

# **İSKENDERUN DEMİR VE ÇELİK A.Ş.**

Annual Report for the period

1 January - 31 December 2016

## INDEPENDENT AUDIT REPORT ON ANNUAL REPORT ISSUED BY THE BOARD OF DIRECTORS

Independent Audit Report on Annual Report issued by the Board of Directors

To the Board of Directors of İskenderun Demir ve Çelik A.Ş.;

We have audited the annual report of İskenderun Demir ve Çelik A.Ş. ("the Company"), for the period ended at 31 December 2016 pursuant to the Independent Audit Standards on Audit.

### **The responsibility of the Board of Directors on the Annual Report**

In accordance with Article 514 of the Turkish Commercial Code 6102 ("TCC") and the provisions of the Communiqué II-14.1 on the Principles of Financial Reporting In Capital Markets" ("the Communiqué") of the Capital Market Board ("CMB"), the management of the Company is responsible for the preparation and fair presentation of the annual report consistent with the financial statements and for the internal controls considered for the preparation of a report of such quality.

### **Responsibility of the Independent Auditor**

Our responsibility is to express an opinion, based on the independent audit we have performed on the Company's annual report in accordance with article 397 of the TCC and the Communiqué, on whether the financial information provided in this annual report is presented fairly and consistent with the Company's financial statements thereon which auditor's report dated February 7, 2017 has been issued.

Our independent audit has been performed in accordance with the Independent Auditing Standards as endorsed by CMB and Independent Auditing Standards which are a part of Turkish Auditing Standards promulgated by the Public Oversight, Accounting and Auditing Standards Authority. These standards require compliance with ethical provisions and the independent audit to be planned and performed to obtain reasonable assurance on whether the financial information provided in the annual report is free from material misstatement and consistent with the financial statements. This independent audit involves the application of auditing procedures in order to obtain audit evidence on the historical financial information. The selection of these procedures is based on the professional judgment of the independent auditor. We believe that the audit evidence we have obtained during our independent audit is sufficient and appropriate to provide a basis for our opinion.

### **Opinion**

In our opinion, the financial information provided in the annual report of the Board of Directors is presented fairly and consistent with the audited financial statements in all material respects.

### **Independent auditor's responsibilities arising from other regulatory requirements**

In accordance with paragraph third of Article 402 of the Turkish Commercial Code ("TCC") 6102, within the framework of the Independent Auditing Standards 570 "Going Concern" no material uncertainty has come to our attention which causes us to believe that the Company will not be able to continue as a going concern in the foreseeable future.

**Guney Bagimsiz Denetim ve Serbest Muhasebeci Mali Musavirlik Anonim Sirketi**

A member firm of Ernst & Young Global Limited

**Ethem Kutucular, SMMM**

**Responsible Auditor**

**February 7, 2017**

**Istanbul Turkey**

## ANNUAL REPORT

(Amounts in ("Thousand TL") unless otherwise stated)

### A - General Information

#### 1. Report Period

01.01.2016-31.12.2016

#### 2. Information on the Company

- Trade Title : İSKENDERUN DEMİR VE ÇELİK A.Ş.
- Trade Registry No : 1599
- Mersis No : 0879000967000028
- Head Office : Karayılan Mahallesi, 31319 İskenderun/HATAY
- İnternet website : [www.isdemir.com.tr](http://www.isdemir.com.tr)

#### 3. Shareholding Structure and Capital Distribution

Paid in Capital : 2.900.000 thousand TL

Shareholders	Share Value (TL)	%
Ereğli Demir ve Çelik Fabrikaları TAŞ.	2.756.978	95,07
Public portion	143.022	4,93
<b>General Total</b>	<b>2.900.000</b>	<b>100,00</b>

During the period the shares of the real persons, whose shares are distributed by İskenderun Demir ve Çelik A.Ş. Employee Benefit Fund Foundation are registered with the Central Registry Agency via OYAK Yatırım Menkul Değerler A.Ş. and started to be traded on the Pre-Market Trading Platform (PPLP)..

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(Amounts in (“Thousand TL”) unless otherwise stated.)

**4. Organization Chart**

- No change occurred in the organization structure of the Company within the period.

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(Amounts in ("Thousand TL") unless otherwise stated.)

### 5. Explanations related to privileged shares and voting rights of the shares

On the A Group shares, a usufruct has been established on behalf of the Privatization Administration to be valid until otherwise decided by the Higher Council for Privatization. Our company does not have any privileged share.

### 6. Information on the Board of Directors, Key Managers and number of personnel

The election of the members of the Board of Directors is carried out by the General Assembly within the framework of the provisions of the Company's Articles of Association in accordance with the Turkish Commercial Code and related regulations. For positions that are open if there is vacancy in the Board of Directors membership during the term, elections shall be held within the framework of the provisions of the Turkish Commercial Code and the Company's Articles of Association; and persons assigned are presented to the approval of the General Assembly. Amendments made during the period are made by the Board of Directors Resolution to be approved at the next Ordinary General Assembly. The Ordinary General Meeting of the Company for the year 2015 was held on 30 March 2016.

In accordance with Articles 9 and 10 of the Company's Articles of Association, the number of members of the Board of Directors has been determined as 9 directors at the Ordinary General Assembly Meeting held on March 30, 2016, within the framework of the provisions of the Turkish Commercial Code and the Capital Markets Law, and 6 Board Members are elected to hold office 1 year and 3 independent Board Members are elected to hold office 1 year.

