KT&G CORPORATION AND SUBSIDIARIES

Consolidated Interim Financial Statements

June 30, 2017 and 2016

(Unaudited)

(With Independent Auditors' Review Report Thereon)

Contents

Independent Auditors' Review Report

Based on a report originally issued in Korean

The Board of Directors and Shareholders
KT&G Corporation:

Reviewed Financial Statements

We have reviewed the accompanying consolidated interim financial statements of KT&G Corporation (the "Parent Company") and its subsidiaries (collectively the "Group"), expressed in Korean won, which comprise the consolidated interim statement of financial position as of June 30, 2017, the consolidated interim statements of comprehensive income for the three- and six-month periods ended June 30, 2017 and 2016, the consolidated interim statements of changes in equity and cash flows for the six-month periods ended June 30, 2017 and 2016 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 consolidated interim financial statements in accordance with Korean International Financial Reporting Standards ("K-IFRS") No.1034 *Interim Financial Reporting*, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Review Responsibility

Our responsibility is to issue a report on these consolidated interim financial statements based on our reviews.

We conducted our reviews in accordance with the Review Standards for Quarterly and Semi-annual Financial Statements established by the Securities and Futures Commission of the Republic of Korea. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Korean Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our reviews, nothing has come to our attention that causes us to believe that the accompanying consolidated interim financial statements referred to above are not prepared, in all material respects, in accordance with K-IFRS No.1034 *Interim Financial Reporting*.

The accompanying consolidated interim financial statements as of and for the three- and six-month periods ended June 30, 2017 have been translated into United States dollars solely for the convenience of the reader and such translation does not comply with K-IFRS. We have reviewed the translation and nothing came to our attention that causes us to believe that the consolidated interim financial statements expressed in Korean won have not been translated into dollars on the basis set forth in note 4 to the consolidated interim financial statements.

Other matters

The procedures and practices utilized in the Republic of Korea to review such consolidated interim financial statements may differ from those generally accepted and applied in other countries.

The consolidated statement of financial position of the Group as of December 31, 2016, and the related consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, which are not accompanying this report, were audited by us in accordance with Korean Standards on Auditing and our report thereon, dated February 24, 2017, expressed an unqualified opinion. The accompanying consolidated statement of financial position of the Group as of December 31, 2016, presented for comparative purposes, is not different from that audited by us in all material respects.

KPMG Samjong Accounting Corp.
Seoul, Korea
August 11, 2017

This report is effective as of August 11, 2017, the review report date. 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 consolidated 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.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Financial Position
(Unaudited)

As of June 30, 2017 and December 31, 2016

In millions of won and thousands of U.S. dollars	*Note*	*June 30, 2017 Korean won*	*June 30, 2017 U.S. dollars (note 4)*	*December 31, 2016 Korean won*
Assets				
Property, plant and equipment	*6,16*	₩ 1,646,890	$ 1,445,147	₩ 1,601,877
Intangible assets	*7*	102,676	90,099	104,929
Investment property	*8,16*	337,459	296,120	341,580
Investments in associates and joint ventures	*5,9*	60,016	52,664	56,476
Available-for-sale financial assets	*10,31*	424,519	372,516	385,096
Other financial assets	*14,16,31*	6,351	5,573	11
Long-term deposits in MSA Escrow Fund	*11,31,33*	518,585	455,059	503,592
Long-term advance payments	*33*	96,235	84,446	86,592
Long-term prepaid expenses		5,453	4,785	6,091
Long-term trade and other receivables	*12,31*	60,374	52,978	69,942
Deferred income tax assets		33,323	29,241	35,757
Total non-current assets		3,291,881	2,888,628	3,191,943
Inventories	*13*	2,036,833	1,787,322	2,265,355
Current available-for-sale financial assets	*10,31*	-	-	1,500
Current other financial assets	*14,16,31,32*	952,425	835,754	1,657,338
Prepaid tobacco excise and other taxes		403,357	353,946	439,413
Trade and other receivables	*12,24,31*	1,298,330	1,139,286	1,283,647
Advance payments	*33*	131,330	115,242	69,364
Prepaid expenses		24,655	21,635	26,924
Cash and cash equivalents	*14,31,32*	998,844	876,487	850,786
Total current assets		5,845,774	5,129,672	6,594,327
Non-current assets held for sale	*5,15*	26,315	23,092	26,315
Total assets		₩ 9,163,970	$ 8,041,392	₩ 9,812,585

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Financial Position, Continued
(Unaudited)

As of June 30, 2017 and December 31, 2016

In millions of won and thousands of U.S. dollars	*Note*	*June 30, 2017 Korean won*	*June 30, 2017 U.S. dollars (note 4)*	*December 31, 2016 Korean won*
Equity				
Ordinary shares	*1,17*	₩ 954,959	$ 837,978	₩ 954,959
Other capital surplus	*17*	(29,715)	(26,075)	(3,430)
Treasury shares	*18*	(328,157)	(287,958)	(328,157)
Gain on reissuance of treasury shares	*18*	513,776	450,839	513,776
Reserves	*19*	4,932,462	4,328,239	4,296,523
Retained earnings	*20*	1,051,739	922,902	1,612,032
Equity attributable to owners of the parent		7,095,064	6,225,925	7,045,703
Non-controlling interests		57,676	50,611	72,554
Total equity		7,152,740	6,276,536	7,118,257
Liabilities				
Long-term borrowings	*16,22,31,32*	104,851	92,007	115,953
Long-term trade and other payables	*16,21,31*	18,021	15,813	14,700
Long-term advance receipts		10,130	8,889	9,877
Defined benefit liabilities	*23*	143,850	126,228	123,610
Provision		5,120	4,493	4,703
Deferred income tax liabilities		294,202	258,162	272,106
Total non-current liabilities		576,174	505,592	540,949
Short-term borrowings	*16,22,31,32*	58,452	51,292	136,599
Current portion of long-term borrowings	*16,22,31,32*	1,625	1,426	9,597
Trade and other payables	*16,21,31*	588,092	516,052	622,208
Advance receipts		10,826	9,500	9,573
Income tax payable	*28*	189,870	166,611	210,213
Tobacco excise and other taxes payable		586,191	514,383	1,165,189
Total current liabilities		1,435,056	1,259,264	2,153,379
Total liabilities		2,011,230	1,764,856	2,694,328
Total equity and liabilities		₩ 9,163,970	$ 8,041,392	₩ 9,812,585

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Comprehensive Income
(Unaudited)

For the six-month periods ended June 30, 2017 and 2016

In millions of won and thousands of U.S. dollars, except earnings per share	*Note*	*2017 Korean won*	*2017 U.S. dollars (note 4)*	*2016 Korean won*
Sales	*5,24,33*	₩ 2,340,446	$ 2,053,743	₩ 2,179,440
Cost of sales	*24,25*	(939,900)	(824,763)	(863,852)
Gross profit		1,400,546	1,228,980	1,315,588
Selling, general and administrative expenses	*25*	(618,633)	(542,851)	(576,769)
Operating profit	*5*	781,913	686,129	738,819
Other income	*26*	24,189	21,226	45,034
Other expenses	*26*	(104,495)	(91,694)	(38,750)
Net finance income	*27,31*	19,243	16,885	29,215
Share of gain of associates	*9*	5,119	4,492	1,406
Share of loss of associates	*9*	-	-	(113)
Profit before income tax		725,969	637,038	775,611
Income tax expense	*28*	(216,115)	(189,641)	(205,303)
Profit for the period		₩ 509,854	$ 447,397	₩ 570,308
Other comprehensive income (loss):				
Items that are or may be reclassified subsequently to profit or loss				
Unrealized net changes in fair value of available-for-sale financial assets, net of tax		₩ 28,095	$ 24,653	₩ (5,564)
Exchange differences on translating foreign operations, net of tax		(3,130)	(2,747)	11,098
Items that will not be reclassified to profit or loss				
Remeasurements of the defined benefit liability, net of tax		(628)	(551)	(203)
Other comprehensive income (loss) for the period, net of tax		24,337	21,355	5,331
Total comprehensive income for the period		₩ 534,191	$ 468,752	₩ 575,639
Profit attributable to:				
- Owners of the Parent Company		₩ 508,803	$ 446,475	₩ 569,334
- Non-controlling interests		1,051	922	974
		₩ 509,854	$ 447,397	₩ 570,308
Total comprehensive income attributable to:				
- Owners of the Parent Company		₩ 530,201	$ 465,252	₩ 574,299
- Non-controlling interests		3,990	3,500	1,340
		₩ 534,191	$ 468,752	₩ 575,639
Earnings per share in won and U.S. dollars:				
Basic and diluted	*29*	₩ 4,030	$ 3.54	₩ 4,514

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES

Consolidated Interim Statements of Comprehensive Income, Continued

(Unaudited)

For the three-month periods ended June 30, 2017 and 2016

In millions of won and thousands of U.S. dollars, except earnings per share	*Note*	*2017 Korean won*	*2017 U.S. dollars (note 4)*	*2016 Korean won*
Sales	*5,24,33*	₩ 1,161,699	$ 1,019,391	₩ 1,088,097
Cost of sales	*24,25*	(461,778)	(405,211)	(439,764)
Gross profit		699,921	614,180	648,333
Selling, general and administrative expenses	*25*	(313,463)	(275,064)	(302,478)
Operating profit	*5*	386,458	339,116	345,855
Other income	*26*	43,842	38,471	34,359
Other expenses	*26*	(38,570)	(33,845)	(11,150)
Net finance income	*27,31*	(1,225)	(1,075)	13,193
Share of gain of associates	*9*	3,650	3,203	802
Share of loss of associates	*9*	6	5	-
Profit before income tax		394,161	345,875	383,059
Income tax expense	*28*	(119,467)	(104,833)	(97,467)
Profit for the period		₩ 274,694	$ 241,042	₩ 285,592
Other comprehensive income (loss):				
Items that are or may be reclassified subsequently to profit or loss				
Unrealized net changes in fair value of available-for-sale financial assets, net of tax		₩ 23,010	$ 20,191	₩ (11,615)
Exchange differences on translating foreign operations, net of tax		1,921	1,686	4,672
Items that will not be reclassified to profit or loss				
Remeasurements of the defined benefit liability, net of tax		(37)	(32)	(53)
Other comprehensive income (loss) for the period, net of tax		24,894	21,845	(6,996)
Total comprehensive income for the period		₩ 299,588	$ 262,887	₩ 278,596
Profit attributable to:				
- Owners of the Parent Company		₩ 274,295	$ 240,695	₩ 284,945
- Non-controlling interests		399	347	647
		₩ 274,694	$ 241,042	₩ 285,592
Total comprehensive income attributable to:				
- Owners of the Parent Company		₩ 299,191	$ 265,541	₩ 277,775
- Non-controlling interests		397	346	821
		₩ 299,588	$ 262,887	₩ 278,596
Earnings per share in won and U.S. dollars:				
Basic and diluted	*29*	₩ 2,172	$ 1.91	₩ 2,259

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Changes in Equity
(Unaudited)

For the six-month period ended June 30, 2017

In millions of won		*Ordinary shares*	*Other capital surplus*	*Treasury shares*	*Gain on reissuance of treasury shares*	*Reserve*	*Retained earnings*	*Owners of the parent*	*Non-controlling interests*	*Total equity*
Balance at January 1, 2017	₩	954,959	(3,430)	(328,157)	513,776	4,296,523	1,612,032	7,045,703	72,554	7,118,257
Total comprehensive income for the period:										
Profit for the period		-	-	-	-	-	508,803	508,803	1,051	509,854
Other comprehensive income (loss):										
Net changes in fair value of available-for-sale financial assets, net of tax		-	-	-	-	28,095	-	28,095	-	28,095
Exchange differences on translating foreign operations, net of tax		-	-	-	-	(6,072)	-	(6,072)	2,194	(3,130)
Remeasurements of the defined benefit liability, net of tax		-	-	-	-	-	(625)	(625)	(3)	(628)
Total other comprehensive income (loss)		-	-	-	-	22,023	(625)	21,398	2,939	24,337
Total comprehensive income for the period		-	-	-	-	22,023	508,178	530,201	3,990	534,191
Transactions with owners, recorded directly in equity:										
Dividends		-	-	-	-	-	(454,555)	(454,555)	-	(454,555)
Transfer from reserve for research and human resource development		-	-	-	-	(10,000)	10,000	-	-	-
Transfer to unconditional reserve		-	-	-	-	623,916	(623,916)	-	-	-
Acquisition of non-controlling interests		-	(26,285)	-	-	-	-	(26,285)	(18,868)	(45,153)
Total transactions with owners		-	(26,285)	-	-	613,916	(1,068,471)	(480,840)	(18,868)	(499,708)
Balance at June 30, 2017	₩	954,959	(29,715)	(328,157)	513,776	4,932,462	1,051,739	7,095,064	57,676	7,152,740

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Changes in Equity, Continued
(Unaudited)

