FARON

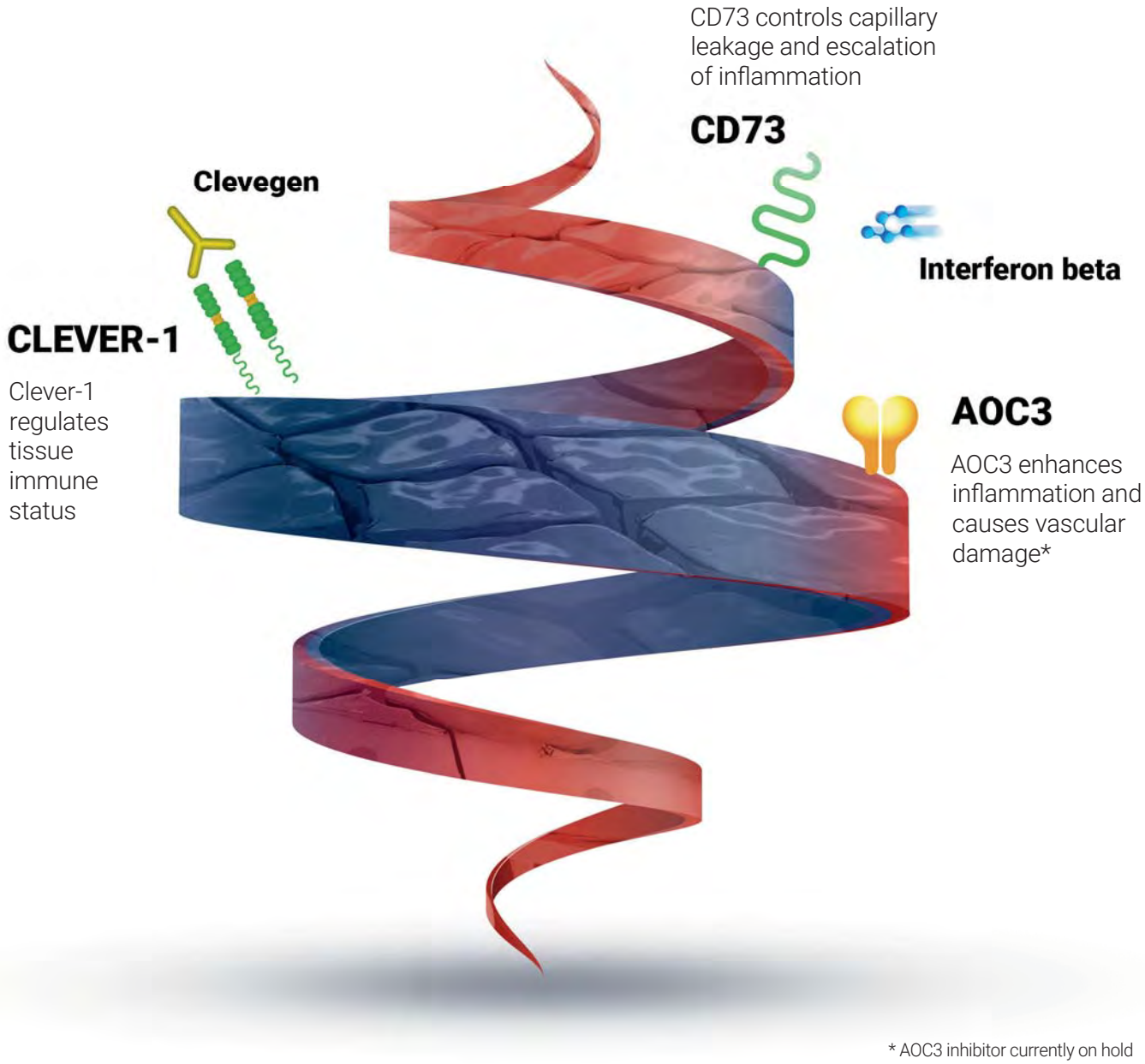
ANNUAL REPORT 2017

Pushing boundaries to save Lives

Contents

Endothelial barrier is everything

Faron's pipeline is based on endothelial receptors involved in regulation of immune responses. Faron has mastered control of this response in both directions; slowing down immune escalation, and removal of immune suppression.



* AOC3 inhibitor currently on hold

The endothelial surface of exhaustive capillary networks control fluid and cell balance between circulation and tissues, and is a factor in many devastating diseases like organ failures and cancer metastasis.

FARON PHARMACEUTICALS

Pushing boundaries to save lives

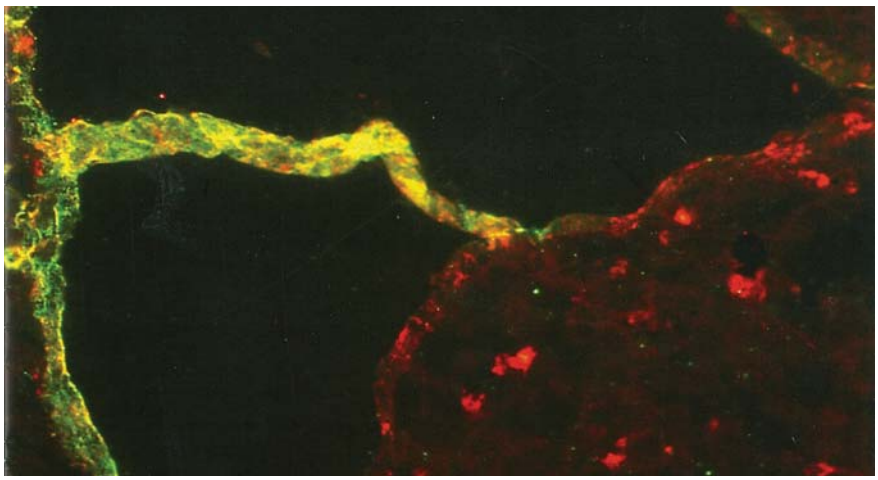
Faron Pharmaceuticals Ltd is a clinical stage biopharmaceutical company developing novel treatments for medical conditions with significant unmet needs. The Company currently has a pipeline focusing on acute organ traumas, vascular damage and cancer immunotherapy. The Company believes that self-commercialisation of the pipeline will produce the highest returns to the shareholders.

The Company's lead candidate Traumakine®, to prevent vascular leakage and organ failures, is currently the only treatment for Acute Respiratory Distress Syndrome (ARDS) undergoing Phase III clinical trials. There is currently no approved pharmaceutical treatment for ARDS. An additional European Phase II Traumakine trial is underway for the Rupture of Abdominal Aorta Aneurysm ("RAAA"). Both patient groups have high mortality due to multi organ failure (MOF) caused by ischemia-reperfusion injury. Faron's second candidate Clevegen is a ground breaking humanized Clever-1 antibody. Clevegen has the ability to switch immune suppression to immune activation in various conditions, with potential across oncology, infectious disease and vaccine development. This novel macrophage-directed immuno-oncology switch called Tumour Immunity Enabling Technology ("TIET") may be used alone or in combination with other immune checkpoint molecules for the treatment of cancer patients.

Faron is based in Turku, Finland and is listed on London AIM under the ticker 'FARN'.

FARON PHARMACEUTICALS

Endothelial Barrier Is Everything



Imagine cars speeding in a dark tunnel, 100,000 kilometers long, without lights, at a speed of 700–800 km/h, navigating their way to their destinations.

The situation described above applies to cells, which migrate in our vasculature system and need to move around. This movement is part of the normal surveillance system to detect any harmful event that would put our existence at risk. This is our innate defence system, but it also provides the initial immunological reaction against any foreign material entering the body.

The "GPS" for these moving cells is a molecular recognition system consisting of special molecules on the surface of migrating cells and their counterparts on the surface of vascular endothelial cells. These "homing" molecules form an essential cellular trafficking guidance system, which we all need to maintain our normal physiology. Unfortunately, many diseases utilise this system as well. This calls for ways to control the guidance system in order to prevent or heal diseases. Among these diseases the most harmful ones are extended inflammations and cancer spread.

Our vascular system also includes a drainage system called lymphatics. The same guidance system also operates there but the recognition molecules are unique. In both of these capillary networks the endothelial cells control the entry of migrating cells and maintain a barrier between circulation and tissues. Without this barrier, we encounter a catastrophic situation, which can lead to life-threatening conditions.

Faron is targeting several endothelial molecules involved in this guidance system and the maintenance of the endothelial barrier. We believe that the control of these molecules provides a unique way of treating many life-threatening conditions with high unmet need. Our lead indications – acute respiratory distress syndrome (ARDS), multi-organ failure (MOF) and control of tumour immunity – are both based on the malfunction of the endothelial barrier, both of which we have learned to control (see page 3).

We hope that our 2017 Annual Report inspires you to explore our technologies, which have originated from world-class academic laboratories and developed by Faron as novel proprietary treatments for ARDS, MOF, and tumour immune suppression.

FARON PHARMACEUTICALS

Highlights

(including post period end)

OPERATIONAL:

Traumakine®

- The INTEREST study did not meet the Day 28 primary composite endpoint with both Traumakine and placebo reporting similar all cause mortality rates. Further investigations are currently underway to provide additional information on the outcome of the current analysis.
- Japanese partner Maruishi continued to progress its pivotal Phase III ARDS trial in Japan and has received two IDMC recommendations to continue the trial as planned. Maruishi anticipates completion of recruitment of this 120-patient study in mid 2018.
- Faron received the first recommendation from the Independent Data Monitoring Committee (IDMC) in the Traumakine Phase II INFORAAA study for the treatment of Multi-Organ Failure (MOF) and mortality prevention of surgically operated Ruptured Abdominal Aorta Aneurysm (RAAA), to continue the trial as planned. Study currently on pause until the INTEREST study analysis completes and the Japanese Phase III ARDS trial is reported.
- US Food and Drug Administration (FDA) proposed that Faron proceed directly to BLA submission for Traumakine in the US upon successful completion of the European and Japanese Phase III trials. FDA Fast Track Designation was granted in January.
- Second independent manufacturing facility established for Traumakine.
- Patent estate for Traumakine strengthened with a formulation patent granted in Finland and filed in the US and PCT for Faron's IV dose form of interferon-beta, in addition to allowed patents in Europe and Japan for the use of certain biomarkers to measure the severity and treatment efficacy of patients with ARDS.

Clevegen®

- Preclinical toxicity studies completed with no sign of serious adverse events indicated.
- Successful production of technical batches of Clevegen by manufacturing partner Abzena.
- Agreement signed with the University of Birmingham Medical School, UK, to initiate a liver cancer clinical trial program, focused on the protocol design for a Phase I/II trial, MATINS. Clinical trial application expected to be filed in H2 2018.
- Filed advice package to the UK Regulatory Agency MHRA on the adaptive protocol design for the MATINS trial to include dose escalation and efficacy measures in four solid tumour cancers (liver, melanoma, pancreas and ovarian).
- Patent granted by the European Patent Office for the use of Clever-1 antibodies, the mechanism behind Clevegen, for the treatment of cancer.

FINANCIAL

- Raised £5.0 million (net €5.4 million) in March 2017 to fund preclinical and early clinical development of Clevegen. Raised £10 million (net €10.4 million) in October 2017 to support the Traumakine pre-launch activities.
- In addition to the above the Company raised €0.4 million through the subscription of shares with warrants and options in April – May 2017.
- Drew down €0.5 million of a €1.5 million R&D loan granted by Tekes in June 2017 to progress the Clevegen programme.
- On 31 December 2017, the Company held cash balances of €9.3 million (2016: €11.5 million). The cash position at end March 2018 was €18.7 million.
- Loss for the period for the financial year ended 31 December 2017 was €21.1 million (2016: €10.1 million loss).
- Net assets on 31 December 2017 were €4.7 million (2016: €8.4 million)
- Post accounting period raised £15.0 million (net €15.9 million) in February 2018 intended to support preparations for the commercialisation of Traumakine and to advance the clinical development of Clevegen in several indications.
- The board will be focussing on reducing cash burn and preservation of existing resources until the full data analysis is complete and it is agreed how best to deliver value to shareholders.

CORPORATE

- Dr Juhana Heinonen was appointed Chief Commercial Officer and Dr Juho Jalkanen was appointed Vice President of Business Development within the period.
- Board strengthened by the appointments of Dr Gregory Brown and Mr John Poulos as Non-Executive Directors in May 2017.
- During the first of quarter 2018, Faron Pharmaceuticals has registered subsidiaries in the United States of America and in Switzerland.

STRATEGIC REPORT

Addressing significant unmet medical needs

Strategy (2017)

Faron's strategy is to maximise the potential of its pipeline of drug candidates and to progress the development of its lead product Traumakine. Faron targets several endothelial molecules involved in the maintenance of the endothelial barrier which is a thin layer (membrane) of cells that lines blood and lymphatic vessels to separate blood content from tissue. The Company believes that the control of these molecules provides a unique way to treat many life-threatening conditions with no efficient treatment options. Faron collaborates with its strategic partners in research, manufacturing and drug development to bring new pharmaceutical products to market in a timely and cost-effective manner and has formed a core team of leading scientists in capillary biology and diseases arising from vascular leakage. The Company has established links with leading laboratories and clinics based at Turku University in Finland, University of Birmingham Medical School in UK and other institutions.

To date, Faron has operated on a relatively low cost basis by employing only key members of staff and outsourcing where possible. Typically, all development work up to the proof-of-concept stage of drug development is carried out in the innovators' laboratories. The Company outsources all of its manufacturing activities in relation to its products to third parties and collaborates with Contract Research Organisations (CROs) to carry out the clinical development programmes. Faron monitors and evaluates potential commercial opportunities for its established drug candidates, such as Traumakine and Clevegen and its technologies, as and when they arise and will consider how best to crystallise as much value as possible for Shareholders, which may include holding rights in main territories for as long as it is feasible, or, in certain circumstances, up to the marketing stage. The Company has decided to take Traumakine to ARDS markets in Europe and US and preparations were initiated in 2017 to promote this success.

STRATEGIC REPORT

Chairman's Statement

During 2017 Faron continued to make progress across all areas of the business, with the highly experienced management team consistently delivering against all strategic objectives for the year. Progress was made with both Traumakine and Clevegen and the Company built out the underlying capabilities within the organisation.

Faron's lead drug candidate, Traumakine, completed patient recruitment into the pivotal, pan-European Phase III INTEREST trial in ARDS according to schedule. We are incredibly disappointed to report that the trial has not met the primary endpoint, and we will now carefully review the data in order to plan the next steps for Traumakine in ARDS.

