U Co., Ltd.	Eviction lawsuit	First trial in progress	101
Others	Nine lawsuits including compensation for damages			630
Sum of lawsuits in which the Group is involved as a plaintiff				20,354
Lawsuits in which the Group is involved as a defendant:				
Seoul Central District Court	National Health Insurance Service	Compensation for damages	First trial in progress	53,742
Patent court	Damin LNT Co., Ltd.	Compensation for damages	Won the first trial/second trial in progress	200
Daegu District Court	Park Sang Tae	Claim for return of contract deposit	First trial in progress	215
Cheongju District Court	Joo Sang Ja	Registration of ownership right cancellation	First trial in progress	13
Seoul Central District Court	V manne piece	Litigation on prohibition of patent infringement	First trial in progress	200
Others	Three lawsuits including cancellation of collateral security rights			1,077
Sum of lawsuits in which the Group is involved as a defendant				55,447

(3) Regular tax investigation on subsidiaries in Indonesia is ongoing as of the end of current quarter; however, the Group expects that there is no significant impact on its consolidated interim financial statements.

(4) As of the end of current quarter, the Group has entered into letter of credit agreements with KEB Hana Bank and other banks with limits in the aggregate of USD 179,700 thousand.

(5) As of the end of current quarter, the Group's trade receivables from the export of cigarettes are insured against non-payment up to USD 31,833 thousand by an export guarantee insurance with the Korea Trade Insurance Corporation.

(6) As of the end of current quarter, the Group has been provided with a foreign currency payment guarantee by KEB Hana Bank and Westchester Fire Insurance Group up to USD 36,000 thousand and USD 20,000 thousand, respectively, for L/C(Letter of Credit) or guarantees related to its foreign exports. Details of guarantees exercised as of the end of current quarter are summarized as follows

(Unit: 1,000 USD, 1,000 THB, 1 million IDR)	
Type	Exercised amount
Customs bond and L/C opening of KT&G USA	USD 31,417
Performance guarantee for export of tobacco sheet to Thailand Tobacco Monopoly	THB 6,043
Payment guarantee for purchase of certificate stamp of PT Trisakti Purwosari Makmur, PT Mandiri Maha Mulia, etc.	IDR 4,221

(7) As of the end of current quarter, the Group has been provided with guarantees of USD 6,164 thousand from Travelers Casualty and Surety Group of America for the execution of escrow deposits.

(8) The Group has maintained a contract with the farmers who grow six-year-old green ginseng for

purchase volume guarantees and recorded contractual amounts paid to the farmers as long-term advance payments and advance payments in the amount of ₩69,359 million (₩69,383 for end of previous term) and ₩59,437 million, respectively.

(9) As of the end of current quarter, the Group has an accounts receivable loan agreement with a limit of ₩107,000 million with KEB Hana Bank and other financial institutions.

(10) The Group has a trade bill loan agreement with a limit of ₩10,000 million with KEB Hana Bank.

(11) As of the end of current quarter, the Group has a borrowing agreement with a limit of ₩203,134 million with KEB Hana Bank.

(12) As of the end of current quarter, the details of notes provided as blank notes with regard to the borrowings of the Group are as follows

Provider	Type	No.	Par value	Details
KTV Credit Co., Ltd. and one other institute	Note	5 copies	₩ 4,000 million	Non-recovered after collection of debt
	Note	1 coy	Blank check	Non-recovered after collection of debt
	Check	2 checks	Blank check	Non-recovered after collection of debt

As of the end of current quarter, the Group lost six notes with unconfirmed provider and face value and one check other than the above-mentioned notes and expects to proceed a judgment of nullification with regard to the said notes.

(13) On March 17, 2011, the Group signed a memorandum of understanding on global investment partnership with National Pension Service to jointly invest in foreign assets with a limit of ₩800,000 million.

(14) With relation to the acquisition of KT&G Life Sciences Corporation, the Parent Company entered into a contract with a former owner of the acquiree, Gwak, Tae-Hwan (the "Individual Shareholder"). Details of the contract are as follows

Description	Details
Restriction of disposal	The Individual Shareholder shall not be permitted to dispose of its shares, in whole or in part, within one year after KT&G Life Sciences Corporation is listed.
Right of first refusal held by the Parent Company	The Individual Shareholder shall not be permitted to make any transfer of its shares, in whole or in part, unless it has offered them first to the Parent Company.
Tag-along right held by the Individual Shareholder	In the event that the Parent Company proposes to enter into a transaction or a series of related transactions with a third-party purchaser to dispose of its shares, then the Individual Shareholder shall elect to participate in such disposition upon the terms and conditions no less favorable than those applicable to the Parent Company.

(15) As of the end of current quarter, the Group is insured by performance guarantee insurance up to ₩4,560 million with the Seoul Guarantee Insurance.