Board of Directors for the reporting period:

Board of Directors	Position	Date of Commence ment
ATAER Holding A.Ş (Representative: Ömer Muzaffer BAKTIR)(**)	Chairman of the Board-Executive Member	15/11/2013
Erdemir Madencilik Sanayi ve Ticaret A.Ş. (Representative: Fatma CANLI)	Deputy Chairman of the Board	08/03/2010
T.C. Başbakanlık Özelleştirme İdaresi Başkanlığı (Representative: Bekir Emre HAYKIR)	Board Member	05/09/2016
OYAK Pazarlama Hizmet ve Turizm A.Ş. (Representative: Ertuğrul AYDIN)	Board Member	18/03/2008
Erdemir Mühendislik, Yönetim ve Danışmanlık Hizmetleri A.Ş. (Representative: Güliz KAYA)	Board Member	25/05/2016
Erdemir Çelik Servis Merkezi Sanayi ve Ticaret A.Ş. (Representative: Ahmet Türker ANAYURT)	Board Member	30/03/2016 (*)
Emin Hakan EM İN SOY	Independent Board Member	18/03/2014
Hakkı Cemal ERERDİ	Independent Board Member	30/03/2015
Ali Tuğrul ALPACAR	Independent Board Member	30/03/2015

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(Amounts in ("Thousand TL") unless otherwise stated.)

### Changes in the Board of Directors within the Year

According to the decision taken at the Ordinary General Assembly Meeting held on March 30, 2016, Mr. Mehmet Şükrü DOĞAN has been assigned as a Board Member, instead of Mustafa YURDABAK, as the representative of TR Prime Ministry Privatization Administration to hold office for 1 year; and Mr. Dursun Özer ÖZDİNÇ instead of the representative Dinc KIZILDEMİR is elected as a Board Member as the representative of Erdemir Mühendislik, Yönetim ve Danışmanlık Hizmetleri A.Ş., and Mr. Ahmet Türker ANAYURT is elected instead of Nihat KARADAĞ as the representative of Erdemir Çelik Servis Merkezi Sanayi ve Ticaret A.Ş.

It was resolved to elect Erdemir Madencilik Sanayi ve Ticaret A.Ş. (Representative: Fatma CANLI) as the Deputy Chairman of the Board in the delegation of powers in the Board of our Company as per the Board resolution no 379 dd. 31.03.2016.

Mr. Bekir Emre HAYKIR started to work on 05 September 2016 instead of Mehmet Şükrü Doğan as the representative of T. R. Prime Ministry Privatization Administration.

Ms. Güliz KAYA started to work on 25 May 2016 instead of Dursun Özer ÖZDİNÇ as the representative of Erdemir Mühendislik, Yönetim ve Danışmanlık Hizmetleri A.Ş..

According to the decision taken at the Ordinary General Assembly Meeting held on March 30, 2016, Emin Hakan EMİNSOY, Hakkı Cemal ERERDİ and Ali Tuğrul ALPACAR are elected as the Independent Board Members.

(\*\*)Pursuant to the resolution no 166 dd. 05 January 2017 of the Board of ATAER Holding A.Ş. Chairman and CEO of our Company; Mr. Ali Aydın PANDIR's office was ended on 06 January 2017 as the legal person representative of ATAER Holding A.Ş., and Mr. Ömer Muzaffer BAKTIR is assigned instead of him effective from January 16, 2017.

### Duties and Powers of Board Members

Chairman of the Board and the Board Members have the duties and powers in the Articles of Association of the Company and the applicable articles of the Turkish Commercial Code.

### Information on Board Members and the Duties of the Managers outside the Company

The Information on Board Members and the Duties of the Managers outside the Company is included in the Annex 1.

### Number of Board meetings within the Year and Attendance of the Board Members in the Meetings

The Board of Directors held 6 meetings within 2016. All of the Board Members attended such meetings regularly.

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(amounts in (“Thousand TL”) unless otherwise stated.)

Top Management

Top Management	Position	Starting Date	Education	Professional Experience
Toker ÖZCAN	General Manager	16/01/2017	Middle East Technical University -Faculty of Mechanical Engineering	25 Years
Şafak ÇAPAR	Deputy General Manager (Businesses)	02/07/2012	Middle East Technical University -Faculty of Metallurgy and Material Engineering	34 Years
Kemal Emre GÜLDEN	Deputy General Manager (Financial Affairs)	30/04/2013	Middle East Technical University - Economics	22 Years
Vacant	Deputy General Manager (Human Resources)	-	-	-
Ali BUĞDAY	Deputy General Manager (Procurement)	08/07/2015	Middle East Technical University - Faculty of metallurgy	21 Years

Changes in the Top Management within the Year

General Manager of our Company Mr. Recep ÖZHAN died on 08 July 2016, and no person was assigned instead of him from such date till the end of the year. Mr. Toker OZCAN was assigned as the General Manager from January 16, 2017.

Yener Burtay KORALTAN has been assigned as our Company’s Deputy General Manager responsible for Human Resources starting from 25 January 2017.

7. The activities of members of the board directly or on behalf of other parties, with the company and activities within the scope of competition prohibition

The Board Members are granted with the permission to conduct the transactions with the company for year 2016 as per the applicable articles of the Turkish Commercial Code (TCC) in the ordinary general Assembly held on 30 March 2016 held for the operations of the Company in 2015.

No transaction was made within the scope of this article.

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(amounts in ("Thousand TL") unless otherwise stated.)

### 8. Personnel and Labor Movements and Collective Bargaining Practices and Rights and Benefits Provided to Personnel and Workers

Number of personnel of İskenderun Demir ve Çelik A.Ş. as of 31 December 2016 and 31 December 2015:

	31 December 2016	31 December 2015
	# of persons	# of persons
Blue collar	3.286	3.446
White collar	1.742	1.816
	5.028	5.262

As of December 31, 2016, the provision for employment termination benefits was calculated by an independent actuary and provision amounting to TRY 188.399 Thousand was allocated.

### 9. Changes in the Articles of Association

No changes were made to the Articles of Association during the period.