The Company continues to believe that Traumakine could have applications across other serious indications and in early 2017, recruited the first patient in a Phase II trial (INFORAAA) assessing Traumakine for the prevention of Multi Organ Failure (MOF) and patient mortality after surgical repair of the acute rupture of abdominal aorta (RAAA). RAAA is a medical emergency with no known treatment and an overall mortality of 30 to 50% for post-operative reperfusion injury for RAAA patients. The study is currently on pause until the INTEREST study analysis completes and the Japanese Phase III ARDS trial is reported.

Faron's second product, Clevegen, is an immunotherapy candidate that causes conversion of the immune environment around a tumour from immune suppressive to immune stimulating by reducing the number of tumour-associated macrophages (TAMs). We continue to believe that Clevegen is well differentiated from other immunotherapies and following encouraging preclinical toxicity studies, we look forward to moving Clevegen into first clinical trials in H2 2018 to study its potential in multiple solid tumours through our partnership with the University of Birmingham Medical School, UK.

The Company remains well funded, having raised £15m gross proceeds during 2017, and a further £15m gross proceeds in February 2018 which provides us with a solid financial foundation.

During the course of the year we further strengthened the Board with the appointment of Dr Gregory Brown and Mr John Poulos in May 2017. Greg and John bring a wealth of global experience in the life sciences and investment community, particularly from a US and commercial angle and I was delighted to welcome them.

The Board's key priority is to now assess the next steps for Traumakine in ARDS, once the data are fully analysed, and to progress our novel and unique immunotherapy agent Clevegen into first human trials. The board will be focussing on reducing cash burn and preservation of existing resources until the full data analysis is complete and it is agreed how best to deliver value to shareholders.

The Board would like to thank the management team, staff and key partners for continued delivery during 2017. The Board is also extremely grateful to the investigators and patients who are part of our clinical trials. We look forward to updating you on our plans in due course.

Dr Frank M Armstrong
Chairman
May 5, 2018

STRATEGIC REPORT

Chief Executive Officer's Review

Overview

Faron is highly focused on developing novel treatments for life-threatening medical conditions with significant unmet need for both individuals and society. Whilst 2017 was a busy year for Faron in anticipation of Traumakine data, we have today reported that the trial did not meet the primary endpoint. We will now seek to analyse and understand, as quickly as possible, the implications and next steps for Traumakine in ARDS.

Dr Markku Jalkanen
Chief Executive Officer
May 5, 2018

Traumakine Development

INTEREST trial

In May 2018, we reported that the Traumakine INTEREST trial did not meet the primary endpoint in ARDS. This is despite many years of research suggesting a potential benefit in these very sick patients. We are conducting further investigations in order to provide additional information on the outcome of the current analysis.

Our partner Maruishi continues to progress its pivotal Phase III trial in Japan and two IDMC recommendations to continue the trial as planned have been received. Maruishi expects to complete recruitment in the second quarter of 2018.

Phase II INFORAAA

We continue to believe that Traumakine has the potential for application in additional disease areas. In February 2017, the first patient was enrolled in the Traumakine Phase II INFORAAA trial for the treatment of Multi-Organ Failure (MOF) and mortality prevention of surgically operated Ruptured Abdominal Aorta Aneurysm (RAAA).

RAAA is a surgical emergency with an overall mortality of 70 to 80% and requires immediate surgery and aortic repair. The main cause of death for these patients is multiple organ failure following a post-operative reperfusion injury of ischemic organs including kidneys, liver, brain and intestines. We believe that Traumakine has the potential to offer significantly improved outcomes for patients following surgery for RAAA. We also believe that the clinical data from the INFORAAA trial could provide us with valuable information on the recovery of ischemic single organ injuries and are planning further trials to treat these injuries. The study is currently on pause until the INTEREST study analysis completes and the Japanese Phase III ARDS trial is reported.

The study currently has six open sites in Finland, two in Lithuania and one in Estonia. The INFORAAA study aims to treat a total of 160 post-operative RAAA patients. The study is currently on pause until the INTEREST study analysis completes and the Japanese Phase III ARDS trial is reported.

Clevegen Development

Faron's second product, its preclinical immunotherapy candidate, Clevegen, causes conversion of the immune environment around a tumour from immune suppressive to immune stimulating by reducing the number and function of tumour-associated macrophages (TAMs). Recent developments in the exciting field of cancer immunotherapy have been well documented with a number of important indications of clini-

cal success. We believe that Clevegen is differentiated from other immunotherapies through its specific targeting of M2 TAMs which facilitate tumour growth, while leaving intact the M1 TAMs that support immune activation against tumours.

Preclinical toxicity studies of Clevegen commenced as planned in 2017, following successful production of technical batches by our manufacturing partner Abzena and initial data indicate no signs of serious adverse events. In April 2017, the Company signed an agreement with the University of Birmingham Medical School, UK, to initiate a liver cancer clinical trial program, focused on the protocol design for a Phase I/II trial MATINS (Macrophage Antibody To INhibit immune Suppression), which was also reviewed by the UK regulatory authority (MHRA) and discussed at the January 2018 meeting. Based on the MHRA positive feedback the Company anticipates filing the clinical trial application (CTA) in H2 2018.

Faron also continues a close collaboration with the MediCity unit of Turku University Medical School, where Faron has sponsored a set of Clevegen related preclinical experiments. Data reported at the international Juselius Symposium (June 2017, Helsinki, Finland) demonstrated how genetic depletion of macrophage Clever-1 resulted in tumour growth resistance and prevented the spread of Lewis lung cancer in preclinical models. Furthermore, signs of strong immune activation were observed, as evidenced by CD8 positive T-cells at the tumour site, in line with the expected effect of Clevegen. Additional data were also outlined during Faron's second R&D day in February 2018.

Corporate

In December 2017, Faron announced the appointment of Dr Juhana Heinonen as Chief Commercial Officer. Dr Heinonen joined Faron from AstraZeneca where he served as the Global Marketing Director for AstraZeneca/Medimmune's Fasenra (benralizumab) for the treatment of asthma, the first biologic launched from the AstraZeneca respiratory unit. Dr Heinonen led the global market shaping and the patient and healthcare professional support strategy development for the new monoclonal antibody, which met the primary endpoints in two Phase III clinical trials in 2016. Prior to this, he held a variety of positions in sales and marketing at Roche between 2008 and 2015, successfully leading the launch and development of a global marketing strategy for the blockbuster treatment for rheumatoid arthritis, RoACTEMRA (tocilizumab).

Dr Juho Jalkanen was appointed as Vice President of Business Development in April 2017 and stepped down from the Board in May 2017, of which he had been a member since 2013. Dr Jalkanen has a Master's degree in Economics and Business Administration from the Turku School of Economics, a Medical Doctor's degree from the University of Turku and was a fully licensed General Practitioner and specialist in Vascular Surgery with expertise in organ protection during major cardiovascular surgery. I extend my gratitude to Juho for his contribution to the Board over the past four years and am pleased he will continue his input to the Company as a management team member.

Financial

The Company has adopted new and amended accounting standards and corrected certain prior period errors in accounting. The 2016 financial statements, as initially reported, have therefore been amended and restated.

Strengthened Board

Dr. Gregory B. Brown and Mr John Poulos were appointed as Non-Executive Directors to the Board in May 2017. Both bring a wealth of global experience in the life sciences and investment community to strengthen our Board, particularly from a US and commercial angle.

Dr. Gregory B. Brown has more than 35 years of experience in healthcare and investment. Most recently, Greg founded HealthCare Royalty Partners, a healthcare-focused private asset management firm investing in biopharmaceutical and medical products, where he currently serves as Vice Chairman. In addition, Greg is currently a director of Caladrius Biosciences Inc (NASDAQ) and Nuron Biotech Inc and previously acted as a director of Invuity Inc (NASDAQ) between October 2014 and December 2015. Prior to this, he was a General Partner at Paul Capital Partners in New York, Co-Head of Investment Banking at Adams, Harkness & Hill, and VP of Corporate Finance at Vector Securities International.

Mr John Poulos has a wealth of expertise in global corporate life sciences, having spent 38 years working for AbbVie and Abbott. Most recently, John served as Vice President, Head of Licensing and Acquisitions for AbbVie, and Group Vice President, Head of Pharmaceutical Licensing and Acquisitions for Abbott Pharmaceuticals. During his career, John was instrumental in the negotiation of numerous acquisitions, including Knoll/BASF Pharma in 2001 for $6.9 billion and Solvay in 2010 for $6.2 billion.

Outlook

Our immediate focus in 2018 will be on determining the next steps for Traumakine in ARDS once we have completed a comprehensive review of the INTEREST Phase III data to understand why Traumakine did not have any effect over placebo in the trial. We also plan to continue to progress our immuno-oncology candidate, Clevegen, into the clinic in H2 2018.

Board of Directors

The Board anticipates the following pipeline progress and catalysts during 2018:

Traumakine:

- Full data analysis from the Phase III INTEREST trial
- Determine next steps for Traumakine in ARDS
- The Company currently expects to announce top-line data from the Japanese Phase III pivotal study for the treatment of ARDS with Traumakine, run by its Japanese licensing partner Maruishi Pharmaceutical Co., in 2018.

Clevegen:

- Faron expects preclinical toxicological studies for Clevegen to be completed in Q2 2018
- The Company expects to file the first CTA with the UK regulatory authorities (MHRA) in H2 2018 based on the preclinical safety data. The first, and primarily safety focused clinical trial is expected to be conducted with liver cancer patients at the Birmingham University Liver Cancer Centre and is expected to continue into a Phase II study via an adapted trial design for HCC patients to recognise early efficacy signals.
- The second set of clinical cancer trials will be conducted in parallel with the HCC trial in Scandinavia with melanoma, pancreas and ovarian cancer patients.
- Faron intends to expedite the expansion of its planned Clevegen clinical development program, the MATINS trial, in several solid tumours (liver, pancreas, ovarian and melanoma) in order to obtain accelerated safety and clinical data read-outs.

Management team

STRATEGIC REPORT

Financial Review

Restatement of previously issued financial statements

Subsequent to the original issuance of the Company's financial statements for the year ended 31 December 2016, the Company has adopted new and amended accounting standards and corrected certain prior period errors in its accounting. The 2016 financial statements, as initially reported, have therefore been amended and restated. The total impact of the restatements on the pre-tax income for periods prior to 31 December 2016 was negative EUR 2.5 million. In total the restatements reduced the 31 December 2016 equity with negative EUR 2.5 million.

Further details of the restatement are set out in Note 1 to the accounts.

Key Performance Indicator

As a clinical stage drug development company, Faron's primary interconnected KPI's are cash burn and cash position. During 2017, the Company's net cash flow decreased by only €1.7 million despite a significant increase in R&D spending. This was mainly due to two successful fundraisings during the year. The Board will consider the appropriateness of monitoring additional KPIs as the Company's operations advance.

Revenue and Other Operating Income

The Company's revenue was €0.0 million for the year ended 31 December 2017 (2016: €1.0 million). The revenue in 2016 included the €0.7 million licence agreement cash signing fee from Korean license partner PharmBio. The Company also recorded €1.5 million (2016: €1.0 million) of other operational income. This comprised of income recognised from the European Commission FP7 grant in support of the Traumakine programme as well as a grant component from public loans.

Research and development costs

The R&D costs more than doubled by €9.9 million (107%) from €9.2 million to €19.1 million. This was a result of very strong investment in the finalisation of the INTEREST trial. The trial completed recruitment in early December 2017 with results reported in May 2018. The increased activity of Clevegen development also contributed to the increase in R&D investment. In September 2017, the Company received a positive recommendation from the FDA regarding the possibility to proceed directly to BLA filing in the US upon successful completion of the European and Japanese Phase III trials without the need to conduct clinical trials for Traumakine in the US. In view of this recommendation and in anticipation of a positive INTEREST trial the Company accelerated the preparatory work for eventual Traumakine launch, including increasing production of active pharmaceutical ingredient (API), with the majority of this work to be completed 2018.

Share-based Compensation

During the year, options over 500,000 ordinary shares (2016: 400,000) were awarded to Directors and key personnel. This had no cash impact on the results for the year, however, accounting standards require this share based compensation to be recognised in the Consolidated Statement of Comprehensive Income, resulting in a charge of €1.2 million (2016: €0.9 million).

Taxation

The Company's tax credit for the fiscal year 2017 can be recorded only after the Finnish tax authorities have approved the tax report and confirmed the amount of tax-deductible losses for 2017. The total amount of cumulative tax losses carried forward approved by tax authorities on 31 December 2017 was €23.5 million (2016: €14.2 million). The Company estimates that it can utilise €23.3 million of these during the years 2019 to 2026 by offsetting them against future profits. In addition, Faron has €2.8 million of research and development costs incurred in the financial years 2010 and 2011 that have not yet been deducted in its taxation. This amount can be deducted over an indefinite period at the Company's discretion.

Losses

Loss before income tax was €21.1 million (2016: €10.1 million). Net loss for the year was €21.1 million (2016: €10.1 million), representing a loss of €0.76 per share (2016: €0.42 per share) (adjusted for the changes in number of issued shares).

Cash Flows

Despite doubling its R&D expenses net cash outflow was only €2.2 million negative for the year ended 31 December 2017, compared to a positive net cash inflow of €0.4 million for the previous year. Cash used for operating activities increased by €9.0 million to €18.4 million for the year, compared to €9.4 million for the year ended 31 December 2016. This increase was mostly driven by a €9.9 million (107%) increase in R&D investment together with a €0.6 million (24%) increase in administrative costs.

Net cash inflow from financing activities was €16.6 million (2016: €9.3 million) due to the two successful equity placings completed during the year.

Fundraising

Faron raised £5million (net €5.4 million) via an oversubscribed financing round in February/March 2017 by issuing 1,422,340 new ordinary shares at a price of 350 pence per share. The proceeds are being used to fund preclinical and early clinical development of Clevegen. The Company also raised £10 million (net €10.4 million) via an oversubscribed financing round in October 2017 by issuing 1,250,000 new ordinary shares at a price of 800 pence per share. The proceeds are being used to support the pre-launch activities for Traumakine and to expedite Clevegen clinical program. Post the period end, Faron also raised £15.0 million (net €15.9 million) in February 2018 via an oversubscribed financing round by issuing 1,863,350 new ordinary shares at a price of 805 pence per share to support preparations for the commercialisation of Traumakine and to advance the clinical development of Clevegen in several indications. After this round, at the end of February 2018, the total number of outstanding shares was 31,027,894.