For the six-month period ended June 30, 2017

In thousands of U.S. dollars (note 4)	*Ordinary shares*	*Other capital surplus*	*Treasury shares*	*Gain on reissuance of treasury shares*	*Reserve*	*Retained earnings*	*Owners of the parent*	*Non-controlling interests*	*Total equity*
Balance at January 1, 2017	$ 837,978	(3,009)	(287,958)	450,839	3,770,203	1,414,558	6,182,611	63,666	6,246,277
Total comprehensive income for the period:									
Profit for the period	-	-	-	-	-	446,475	446,475	922	447,397
Other comprehensive income (loss):									
Net changes in fair value of available-for-sale financial assets, net of tax	-	-	-	-	24,653	-	24,653	-	24,653
Exchange differences on translating foreign operations, net of tax	-	-	-	-	(5,328)	-	(5,328)	2,581	(2,747)
Remeasurements of the defined benefit liability, net of tax	-	-	-	-	-	(548)	(548)	(3)	(551)
Total other comprehensive income (loss)	-	-	-	-	19,325	(548)	18,777	2,578	21,355
Total comprehensive income for the period	-	-	-	-	19,325	445,927	465,252	3,500	468,752
Transactions with owners, recorded directly in equity:									
Dividends	-	-	-	-	-	(398,872)	(398,872)	-	(398,872)
Transfer from reserve for research and human resource development	-	-	-	-	(8,775)	8,775	-	-	-
Transfer to unconditional reserve	-	-	-	-	547,486	(547,486)	-	-	-
Acquisition of non-controlling interests	-	(23,066)	-	-	-	-	(23,066)	(16,555)	(39,621)
Total transactions with owners	-	(23,066)	-	-	538,711	(937,583)	(421,938)	(16,555)	(438,493)
Balance at June 30, 2017	$ 837,978	(26,075)	(287,958)	450,839	4,328,239	922,902	6,225,925	50,611	6,276,536

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Changes in Equity, Continued
(Unaudited)

For the six-month period ended June 30, 2016

In millions of won	*Ordinary shares*	*Other capital surplus*	*Treasury shares*	*Gain on reissuance of treasury shares*	*Reserve*	*Retained earnings*	*Owners of the parent*	*Non-controlling interests*	*Total equity*
Balance at January 1, 2016	₩ 954,959	(9,928)	(337,062)	494,648	3,704,315	1,401,975	6,208,907	66,592	6,275,499
Total comprehensive income for the period:									
Profit for the period	-	-	-	-	-	569,334	569,334	974	570,308
Other comprehensive income (loss):									
Remeasurements of net defined benefit liability, net of tax	-	-	-	-	-	(202)	(202)	(1)	(203)
Unrealized net changes in fair value of available-for-sale financial assets, net of tax	-	-	-	-	(5,564)	-	(5,564)	-	(5,564)
Exchange differences on translating foreign operations, net of tax	-	-	-	-	10,731	-	10,731	367	11,098
Total other comprehensive income (loss)	-	-	-	-	5,167	(202)	4,965	366	5,331
Total comprehensive income for the period	-	-	-	-	5,167	569,132	574,299	1,340	575,639
Transactions with owners, recorded directly in equity:									
Dividends	-	-	-	-	-	(428,284)	(428,284)	-	(428,284)
In-kind donation of treasury shares	-	-	5,290	10,543	-	-	15,833	-	15,833
Transfer from reserve for research and human resource development	-	-	-	-	(10,000)	10,000	-	-	-
Transfer to unconditional reserve	-	-	-	-	577,602	(577,602)	-	-	-
Conversion of redeemable convertible preferred shares of subsidiaries	-	(139)	-	-	-	-	(139)	139	-
Others	-	-	-	-	-	-	-	20	20
Total transactions with owners	-	(139)	5,290	10,543	567,602	(995,886)	(412,590)	159	(412,431)
Balance at June 30, 2016	₩ 954,959	(10,067)	(331,772)	505,191	4,277,084	975,221	6,370,616	68,091	6,438,707

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Cash Flows
(Unaudited)

For the six-month periods ended June 30, 2017 and 2016

In millions of won and thousands of U.S. dollars	*Note*	*2017 Korean won*	*2017 U.S. dollars (note 4)*	*2016 Korean won*
Cash flows from operating activities				
Cash generated from operations	*34*	₩ 411,330	$ 360,943	₩ 742,743
Income tax paid		(220,028)	(193,075)	(225,151)
Net cash provided by (used in) operating activities		191,302	167,868	517,592
Cash flows from investing activities	*34*			
Interest received		25,254	22,160	20,953
Investment income received from long-term deposits in MSA Escrow Fund		2,625	2,304	-
Dividends received		12,657	11,106	11,620
Proceeds from sale of property, plant and equipment		1,497	1,313	5,332
Proceeds from sale of intangible assets		1,440	1,264	1,092
Proceeds from sale of investments in associates and joint ventures		-	-	13,095
Proceeds from sale of available-for-sale financial assets		3,462	3,038	-
Collection of loans		8,682	7,618	7,558
Withdrawal of guarantee deposits		14,155	12,421	11,935
Proceeds from sale of non-current assets held for sale		2,145	1,882	5,800
Acquisition of property, plant and equipment		(125,492)	(110,120)	(74,117)
Acquisition of intangible assets		(2,686)	(2,357)	(6,040)
Acquisition of available-for-sale financial assets		(28,570)	(25,070)	-
Acquisition of investments in associates and joint ventures		(46,046)	(40,405)	-
Increase in loans		(690)	(605)	(171)
Payments of guarantee deposits		(19,525)	(17,133)	(19,138)
Payments of long-term deposits in MSA Escrow Fund		(42,829)	(37,582)	(46,228)
Decrease in other financial assets, net		697,494	612,052	167,147
Net cash provided by investing activities		503,573	441,886	98,838
Cash flows from financing activities				
Interest paid		(21,435)	(18,809)	(1,506)
Dividends paid		(460,410)	(404,011)	(428,284)
Payment of share issuance cost		(23)	(20)	(128)
Proceeds from borrowings		230,575	202,330	272,834
Increase in deposits received		8,002	7,022	1,223
Repayment of borrowings		(297,602)	(261,146)	(370,957)
Decrease in deposits received		(2,058)	(1,806)	(1,941)
Net cash used in financing activities		(542,951)	(476,440)	(528,759)
Effect of exchange rate fluctuation on cash held		(3,866)	(3,392)	1,539
Net increase in cash and cash equivalents		148,058	129,922	89,210
Cash and cash equivalents at January 1		850,786	746,565	546,213
Cash and cash equivalents at June 30		₩ 998,844	$ 876,487	₩ 635,423

See accompanying notes to the consolidated interim financial statements.

1. Reporting Entity

(a) Description of the Controlling Company

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

As of June 30, 2017, the Parent Company has three manufacturing plants, including the Shintanjin plant, and 14 local headquarters and 123 branches for the sale of tobacco throughout the country. Also, the Parent Company has the Gimcheon plant for fabrication of leaf tobacco and the Cheonan printing plant for the manufacturing of packaging. The head office of the Parent Company is located at 71, Beotkkot-gil, Daedeok-gu, Daejeon.

Pursuant to the Korean government's privatization program and management reorganization plan, on December 28, 1998, the shareholders approved a plan to split the Parent 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 Parent Company's contribution of the assets and liabilities in the red ginseng business segment into a wholly-owned subsidiary, Korea Ginseng Corporation.

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

The ownership of the Parent Company's issued ordinary shares as of June 30, 2017 is held as follows:

Shareholder	Number of shares	Percentage of ownership
National Pension Service	11,958,664	8.71%
Industrial Bank of Korea	9,510,485	6.93%
Employee Share Ownership Association	2,894,364	2.11%
Treasury shares	11,027,370	8.03%
Others	101,901,614	74.22%
	137,292,497	100.00%

1. Reporting Entity, Continued

(b) Consolidated Subsidiaries

(i) List of consolidated subsidiaries

Next most senior parent	Subsidiary	Principal operation	Percentage of ownership	Reporting date	Location
KT&G Corporation	Korea Ginseng Corporation	Manufacturing and selling ginseng	100.00%	June 30	Korea
	Yungjin Pharm. Co., Ltd.	Manufacturing and selling pharmaceuticals	52.45%	June 30	Korea
	Tae-a Industry Co., Ltd.	Manufacturing tobacco materials	100.00%	June 30	Korea
	KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	Manufacturing and selling tobaccos	99.99%	June 30	Turkey
	Korea Tabacos do Brasil Ltda.	Processing leaf tobaccos	99.99%	June 30	Brazil
	KT&G Pars	Manufacturing and selling tobaccos	99.99%	June 30	Iran
	KT&G Rus L.L.C.	Manufacturing and selling tobaccos	100.00%	June 30	Russia
	KT&G USA Corporation	Selling tobaccos	100.00%	June 30	USA
	Cosmocos Co., Ltd.	Manufacturing and selling cosmetics	98.56%	June 30	Korea
	Renzoluc Pte., Ltd.(*)	Manufacturing and selling tobaccos	100.00%	June 30	Singapore
	KGC Yebon Corporation	Manufacturing and selling medical herbs	100.00%	June 30	Korea
	PT KT&G Indonesia	Manufacturing and selling tobaccos	99.99%	June 30	Indonesia
	SangSang Stay, Inc.	Hotel	100.00%	June 30	Korea
	KT&G Global Rus L.L.C.	Selling tobaccos	100.00%	June 30	Russia
Renzoluc Pte., Ltd.	PT Trisakti Purwosari Makmur	Manufacturing and selling tobaccos	99.99%	June 30	Indonesia
	PT Mandiri Maha Mulia	Manufacturing and selling tobaccos	99.98%	June 30	Indonesia
PT Trisakti Purwosari Makmur	PT Sentosa Ababi Purwosari	Manufacturing and selling tobaccos	100.00%	June 30	Indonesia
	PT Purindo Ilufa	Manufacturing and selling tobaccos	100.00%	June 30	Indonesia
	PT Nusantara Indag Makmur	Selling tobaccos	100.00%	June 30	Indonesia
Korea Ginseng Corporation	KGC Life & Gin Co., Ltd.	Selling ginseng door-to-door	100.00%	June 30	Korea
	Cheong Kwan Jang Taiwan Corporation	Manufacturing and selling ginseng	100.00%	June 30	Taiwan
	Korean Red Ginseng Corp., Inc.	Manufacturing and selling ginseng	100.00%	June 30	USA
	Korea Ginseng (China) Corp.	Manufacturing and selling ginseng	100.00%	June 30	China
	Korea Ginseng Corporation Japan	Manufacturing and selling ginseng	100.00%	June 30	Japan
	PT CKJ INDONESIA	Manufacturing and selling ginseng	99.88%	June 30	Indonesia
	Jilin Hanzheng Ginseng Co., Ltd.	Manufacturing and selling ginseng	100.00%	June 30	China
Cosmocos Co., Ltd.	K&I HK Co., Ltd.	Selling cosmetics	100.00%	June 30	Hong Kong
	K&I China Co., Ltd.	Selling cosmetics	100.00%	June 30	China

(*) The Group's percentage of ownership, shown above, excludes redeemable convertible preferred shares. As of June 30, 2017, the Group's percentage of ownership would be 88.60% if preferred shares are included.

1. Reporting Entity, Continued

(b) Consolidated Subsidiaries, Continued

(i) List of consolidated subsidiaries, Continued

For the six-month period ended June 30, 2017, the Parent Company made a capital contribution in-kind to Cosmocos Co., Ltd. by transferring its interest in K&I HK Co., Ltd. and K&I China Co., Ltd., increasing its ownership from 98.49% to 98.56%.

As the Parent Company acquired additional shares of PT Sentosa Ababi Purwosari, PT Trisakti Purwosari Makmur and PT Mandiri Maha Mulia for the six-month period ended June 30, 2017, its ownership interest increased to 100.00%, 99.99% and 99.98% from 99.24%, 60.17% and 66.47%, respectively.

(ii) Financial information of subsidiaries as of and for the six-month period ended June 30, 2017

In millions of won

Subsidiary		Total assets	Total liabilities	Revenue	Net profit(loss)	Total comprehensive income (loss)
Korea Ginseng Corporation	₩	1,808,571	222,088	596,037	95,362	95,321
Yungjin Pharm. Co., Ltd.		210,676	91,764	94,523	2,510	2,504
Tae-a Industry Co., Ltd.		12,951	1,302	6,798	373	373
KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.		43,191	36,843	1,884	(622)	(1,064)
Korea Tabacos do Brasil Ltda.		2,615	6	-	-	-
KT&G Pars		23,529	53,848	2,802	(4,140)	(4,140)
KT&G Rus L.L.C.		147,227	71,990	18,881	5,389	2,209
KT&G USA Corporation		49,487	31,740	57,495	(1,444)	(2,601)
Cosmocos Co., Ltd.		71,673	20,723	38,453	(8,495)	(8,520)
Renzoluc Pte., Ltd.		139,683	29,817	-	(1,002)	772
KGC Yebon Corporation		60,298	12,244	5,837	811	782
PT KT&G Indonesia		29,708	52,042	21,184	1,852	3,063
SangSang Stay, Inc.		10,449	2,353	7,599	(3,381)	(3,381)
KT&G Global Rus L.L.C.		80,693	78,731	21,687	379	299
PT Trisakti Purwosari Makmur, etc.		127,797	17,403	23,116	1,791	836
PT Mandiri Maha Mulia		44,970	32,058	23,519	5,981	5,618
PT Nusantara Indag Makmur(*)		16,427	13,900	-	-	-
KGC Life & Gin Co., Ltd.		25,815	6,916	24,249	2,312	2,310
Cheong Kwan Jang Taiwan Corporation		9,918	8,159	8,193	542	550
Korean Red Ginseng Corp., Inc.		10,248	7,371	7,489	(226)	(1,432)
Korea Ginseng (China) Corp.		30,734	17,041	14,065	(1,284)	(1,783)
Korea Ginseng Corporation Japan		5,499	4,145	6,678	111	88
PT CKJ INDONESIA		992	1,073	-	-	4
Jilin Hanzheng Ginseng Co., Ltd.		68,378	6,960	2,494	(2,724)	(4,838)
K&I HK Co., Ltd.		794	322	621	(74)	(110)
K&I China Co., Ltd.		2,846	880	1,070	(448)	(531)

(*) Since the Group was unable to obtain the financial statements of the acquiree as of the acquisition date, the accounting for the business combination reflected in the accompanying interim consolidated financial statements is based on management's preliminary evaluation. Upon finalization of the accounting treatment, the recorded impacts on the Group's consolidated financial statements may change. In addition, no profit or loss of the acquiree subsequent to the acquisition date has been reflected in the accompanying consolidated interim financial statements as such information was not available.