### B – Board Member and Financial Rights provided to Top Managers

#### 1. Total amount of financial benefits such as attendance fee, wages, premiums, bonuses, profit shares provided

At the Ordinary General Assembly of our Company held on 30 March 2016 it is resolved that;

- No salary is to be paid to any of the Board Members elected as the Group B Shares,
- Net monthly salary of 2.360.-TL is to be paid to each of the Board Members elected for Group A Shareholders (in advance at the beginning of each month),
- Net monthly salary of 4.800.-TL is to be paid to each of the Board Members elected as Group A Shareholders (in advance at the beginning of each month),
- Such new salaries shall be applied starting from 01.04.2016.

Individual Accident and Death insurance was taken out for each of the Board of Directors and the Chairman of the Board.

No bonus payment was made to any of the Board Members as a reward for performance recognition.



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No debt was given to any of the Board Members and the managers within the period, or no guarantee or collateral was given for any of them to allow them to obtain any loan.

The salaries of the senior managers of our company are determined by the Board of Directors. Performance based additional payments are made to the personnel out of scope, including the senior managers of the company.

### **2. Information on the total amount of allowances, travel, accommodation and representation expenses, and cash and non-cash payments, insurance and similar guarantees**

Total annual expenses of 4.192 thousand TL were recorded related to the company managers including salary, premium and similar other benefits for the year ended on 31 December 2016. (31 December 2015: 4.933 Thousand TL).

### **C - Research and Development Works**

The official opening of the R&D Center in Erdemir Group, to which our company is affiliated, was realized on May 22, 2015 by the Minister of Science, Industry and Technology.

Raw materials projects for waste disposal and cost reduction, iron production for process improvement, steel production projects, and hot and cold product & process development projects continued. The activities of the three projects supported by TÜBİTAK TEYDEB continue successfully. Patent, utility model registration studies have been carried out. Through the purchase of various consultancy and training services, articles and papers were shared in national and international organizations.

Construction, renovation of buildings, projecting for simulators, procurement and procurement processes for the establishment of R & D Center building and simulation laboratories continued.

Within the scope of flat product development studies, development works of Erdemir Group R&D Center and S700 MC and DP 600 qualities are being carried out. In the long product, 1082 PC strand and 38Si7 Rail Connection equipment development works are being done. Steel production projects for process improvement, hot process development and coil process development projects have continued. We have 433 qualities, 268 being long products and 165 being flat products. In 2016, a total of 19 quality grades were developed, 7 of which are long and 12 of which are flat.

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(Amounts in (“Thousand TL”) unless otherwise stated.)

D - Activities and Significant Developments related to the Activities

1. Investment Activities

The total number of projects in Isdemir in 2016 is 14. Four projects from these projects have been launched this year; and 3 projects were completed in 2016. In 2016, the 2nd Blast Furnace Re-line, the Hot Rolling Mill Harmonic Filter / Compensation System and the 3rd and 4th Blast Furnace TRT Projects were completed; and facilities have been put into operation. 22 projects from the Environment Package project consisting of 25 proposals for the surrounding area were completed; Three projects are pending. Engineering works and field applications are continuing in the projects of the construction of the South Harbor and Filling Site, Electrical Station Dust Control and Water Cooling System Modernization, New Air Separation Facility and Hot Slab Marking Machine. Hot Rolling Mill Development Investments and 3rd Coke Battery Modernization Projects are investments that are in the process of procurement. Tender process and evaluation studies are ongoing for Under-Vacuum Gas Removal Facility, Isdemir Education Directorate Building, Inventory Combinations in Single Locations and Slab Casting Mold Level Control System Modernization Projects, which were decided to be started in 2016. Total investment expenditures of İskenderun Demir ve Çelik A.Ş. as of 31 December 2016 is 76.359 Bin USD (31 December 2015: 103.020 Bin USD)

2. Internal control system and internal audit activities

Our company does not have an Internal Audit Department. However, in Erdemir Group our company is included; the Internal Audit Directorate is available reporting to the Chairman of the Board and CEO to evaluate and improve effectiveness of Risk Management, Control and Governance processes.

3. Direct and Indirect Affiliates

The scope and proportion of the company in which the Company participates in its capital is as follows:

Company name	Country of Operation	Area of Operation	2016	2015
			Participation	Participati
			Ratio	on Ratio
			%	%
Teknopark Hatay A.Ş.	Türkiye	R & D Center	5	5
İsdemir Ünde Gaz Ortaklığı A.Ş.	Türkiye	Industrial Gas Production and Sales	50	

4. Information on the shares of company purchased back by the Company

None.

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(Amounts in ("Thousand TL") unless otherwise stated,)

### 5. Explanations related to independent audit and public audit

It is resolved in the ordinary general Assembly held on 30 March 2016 to contract with the independent audit company "Güney Bağımsız Denetim ve Serbest Muhasebeci Mali Müşavirlik A.Ş. (A Member Firm of Ernst & Young Global Limited) for the independent audit services in 2016.

The Company has been subject to limited audit by the Turkish Large-scale Taxpayers Group Presidency of the Ministry of Finance, the Tax Inspection Board of the Ministry of Finance for the period 2010-2011 and the tax and penalty notices have been notified to the Company in the amount of TRY 91 Thousand in total, composed of 37 Thousand TL of year 2010 and 54 Thousand TL of year 2010. We filed a lawsuit for cancellation of notifications.

Our Company has been subject to limited review for the period of 2013-2014 due to the SCT refund request. A total of TRY 184 Thousand refund / deduction request has been rejected within this scope: 101 Thousand TL for 2013 / August-2014 / February period; 18 thousand TL for 2014 / February-March period; and 64 thousand TL for the period of 2014 / May-October. In addition, as Private / General Irregularity Criminal, 4 Thousand TL tax / penalty notice was issued for the year 2013 and 5 Thousand tax / penalty notice was issued for 2014. The audit was challenged before a court and the case is pending.