Financial Position

As at 31 December 2017, total cash and cash equivalents held were €9.3 million (2016: €11.5 million). This excludes the funds raised in the financing round announced on 21 February 2018. The cash at end of March 2018 was €18.7 million. The board will be focussing on reducing cash burn and preservation of existing resources until the full data analysis is complete and it is agreed how best to deliver value to shareholders.

Headcount

Average headcount of the Company for the year was 18 (2016: 10). The increase in headcount is attributable to the expansion of the Traumakine and Clevegen programs, in addition to preparation for the commercialisation of Traumakine.

Shares and Share Capital

Using the share authorities granted at the Annual General Meetings held on 26 May 2016 and on 16 May 2017, in February 2017 the Company issued 1,422,340 new ordinary shares at a subscription price of £3.50 pursuant to a fundraising and in October 2017 issued 1,250,000 new ordinary shares at a price of £8.00 per share pursuant to a further fundraise. The subscription price was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased.

Additionally during 2017, warrants over 109,800 ordinary shares in the Company were exercised at a price of €1.55 per share and further warrants over 41,600 ordinary shares in the Company were exercised at a price of €2.01 per share.

In May 2017 options over 15,000 ordinary shares in the Company were exercised at a price of €3.71 per share and options over a further 14,100 ordinary shares in the Company were exercised at a price of €2.90 per share.

The Company has no shares in treasury; therefore at the end of 2017 the total number of voting rights was 29,164,544.

Money Raised to Date

To date, the Company has been funded with a total of approximately €61 million, made up of a combination of equity, debt and grant funding, which has been used to develop the Company's products and intellectual property. The Company has also generated cash revenues of €4.5 million to date through the receipt of milestone payments pursuant to certain of its licensing arrangements and the sale of surplus raw materials.

Yrjö E K Wichmann
Chief Financial Officer
May 5, 2018

STRATEGIC REPORT

Risks and Uncertainties

Faron is a late clinical stage biopharmaceutical company and, in common with other companies operating in this field, is subject to a number of risks and uncertainties. The principal risks and uncertainties identified by Faron for the year ended 31 December 2016 are below.

Research and Development

Faron's main product is in the late stages of clinical development however may not be successful in the clinical trials and may not be able to develop approved or marketable products. Technical risk is also present at each stage of the discovery and development process of other, earlier stage products with challenges in biology (including the ability to produce candidate drugs with appropriate safety, efficacy and usability characteristics). Additionally, drug development is a highly regulated environment which itself presents technical risk through the need for study designs and data to be accepted by regulatory agencies. Furthermore, there can be no guarantee that the Company will be able to, or that it will be commercially advantageous for the Company to, monetize the value of its intellectual property through entering into licensing or other co-operation deals with pharmaceutical companies.

Commercial

Faron's industry, being biotechnology and pharmaceutical industries, are very competitive. The Company's competitors include major multinational pharmaceutical companies, biotechnology companies and research institutions. Many of its competitors have substantially greater financial, technical and other resources, such as larger research and development resources and staff. The Company's competitors may succeed in developing, acquiring or licensing drug product candidates that are more effective or less costly than any of the product candidates which the Company is currently developing or which it may develop and may have a material adverse impact on the Company.

Dependence on key personnel and scientific and clinical collaborators

The Company's success is highly dependent on the expertise and experience of the Directors and the key Management. Whilst the Company has entered into employment and other agreements with each of these key personnel, the retention of such personnel cannot be guaranteed. Should key personnel leave or no longer be party to agreements or collaborations with the Company, the Company's business prospects, financial condition and/or results of operations may be materially adversely affected. To develop new products and commercialise its current pipeline of products, the Company relies, in part, on the recruitment of appropriately qualified personnel, including personnel with a high level of scientific and technical expertise. There is currently a shortage of such personnel in the pharmaceutical industry, meaning that the Company is likely to face significant competition in recruitment. The Company may be unable to find a sufficient number of appropriately highly trained individuals to satisfy its growth rate, which could affect its ability to develop as planned.

Regulatory environment

The Company operates in a highly regulated environment. Whilst the Company will take every effort to ensure that the Company and its partners comply with all applicable regulations and reporting requirements, there can be no guarantee of this. Failure to comply with applicable regulations could result in the Company being unable to successfully commercialise its products and/or result in legal action being taken against the Company, which could have a material adverse effect on the Company.

The Company will need to obtain various regulatory approvals (including from the FDA and the EMA) and comply with extensive regulations regarding

safety, quality and efficacy standards in order to market its products. While efforts have been and will be made to ensure compliance with governmental standards and regulations, there is no guarantee that any product will be able to achieve the necessary regulatory approvals to promote that product in any of the targeted markets and any such regulatory approval may include significant restrictions for which the Company's products can be used. In addition, the Company may be required to incur significant costs in obtaining or maintaining its regulatory approvals. Delays or failure in obtaining regulatory approval for products would likely have a serious adverse effect on the value of the Company and have a consequent impact on its financial performance.

Intellectual property and proprietary technology

The Company relies and will rely on intellectual property laws and third party non-disclosure agreements to protect its patents and other proprietary rights. The IPR on which the Company's business is based is a combination of patent applications and confidential business know-how. No assurance can be given that any currently pending patent applications or any future patent applications will result in patents being granted. In addition, there can be no guarantee that the patents will be granted on a timely basis, that the scope of any patent protection will exclude competitors or provide competitive advantages to the Company, that any of the Company's patents will be held valid if challenged, or that third parties will not claim rights in, or ownership of, the patents and other proprietary rights held by the Company.

Despite precautions taken by the Company to protect its products, unauthorized third parties may attempt to copy, or obtain and use the Company's IPR and other technology that is incorporated into its pharmaceutical products. In addition, alternative technological solutions similar to the Company's products may become available to competitors or prospective competitors of the Company. It should be noted that once granted, a patent could be challenged both in the relevant patent office and in the courts by third parties. Third parties can bring material and arguments, which the patent office granting the patent may not have seen at the time of granting the patent. Therefore, whilst a patent may be granted to the Company it could in the future be found by a court of law or by the patent office to be invalid or unenforceable or in need of further restriction. Should the Company be required to assert its IPR, including any patents, against third parties it is likely to use a significant amount of the Company's resources as patent litigation can be both costly and time consuming. No assurance can be given that the Company will be in a position to devote sufficient resources to pursue such litigation. Any unfavourable outcomes in respect of patent litigation could limit the Company's IPR and activities moving forward.

The Directors do not believe that its lead pharmaceutical drug candidates, future drug candidates in development, and proprietary processes for generating those candidate compounds infringe the IPR of any third parties. However, it is impossible to be aware of all third party intellectual property. The Company's research has included searching and reviewing certain publicly available resources, which are examined by senior levels of management in order to keep abreast of developments in the field.

Financial

The Company has incurred significant losses since its inception and does not have any approved or revenue-generating products. The Company expects to incur losses for the foreseeable future, and there is no certainty that the business will generate a profit. The Company may not be able to raise additional funds that will be needed to support its product development programs or commercialisation efforts, and any additional funds that are raised could cause dilution to existing investors.

Operational

The Company's development and prospects depend to a significant degree on the experience, performance and continued service of its senior management team including the Directors. The Company has invested in its management team at all levels. The Directors also believe that the senior management team is appropriately structured for the Company's size and is not overly dependent upon any particular individual. The Company has entered into contractual arrangements with these individuals with the aim of securing the services of each of them. Retention of these services or the identification of suitable replacements, however, cannot be guaranteed. The loss of the services of any of the Directors or other members of the senior management team and the costs of recruiting replacements may have a material adverse effect on the Company and its commercial and financial performance and reduce the value of an investment in the Ordinary Shares.

This report was approved by the Board on 5 May 2018 and signed on its behalf.

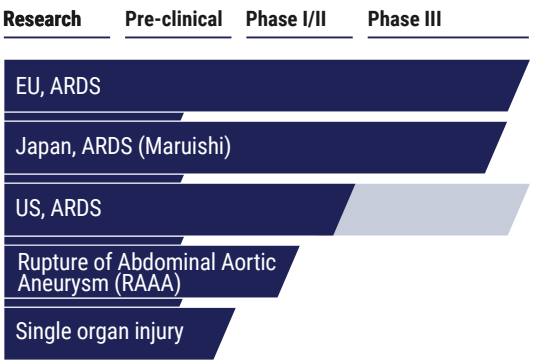
PIPELINE

Revolutionising the treatment of ARDS and activation of tumour immunity

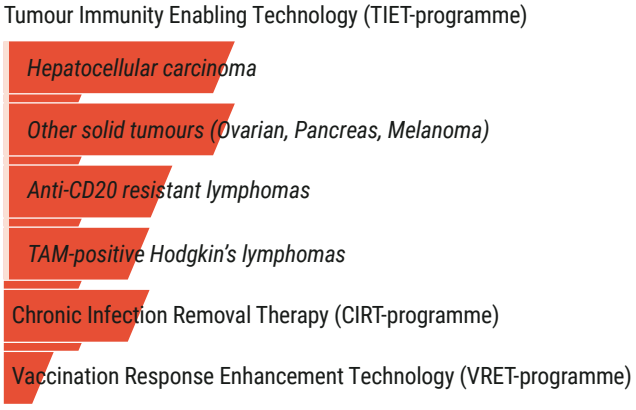
Faron has identified several molecular mechanisms involved in the control of endothelial functions as a source of innovation. The Company currently has a pipeline focusing on acute organ traumas, cancer immunotherapy and vascular damage.

The fast evolving Faron pipeline consists of drug candidates (FP-1201-lyo and FP-1305) from two major Faron programmes – Traumakine and Clevegen, respectively. The lead indication of the Traumakine programme is Acute Respiratory Distress Syndrome (ARDS). This and the other indications (prevention of MOF after a ruptured of abdominal aortic aneurysm RAAA) are all based on the same Chemistry and Manufacturing Controls (CMC) dossier sections, allowing fast protocol adjusted filing for indication expansion. Similarly, Clevegen indications utilise one common dossier with a protocol adapted to each indication.

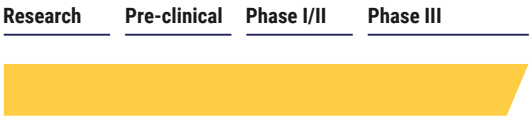
Traumakine® is Faron's spearhead project



Clevegen®



D-ARDS



PIPELINE: TRAUMAKINE®

Acute Respiratory Distress Syndrome (ARDS)

Faron´s lead candidate, Traumakine, addresses the treatment of Acute Respiratory Distress Syndrome (ARDS), a severe, orphan lung disease. Currently there is no pharmaceutical treatment for this condition with a reported mortality rate of 30 to 45%. The scientific rationale for Traumakine treatment is based on the use of interferon-beta for the restoration of the endothelial barrier function in ARDS patients.

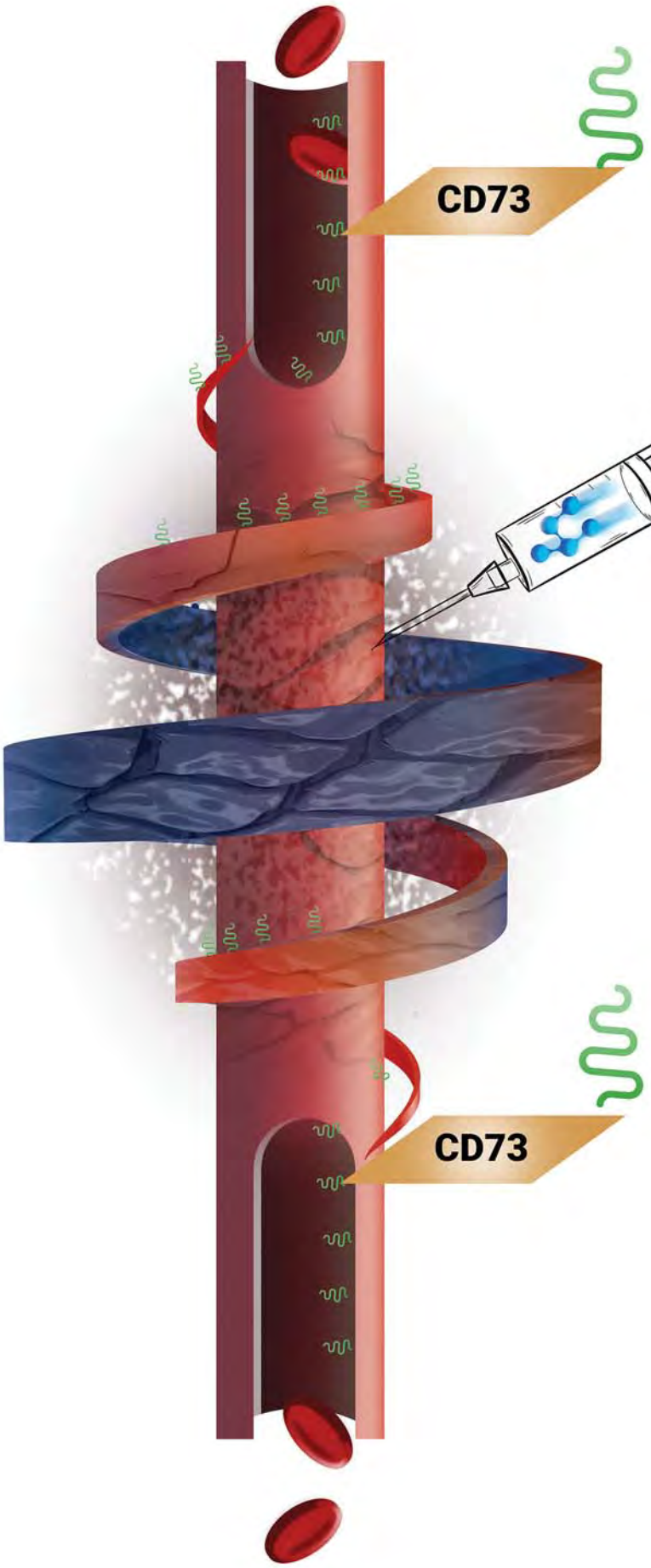
"ARDS is the leading cause of respiratory failure in intensive care unit patients requiring mechanical ventilation."

