



# **KT&G CORPORATION**

**Interim Financial Statements  
First Half of the 32nd Fiscal Year  
From January 1, 2018 to June 30, 2018**

**ATTACHMENT: INDEPENDENT AUDITORS' REPORT**

**KT&G CORPORATION**



## Contents

Review Report on Condensed Interim Financial Statements .....	1
Independent Auditors' Review Report.....	3
(Attachment) Accompanying Condensed Interim Financial Statements.....	7
Notes to Condensed Interim Financial Statements.....	17



KT&G CORPORATION

Review Report on Condensed Interim Financial Statements

First Half of the 32nd Fiscal Year  
from January 1, 2018, to June 30, 2018

Deloitte Anjin LLC



## Independent Auditors' Review Report

English Translation of Independent Auditors' Review Report Originally Issued in Korean

To the Shareholders and Board of Directors of  
KT&G Corporation:

### *Reviewed condensed interim financial statements*

We have reviewed the accompanying condensed interim financial statements of KT&G Corporation (the "Company"), which comprise the condensed interim statement of financial position as of June 30, 2018, and the related condensed interim statement of comprehensive income for the three months and six months ended June 30, 2018, and condensed interim statement of changes in equity and condensed interim statement of cash flows for the six months ended June 30, 2018, all expressed in Korean won, 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 interim financial statements in accordance with Korean International Financial Reporting Standards ("K-IFRSs"), and for such internal control as management determines is necessary to enable the preparation of condensed 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 interim financial statements based on our review.

We conducted our review in accordance with the Korean Standards on reviewing the interim and semiannual 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 auditors will be aware of all significant issues that would have been identified in the audit. Therefore, we do not express our opinion.





## ***Review results***

As a result of the review, we did not find any material items that are not fairly stated in terms of materiality in accordance with K-IFRS No. 1034 ‘Interim Financial Reporting.’

## ***Other matters***

The Company’s comparative condensed interim statement of comprehensive income for the three months and six months ended June 30, 2017, and comparative condensed interim statement of changes in equity and comparative condensed interim statement of cash flows for the six months ended June 30, 2017, were reviewed by KPMG Samjong Accounting Corporation, whose review report dated August 13, 2017, stated that no unfairly presented item was found in these condensed interim financial statements, in all material respects, in terms of K-IFRS No. 1034 ‘Interim Financial Reporting.’

The statement of financial position as of December 31, 2017, and the related statement of comprehensive income, statement of changes in equity and statement of cash flows (not included in this review) for the year ended December 31, 2017, were audited in accordance with the Korean Auditing Standards by 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 statement of financial position with respect to materiality.

10, Gukjegeumyung-ro, Yeongdeungpo-gu, Seoul

Lee Jung Hee, CEO of Anjin Deloitte LLC



August 14, 2018

## **Notice to Readers**

This report is effective as of the review report date (August 14, 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 interim 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 Condensed Interim Financial Statements

KT&G CORPORATION

First Half of the 32nd Fiscal Year  
from January 1, 2018, to June 30, 2018

First Half of the 31st Fiscal Year  
From January 1, 2017, to June 30, 2017

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

Address of headquarters: (Road name and address) 71, Beotkkot-gil, Daedeok-gu, Daejeon  
(Telephone) 080-931-0399



# Condensed Interim Statements of Financial Position

First half of the 32nd Fiscal Year As of June 30, 2018

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

KT&G CORPORATION

Korean won

Accounts	Notes	As of June 30, 2018	As of December 31, 2017
Assets:			
Current assets:			
Cash and cash equivalents	4,33,36,37	625,577,189,404	1,104,824,809,222
Current other financial assets	4,33,37	140,000,000,000	1,530,000,000,000
Financial assets at fair value through profit or loss	5,33,37	1,962,839,454,893	-
Derivative financial assets	20,33	387,862,284	-
Prepaid tobacco excise and other taxes		217,307,017,847	255,821,995,393
Trade and other receivables	6,32,33,37	780,808,793,327	951,435,036,855
Inventories	7	860,642,306,336	872,084,980,486
Advance payments		24,179,977,546	20,259,419,135
Prepaid expenses		5,120,381,173	4,163,466,088
Total current assets		4,616,862,982,810	4,738,589,707,179
Non-current assets:			
Non-current other financial assets	4,15,33,37	6,340,300,000	6,340,300,000
Long-term deposits in MSA Escrow Fund	8,33,37	578,397,436,030	510,223,375,080
Available-for-sale financial assets	9,33,37	-	454,051,493,361
Financial assets at fair value through other comprehensive income	9,33,37	249,327,586,168	-
Financial assets at fair value through profit or loss (non-current)	5,33,37	194,649,252,265	-
Investments in associates and joint ventures	10	51,930,010,000	51,930,010,000
Investments in subsidiaries	11	1,208,227,973,493	1,208,227,973,493
Property, plant and equipment	12,15	1,215,103,994,559	1,267,824,790,396
Intangible assets	13	29,702,619,223	27,235,455,547
Investment property	14,15	512,780,066,996	325,422,834,006
Long-term trade and other receivables	6	120,480,893,339	80,534,875,600
Long-term prepaid expenses		7,503,861,881	4,582,421,362
Total non-current assets		4,174,443,993,954	3,936,373,528,845
Total assets		8,791,306,976,764	8,674,963,236,024
Equity and Liabilities:			
Liabilities:			
Current liabilities:			
Short-term borrowings	16,33	1,609,795,395	1,958,661,660
Trade and other payables	17,32,33	428,166,033,133	386,586,874,355
Advance receipts		15,478,450,833	1,801,036,938
Income tax payable		159,336,613,901	145,928,809,669

Tobacco excise and other taxes payable		1,041,961,106,232	914,754,090,453
Refund liabilities and provisions	19	4,062,420,875	-
Derivative liabilities	20	5,506,391,199	-
Total current liabilities		1,656,120,811,568	1,451,029,473,075
Non-current liabilities:			
Long-term trade and other payables	17,33	31,961,422,574	21,655,355,805
Long-term advance receipts		656,661,939	581,716,864
Net defined benefit liability	18,32	33,749,925,569	19,084,241,508
Deferred income tax liabilities	37	1,996,189,024	35,969,370,768
Refund liabilities (non-current)	19	2,297,877,275	3,086,128,572
Total non-current liabilities		70,662,076,381	80,376,813,517
Total liabilities		1,726,782,887,949	1,531,406,286,592
Equity:			
Ordinary shares	21	954,959,485,000	954,959,485,000
Other capital surplus	21	3,582,160,908	3,582,160,908
Treasury shares	22	(328,157,286,128)	(328,157,286,128)
Gain on sale of treasury shares	22	513,775,933,891	513,775,933,891
Reserves	23	5,443,503,830,628	5,009,300,640,505
Retained earnings	24	476,859,964,516	990,096,015,256
Total equity		7,064,524,088,815	7,143,556,949,432
Total equity and liabilities		8,791,306,976,764	8,674,963,236,024

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

# Condensed Interim Statements of Comprehensive Income

From January 1, 2018, to June 30, 2018

From January 1, 2017, to June 30, 2017

KT&G CORPORATION

Korean won

Accounts	Notes	2018		2017	
		Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Sales	25	705,516,360,607	1,277,831,947,370	801,257,660,991	1,527,247,279,795
Manufacture of tobacco		626,671,802,139	1,150,299,570,932	693,409,056,019	1,356,163,020,203
Real estate	26	24,385,456,385	38,349,058,112	65,519,150,605	98,851,034,897
Exports of leaf tobacco and others		54,459,102,083	89,183,318,326	42,329,454,367	72,233,224,695
Cost of sales	27	(270,299,240,165)	(476,136,025,843)	(292,409,527,975)	(552,091,274,311)
Manufacture of tobacco		(219,696,702,796)	(394,753,901,331)	(219,219,931,575)	(440,936,644,268)
Real estate		(7,585,398,650)	(10,221,029,797)	(44,621,547,444)	(63,787,970,216)
Exports of leaf tobacco and others		(43,017,138,719)	(71,161,094,715)	(28,568,048,956)	(47,366,659,827)
Gross profit		435,217,120,442	801,695,921,527	508,848,133,016	975,156,005,484
Selling, general and administrative expenses (excluding bad debt expenses)	27	(159,205,252,227)	(306,053,153,412)	(163,059,334,602)	(309,153,024,617)
Bad debt expenses		(301,682,190)	(6,619,247,512)	(2,696,163,047)	(3,022,204,064)
Operating profit	27	275,710,186,025	489,023,520,603	343,092,635,367	662,980,776,803
Other income (excluding reversal of impairment loss)	28	62,600,546,509	83,679,929,586	48,194,091,158	19,189,160,230
Reversal of impairment loss on other receivables	28	2,422,896,780	2,153,239,191	847,503,045	2,012,265,950
Other expenses (excluding impairment loss)	28	(21,994,074,605)	(23,021,154,291)	(22,913,931,350)	(87,120,246,036)
Finance income (excluding interest income at effective interest rate)	29,33	26,293,635,561	117,311,989,409	14,971,504,400	102,443,826,193
Interest income at effective interest rate	29	365,366,362	754,506,299	502,636,514	1,079,165,068
Finance costs	29	(614,884,199)	(858,660,945)	(14,862,340,451)	(15,167,092,319)
Net finance income	29,33	26,044,117,724	117,207,834,763	611,800,463	88,355,898,942
Profit before income tax expense		344,783,672,433	669,043,369,852	369,832,098,683	685,417,855,889
Income tax expense	30	(92,165,725,333)	(159,494,290,487)	(106,390,211,218)	(168,817,135,161)
Profit for the period		252,617,947,100	509,549,079,365	263,441,887,465	516,600,720,728
Other comprehensive income for the period, net of tax:					
Items that are not reclassified to profit or loss					
Remeasurements of net defined benefit liability, net of tax		(346,723,870)	(1,224,472,868)	40,152,974	(398,503,653)
Unrealized changes in fair value of equity instruments at fair value through other comprehensive income		29,744,228,240	(13,918,831,805)	-	-
Gain and loss on sale in fair value of equity instruments at fair value through other comprehensive income		(147,755,932)	(147,755,932)	-	-

Items that may be reclassified subsequently to profit or loss					
Unrealized changes in fair value of available-for-sale financial assets		-	-	22,946,275,207	27,968,033,971
Other comprehensive income for the period, net of tax		29,249,748,438	(15,291,060,605)	22,986,428,181	27,569,530,318
Total comprehensive income for the period		281,867,695,538	494,258,018,760	286,428,315,646	544,170,251,046
EPS in Korean won and U.S. dollars:					
Basic and diluted EPS in Korean won	31	2,001	4,036	2,086	4,091