1. Reporting Entity, Continued

(c) Change in the Consolidation Group

During the six-month period ended June 30, 2017, K-Q HongKong I, Limited was liquidated.

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

For the six-month periods ended June 30, 2017, the Group obtained control of PT Nusantara Indag Makmur, a selling tobacco, by acquiring 100% of shares and voting interests in the company.

2. Basis of Preparation

(a) Statement of Compliance

The consolidated interim financial statements have been prepared in accordance with Korean International Financial Reporting Standards ("K-IFRS") as prescribed in the *Act on External Audits of Corporations*. These consolidated interim financial statements were prepared in accordance with K-IFRS No. 1034 *Interim Financial Reporting* as part of the period covered by the Group's K-IFRS annual consolidated financial statements.

The consolidated interim financial statements were authorized for issue by the Board of Directors on July 27, 2017.

(b) Basis of Measurement

The consolidated interim financial statements have been prepared on the historical cost basis, except for the following material items in the consolidated interim statements of financial position:

- 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

(c) Functional and Presentation Currency

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

(d) Use of Estimates and Judgments

The preparation of the consolidated interim financial statements in conformity with K-IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. In preparing these consolidated interim financial statements, the significant judgments made by management in applying the Group's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the financial statements as of and for the year ended December 31, 2016.

3. Significant Accounting Policies

The significant accounting policies applied by the Group in preparation of its consolidated interim financial statements are included below. The accounting policies set out below have been applied consistently to all periods presented in these consolidated interim financial statements.

(a) Basis of Consolidation

(i) Non-controlling interests

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

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

(ii) Subsidiaries

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

(iii) Loss of control

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

(iv) Interests in equity-accounted investees

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

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

(v) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated. Unrealised gains arising from transactions with equity-accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

3. Significant Accounting Policies, Continued

(b) Joint Arrangements

A joint arrangement is an arrangement of which two or more parties have joint control. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. Joint arrangements are classified into two types - joint operations and joint ventures. A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement (i.e. joint operators) have rights to the assets, and obligations for the liabilities, relating to the arrangement. A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement (i.e. joint ventures) have rights to the net assets of the arrangement.

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

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

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

(c) 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 attribute 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 Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

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

3. Significant Accounting Policies, Continued

(c) Property, Plant and Equipment, Continued

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

	Useful lives (years)		Useful lives (years)
Buildings	10 ~ 60	Vehicles	4 ~ 10
Structures	5 ~ 40	Tools	4 ~ 5
Machinery	5 ~ 20	Furniture and fixtures	2 ~ 5

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

(d) Borrowing Costs

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

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

(e) Government Grants

Government grants are not recognized unless there is reasonable assurance that the Group will comply with the grant's conditions and that the grant will be received. Government grants which are intended to compensate the Group for expenses incurred are recognized as other income in profit or loss over the periods in which the Group recognizes the related costs as expenses.

3. Significant Accounting Policies, Continued

(f) Intangible Assets except for Goodwill

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

The estimated useful lives were as follows:

	Useful lives (years)
Industrial property rights	5 ~ 20 or indefinite
Facility usage rights	indefinite
Other intangible assets	3 ~ 5 or indefinite

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

(g) Investment Property

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

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

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

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

3. Significant Accounting Policies, Continued

(h) 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, the asset (or disposal group) must be available for immediate sale in its present condition and its sale must be highly probable. The assets or disposal group that are classified as non-current assets held for sale are measured at the lower of their carrying amount and fair value less cost to sell.

The Group recognizes an impairment loss for any initial or subsequent write-down of an asset (or 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*.

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).

(i) Inventories

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

The cost of inventories is determined by the weighted-average method for merchandise, finished goods, by-products, work-in-progress and tobacco leaf in raw materials, by the moving-average method for raw materials and supplies; and by the specific identification method for all other inventories.

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

Tobacco leaf inventories which have an operating cycle that exceeds 12 months are classified as current assets, consistent with recognized industry practice. The estimated amounts of inventories in current assets which are not expected to be consumed within 12 months are ₩289,659 million and ₩314,457 million, respectively, as of June 30, 2017 and December 31, 2016.

(j) Impairment of Non-financial Assets

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

3. Significant Accounting Policies, Continued

(j) Impairment of Non-financial Assets, Continued

The Group estimates the recoverable amount of an individual asset. If it is impossible to measure the individual recoverable amount of an asset, then the Group estimates the recoverable amount of cash-generating unit ("CGU"). A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. The value in use is estimated by applying a pre-tax discount rate that reflect current market assessments of the time value of money and the risks specific to the asset or CGU for which estimated future cash flows have not been adjusted, to the estimated future cash flows expected to be generated by the asset or CGU. An impairment loss is recognized if the carrying amount of an asset or a CGU exceeds its recoverable amount. Impairment losses are recognized in profit or loss.

Except for impairment losses in respect of goodwill which are never reversed, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(k) Non-derivative Financial Assets

The Group recognizes and measures non-derivative financial assets by the following four categories: financial assets at fair value through profit or loss, held-to-maturity investments, loans and receivables and available-for-sale financial assets. The Group recognizes financial assets in the statement of financial position when the Group becomes a party to the contractual provisions of the instrument.

Upon initial recognition, non-derivative financial assets are measured at their fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the asset's acquisition or issuance.

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

A financial asset is classified as financial assets are classified at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Upon initial recognition, transaction costs are recognized in profit or loss when incurred. Financial assets at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss.

(ii) Held-to-maturity investments

A non-derivative financial asset with a fixed or determinable payment and fixed maturity, for which the Group has the positive intention and ability to hold to maturity, are classified as held-to-maturity investments. Subsequent to initial recognition, held-to-maturity investments are measured at amortized cost using the effective interest method.

(iii) Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method except for loans and receivables of which the effect of discounting is immaterial.

3. Significant Accounting Policies, Continued

(k) Non-derivative Financial Assets, Continued

(iv) Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified as financial assets at fair value through profit or loss, held-to-maturity investments or loans and receivables. Subsequent to initial recognition, they are measured at fair value, which changes in fair value, net of any tax effect, recorded in other comprehensive income in equity. Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments are measured at cost.

(v) De-recognition of financial assets

The Group derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognized as a separate asset or liability.

If the Group retains substantially all the risks and rewards of ownership of the transferred financial assets, the Group continues to recognize the transferred financial assets and recognizes financial liabilities for the consideration received.

(vi) Offsetting between financial assets and financial liabilities

Financial assets and financial liabilities are offset and the net amount is presented in the statement of financial position only when the Group currently has a legally enforceable right to offset the recognized amounts, and there is the intention to settle on a net basis or to realize the asset and settle the liability simultaneously.

(l) Derivative financial instruments

Derivatives are initially recognized at fair value. Subsequent to initial recognition, derivatives are measured at fair value, and changes in the fair value of derivative financial instruments are recognized immediately in profit or loss.

Embedded derivatives are separated from the host contract and accounted for separately only if the following criteria have been met:

- The economic characteristics and risks of the embedded derivative are not closely related to those of the host contract;
- A separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and
- The hybrid instrument is not measured at fair value with changes in fair value recognized in profit or loss.

3. Significant Accounting Policies, Continued

(m) Impairment of Financial Assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably. However, losses expected as a result of future events, regardless of likelihood, are not recognized.

If financial assets have objective evidence that they are impaired, impairment losses should be measured and recognized.

(i) Financial assets measured at amortized cost

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of its estimated future cash flows discounted at the asset's original effective interest rate. If it is not practicable to obtain the instrument's estimated future cash flows, impairment losses would be measured by using prices from any observable current market transactions. The Group can recognize impairment losses directly or establish a provision to cover impairment losses. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed either directly or by adjusting an allowance account.

(ii) Financial assets carried at cost

If there is objective evidence that an impairment loss has occurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses are not reversed.

(iii) Available-for-sale financial assets

When a decline in the fair value of an available-for-sale financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized in other comprehensive income is reclassified from other comprehensive income to profit or loss as a reclassification adjustment even though the financial asset has not been derecognized. Impairment losses recognized in profit or loss for an investment in an equity instrument classified as available-for-sale are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed, with the amount of the reversal recognized in profit or loss. For an investment in an equity security, objective evidence of impairment includes a significant or prolonged decline in its fair value below its cost. The Group considers a decline of 20% to be significant and a period of nine months to be prolonged.

3. Significant Accounting Policies, Continued

(n) Cash and Cash Equivalents

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

(o) Non-derivative Financial Liabilities

The Group classifies non-derivative financial liabilities into financial liabilities at fair value through profit or loss, financial guarantee liabilities and other financial liabilities in accordance with the substance of the contractual arrangement and the definitions of financial liabilities. The Group recognizes financial liabilities in the statement of financial position when the Group becomes a party to the contractual provisions of the financial liability.

(i) Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading or designated as such upon initial recognition. Subsequent to initial recognition, financial liabilities at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss. Upon initial recognition, transaction costs that are directly attributable to the acquisition are recognized in profit or loss as incurred.

(ii) Financial guarantee liabilities

Financial guarantee liability is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified term of a debt instrument. Upon initial recognition, financial guarantee liabilities are measured at their fair value plus, transaction costs that are directly attributable to the acquisition or issue of the financial guarantee liability.

After initial recognition, an issuer of such a contract measures it at the higher of the amount determined in accordance with K-IFRS No. 1037 *Provisions, Contingent Liabilities and Contingent Assets* and the amount initially recognized less, when appropriate, cumulative amortisation recognized in accordance with K-IFRS No. 1018 *Revenue.*

(iii) Other financial liabilities

Non-derivative financial liabilities other than financial liabilities at fair value through profit or loss or financial guarantee liabilities are classified as other financial liabilities. At the date of initial recognition, other financial liabilities are measured at fair value minus transaction costs that are directly attributable to the acquisition. Subsequent to initial recognition, other financial liabilities are measured at amortized cost using the effective interest method.

The Group derecognizes a financial liability from the statement of financial position when it is extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

3. Significant Accounting Policies, Continued

(p) Employee Benefits

(i) Short-term employee benefits

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

(ii) Retirement benefits: defined contribution plans

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

(iii) Retirement benefits: defined benefit plans

The calculation of defined benefit obligations is performed annually by a qualified actuary using the projected unit credit method. When the calculation results in a potential asset for the Group, the recognized asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. To calculate the present value of economic benefits, consideration is given to any applicable minimum funding requirements.

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognized immediately in other comprehensive income. The Group determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to defined benefit plans are recognized in profit or loss.

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

(iv) Termination benefits

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

3. Significant Accounting Policies, Continued

(q) Provisions

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

The risks and uncertainties that inevitably surround many events and circumstances are taken into account in reaching the best estimate of a provision. Where the effect of the time value of money is material, provisions are determined at the present value of the expected future cash flows.

Where some or all of the expenditures required to settle a provision are expected to be reimbursed by another party, the reimbursement shall be recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The reimbursement shall be treated as a separate asset.

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

(r) Equity Capital

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

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

(s) Revenue Recognition

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

Revenue from sale of goods is measured at the fair value of the consideration received or receivable, net of tobacco excise and other taxes, trade discounts and volume rebates. Revenue from the sale of goods is recognized when the Group has transferred to the buyer the significant risks and rewards of ownership of the goods, the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group and the costs incurred or to be incurred in respect of the transaction can be measured reliably. Tobacco excise and other taxes deducted from revenue for the six-month periods ended June 30, 2017 and 2016 were ₩3,103,837 million and ₩3,135,929 million, respectively.

3. Significant Accounting Policies, Continued

(s) Revenue Recognition, Continued

Revenue from the construction of real estate includes the initial amount agreed in the contract plus any variations in contract work, claims and incentive payments, to the extent that it is probable that they will result in revenue and can be measured reliably. As soon as the outcome of a construction contract can be estimated reliably, contract revenue is recognized in profit or loss in proportion to the stage of completion of the contract. The stage of completions is assessed by reference to surveys of work performed. Meanwhile, profits from an apartment house for self-instalment sales is recognized on percentage-of-completion method according to Q&A of Korea Accounting Institute, namely 2011-I-KQA. This accounting treatment is valid only under the K-IFRS as stated in subclause1 of clause 1, Article 13 of *the Act on External Audit of Stock* companies.

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

Rental income from investment property, net of lease incentives granted, is recognized in profit or loss on a straight-line basis over the term of the lease.