(16) As of the end of current quarter, the Group recognizes other financial assets of ₩6,340 million deposited in Nonghyup Bank and restricted in use in order to provide a performance guarantee for the commercial district development project in Sejong-si.

(17) As of the end of current quarter, the Group has signed an agreement with a limit of USD 9,728 thousand with KEB Hana Bank and USD 7,626 thousand with Nonghyup Bank in relation to the derivative financial instrument.

(18) As of the end of current quarter, the Group has provided ₩424 million in guarantees for the Korea Special Sales Financial Corporative Association regarding Donginbi Jungnang Agency and one addition.

(19) As of the end of current quarter and end of previous term, the Group has entered into a management trust agreement with Marriott International Management Company B.V. and has been provided international Public Relations services through Global Hospitality Licensing S.A.R.L. Also, the Group has been provided technical advice by Marriott International Design & Construction Services., Inc.

36. Cash Flows

(1) Details of cash generated from operations for the three-month periods ended March 31, 2018 and 2017

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Profit for the quarter	249,369	235,036
Adjustments for:		
Income tax expense	110,436	96,648
Finance cost	2,670	1,533
Finance income	(35,595)	(22,001)
Depreciation	37,385	38,121
Amortization	1,169	1,324
Retirement and termination benefits	16,268	14,977
Foreign currency translation loss	12,136	81,274
Impairment loss (reversal) on trade and other receivables	(418)	57
Loss of write-down of inventories	743	412
Impairment loss on intangible assets	347	306
Loss on sale of intangible assets	6	162
Loss on sale of investment of joint ventures	–	1,794
Other expenses (losses), etc.	203	1,105
Share of gain of associates	–	(1,469)
Share of loss of associates	52	6
Foreign currency translation gain	(3,383)	(6,239)
Gain on sale of property, plant and equipment	(474)	(121)
Gain on sale of intangible assets	–	(685)
Subtotal	390,914	442,240
Changes in working capital:		
Increase in trade and other receivables	(8,974)	(2,523)

Increase in advance payments	(6,501)	(32,543)
Decrease (increase) in prepaid expenses	(10,822)	1,080
Decrease in prepaid tobacco excise and other taxes	13,056	916
Decrease in inventories	62,773	131,913
Decrease in trade and other payables	(19,654)	(108,270)
Decrease in tobacco excise and other taxes payable	(33,249)	(554,454)
Payment of retirement and termination benefits	(3,282)	(9,482)
Increase (decrease) in other advance receipts	(1,254)	62
Cash generated from operations	383,007	(131,061)

(2) Details of material transactions without cash inflow and outflow for the three-month periods ended March 31, 2018 and 2017 were as follows

In millions of Korean won		
Type	For the three-month period ended March 31, 2018	For the three-month period ended March 31, 2017
Reclassification of accrued dividends of retained earnings	505,061	454,554
Increase (decrease) in accrued expenses related to payment of retirement and termination benefits	2,567	(3,076)
Reclassification of current term's profit (loss) of other financial assets-Financial assets at fair value account	1,627,787	–
Increase (decrease) in other payables related to acquisition of property, plant and equipment	4,197	(2,708)
Decrease in accounts receivable related to sale of property, plant and equipment	539	157
Reclassification of construction in progress	(49,432)	4,373

(3) Changes in liabilities due to financial activities

Changes in liabilities due to financial activities for the three-month periods ended March 31, 2018 and 2017 are as follows

① For the three-month period ended March 31, 2018

In millions of Korean won				
Type	Beginning of term	Cash flows from financing activities	Others	As of March 31, 2018
Payable dividends	–	–	505,061	505,061
Short-term borrowings (including current portion of long-term borrowings)	178,359	(120,686)	(3,027)	54,646
Long-term borrowings	100,589	190	(1,464)	99,315
Deposits received	32,595	(2,517)	4,288	34,366
Total	311,543	(123,013)	504,858	693,388

② For the three-month period ended March 31, 2017

In millions of Korean won				
Type	Beginning of term	Cash flows from financing activities	Other	As of December 31, 2017r
Payable dividends	–	–	454,554	454,554
Short-term borrowings (including current portion of long-term borrowings)	146,196	(96,469)	(9,598)	40,129
Long-term borrowings	115,953	(20,514)	4,750	100,189
Deposits received	27,606	3,566	6	31,178
Total	289,755	(113,417)	449,712	626,050

(4) The Group has presented net inflows and outflows of short-term financial instruments for which the transactions occur frequently with large amounts and expire soon.