ARDS is a life-threatening medical condition characterised by widespread inflammation in the lungs and sudden failure of the respiratory system. ARDS causes inflammation of the alveoli in the lungs which become unable to perform the normal oxygenation of blood. It is characterised by rapid breathing, difficulty getting enough air into the lungs and low blood oxygen levels. Common causes of ARDS include sepsis, pneumonia, aspiration of fumes, food or stomach contents going into the lung or significant trauma. The condition was first described in 1967 and gained wide attention during the Vietnam War when it was nicknamed "white lung" as X-rays presented the lungs of the patients as white.

ARDS is the leading cause of respiratory failure in intensive care unit patients requiring mechanical ventilation. Despite progress in critical care medicine, ARDS is currently associated with a mortality rate of 30 to 45% depending on the severity of the condition. Although ARDS mortality has decreased in the last decade due to improvements in supportive care and in the treatment of the underlying conditions, it still remains high. Currently, patients suffering from ARDS are generally treated with lung-protective mechanical ventilation. This treatment is accompanied by ancillary support such as positioning, fluid management and food restrictions. Extra corporeal support may also be provided depending on the severity of the condition. Complications which can also arise whilst a patient is being treated for ARDS include the development of infections, pneumothorax, lung scarring and blood clots which can develop into a pulmonary embolism. Patients who recover from ARDS often suffer other consequences of the condition after being discharged from the intensive care unit. A recovering patient's quality of life may be adversely affected by permanent damage to the lungs, respiratory problems, scar tissue, muscle weakness, depression and post-traumatic distress syndrome, all of which can have an adverse effect on the patient's quality of life.

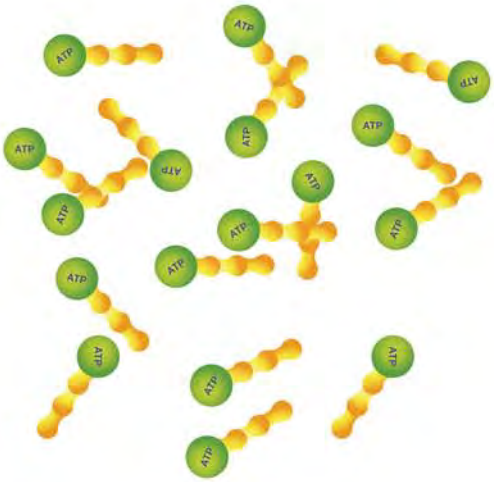
ARDS

- **A severe, life-threatening medical condition, most often as a result of sepsis, pneumonia or significant trauma**
- **Orphan lung disease with no available drug treatment**
- **The leading cause of respiratory failure in intensive care unit patients who require mechanical ventilation**
- **Annual ARDS incidence in Europe is c. 125,000 and in the US c. 200,000 patients**
- **High mortality rate of 30 to 45% and survivors suffer long-term mental and physical problems**

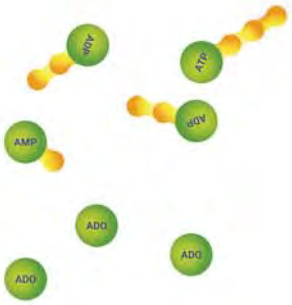


CD73 ectoenzyme produces local anti-inflammatory adenosine

Interferon-beta upregulates expression CD73

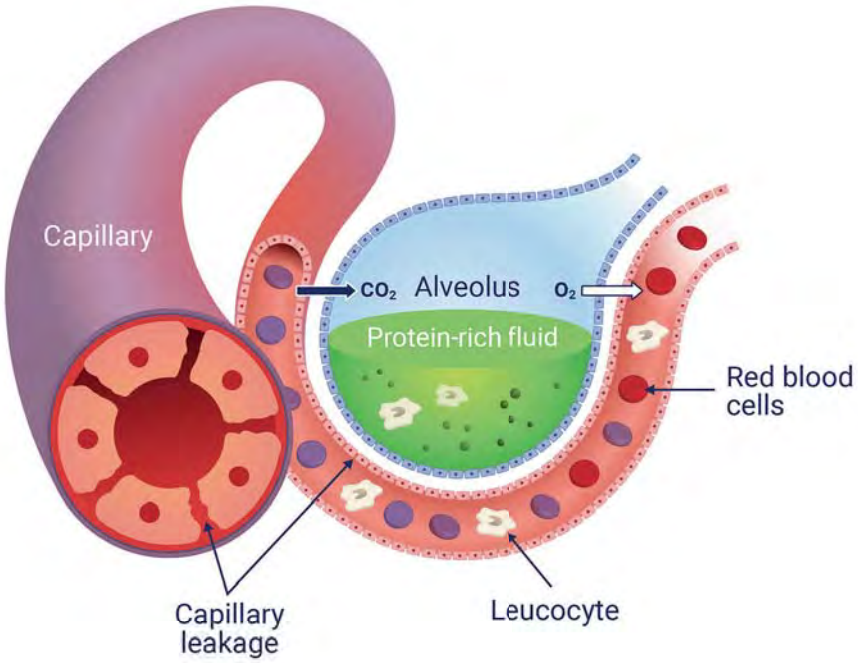


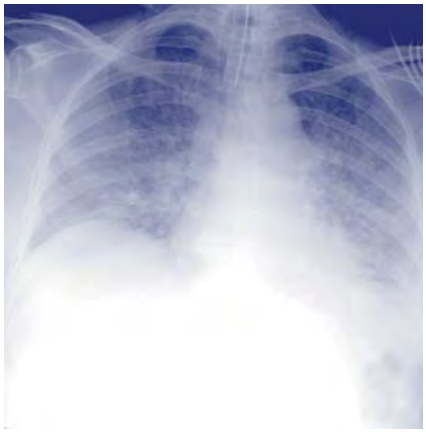
Loss of CD73 results in high amounts of proinflammatory ATP



Inflammation reduces CD73 amounts and its adenosine production

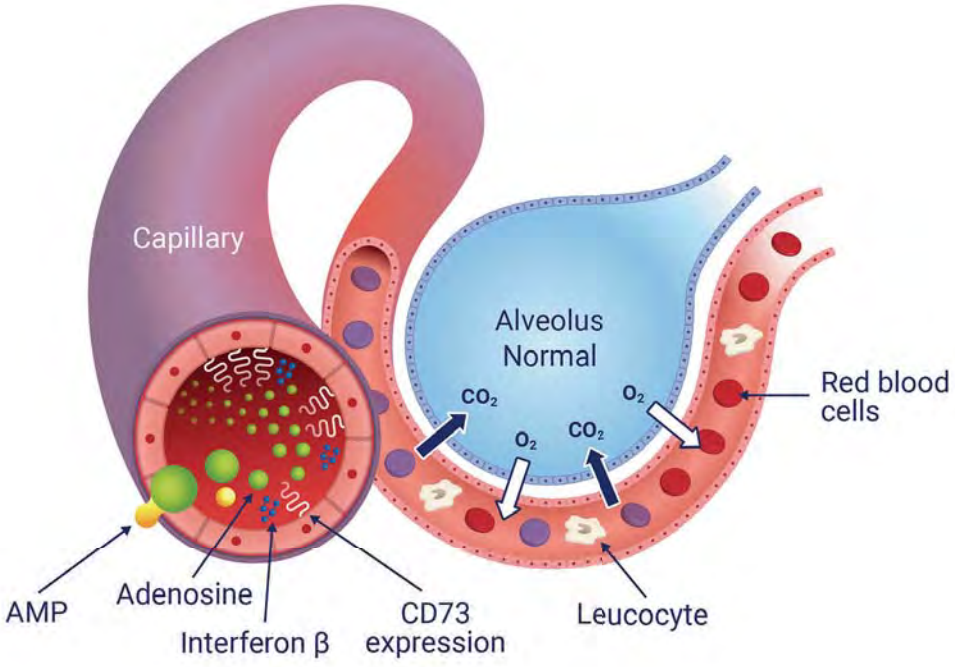
ARDS lung

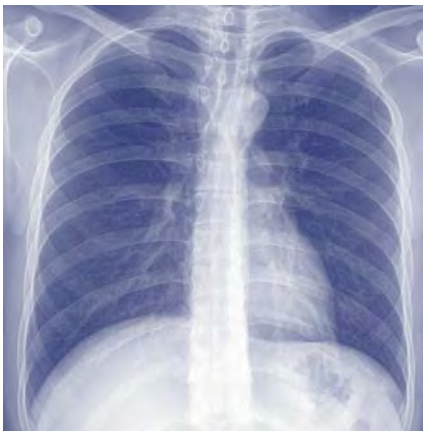




Widely used X-ray pictures can reveal lungs filled with blood material. This shows up as white dense material in lung air space and for this reason the lungs of these patients are often called "white lungs". Typically this picture confirms that the patient has a condition called Acute Respiratory Distress Syndrome (ARDS) and has a life-threatening disease.

Normal lung





Normally functioning lung X-ray shows no "white" material, indicating that lung air space is free of blood material, in contrast to the ARDS lungs above. Long term exposure to a respiratory syndrome like ARDS, can also cause permanent loss of lung capacity due to a fibrotic process that replaces lung alveoli with scar tissue. This serious side effect of ARDS results in permanently reduced respiratory capacity.

Treating ARDS

Supply of oxygen and nutrients to individual cells of various organs are maintained by vasculature and especially by the long and thin blood vessels called capillaries. Their integrity is sustained by endothelial cells covering the inner surfaces of these vessels forming a barrier between circulation and tissues. The breakdown of this barrier results in leakage of blood content to tissues. If this happens in lungs, the lung air space is filled with protein-rich fluid and blood cells preventing normal gas exchange.

The key molecule involved in maintaining endothelial barrier and lung function is CD73, an endothelial ectoenzyme, which can produce local adenosine. Traumakine's active pharmaceutical ingredient, interferon-beta, increases CD73 expression resulting in increased local adenosine. Subsequently, high local adenosine levels reduce capillary leakage and increase lung function by allowing normal gas exchange to return.

Traumakine® Clinical Programme

The first indication that Faron´s lead candidate, Traumakine, addresses is the treatment of ARDS. The scientific rationale for Traumakine treatment is based on the use of interferon beta for the restoration of the endothelial barrier function in ARDS patients. Traumakine (FP-1201-lyo) is based on a patent-protected use of interferon beta to prevent leakage of vascular beds in acute lung injuries. The active pharmaceutical ingredient in Traumakine is recombinant human IFN beta-1a. Traumakine has completed recruitment of a pan-European Phase III trial in respect of the treatment of ARDS. The first patient in the INTEREST Study was enrolled in December 2015 and the study has progressed as planned during 2016-17. The first clinical trial in the Traumakine programme was a phase I/II open-label study to assess the safety, tolerability and preliminary efficacy of interferon beta in the treatment of patients with ARDS. This study consisted of dose escalation (Phase I) and dose expansion (Phase II) phases. In the dose escalation phase, four interferon beta levels were tested. The dose expansion phase was conducted using the optimal tolerated dose. A total of 37 ARDS patients were treated at nine hospitals in the UK with highly encouraging results. Interferon beta was found to be safe and well tolerated in ARDS patients and the optimal tolerated dose was established. The selected pharmacodynamic marker for interferon beta bioactivity showed clear dose response and the treatment target molecule (CD73) levels were induced during the dosing period. Most importantly, interferon beta treatment significantly reduced the all-cause mortality at day 28, the primary end point of the study, compared to the control cohort1. Traumakine was associated with an 81% reduction in odds of 28-day mortality. Comparable results were obtained from Traumakine Phase II Japanese study conducted by Faron´s Japanese licensing partner, Maruishi Pharmaceutical Co., Ltd. in Japan, as announced in January 2016.

Phase III INTEREST Study

The Phase III INTEREST trial was a double-blind, randomised, parallel-group comparison of efficacy and safety of interferon beta and placebo in the treatment of patients with moderate to severe ARDS. The study was conducted in 60 hospitals across Belgium, Finland, France, Germany, Italy, Spain and the UK and 301 ARDS patients were recruited. INTEREST has received €6 million funding from the European Union Seventh Framework Programme (FP7). Mechanism of Action The mechanism behind Traumakine's action was invented by scientists at Turku University during the period 1995 to 2003. Through extensive research and ex-vivo studies, it was identified that a molecule called CD73 is essential in maintaining the endothelial barrier function. CD73 is an ectoenzyme capable of breaking down extracellular AMP to produce locally active adenosine. Adenosine maintains the endothelial barrier and downregulates inflammation escalation, preventing both early vascular leakage and escalation of inflammation, which are the two early patho-physiological events leading to ARDS. One of the key findings that led to the development of Traumakine, was a discovery that interferon-beta could enhance CD73 expression and could therefore, be used to treat a range of vascular leakage conditions including ARDS. Traumakine works by enhancing CD73 expression in the lungs and increasing production of anti-inflammatory adenosine such that vascular leaking and escalation of inflammation are reduced.

"Traumakine (FP-1201-lyo) is based on a patent-protected use of interferon-beta to prevent leakage of vascular beds in acute lung injuries."

[1] Bellingan et al. (2014). The effect of intravenous interferon-beta-1a (FP-1201) on lung CD73 expression and on acute respiratory distress syndrome mortality: an open-label study. The Lancet Respiratory Medicine 2014: 2: 98-107.