(t) Finance Income and Finance Costs

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

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

(u) Income Taxes

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

(i) Current tax

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

3. Significant Accounting Policies, Continued

(u) Income Taxes, Continued

(ii) Deferred tax

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

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

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

Deferred tax assets and liabilities are offset only if there is a legally enforceable right to offset the related current tax liabilities and assets, and 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.

(v) Foreign Currencies

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of the Group at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated to the functional currency using the reporting date's exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that 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, which are recognized in other comprehensive income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

(ii) Foreign operations

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

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

3. Significant Accounting Policies, Continued

(v) Foreign Currencies, Continued

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

When a foreign operation is disposed of, the relevant amount in the translation is transferred to profit or loss as part of the profit or loss on disposal.

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

(w) Earnings per Share

The Group presents basic and diluted earnings per share ("EPS") data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Group 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.

(x) New Standards and Interpretations Not Yet Adopted

The following new standards are effective for annual periods beginning on or after January 1, 2018 and earlier application is permitted; however, the Group has not early adopted the following new standards in preparing these consolidated financial statements.

K-IFRS No. 1109 *Financial Instruments*
K-IFRS 1109 is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. It replaces the existing guidance in K-IFRS No. 1039 *Financial Instruments: Recognition and Measurement*. K-IFRS 1109 includes revised guidance on the classification and measurement of financial instruments, a new expected credit loss model for calculating impairment on financial assets, and new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from K-IFRS No. 1039.

3. Significant Accounting Policies, Continued

(x) New Standards and Interpretations Not Yet Adopted, Continued

K-IFRS No. 1115 *Revenue from Contracts with Customers*
K-IFRS 1115 is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. It replaces existing revenue recognition guidance, including K-IFRS No. 1018 *Revenue*, K-IFRS No. 1011 *Construction Contracts,* K-IFRS No. 2031 *Revenue—Barter Transactions Involving Advertising Services*, K-IFRS No. 2113 *Customer Loyalty Programmes,* K-IFRS No. 2115 *Agreements for the Construction of Real Estate* and K-IFRS No. 2118 *Transfers of Assets from Customers*. K-IFRS 1115 establishes a comprehensive framework for determining whether, how much and when revenue is recognized.

The Group currently plans to apply K-IFRS No. 1109 and K-IFRS No. 1115 initially on January 1, 2018. The actual impact of adopting those new standards will be dependent on the financial instruments that the Group holds and economic conditions at that time as well as accounting elections and judgements that it will make in the future. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of those new standards and expects to disclose additional quantitative information before it adopts them.

4. Convenience Translation

The consolidated financial statements are presented in Korean won and have been translated into U.S. dollars at the rate of ₩1,139.60 to $1, the basic exchange rate on June 30, 2017 posted by Seoul Money Brokerage Services, solely for the convenience of the reader. This translation does not comply with K-IFRS and should not be construed as a representation that any or all of the amounts shown could be converted into U.S. dollars at this or any other rate.

5. Operating Segments

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

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

5. Operating Segments, Continued

(b) Segment information on sales and operating profit for the six-month period ended June 30, 2017 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Sales:								
Total segment sales	₩	1,528,350	631,337	99,318	252,916	2,511,921	(171,475)	2,340,446
Less: Inter-segment sales		92,996	36,542	6,598	35,339	171,475	(171,475)	-
External sales	₩	1,435,354	594,795	92,720	217,577	2,340,446	-	2,340,446
Segment profit:								
Operating profit	₩	640,579	112,711	19,735	14,384	787,409	(5,496)	781,913

(c) Segment information on sales and operating profit for the six-month period ended June 30, 2016 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Sales:								
Total segment sales	₩	1,436,508	576,612	74,707	224,235	2,312,062	(132,622)	2,179,440
Less: Inter-segment sales		77,490	24,224	3,909	26,999	132,622	(132,622)	-
External sales	₩	1,359,018	552,388	70,798	197,236	2,179,440	-	2,179,440
Segment profit:								
Operating profit	₩	613,656	97,388	17,192	18,472	746,708	(7,889)	738,819

(d) Segment information on assets and liabilities as of June 30, 2017 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Assets:								
Segment assets	₩	4,975,105	1,783,066	267,242	279,097	7,304,510	(336,852)	6,967,658
Investments in associates and joint ventures		-	-	56,792	3,224	60,016	-	60,016
Non-current assets held for sale		-	5,150	21,165	-	26,315	-	26,315
		4,975,105	1,788,216	345,199	282,321	7,390,841	(336,852)	7,053,989
Unallocated assets								2,109,981
Total assets	₩							9,163,970
Acquisition of non-current assets	₩	104,820	18,209	-	6,311	129,340	-	129,340
Liabilities:								
Segment liabilities	₩	1,382,525	156,216	-	89,367	1,628,108	(117,692)	1,510,416
Unallocated liabilities								500,814
Total liabilities	₩							2,011,230

5. Operating Segments, Continued

(e) Segment information on assets and liabilities as of December 31, 2016 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Assets:								
Segment assets	₩	3,993,355	1,847,372	296,699	286,075	6,423,501	(247,874)	6,175,627
Investments in associates and joint ventures		-	-	53,475	3,001	56,476	-	56,476
Non-current assets held for sale		-	5,150	21,165	-	26,315	-	26,315
		3,993,355	1,852,522	371,339	289,076	6,506,292	(247,874)	6,258,418
Unallocated assets								3,554,167
Total assets	₩							9,812,585
Acquisition of non-current assets	₩	130,104	32,727	-	14,109	176,940	(5,973)	170,967
Liabilities:								
Segment liabilities	₩	1,875,081	167,383	-	96,254	2,138,718	(216,457)	1,922,261
Unallocated liabilities								772,067
Total liabilities	₩							2,694,328

(f) Revenues from major customers which amount to more than 10 percent of the Group's consolidated total revenues for the six-month periods ended June 30, 2017 and 2016 were as follows:

In millions of won		2017	2016
Alokozay International Limited	₩	260,162	242,404

6. Property, Plant and Equipment

(a) Details of property, plant and equipment as of June 30, 2017 and December 31, 2016 are summarized as follows:

			June 30 2017			December 31 2016	
In millions of won		Cost	Accumulated depreciation and impairment	Carrying amount	Cost	Accumulated depreciation and impairment	Carrying amount
Land	₩	578,528	-	578,528	541,980	-	541,980
Buildings		991,434	(440,431)	551,003	962,633	(423,925)	538,708
Structures		73,029	(43,603)	29,426	72,551	(42,153)	30,398
Machinery		1,338,157	(1,026,659)	311,498	1,324,784	(998,291)	326,493
Vehicles		12,117	(9,134)	2,983	11,771	(9,356)	2,415
Tools		68,659	(58,103)	10,556	67,597	(56,227)	11,370
Furniture and fixtures		252,650	(192,041)	60,609	241,915	(179,217)	62,698
Others		2,350	-	2,350	1,907	-	1,907
Construction-in-progress		99,937	-	99,937	85,908	-	85,908
	₩	3,416,861	(1,769,971)	1,646,890	3,311,046	(1,709,169)	1,601,877

(b) Changes in property, plant and equipment for the six-month period ended June 30, 2017 were as follows:

In millions of won		January 1 2017	Acquisition	Disposal	Depreciation	Transfer of Construction -in-progress	Net exchange difference and others	Business Combination	June 30 2017
Land	₩	541,980	3	(136)	-	37,247	(566)	-	578,528
Buildings		538,708	2,113	(449)	(18,059)	31,336	(2,646)	-	551,003
Structures		30,398	580	(149)	(1,648)	339	(94)	-	29,426
Machinery		326,493	4,711	(798)	(34,384)	16,363	(887)	-	311,498
Vehicles		2,415	644	(29)	(447)	417	(17)	-	2,983
Tools		11,370	1,664	(28)	(2,496)	77	(31)	-	10,556
Furniture and fixtures		62,698	11,263	(70)	(13,705)	448	(25)	-	60,609
Others		1,907	23	-	-	-	-	420	2,350
Construction-in-progress		85,908	100,351	-	-	(86,227)	(95)	-	99,937
	₩	1,601,877	121,352	(1,659)	(70,739)	-	(4,361)	420	1,646,890

For the six-month period ended June 30, 2017, land, buildings and structures with a carrying amount of ₩1,325 million were transferred to investment property.

The Group was unable to finalise the initial accounting for business combination related to PT Nusantara Indag Makmur (see note 35), therefore, the above amount is provisional. The amount regarding the accounting for business combination might be adjusted during the measurement period.

6. Property, Plant and Equipment, Continued

(c) Changes in property, plant and equipment for the year ended December 31, 2016 were as follows:

In millions of won		January 1 2016	Acquisition	Disposal	Depreciation	Transfer of construction -in-progress	Net exchange difference and others	December 31 2016
Land	₩	583,481	300	(2,633)	-	62,207	(101,375)	541,980
Buildings		574,174	3,933	(1,423)	(37,014)	101,215	(102,177)	538,708
Structures		33,179	1,020	(809)	(3,416)	745	(321)	30,398
Machinery		344,965	7,585	(994)	(72,810)	47,264	483	326,493
Vehicles		2,335	621	(425)	(747)	554	77	2,415
Tools		10,803	4,569	(26)	(4,789)	823	(10)	11,370
Furniture and fixtures		49,437	32,839	(1,468)	(24,523)	6,398	15	62,698
Others		1,508	93	-	-	306	-	1,907
Construction-in-progress		189,897	112,438	-	-	(219,512)	3,085	85,908
	₩	1,789,779	163,398	(7,778)	(143,299)	-	(200,223)	1,601,877

For the year ended December 31, 2016, the Group received ₩3,777 million of government grant related with acquisition of buildings, furniture and fixtures and machinery.

For the year ended December 31, 2016, land, buildings and structures with a carrying amount of ₩207,255 million were transferred to investment property and construction-in-progress with a carrying amount of ₩137 million were transferred to intangible assets.

7. Intangible Assets

(a) Details of intangible assets as of June 30, 2017 and December 31, 2016 are summarized as follows:

				June 30 2017			December 31 2016
In millions of won		Cost	Accumulated amortization and impairment	Carrying amount	Cost	Accumulated amortization and impairment	Carrying amount
Goodwill	₩	88,368	(72,841)	15,527	87,902	(72,841)	15,061
Industrial property rights		50,443	(38,146)	12,297	47,759	(36,078)	11,681
Facility usage rights		33,660	(1,709)	31,951	35,080	(2,731)	32,349
Other intangible assets		115,318	(75,582)	39,736	115,256	(73,508)	41,748
Intangible assets under development		5,075	(1,910)	3,165	6,460	(2,370)	4,090
	₩	292,864	(190,188)	102,676	292,457	(187,528)	104,929

7. Intangible Assets, Continued

(b) Changes in intangible assets for the six-month period ended June 30, 2017 were as follows:

In millions of won		January 1 2017	Acquisition	Disposal	Amortization	Transfer	Net exchange difference and others	Business Combination	June 30 2017
Goodwill	₩	15,061	-	-	-	-	-	466	15,527
Industrial property rights		11,681	397	-	(382)	602	(1)	-	12,297
Facility usage rights		32,349	519	(917)	-	-	-	-	31,951
Other intangible assets		41,748	481	-	(2,235)	25	(283)	-	39,736
Intangible assets under development		4,090	60	(385)	-	(602)	2	-	3,165
	₩	104,929	1,457	(1,302)	(2,617)	25	(282)	466	102,676

The Group was unable to finalise the initial accounting for business combination related to PT Nusantara Indag Makmur (see note 35), therefore, the above amount is provisional. The amount regarding the accounting for business combination might be adjusted during the measurement period.

(c) Changes in intangible assets for the year ended December 31, 2016 were as follows:

In millions of won		January 1 2016	Acquisition	Disposal	Transfer of intangible assets under development	Amortization	Impairment	Net exchange difference and others	December 31, 2016
Goodwill	₩	15,061	-	-	-	-	-	-	15,061
Industrial property rights		14,791	1,961	(30)	5	(1,148)	(3,898)	-	11,681
Facility usage rights		25,551	8,280	(1,518)	36	-	-	-	32,349
Other intangible assets		46,199	326	-	101	(4,743)	-	(135)	41,748
Intangible assets under development		3,826	284	-	(5)	-	(15)	-	4,090
	₩	105,428	10,851	(1,548)	137	(5,891)	(3,913)	(135)	104,929

For the year ended December 31, 2016, the Group recognized ₩3,913 million of impairment losses on industrial property rights and intangible assets under development since the carrying amounts exceeded their recoverable amounts.