37. Changes in accounting policies

37.1 K-IFRS No. 1109 ‘ Financial Instruments’ (enacted)

(1) Classification and measurement of financial instruments

Details of changes in retained earnings due to the classification and measurement of financial instruments are as follows

In millions of Korean won	
Adjustment details	Amount
Retained earnings at the beginning of term-K-IFRS No. 1039	1,733,863
Reclassification of loans and receivables as current term’s profit (loss)-Financial assets at fair value	(14,514)
Increase in trade and other receivables-net of allowance	(69,258)
Reclassification of available-for-sale securities as current term’s profit (loss)-Financial assets measured at fair value	3,895
Reclassification of available-for-sale securities as other comprehensive profit (loss)-Financial assets measured at fair value	32,870
Measurement of long-term deposits in MSA Escrow Fund at amortized cost	8,115
Reduction of deferred income tax following the adjustment of surplus at the beginning of term	22,177
Adjustment of total surplus due to adoption of K-IFRS No. 1109	(16,715)
Retained earnings at the beginning of term-K-IFRS No. 1109	1,717,148

Management has evaluated the business model applied to the financial assets held as of January 1, 2018, the initial application date of K-IFRS No. 1109, and classified the financial assets in accordance with K-IFRS No. 1109. The effect of this reclassification is as follows

In millions of Korean won							
Financial assets at the beginning of current term	Current term’s profit (loss)-Financial assets measured at fair value	Other comprehensive income (loss) – Financial assets measured at fair value (available-for-sale financial assets in the previous term)	Financial assets measured at amortized cost (Loans and receivables as of December 31, 2017)				Total
			Trade and other receivables	Long-term deposits in MSA Escrow Fund	Other financial assets	Cash and cash equivalents	
Carrying amount at the beginning of term-K-IFRS No. 1039	–	471,763	1,190,594	510,223	1,563,900	1,230,176	4,966,656
Current term’s profit (loss) on loans and receivables-Reclassification as financial assets measured at fair value	1,314,296	–	(6,548)	–	(1,320,000)	(2,262)	(14,514)
Current term’s profit (loss) in available-for-sale securities -Reclassification as financial assets measured at fair value	184,169	(184,169)	–	–	–	–	–
Amortized cost-measurement of long-term deposits in MSA Escrow Fund	–	–	1,971	9,402	–	–	11,373
Carrying amount at the beginning of term-Standard No. 1109	1,498,465	287,594	1,186,017	519,625	243,900	1,227,914	4,963,515

① Reclassified loans and receivables to financial assets at fair value through profit or loss

Of the cash equivalents and other financial assets as of January 1, 2018, money trust of ₩1,320,000 million, which was not composed of principal and interest on principal balance, has been reclassified to financial assets at fair value through profit or loss.

The difference of ₩14,514 million between the amortized cost of the money trust and the fair value as of January 1, 2018 has been reclassified to retained earnings. During the current period, ₩20,664 million, including changes in fair value related to these financial assets, has been recognized in profit in the current period.

② Reclassified available-for-sale financial assets to financial assets at fair value through profit or loss

Of the available-for-sale financial assets as of January 1, 2018, the investments in real estate investment funds of ₩184,169 million has been reclassified as financial assets at fair value through profit or loss. The financial assets do not meet the conditions that the contractual cash flows are measured at amortized cost because they do not represent only principal payments. Accumulated other comprehensive income of ₩3,895 million as of January 1, 2018 has been reclassified to retained earnings. During the current period, ₩1,315 million, including changes in fair value related to these financial assets, has been recognized in profit in the current period.

③ Reclassified available-for-sale financial assets to financial assets at fair value through other comprehensive income (or loss)

The changes in the fair value of equity instruments that were not for trading purposes and were previously classified as available-for-sale financial assets have been reclassified to financial assets at fair value through other comprehensive income and presented in other comprehensive income. Accordingly, ₩269,882 million has been reclassified to financial assets at fair value through other comprehensive income (loss). The related accumulated other comprehensive income of ₩32,870 million as of January 1, 2018 shall not be reclassified to profit or loss even if the financial asset is disposed of.

④ Long-term deposits in MSA Escrow Fund measured at amortized cost

The long-term deposits amounting to ₩510,223 million as of January 1, 2018 have been reclassified to financial assets at fair value through profit or loss. The financial assets should be measured at amortized cost because the assets have the cash flow that consists of the principal and interest on the principal balance alone under the contract having the aim to receive the cash flow. Long-term deposits of ₩11,048 million and retained earnings of ₩8,115 million have been increased, respectively, as of January 1, 2018 Interest income related to the long-term deposits amounting to ₩1,756 million was recognized during the period.