PIPELINE: TRAUMAKINE®

The INTEREST Study

The INTEREST Study (protocol FPCLI002) is a Phase III clinical study to investigate efficacy and safety of FP-1201-lyo (recombinant human interferon- beta-1a) in patients with moderate or severe ARDS. This study was designed based on previous results from the UK clinical trial which demonstrated a significant reduction in mortality of ARDS patients and has been published in the Lancet Respiratory Medicine[1]. In the double-blinded and randomised INTEREST study pivotal effectiveness and safety of FP-1201-lyo was compared to placebo. Both treatment groups also received standard supportive care. The primary objective of the INTEREST Study was to demonstrate the efficacy of FP-1201-lyo in improving the clinical course and outcome based on survival and need for mechanical ventilation in patients with moderate or severe ARDS. Other study objectives were to assess the safety and efficacy of FP-1201-lyo compared to placebo, in regard to mortality, organ failure, need for mechanical ventilation and vasoactive support, length of the stay in ICU and hospital as well as quality of life and pharmacoeconomic parameters. In total, approximately 60 hospitals in seven countries within the European Union – Belgium, Finland, France, Germany, Italy, Spain, UK – participated in the INTEREST Study. INTEREST has received funding from the European Union Seventh Framework Programme (FP7) under the Traumakine project name. The patients enrolled in the study were screened from patients who had been admitted to intensive care units (ICU) at participating hospitals. To further ensure appropriate patient enrolment into the study across all hospitals, the study design incorporated an eligibility process via the electronic data capture system, involving an independent medical monitor. After all screening procedures were successfully performed, and eligibility for inclusion in the study was confirmed, the patient was randomised into the study. Following randomisation, the patients were treated daily with either FP-1201-lyo 10 µg or placebo for 6 days and underwent daily assessments while in the ICU for a maximum of 28 days. The patients were followed up at 3, 6 and 12 months after enrolment. Information on the need for ventilator support, as well as the need for hospital and ICU care, was collected during this follow-up period. Other collected data included e.g. respiratory and neurological functions and quality of life. The main analysis and clinical study report will be written on the data from the 6 months long-term follow-up. The data from the extended follow-up period from 6–12 months will be reported separately in an addendum to the clinical study report.

[1] Bellingan et al., 2014

Safety Monitoring

An Independent Data Monitoring Committee was established in order to monitor safety in this study. This safety review committee has periodically conducted an independent unblinded review of safety data generated during the study and provided five recommendations during 2016-17 to continue the study as planned.

The study also has an esteemed Steering Committee that provides expert scientific and clinical guidance to the practical study design and conduct. The rights, safety and well-being of the patients are the basis for all considerations.

More details on the study can be found on www.clinicaltrialsregister.eu (reference EudraCT No. 2014-005260-15) and clinicaltrials. gov (reference NCT02622724). The mode of action of FP-1201-lyo is described on the video found at Faron web pages (www.faron-pharmaceuticals.com).

INTEREST Study

- **Pivotal Phase III trial for Traumakine in development for the treatment of ARDS.**
- **Conducted in 60 ICUs (Intensive Care Units) in seven European countries.**
- **300 adult patients with moderate to severe ARDS were enrolled in the study.**
- **First patient enrolled in December 2015.**
- **The last patient was recruited in December 2017.**

INFORAAA trial initiation

Ruptured Abdominal Aortic Aneurysm (RAAA) is a surgical emergency with an overall mortality of up to 80%. It requires immediate surgery and aortic repair. Approximately half of the deaths of RAAA patients are due to not reaching the hospital in time, and, despite immediate surgery and intensive care treatment, the second half die in hospital within 30 days post-operatively, mostly due to multi-organ failure. The cause of high post-operative mortality is mainly due to prolonged hypotension/hypoxia from the ruptured aorta and the aftermath of restoring blood flow: reperfusion, vascular leakage and failure of vital organs. Currently, there are an estimated 20,000 US and European patients per annum eligible for treatment.

The high mortality rate of RAAA, which accounts for 4-5 deaths per 100,000 population[2], requires new treatments to prevent post-operative reperfusion injury leading to the death of RAAA patients, which exhibits a 30-50% mortality rate post-operatively. RAAA accounts for 13-14/100,000 hospital admissions annually[3], and is the second indication for Traumakine targeted by Faron.

Open surgical aortic repair to treat RAAA patients is associated with a Systemic Inflammatory Response Syndrome (SIRS) affecting vital organs, especially the heart, lungs, kidneys, and intestines. The death of approximately 80% of the operated RAAA patients is caused by MOF, similar to patients with ARDS. Traumakine (FP-1201-lyo) is currently in a European Phase III clinical trial for the treatment of ARDS, with encouraging Phase I/II data. The Directors consider that data seen to date supports the rationale for extending the use of Traumakine in similar conditions to potentially treat single, and multiple, organ failures. For example, during the Traumakine phase I/II study, there was a reduced need for haemodialysis (an indication of improved kidney function) among the ARDS patients on Traumakine.

INFORAAA

[1] Bellingan et al., 2014

[2] Karthikesalingam et al., 2014

[3] Anjum et al., 2012

Clevegen can switch immune suppression to immune activation

Many common tumours may be treated with macrophage-directed cancer immunotherapy*	
Liver	782 000 patients / year
Other solid tumours (Ovarian, Pancreas, Melanoma)	809 000 patients / year

*WHO, World Cancer Report 2014

CLEVEGEN

PIPELINE: CLEVEGEN®

One of Faron's key areas of focus is to develop a cancer treatment which supports the hosts' immune defences against tumours, as these are often suppressed in cancer patients. Our second most advanced drug development project, Clevegen, revolves around a common lymphatic endothelial and vascular endothelial receptor-1 (CLEVER-1).

Clever-1 an immuno switch molecule

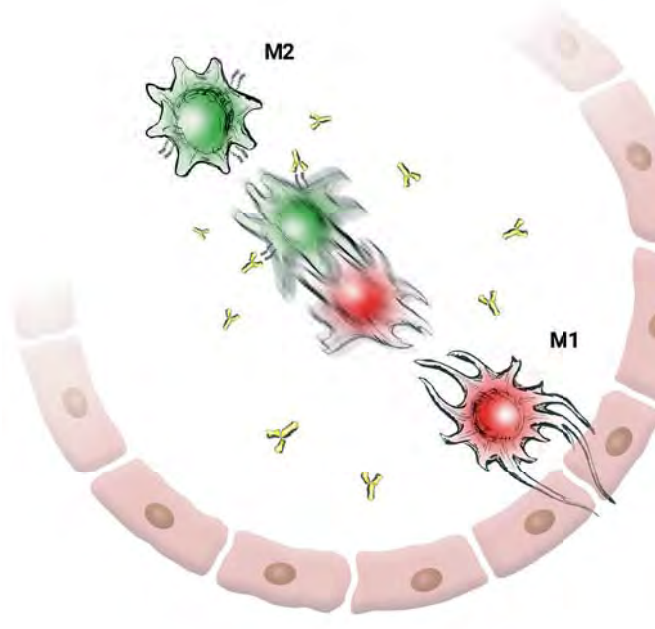
CLEVER-1, also known as Stabilin-1, is a large glycoprotein, which originally was described to function as a scavenging receptor and an adhesion molecule. Its intracellular part regulates the recycling of the receptor between the cell surface and intracellular compartments. CLEVER-1 is present on lymphatic vessels and is induced on a subpopulation of type 2 (immunosuppressive) macrophages during their polarization. It is induced on cancer vasculature. Moreover, its expression on tumour-associated macrophages is a sign of poor prognosis in colorectal cancers of advanced stage. More recently, it has become very clear that CLEVER-1 maintains the immunosuppressive phenotype of tumour associated macrophages (TAMs). Blocking or silencing of CLEVER-1 on human macrophages induces MHC expression and promotes IFN-γ production in human leukocyte cultures. Genetic disruption or pharmaceutical inhibition of CLEVER-1 attenuates tumour progression in mice. The active pharmaceutical ingredient of Clevegen is a humanised anti-Clever-1 antibody, which modulate Clever-1 function to switch the immunosuppressive M2 macrophages to immune stimulating M1 macrophages.

Mechanism of Action

All tumours are infiltrated by immune cells, for example macrophages, neutrophils, T cells, dendritic cells, mast cells, myeloid derived suppressor cells and natural killer cells. Depending on the immune cell content and the activation status of the immune cells, they can either protect the host through suppression of tumour growth and elimination of tumour or harm the host by promoting tumour growth, invasion, metastasis and angiogenesis. Tumour associated macrophages (TAMs) have emerged as an essential constituent of the tumour environment. TAMs can promote tumour progression directly by inducing cancer cell proliferation and survival as well as indirectly via the surrounding elements by stimulating angiogenesis or help in escaping from antitumour specific immunity. When TAMs populate a tumour, one of the very significant influences they exert over it is a strong increase in immuno-

Clever-1-positive TAMs represent one major macrophage population involved in the elimination of host immune activity against the tumour cells.

Clevegen switches immune suppressive type 2 (M2) macrophages to immune stimulating (M1) macrophages and provides new ways to stimulate host immune system to fight cancer.



suppression. Clever-1-positive TAMs represent a major macrophage population involved in the elimination of host immune activity against the tumour cells. Clevegen is an anti-Clever-1 antibody which targets Clever-1-positive TAMs in cancer patients and converts these highly immunosuppressive type 2 "healing" macrophages (M2) to type 1 "pro-inflammatory" macrophages (M1).

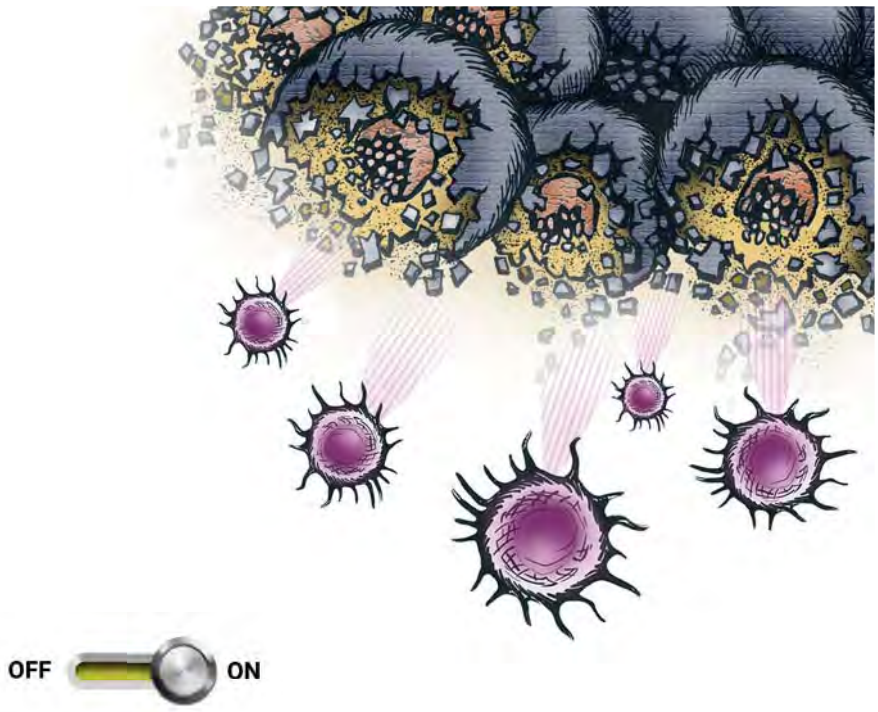
Clevegen also prevents TAM infiltration into a tumour and therefore blocks their accumulation at tumour sites and can, therefore, also control the tumour content of regulatory T-cells, which are dependent on M2 macrophage support. Inhibition of CLEVER-1 alters IFN-gamma production in immune cells and reduces the number of regulatory T-cells within the tumour. Expansion of Clevegen's use, to include removal of local immune suppression in chronic infections and vaccination sites, are also being explored alongside tumours. These platforms are called CIRT, VRET and TIET, respectively and are all based on the same anti- Clever-1 antibody.

Blocking TAM infiltration into a Tumour

Tumour endothelial cells are Clever-1 positive and when anti-Clever-1 antibodies bind to the Clever-1 receptor, the infiltration of TAMs is prevented. Through blocking the infiltration of TAMs into the tumour, the ability of the tumour to suppress the hosts' immune system is reduced.

Change in Tumour Immunity

Anti-Clever-1 antibodies change the tumour immunity by lowering the presence of tumour supportive TAMs in the tumour. This will allow other immune cells to attack tumour cells and drive them to programmed cell death (apoptosis). In some tumours up to 50% of the tumour mass may contain immunosuppressive TAMs and the only way to eliminate this dominance is remove them from tumours and/or convert them to stimulate other cells of the immune system. It is these highly immunosuppressive CLEVER-1 positive TAM cells that are the main target of the Clevegen programme.



Anti-Clever-1 antibodies switch innate immune system to adaptive one and allow other immune cells to attack tumour cells and drive them to programmed cell death (apoptosis).

About Tumor Immunity Enabling Technology (TIET)

The TIET technology is built around the humanised anti-Clever-1 antibody FP-1305, which binds to a specific Clever-1 proprietary epitope. Clevegen binds to this epitope, activating conversion of type 2 tumour associated macrophages to type 1 macrophages, resulting in the transformation of the tumour environment from immunosuppression to activation of the immune system. As the TIET technology is based on a humanised antibody, the Faron Directors believe it can be combined with a number of other immunotherapies without a significant risk of increased adverse events. The TIET technology could provide a significant boost for the efficacy of other immune checkpoint molecules, as its target is unique and represents a completely separate control of immunity.

"In some tumours up to 50% of the tumour mass may contain TAMs and the only way to eliminate this dominance is remove them from tumours."