(d) Research and development expenditures not capitalized for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

In millions of won		2017 Three-month	2017 Six-month	2016 Three-month	2016 Six-month
Cost of sales	₩	627	1,082	220	553
Selling, general and administrative expenses		10,288	17,908	7,365	14,624
	₩	10,915	18,990	7,585	15,177

8. Investment Property

(a) Details of investment property as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won		June 30 2017			December 31 2016		
		Cost	Accumulated depreciation and impairment	Carrying amount	Cost	Accumulated depreciation and impairment	Carrying amount
Land	₩	130,052	-	130,052	129,655	-	129,655
Buildings		283,570	(76,163)	207,407	282,357	(70,432)	211,925
	₩	413,622	(76,163)	337,459	412,012	(70,432)	341,580

(b) Changes in investment property for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017 Land	Buildings	Total	2016 Land	Buildings	Total
Beginning balance	₩	129,655	211,925	341,580	49,123	115,366	164,489
Depreciation		-	(5,446)	(5,446)	-	(8,999)	(8,999)
Transfer from property, plant and equipment		397	928	1,325	101,697	105,558	207,255
Transfer to non-current assets held for sale		-	-	-	(21,165)	-	(21,165)
Ending balance	₩	130,052	207,407	337,459	129,655	211,925	341,580

(c) The amounts recognized in profit or loss from investment property for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

In millions of won		2017 Three-month	Six-month	2016 Three-month	Six-month
Rental income	₩	11,362	22,432	8,426	17,580
Direct operating expense		(2,696)	(5,446)	(2,224)	(3,839)
	₩	8,666	16,986	6,202	13,741

(d) The carrying amount and the fair value of investment property as of June 30, 2017 and December 31, 2016 were as follows:

In millions of won		June 30 2017		December 31 2016	
		Fair value	Carrying amount	Fair value	Carrying amount
Land	₩	594,810	130,052	539,689	129,655
Buildings		257,386	207,407	232,806	211,925
	₩	852,196	337,459	772,495	341,580

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

9. Investments in Associates and Joint Ventures

(a) Investments in associates and joint ventures as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won, except percentage of ownership

Company	Location	Principal operation	2017 Percentage of owner ship	2017 Carrying amount	2016 Percentage of owner ship	2016 Carrying amount
Lite Pharm Tech, Inc.	Korea	Manufacturing medical supplies	20.24%	₩ 3,224	20.24%	₩ 3,001
KVG REIT 1 Co., Ltd. (*1)	Korea	Renting of real estate	29.67%	9,001	29.67%	6,426
JR REIT V Co., Ltd.	Korea	Renting of real estate	34.63%	5,386	34.63%	5,420
JR REIT VIII Co., Ltd.	Korea	Renting of real estate	21.74%	9,382	21.74%	9,555
LSK Global Pharma Services Co., Ltd.	Korea	Researching and developing medicine	23.15%	-	23.15%	-
JR REIT X Co., Ltd.	Korea	Renting of real estate	28.79%	8,591	28.79%	8,697
JR REIT XIII Co., Ltd.	Korea	Renting of real estate	27.03%	4,761	27.03%	4,742
KB Gimpo Logistics CR REIT Co., Ltd.(*2)	Korea	Renting of real estate	12.00%	3,106	12.00%	2,943
KORAMCO Private REIT 50 Fund(*3)	Korea	Renting of real estate	84.21%	16,565	84.21%	15,692
				₩ 60,016		₩ 56,476

(*1) During May 2017, KVG REIT 1 Co., Ltd. completed its sale of underlying assets and was preparing for liquidation. The Group used financial statements of KVG REIT 1 Co., Ltd. as of May 31, 2017 in preparing these consolidated interim financial statements.

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

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

In 2016, the Group made an investment of ₩3,000 million and ₩16,000 million in KB Gimpo Logistics CR REIT Co., Ltd and KORAMCO Private REIT 50 Fund, respectively.

In 2016, the Group received ₩13,095 million of dividend related to liquidation of KOCREF REIT 17 Co., Ltd.

9. Investments in Associates and Joint Ventures, Continued

(b) Financial information of associates and joint ventures accounted for using the equity method as of and for the six-month period ended June 30, 2017 are summarized as follows:

(i) Summarized information

In millions of won

Company		Total assets	Total liabilities	Revenue	Total comprehensive income
Lite Pharm Tech, Inc.	₩	22,129	6,200	5,833	426
KVG REIT 1 Co., Ltd.		34,980	4,642	2,781	10,044
JR REIT V Co., Ltd.		31,261	15,707	1,325	848
JR REIT VIII Co., Ltd.		107,496	64,341	3,723	1,284
LSK Global Pharma Services Co., Ltd.		5,970	10,104	9,083	(2,309)
JR REIT X Co., Ltd.		85,741	55,902	2,167	373
JR REIT XIII Co., Ltd.		47,276	29,661	894	88
KB Gimpo Logistics CR REIT Co., Ltd.		63,467	37,585	2,150	812
KORAMCO Private REIT 50 Fund		48,235	28,565	1,634	617

(ii) Additional information about joint ventures

In millions of won

Company		Cash and cash equivalents	Current financial liabilities	Non-current financial liabilities	Depreciation	Amortization	Interest income	Interest costs	Income tax expense
KB Gimpo Logistics CR REIT Co., Ltd.	₩	1,704	34,204	3,381	461	-	-	556	-
KORAMCO Private REIT 50 Fund		1,295	25,995	2,570	350	-	-	423	-

9. Investments in Associates and Joint Ventures, Continued

(c) Financial information of associates and joint ventures accounted for using the equity method as of and for the year ended December 31, 2016 are summarized as follows:

(i) Summarized information

In millions of won

Company		Total assets	Total liabilities	Revenue	Total comprehensive income
Lite Pharm Tech, Inc.	₩	21,629	6,804	11,001	1,272
KVG REIT 1 Co., Ltd.		49,567	27,907	5,995	1,702
JR REIT V Co., Ltd.		30,837	15,187	2,588	1,422
JR REIT VIII Co., Ltd.		106,992	63,040	7,612	3,391
LSK Global Pharma Services Co., Ltd.		12,427	13,592	20,090	326
JR REIT X Co., Ltd.		86,237	56,027	4,328	812
JR REIT XIII Co., Ltd.		47,318	29,776	1,434	(145)
KB Gimpo Logistics CR REIT Co., Ltd.		64,116	39,597	359	129
KORAMCO Private REIT 50 Fund		48,728	30,094	273	98

(ii) Additional information about joint ventures

In millions of won

Company		Cash and cash equivalents	Current financial liabilities	Non-current financial liabilities	Depreciation	Amortization	Interest income	Interest costs	Income tax expense
KB Gimpo Logistics CR REIT Co., Ltd.	₩	1,258	36,010	3,481	77	-	102	102	-
KORAMCO Private REIT 50 Fund		956	27,367	2,646	58	-	78	78	-

9. Investments in Associates and Joint Ventures, Continued

(d) Changes in investments in associates and joint ventures for the six-month period ended June 30, 2017 were as follows:

In millions of won

Company		January 1 2017	Acquisition	Share of gain (loss)	Dividends	June 30 2017
Lite Pharm Tech, Inc.	₩	3,001	-	223	-	3,224
KVG REIT 1 Co., Ltd.		6,426	-	2,950	(375)	9,001
JR REIT V Co., Ltd.		5,420	-	461	(495)	5,386
JR REIT VIII Co., Ltd.		9,555	-	284	(457)	9,382
JR REIT X Co., Ltd.		8,697	-	146	(252)	8,591
JR REIT XIII Co., Ltd.		4,742	-	20	-	4,762
KB Gimpo Logistics CR REIT Co., Ltd.		2,943	-	164	-	3,107
KORAMCO Private REIT 50 Fund		15,692	-	871	-	16,563
	₩	56,476	-	5,119	(1,579)	60,016

(e) Changes in investments in associates and joint ventures for the year ended December 31, 2016 were as follows:

In millions of won

Company		January 1 2016	Acquisition	Disposal	Share of gain (loss)	Dividends	December 31 2016
Lite Pharm Tech, Inc.	₩	2,720	-	-	281	-	3,001
KVG REIT 1 Co., Ltd.		6,635	-	-	526	(735)	6,426
KOCREF REIT 17 Co., Ltd.		13,208	-	(13,095)	(113)	-	-
JR REIT V Co., Ltd.		5,470	-	-	741	(791)	5,420
JR REIT VIII Co., Ltd.		9,693	-	-	733	(871)	9,555
LSK Global Pharma Services Co., Ltd.		-	-	-	-	-	-
JR REIT X Co., Ltd.		8,907	-	-	265	(475)	8,697
JR REIT XIII Co., Ltd.		4,888	-	-	(1)	(145)	4,742
KB Gimpo Logistics CR REIT Co., Ltd.		-	3,000	-	(57)	-	2,943
KORAMCO Private REIT 50 Fund		-	16,000	-	(308)	-	15,692
	₩	51,521	19,000	(13,095)	2,067	(3,017)	56,476

9. Investments in Associates and Joint Ventures, Continued

(f) Reconciliation of the summarized financial information presented to the carrying amount of the Group's interest in the associate and joint ventures as of June 30, 2017 are summarized as follows:

In millions of won, except percent of ownership

Company	Percentage of ownership		Equity attributable to owners of the parent	Share of net assets	Share of loss not recognized	Carrying amount
Lite Pharm Tech, Inc.	20.24%	₩	15,929	3,224	-	3,224
KVG REIT 1 Co., Ltd.	29.67%		30,338	9,001	-	9,001
JR REIT V Co., Ltd.	34.63%		15,554	5,386	-	5,386
JR REIT VIII Co., Ltd.	21.74%		43,155	9,382	-	9,382
LSK Global Pharma Services Co., Ltd.	23.15%		(4,134)	(957)	957	-
JR REIT X Co., Ltd.	28.79%		29,839	8,591	-	8,591
JR REIT XIII Co., Ltd.	27.03%		17,615	4,761	-	4,761
KB Gimpo Logistics CR REIT Co., Ltd.	12.00%		25,882	3,106	-	3,106
KORAMCO Private REIT 50 Fund	84.21%		19,670	16,565	-	16,565
		₩				60,016

(g) Reconciliation of the summarized financial information presented to the carrying amount of the Group's interest in the associate and joint ventures as of December 31, 2016 are summarized as follows:

In millions of won

Company	Percentage of ownership		Equity attributable to owners of the parent	Share of net assets	Share of loss not recognized	Carrying amount
Lite Pharm Tech, Inc.	20.24%	₩	14,825	3,001	-	3,001
KVG REIT 1 Co., Ltd.	29.67%		21,660	6,426	-	6,426
JR REIT V Co., Ltd.	34.63%		15,650	5,420	-	5,420
JR REIT VIII Co., Ltd.	21.74%		43,952	9,555	-	9,555
LSK Global Pharma Services Co., Ltd.	23.15%		(1,165)	(270)	270	-
JR REIT X Co., Ltd.	28.79%		30,210	8,697	-	8,697
JR REIT XIII Co., Ltd.	27.03%		17,542	4,742	-	4,742
KB Gimpo Logistics CR REIT Co., Ltd.	12.00%		24,519	2,943	-	2,943
KORAMCO Private REIT 50 Fund	84.21%		18,634	15,692	-	15,692
		₩				56,476

10. Available-for-sale Financial Assets

(a) Changes in available-for-sale financial assets for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017	2016
Beginning balance	₩	386,596	364,681
Acquisitions		28,570	31,000
Net changes in fair value		23,438	25,013
Reclassification		(2,054)	-
Disposals and exercise of convertible right		(12,031)	(34,098)
Ending balance	₩	424,519	386,596
Statements of financial position:			
Current	₩	-	1,500
Non-current		424,519	385,096
	₩	424,519	386,596

For the six-month period ended June 30, 2017, the Group reclassified ₩2,054 million of investment in the debt security of LSK Global Pharma Services Co., Ltd., whose maturity has been expired, to loans. The Group recognized ₩554 million of gain on sale of available-for-sale financial assets difference between the fair value and the carrying amount of the investment.

For the six-month period ended June 30, 2017, the Group recognized ₩460 million of gain on sale of available-for-sale financial assets.

For the six-month period ended June 30, 2017, the Group recognized ₩14,640 million of impairment loss on its investment in an equity instrument of U&I Corporation as there was a significant and prolonged decline in the fair value below below its cost.

For the year ended December 31, 2016, the Group recognized ₩13,988 million of gain on sale of available-for-sale financial assets upon liquidation of Mastern 2 REIT Co., Ltd.

For the year ended December 31, 2016, the Group recognized ₩4,067 million of impairment loss on its investment in an equity instrument of Rexahn Pharmaceuticals, Inc. as there was a significant and prolonged decline in the fair value below its cost.

10. Available-for-sale Financial Assets, Continued

(b) Available-for-sale financial assets as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won		June 30 2017	December 31 2016
Available-for-sale debt instruments:			
Corporate bonds	₩	-	1,500
Total available-for-sale debt instruments		-	1,500
Available-for-sale equity instruments:			
Listed			
– YTN Co., Ltd.		20,950	20,782
– Oscotech, Inc.		4,266	3,775
– Shinhan Financial Group Co., Ltd.		197,612	181,378
– Rexahn Pharmaceuticals, Inc.		2,083	1,081
– U&I Corporation		14,350	14,060
		239,261	221,076
Unlisted		185,258	164,020
Total available-for-sale equity instruments		424,519	385,096
Total available-for-sale financial assets	₩	424,519	386,596

The fair value of listed available-for-sale equity instruments is principally based on quoted prices in an active market.

As of June 30, 2017 and December 31, 2016, ₩37,659 million and ₩32,564 million of available-for-sale financial assets that do not have a market price in an active market and whose fair value cannot be reliably measured are measured at cost, respectively.

11. Long-term Deposits in MSA Escrow Fund

Long-term deposits in MSA Escrow Fund as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won		June 30 2017	December 31 2016
Demand deposits	₩	28,069	-
MMF		-	56,069
Treasury bill		-	21,559
Treasury note		490,516	425,964
	₩	518,585	503,592

As discussed in note 33 to the consolidated interim financial statements, long-term deposits in MSA Escrow Fund are deposited to the United States government related to the export of tobacco to the United States.