For Year 2016 our company was audited by the Customs and Trade Inspectors affiliated to the Ministry of Customs and Trade; and the penalty decision was notified to us with the penalty resolution no 05.01.2017/17CK3106008 with the additional accrual decision dated/ numbered 04.01.2017/17ET3106001-1 for the understated demurrage related to the free circulation declaration, with registry number 153106001M002248 dated on 27 October 2015 by the Customs Directorate as per the report although not given to us currently.

As a result of the additional accrual decision, TL 32 Thousand was paid; With respect to VAT fines of 97 thousand TL, the Regional Directorate objected. In the period concerned, if the objection is rejected by the Regional Directorate in accordance with the opinion of our customs consultancy (as of December 31, 2016, our contract was expired), the matter will be brought to a court of law.

### 6. Legal matters

#### a) lawsuits

Taking into account the opinions of legal counsel and non-profit specialist attorneys, the Company Management determines the allowance amounts related to the ongoing lawsuits through possible cash outflows based on management's best estimate of the probability of loss and the liabilities to be incurred in case of loss. As of 31 December 2016, there is a provision amounting to TL 20,910 thousand in the statement of financial position.

#### b) Administrative-Legal Sanctions

None.

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(Amounts in ("Thousand TL") unless otherwise stated.)

7. General Assemblies

The ordinary general assembly meetings of our company are held in March every year in accordance with the applicable provisions of the Turkish Commercial Code and the Articles of Association of the Company, and any decision made in such meetings are performed within due times.

8. Grants and Social Responsibility Projects

The total amount of grants made by the Company to the public entitles and institutions for training, food and maintenance-repair is given in the below table:

(thousand TL)	1 January-31 December 2016	1 January- 31 December 2015
Cooperation Developed with Public Institutions and Organizations	1.653	504
Education and Training Activities	538	527
Cooperation Activities for Voluntary Work and Charity Works	131	126
Foundation, Association, Chamber and Ens. Cooperation Activities with	-	144
Sports Activities	-	125
Cultural and Artistic Activities	37	26
Support Activities in Health and Financial Issues	4	3
Grand total	2.363	1.455

9. Affiliated Companies (Related Party transactions)

a) Transactions

Our Company was not involved in any transaction with or as directed by or by the instructions of Ordu Yardımlaşma Kurumu (OYAK) and/ or OYAK's affiliates as the controlling shareholder of our company in 2016, and there was no legal transaction committed or avoided by our company for the interests of OYAK or any of its affiliates. It was resolved that all commercial operations of our controlling party and its affiliates with our company are in accordance with arm's length principle in 2016, that this report is prepared in accordance with the proper and honest accountability principles, in the resolution no 405 dd. 07 February 2017.

b) Explanation related to the transactions

İskenderun Demir ve Çelik A.Ş. produces sales to third parties using the information systems infrastructure and marketing management systems with Erdemir's staff for flat products. The products produced at Isdemir plants are sold by Erdemir without being included in the flow of production at all. In terms of Erdemir, these goods are "Commercial Inventory". Erdemir realizes the sale of the ordering customer based on the price and date purchased from Isdemir without adding any profit. Such products are considered as "raw materials" for Erdemir.

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(Amounts in ("Thousand TL") unless otherwise stated.)

As it is found the commercial operation in continues nature between our main shareholder Ereğli Demir Çelik Fabrikaları T.A.Ş. and our Company exceeds 10% of the total cost of sales in 2016, it is considered reasonable that the same transactions in 2017 will continue in accordance with the specified principles and that the transactions in question are compared with market conditions compatible with previous years.

### E - Financial Situation

#### 1. Summary of Financial Statements

Financial statements are prepared in accordance with financial reporting standards issued by the Capital Market Board. The financial statements for 31.12.2016 and 31.12.2015 were audited.

##### Summary Balance Sheet

	( Audited) Current Period	( Audited) Current Period
(thousand TL)	31 December 2016	31 December 2015
Current Assets	4.636.984	2.652.319
Fixed Assets	7.319.905	6.216.997
Total Assets	11.956.889	8.869.316
Short term liabilities	1.966.469	934.292
Long term liabilities	1.505.009	1.339.911
Equity	8.485.411	6.595.113
Total Assets	11.956.889	8.869.316

##### Summary Income Statement

	( Audited) Current Period	( Audited) Current Period
(thousand TL)	1 January 31 December 2016	1 January 31 December 2015
Revenues	6.470.668	5.916.385
Gross Profit	1.450.719	915.622
Operating Profit	1.271.824	775.043
Profit Before Tax	1386.861	933.593
Net Profit for the Period	942.849	575.243
EBITDA	1,619.218	1.056.338

The company is making the budget within the framework of its annual strategic targets and the prepared budget is approved by the Board of Directors.

The current status of the Company is reviewed in regular meetings of the Board of Directors, and Company activities are compared with previous periods and budget targets.

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(Amounts in ("Thousand TL") unless otherwise stated.)

### 2. Important Business Indicators and Financial Ratios

(%)	1 January 31 December 2016	1 January 31 December 2015
Gross Profit Margin	%22,4	%15,5
Operating profit Margin	%19,7	%13,1
EBITDA Margin	%25,0	%17,9
Net Profit Margin	%14,6	%9,7

### 3. Financial Strength

It is not foreseen that the capital of the company may be lost considering the calculations made based on the ratios defined in the article 376 of TCC.

### 4. Development of Financing Sources and Policies Applied by the Operator in the Field of Development

It is foreseen that the company will repay the existing loan debts by cash generated from the activities.