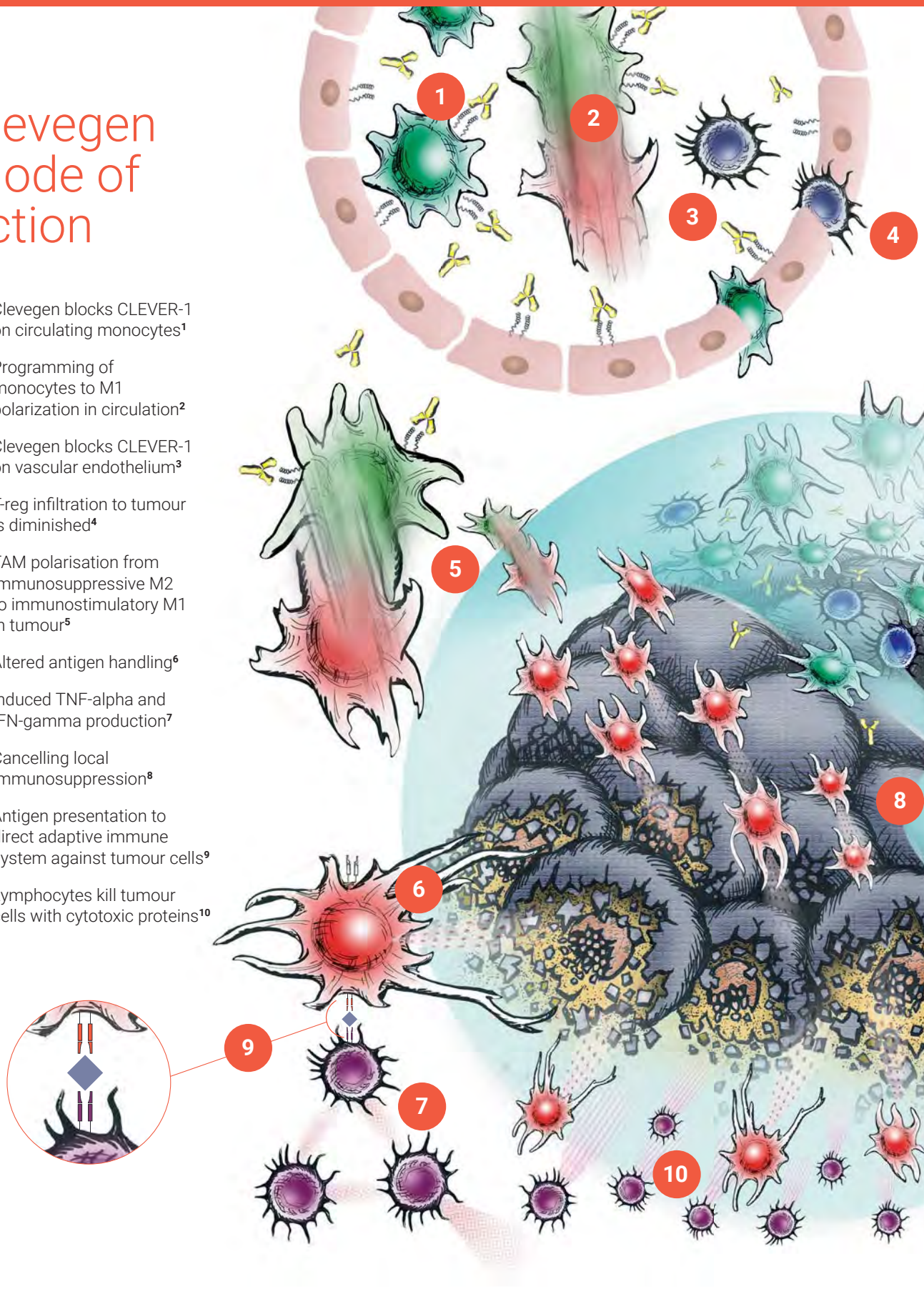
References:

Karikoski et al. (2014) Clever-1/Stabilin-1 controls cancer growth and metastasis. Clin. Cancer Res. 2014: 20: 6452-64.

Palani et al. (2016). Monocyte Stabilin-1 suppresses the activation of Th1 lymphocytes. Journal of Immunology 2016: 196: 115-123.

Clevegen mode of action

1. Clevegen blocks CLEVER-1 on circulating monocytes[1]
2. Programming of monocytes to M1 polarization in circulation[2]
3. Clevegen blocks CLEVER-1 on vascular endothelium[3]
4. T-reg infiltration to tumour is diminished[4]
5. TAM polarisation from immunosuppressive M2 to immunostimulatory M1 in tumour[5]
6. Altered antigen handling[6]
7. Induced TNF-alpha and IFN-gamma production[7]
8. Cancelling local immunosuppression[8]
9. Antigen presentation to direct adaptive immune system against tumour cells[9]
10. Lymphocytes kill tumour cells with cytotoxic proteins[10]



References: 1. Clevegen blocks CLEVER-1 on circulating monocytes (Palani et al. 2016). **2.** Programming of monocytes to M1 polarization in circulation (Palani et al. 2016). **3.** Clevegen blocks CLEVER-1 on vascular endothelium (Irjala et al 2003; Shetty et al 2011). **4.** T-reg infiltration to tumour is diminished (Shetty et al 2011; Karikoski et al 2014). **5.** TAM polarisation from immunosuppressive M2 to immunostimulatory M1 in tumour (Karikoski et al 2014; Palani et al 2016). **6.** Altered antigen handling (Palani et al 2016). **7.** Induced TNF-alpha and IFN-gamma production (Palani et al 2016). **8.** Cancelling local immunosuppression (Karikoski et al 2014; Palani et al 2016). **9.** Antigen presentation to direct adaptive immune system against tumour cells (Karikoski et al 2014; Palani et al 2016). **10.** Lymphocytes kill tumour cells with cytotoxic proteins (Karikoski et al 2014).

Full control of immune mechanisms may help us to convert lethal cancers to treatable conditions. Removal of immunosuppressive elements like type 2 macrophages help to conquer this aim.

CLEVEGEN

Corporate Governance

The Board of Faron emphasises the importance of good corporate governance and is aware of its responsibility for overall corporate governance, and for supervising the general affairs and business of the Company.

Faron is not required to comply with the UK Corporate Governance Code by virtue of being an AIM quoted company. The Board does, however, seek to apply the QCA´s Corporate Governance Code for Small and Medium Sized Companies (as devised by the QCA in consultation with a number of significant institutional small company investors) to the extent that is appropriate and practical for a Company of its nature and size.

CORPORATE GOVERNANCE

Board of Directors

Dr Frank Armstrong

Non-Executive Chairman

Dr Armstrong has held Chief Executive roles with five biotechnology companies (both public and private) including Fulcrum Pharma PLC (AIM). He led Medical Science and Innovation at Merck Serono and was previously Executive Vice President of Product Development at Bayer and Senior Vice President of Medical Research and Communications at Zeneca. Dr Armstrong is currently the Chairman of Summit Therapeutics (AIM and NASDAQ) and Caldan Therapeutics and a Non-Executive Director of and Mereo BioPharma (AIM). He is a member of the Senior Advisory Board at Healthcare Royalty Partners and an SAB Member at Epidarex Capital. Dr Armstrong is a Member of the Court of the University of Edinburgh. Dr Armstrong is a physician and a Fellow of the Royal College of Physicians (Edinburgh).

He was appointed as a Non-Executive Director of the Company in September 2015.

Matti Manner

Non-Executive Vice-Chairman

Mr Matti Manner was appointed as a partner of Brander & Manner Attorneys Ltd in 1980 having previously sat as a judge at Turku Appeal Courts. He has significant experience in national and international business deals, corporate law and mergers and acquisitions having held a number of board memberships throughout his career. Mr Manner joined the Board of the Company as Chairman in 2007 having previously been the Chairman of Faron Ventures Oy from 2002.

He is currently Chairman of Turun Osuuskauppa and Ruissalo Foundation and a member of the board of Marva Media Ltd, Satatuote Ltd, YH VS-Rakennuttajat Ltd, Kauppakeskus Mylly Ltd and Nurmi-Yhtiöt Oy.

Mr Manner has experience of several trustee posts including the Presidency of the Finnish Bar (Lawyers) Association during the period of 1998 to 2004. Mr Manner obtained a Master of Laws from the University of Turku. He became an honorary Chief Justice in Finland in 2013.

Dr Markku Jalkanen

Chief Executive Officer

Dr Jalkanen has more than 25 years of experience within biomedical research, biotech development and the biopharmaceutical industry. He was a founding member of the Company and is the Company´s CEO. In addition to his role as CEO of the Company, Dr Jalkanen is an advisor for the only active Finnish life sciences fund – Inveni Capital. Between 1996 and 2002, Dr Jalkanen was the founding CEO and President of BioTie Therapies Corp which has since become the first publically traded Finnish biotech company to have listed on NASDAQ. Dr Jalkanen has published over 130 peer reviewed scientific publications in various highly ranked international journals and has held several board memberships for both public and private companies.

Dr Jalkanen obtained a Masters in Medical Biochemistry from the University of Kuopio and subsequently received a PhD in Medical Biochemistry from the University of Turku. He completed a side-laudatur examination in Molecular Biology from the University of Turku and completed his post-doctoral training at Stanford University, California between 1983 and 1986. Dr Jalkanen obtained the position of docent in Biochemistry from University of Helsinki and the same qualification in Molecular and Cell Biology from the University of Turku. He became a Professor at the University of Turku in 1992 as well as Head of Turku Centre for Biotechnology.

Dr Gregory B. Brown

Non-Executive Director

Dr. Gregory B. Brown has more than 35 years of experience in healthcare and investment. Most recently, Greg founded HealthCare Royalty Partners, a healthcare-focused private asset management firm investing in biopharmaceutical and medical products, where he currently serves as Vice Chairman. In addition, Greg is currently a director of Caladrius Biosciences Inc (NASDAQ), Cambrex Corporation (NYSE) and Aquestive Therapeutics and previously acted as a director of Invuity Inc (NASDAQ) between October 2014 and December 2015. Prior to this, he was a General Partner at Paul Capital Partners in New York, Co-Head of Investment Banking at Adams, Harkness & Hill, and VP of Corporate Finance at Vector Securities International.

He was appointed as a Non-Executive Director of the Company in May 2017.

Dr Jonathan Knowles

Non-Executive Director

Dr Jonathan Knowles has a career spanning over 40 years in the biotech industry, including founding the molecular biology group within the VTT Biotechnical Laboratory, Helsinki in 1980. He is currently the Chairman of the Genomics England Access committee, the external oversight committee of the Genomics England Initiative and is a visiting Professor at the University of Oxford, a Research Director at FIMM institute in University of Helsinki (2010–2014 FiDiPro Distinguished Professor), and Professor Emeritus at EPFL, Lausanne. He is a member of EMBO.

Dr Jonathan Knowles serves on the boards of a number of biotech companies in Europe and the USA and was the former Chairman of Adaptimmune Therapeutics PLC (NASDAQ) and Immunocore Ltd. Dr Knowles was appointed as the President of Global Research at F. Hoffman-La Roche Ltd and subsequently the President of Group Research. He retired at the end of 2009. Prior to joining Roche, Dr Knowles was the Head of the Glaxo Institute for Molecular Biology in Geneva and subsequently the Research Director for Glaxo Wellcome Europe.

Dr Knowles was appointed as a Non-Executive Director of the Company in September 2015.

Dr Huaizheng Peng

Non-Executive Director

Dr Peng is a General Manager of China Medical System Holdings, a specialty pharmaceutical company listed on the Hong Kong Stock Exchange. He is in charge of international operations for the Company, including pharmaceutical asset acquisition/product licensing-in/out, international business development, outbound investment and asset management, among others. Dr Peng served as an independent Non-Executive Director of China Medical System Holdings Ltd for three years, and the Company was admitted to trading on AIM (between 2007 and 2010). Dr Peng was a partner of Northland Bancorp, a private equity firm. Before that, he worked as a head of life sciences and as a director of corporate finance at Seymour Pierce, a Londonbased investment bank and stockbroker. In addition, he was a Non-Executive Director of China Medstar, an AIM listed medical device company. Earlier in his career Dr Peng was a senior portfolio manager, specialising in global life science and Asian technology investment at Reabourne Technology Investment Management Limited.

Dr Peng received his Bachelor´s degree in medicine from Hunan Medical College (now Central South University Siangya School of Medicine) in Changsha, Hunan Province, China and subsequently he obtained a Master´s degree in medicine from Hunan Medical College. Dr Peng was awarded his PhD in molecular pathology from University College London (UCL) Medical School and subsequently practiced as a clinical lecturer there.

Dr Peng was appointed as a Non-Executive Director of the Company in September 2015.

John Poulos

Non-Executive Director

Mr John Poulos has a wealth of expertise in global corporate life sciences, having spent 38 years working for AbbVie and Abbott. Prior to retiring in 2016, John served as Vice President, Head of Licensing and Acquisitions for AbbVie, and Group Vice President, Head of Pharmaceutical Licensing and Acquisitions for Abbott Pharmaceuticals. During his career, John was instrumental in the negotiation of numerous acquisitions, including Knoll/BASF Pharma in 2001 for $6.9 billion, Solvay in 2010 for $6.2 billion and Pharmacyclics in 2015 for $21 billion. He was appointed as a Non-Executive Director of the Company in May 2017.

Leopoldo Zambeletti

Non-Executive Director

During a 19-year career as an investment banker, Mr Zambeletti led the European Healthcare Investment Banking team at JP Morgan for eight years before taking up the same position at Credit Suisse for a further five years. Since 2013 he has been an independent strategic advisor to life science companies on merger and acquisitions, out-licencing deals and financing strategy.

He is a Non-Executive Director of Philogen, Qardio Inc., Summit Therapeutics PLC (NASDAQ and AIM), Nogra Pharma and Tiziana Life Sciences (AIM). Mr Zambeletti started his career at KPMG as an auditor.

Mr Zambeletti received a BA in Business from Bocconi University in Milan, Italy. Mr Zambeletti was appointed as a Non-Executive Director of the Company in September 2015.

Yrjö E K Wichmann

Chief Financial Officer

Mr Wichmann has a career spanning over 20 years in financing and investment banking. He was appointed as a Chief Financial Officer of the Company in 2014. Prior to his appointment at the Company, Mr Wichmann held a number of senior positions within the life sciences and biotechnology sector, most recently at IP Finland Oy, Biohit Oyj (NASDAQ OMX Helsinki), Capman Oyj, FibroGen Europe Oyj (NASDAQ) and D. Carnegie & Co AB. Whilst carrying out these roles Mr Wichmann has participated in healthcare IPOs on the London, Stockholm and Helsinki stock exchanges as both an investment banker and as a member of the board. Mr Wichmann is a member of the Investment Committee at Dasos Timberland Fund I and II.

Mr Wichmann obtained a Masters in Economics from Helsinki University.

He was appointed as an Executive Director of the Company in 2015.

CORPORATE GOVERNANCE

Directors' Report

For the year ended 31 December 2017.

The Directors present their report together with the audited financial statements for the year ended 31 December 2017.