For the six-month periods ended June 30, 2017 and 2016, ₩42,829 million and ₩46,228 million were paid into long-term deposits in MSA Escrow Fund, respectively.

Long-term deposits in MSA Escrow Fund are invested in demand deposits of financial institutions or government and public bonds. Investment income on long-term deposits in MSA Escrow Fund for the six-month periods ended June 30, 2017 and 2016 are ₩4,067 million and ₩4,089 million, respectively.

12. Trade and Other Receivables

(a) Trade and other receivables as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won		June 30 2017 Current	June 30 2017 Non-current	December 31 2016 Current	December 31 2016 Non-current
Loans to employees	₩	16,157	32,510	16,745	38,984
Loans		1,585	982	652	325
Other receivables		25,101	125	108,706	240
Guarantee deposits		45,690	26,757	36,883	30,393
Accrued income		2,177	-	7,215	-
Trade receivables		1,207,620	-	1,113,446	-
	₩	1,298,330	60,374	1,283,647	69,942

(b) Trade and other receivables as of June 30, 2017 and December 31, 2016 have been reported in the consolidated statements of financial position net of allowances as follows:

In millions of won		June 30 2017 Current	June 30 2017 Non-current	December 31 2016 Current	December 31 2016 Non-current
Gross trade and other receivables	₩	1,329,809	60,374	1,315,237	69,942
Allowance:					
Loans		(197)	-	(197)	-
Other receivables		(2,353)	-	(2,345)	-
Trade receivables		(28,929)	-	(29,048)	-
		(31,479)	-	(31,590)	-
Net trade and other receivables	₩	1,298,330	60,374	1,283,647	69,942

(c) Changes in the allowance account for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017	2016
Beginning balance	₩	31,590	33,242
Impairment loss		230	2,858
Reversal of impairment loss		(71)	(3)
Net exchange difference and others		(270)	(4,507)
Ending balance	₩	31,479	31,590

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

12. Trade and Other Receivables, Continued

(d) The aging schedule of trade and other receivables which were past due but not impaired as of June 30, 2017 and December 31, 2016 is as follows:

In millions of won		June 30 2017	December 31 2016
Within 1 month	₩	116,961	77,420
Between 1 and 2 months		64,159	78,179
Beyond 2 months		160,318	212,286
	₩	341,438	367,885

There is no significant concentration of credit risk with respect to trade and other receivables since trade and other receivables, excluding export trade receivables, are widely dispersed amongst a number of customers. The Group holds pledged assets and guarantees in respect of some of the past due debtor balances.

(e) Details of trade and other receivables that are measured at amortized cost as of June 30, 2017 and December 31, 2016 were as follows:

In millions of won, except percentage of interest rate	June 30 2017			December 31 2016		
	Effective interest rate	Current	Non-current	Effective interest rate	Current	Non-current
Loans to employees	1.89~5.68%	16,157	32,510	1.89~5.68%	16,745	38,984
Loans	1.93~2.71%	330	232	1.93~2.71%	330	325
Guarantee deposits	1.30~5.68%	44,290	24,907	1.30~5.68%	35,917	28,301
		60,777	57,649		52,992	67,610

13. Inventories

(a) Inventories as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won		June 30 2017	December 31 2016
Merchandise, net of loss on the write-down of inventories	₩	20,672	16,666
Finished goods, net of loss on the write-down of inventories		743,846	686,950
Work-in-progress, net of loss on the write-down of inventories		436,854	627,863
Raw materials, net of loss on the write-down of inventories		771,475	825,315
Supplies		30,293	29,899
By-products		7,397	6,733
Buildings under construction		992	699
Sites for lotting-out construction		6,356	12,985
Goods-in-transit		18,948	58,245
	₩	2,036,833	2,265,355

13. Inventories, Continued

(b) The amount of inventories recognized as an expense for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

In millions of won		2017 Three-month	2017 Six-month	2016 Three-month	2016 Six-month
Cost of sales:					
(Reversal of) loss on valuation of inventories	₩	965	1,377	120	(194)
Loss on retirement of inventories		944	2,099	3,530	4,573
Other expense:					
Loss on retirement of inventories		253	1,844	792	977
Foreign currency differences in allowance for valuation of inventories		(57)	-	-	-
	₩	2,105	5,320	4,442	5,356

14. Cash and Cash Equivalents

(a) Cash and cash equivalents as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won		June 30 2017	December 31 2016
Cash on hand	₩	1,157	1,243
Demand deposits		269,474	233,697
Short-term investment assets		728,213	615,846
	₩	998,844	850,786

(b) Other financial assets as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won		June 30 2017 Current	June 30 2017 Non-current	December 31 2016 Current	December 31 2016 Non-current
Time deposits	₩	109,946	6,340	113,450	-
Certificates of deposit		41,368	-	41,450	-
Money trust		801,111	-	1,502,438	-
Security deposits for checking accounts		-	11	-	11
	₩	952,425	6,351	1,657,338	11

(c) Financial assets restricted in use as of June 30, 2017 and December 31, 2016 were as follows:

In millions of won			June 30 2017	December 31 2016
Other financial assets	Security deposits for checking accounts	₩	11	11
Other financial assets	Performance guarantee		6,340	-
Current other financial assets	Pledge for borrowings		1,368	1,450
		₩	7,719	1,461

15. Non-current Assets Held for Sale

Changes in non-current assets held for sale for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017	2016
Beginning balance	₩	26,315	6,692
Transfer from property, plant and equipment		-	21,165
Disposal		-	(1,542)
Ending balance	₩	26,315	26,315

16. Pledged Assets

(a) The followings assets were pledged as collateral for borrowings as of June 30, 2017.

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Holder
Investment property	₩	150,940	Leasehold deposits received	₩	12,837	13,724	MetLife Insurance Korea Co., Ltd., and etc.
Property, plant and equipment, investment property, etc.		106,850	Short-term borrowings		11,500	89,000	KEB Hana Bank
			Long-term borrowings		13,000		Kookmin Bank
Property, plant and equipment		126,455	Investment subsidy		-	4,189	Wonju-si
			Investment subsidy		-	660	Chungju-si
			Short-term borrowings		1,500	14,500	The Korea Development Bank
			Long-term borrowings		8,500		
Other financial assets		1,368	ACH pledged		-	1,368	Bank of Oklahoma
		6,340	Performance guarantee		-	6,340	Korea Land & Housing Corporation
	₩	391,953		₩	47,337	129,781	

(b) The followings assets were pledged as collateral for borrowings as of December 31, 2016.

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Holder
Investment property	₩	68,810	Leasehold deposits received	₩	9,241	9,467	MetLife Insurance Korea Co., Ltd., etc.
Property, plant and equipment, investment property, etc.		57,748	Short-term borrowings		9,500	48,660	KEB Hana Bank, etc.
			Long-term borrowings		13,075	16,340	KEB Hana Bank, etc.
Property, plant and equipment		128,542	Investment subsidy		-	4,186	Wonju-si
			Investment subsidy		-	660	Chungju-si
			Short-term and long-term borrowings		7,654	14,500	The Korea Development Bank
Other financial assets		1,450	ACH pledged		-	1,450	Bank of Oklahoma
	₩	256,550		₩	39,470	95,263	

17. Share Capital and Other Capital Surplus

(a) Details of share capital as of June 30, 2017 and December 31, 2016 were as follows:

		June 30 2017	December 31 2016
Number of ordinary shares:			
Authorized		800,000,000	800,000,000
Issued		137,292,497	137,292,497
Outstanding		126,265,127	126,265,127
Par value in won	₩	5,000	5,000

The Parent Company has 53,699,400 shares of treasury shares reacquired and retired in prior years. Accordingly, as of June 30, 2017, the Parent Company's ordinary share differs from the aggregate par value of issued shares by ₩268,497 million.

(b) Changes in the number of shares for the six-month period ended June 30, 2017 and the year ended December 31, 2017 were as follows:

	2017			2016		
Number of share	Ordinary shares	Treasury shares	Total	Ordinary shares	Treasury shares	Total
Beginning balance	137,292,497	(11,027,370)	126,265,127	137,292,497	(11,326,605)	125,965,892
Donation of treasury shares	-	-	-	-	299,235	299,235
Ending balance	137,292,497	(11,027,370)	126,265,127	137,292,497	(11,027,370)	126,265,127

(c) Changes in other capital surplus for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017	2016
Beginning balance	₩	(3,430)	(9,928)
Paid-in capital increase of subsidiary		-	7,780
Conversion of redeemable convertible preference shares of subsidiary		(26,285)	(1,282)
Ending balance	₩	(29,715)	(3,430)

For the six-month period ended June 30, 2017, the Parent Company acquired additional shares of PT Sentosa Ababi Purwosari, PT Trisakti Purwosari Makmur and PT Mandiri Maha Mulia.

For the year ended December 31, 2016, changes in the ownership interest in KT&G Life Sciences Corporation resulting from the conversion of redeemable convertible preferred shares and acquisition of additional shares of the investee were recognized in other capital surplus.

18. Treasury Shares

(a) Changes in treasury shares for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won, except number of shares	2017 Number of shares	2017 Carrying amount	2016 Number of shares	2016 Carrying amount
Beginning balance	11,027,370	₩ 328,157	11,326,605	₩ 337,062
Donation of treasury shares	-	-	(299,235)	(8,905)
Ending balance	11,027,370	₩ 328,157	11,027,370	₩ 328,157

(b) Changes in gain on reissuance of treasury shares for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017	2016
Beginning balance	₩	513,776	494,648
Donation of treasury shares, net of tax		-	19,128
Ending balance	₩	513,776	513,776

19. Reserves

(a) Details of reserves as of June 30, 2017 and December 31, 2016 were as follows:

In millions of won		June 30 2017	December 31 2016
Available-for-sale financial assets - net change in fair value	₩	9,153	(18,942)
Foreign operations - foreign currency translation differences		(88,013)	(81,940)
Legal reserve		603,145	603,145
Voluntary reserve		4,408,177	3,794,260
	₩	4,932,462	4,296,523

(b) Available-for-sale financial assets - net change in fair value as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won		June 30 2017	December 31 2016
Available-for-sale financial assets - net change in fair value before tax	₩	12,075	(24,990)
Tax effect		(2,922)	6,048
	₩	9,153	(18,942)

(c) Legal Reserve

The Korean Commercial Act requires the Parent 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.

19. Reserves, Continued

(d) Details of voluntary reserve as of June 30, 2017 and December 31, 2016 were as follows:

In millions of won		June 30 2017	December 31 2016
Reserve for business rationalization	₩	12,851	12,851
Reserve for research and human resource development		10,000	20,000
Reserve for business expansion		698,881	698,881
Unconditional reserve		3,686,445	3,062,528
	₩	4,408,177	3,794,260

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

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

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

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

20. Retained Earnings

Changes in retained earnings for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017	2016
Beginning balance	₩	1,612,032	1,401,975
Dividends		(454,555)	(428,284)
Transfer from reserve for research and human resource development		10,000	10,000
Transfer to unconditional reserve		(623,916)	(577,602)
Profit for the periods		509,854	1,226,030
- Less: non-controlling interests		(1,051)	5,244
Remeasurements of net defined benefit liability, net of tax		(628)	(24,611)
- Less: non-controlling interests		3	(720)
Ending balance	₩	1,051,739	1,612,032

21. Trade and Other Payables

Trade and other payables as of June 30, 2017 and December 31, 2016 are summarized as follows:

		June 30 2017		December 31 2016	
In millions of won		Current	Non-current	Current	Non-current
Leasehold deposits received	₩	21,428	12,439	21,418	6,188
Trade payables		94,009	-	103,826	-
Withholdings		229,198	43	212,413	85
Accrued expenses		173,437	-	192,629	-
Other payables		70,020	5,539	91,922	8,427
	₩	588,092	18,021	622,208	14,700

22. Borrowings

(a) Short-term borrowings as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won	Lender	Annual interest rate		June 30 2017	December 31 2016
Borrowings from financial institution	Kookmin Bank, etc.	0.00%	₩	-	58,000
	KEB Hana Bank	3.02 ~ 3.20%		11,500	8,000
	KEB Hana Bank	3M LIBOR+1.10%		6,246	6,610
	The Korea Development Bank	2.51%		1,500	39,239
	PT Bank Woori Saudara	10.66%		-	2,694
Customer credit contracts(*)	Nonghyup Bank, etc.	5.92%, etc.		24,206	22,056
Borrowings from public entity	Korea agro-Fisheries & Food Trade Corporatio	1.00%		15,000	-
			₩	58,452	136,599

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

22. Borrowings, Continued

(b) Long-term borrowings as of June 30, 2017 and December 31, 2016 are summarized as follows:

In millions of won	Lender	Maturity	Annual interest rate		June 30 2017	December 31 2016
Borrowings from financial institution	Nonghyup Bank	Mar.2022	0.00%	₩	49,636	44,443
	KEB Hana Bank	-	0.00%		-	75
	Kookmin Bank	Sep.2023	2.48 ~ 3.03%		13,000	13,000
	The Korea Development Bank	Nov.2022	2.33 ~ 2.90%		8,500	5,950
Convertible bond					-	8,980
Redeemable convertible preferred shares					35,340	35,340
Redeemable preferred shares					-	17,762
				₩	106,476	125,550
Statement of financial position:						
Current				₩	1,625	9,597
Non-current					104,851	115,953
				₩	106,476	125,550

Details of redeemable convertible preferred shares as of June 30, 2017 are summarized as follows:

Description	Issuing company	Details
Redeemable convertible preferred shares	Renzoluc Pte, Ltd.	Issue date: Sep.2012 Issued value: ₩35,340 million Carrying amount: ₩35,340 million The convertible instrument will mature ten years from the date of establishment of QCP 2011 Corporate Partnership Private Equity Fund (the "PEF"). The instrument can be converted into 6,978,948 ordinary shares at any time after five years from the issue date. Payable on demand from 270 days prior to the expiration of the PEF

(*) The fair value of the liability component was calculated using the market interest rate for an equivalent non-convertible bond. The fair value of the equity component was determined by deducting the fair value of the liability component from the fair value of the compound financial instrument as a whole.