### 5. Nature and Amount of the Capital Market Instruments issued

No capital market instrument is issued for the period.

### 6. Dividend payment

Dividend Payment Policy submitted to the General Assembly held on 30 March 2016;

In principle, the Company has adopted a policy of distributing the entire cash distributable profit for the full amount of the distributable profit for the period allowed by the prospective free cash creation expectation, including market lease and financial leverage ratios and investment / financing requirements, within the framework of applicable legislation and the Company's Articles of Association. The profit distribution policy is reviewed every year by the Board of Directors according to national and global economic conditions, the projects on the agenda and the status of funds.

Dividends shall be paid in full and in cash, within the framework of the provisions of the legislation, by the Board of Directors at the General Assembly meeting decided to be distributed until 15 December of the relevant calendar year in one time..

The General Assembly is authorized to distribute Advance Dividend within the framework of the relevant legislative provisions."

It is resolved to pay out dividend 49,000 Thousand TL in cash from the profit for the year 2015 at the Ordinary General Assembly Meeting held on 30 March 2016 (dividend payment per gross share: 0.17 TL). The dividend payment is started on 25 May 2016.

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(Amounts in ("Thousand TL") unless otherwise stated.)

### 7. Information on the Industry of the Firm

World crude steel production reached 1.6 Billion Tons in 2016, down 0.8%. In 2016, China's crude steel production amounted to 808.4 million tons, down 1.2%, Japan's 0,3% down 104.8 million tons and South Korea's to 69.7 million tons with 1.6%, so that crude steel production in Asia amounted to 1.1 Billion Tons, down 1.6 percent year per annum. Germany, one of the European Union's major producers of steelmakers, recorded 42.1 million tons of crude steel production down 1.4% from last year, Italy as 23.3 million tons down 6.0% and France 14.6 million tons, down 2.3%; and 162.3 million tons of crude steel production in the EU-28 region, down 2.3 percent year in the year. The Commonwealth of Independent States countries produced 102.4 million tons of crude steel in 2016, indicating a slip of 0.8 percent on yearly basis; and in the same year North America produced 111 million tons of crude steel.

In the South America, the production of crude steel was reduced to 39.2 million Tons by 10.6% slip in 2016. In 2016, the average capacity usage rate is recorded as 69.3%. World hot product price change is given in the chart below:

Turkey's crude steel production in 2016 was recorded as 33.19 million tons, with the decrease of 5.3% compared to last year. The crude steel production of electric arc furnace plants decreased by 6.8% to 21.87 million tons in 2016 while crude steel production of integrated plants increased by 2.6% to 11.32 million tons.

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(Amounts in ("Thousand TL") unless otherwise stated.)

### 8. Place of the Company in the Company

In 2015, İskenderun Demir ve Çelik A.Ş. produced 5.2 million tons of crude steel. In 2016, crude steel production in our facilities increased by 8.4% to 5.584 thousand tons.

### 9. Incentives

The rights of the Company to be used by all companies that meet the criteria required by the legislation without sectoral separation are as follows:

- incentives under the research and development law (100% corporation tax exemption etc.),
- Cash support from Tübitak – Teydeb for research and development expenditures,
- Documents for inward processing,
- Social Security Institution incentives,
- Insurance premium employer support.

### 10. Development of the Company

İskenderun Demir ve Çelik A.Ş., as the Turkey's only integrated long and flat steel producer continued maintenance and modernization work successfully in all facilities, continued to optimize costs and to conduct activities as per the quality manufacturing principles in line with activities with maximum efficiency in 2016, and managed to produce 17% of Turkey's crude steel production.

In 2016, 2th Blast Furnace Re-line Project, Hot Rolling Mill Harmonic Filter / Compensation System and 3rd and 4th Blast Furnace TRT Projects were completed and the facilities were put into operation.

### 11. Business Units and Productivity of the Firm

Capacity utilization rates of İskenderun Demir ve Çelik A.Ş. are provided below:

	1 January-31 December 2016	1 January-31 December 2015
Capacity Utilization ratios (%)		
Liquid Steel	%98	%100
Slab	%80	%71
Ingot	%63	%63



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(Amounts in ("Thousand TL") unless otherwise stated)

12. Products

Below is a list of the main products produced in İskenderun Demir ve Çelik A.Ş. :

İsdemir  
Billet  
Coil  
Slab  
Hot Roll

13. Production (quantity)

Finished Product (000 Ton)	1 January - 31 December 2016	1 January - 31 December 2015
Slab	1006	455
Flat products	2.874	3.040
Long products	1572	1.563

14.Developments in Sales

Iron-steel industry is the driving force for the economy of a country. Turkey is one of the leading countries in this sector in the world in terms of both production and consumption. Our country which is the 8th largest steel consumer in the world, continued its growth in 2016 by 1%, also recorded a growth in 2015 by 11.7%.

Along with the increasing consumption in the sector, İskenderun Demir ve Çelik A.Ş.'s total flat product sales in 2016 reached to 3.9 million tons. Domestic flat product sales decreased by 15% to 3.4 million tons compared to the previous year. Long product sales increased by 2% to 1.6 million tons. Domestic long product sales did not change and was realized as 1.4 million tons.

İskenderun Demir ve Çelik A.Ş. exported 748 thousand tons of final products, composed of 197 thousand tons of flat products and 551 thousand tons of long products. This amount accounts for 14% of total final product sales. It exported flat products to 39 countries and long products to 14 countries

Despite the geopolitical problems in our geography, our company continues to deliver shipments in packaging, automotive, steel pipe, construction and manufacturing industries in line with its targets. The Company managed to include 45 new customers in its customer portfolio composed of 11 customers for long products and 34 customers for flat products, in 2016.