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



# Condensed Interim Statements of Changes in Equity

From January 1, 2018, to June 30, 2018

From January 1, 2017, to June 30, 2017

KT&G CORPORATION

Korean won

Accounts	Ordinary shares	Other capital surplus	Treasury shares	Gain on sale of treasury shares	Reserves	Retained earnings	Total
Balance at January 1, 2017	954,959,485,000	3,582,160,908	(328,157,286,128)	513,775,933,891	4,366,268,230,007	1,068,469,079,666	6,578,897,603,344
Total comprehensive income for the period:							
Profit for the period	-	-	-	-	-	253,158,833,263	253,158,833,263
Other comprehensive income (loss):							
- Remeasurements of net defined benefit liability, net of tax	-	-	-	-	-	(398,503,653)	(398,503,653)
- Unrealized net changes in fair value of available-for-sale financial assets	-	-	-	-	27,968,033,971	-	27,968,033,971
Total other comprehensive income (loss)	-	-	-	-	27,968,033,971	(398,503,653)	27,569,530,318
Total comprehensive income for the period	-	-	-	-	27,968,033,971	516,202,217,075	544,170,251,046
Transactions with owners, recorded directly in equity:							
Dividends	-	-	-	-	-	(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)	-
Total transactions with owners	-	-	-	-	613,914,622,466	(1,068,469,079,666)	(454,554,457,200)
Balance at June 30, 2017	954,959,485,000	3,582,160,908	(328,157,286,128)	513,775,933,891	5,008,150,886,444	516,202,217,075	6,668,513,397,190
Balance at January 1, 2018	954,959,485,000	3,582,160,908	(328,157,286,128)	513,775,933,891	5,009,300,640,505	990,096,015,256	7,143,556,949,432
Effects of changes in accounting policies	-	-	-	-	(36,765,729,396)	(31,464,641,981)	(68,230,371,377)
Balance at January 1, 2018 (basic after revision)	954,959,485,000	3,582,160,908	(328,157,286,128)	513,775,933,891	4,972,534,911,109	958,631,373,275	7,075,326,578,055
Total comprehensive income for the period:							
Profit for the period	-	-	-	-	-	509,549,079,365	509,549,079,365
Other comprehensive income (loss)							
- Remeasurements of net defined benefit liability, net of tax	-	-	-	-	-	(1,224,472,868)	(1,224,472,868)
- Unrealized changes in fair value of equity instruments at fair value through other comprehensive income	-	-	-	-	(13,918,831,805)	-	(13,918,831,805)
- Gain and loss on sale in fair value of equity instruments at fair value through other comprehensive income	-	-	-	-	(147,755,932)	-	(147,755,932)
Total other comprehensive income (loss)	-	-	-	-	(14,066,587,737)	(1,224,472,868)	(15,291,060,605)
Total comprehensive income for the period	-	-	-	-	(14,066,587,737)	508,324,606,497	494,258,018,760
Transactions with owners, recorded directly in equity:							
Dividends paid	-	-	-	-	-	(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	-	-	-	-	485,035,507,256	(990,096,015,256)	(505,060,508,000)
Balance at June 30, 2018	954,959,485,000	3,582,160,908	(328,157,286,128)	513,775,933,891	5,443,503,830,628	476,859,964,516	7,064,524,088,815

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



# Condensed Interim Statements of Cash Flows

From January 1, 2018, to June 30, 2018

From January 1, 2017, to June 30, 2017

KT&G CORPORATION

Korean won

Accounts	Note	Six months ended June 30, 2018	Six months ended June 30, 2017
Cash flows from operating activities:			
Cash generated from operations	36	855,419,158,775	218,119,410,889
Income tax paid		(148,339,196,112)	(187,765,557,341)
Net cash provided by (used in) operating activities		707,079,962,663	30,353,853,548
Cash flows from investing activities:			
Interest received		5,662,170,884	27,135,449,599
Dividends received		64,867,984,985	78,230,988,688
Proceeds from sale of property, plant and equipment		5,321,655,357	2,000,929,845
Proceeds from sale of intangible assets		350,484,000	1,350,000,000
Disposals of financial assets at fair value through other comprehensive income		1,152,600,000	-
Disposition of investments in subsidiaries		-	17,723,668,000
Disposals of financial assets at fair value through profit or loss		30,832,952,910	3,462,129,718
Disposals of available-for-sale financial assets		-	8,301,403,692
Collection of loans		8,353,550,300	11,426,000,000
Withdrawal of guarantee deposits		9,297,923,935	(97,466,325,710)
Acquisition of property, plant and equipment		(181,064,221,595)	(758,470,200)
Acquisition of intangible assets		(2,859,287,722)	(97,201,843,321)
Acquisition of available-for-sale financial assets		-	(20,000,000,000)
Acquisition of financial assets at fair value through profit or loss		(33,000,000,000)	-
Increase in loans		-	(636,898,315)
Increase in guarantee deposits		(13,022,760,000)	(14,412,025,300)
Payments of long-term deposits in MSA Escrow Fund		(32,924,693,568)	(42,828,595,886)
Increase (decrease) in other financial assets, net		(548,856,477,823)	693,659,700,000
Net cash provided by investing activities		(685,888,118,337)	569,986,110,810
Cash flows from financing activities:			
Dividends paid		(505,060,508,000)	(454,554,457,200)
Decrease in deposits received		(2,560,110,800)	(1,855,329,280)
Increase in deposits received		5,229,478,054	7,764,209,110
Net cash provided by (used in) financing activities	36	(502,391,140,746)	(448,645,577,370)
Effect of exchange rate fluctuation on cash held		1,951,676,602	34,295,159
Net increase in cash and cash equivalents		(479,247,619,818)	151,728,682,147
Cash and cash equivalents at January 1		1,104,824,809,222	688,735,175,839
Cash and cash equivalents at June 30		625,577,189,404	840,463,857,986

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



## Notes to Condensed Interim Financial Statements

From January 1, 2018, to June 30, 2018

From January 1, 2017, to June 30, 2017

KT&G CORPORATION

### 1. ORGANIZATION AND DESCRIPTION OF BUSINESS:

KT&G Corporation (the “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. As of June 30, 2018, the 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 Company has the Gimcheon plant for fabrication of leaf tobacco and the Cheonan printing plant for manufacturing of packaging material. The headquarters of the Company is located at 71, Beotkkot-gil, Daedeok-gu, Daejeon.

On April 1, 1989, the 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 Company was excluded from the application of the Act for the Management of Government Invested Enterprises. Accordingly, the Company became an entity existing and operating under the Commercial Act of Korea. Pursuant to the Korean government’s privatization program and management reorganization plan, on December 28, 1998, the shareholders approved a plan to split the Company into two companies by setting up a subsidiary for its red ginseng business segment effective January 1, 1999. The separation was accomplished by the Company’s contribution of the assets and liabilities in the red ginseng business segment into a wholly owned subsidiary, Korea Ginseng Corporation. On December 27, 2002, the Company changed its name again to KT&G Corporation from Korea Tobacco and Ginseng Corporation.

The Korean government sold 28,650,000 shares of the Company to the public during 1999, and the Company listed its shares on the Korea Exchange on October 8, 1999. On October 17, 2002, and October 31, 2001, the 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 Company) on the Luxembourg Stock Exchange pursuant to the Korean government’s privatization program. Also, on June 25, 2009, the listing market of the Company’s GDR was changed from the BdL market to the Euro MTF in the Luxembourg Stock Exchange.

The ownership of the issued ordinary shares of the Company as of June 30, 2018, is as follows:

Item	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	2,891,014	2.11%
Treasury shares	11,027,370	8.03%
Others	100,672,254	73.32%
Total	137,292,497	100.00%

## **2. BASIS OF PREPARATION:**

### **(1) Statement of Compliance**

The Company has prepared its condensed interim financial statements in accordance with Korean International Financial Reporting Standards ("K-IFRSs"). The Company's condensed interim financial statements are the condensed interim financial statements prepared in accordance with K-IFRS No. 1034, Interim Financial Reporting.

These condensed interim financial statements are separate financial statements prepared in accordance with K-IFRS No. 1027, Separate Financial Statements, presented by a parent, an investor in an associate or a venture in a jointly controlled entity, in which the investments are accounted for on the basis of the direct equity interest rather than on the basis of the reported results and net assets of the investees.

The separate financial statements were authorized for issue by the board of directors on August 9, 2018.

### **(2) Basis of Measurement**

The condensed interim financial statements have been prepared on the historical cost basis, except for the following material items in the condensed interim 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**

These condensed interim financial statements are presented in Korean won, which is the Company's functional currency and the currency of the primary economic environment in which the Company operates.

### **(4) Use of Estimates and Judgments**

The preparation of the condensed interim financial statements in conformity with K-IFRSs 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 Company's accounting policies used in the condensed 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 amendments to standards effective from January 1, 2018, set out below have been applied consistently to all periods presented in these condensed 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 payments if classified as such; and 3) If the terms of the cash-settled share-based payment transactions 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. There is no material impact on the Company's condensed interim financial statements.

**- 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 do not have a material impact on the Company's condensed interim financial statements.

**- 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 advance 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 advance payment or receipt of the consideration that is made. The interpretation also stipulates that the transaction date for each advance payment or receipt must be determined separately if the payment or receipt is made several times.

The Company has already accounted for the foreign currency advance payment or receipt of the considerations in a manner consistent with the interpretation. Accordingly, the interpretation has no impact on the condensed interim financial statements of the Company.

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

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

The main provisions of the new regulations are as follows, and the effect on the Company's condensed interim financial statements 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 foregoing, the Company may make the following irrevocable choice or designation at the time of initial recognition of a financial asset:

- 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 Company 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 item at fair value through profit or loss.



If the debt instrument measured at fair value through other comprehensive income (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 (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 (loss) subsequently are subject to the impairment provisions.

Management has reviewed and assessed the financial assets held by the Company 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 Company'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 (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 under 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 condensed interim statements of comprehensive income as items at fair value through profit or loss under K-IFRS No. 1109.

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

## (2) Impairment of financial assets

The Company 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 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 one recognizes credit losses.

The Company 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 (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 Company applies the simplified method for trade receivables and contract assets.

In accordance with K-IFRS No. 1109, management of the Company 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 Company 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 (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 Company'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 Company's risk management activities.

In accordance with the transitional provisions of K-IFRS No. 1109 for hedge accounting, the Company adopted the hedge accounting provisions of K-IFRS No. 1109 prospectively from January 1, 2018, but the Company 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 Company 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 K-IFRS No. 1115 on January 1, 2018, the date of initial application. In addition, the Company 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 condensed interim 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 on January 1, 2018, to be recognized in retained earnings. Details of the accounting policies and the financial impact of adopting K-IFRS No. 1115 are explained in Note 37.

- 2014-2016 Annual Improvements to K-IFRSs

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 that 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 associate, 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 as the investment company.

Since the Company did not adopt K-IFRSs to date and is not a venture capital investment organization, the amendment does not have any effect on the condensed interim financial statements.

The significant accounting policies applied by the Company for the preparation of the condensed interim financial statements in accordance with K-IFRSs are as follows:

#### (1) Investments in Subsidiaries and Associates

The Company's condensed interim financial statements are separate financial statements in accordance with K-IFRS No. 1027. The Company applied the cost method to investments in subsidiaries and associates in accordance with K-IFRS No. 1027. Dividends from subsidiaries and associates are recognized in profit or loss when the right to receive the dividend is established.

#### (2) 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 the items.

Subsequent costs are included in the 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 Company 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 condensed interim statement of comprehensive income during the separate financial period in which they are incurred.

Property, plant and equipment, except for land and other tangible fixed assets, are depreciated on a straight-line basis over the following estimated useful lives for the acquisition cost of assets less residual value:

Type	Useful life (years)
Buildings	10-60
Structures	10-40
Machinery	10-12
Vehicles	4
Tools	4
Furniture and fixtures	4

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 condensed interim statements of comprehensive income.

### (3) Borrowing Costs

The Company 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 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 Company borrows funds specifically for obtaining a qualifying asset, the Company determines the amount of borrowing costs eligible for capitalization as the actual borrowing costs incurred on those borrowings during the period less any investment income on the temporary investment of those borrowings. To the extent that the Company borrows funds generally and uses them for obtaining a qualifying asset, the Company 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 Company that are outstanding during the period, other than borrowings made specifically for obtaining a qualifying asset. The amount of borrowing costs that the Company capitalizes during a period does not exceed the amount of borrowing costs incurred during that period.

### (4) Government Grants

Government grants are not recognized, unless there is reasonable assurance that the Company will comply with the grant's conditions and that the grant will be received.

Government grants that are intended to compensate the Company for expenses incurred are recognized in profit or loss in the condensed interim statements of comprehensive income over the periods in which the Company recognizes the related costs as expenses.

#### (5) Intangible Assets

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 the 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 life (years)
Industrial property rights	Between 10 and 20 years or indefinite
Facility usage rights	Indefinite
Intangible assets	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 for 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.

#### (6) Investment Property

Property held for 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 an item will flow to the Company 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 of investment property are reviewed at the end of each reporting period and adjusted, if appropriate. The change is accounted for as a change in an accounting estimate.

#### (7) 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 continuing 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 Company recognizes an impairment loss for any initial or subsequent write-down of an asset (or a 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. 1036, Impairment of Assets. However, deferred income tax assets, assets generated from employees' salaries and financial assets covered by K-IFRS No. 1039, Financial Instruments: Recognition and Measurement, are measured according to the relevant criteria sheet.