(c) As discussed in note 16 to the consolidated interim financial statements, the Group provided collateral for the above borrowings as of June 30, 2017.

23. Retirement Benefits Plan

(a) The components of retirement benefits for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

In millions of won		2017 Three-month	2017 Six-month	2016 Three-month	2016 Six-month
Defined benefit plans:					
Current service cost	₩	11,210	22,510	10,440	20,856
Net interest cost		549	1,296	789	1,525
		11,759	23,806	11,229	22,381
Defined contribution plans:					
Contributions recognized as expense		1,294	3,535	924	2,889
	₩	13,053	27,341	12,153	25,270

The Group recognized termination benefits amounting to ₩762 million and ₩195 million as an expense for the six-month periods ended June 30, 2017 and 2016, respectively.

(b) Net defined benefit liability as of June 30, 2017 and December 31, 2016 were summarized as follows:

In millions of won		June 30 2017	December 31 2016
Present value of defined benefit obligations	₩	442,699	426,116
Fair value of plan assets		(298,849)	(302,506)
	₩	143,850	123,610

24. Revenue from Real Estate Sales

(a) Details of agreements for real estate sales under construction as of June 30, 2017 were as follows:

In millions of won	Construction period		Total revenue estimated	Total revenue contracted
Daegu Station Central-Xi	Dec.2014 ~ Oct.2017	₩	343,958	342,130

(b) Changes in the balance of contract amount for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017	2016
Beginning balance	₩	133,491	246,340
Other changes		(95)	23,700
Revenue recognized		(71,921)	(136,549)
Ending balance	₩	61,475	133,491

(c) Recognized profits and related balances for agreements under construction as of June 30, 2017 were as follows:

In millions of won	Stage of completion		Cumulative revenue	Cumulative cost	Due from customers for contract work
Daegu Station Central-Xi	82.03%	₩	280,655	224,369	50,910

Due from customers for contract work is recognized as trade and other receivables in consolidated financial statements.

(d) There was no change in the estimates of total revenue and total costs for the six-month period ended June 30, 2017. The total revenue and the total costs are estimated based on the information and circumstances available at the end of the reporting period and actual results may differ from these estimates.

25. Result from Operating Activities

(a) Details of expenses classified by nature for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

(b)

In millions of won		2017 Three-month	2017 Six-month	2016 Three-month	2016 Six-month
Changes in inventories	₩	84,484	228,522	68,119	148,468
Raw materials and consumables purchased		206,592	396,832	224,424	467,767
Salaries		125,032	259,235	132,601	258,665
Retirement and termination benefits		13,126	28,103	12,328	25,465
Depreciation		38,189	76,185	37,802	75,699
Amortization		1,293	2,617	1,484	2,992
Employee welfare		18,463	34,440	22,627	42,571
Advertising		65,035	126,493	57,044	108,443
Commissions		83,730	174,864	77,433	156,308
Other expenses		139,297	231,242	108,380	154,243
	₩	775,241	1,558,533	742,242	1,440,621

(c) Details of selling, general and administrative expenses for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

(d)

In millions of won		2017 Three-month	2017 Six-month	2016 Three-month	2016 Six-month
Salaries	₩	83,883	173,923	88,170	171,921
Retirement and termination benefits		9,090	18,967	8,218	16,837
Employee welfare		12,696	23,394	16,943	31,765
Travel		4,464	8,064	3,694	6,117
Communications		1,294	2,522	1,361	2,632
Utilities		1,810	4,382	1,882	4,511
Taxes and dues		14,347	16,971	13,278	15,214
Supplies		1,081	1,993	3,269	4,108
Rent		6,201	12,731	5,822	11,460
Depreciation		10,701	21,234	10,039	20,128
Amortization		1,089	2,207	1,434	2,894
Repairs and maintenance		1,787	2,404	1,256	2,164
Vehicles		1,556	2,999	1,431	2,780
Insurance		646	1,315	545	1,053
Commissions		69,228	146,779	62,665	129,449
Freight and custody		14,527	27,478	12,160	24,446
Conferences		1,224	2,485	922	1,369
Advertising		64,979	126,414	56,979	108,363
Training		1,504	2,780	1,558	2,885
Prizes and rewards		651	982	599	845
Cooperation		315	549	213	383
Normal research and development		10,288	17,908	7,365	14,624
Impairment loss (reversal of impairment loss) on trade receivables		102	152	2,675	821
	₩	313,463	618,633	302,478	576,769

26. Other Income and Expenses

(a) Details of other income for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

			2017		2016
In millions of won		Three-month	Six-month	Three-month	Six-month
Foreign currency transaction gain	₩	3,927	7,913	4,583	13,849
Foreign currency translation gain		33,489	3,651	14,035	12,201
Reversal of impairment loss on other receivables		-	-	-	3
Gain on sale of property, plant and equipment		511	632	8,498	8,591
Gain on sale of intangible assets		-	685	-	50
Others		5,915	11,308	7,243	10,340
	₩	43,842	24,189	34,359	45,034

(b) Details of other expenses for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

			2017		2016
In millions of won		Three-month	Six-month	Three-month	Six-month
Foreign currency transaction loss	₩	17,534	33,372	5,971	11,754
Foreign currency translation loss		-	45,197	-	15,776
Impairment loss on other receivables		-	7	-	-
Donations		1,776	3,870	1,405	3,981
Loss on sale of property, plant and equipment		979	1,285	1,674	1,841
Loss on sale of intangible assets		385	547	5	5
Impairment loss on intangible assets		-	1,794	-	-
Others		17,896	18,423	2,095	5,393
	₩	38,570	104,495	11,150	38,750

27. Net Finance Income

(a) Details of net finance income for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

		2017		2016	
In millions of won		Three-month	Six-month	Three-month	Six-month
Finance cost:					
Interest expense	₩	(1,429)	(2,962)	(1,847)	(3,550)
Loss on sale of available-for-sale financial instruments		(5)	(5)	-	-
Impairment loss on available-for-sale financial instruments		(14,640)	(14,640)	-	-
		(16,074)	(17,607)	(1,847)	(3,550)
Finance income:					
Interest income		8,930	20,530	9,260	18,756
Dividend income		3,436	11,239	3,723	9,920
Interest income on long-term deposits in MSA Escrow Fund		2,023	4,067	2,057	4,089
Gain on sale of available-for-sale financial assets		460	1,014	-	-
		14,849	36,850	15,040	32,765
Net finance income	₩	(1,225)	19,243	13,193	29,215

(b) Details of interest expenses for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

		2017		2016	
In millions of won		Three-month	Six-month	Three-month	Six-month
Borrowings	₩	1,154	1,841	1,026	2,058
Trade and other payables		274	1,120	820	1,490
Others		1	1	1	2
	₩	1,429	2,962	1,847	3,550

(c) Details of interest income for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

		2017		2016	
In millions of won		Three-month	Six-month	Three-month	Six-month
Deposits	₩	8,850	19,641	8,123	16,769
Available-for-sale financial assets		55	62	8	15
Trade and other receivables		25	827	1,129	1,972
	₩	8,930	20,530	9,260	18,756

28. Income Tax

(a) Income tax expense was recognized as current tax expense adjusted to current adjustments for prior periods, deferred tax expense (income) by origination and reversal of deferred tax assets (liabilities) and temporary differences, and income tax recognized in other comprehensive income. The average effective tax rate was 29.77% and 26.47% for the six-month periods ended June 30, 2017 and 2016, respectively.

(b) Deferred tax assets have been recognized to the extent the Group has determined it is probable that future profits will be available against which the Group can utilize the related benefit.

29. Earnings per Share

Basic and diluted earnings per share for the three- and six-month periods ended June 30, 2017 and 2016 were as follows:

In millions of won, except share information		2017 Three-month	2017 Six-month	2016 Three-month	2016 Six-month
Profit for the period attributable to owners of the parent in millions of won	₩	274,295	508,803	284,945	569,334
Weighted-average number of ordinary shares outstanding		126,265,127	126,265,127	126,143,670	126,133,902
Basic and diluted earnings per share in won	₩	2,172	4,030	2,259	4,514

The weighted average number of ordinary shares outstanding during the period 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-weighting factor.

30. Transactions and Balances with Related Parties

(a) The Group has no significant transactions for the six-month period ended June 30, 2017.

(b) Details of receivables and liabilities with related parties, as of June 30, 2017 were as follows:

In millions of won		2017 Loans	2016 Loans
Investments in associates and joint ventures			
LSK Global Pharma Services Co., Ltd.	₩	1,854	-

(c) Details of financial transactions with related parties for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017 Capital Increase	2017 Loans Increase	2017 Loans Collection	2016 Capital Increase
Investments in associates and joint ventures					
LSK Global Pharma Services Co., Ltd.	₩	-	2,054	200	-

30. Transactions and Balances with Related Parties, Continued

(d) There is no guarantee provided by or providing to related parties as of June 30, 2017.

(e) Details of key management personnel compensation for the three- and six-month periods ended June 30, 2017 and 2016 are summarized as follows:

In millions of won		2017 Three-month	2017 Six-month	2016 Three-month	2016 Six-month
Short-term employee benefits	₩	6,648	13,686	5,606	11,161
Retirement benefits		460	1,486	454	1,336
	₩	7,108	15,172	6,060	12,497

31. Risk Management and Fair Value of Financial Instruments

(a) Overview

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

- Market risk
- Credit risk
- Liquidity risk

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

(b) Risk Management Framework

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

(c) Management of Financial Risks

(i) 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 Group'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.

31. Risk Management and Fair Value of Financial Instruments, Continued

(c) Management of Financial Risks, Continued

(i) Market Risk, Continued

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

The carrying amounts of monetary assets and liabilities denominated in a currency other than the functional currency as of June 30, 2017 and December 31, 2016 were as follows:

		June 30 2017		December 31 2016	
In millions of won		Assets	Liabilities	Assets	Liabilities
USD	₩	1,917,203	55,046	950,652	69,029
EUR		33,513	4,862	940	3,125
Others		72,231	2,917	9,727	5,046
	₩	2,022,947	62,825	961,319	77,200

As of June 30, 2017 and December 31, 2016, the effects of a 10% strengthening or weakening of functional currency against foreign currencies on profit before tax were as follows:

		June 30 2017		December 31 2016	
In millions of won		10% weakening	10% strengthening	10% weakening	10% strengthening
Increase (decrease) in profit before tax	₩	196,012	(196,012)	88,412	(88,412)

Equity Price Risk
The Group has exposure to the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Other market price risk arises from available-for-sale equity instruments held for investments. The Group's management has monitored the mix of debt and equity instruments in its investment portfolio based on market indices. Material investments within the portfolio are managed on an individual basis and all buy and sell decisions are approved by the Group's management.

As of June 30, 2017 and December 31, 2016, the effects of a 5% fluctuation of the price index of stocks on other comprehensive income were as follows:

		June 30 2017		December 31 2016	
In millions of won		5% increase	5% decrease	5% increase	5% decrease
Increase (decrease) in comprehensive income before tax	₩	8,449	(8,449)	5,879	(5,879)

31. Risk Management and Fair Value of Financial Instruments, Continued

(c) Management of Financial Risks, Continued

(i) Market Risk, Continued

Interest Rate Risk
The Group has exposure to the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group's management has monitored the level of interest rates regularly and has maintained the balance of borrowings at variable rates and fixed rates. As of June 30, 2017, 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.