Directors

During the year ended 31 December 2017 following persons have been members of Board of Directors of the Company:

Executive
Dr Markku Jalkanen, PhD, Chief Executive Officer
Mr Yrjö Wichmann, MSc, Chief Financial Officer

Non-Executive
Dr Frank Armstrong, FRCPE, FFPM, Chairman
Mr Matti Manner, LLM, Vice-chairman
Dr Juho Jalkanen, MD, MSc, Non-Executive Director*
Dr Jonathan Knowles, PhD, Non-Executive Director
Dr Huaizheng Peng, MD, PhD, Non-Executive Director
Mr Leopoldo Zambeletti, Non-Executive Director
Mr John Poulos, Non-Executive Director**
Dr Gregory B. Brown, Non-Executive Director**

* resigned in the AGM 16 May 2017 ** appointed in the AGM May 2017

The Directors of the Company held the following beneficial interests in the shares and share options of Faron Pharmaceuticals Ltd on the date of this report:

2017	Issued Share Capital		Share Options	
Executive	Ordinary shares	Percentage held	Ordinary shares	Average exercise price, € cent
Jalkanen Markku[1)]	2,873,390	9.9%	240,000	5.00
Jalkanen Juho[2)]	1,082,570	3.7%	40,000	3.31
Manner Matti	484,900	1.7%	60,000	5.00
Knowles Johathan	110,712	0.4%	60,000	5.00
Wichmann Yrjö	69,440	0.2%	90,000	5.00
Zambeletti Leopold	17,461	0.1%	60,000	5.00
Armstrong Frank[3)]	9,096	0.0%	120,000	5.00
Peng Huaizheng	4,000	0.0%	60,000	5.00
Brown Gregory	0	0.0%	20,000	8.39
Poulos John	0	0.0%	20,000	8.39
	4,651,569	**15.9 %**	**770,000**	

[1)] of which, 1,794,890 are held by Markku Jalkanen directly, and 1,078,500 are held by Markku Jalkanen's wife being Sirpa Jalkanen. [2)] of which, 1,078,500 are held by Juho Jalkanen directly, and 4,070 are held by Juho Jalkanen´s family being Aaro Jalkanen, Enna Jalkanen and Heikki Jalkanen.
[3)] held by Frank Armstrong's company Shore Capital.

For a more detailed description of the remuneration of the Directors, see page Directors´ Remuneration Report.
The Company maintained Directors' and officers' liability insurance cover throughout the year.

Principal risks and uncertainties

For a discussion of the principal risks and uncertainties which face Faron please see page Risks and uncertainties.

Results and dividends

The Consolidated Statement of Comprehensive Income for the year is set out on here.

The Company's loss for the financial year after taxation and other comprehensive losses was € 21.1 million (2016: € 10.1 million).

The Company has no distributable equity and thus the Directors do not recommend the payment of a dividend (2016: nil).

Financial information

The Company produces budgets and cash flow projections on an annual basis for approval by the Board. These are reviewed during the year and updated if needed to reflect any changes in the business. Detailed management accounts are produced on a monthly basis, with all significant variances investigated promptly. The management accounts are reviewed and commented on by the Board at Board meetings and are reviewed and reported to the Directors on a monthly basis by the management team.

Financial Key Performance Indicators ('KPIs')

The For a review of the Group's KPIs please see page Financial Review.

Research and development

Details of Company's key research and development programs can be found in the Strategic Report and the detailed program sections. See also notes 2.8 and 6. Further information is also available on the Company website, www.faron.com.

Post balance sheet events

On 21 February 2018 Faron announced that the Company raised EUR 15,863 thousand before expenses by way of the placing of 1,863,350 ordinary shares at the Issue Price of GBP 8.05 per share.

During the first quarter 2018, Faron Pharmaceuticals Ltd has registered subsidiaries in the United States of America and in Switzerland.

Mr. Juhana Heinonen was appointed to Chief Commercial Officer and Mrs. Maria Lahtinen to Supplier Management Director, both are members of Company's management team as of January 2018.

On May 5th the preliminary results of the INTEREST -trial were reported to the Board. The Company continues to investigate the results.

Financial instruments and management of liquid resources

The Company's principal financial instrument comprises cash, and this is used to finance Company's operations. The Company has also other financial instruments such as leasing facilities that arise directly from its operations.

The Company has a policy, which has been consistently followed, of not trading in financial instruments and to minimize currency exposure by actively matching currency expenses and income to the extent possible. The Company's cash is held on bank accounts in reputable bank in Finland. The Group's treasury policy is reviewed annually. See Note 2.17 'Financial assets', Note 19 'Financial assets and liabilities' and Note 20, 'Financial risk management' in the Notes to the Financial Statements for IFRS disclosure regarding financial instruments.

Substantial shareholdings

On 31 December 2017 the Company had been notified of the following holdings of more than 3% or more of the issued share capital of the Company.

Name	Number of shares	%
A&B (HK) Company Limited	3,408,409	11.69
Marko Salmi	3,279,570	11.25
Tom-Erik Lind	2,552,523	8.75
Markku Jalkanen	1,794,890	6.15
Aviva Investos	1,518,814	5.21
Polar Capital	1,442,000	4.49
Legal & General Investment Management	1,265,000	4.34
City Financial	1,132,530	3.88
Juho Jalkanen*	1,082,570	3.71
Sirpa Jalkanen	1,078,500	3.70
Timo Syrjälä****	993,656	3.41
Katriina Peltola***	978,500	3.36
Hargreave Hale	917,900	3.15
Maija-Leena Hollmén**	878,500	3.01

* Held by Juho Jalkanen and connected parties.
** Held by Maija-Leena Hollmén and connected parties.
*** Held by Katriina Peltola and connected parties.
**** of which, 520,830 are held directly by Timo Syrjälä and 472,826 are held by Acme Investments SPF S.à.r.l., an entity which is wholly owned by Timo Syrjälä.

Annual General Meeting

The AGM will be held in 31 May 2018 and further details will be provided to shareholders in advance of the meeting.

Independent auditors

PricewaterhouseCoopers have expressed their willingness to continue in office as auditors for the year. A resolution to reappoint them will be proposed at the forthcoming AGM.

Disclosure and information to auditors

Each of the current Directors hereby confirms that:

(a) So far as he or she is aware, there is no relevant audit information of which the auditors are unaware; and

(b) He or she has taken all reasonable steps to ascertain any relevant audit information and to ensure that the auditors are aware of such information

On behalf of the Board
Frank M Armstrong
Chairman
5 May 2018

CORPORATE GOVERNANCE

Corporate Governance Report

The Board

At 31 December 2017, the Board comprised seven Non-Executive Directors, and two Executive Directors.

The composition of the board of directors as well as Directors' biographies are described on pages Board of Directors.

The Board is responsible to the shareholders for the proper management of the Company and meets regularly to set the overall direction and strategy of the Company, to review scientific, operational and financial performance, and to advise on management appointments. The Board has also convened by telephone conference during the year to review the strategy and activities of the business. The Board held 16 meetings during 2017.

All key operational and investment decisions are subject to Board approval. The roles of Chief Executive Officer and Non-Executive Chairman are well defined and clearly separated. The Chairman oversees the Board´s work, ensures that the Board's decision-making is balanced and that the Non-Executive Directors have all relevant information on matters to be decided.

The Chief Executive Officer is responsible for implementing the strategy of the Board and managing the day-to-day business activities of the Company. The management of the Company prepares a monthly management and financial accounts pack, which is distributed to the Board every month and in advance of Board meetings.

The Board considers there to be sufficient independence on the Board and that all the Non-Executive Directors are of sufficient competence and calibre to add strength and objectivity to the Board, and to bring considerable experience in terms of their knowledge of the scientific, operational and financial development of biopharmaceutical products and companies. Where necessary, the Company facilitates that Non-Executive Directors obtain specialist external advice from appropriate advisers. The term of office of each Director expires on the closing of the AGM immediately following his/her appointment to the Board. Under the Finnish Companies Act and the Articles, the Directors are elected by the Shareholders at General Meetings annually. Under the Finnish Companies Act, Directors may be removed from office at any time, with or without cause, by a majority of votes cast at a General Meeting. Vacancies on the Board may only be filled by a majority of Shareholder votes cast at a General Meeting.

Performance Evaluation

The Board has a process for evaluation of its own performance, that of its committees and individual Directors, including the Chairman. These evaluations are carried out at least annually.

Board Committees

In conjunction with the being admitted to trading on AIM, the Company has established audit, nomination and remuneration committees of the Board with formally delegated duties and responsibilities.

Remuneration Committee

The Remuneration Committee comprises Frank Armstrong as Chairman together with Jonathan Knowles and John Poulos. The committee is responsible for the review and recommendation of the scale and structure of remuneration for senior management, including any bonus arrangements or the award of share options with due regard to the interests of the Shareholders and the performance of the Company. The Remuneration Committee held three meetings during 2017.

Audit Committee

The Audit Committee, which comprises Leopoldo Zambeletti as Chairman together with Matti Manner and Gregory Brown, meets not less than twice a year. The committee is responsible for making recommendations to the New Board on the appointment of auditors and the audit fee and for ensuring that the financial performance of the Company is properly monitored and reported. In addition, the Audit Committee will receive and review reports from management and the auditors relating to the interim report, the annual report and accounts and the internal control systems of the Company. The audit committee held four meeting during 2017.

Nomination Committee

The Nomination Committee comprises of Matti Manner as Chairman together with Frank Armstrong and Huaizheng Peng. The Nomination Committee monitors the size and composition of the Board and the other Board committees and is responsible for identifying suitable candidates for Board membership. The nomination committee held two meetings during 2017.

Risk management and Internal control

The Board is responsible for the systems of internal control and for reviewing their effectiveness. The internal controls are designed to manage rather than eliminate risk and provide reasonable but not absolute assurance against material misstatement or loss. The Board reviews the effectiveness of these systems annually by considering the risks potentially affecting the Company.The Company does not consider it necessary to have an internal audit function due to the small size of the administrative function and the frequent interaction with the auditors and the supervision of the Audit Committee. There is a monthly review and authorisation of transactions by the Chief Financial Officer and Chief Executive Officer. A comprehensive budgeting process is completed once a year and is reviewed and approved by the Board. The Company's results, compared with the budget, are reported to the Board on regular basis and discussed in detail.

The Company maintains appropriate insurance cover in respect of actions taken against the Directors because of their roles, as well as against material loss or claims against the Company. The insured values and type of cover are comprehensively reviewed on a periodic basis.

Corporate Social Responsibility

The Company is committed to maintaining and promoting high standards of business integrity. Company values, which incorporate the principles of Corporate Social Responsibilities (CSR) and sustainability, guide the Company's relationships with clients, employees and the communities and environment in which we operate. The Company's approach to sustainability addresses both our environmental and social impacts, supporting the Company's vision to remain an employer of choice, while meeting client demands for socially responsible partners.

The Company respects laws and customs while supporting international laws and regulations.

Relations with Shareholders

The Board recognises the importance of communication with its shareholders to ensure that its strategy and performance is understood and that its remains accountable to shareholders. Our website, www.faron.com, has a section dedicated to investor matters and provides useful information for the Company's owners.

Attendance at Board meetings

During 2017 the Board held 16 meetings. The table below lists the Directors attendance to the Board meetings during the year:

Faron Board	Attendance to meetings
Executive directors	
Markku Jalkanen	14
Yrjö E K Wichmann	15
Non-executive directors	
Dr Frank Armstrong	16
Mr Matti Manner	15
Dr Juho Jalkanen*	7
Dr Jonathan Knowles	9
Dr Huaizheng Peng	15
Mr Leopoldo Zambeletti	14
Mr Greg Brown**	7
Mr John Poulos**	7

* Resigned from board on 16 May 2017

** Joined board on 16 May 2017

Compliance with the Principles of the QCA Code

The Principles of the QCA Code	Comply/ Explain	Reference
1. Setting out the vision and strategy	Comply	Strategic Report
2. Managing and communicating risk and implementing internal control	Comply	CGR (Risk Management and Internal Control), Risks and Uncertainties
3. Articulating strategy through corporate communication and investor relations	Comply	CGR (Relations with shareholders)
4. Meeting the needs and objectives of shareholders	Comply	CGR (Relations with shareholders)
5. Meeting stakeholders and social responsibilities	Comply	GCR (Corporate Social Responsibility)
6. Using cost effective and value added arrangements	Comply	Strategic Report
7. Developing structures and processes	Comply	Strategic Report
8. Being responsible and accountable	Comply	CGR (The Board)
9. Having balance on the board	Comply	CGR (The Board)
10. Having appropriate skills and capabilities on the board	Comply	CGR (The Board)
11. Evaluating board performance and development	Comply	CGR (Performance evaluation)
12. Providing information and support	Comply	CGR (The Board)

CGR = Corporate Governance Report

CORPORATE GOVERNANCE

Directors' Remuneration Report

Audited Information
Remuneration policy for Executive Directors

The Remuneration Committee sets the remuneration policy that aims to align Executive Director remuneration with shareholders' interests and attract and retain the best talent for the benefit of the Company.

The remuneration of the Executive Directors during the year ended 31 December 2017 is set out below:

For the year ended 31 December 2017.

This report sets out Faron´s remuneration policy for the Executive and Non-Executive Directors. No Director is involved in discussions relating to their own remuneration.

Basic salary

Basic salaries are reviewed annually. The review process is managed by the Remuneration Committee with reference to market salary data, the Executive Director's performance and contribution to the Company during the year.

Bonuses

Annual bonuses are based on the achievement of Company strategic and financial targets and personal performance objectives. The Non-Executive Directors believe that bonuses are an incentive to achieve the targets and objectives, and represent an important element of the total compensation of the Executive Directors; they have established that the annual bonus potential will be 40% for the Executive Directors. On 20 February 2018 the Chief Executive Officer was awarded a bonus representing 50% and the Chief Financial Officer was awarded a bonus representing 30% of their 2017 gross basic salaries.

Longer Term Incentives

In order to further incentivise the Executive Directors and employees, and align their interests with Shareholders, the Extraordinary General Meeting of the Company on 15 September 2015 approved a share option plan and granted share options to the members of the board under this option plan. Details of the option plan are in the table below. The Company's policy is to maintain an incentive policy also in the future.

Pension

Faron has a law-defined contribution plan under which it pays fixed contributions into a separate entity. The plan covers all the employees of Faron including the Executive Directors. Faron has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

Other benefits

Some employees have the possibility to take a company car allowance, which is part of their gross salary. All employees have a company mobile phone that constitutes a company mobile phone allowance.

Executive Directors' service contracts and termination provisions

The service contracts of Executive Directors are approved by the Board and are one year rolling contracts. The service contract may be terminated by either party giving six months' notice to the other.

The details of the Executive Directors' contracts are summarised below:

		Date of contract	Notice period
Markku Jalkanen	CEO	16.09.2015	6 months
Yrjö E K Wichmann	CFO	16.09.2015	6 months

Non-Executive Directors' service contracts and remuneration

The remuneration and compensation payable to the members of the Board including the Non-Executive Directors shall be approved by the Shareholders at the AGM. Any Non-Executive Director who, by request, goes or resides abroad for any purposes of the Company or who performs services which in the opinion of the Board goes beyond the ordinary duties of a Director may be paid extra remuneration or may receive such other benefits as the remuneration committee may approve. Non-Executive Directors are entitled to be reimbursed in respect of their reasonably and properly incurred travelling, accommodation and incidental expenses for attending and returning from meetings of the Board, committee meetings or the general meetings of Shareholders.