We continued to organize customer events, customer visits, national and international congresses, fair attendances, sector associations and official organizations, meetings with customers, to develop our relations with the customers who became the focus point by rebuilding the marketing and sales organization. With our new quality and product development studies aimed at end users, we continued to develop our product range dynamically managed in line with customer expectations and the improvements made have helped İskenderun Demir ve Çelik A.Ş. increase the power of the market.

(Amounts in (“Thousand TL”) unless otherwise stated.)

15. Sales (quantity)

Finished Product (000 Ton)	1 January - 31 December 2016	1 January - 31 December 2015
Slab (*)	973	481
Flat Products sales	2.964	2.920
Long Products sales	1.587	1.552

(\*) Slab sales are composed of intragroup sales.

F - Risks and Evaluation by the Board of Directors

1. Risk management policy

Risk is monitored and managed in accordance with the regulation on the development of hedging methods and the rules on managing market risks and receivables risks so that the risks faced by Iskenderun Demir ve Çelik A.Ş. may be measured and kept within the prescribed risk tolerances. In order to manage the interest risks exposed to our company, the durations are calculated on the basis of the loan portfolio and cash flow projections and the gain / loss amounts to be experienced in possible interest changes are measured by sensitivity analysis.

In addition, applications are being made to ensure that the rate of the variable rate loans in Iskenderun Demir ve Çelik A.Ş. 's total loan portfolio is monitored and kept within a certain limit. According to the needs of the company and the market, derivative instrument options are evaluated and detailed analyzes are carried out and appropriate actions are taken within limits. Similarly, for liquidity risk management, the use of credit and repayments and cash flow projections are followed, and necessary action plans are prepared.

The feasibility report, which includes the financial and technical evaluations of all investments planned to be made in the middle / long term strategic road map of Iskenderun Demir ve Çelik A.Ş., is prepared by the System Development Directors within the scope of Technical Services Deputy General Director and presented to the Assistant General Manager of Financial Affairs. The Vice Chief Financial Officer reviews the financial feasibility of the feasibility report and presents the financial valuation report to the Group Financial Coordinator, which reviews and evaluates the profitability, net present value, internal rate of return, return on investment and return on investment ratios, and then submitted to the Board in the event of approval thereof.

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(Amounts in ("Thousand TL") unless otherwise stated.)

### **2. Early Detection of Risk Committee**

None.

### **3. Prospective Risks**

1) Market risks: The price risks that started in commodity markets after 2008 are still continuing as of 2016. In particular, over capacity from Europe is exerting pressure on steel prices. However, fluctuations in iron ore prices formed according to China's iron ore needs, also cause fluctuations in raw material prices as iron ore is subject to contracts in quarterly terms.

The fluctuations in the prices of iron ore and coking coal, which are the production inputs of our company, the fluctuations in the price of steel products as production output, and the periods between supply and delivery times are longer in the iron and steel sector than in other sectors and therefore fluctuations in profit margins are the most important market risks.

2) Macroeconomic risks: Due to US Dollar denomination of raw material prices and sales prices of the products, fluctuations occur in the demand for steel products and costs related to steel. In addition, the possibility of reduction in steel demand in Turkey due to liquidity reduction in the markets due to decrease in the asset purchases by FED are among the most important risks that our Group may face.

Operational and financial risks that may arise in addition to these risks are continuously monitored by the Group Risk Management Department and are reported to the Board of Directors by the risk early detection committee operating within the Group Management.

### **G – Other Issues**

#### **1. Organizations outside the Head Office**

None.

#### **2. Information on change in legislations that may affect the operations of the Company significantly**

None.

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(Amounts in ("Thousand TL") unless otherwise stated.)

### **3. Conflicts of Interest between the Company and the Institutions Providing Services to the Company, on the subjects such as Investment Advisory and Rating, and Information on Measures taken by the Company to Prevent these Conflicts of Interest**

None.

### **4. Information on the Social Rights, Vocational Training of the Employees and Other Activities of the Company having Social and Environmental Consequences**

Our employees within the scope are entitled to annual leave, total of 120 days bonus, holiday allowance, fuel allowance, annual paid leave allowance, marriage / birth / death allowance, active military benefit, child / education allowance, supplementary health insurance, with notice period and compensation in accordance with the collective bargaining agreement. Employees within and out of scope are entitled to social benefits such as food and vehicle supports, incentives to encourage senior labor, private health insurance for out-of-scope personnel, and individual retirement plan benefits for the managers and upper level personnel. İskenderun Demir ve Çelik A.Ş. considering providing secure and healthy business environment to its employees as a priority, provides preventive medicine, work entry examinations, periodic examinations, occupational accidents and occupational diseases preventive works, first aid and emergency treatment services.

Many training opportunities are made available such as in-Unit Training System (ITS), seminars and conferences both in Turkey and abroad. The training programs are planned to contribute to the realization of the strategic goals of İskenderun Demir ve Çelik A.Ş., and to realize the basic principles of the Quality, HSE, Environmental and Energy Management Systems Policy. Performance appraisal outputs are used to determine the training and development needs of employees.

OHS trainings are given in accordance with the Law No. 6331, informing employees about their legal rights and responsibilities, determining the hazards and risks they face, and measures to be taken. Furthermore, trainings are carried out within the scope of the regulation stipulating that employees who have not received required vocational training cannot be operated dangerously and very dangerously. Work at Height training –as one of these trainings organized for those who work in different high platforms- and the scaffolding trainings organized for the employees installing scaffolds were realized with theoretical-practical applications, and certificates were given to our successful employees.

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[Amounts in ("Thousand TL") unless otherwise stated.]

### 5. Related party transactions and Information required to be given on balances

The parent shareholder of the Company is Ereğli Demir ve Çelik Fabrikaları T.A.Ş. And its ultimate shareholder is Ordu Yardımlaşma Kurumu (Military Assistance Agency).