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).

#### (8) 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 method of determining the unit cost for each inventory classified by the Company is as follows:

Type	Method
Finished goods, work in progress and byproducts	Total averaging method
Processed leaf tobacco and purchased leaf tobacco in raw materials	Total averaging method
Raw materials (excluding processed leaf tobacco and purchased leaf tobacco) and supplies	Moving-average method
Buildings under construction, sites for allotting-out construction and goods in transit	Individual 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 or valuation loss 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.

#### (9) Impairment of Non-Financial Assets

The carrying amounts of the Company'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 Company estimates the recoverable amount of an individual asset. If it is impossible to measure the individual recoverable amount of an asset, then the Company estimates the recoverable amount of a cash-generating unit (“CGU”). The recoverable amount of an asset or a CGU is the greater of its value in use or its fair value less costs to sell. The value in use is estimated by applying a pretax discount rate, which 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.

#### (10) Financial Assets

##### - Classification:

Effective January 1, 2018, the Company shall classify the financial assets in the following measurement categories:

- Financial assets measured at fair value (recognizing changes in fair value in other comprehensive income (loss) or profit or loss)
- Financial assets measured at amortized cost

Financial assets are categorized based on business models for management and contractual cash flow specialization. Gains or losses on financial assets measured at fair value are recognized in profit or loss or other comprehensive income. Investments in debt instruments are recognized in profit or loss or other comprehensive income depending on the business model in which the asset is held. The Company reclassifies debt instruments only when it changes the business model that manages financial assets. Investments in equity instruments other than short-term investments are subject to irrevocable election to specify that subsequent fair value changes will be presented in other comprehensive income at initial recognition. Otherwise (if not specified), changes in the fair value of investments in the equity instruments are recognized in profit or loss.

##### - Measurement

The Company measures financial assets at their fair value at initial recognition, and the transaction costs directly related to the acquisition of the financial asset or the issuance of the financial liability are added to the fair value when it is not a financial asset measured at fair value through profit or loss. The transaction costs of the financial asset measured at fair value through profit or loss are recognized in profit or loss. A hybrid contract that includes an embedded derivative considers the entire hybrid contract when determining whether contractual cash flows consist solely of principal and interest.

#### ① Debt instrument

Subsequent measurement of financial assets is based on the contractual cash flow characteristics of the financial asset and the business model for managing the financial asset. The Company shall classify debt products into the following three categories:

(a) Amortized cost

The financial assets 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 measured at amortized cost. The gain or loss on a financial asset measured at amortized cost, which is not subject to hedge accounting, is recognized in profit or loss when the financial asset is derecognized or impaired. Interest income from financial assets recognized under the effective interest method is included in financial income.

(b) Financial assets at fair value through other comprehensive income

Financial assets held under a business model that achieves the objective through both receipt of contractual cash flows and sale of financial assets and whose contractual cash flows consist of only principal and interest payments are measured at fair value through other comprehensive income (loss). Except for impairment losses (reversals), interest income and foreign exchange gains and losses, the gain or loss on the financial asset measured at fair value through other comprehensive income (loss) is recognized in other comprehensive income. When a financial asset is derecognized, the cumulative gain or loss previously recognized is reclassified from equity to profit or loss. Interest income from financial assets recognized under the effective interest method is included in financial income. Foreign exchange gains and losses are recognized in other income or expense, and the impairment loss is recognized as other expense.

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

Debt instruments, except for the financial assets measured at amortized cost or measured at fair value through other comprehensive income, are measured at fair value through profit or loss. Gains or losses on the debt instruments at fair value through profit or loss that are not subject to hedge accounting are recognized in profit or loss and are presented as financial income or financial expense in the condensed interim statement of income during the period.

② Equity instruments

The Company subsequently measures the investments in all equity instruments at fair value. For equity instruments for which changes in fair value are elected to be presented in other comprehensive income, the amounts recognized in other comprehensive income are not reclassified to profit or loss even when equity instruments are eliminated. Dividend income on these equity instruments is recognized in profit or loss as financial income when the Company's right to receive dividends is established.

- Impairment

The Company assesses expected credit losses on debt instruments measured at amortized cost or fair value through other comprehensive income (loss) based on forward-looking information. The manner of impairment is determined when the credit risk increases significantly. However, for trade receivables, the Company applies the simplified method of recognizing expected credit losses for the whole period from the date of initial recognition of the receivables.



## (11) Financial Liabilities

- All financial liabilities are subsequently classified as measured at amortized cost, except for the following:
  - Such liabilities, including financial liabilities at fair value measurement through profit or loss and derivative liabilities, are subsequently measured at fair value.
  - Financial liabilities arise when the transfer of a financial asset does not meet the elimination conditions or when a continuing involvement approach is applied.
  - Financial guarantee contracts are measured at fair value at initial recognition, and subsequently, the issuer of such contracts subsequently measures the contract at the greater of the following:
    - Allowance for losses estimated based on expected credit losses
    - The amount recognized as a deduction from accumulated profit recognized in accordance with K-IFRS No. 1115 at initial recognition
  - Commitment to lend at an interest rate lower than the market interest rate; after initial recognition, the issuer of such an arrangement will subsequently measure the arrangement at the greater of the following:
    - Allowance for losses estimated based on expected credit losses
    - The amount recognized as a deduction from accumulated profit recognized in accordance with K-IFRS No. 1115 at initial recognition
  - The contingent consideration recognized by the acquirer in a business combination under K-IFRS No. 1103; such contingent consideration is subsequently measured at fair value through profit or loss

## (12) Derivatives

Derivatives are initially measured at fair value at the date of contract and subsequently measured at fair value at the end of each financial year. Unrealized gains or losses arising from changes in the fair value of derivatives are recognized in profit or loss.

## (13) 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 Company 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.

## (14) 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 Company during an accounting period, the Company recognizes the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.

### ② Other long-term employee benefits

Other long-term employee benefits that are not to be paid within 12 months after the end of the reporting period for which the employees have provided relevant services are discounted to their present value based on the future benefits received in exchange for services rendered during the current and prior periods. Changes in remeasurement are recognized in profit or loss in the period in which they arise.

### ③ Retirement benefits: defined contribution plans

When an employee has rendered service to the Company during a period, the Company 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 Company 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 Company, 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 Company determines the net interest expense (income) on the net defined benefit liability (asset) for the year 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), considering 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 Company 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 Company can no longer withdraw the offer of those benefits or when the Company recognizes costs for a restructuring.

### (15) Refund Liabilities and Provisions

Refund liabilities and provisions are recognized when the Company has a present obligation (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 considered in reaching the best estimate of a provision. Where the effect of the time value of money is material, refund liabilities and 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.

Refund liabilities and 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.

#### (16) 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 Company 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 profit or loss.

#### (17) Revenue Recognition

The Company's revenue categories consist of revenue from goods sold, services and other income.

##### ① Sales of goods

Revenue from sales of goods is measured at the fair value of the consideration received or receivable. Revenue from the sales of goods is recognized when the Company has transferred to the buyer the significant risks and rewards of ownership of the goods, the Company 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 Company and the costs incurred or to be incurred in respect of the transaction can be measured reliably.

The Company accepts returns from contracts to supply customers, so the income it receives may vary. The Company estimates a variable amount using an expected value method, through which it anticipates a better consideration to which it is entitled, and recognizes the revenue when the due date has passed, with the variable amount included in the transaction price only to the extent it is highly possible that it will not return a significant portion of the cumulative revenue it has already recognized. Of the consideration received or receivable, amounts that the Company does not anticipate will be entitled to are recognized as a refund liability.

##### ② Provision of services

The profits from the provision of services are recognized according to the progress when the revenue and progress can be measured reliably, the economic benefits can be introduced and the costs incurred for completing the transaction can be reliably measured. However, if the performance of the service provision transaction cannot be reliably estimated, only the amount within the recoverable costs recognized is recognized as a profit.

### ③ Construction of residential real estates

The Company constructs and sells residential real estates under long-term contracts with customers. These contracts are concluded before the construction of residential real estate commences. Under the terms of the agreement, the transfer of real estate to other customers is contractually restricted and the Company has the right to make payments that are enforceable for the services already performed. Therefore, revenues from residential real estates are recognized on the cost basis (i.e., proportionate to the costs incurred for the operations performed to date against the estimated costs) over the period. Management believes that the use of the input method is an appropriate measure under K-IFRS No. 1115 for measuring the progress to completion of the performance obligation.

The Company has the right to charge the clients for the construction of residential real estate as a result of the milestones associated with a series of work. When a specific milestone is reached, the customer sends out a related work statement signed by a third-party evaluator and issues an invoice related to the milestone consideration. Contract assets that are recognized for all previously performed operations are reclassified to receivables at the time the customer is charged. If the amount of the milestone payments exceeds the revenue recognized up to that date under the cost-based input method, the Company recognizes the difference as a contractual liability. The Company believes that there is no significant financial component in the construction contracts with customers because the time difference between the revenue recognition based on the cost-based input method and the milestone payment is always less than one year.

The Company pays sales commissions to brokers in connection with the conclusion of residential real estate sales contracts. The Company capitalizes the incremental costs when they are expected to be recovered and amortizes the costs over the period for which the residential real estate is transferred to the customer.

### ④ Real estate lease

Rental income from investment properties is recognized on a straight-line basis over the period of the lease.

### (18) Finance Income and Finance Costs

Finance income comprises interest income and dividend income from investment in financial assets. 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 that the Company's right to receive payment is established.

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

### (19) 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 they relate 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 year 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

The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the way the Company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. The Company recognizes a deferred tax asset for all deductible temporary differences to the extent 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 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 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 way the Company expects at the end of the reporting period to recover or settle the carrying amount of its assets and liabilities.

Deferred income tax assets and liabilities are measured using the average tax rate that is expected to apply to the taxable income for the period in which the asset is realized or the liability is settled based on tax legislation enacted or substantively enacted at the end of the reporting period. Deferred tax assets and liabilities are measured at the tax rates that are expected to be recovered or settled based on the carrying amount of the related assets and liabilities at the end of the reporting period.

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.

### (20) Foreign Currencies

Transactions in foreign currencies are translated to the respective functional currencies of the Company 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.

#### (21) Earnings per Share

The Company 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 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.

#### (22) Operating Segment

An operating segment is a component of the Company that engages in business activities from which it may earn revenues or incur expenses, including revenues and expenses that relate to transactions with any of the Company’s other components. All operating segments’ operating results are reviewed regularly by the Company’s chief executive officer to make decisions about resources to be allocated to a segment and assess its performance, and for which discrete financial information is available. Operating segment disclosures are included in the separate (or consolidated) financial statements in accordance with K-IFRS No. 1108, Operating Segments.

#### (23) Greenhouse Gases Emission Right

The Company 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 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 Company 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) Separate Financial Statements' Liquidity Arrangement

The Company has changed liquidity presentation order of its separate statements of financial position to provide reliable and purposeful information. The financial statements for the prior period have been presented in the order of liquidity to facilitate comparison with the separate financial statements of the current period. Such reclassifications do not affect the reported net income or net asset value.

## (25) New Standards and Interpretations Not Yet Adopted

The following standards and interpretations have been enacted, but are not effective for the fiscal years beginning after January 1, 2018; however, earlier application is permitted, but the Company has not early adopted the following new standards and interpretations in preparing these separate financial statements.

### - K-IFRS No. 1116 'Lease' (enacted)

K-IFRS No. 1116 'Lease' established on May 22, 2017, is effective for annual periods beginning on or after January 1, 2019, 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 Company 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 Company 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 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 Company has not selected between the two methods.

In order to assess the financial impact of the initial adoption of K-IFRS No. 1116, the Company is conducting a preliminary analysis for evaluating its potential effects on 2018 separate financial statements based on the current situation and available information as of June 30, 2018, but it is difficult in practice to provide reasonable estimates of financial impact until the Company completes this analysis.