(ii) Credit Risk

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

The carrying amount of financial assets is maximum exposure to credit risk. The maximum exposure to credit risk as of June 30, 2017 and December 31, 2016 is as follows:

In millions of won		June 30 2017	December 31 2016
Available-for-sale debt instruments	₩	-	1,500
Long-term deposits in MSA Escrow Fund		518,585	503,592
Trade and other receivables		1,358,704	1,353,589
Other financial assets		958,776	1,657,349
Cash and cash equivalents (excluding cash on hand)		997,687	849,543
Financial guarantee contract		231,670	153,145
	₩	4,065,422	4,518,718

31. Risk Management and Fair Value of Financial Instruments, Continued

(c) Management of Financial Risks, Continued

(iii) Liquidity Risk

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

The contractual maturity analysis of financial liabilities as of June 30, 2017 and December 31, 2016 is as follows:

				Residual contractual maturity			
In millions of won		Carrying amount	Contractual cash flow	Within 3 months	Between 3 months and 1 year	Between 1 and 5 years	Beyond 5 years
As of June 30, 2017:							
Trade and other payables	₩	376,872	378,037	331,710	28,457	16,794	1,076
Long-term borrowings		104,851	107,236	78	235	68,718	38,205
Current portion of long-term borrowings		1,625	1,670	11	1,659	-	-
Short-term borrowings		58,452	58,738	36,157	22,581	-	-
Financial guarantee contract		-	231,670	-	231,670	-	-
	₩	541,800	777,351	367,956	284,602	85,512	39,281
As of December 31, 2016:							
Trade and other payables	₩	424,410	425,970	386,382	24,748	11,729	3,111
Long-term borrowings		115,953	117,978	37	111	54,105	63,725
Current portion of long-term borrowings		9,597	9,611	79	9,532	-	-
Short-term borrowings		136,599	137,591	64,221	73,370	-	-
Financial guarantee contract		-	153,145	-	-	153,145	-
	₩	686,559	844,295	450,719	107,761	218,979	66,836

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

31. Risk Management and Fair Value of Financial Instruments, Continued

(d) Fair Value of Financial Instruments

The carrying amount of each category of financial assets and liabilities as of June 30, 2017 and December 31, 2016 are as follows:

In millions of won		June 30 2017	December 31 2016
Financial assets:			
Available-for-sale financial assets	₩	424,519	386,596
Loans and receivables:			
- Long-term deposits in MSA Escrow Fund		518,585	503,592
- Trade and other receivables		1,358,704	1,353,589
- Other financial assets		958,776	1,657,349
- Cash and cash equivalents		998,844	850,786
		3,834,909	4,365,316
Total financial assets	₩	4,259,428	4,751,912
Financial liabilities:			
Financial liabilities measured at amortized cost:			
- Trade and other payables	₩	376,872	424,410
- Long-term borrowings		104,851	115,953
- Current portion of long-term borrowings		1,625	9,597
- Short-term borrowings		58,452	136,599
Total financial liabilities	₩	541,800	686,559

The fair value measurements classified by fair value hierarchy as of June 30, 2017 and December 31, 2016 were as follows

			Fair value		
In millions of won		Carrying amount	Level I	Level II	Level III
As of June 30, 2017:					
- Available-for-sale financial assets	₩	393,456	239,261	-	154,195
As of December 31, 2016:					
- Available-for-sale financial assets	₩	354,032	221,076	-	132,956

There is no transfer between fair value hierarchy levels of recurring fair value measurements for the six-month period ended June 30, 2017 and the year ended December 31, 2016.

31. Risk Management and Fair Value of Financial Instruments, Continued

(d) Fair Value of Financial Instruments, Continued

The fair value measurements for available-for-sale equity instruments in real estate trust fund have been measured using the adjusted net asset method and categorized as a level 3 fair value based on the inputs to the valuation techniques used. Changes in fair value classified as level 3 for the six-month period ended June 30, 2017 and the year ended December 31, 2016 were as follows:

In millions of won		2017	2016
Beginning balance	₩	132,956	115,108
Acquisition		20,000	16,000
Disposal		(3,462)	-
Changes in fair value		4,701	1,848
Ending balance	₩	154,195	132,956

(e) Finance income (costs)

(i) Details of finance income (costs) by categories for the six-month period ended June 30, 2017 were as follows:

In millions of won		Available -for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
Profit or loss:					
- Interest income	₩	62	20,468	-	20,530
- Dividend income		11,239	-	-	11,239
- Investment income on long-term deposits in MSA Escrow Fund		-	4,067	-	4,067
- Gain on sale of available-for-sale financial assets		1,014	-	-	1,014
- Interest expense		-	-	(2,962)	(2,962)
- Impairment loss		(14,640)	(159)	-	(14,799)
	₩	(2,352)	24,403	(2,962)	19,089
Comprehensive income before tax					
- Net change in fair value	₩	23,439	-	-	23,439
- Disposal		(1,014)	-	-	(1,014)
- Reclassification due to impairment		14,640			14,640
	₩	37,065	-	-	37,065

31. Risk Management and Fair Value of Financial Instruments, Continued

(e) Finance income (costs), Continued

(ii) Details of finance income (costs) by categories for the six-month period ended June 30, 2016 were as follows:

In millions of won		Available -for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
Profit or loss:					
- Interest income	₩	15	18,741	-	18,756
- Dividend income		9,920	-	-	9,920
- Investment income on long-term deposits in MSA Escrow Fund		-	4,089	-	4,089
- Interest expense		-	-	(3,550)	(3,550)
	₩	9,935	22,830	(3,550)	29,215
Comprehensive income before tax					
- Net change in fair value	₩	(7,340)	-	-	(7,340)

32. Capital Management

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

The Group monitors capital using net debt by deducting cash and cash equivalents and current financial instruments from borrowings and equity. The Group applied the same capital management strategy that was applied in the previous year.

As of June 30, 2017 and December 31, 2016, the Group's equity and net debt structure are as follows:

In millions of won		June 30 2017	December 31 2016
Net debt (asset):			
Debt (borrowings)	₩	164,928	262,149
Less:			
- Cash and cash equivalents		(998,844)	(850,786)
- Current other financial assets		(952,425)	(1,657,338)
		(1,786341)	(2,245,975)
Equity	₩	7,152,740	7,118,257

33. Contingent Liabilities and Commitments

(a) Each year the Group 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 United States government. The MSA Escrow Funds are maintained to pay the medical expenses of tobacco purchasers who have suffered health effects as a result of smoking. The unused portion of this fund will be refunded to the Group 25 years from the date of each annual funding. The Group recorded as long-term deposits the amounts paid into the MSA Escrow Funds of State governments in the United States against potential litigation and damages related to the export of tobacco into the United States.

(b) As of June 30, 2017, a lawsuit by National Health Insurance Service claiming damages of ₩53,742 million has been filed against the Group. Additionally, as of June 30, 2017, the Group is involved in twenty lawsuits as a plaintiff for alleged damages totalling ₩26,966 million and nine lawsuits as a defendant for alleged damages totalling ₩2,748 million. The amount of the liability the Group may ultimately be liable for with respect to the litigation cannot be reasonably estimated as of June 30, 2017.

(c) As of June 30, 2017, the Group has entered into letter of credit agreements with KEB Hana Bank and other bank with limits in the aggregate of USD 64,100 thousand.

(d) As of June 30, 2017, the Group's trade receivables from the export of cigarettes are insured against non-payment up to USD 22,413 thousand by an export guarantee insurance with the Korea Export Insurance Corporation.

(e) The Group has been provided with a foreign currency payment guarantee by KEB Hana Bank and Westchester Fire Insurance Company up to USD 40,000 thousand and USD 20,000 thousand for L/C or guarantees related with its foreign exports, respectively. Details of guarantees exercised as of June 30, 2017, are summarized as follows:

In thousands of USD, THB and millions of IDR		Exercised amount
Customs bond and L/C opening of KT&G USA Corporation.	USD	31,417
Performance guarantee for export of tobacco sheet to Thailand Tobacco Monopoly	THB	3,211
Payment guarantee for purchase of certificate stamp of PT Mandiri Maha Mulia, etc.	IDR	160,234

33. Contingent Liabilities and Commitments, Continued

(f) The Group has maintained a contract with the farmers who grow six-year old green ginseng for purchase volume guarantees and recorded contractual amounts paid to the farmers as advance payments in the amount of ₩176,084 million and ₩128,633 million as of June 30, 2017 and December 31, 2016, respectively.

(g) As of June 30, 2017, the Group has an account receivable loan agreement with a limit of ₩107,000 million with KEB Hana Bank and other financial institution.

(h) As of June 30, 2017, the Group has a trade bill borrowing agreement with a limit of ₩10,000 million with KEB Hana Bank.

(i) As of June 30, 2017, the Group has a borrowing agreement with a limit of ₩219,236 million with Shinhan Bank and other financial institutions.

(j) As of June 30, 2017, the Group has provided one blank note, five notes amounting to ₩4,000 million and two blank checks to Nara Credit and other financial institution. Besides, As of June 30, 2017, the Group lost seven blank notes and one blank check and expects to seek judgment of nullification.

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

(l) With relation to the acquisition of KT&G Life Sciences Corporation, which was merged into Yungjin Pharm. Co., Ltd., the Parent Company entered into a contract with a former owner of the acquiree, Gwak, Tae-Hwan ("Individual Shareholder"). Details of the contract are as follows:

Description	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 Parent Company	Individual Shareholder shall not be permitted to make any transfer of its shares, in whole or in part, unless Individual Shareholder has offered them first to the Parent Company.
Tag-along right held by Individual Shareholder	In the event that the Parent Company proposes to enter into a transaction or a series of related transactions with a third party purchaser to dispose of its shares, then Individual Shareholder shall elect to participate in such disposition upon the terms and conditions no less favorable than those applicable to the Parent Company.

(m) As of June 30, 2017, the Group has provided guarantees up to ₩237,516 million with an exercised amount of ₩193,058 million for the buyers of apartments in respect of their borrowings from Shinhan Bank.

(n) As of June 30, 2017, the Group is insured by performance bond insurance up to ₩5,081 million with the Seoul Guarantee Insurance.

(o) As of June 30, 2017, the Group recognizes other financial assets of ₩6,340 million deposited in Nonghyup bank and restricted in use in order to provide a performance guarantee for the commercial district development project in Sejong-si.

34. Cash Flows

(a) Details of cash generated from operations for the six-month period ended June 30, 2017 and 2016 were as follows:

In millions of won		2017	2016
Profit for the period	₩	509,854	570,308
Adjustments for:			
Income tax expense		216,115	205,303
Finance costs		17,607	3,550
Finance income		(36,850)	(32,765)
Depreciation		76,185	75,699
Amortization		2,617	2,992
Retirement and termination benefits		28,103	25,465
Foreign currency translation loss		45,197	15,776
Impairment loss on trade and other receivables		159	821
Reversal of the write-down of inventories		1,377	(194)
Loss on sale of property, plant and equipment		1,285	1,841
Loss on sale of intangible assets		547	5
Loss on sale of investment in subsidiaries		1,794	-
Other expense		10,067	5,198
Share of gain of associates and joint ventures		(5,119)	113
Share of loss of associates and joint ventures		-	(1,406)
Foreign currency translation gain		(3,651)	(12,201)
Reversal of impairment loss on trade and other receivables		-	(3)
Gain on sale of property, plant and equipment		(632)	(8,591)
Gain on sale of intangible assets		(685)	(50)
		863,970	851,861
Changes in working capital:			
Trade and other receivables		(17,625)	(41,350)
Advance payments		(71,688)	(59,090)
Prepaid expenses		3,229	(4,758)
Prepaid tobacco excise and other taxes		36,018	(32,964)
Inventories		227,335	146,640
Trade and other payables		(39,123)	4,007
Advance receipts		595	(19,961)
Tobacco excise and other taxes payable		(579,762)	(93,772)
Payment of retirement and termination benefits		(11,619)	(7,870)
Cash generated from operations	₩	411,330	742,743

34. Cash Flows, Continued

(b) Details of material transactions without cash inflow and outflow for the six-month period ended June 30, 2017 and 2016 were as follows:

In millions of won		2017	2016
Decrease in accrued expenses related with payment of retirement and termination benefits	₩	(2,717)	-
Increase in other payables related with acquisition of property, plant and equipment		(4,140)	3,394
Increase (decrease) in other payables related with acquisition of intangible assets		(1,229)	-
Increase (decrease) in advance receipts related with disposal of property, plant and equipment and non-current assets held for sale		-	(623)
Decrease in other receivables related with disposal of property, plant and equipment		491	3,139
Transfer of available-for-sale financial instrument to loans		2,054	-
Transfer to property, plant and equipment from construction-in-progress		2,062	-

(c) The Group presented cash flows arising from short-term financial instruments on a net basis.

35. Business combination

(a) Details of business combination for the six-month period ended June 30, 2017 were as follows:

In millions of Won

Name	Principal operation	Acquisition date	Percentage of voting equity acquired	Considerations transferred	Acquisition purpose
PT Nusantara Indag Makmur	Selling tobaco	April 10, 2017	100%	2,993	Business expansion

(b) Details of fair value of assets and liabilities recognized on acquisition date due to business combination for the six-month period ended June 30, 2017 were as follows:

In millions of won		
Fair value of identifiable assets	₩	16,427
Fair value of identifiable liabilities		13,900
Fair value of identifiable net assets	₩	2,527

35. Business combination, Continued

(c) Details of goodwill recognized from business combination for the six-month period ended June 30, 2017 were as follows:

In millions of won		
Fair value of consideration transferred	₩	2,993
Amount recognized for identifiable assets and liabilities:		
Property, plant and equipment		420
Inventories		11,181
Accounts receivables and other receivables		2,283
Other assets		800
Cash and cash equivalents		1,743
Defined benefit liabilities		917
Accounts payable and other payable		12,918
Other liabiities		65
Total identifiable net assets		2,527
Goodwill	₩	466

(d) Details of net cash transferred due to business combination for the six-month period ended June 30, 2017 were as follows:

In millions of won		
Transferred cash	₩	2,993
Acquired cash and cash equivalents		(1,743)
Net cash transferred	₩	1,250

(e) Incomplete purchase accounting

Since the Group was unable to obtain the financial statements of the acquiree as of the acquisition date, the accounting for the business combination reflected in the accompanying interim consolidated financial statements is based on management's preliminary evaluation. Upon finalization of the accounting treatment, the recorded impacts on the Group's consolidated financial statements may change. In addition, no profit or loss of the acquiree subsequent to the acquisition date has been reflected in the accompanying consolidated interim financial statements as such information was not available.