The details of the commercial transactions between the Company and its related parties:

	31 December 2016	31 December 2015
<b>Receivables from related parties (short term)</b>		
Ereğli Demir ve Çelik Fabrikaları T.A.Ş. <sup>(1)</sup>	308.982	277.578
Erdemir Çelik Servis Merkezi San. ve Tic. A.Ş. <sup>(2)</sup>	23.817	10.930
Adana Çimento Sanayi T.A.Ş. <sup>&lt;3)</sup>	6.066	6.070
Aslan Çimento A.Ş. <sup>(3)</sup>	645	168
Erdemir Asia Pacific PTE LTD <sup>(2)</sup>	4.804	5.243
Omsan Lojistik A.Ş. <sup>(3)</sup>	41	98
Oyak Pazarlama Hizmet ve Turizm A.Ş. <sup>&lt;3)</sup>	84	39
Oyak Savunma ve Güvenlik Sistemleri A.Ş. <sup>(3)</sup>	53	54
Omsan Denizcilik A.Ş. <sup>(3)</sup>	4	59
	344.496	300.239

The details between the Company and the related parties are explained below.

	31 December 2016	31 December 2015
<b>Other Receivables from related parties (short term)</b>		
Ereğli Demir ve Çelik Fabrikaları T.A.Ş. <sup>(1)</sup>	2.050.619	751.026
	2.050.619	751.026

**Other Receivables from related parties (short term) consist of the monetary receivables extended as per the central cash planning.**

The Company produces sales to third parties using the information systems infrastructure and marketing management systems with Erdemir's staff for flat products. The products produced at Isdemir plants are sold by Erdemir without being included in the flow of production at all. In terms of Erdemir, these goods are "Commercial Inventory". Erdemir realizes the sale of the ordering customer based on the price and date purchased from Isdemir without adding any profit. In this sense, trade receivables and other receivables occur from sales though single center in the balance sheets depending on sales and delivery of the flat products to third parties between Erdemir and Isdemir.

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(Amounts in (“Thousand TL”) unless otherwise stated.)

The details of the commercial transactions between the Company and its related parties are as follows:

Trade payables to the related parties (short term)	31 December 2016	31 December 2015
Erdemir Madencilik San. ve Tic. A.Ş.<2>	24.641	5.051
Oyak Pazarlama Hizmet ve Turizm A.Ş.<3>	1.907	2.242
Erdemir Asia Pacific PTE LTD<2>	28.137	5.214
Omsan Lojistik A.Ş. <3>	3.680	1.539
OYAK Savunma ve Güvenlik Sistemleri A.Ş.<1>	2.053	1.498
Erdemir Müh. Yön. ve Dan. Hiz. A.Ş.<2>	3.722	7.767
Omsan Denizcilik A.Ş.<3>	1.640	1.436
Erdemir Çelik Servis Merkezi San. ve Tic. A.Ş.<1>	1.458	715
Other	950	149
	68.18S	25.611

Trade payables due to the related parties are generally caused by service purchases.

	1 January -31 December 2016	1 January-31 December 2015
Significant sales to the related parties		
Ereğli Demir ve Çelik Fabrikaları T.A.Ş.<1>	4.004.851	3.585.249
Erdemir Çelik Servis Merkezi San. ve Tic. A.Ş.	1.810	2.586
Adana Çimento Sanayi T.A.Ş. <1>	16.523	20.700
Erdemir Asia Pacific PTE LTD<2>	60.158	50.636
Erdemir Madencilik San. ve Tic. A.Ş.<1>	-	47
Aslan Çimento A.Ş.<3>	1.635	1.209
Erdemir Müh. Yön. ve Dan. Hiz. A.Ş.<1>	476	315
Other	2.183	3.272
	4.087.636	3.664.014

Parent company  
An affiliate of the parent company  
An affiliate of the ultimate  
shareholder company

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	1 January-31 December 2016	1 January-31 December 2015
Significant purchases from the related parties		
Erdemir Madencilik San. ve Tic. A.Ş.	329.217	355.478
Erdemir Asia Pacific PTE LTD <sup>(2)</sup>	95.044	77.459
Ereğli Demir ve Çelik Fabrikaları T.A.Ş. <sup>**</sup>	113.120	70.785
Oyak Pazarlama Hizmet ve Turizm A.Ş. <sup>&lt;3)</sup>	18.720	22.741
Omsan Denizcilik A.Ş. <sup>&lt;3)</sup>	27.105	15.230
Oyak Savunma ve Güvenlik Sistemleri A.Ş. <sup>(3)</sup>	17.519	16.805
Omsan Lojistik A.Ş. <sup>(3)</sup>	30.827	11.811
Erdemir Çelik Servis Merkezi San. ve Tic. A.Ş. <sup>(2)</sup>	8.232	8.028
Erdemir Müh. Yön. ve Dan. Hiz. A.Ş. <sup>&lt;-&gt;</sup>	25.319	10.043
Other	3.153	3.281
	668.256	591.661

(1) Parent company

(2) An affiliate of the parent company

(3) An affiliate of the ultimate shareholder company

Terms and conditions of transactions with related parties:

At the end of the period, the balances realized for commercial products are secured and the payments are made in cash. Other receivables are unsecured, interest-bearing and cash-based. For the year ended December 31, 2016, the Company did not allocated any provision for doubtful receivables from related parties. (31 December 2015: None).

6. Information to Stakeholders

The capital of İsdemir Linde Gaz Ortaklığı A.Ş. in which İskenderun Demir ve Çelik A.Ş. is a shareholder as well, being 50 Thousand TL, was increased to 27.000 thousand TL by the increase of 26.950 thousand TL at the Ordinary General Assembly for the year 2016, and all of the capital increased was paid by the shareholders on 27 January 2017.