#### **4. CASH AND CASH EQUIVALENTS AND OTHER FINANCIAL ASSETS:**

(1) Cash and cash equivalents as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Cash on hand	534	705
Demand deposits	174,258	104,120
Specific money in trust	450,785	1,000,000
Total	625,577	1,104,825

(2) Current other financial assets as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Certificates of deposit	100,000	6,340	100,000	6,340
Money trust	40,000	-	1,400,000	-
Certificates of deposit	-	-	30,000	-
Total	140,000	6,340	1,530,000	6,340

(3) Financial assets restricted in use as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won			
Type		As of June 30, 2018	As of December 31, 2017
Other financial assets	Real estate development performance guarantee	6,340	6,340



## 5. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS:

As explained in Note 3, the Company 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 condensed interim financial statements.

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

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Money trust	1,962,839	-	1,320,000	-
Real estate beneficiary securities	-	194,649	-	184,169
Total(*)	1,962,839	194,649	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. 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	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Unrealized changes in fair value of financial assets through profit or loss (*)	(60)	14,158	-	-
Gains or losses on disposals in fair value of financial assets through profit or loss (*)	19,126	26,888	-	-
Total	19,066	41,046	-	-

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

## 6. TRADE AND OTHER RECEIVABLES:

(1) Trade and other receivables as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Loans to employees	16,248	29,485	17,048	35,931
Loans	8,740	11,974	7,982	21,978
Other receivables	15,535	8,140	26,467	5,789
Guarantee deposits	26,954	21,018	27,852	16,837
Accrued income	3,450	1,240	10,361	-
Trade receivables	709,882	48,624	861,725	-
Total	780,809	120,481	951,435	80,535

(2) Trade and other receivables and allowance for doubtful accounts as of June 30, 2018, and December 31, 2017, are as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Gross trade and other receivables	854,181	189,332	996,982	91,913
Allowance				
Loans	(4,630)	(17,110)	-	(11,378)
Other receivables	(197)	(10,859)	(11,346)	-
Accrued income	(24)	(2,871)	(2,072)	-
Trade receivables	(68,521)	(38,011)	(32,129)	-
Total allowance	(73,372)	(68,851)	(45,547)	(11,378)
Net trade and other receivables	780,809	120,481	951,435	80,535

(3) Changes in allowance for trade and other receivables for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won		
Type	Six months ended June 30, 2018	Six months ended June 30, 2017
Beginning balance	56,925	71,765
Changes in accounting policies	86,149	-
Impairment loss	6,619	3,022
Reversal of impairment loss	(2,153)	(2,012)
Elimination	(5,317)	-
Ending balance	142,223	72,775

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.

## 7. INVENTORIES:

(1) Inventories as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won						
Type	As of June 30, 2018			As of December 31, 2017		
	Cost	Valuation allowance	Carrying amount	Cost	Valuation allowance	Carrying amount
Goods	13,347	-	13,347	981	-	981
Finished goods	91,178	(1,542)	89,636	57,801	(833)	56,968
Work in progress	12,906	-	12,906	18,759	-	18,759
Raw materials	676,335	-	676,335	716,034	-	716,034
Supplies	24,068	-	24,068	23,176	-	23,176
Byproducts	6,705	-	6,705	5,591	-	5,591
Buildings under construction	88	-	88	-	-	-
Sites for lotting-out construction	8,112	-	8,112	-	-	-
Goods in transit	29,445	-	29,445	50,576	-	50,576
Total	862,184	(1,542)	860,642	872,918	(833)	872,085

(2) The amount of loss on valuation and disposals of inventories recognized as an expense for the six months ended June 30, 2018 and 2017, is as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Cost of sales:				
Loss on valuation of inventories	289	709	330	341
Loss on disposal of inventories	1,211	1,818	595	1,354
Other expense:				
Loss on disposal of inventories	50	51	12	45
Total	1,550	2,578	937	1,740

## **8. LONG-TERM DEPOSITS IN MSA ESCROW FUND:**

Long-term deposits in MSA Escrow Fund as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Demand deposits	199	1,921
T-Note	578,198	508,302
Total	578,397	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 six months ended June 30, 2018 and 2017, ₩32,925 million and ₩42,829 million, respectively, were paid into long-term deposits in MSA Escrow Fund.

## **9. FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME:**

(1) Financial assets at fair value through other comprehensive income as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Listed equity instruments		
– Oscotech, Inc.	10,666	8,686
– Shinhan Financial Group Co., Ltd.	173,562	198,013
– Rexahn Pharmaceuticals, Inc.	965	1,382
– U&I Corporation	15,413	12,079
Subtotal	200,606	220,160
Unlisted equity instruments (*)	48,722	233,891
Total	249,328	454,051

(\*) In the prior year, the Company classified unlisted equity instruments as available-for-sale financial assets for 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 K-IFRS No. 1109.

(2) Changes in other comprehensive income (loss)-financial assets measured at fair value for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won		
Type	Six months ended June 30, 2018	Six months ended June 30, 2017
Beginning balance	454,051	365,805
Changes in accounting policies	(184,169)	-
Acquisition	-	20,000
Net change in fair value	(19,554)	23,271
Disposal and account substitution	(1,000)	(5,515)
Ending balance	249,328	403,561
Condensed interim statements of financial position:		
Current	-	-
Non-current	249,328	403,561
Total	249,328	403,561

## **10. INVESTMENTS IN ASSOCIATES AND JOINT VENTURES:**

Investments in associates as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won						
Company	Location	Principal operation	As of June 30, 2018		As of December 31, 2017	
			Percentage of ownership	Carrying amount	Percentage of ownership	Carrying amount
Cosmo Tobacco Co. Ltd.	Mongolia	Manufacturing and selling tobaccos	40.00%	-	40.00%	-
Lite Pharm Tech, Inc.	Korea	Manufacturing medical supplies	20.24%	1,830	20.24%	1,830
JR REIT V Co., Ltd.	Korea	Renting real estate	34.63%	5,600	34.63%	5,600
JR REIT VIII Co., Ltd.	Korea	Renting real estate	21.74%	10,000	21.74%	10,000
LSK Global Pharma Services Co., Ltd.	Korea	Researching and developing medicine	23.15%	-	23.15%	-
JR REIT X Co., Ltd.	Korea	Renting real estate	28.79%	9,500	28.79%	9,500
JR REIT XIII Co., Ltd.	Korea	Renting real estate	27.03%	5,000	27.03%	5,000
KB Gimpo Logistics CR REIT Co., Ltd. (*1)	Korea	Renting real estate	12.00%	3,000	12.00%	3,000
KORAMCO Private REIT 50 Fund (*2)	Korea	Renting real estate	84.21%	16,000	84.21%	16,000
Yong In Jung Sim Co., Ltd.	Korea	Renting real estate	22.22%	1,000	22.22%	1,000
Total				51,930		51,930

(\*1) KB Gimpo Logistics CR REIT Co., Ltd. is classified as a joint venture since decisions about the significant financial and operating policies 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.

(\*2) KORAMCO Private REIT 50 Fund is classified as a joint venture since decisions about the significant financial and operating policies of the investee cannot be made without unanimous consent of the parties that control the arrangement collectively.

## 11. INVESTMENTS IN SUBSIDIARIES:

Investments in subsidiaries as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won						
Subsidiary	Location	Principal operation	As of June 30, 2018		As of December 31, 2017	
			Percentage of ownership	Carrying amount	Percentage of ownership	Carrying amount
Korea Ginseng Corporation	Korea	Manufacturing and selling ginseng	100.00%	716,148	100.00%	716,148
Yungjin Pharm. Co., Ltd.	Korea	Manufacturing and selling pharmaceutical	52.45%	73,299	52.45%	73,299
Tae-a Industry Co., Ltd.	Korea	Manufacturing tobacco materials	100.00%	15,698	100.00%	15,698
KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	Turkey	Manufacturing and selling tobaccos	99.99%	12,741	99.99%	12,741
Korea Tabacos do Brasil Ltda.	Brazil	Processing leaf tobaccos	99.99%	2,891	99.99%	2,891
KT&G Pars	Iran	Manufacturing and selling tobaccos	99.99%	-	99.99%	-
KT&G Rus L.L.C.	Russia	Manufacturing and selling tobaccos	100.00%	110,297	100.00%	110,297
KT&G USA Corporation	USA	Manufacturing and selling tobaccos	100.00%	4,913	100.00%	4,913
Cosmococ Co., Ltd.	Korea	Manufacturing and selling cosmetics	98.56%	56,581	98.56%	56,581
Renzoluc Pte., Ltd. (*)	Singapore	Holding company	100.00%	148,834	100.00%	148,834
KGC Yebon Corporation	Korea	Manufacturing and selling medical herbs	100.00%	49,828	100.00%	49,828
PT KT&G Indonesia	Indonesia	Manufacturing and selling tobaccos	99.99%	1,240	99.99%	1,240
SangSang Stay, Inc.	Korea	Hotel	100.00%	14,261	100.00%	14,261
KT&G Global Rus L.L.C.	Russia	Manufacturing and selling tobaccos	100.00%	1,497	100.00%	1,497
Total				1,208,228		1,208,228

(\*) The Company's percentage of ownership, shown above, excludes redeemable convertible preferred shares. As of June 30, 2018, the Company's percentage of ownership would be 88.6% if preferred shares are included.

## 12. PROPERTY, PLANT AND EQUIPMENT:

(1) Details of property, plant and equipment as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won						
Type	As of June 30, 2018			As of December 31, 2017		
	Cost	Accumulated depreciation	Carrying amount	Cost	Accumulated depreciation	Carrying amount
Land	502,101	-	502,101	549,343	-	549,343
Buildings	723,538	(369,073)	354,465	713,395	(356,312)	357,083
Structures	45,815	(33,634)	12,181	45,867	(32,937)	12,930
Machinery	1,006,321	(815,225)	191,096	986,214	(798,513)	187,701
Vehicles	1,511	(1,121)	390	1,791	(1,379)	412
Tools	35,326	(31,122)	4,204	34,827	(30,080)	4,747
Furniture and fixtures	140,529	(106,103)	34,426	134,394	(97,545)	36,849
Other property, plant and equipment	1,594	-	1,594	1,594	-	1,594
Construction in progress	114,647	-	114,647	117,166	-	117,166
Total	2,571,382	(1,356,278)	1,215,104	2,584,591	(1,316,766)	1,267,825

(2) Changes in property, plant and equipment as of June 30, 2018 and 2017, are as follows:

### A. For the Six Months Ended June 30, 2018

In millions of Korean won							
Type	Beginning balance	Acquisition	Disposal	Depreciation	Transfer	Others	Ending balance
Land	549,343	44,847	(377)	(91)	34,534	(126,155)	502,101
Buildings	357,083	27,342	(2,738)	(12,559)	12,898	(27,561)	354,465
Structures	12,930	129	-	(957)	65	14	12,181
Machinery	187,701	14,854	(286)	(19,138)	7,965	-	191,096
Vehicles	412	64	-	(86)	-	-	390
Tools	4,747	511	(129)	(1,240)	315	-	4,204
Furniture and fixtures	36,849	5,686	(2)	(8,985)	878	-	34,426
Other property, plant and equipment	1,594	-	-	-	-	-	1,594
Construction in progress	117,166	104,840	-	(3,594)	(56,655)	(47,110)	114,647
Total	1,267,825	198,273	(3,532)	(46,650)	-	(200,812)	1,215,104



B. For the Six Months Ended June 30, 2017

In millions of Korean won							
Type	Beginning balance	Acquisition	Disposal	Depreciation	Transfer	Others	Ending balance
Land	426,463	-	(136)	-	37,247	(248)	463,326
Buildings	353,952	1,034	(78)	(12,826)	26,264	(410)	367,936
Structures	14,480	265	(41)	(1,015)	125	(3)	13,811
Machinery	207,199	2,535	(1,731)	(21,856)	7,160	-	193,307
Vehicles	360	165	-	(82)	-	-	443
Tools	5,355	632	(28)	(1,207)	-	-	4,752
Furniture and fixtures	42,306	4,939	(14)	(9,327)	221	-	38,125
Other property, plant and equipment	1,681	13	-	-	-	-	1,694
Construction in progress	65,472	87,229	-	-	(71,017)	-	81,684
Total	1,117,268	96,812	(2,028)	(46,313)	-	(661)	1,165,078