The effect of these changes on the Group's capital is as follows

In millions of Korean won		
Type	Change in accumulated amount of other comprehensive profit (loss)	Change in retained earnings
Carrying amount at the beginning of term-K-IFRS No. 1039	7,730	1,733,863
Reclassification of loans and receivables as financial assets measured at fair value through current term's profit or loss	–	(14,514)
Increase in trade and other receivables allowance (*)	–	(69,258)
Reclassification from available-for-sale securities to financial assets measured at fair value through current term's profit or loss	(3,895)	3,895
Reclassification from available-for-sale securities to financial assets measured at fair value through other comprehensive profit or loss	(32,870)	32,870
Measurement of long-term deposits in MSA Escrow Fund at amortized cost	–	8,115
Reduction of deferred income tax following the adjustment of surplus at the beginning of term	–	22,177
Total	(36,765)	(16,715)
Carrying amount at the beginning of term-K-IFRS No. 1109	(29,035)	1,717,148

(*) For the related notes on loss allowance, refer to (2) Impairment of the financial assets in the below.

The reclassification of financial assets due to adoption of K-IFRS No. 1109 is as follows, as of January 1, 2018 (the initial application date)

In millions of Korean won					
Type	Measurement scope		Carrying amount		
	K-IFRS No. 1039	K-IFRS No. 1109	K-IFRS No. 1039	K-IFRS No. 1109	Difference
Cash and cash equivalents	Loans and receivables	Financial assets measured at amortized cost	1,230,176	1,227,914	(2,262)
Other financial assets	Loans and receivables	Financial assets measured at amortized cost	1,563,900	243,900	(1,320,000)
Other financial assets	Loans and receivables	Financial assets measured at fair value through current term's profit or loss	-	1,314,296	1,314,296
Long-term deposits in MSA Escrow Fund	Financial assets recognized as current term's profit (loss)	Financial assets measured at amortized cost	510,223	519,625	9,402
Financial assets measured at fair value through other comprehensive profit or loss	Available-for-sale financial assets	Financial assets measured at fair value through other comprehensive profit or loss	471,763	287,594	(184,169)

Financial assets measured at amortized cost	Available-for-sale financial assets	Financial assets measured at amortized cost	-	184,169	184,169
Trade and other receivables	Loans and receivables	Financial assets measured at amortized cost	1,190,594	1,186,016	(4,578)
Total			4,966,656	4,963,514	(3,142)

(2) Impairment of financial assets

The Group has the following two types of financial assets subject to the new expected credit loss model in K-IFRS No. 1109

- Trade receivables from sales of inventories
- Debt instrument measured at amortized cost

The Group changed the policy on recognition of impairment loss as a result of the adoption of K-IFRS No. 1109. Please refer to the table in the above (1) for the effect on the beginning balance of the retained earnings for the period.

37.2 Application of the K-IFRS No. 1115 'Revenue from contracts with customers' (enacted)

As noted in Note 2, the Group has adopted K-IFRS No. 1115 from the beginning of the period. The financial statements of the prior period presented here for the comparison purpose have not been restated in accordance with the transitional provisions. The effect of adoption of the K-IFRS on the financial statements is as follows.

(1) Adjustments reflected as of January 1, 2018 (the initial application date) in the statement of financial position are as follows

In millions of Korean won			
Type	As of December 31, 2017 Before adjustments	Adjustment	As of January 01, 2018 After adjustments
Current assets	6,585,398	50	6,585,448
Non-current assets	3,390,507	1,333	3,391,840
Total assets	9,975,905	1,383	9,977,288
Current liabilities	1,802,999	3,479	1,806,478
Non-current liabilities	343,146	1,333	344,479
Total liabilities	2,146,145	4,812	2,150,957
Total equity	7,829,760	(3,429)	7,826,331

The Group provides logistics cost, insurance cost and credit card commissions with regard to some of the contracts signed with customers. Logistics cost and others belong to the amount payable to the customers in accordance with K-IFRS No. 1115, so they are recognized as deduction of profit.

(2) The items in the financial statements that are affected by the pre-change standards in the period of the initial application of K-IFRS No. 1115 are as follows

In millions of Korean won			
Type	Reported amount	Adjustment	In case K-IFRS No. 1115 is not adopted
Current assets	6,663,306	(953)	6,662,353
Non-current assets	3,423,849	(128)	3,423,721
Total assets	10,087,155	(1,081)	10,086,074
Current liabilities	2,227,380	(1,632)	2,225,748
Non-current liabilities	360,428	(128)	360,300
Total liabilities	2,587,808	(1,760)	2,586,048
Total equity	7,499,347	679	7,500,026
Sales	1,067,590	4,151	1,071,741
Cost of sales	433,470	(1,033)	432,437
Selling, general and administrative expenses	322,752	(1,971)	320,781
Income tax	110,436	–	110,436
Net profit for the period	249,369	43	249,412
Total comprehensive profit (loss)	231,556	43	231,599

(3) The cash flows from adoption of K-IFRS No. 1115 are the same as cash flows under previous standards.