Annex-1 Other positions of the Board Members held by them outside the Company		
Board of Directors	Position	Positions executed by the representative outside the Company
ATAER Holding A.Ş. Representative - Ömer Muzaffer BAKTIR	Chairman of the Board and Executive Member	<ul style="list-style-type: none"> <li>- Ereğli Demir ve Çelik Fabrikaları T.A.Ş. - Chairman of the Board, Executive Member (Representative)</li> <li>- Erdemir Mühendislik Yönetim ve Danışmanlık Hizmetleri A.Ş.- Chairman of the Board (Representative)</li> <li>- Erdemir Romania SRL - Chairman of the Board</li> <li>- Erdemir Çelik Servis Merkezi San. ve Tic. A.Ş. - Chairman of the Board (Representative)</li> <li>- Erdemir Asia Pacific Pte. Ltd. - Chairman of the Board</li> </ul>
Erdemir Madencilik San. ve Tic. A.Ş. Representative - Fatma CANLI	Deputy Chairman of the Board	<ul style="list-style-type: none"> <li>- Ereğli Demir ve Çelik Fabrikaları A.Ş. - Board Member (Representative)</li> <li>- Erdemir Mühendislik Yönetim ve Danışmanlık Hizmetleri A.Ş. - Board Member (Representative)</li> <li>- Erdemir Asia Pacific Pte. Ltd. - Board Member</li> <li>- HEKTAŞ Tic. T.A.Ş.- Chairman of the Board (Representative)</li> <li>- Akdeniz Kimya San. ve Tic. A.Ş.- Board Member (Representative)</li> <li>- OYAK Global Investments-Board Member</li> <li>- Micromedicine Inc. - Board Member</li> <li>- İskenderun Enerji Üretim ve Tic. A.Ş.- Board Member (Representative)</li> <li>- OYAK Renault Otomobil Fabrikaları A.Ş. - Board Member (Representative)</li> <li>- OYAK Anker Bank GmbH - Member of Supervisory Board</li> <li>- Örfin Finansman A.Ş. - Board Member</li> <li>- MAİS Motorlu Araçlar imal ve Satış A.Ş. - Board Member (Representative)</li> <li>- ORF Kiralama Pazarlama ve Pazarlama Danışmanlığı A.Ş.- Board Member (Representative)</li> </ul>



T.C. Başbakanlık özelleştirme İdaresi Başkanlığı Representative - Bekir Emre HAYKIR	Board Member	Başbakanlık Özelleştirme idaresi Vice President
OYAK Pazarlama Hizmet ve Turizm A.Ş. Representative - Ertuğrul AYDIN	Board Member	<ul style="list-style-type: none"><li>- ATAER Holding A.Ş. - Chairman of the Board (Representative)</li><li>- Ereğli Demir ve Çelik Fabrikaları A.Ş. - Deputy Chairman of the Board(Representative)</li><li>- Erdemir Asia Pacific Pte. Ltd. - Board Member</li><li>- OSİAT Sigorta Acentelik Hizmetleri A.Ş. - Chairman of the Board (Representative)</li><li>- Akdeniz Kimya San. ve Tic. A.Ş.- Chairman of the Board (Representative)</li><li>-OYAK Global Investments-Board Member Chemson Polymer Additive AG (Austria) - Member of Supervisory Board</li><li>- Akdeniz Kimyasal Ürünler Pazarlama iç ve Dış Tic. A.Ş. - Board Member (Representative)</li><li>- İskenderun Enerji Üretim ve Tic. A.Ş.- Yönetim Kurulu 1. Başkan Yrd. (Representative)</li><li>- OYAK Anker Bank GmbH - Member of Supervisory Board</li><li>-OYAK Portföy Yönetimi- - Chairman of the Board</li></ul>
Erdemir Çelik Servis Merkezi San. Ve Tic. A.Ş. Representative - Ahmet Türker ANAYURT	Board Member	<ul style="list-style-type: none"><li>- Ereğli Demir ve Çelik Fabrikaları A.Ş. - Board Member (Representative)</li><li>- Erdemir Madencilik San. ve Tic. A.Ş.- Board Member (Representative)</li><li>- Erdemir Romania SRL. - Board Member</li><li>- Erdemir Çelik Servis Merkezi San. ve Tic. A.Ş. - Board Member (Representative)</li><li>- Akdeniz Kimya San. ve Tic. A.Ş.- Board Member (Representative)</li><li>-OYAK Global Investments- Board Member</li><li>- OYAK Çimento AŞ.- Board Member (Representative)</li><li>- OMSAN Lojistik A.Ş.- Board Member (Representative)</li><li>- OMSAN Havacılık A.Ş.- Board Member (Representative)</li><li>- OMSAN Denizcilik A.Ş. Board Member (Representative)</li></ul>

Erdemir Mühendislik, yönetim ve Danışmalık Hizmetleri A.Ş. Representative - Güliz KAYA	Board Member	- Ereğli Demir ve Çelik Fabrikaları A.Ş. - Board Member (Representative)
Emin Hakan EMINSOY	Independent Board Member	- Ereğli Demir ve Çelik Fabrikaları A.Ş. - Independent Board Member - Sardes Faktoring A.Ş. - Chairman of the Board - AK Sigorta A.Ş. - Independent Board Member
Hakkı Cemal ERERDİ	Independent Board Member	- Ereğli Demir ve Çelik Fabrikaları A.Ş. - Independent Board Member - Ethica Sigorta A.Ş. - Deputy Chairman of the Board - Ethica Sigorta A.Ş. - General Manager
Ali Tuğrul ALPACAR	Independent Board Member	Alpacar Associates Executive Partner