### 13. INTANGIBLE ASSETS:

(1) Details of intangible assets as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won						
Type	As of June 30, 2018			As of December 31, 2017		
	Cost	Accumulated amortization	Carrying amount	Cost	Accumulated amortization	Carrying amount
Industrial property rights	8,916	(5,627)	3,289	8,696	(5,597)	3,099
Facility usage rights	25,470	(23)	25,447	23,845	(23)	23,822
Intangible assets under development	967	-	967	314	-	314
Total	35,353	(5,650)	29,703	32,855	(5,620)	27,235

(2) Changes in intangible assets for the six months ended June 30, 2018 and 2017, are as follows:

A. For the Six Months Ended June 30, 2018

In millions of Korean won						
Type	Beginning balance	Acquisition	Disposal	Transfer	Amortization	Ending balance
Industrial property rights	3,099	-	(6)	226	(30)	3,289
Facility usage rights	23,822	1,982	(357)	-	-	25,447
Intangible assets under development	314	877	-	(226)	-	967
Total	27,235	2,859	(363)	-	(30)	29,703

B. For the Six Months Ended June 30, 2017

In millions of Korean won						
Type	Beginning balance	Acquisition	Disposal	Transfer	Amortization	Ending balance
Industrial property rights	2,162	226	-	602	(15)	2,975
Facility usage rights	23,206	472	(917)	-	-	22,761
Intangible assets under development	3,560	60	(385)	(602)	-	2,633
Total	28,928	758	(1,302)	-	(15)	28,369

(3) Research and development expenditures recognized as expenses for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Cost of sales	23	56	31	49
Selling, general and administrative expenses	3,374	6,765	4,241	6,730
Total	3,397	6,821	4,272	6,779

#### 14. INVESTMENT PROPERTY:

(1) Details of investment property as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won						
Type	As of June 30, 2018			As of December 31, 2017		
	Cost	Accumulated depreciation	Carrying amount	Cost	Accumulated depreciation	Carrying amount
Land	243,928	-	243,928	125,011	-	125,011
Buildings	302,638	(83,601)	219,037	280,302	(79,890)	200,412
Construction in progress	49,815	-	49,815	-	-	-
Total	596,381	(83,601)	512,780	405,313	(79,890)	325,423

(2) Changes in investment property for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won							
Type	Six months ended June 30, 2018				Six months ended June 30, 2017		
	Land	Buildings	Construction in progress	Total	Land	Buildings	Total
Beginning balance	125,011	200,412	-	325,423	124,763	210,433	335,196
Depreciation	-	(5,335)	-	(5,335)	-	(5,376)	(5,376)
Transfer from property, plant and equipment	118,917	23,960	49,815	192,692	248	413	661
Ending balance	243,928	219,037	49,815	512,780	125,011	205,470	330,481

(3) Details of profit or loss recognized related to the investment property for the six months ended June 30, 2018 and 2017, are summarized as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Rental income	15,774	27,365	11,116	21,968
Direct operating expense	(2,669)	(5,335)	(2,661)	(5,376)
Total	13,075	22,030	8,455	16,592

(4) The carrying amount and the fair value of investment property as of June 30, 2018, and December 31, 2017, are as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Fair value	Carrying amount	Fair value	Carrying amount
Land	775,580	243,928	744,481	125,011
Buildings	311,670	219,037	291,122	200,412
Construction in progress	49,815	49,815	-	-
Total	1,137,065	512,780	1,035,603	325,423

The fair value of investment property was determined based on the yield capitalization method by external and 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.

## 15. PLEDGED ASSETS:

Assets pledged as collateral as of June 30, 2018, and December 31, 2017, are summarized as follows:

(1) As of June 30, 2018

In millions of Korean won					
Type	Carrying amount	Type	Received amount	Collateralized amount	Secured party
Investment property	215,237	Leasehold deposits received	13,124	14,243	MetLife Insurance Korea Co., Ltd. and others
Other financial assets	6,340	Performance guarantee	-	6,340	Korea Land and Housing Corporation
Property, plant and equipment	24,005	Right to collateral security/right to lease on a deposit basis	3,081	3,493	Labor Welfare Corporation and others
Total	245,582		16,205	24,076	

(2) As of December 31, 2017

In millions of Korean won					
Type	Carrying amount	Type	Received amount	Collateralized amount	Secured party
Investment property	148,810	Leasehold deposits received	12,982	13,889	MetLife Insurance Korea Co., Ltd. and others
Other financial assets	6,340	Performance guarantee	-	6,340	Korea Land and Housing Corporation
Property, plant and equipment	24,601	Right to collateral security/right to lease on a deposit basis	3,104	3,493	Labor Welfare Corporation and others
Total	179,751		16,086	23,722	

## **16. SHORT-TERM BORROWINGS:**

The Company provides payment guarantees to financial institutions in accordance with consumer financing arrangements in connection with retail receivables, receives the related receivables immediately from financial institutions in exchange for the guarantees provided and recognizes them as short-term borrowings. Short-term borrowings as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won			
Customer credit contracts	Annual interest rate	As of June 30, 2018	As of December 31, 2017
Nonghyup Bank	5.92%	1,304	1,660
KEB Hana Card Co., Ltd.	3-month CD rate+2.5%	306	299
Total		1,610	1,959

## **17. TRADE AND OTHER PAYABLES:**

Trade and other payables as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Leasehold deposits received	24,077	11,166	23,189	9,565
Trade payables	54,028	-	34,293	-
Withholdings	12,117	-	4,336	-
Value-added tax withholdings	166,104	-	148,065	-
Accrued expenses	123,490	12,805	129,083	12,090
Other payables	48,350	7,990	47,621	-
Total	428,166	31,961	386,587	21,655

## 18. RETIREMENT BENEFITS PLAN:

(1) Details of profit or loss recognized related to retirement benefits for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Defined benefit plans:				
Current service cost	6,437	12,882	6,674	13,348
Net interest on net defined benefit liability	122	243	235	471
	6,559	13,125	6,909	13,819
Defined contribution plans:				
Contributions recognized as expense	1,113	3,299	1,131	3,349
Other long-term employee benefits:				
Current service cost	570	1,108	-	-
Early retirement:				
Termination benefits	21	2,528	2	15
Total	8,263	20,060	8,042	17,183

(2) Net defined benefit liabilities as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Present value of defined benefit obligations	291,406	283,055
Fair value of plan assets	(257,656)	(263,971)
Total	33,750	19,084

## **19. REFUND LIABILITIES AND PROVISIONS:**

(1) Refund liabilities and provisions as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Refund liabilities	2,282	2,298	-	3,086
Provisions	1,780	-	-	-
Total	4,062	2,298	-	3,086

(2) Changes in refund liabilities and provisions for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won								
Type	Six months ended June 30, 2018				Six months ended June 30, 2017			
	Beginning	Increase	Decrease	Ending	Beginning	Increase	Decrease	Ending
Refund liabilities	3,086	1,552	58	4,580	-	-	-	-
Provisions	-	1,780	-	1,780	-	-	-	-
Total	3,086	3,332	58	6,360	-	-	-	-

## **20. DERIVATIVES:**

(1) Details of derivatives as of June 30, 2018, and December 31, 2017, are as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Current	Non-current	Current	Non-current
Currency forward:				
Derivative assets	388	-	-	-
Derivative liabilities	(5,506)	-	-	-
Total	(5,118)	-	-	-

(2) Changes in derivatives for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won		
Type	Six months ended June 30, 2018	Six months ended June 30, 2017
Beginning balance	-	-
Valuation gain	388	-
Valuation loss	(5,506)	-
Ending balance	(5,118)	-

## **21. SHARE CAPITAL:**

(1) Details of share capital as of June 30, 2018, and December 31, 2017, are as follows:

Type	As of June 30, 2018	As of December 31, 2017
Authorized	800,000,000 shares	800,000,000 shares
Par value in Korean won	₩5,000	₩5,000
Issued	137,292,497 shares	137,292,497 shares
Ordinary shares	954,959 million	954,959 million

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

(2) There was no change in other capital surplus as of June 30, 2018 and 2017.

## **22. TREASURY SHARES:**

(1) Treasury shares as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Number of shares	Carrying amount	Number of shares	Carrying amount
Treasury shares	11,027,370 shares	328,157	11,027,370 shares	328,157

(2) There was no change in gain on sale of treasury shares as of June 30, 2018 and 2017.



## 23. RESERVES:

(1) Reserves as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Other comprehensive income (loss)	(52,644)	(1,812)
Legal reserve	602,937	602,937
Voluntary reserve	4,893,211	4,408,176
Total	5,443,504	5,009,301

(2) Other comprehensive income (loss) as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Accumulated other comprehensive income (loss) before taxes	(72,612)	(2,499)
Tax effect	19,968	687
Accumulated other comprehensive income (loss) after taxes	(52,644)	(1,812)

(3) The Commercial Act of Korea 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 June 30, 2018, and December 31, 2017, is summarized as follows:

In millions of Korean won		
Type	As of June 30, 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 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 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 the remaining amounts could be reclassified as a voluntary reserve.

③ Reserve for business expansion and other reserves

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

## **24. RETAINED EARNINGS:**

Changes in retained earnings for the six months ended June 30, 2018 and 2017, are as follows

In millions of Korean won		
Type	Six months ended June 30, 2018	Six months ended June 30, 2017
Beginning balance	990,096	1,068,469
Changes in accounting policies	(31,465)	-
Dividends	(505,061)	(454,554)
Transfer from reserve for research and human resource development	10,000	10,000
Transfer to unconditional reserve	(495,036)	(623,915)
Profit for the period	509,549	516,601
Remeasurements of net defined benefit liability, net of tax	(1,223)	(399)
Ending balance	476,860	516,202

## 25. SALES:

The Company creates revenues by transferring goods and services over a period or at any of the following major business lines. The classification of major business segments is consistent with the reporting segment's revenue disclosure information in accordance with K-IFRS No. 1108.

In millions of Korean won						
Type			2018		2017	
			Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Revenue recognized at one point in time:						
Manufacturing and selling tobaccos	Korea	Wholesalers and retailers	423,754	777,407	418,007	790,617
		Special sales (duty free)	52,707	104,115	46,544	100,121
	Export	Wholesalers and retailers	183,024	314,337	228,858	465,425
Manufacture and sale of semifinished tobacco products	Export	Subsidiaries	15,485	33,814	17,066	28,332
Manufacture and sale of tobacco raw materials	Korea	Direct sales	1,637	2,279	17,254	28,840
	Export	Direct sales	3,095	4,633	4,350	5,911
Others	Korea	Direct sales	110	399	109	138
Subtotal			679,812	1,236,984	732,188	1,419,384
Revenue recognized over time:						
Toll processing revenue	Korea	Direct sales	127	289	3,551	9,012
Logistics sales	Export	Wholesalers and retailers	1,191	2,210	-	-
Sale and lease of real estate	Korea	Sale	10,984	10,984	52,061	71,921
	Korea	Lease	13,402	27,365	13,458	26,930
Subtotal			25,704	40,848	69,070	107,863
Total			705,516	1,277,832	801,258	1,527,247

## 26. REVENUE FROM REAL ESTATE SALES:

(1) Details of the sale contract under construction as of June 30, 2018, are as follows:

In millions of Korean won			
Project	Period	Presale amount	Contract amount
Suwon Hwaseo ParkPurgio	2018. 02–2021.08	1,213,201	1,191,333

(2) Changes in balance of contract amount for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won		
Type	Six months ended June 30, 2018	Six months ended June 30, 2017
Beginning balance of contracts	-	133,491
Increase	1,191,333	(95)
Revenue recognized	(11,827)	(71,921)
Ending balance of contracts	1,179,506	61,475

(3) Details of accumulative presale cost of sale contract under construction as of June 30, 2018, are as follows:

In millions of Korean won				
Project	Progress rate	Accumulative presale revenue	Accumulative presale cost	Unbilled revenue (*)
Suwon Hwaseo ParkPurgio	0.99%	11,827	(4,886)	-

(4) Estimated total contract revenue and total contract cost as of June 30, 2018, did not change.

Estimated total contract revenue and total contract costs of ongoing construction contracts are based on the situation occurring until June 30, 2018. It may change in future periods.

## 27. OPERATING PROFIT:

(1) Details of expenses, classified by nature, incurred for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Changes in inventories	23,819	11,443	59,564	106,895
Raw materials and consumables purchased	146,657	327,061	145,158	295,340
Salaries	83,798	178,350	81,437	167,280
Retirement and termination benefits	7,693	18,952	8,042	17,183
Depreciation	24,065	48,299	25,863	51,689
Amortization	16	30	9	15
Employee welfare	11,138	21,366	11,471	22,029
Advertising	25,678	46,845	26,039	48,473
Commissions	31,871	60,295	30,415	59,469
Other expenses	75,071	76,167	70,168	95,894
Total	429,806	788,808	458,166	864,267

(2) Details in selling, general and administrative expenses for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Salaries	56,288	120,317	54,257	112,636
Retirement benefits	5,370	13,417	5,760	12,048
Employee welfare	7,887	15,401	8,145	15,632
Travel	2,514	4,540	2,237	3,858
Communications	757	1,488	766	1,497
Utilities	1,859	4,893	1,750	4,238
Taxes and dues	14,918	16,032	13,627	15,165
Supplies	457	917	471	929
Rent	3,222	6,728	2,894	6,198
Depreciation	8,108	16,359	8,414	16,742
Amortization	16	30	8	15
Repairs and maintenance	1,002	1,598	1,421	1,696
Vehicles	1,025	1,988	1,010	2,006
Commissions	21,174	38,303	22,109	43,268
Freight and custody	2,871	5,281	7,893	13,842
Conferences	833	1,634	784	1,622
Advertising	25,637	46,780	25,982	48,394
Training	1,525	2,080	921	1,609
Normal research and development	3,374	6,765	4,069	6,730
Impairment loss on trade receivables	301	6,619	2,696	3,022
Insurances	14	509	27	259
Prizes and rewards	355	993	514	769
Total	159,507	312,672	165,755	312,175

## 28. OTHER INCOME AND EXPENSES:

(1) Details of other income for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Foreign currency transaction gain	3,688	4,414	2,694	5,395
Foreign currency translation gain	53,616	50,936	37,035	1,021
Reversal of impairment loss on other receivables	2,423	2,153	848	2,012
Gain on sale of property, plant and equipment	421	551	4,096	4,162
Gain on sale of intangible assets	-	-	-	595
Unrealized changes in fair value of derivatives	388	388	-	-
Gain from trading of derivatives	1,610	2,434	-	-
Others	2,878	24,957	4,369	8,016
Total	65,024	85,833	49,042	21,201

(2) Details of other expenses for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Foreign currency transaction loss	1,009	1,742	15,837	29,961
Foreign currency translation loss	-	1,833	-	39,403
Loss on unrealized changes in derivatives	11,512	5,506	-	-
Loss from trading of derivatives	3,194	3,194	-	-
Loss on disposals of investments in associates and joint ventures	-	-	-	8,945
Donations	2,217	3,065	1,672	3,038
Loss on disposals of property, plant and equipment	72	188	135	135
Impairment loss on property, plant and equipment	3,685	3,685	-	-
Loss on disposals of intangible assets	6	12	385	547
Others	299	3,796	4,885	5,091
Total	21,994	23,021	22,914	87,120

## 29. NET FINANCE INCOME:

(1) Details of net finance income for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Finance income:				
Interest income (*)	2,641	5,786	8,476	20,050
Dividend income	4,812	71,095	4,514	78,392
Interest income on long-term deposits in MSA Escrow Fund	-	-	2,024	4,067
Unrealized changes in fair value of financial assets measured at fair value through profit or loss	80	14,298	-	-
Gain on sale of financial assets measured at fair value through profit or loss	19,126	26,888	-	-
Gain on sale of available-for-sale financial assets	-	-	460	1,014
Finance income	26,659	118,067	15,474	103,523
Finance costs:				
Interest expense	(475)	(719)	(222)	(527)
Loss on disposal of financial assets at fair value through profit or loss	(140)	(140)	-	-
Impairment loss on available-for-sale financial assets	-	-	(14,640)	(14,640)
Finance costs	(615)	(859)	(14,862)	(15,167)
Net finance income	26,044	117,208	612	88,356

(\*) Includes ₩755 million of interest income at effective interest rate.

(2) Details of interest income included in finance income for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Deposits	322	847	7,821	17,478
Financial assets at fair value through profit or loss	-	-	-	7
Trade and other receivables	394	1,258	655	2,565
Long-term deposits in MSA Escrow Fund	1,925	3,681	-	-
Total	2,641	5,786	8,476	20,050

(3) Details of interest income included in finance income for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Trade and other payables	475	719	222	527



### **30. INCOME TAX EXPENSE:**

Income tax expense is calculated by adjusting the following items in the current income tax expense: adjustments recognized in the current and prior periods for the previous period's income tax, deferred income tax expense due to the occurrence and termination of temporary differences and income tax expense related to items recognized as other than profit or loss.

The average effective tax rates for the current and prior periods are 23.84% and 24.63%, respectively.

### **31. EPS:**

Changes in EPS for the six months ended June 30, 2018 and 2017, are as follows:

Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Profit for the period (in millions of Korean won)	252,618	509,549	263,442	516,601
Weighted-average number of ordinary shares outstanding	126,265,127	126,265,127	126,265,127	126,265,127
Basic and diluted EPS in Korean won	2,001	4,036	2,086	4,091

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 June 30, 2018, and December 31, 2017, are as follows:

Type	Company	Note	Location	Percentage of ownership					
				As of June 30, 2018			As of December 31, 2017		
				Parent	Subsidiary	Total	Parent	Subsidiary	Total
Subsidiary	Korea Ginseng Corporation		Korea	100.00%	-	100.00%	100.00%	-	100.00%
	Yungjin Pharm. Co., Ltd.		Korea	52.45%	-	52.45%	52.45%	-	52.45%
	Tae-a Industry Co., Ltd.		Korea	100.00%	-	100.00%	100.00%	-	100.00%
	KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.		Turkey	99.99%	-	99.99%	99.99%	-	99.99%
	Korea Tabacos do Brasil Ltda.		Brazil	99.99%	-	99.99%	99.99%	-	99.99%
	KT&G Pars		Iran	99.99%	-	99.99%	99.99%	-	99.99%
	KT&G Rus L.L.C.		Russia	100.00%	-	100.00%	100.00%	-	100.00%
	KT&G USA Corporation		USA	100.00%	-	100.00%	100.00%	-	100.00%
	Cosmococ Co., Ltd.		Korea	98.56%	-	98.56%	98.56%	-	98.56%
	Renzoluc Pte., Ltd.	(*1)	Singapore	100.00%	-	100.00%	100.00%	-	100.00%
	KGC Yebon Corporation		Korea	100.00%	-	100.00%	100.00%	-	100.00%
	PT KT&G Indonesia		Indonesia	99.99%	-	99.99%	99.99%	-	99.99%
	K&I HK Co., Ltd.		Hong Kong	-	100.00%	100.00%	-	100.00%	100.00%
	K&I China Co., Ltd.		China	-	100.00%	100.00%	-	100.00%	100.00%
	SangSang Stay, Inc.		Korea	100.00%	-	100.00%	100.00%	-	100.00%
	KT&G Global Rus L.L.C.		Russia	100.00%	-	100.00%	100.00%	-	100.00%
	KGC Life & Gin Co., Ltd.		Korea	-	100.00%	100.00%	-	100.00%	100.00%
	Jilin Hanzheng Ginseng Co., Ltd.		China	-	100.00%	100.00%	-	100.00%	100.00%
	Cheong Kwan Jang Taiwan Corporation		Taiwan	-	100.00%	100.00%	-	100.00%	100.00%
	Korean Red Ginseng Corp., Inc.		USA	-	100.00%	100.00%	-	100.00%	100.00%
	Korea Ginseng (China) Corp.		China	-	100.00%	100.00%	-	100.00%	100.00%
	Korea Ginseng Corporation Japan		Japan	-	100.00%	100.00%	-	100.00%	100.00%
	PT CKJ INDONESIA	(*2)	Indonesia	-	99.88%	99.88%	-	99.88%	99.88%
	PT Trisakti Purwosari Makmur		Indonesia	-	99.99%	99.99%	-	99.99%	99.99%
	PT Mandiri Maha Mulia		Indonesia	-	99.98%	99.98%	-	99.98%	99.98%
	PT Sentosa Ababi Purwosari		Indonesia	-	100.00%	100.00%	-	100.00%	100.00%
	PT Purindo Ilufa		Indonesia	-	100.00%	100.00%	-	100.00%	100.00%
	PT Nusantara Indah Makmur		Indonesia	-	100.00%	100.00%	-	100.00%	100.00%
Investments in associates and joint ventures	Cosmo Tobacco Co LTD		Mongolia	40.00%	-	40.00%	40.00%	-	40.00%
	Lite Pharm Tech, Inc.		Korea	20.24%	-	20.24%	20.24%	-	20.24%
	JR REIT V Co., Ltd.		Korea	34.63%	-	34.63%	34.63%	-	34.63%
	JR REIT VIII Co., Ltd.		Korea	21.74%	-	21.74%	21.74%	-	21.74%
	LSK Global Pharma Services Co., Ltd.		Korea	23.15%	-	23.15%	23.15%	-	23.15%
	JR REIT X Co., Ltd.		Korea	28.79%	-	28.79%	28.79%	-	28.79%
	JR REIT XIII Co., Ltd.		Korea	27.03%	-	27.03%	27.03%	-	27.03%
	KB Gimpo Logistics CR REIT Co., Ltd.		Korea	12.00%	-	12.00%	12.00%	-	12.00%
	KORAMCO Private REIT 50 Fund		Korea	84.21%	-	84.21%	84.21%	-	84.21%
	Yong In Jung Sim Co., Ltd.		Korea	22.22%	-	22.22%	22.22%	-	22.22%

(\*1) The percentage of ownership, shown above, excludes preferred shares. As of June 30, 2018, the Company's percentage of ownership would be 88.6% if preferred shares are included.

(\*2) PT CKJ INDONESIA has been liquidated in the middle of the current half-year and excluded from the scope of related parties as of June 30, 2018.

(2) Significant transactions that occurred in the normal course of business with related companies as of June 30, 2018 and 2017, are summarized as follows:

① Sales and other revenues

In millions of Korean won					
Type	Company	2018		2017	
		Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Subsidiary	Korea Ginseng Corporation	2,387	3,749	1,905	3,690
	Yungjin Pharm. Co., Ltd.	49	88	44	86
	Tae-a Industry Co., Ltd.	7	8	1	4
	KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	548	1,275	2,987	4,093
	KT&G Pars	-	-	602	602
	KT&G Rus L.L.C.	8,601	20,796	8,434	11,640
	KGC Life & Gin Co., Ltd.	57	64	35	65
	KT&G USA Corporation	7,407	24,658	27,557	52,441
	Cosmococ Co., Ltd.	33	38	31	54
	Renzoluc Pte., Ltd.	-	-	288	763
	KGC Yebon Corporation	11	12	7	12
	PT KT&G Indonesia	242	491	237	478
	PT Mandiri Maha Mulia	3,104	4,328	3,583	6,251
	Korea Tabacos do Brazil Ltda	4	4	-	-
	SangSang Stay, Inc.	1,503	3,056	1,737	3,292
Investments in associates and joint ventures	KVG REIT 1 Co., Ltd.	-	-	-	375
	JR REIT V Co., Ltd.	34	34	495	495
	JR REIT VIII Co., Ltd.	-	-	457	457
	JR REIT X Co., Ltd.	289	289	253	253
	KB Gimpo Logistics CR REIT Co., Ltd.	-	45	-	-
	KORAMCO Private REIT 50 Fund	-	220	-	-
Total		24,276	59,155	48,653	85,051

In addition to the above transactions, the Company sold the tangible assets of ₩164 million to KT&G Rus L.L.C. and purchased the tangible assets of ₩521 million from PT Sentosa Ababi Purwosari.

② Purchases and other expense

In millions of Korean won				
Company	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Korea Ginseng Corporation	89	618	261	1,688
Yungjin Pharm. Co., Ltd.	3	9	5	7
Tae-a Industry Co., Ltd.	3,629	7,167	3,527	6,798
KT&G Rus L.L.C.	-	-	335	335
KGC Life & Gin Co., Ltd.	3	3	34	183
Cosmocos Co., Ltd.	21	299	41	61
KGC Yebon Corporation	54	107	-	-
K&I China Co., Ltd.	-	-	8	23
Total	3,799	8,203	4,211	9,075

(3) Account balances with related companies as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won					
Type	Company	As of June 30, 2018		As of December 31, 2017	
		Receivables	Payables	Receivables	Payables
Subsidiary	Korea Ginseng Corporation	50	1,958	343	2,075
	Yungjin Pharm. Co., Ltd.	9	30	66	30
	Tae-a Industry Co., Ltd.	-	1,462	4	-
	KT&G Tutun Mamulleri Sanayi ve Ticaret A.S. (*)	38,536	-	37,029	-
	Korea Tabacos do Brasil Ltda.	104	-	103	-
	KT&G Pars (*)	44,888	-	43,791	-
	KT&G Rus L.L.C. (*)	71,820	-	53,810	-
	KT&G USA Corporation	27,266	281	38,696	-
	Cosmocos Co., Ltd.	3	17	29	16
	PT KT&G Indonesia (*)	28,546	-	27,380	-
	KGC Life & Gin Co., Ltd.	-	120	14	120
	PT Trisakti Purwosari Makmur	138	-	313	-
	PT Sentosa Ababi Purwosari	107	-	162	-
	PT Purindo Ilufa	107	-	-	-
	PT Mandiri Maha Mulia	11,171	-	13,279	-
	KGC Yebon Corporation	-	-	3	-
	SangSang Stay, Inc.	-	-	3	-
Investments in associates	LSK Global Pharma Services Co., Ltd.	750	-	1,500	-
	JR REIT V Co., Ltd.	-	-	242	-
	JR REIT VIII Co., Ltd.	67	-	212	-
	JR REIT XIII Co., Ltd.	145	-	145	-
	KB Gimpo Logistics CR REIT Co., Ltd.	101	-	60	-
	KORAMCO Private REIT 50 Fund	204	-	-	-
Total		224,012	3,868	217,184	2,241

(\*) Above receivables are the gross amounts before ₩75,176 million and ₩38,176 million of allowance for doubtful accounts as of June 30, 2018, and December 31, 2017, respectively.

(4) Details of financial transactions with related parties as of June 30, 2018, and December 31, 2017, are as follows:

In millions of Korean won					
Type	Company	As of June 30, 2018	As of December 31, 2017		
		Loans collection	Capital increase	Loans increase	Loans collection
Subsidiary	Yungjin Pharm. Co., Ltd.	-	6,944	-	-
	Cosmocos Co., Ltd.	-	5,544	-	-
	Renzoluc Pte., Ltd.	-	144,691	-	47,489
Investments in associates and joint ventures	LSK Global Pharma Services Co., Ltd.	750	-	2,054	554
	Yong In Jung Sim Co., Ltd.	-	1,000	-	-
Total		750	158,179	2,054	48,043

(5) Details of key management personnel compensation for the six months ended June 30, 2018 and 2017, are summarized as follows:

In millions of Korean won				
Type	2018		2017	
	Three months ended June 30,	Six months ended June 30,	Three months ended June 30,	Six months ended June 30,
Short-term employee benefits	4,790	9,997	4,413	9,659
Retirement benefits	352	762	538	1,079
Total	5,142	10,759	4,951	10,738

### **33. RISK MANAGEMENT AND FAIR VALUE OF FINANCIAL INSTRUMENTS:**

#### **(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 Company 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 Company'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 June 30, 2018, and December 31, 2017, are as follows:

In millions of Korean won				
Type	As of June 30, 2018		As of December 31, 2017	
	Monetary foreign currency assets	Monetary foreign currency liabilities	Monetary foreign currency assets	Monetary foreign currency assets
USD	1,200,554	7,079	1,039,421	30,912
IDR	1,559	-	1,581	-
EUR	33,268	11,028	33,424	3,580
Others	45,152	17	27,991	-
Total	1,280,533	18,124	1,102,417	34,492

For the six months ended June 30, 2018 and 2017, the effects of a 10% weakening or strengthening of functional currency against foreign currencies on profit or loss are as follows:

In millions of Korean won				
Type	Six months ended June 30, 2018		Six months ended June 30, 2017	
	10% increase	10% decrease	10% increase	10% decrease
Increase (decrease) in net income before tax	126,241	(126,241)	112,204	(112,204)

#### **② Equity price risk**

The Company has exposure to equity price risk, which arises from listed available-for-sale equity instruments. The Company'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 Company's management.

For the six months ended June 30, 2018 and 2017, the effects of a 5% fluctuation in the price index of stocks on comprehensive income are as follows:

In millions of Korean won				
Type	Six months ended June 30, 2018		Six months ended June 30, 2017	
	5% increase	5% decrease	5% increase	5% decrease
Increase (decrease) in comprehensive income before tax	990	(990)	7,229	(7,229)

### ③ Interest rate risk

The Company 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 Company'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 June 30, 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 Company 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 Company 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 Company 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 Company's assets.

The carrying amount of financial assets is maximum exposure to credit risk. The maximum exposure to credit risk as of June 30, 2018, and December 31, 2017, is as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Cash and cash equivalents (excluding cash on hand) (*)	174,259	1,104,120
Other financial assets	146,340	1,536,340
Financial assets at fair value through profit or loss (*)	2,608,273	-
Trade and other receivables	901,290	1,031,970
Long-term deposits in MSA Escrow Fund	578,397	510,223
Derivatives	388	-
Total	4,408,947	4,182,653

(\*) Money trust amount as of June 30, 2018, is included in the financial assets at fair value through profit or loss.

### (3) Liquidity risk

The Company has exposure to the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. The Company'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 Company's management determines if 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 June 30, 2018, and December 31, 2017, is as follows:

In millions of Korean won						
Type	Carrying amount	Contractual cash flow	Residual contractual maturity			
			Within three months	Between three months and one year	Between one year and five years	More than five years
As of June 30, 2018:						
Short-term borrowings	1,610	1,610	1,610	-	-	-
Trade and other payables	281,907	283,510	226,089	24,400	33,021	-
Derivative liabilities	5,506	5,506	3,207	2,299	-	-
Total	289,023	290,626	230,906	26,699	33,021	-
As of December 31, 2017:						
Short-term borrowings	1,959	1,959	1,959	-	-	-
Trade and other payables	243,751	244,566	210,997	23,405	9,879	285
Total	245,710	246,525	212,956	23,405	9,879	285

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



(4) The carrying amounts of each category of financial assets and liabilities as of June 30, 2018, and December 31, 2017, are summarized as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Financial assets:		
Available-for-sale financial assets	-	454,051
Financial assets at fair value through profit or loss (*)	2,608,273	-
Financial assets at fair value through other comprehensive income	249,328	-
Derivatives	388	-
Financial assets measured at amortized cost		
–Cash and cash equivalents	174,793	1,104,825
–Other financial assets	146,340	1,536,340
–Trade and other receivables	901,290	1,031,970
–Long-term deposits in MSA Escrow Fund	578,397	510,223
Subtotal	1,800,820	4,183,358
Total financial assets	4,658,809	4,637,409
Financial liabilities:		
Derivative liabilities	5,506	-
Financial liabilities measured at amortized cost		
–Short-term borrowings	1,610	1,959
–Trade and other payables	281,907	243,751
Subtotal	283,517	245,710
Total financial liabilities	289,023	245,710

(\*) Money trust amounting to ₩450,785 million as of June 30, 2018, is included in the financial assets at fair value through profit or loss.

(5) The fair value measurements classified by fair value hierarchy as of June 30, 2018, and December 31, 2017, are as follows:

In millions of Korean won				
Type	Carrying amount	Fair value		
		Level 1	Level 2	Level 3
As of June 30, 2018:				
Financial assets at fair value through profit or loss (*)	2,608,273	-	2,413,624	194,649
Financial assets at fair value through other comprehensive income	249,328	200,606	-	48,722
Derivative assets	388	-	388	-
Derivative liabilities	(5,506)	-	(5,506)	-
Total	2,852,483	200,606	2,408,506	243,371
As of December 31, 2017:				
Available-for-sale financial assets	404,329	220,160	-	184,169

(\*) Money trust amount as of June 30, 2018, is included in the financial assets at fair value through profit or loss.

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

The available-for-sale equity instruments in real estate trust fund have been measured using the adjusted net asset method, discounted cash flow and option-pricing model and categorized under Level 3 fair value based on the inputs to the valuation techniques used. Changes in fair value classified as Level 3 as of June 30, 2018, and December 31, 2017, are as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Beginning balance (*)	233,891	132,956
Acquisitions	33,000	70,946
Disposal	(25,440)	(22,798)
Net change in fair value	1,920	3,065
Ending balance	243,371	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 condensed interim financial statements as of June 30, 2018, with the amount of ₩49,722 million included.

(6) Details of finance income (costs) by categories for the six months ended June 30, 2018 and 2017, are as follows:

① For the Six Months Ended June 30, 2018

In millions of Korean won						
Type	Financial assets at fair value through profit or loss	Financial assets at fair value through other comprehensive income	Derivatives assets (liabilities)	Financial assets measured at amortized cost	Financial liabilities measured at amortized cost	Total
Profit or loss:						
Interest income	-	-	-	5,786	-	5,786
Dividend income	-	12,506	-	-	-	12,506
Unrealized net changes in fair value	14,158	-	(5,119)	-	-	9,039
Gain on sale	26,888	-	(759)	-	-	26,129
Interest expense	-	-	-	-	(719)	(719)
Impairment loss	-	-	-	(4,466)	-	(4,466)
Total	41,046	12,506	(5,878)	1,320	(719)	48,275
Other comprehensive income before tax:						
Net change in fair value	-	(19,554)	-	-	-	(19,554)
Reclassification by disposal	-	153	-	-	-	153
Total	-	(19,401)	-	-	-	(19,401)

② For the Six Months Ended June 30, 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	20,043	-	20,050
Dividend income	11,113	-	-	11,113
Interest income on long-term deposits in MSA Escrow Fund	-	4,067	-	4,067
Gain on sale and conversion	1,014	-	-	1,014
Interest expense	-	-	(527)	(527)
Impairment loss	(14,640)	(1,010)	-	(15,650)
Total	(2,506)	23,100	(527)	20,067
Other comprehensive income before tax:				
Net change in fair value	23,271	-	-	23,271
Reclassification adjustments on sale	(1,014)	-	-	(1,014)
Reclassification adjustments on impairment	14,640	-	-	14,640
Total	36,897	-	-	36,897

### **34. CAPITAL MANAGEMENT:**

The Company'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 Company monitors capital using equity and net debt by deducting cash and cash equivalents and current financial instruments from borrowings. The Company applied the same capital management strategy that was applied in the previous year. The Company's capital structure as of June 30, 2018, and December 31, 2017, is as follows:

In millions of Korean won		
Type	As of June 30, 2018	As of December 31, 2017
Debt (borrowings)	1,610	1,959
Less: Cash and cash equivalents	(625,577)	(1,104,825)
Less: Current other financial assets and financial assets at fair value through other comprehensive income	(2,102,839)	(1,530,000)
Net debt (asset)	(2,726,806)	(2,632,866)
Equity	7,064,524	7,143,557

### 35. CONTINGENT LIABILITIES AND COMMITMENTS:

(1) Payment of long-term deposits (MSA Escrow Fund)

Each year, the Company deposits a proportion of sales of tobacco products in the United States in accordance with the Tobacco Master Settlement Agreement (MSA) under the Escrow Statute of the U.S. government. The MSA Escrow Fund is 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 Company 25 years from the date of each annual funding. The Company 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 June 30, 2018, the Company's pending litigations are as follows:

In millions of Korean won				
Type	Suit parties	Case contents	Progress	Litigation value
Cases in which the Company is involved as the plaintiff:				
Seoul Central District Court	Lee Young-keun and one other	Claiming damages	The first trial in progress	602
Seoul Eastern District Court	Han Jae-geuk and four others	Claiming damages	The first trial in progress	3,338
Daejeon District Court	Head of the North Daejeon Tax Office	Claiming for cancellation of the imposed corporation tax	Won partly in the first trial/the second trial in progress	3,440
Seoul Central District Court	Tong Yang Moolsan Co., Ltd and two others	Claiming damages	The first trial in progress	222
Seoul Central District Court	Kim Mu-seok and four others	Claiming damages	The first trial in progress	4,774
Seoul Central District Court	Seol Yeong-geon, representative director of Cell Corporation and four others	Claiming damages	The first trial in progress	1,543
Seoul Central District Court	Union Tech Co., Ltd. and three others	Claiming damages	The first trial in progress	4,958
Seoul Central District Court	ITNU Co., Ltd.	Eviction suit	The first trial in progress	101
Total litigation value of the cases in which the Company is involved as the plaintiff				18,978
Cases in which the Company is involved as the defendant:				
Seoul Central District Court	National Health Insurance Corporation	Claiming damages	The first trial in progress	53,742
Cheongju District Court	Ju Sang-ja	Ownership cancellation	The first trial in progress	13
Seoul Central District Court	V manne piece	Patent infringement litigation	The first trial in progress	200
Total litigation value of the cases in which the Company is involved as the defendant				53,955

(3) The Company has entered into letter of credit ("L/C") agreements with financial institutions, such as KEB Hana Bank (limit: USD 177,000 thousand), as of June 30, 2018.

(4) As of June 30, 2018, the Company's trade receivables from the export of cigarettes are insured against non-payment up to USD 29,233 thousand by short-term export insurances with the Korea Trade Insurance Corporation.

(5) The Company has been provided with a foreign currency payment guarantee for local dealers in Russia and other countries up to USD 36,000 thousand and USD 20,000 thousand by KEB Hana Bank and Westchester Fire Insurance Company, respectively.

Details of guarantees exercised as of June 30, 2018, are summarized as follows:

In thousands of USD, THB	
Type	Exercised amount
Customs bond and L/C opening of KT&G USA Corporation	USD 26,342
Performance guarantee for export of tobacco sheet to Thailand Tobacco Monopoly	THB 2,832

(6) As of June 30, 2018, the Company has been provided with guarantees of USD 6,364 thousand from TRAVELERS CASUALTY AND SURETY COMPANY OF AMERICA for the execution of escrow deposits.

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

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

Type	Details
Restriction of disposal	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 Company	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 Company.
Tag-along right held by Individual Shareholder	If the Company proposes to enter into a transaction or a series of related transactions with a third-party purchaser to dispose of its shares, then Individual Shareholder shall elect to participate in such disposition upon the terms and conditions no less favorable than those applicable to the Company.

(9) As of June 30, 2018, the Company is insured by performance bond insurance up to ₩3,050 million with the Seoul Guarantee Insurance.

(10) As of June 30, 2018, the Company 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.

(11) As of June 30, 2018, the Company has entered into an agreement with KEB Hana Bank and others for USD 153,700 thousand related to derivative financial instruments.

(12) As of June 30, 2018, in connection with the sale of the building, the Company has entered into a housing sale guarantee contract with the Housing Guarantee Corporation for housing construction amounting to ₩889,040 million.

### 36. CASH FLOWS:

(1) Details of cash generated from operations for the six months ended June 30, 2018 and 2017, are as follows:

In millions of Korean won		
Type	Six months ended June 30, 2018	Six months ended June 30, 2017
Profit for the period	509,549	516,601
Adjustments for:		
Income tax expense	159,493	168,817
Finance costs	859	15,167
Finance income	(118,067)	(103,523)
Depreciation	48,299	51,689
Amortization	30	15
Retirement and termination benefits	18,946	17,168
Foreign currency translation loss	1,833	39,403
Impairment loss on trade and other receivables	6,619	3,022
Loss on valuation of inventories	709	341
Loss on disposals of property, plant and equipment	188	135
Impairment loss on property, plant and equipment	3,685	-
Loss on disposals of intangible assets	12	547
Loss on disposals of investments in associates and joint ventures	-	8,945
Other expenses	14,335	7,077
Foreign currency translation gain	(50,936)	(1,021)
Reversal of impairment loss on trade and other receivables	(2,153)	(2,012)
Gain on sale of property, plant and equipment	(551)	(4,162)
Gain on sale of intangible assets	-	(595)
Subtotal	592,850	717,614
Changes in working capital:		
Trade and other receivables	56,951	(25,863)
Advance payments	(3,921)	(20,205)
Prepaid expenses	(3,035)	2,904
Prepaid tobacco excise and other taxes	38,515	36,056
Inventories	14,078	102,756
Trade and other payables	26,099	(14,186)
Increase (decrease) in net income before tax	12,895	(283)
Tobacco excise and other taxes payable	127,207	(574,219)
Payment of retirement and termination benefits	(6,162)	(6,455)
Refund liabilities	(58)	-
Cash generated from operations	855,419	218,119

(2) Details of material transactions without cash inflow and outflow as of June 30, 2018 and 2017, are as follows:

In millions of Korean won		
Type	Six months ended June 30, 2018	Six months ended June 30, 2017
Increase (decrease) in accrued expenses related to payment of retirement and termination benefits	(193)	(2,554)
Other long-term employee benefits	1,108	-
Increase (decrease) in other payables related to acquisition of property, plant and equipment	17,208	(655)
Substitution of the construction in progress to the original account	56,655	-
Increase (decrease) in receivables related to disposal of tangible and non-current assets to be sold	(1,427)	4,054
Increase (decrease) in investments in subsidiaries as a result of investment conversion of subsidiaries' loan	-	47,490

### (3) Changes in liabilities due to financial activities

Changes in liabilities due to financial activities for the six months ended June 30, 2018 and 2017, are as follows:

#### ① For the Six Months Ended June 30, 2018

In millions of Korean won				
Type	Beginning balance	Cash flows from financing activities	Others	Ending balance
Leasehold deposits received	32,754	2,669	(180)	35,243

#### ② For the Six Months Ended June 30, 2017

In millions of Korean won				
Type	Beginning balance	Cash flows from financing activities	Others	Ending balance
Leasehold deposits received	28,266	5,909	(525)	33,650

(4) The Company has presented net inflows and outflows of some financial assets at fair value through profit or loss 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	
Adjustments	Amounts
Retained earnings at the beginning of the period - K-IFRS No. 1039	990,096
Reclassified loans and receivables to financial assets at fair value through profit or loss	(14,514)
Reclassified available-for-sale securities to financial assets at fair value through profit or loss	3,895
Reclassified available-for-sale securities to financial assets at fair value through other comprehensive income	32,870
Long-term deposits in MSA Escrow Fund measured at amortized cost	8,115
Increase in loss allowance on trade and other receivables	(86,149)
Decrease in deferred income tax due to adjustment of retained earnings at the beginning of the period	27,683
Adjustment of total retained earnings due to adoption of K-IFRS No. 1109	(28,100)
Retained earnings at the beginning of the period - K-IFRS No. 1109	961,996

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 as of January 1, 2018	Financial assets at fair value through profit or loss	Financial assets at fair value through other comprehensive income (loss) (Available-for-sale financial assets as of December 31, 2017)	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 the period-K-IFRS No. 1039	-	454,051	1,031,970	510,223	1,536,340	1,104,825	4,637,409
Reclassified loans and receivables to financial assets at fair value through profit or loss	1,314,296	-	(6,548)	-	(1,320,000)	(2,262)	(14,514)
Reclassified available-for-sale securities to financial assets at fair value through profit or loss	184,169	(184,169)	-	-	-	-	-
Long-term deposits in MSA Escrow Fund measured at amortized cost	-	-	1,971	9,402	-	-	11,373
Carrying amount at the beginning of the period-K-IFRS No. 1109	1,498,465	269,882	1,027,393	519,625	216,340	1,102,563	4,634,268

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, ₩32,733 million, including changes in fair value related to these financial assets, has been recognized in profit.

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 investment 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, ₩8,313 million, including changes in fair value related to these financial assets, has been recognized in profit.

③ Reclassified available-for-sale financial assets to financial assets at fair value through other comprehensive income (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 ₩9,402 million and retained earnings of ₩8,115 million have been increased as of January 1, 2018. Interest income related to the long-term deposits amounting to ₩3,680 million was recognized during the current period.

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

In millions of Korean won		
Type	Changes in accumulated other comprehensive income	Changes in retained earnings
Carrying amount at the beginning of the period- K-IFRS No. 1039	(1,812)	990,096
Reclassified loans and receivables to financial assets at fair value through profit or loss	-	(14,514)
Reclassified available-for-sale securities to financial assets at fair value through profit or loss	(3,895)	3,895
Reclassified available-for-sale securities to financial assets at fair value through other comprehensive income	(32,870)	32,870
Measured the long-term deposits in MSA Escrow Fund at the amortized cost	-	8,115
Increase in loss allowance on trade and other receivables (*)	-	(86,148)
Decrease in deferred income tax due to adjustment of retained earnings at the beginning of period	-	27,682
Total	(36,765)	(28,100)
Carrying amount at the beginning of period- K-IFRS No. 1109	(38,577)	961,996

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

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

In millions of Korean won					
Type	Measurement categories		Carrying amount		
	K-IFRS No. 1039	K-IFRS No. 1109	K-IFRS No. 1039	K-IFRS No. 1109	Difference
Cash and cash equivalents	Amortized cost	Amortized cost	1,104,825	1,102,563	(2,262)
Other financial assets	Amortized cost	Amortized cost	1,536,340	216,340	(1,320,000)
Other financial assets	Amortized cost	Fair value through profit or loss	-	1,314,296	1,314,296
Long-term deposits in MSA Escrow Fund	Financial assets at fair value through profit or loss	Amortized cost	510,223	519,625	9,402
Available-for-sale financial assets	Available-for-sale financial assets	Available-for-sale financial assets	454,051	269,882	(184,169)
Available-for-sale financial assets	Available-for-sale financial assets	Fair value through profit or loss	-	184,169	184,169
Trade and other receivables	Amortized cost	Amortized cost	1,031,970	1,027,393	(4,577)

## (2) Impairment of financial assets

The Company 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 instruments measured at amortized cost

The Company 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 K-IFRS No. 1115 'Revenue from Contracts with Customers'

As noted in Note 3, the Company 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 K-IFRS No. 1115 on the condensed interim financial statements is as follows:

(1) Adjustments reflected as of January 1, 2018 (the initial application date), in the condensed interim statements of financial position are as follows:

In millions of Korean won			
Type	As of December 31, 2017, before adjustments	Adjustments	As of January 1, 2018, after adjustments
Current assets	4,738,590	-	4,738,590
Non-current assets	3,936,373	-	3,936,373
Assets	8,674,963	-	8,674,963
Current liabilities	1,451,029	4,641	1,455,670
Non-current liabilities	80,377	(1,276)	79,101
Liabilities	1,531,406	3,365	1,534,771
Equity	7,143,557	(3,365)	7,140,192

The Company provides services to pay for logistics, insurance and card fees on behalf of customers for certain contracts signed with customers. Logistics costs, etc., are recognized as a deduction of revenue as they are payable to customers in accordance with K-IFRS No. 1115.

As a result of such changes in the standards, the Company recognized the payables amounting to ₩4,641 million additionally and reduced the retained earnings by ₩3,365 million.

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

In millions of Korean won			
Type	Amounts reported	Adjustments	If K-IFRS No. 1115 has not been applied
Sales	1,277,832	12,697	1,290,529
Cost of sales	476,136	(2,210)	473,926
Selling, general and administrative expenses	306,053	(10,487)	295,566
Income taxes	159,494	-	159,494
Profit for the period	509,549	-	509,549
Total comprehensive income for the period	494,258	-	494,258

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