The Non-Executive Directors do not receive any pension, bonus or benefits from the Company. The contracts of the Non-Executive Directors, excluding remuneration and compensation, are reviewed by the Board annually.

Current contracts are summarised below:

Non-Executive Directors' Contracts	Contract	Date of Contract
Frank Armstrong	Chairman	16.09.2015
Matti Manner	Vice-chairman	16.09.2015
Gregory Brown	Member	16.05.2017
Jonathan Knowles	Member	16.09.2015
Huaizheng Peng	Member	16.09.2015
John Poulos	Member	16.05.2017
Leopoldo Zambeletti	Member	16.09.2015

The appointments of Non-Executive Directors are terminable with immediate effect in accordance with the Articles of Association and pursuant to the Finnish Companies Act, through a resolution of Shareholders at a General Meeting on any grounds. The Non-Executive Directors may resign as a director by delivering three months' notice to the Registered Office of the Company or through tendering such resignation at a meeting of the Board.

Audited Information
Directors' remuneration

The Directors received the following remuneration during the year:

	Salaries and fees	Bonus 2017	Taxable benefits	Total
Executive				
Markku Jalkanen	234,562.00	123,641.00	12,720.00	370,923.00
Yrjö E K Wichmann	174,168.00	52,322.40	240.00	226,730.40
Non-Executive				
Frank Armstrong	85,834.25	-	-	85,834.25
Matti Manner	48,127.40	-	-	48,127.40
Juho Jalkanen	17,164.38	-	-	17,164.38
Jonathan Knowles	40,065.75	-	-	40,065.75
Huaizheng Peng	41,565.75	-	-	41,565.75
Leopoldo Zambeletti	45,627.40	-	-	45,627.40
Gregory Brown	28,901.37	-	-	28,901.37
John Poulos	28,901.37	-	-	28,901.37
	744,917.67	175,963.40	12,960.00	933,841.07

Directors' share options

Aggregate remunerations disclosed above do not include any amounts for the value of options to acquire Ordinary Shares in the Company granted to or held by the Directors. A share option plan was adopted by the Company at the Extraordinary General Meeting held on 15 September 2015 and amended in Annual shareholders Meeting on 16 May 2017. The option plan allows the Company to offer options for subscription free of charge to members of the Board, and to such officers and employees of the Company as the Board sees fit. Each option will entitle the holder of the option to subscribe for one Ordinary Share. Under the terms of the option plan, an aggregate maximum number of 1,800,000 options may be granted, such aggregate being made up of a maximum of 400,000 "A" options, the subscription period for which ended on 9 June 2016 (such options exercisable between 2 November 2015 and 30 September 2021), a maximum of 400,000 "B" options to be subscribed for between 8 October 2016 and 30 September 2019 (exercisable between 8 October 2016 and 30 September 2021), a maximum of 500,000 "C" options to be subscribed for between 8 October 2017 and 30 September 2019 (exercisable between 8 October

2017 and 30 September 2021), and a maximum of 500,000 "D" options to be subscribed for between 8 October 2018 and 30 September 2019 (exercisable between 8 October 2018 and 30 September 2021).

The exercise price for Ordinary Shares based on "A" options shall be €3.71. The exercise price for Ordinary Shares based on "B" options shall be €2.90. The exercise price for Ordinary Shares based on "C" options shall be €8.39. The exercise price for Ordinary Shares based on "D" options shall be determined by the Euro equivalent to the average share price of the publicly traded Ordinary Shares of the Company on AIM between 1 July and 30 September of 2018 respectively. The exercise price will be disclosed in Euros based on the exchange reference rate published by the European Central Bank on the last day of the period for determination of the subscription price, and rounded to the nearest Euro cent.

Details of these options are as follows:

2015A Options	Date of grant of A options[1)]	At 1 January 2017	Granted during the period	Cancelled during the period	At 31 December 2017	Subscription price per share, €	Date from which exercisable	Expiry date of A options
Markku Jalkanen	16.09.2015	80,000	0	0	80,000	3.71	02.11.2015	30.09.2021
Yrjö E K Wichmann	16.09.2015	30,000	0	0	30,000	3.71	02.11.2015	30.09.2021
Frank Armstrong	16.09.2015	40,000	0	0	40,000	3.71	02.11.2015	30.09.2021
Matti Manner	16.09.2015	20,000	0	0	20,000	3.71	02.11.2015	30.09.2021
Juho Jalkanen	16.09.2015	20,000	0	0	20,000	3.71	02.11.2015	30.09.2021
Jonathan Knowles	16.09.2015	20,000	0	0	20,000	3.71	02.11.2015	30.09.2021
Huaizheng Peng	16.09.2015	20,000	0	0	20,000	3.71	02.11.2015	30.09.2021
Leopoldo Zambeletti	16.09.2015	20,000	0	0	20,000	3.71	02.11.2015	30.09.2021
Gregory Brown	-	0	0	0	0	-	-	-
John Poulos	-	0	0	0	0	-	-	-
		250,000			250,000			

2015B Options	Date of grant of B options[1)]	At 1 January 2017	Granted during the period	Cancelled during the period	At 31 December 2017	Subscription price per share, €	Date from which exercisable	Expiry date of B options
Markku Jalkanen	18.11.2016	80,000	0	0	80,000	2.90	08.10.2016	30.09.2021
Yrjö E K Wichmann	18.11.2016	30,000	0	0	30,000	2.90	08.10.2016	30.09.2021
Frank Armstrong	18.11.2016	40,000	0	0	40,000	2.90	08.10.2016	30.09.2021
Juho Jalkanen	18.11.2016	20,000	0	0	20,000	2.90	08.10.2016	30.09.2021
Matti Manner	18.11.2016	20,000	0	0	20,000	2.90	08.10.2016	30.09.2021
Jonathan Knowles	18.11.2016	20,000	0	0	20,000	2.90	08.10.2016	30.09.2021
Huaizheng Peng	18.11.2016	20,000	0	0	20,000	2.90	08.10.2016	30.09.2021
Leopoldo Zambeletti	18.11.2016	20,000	0	0	20,000	2.90	08.10.2016	30.09.2021
Gregory Brown	-	0	0	0	0	-	-	-
John Poulos	-	0	0	0	0	-	-	-
		250,000	0	0	250,000			

2015C Options	Date of grant of C options[1)]	At 1 January 2017	Granted during the period	Cancelled during the period	At 31 December 2017	Subscription price per share, €	Date from which exercisable	Expiry date of C options
Markku Jalkanen	4.10.2017	0	80,000	0	80,000	8.39	08.10.2017	30.09.2021
Yrjö E K Wichmann	4.10.2017	0	30,000	0	30,000	8.39	08.10.2017	30.09.2021
Frank Armstrong	4.10.2017	0	40,000	0	40,000	8.39	08.10.2017	30.09.2021
Matti Manner	4.10.2017	0	20,000	0	20,000	8.39	08.10.2017	30.09.2021
Juho Jalkanen	-	0	0	0	0	-	-	-
Jonathan Knowles	20.10.2017	0	20,000	0	20,000	8.39	08.10.2017	30.09.2021
Huaizheng Peng	8.11.2017	0	20,000	0	20,000	8.39	08.10.2017	30.09.2021
Leopoldo Zambeletti	14.11.2017	0	20,000	0	20,000	8.39	08.10.2017	30.09.2021
Gregory Brown	13.10.2017	0	20,000	0	20,000	8.39	08.10.2017	30.09.2021
John Poulos	4.10.2017	0	20,000	0	20,000	8.39	08.10.2017	30.09.2021
		0	270,000	0	270,000			

Total Options	At 1 January 2017	Granted during the period	Cancelled during the period	At 31 December 2017	Average subs. price per shares, €
Markku Jalkanen	160,000	80,000	0	240,000	5.00
Yrjö E K Wichmann	60,000	30,000	0	90,000	5.00
Frank Armstrong	80,000	40,000	0	120,000	5.00
Matti Manner	40,000	20,000	0	60,000	5.00
Juho Jalkanen	40,000	0	0	40,000	3.31
Jonathan Knowles	40,000	20,000	0	60,000	5.00
Huaizheng Peng	40,000	20,000	0	60,000	5.00
Leopoldo Zambeletti	40,000	20,000	0	60,000	5.00
Gregory Brown	0	20,000	0	20,000	8.39
John Poulos	0	20,000	0	20,000	8.39
	500,000	270,000	0	770,000	

Directors' shareholdings

The Directors who served during the period, together with their beneficial interests in the shares of the Company, are as follows

2017	Issued Share Capital		Share Options	
Executive	Ordinary shares	Percentage held	Ordinary shares	Average exercise price, € cent
Jalkanen Markku[1)]	2,873,390	9.9%	240,000	5.00
Jalkanen Juho[2)]	1,082,570	3.7%	40,000	3.31
Manner Matti	484,900	1.7%	60,000	5.00
Knowles Johathan	110,712	0.4%	60,000	5.00
Wichmann Yrjö	69,440	0.2%	90,000	5.00
Zambeletti Leopold	17,461	0.1%	60,000	5.00
Armstrong Frank[3)]	9,096	0.0%	120,000	5.00
Peng Huaizheng	4,000	0.0%	60,000	5.00
Brown Gregory	0	0.0%	20,000	8.39
Poulos John	0	0.0%	20,000	8.39
	4,651,569	**15.9%**	**770,000**	

[1)] of which, 1,794,890 are held by Markku Jalkanen directly, and 1,078,500 are held by Markku Jalkanen's wife being Sirpa Jalkanen.

[2)] of which, 1,078,500 are held by Juho Jalkanen directly, and 4,070 are held by Juho's Jalkanens' family being Aaro Jalkanen, Enna Jalkanen and Heikki Jalkanen.

[3)] held by Frank Armstrongs' company Shore Capital.

CORPORATE GOVERNANCE

Statement of Responsibilities

Under the Finnish Companies Act and the Finnish Accounting Act the Company must prepare an Annual Report and financial statements in accordance with applicable law and regulations.

The Board of Directors and the Managing Director are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, as well as for the preparation of financial statements and the report of the Board of Directors that give a true and fair view in accordance with the laws and regulations governing the preparation of the financial statements and the report of the Board of Directors in Finland. The Board of Directors is responsible for the appropriate arrangement of the control of the company's accounts and finances, and the Managing Director shall see to it that the accounts of the company are in compliance with the law and that its financial affairs have been arranged in a reliable manner. In accordance with the rules of the London Stock Exchange for companies trading securities on the Alternative Investment Market, the Company is also required to prepare annual accounts and financial statements under IFRS.

In preparing these financial statements, the Board of Directors is required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the European Union, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The Board of Directors and the Managing Director are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the requirements of the Finnish Accounting Act. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Website publication

The Directors are responsible for ensuring that the annual report and the financial statements are made available on a website. Financial statements are published on the company's website in accordance with the AIM rule 26 and the recommendations of the QCA´s Corporate Governance Code for Small and Medium Sized Companies.

On behalf of the Board
Frank Armstrong
Chairman
5 May 2018

FINANCIAL STATEMENTS

Statement of Comprehensive Income

€'000	Note	For the year ended 31 December 2017	For the year ended 31 December 2016 (Restated)
Revenue	**3, 4**	**-**	**952**
Other operating income	5	1,495	1,025
Research and development expenses	6, 7, 8	(19,100)	(9,223)
General and administrative expenses	7, 8	(3,054)	(2,457)
Operating loss		**(20,659)**	**(9,703)**
Financial expense	9	(408)	(360)
Financial income	9	7	-
Loss before tax		**(21,060)**	**(10,063)**
Tax expense	10	(1)	(75)
Loss for the period		**(21,061)**	**(10,138)**
Comprehensive loss for the period attributable to the equity holders of the Company		**(21,061)**	**(10,138)**
Loss per ordinary share			
Basic and diluted loss per share, EUR	11	(0.76)	(0.42)

FINANCIAL STATEMENTS

Balance Sheet

€'000	Note	As at 31 December 2017	As at 31 December 2016 (Restated)	As at 1 January 2016 (Restated)
Assets				
Non-current assets				
Machinery and equipment	12	22	21	28
Intangible assets	12	325	304	283
Prepayments and other receivables	13	1,310	1,475	1,885
Total non-current assets		**1,657**	**1,800**	**2,196**
Current assets				
Prepayments and other receivables	15	3,920	2,469	489
Cash and cash equivalents	16	9,310	11,478	11,068
Total current assets		**13,230**	**13,947**	**11,557**
Total assets		**14,887**	**15,747**	**13,753**
Equity and liabilities				
Capital and reserves attributable to the equity holders of the Company				
Share capital		2,691	2,691	2,691
Reserve for invested unrestricted equity		48,576	32,362	23,843
Accumulated deficit		(46,524)	(26,652)	(17,450)
Total equity	**17, 18**	**4,743**	**8,401**	**9,084**
Non-current liabilities				
Borrowings	19	2,088	2,083	1,446
Other liabilities	21	-	614	241
Total non-current liabilities		**2,088**	**2,697**	**1,687**
Current liabilities				
Borrowings	19	338	93	245
Trade payables	22	3,196	2,021	620
Other current liabilities	22	4,522	2,535	2,117
Total current liabilities		**8,056**	**4,649**	**2,982**
Total liabilities		**10,144**	**7,346**	**4,669**
Total equity and liabilities		**14,887**	**15,747**	**13,753**

FINANCIAL STATEMENTS

Statement of Changes in Equity

€'000	Note	Share capital	Reserve for invested unrestricted equity	Accumulated deficit	Total equity
Balance as at 1 January 2016		**2,691**	**24,533**	**(16,046)**	**11,178**
Impact of restatements (net of tax) 1 January 2016	*2.2*		*(690)*	*(1,404)*	*(2,094)*
Balance as at 1 January 2016, restated		**2,691**	**23,843**	**(17,450)**	**9,084**
Comprehensive loss for the period				(10,138)	(10,138)
Transactions with equity holders of the Company					
Issue of ordinary shares, net of transaction cost EUR 811 thousand	17	-	8,519	-	8,519
Share-based compensation	18	-	-	936	936
		-	**8,519**	**936**	**9,455**
Balance as at 31 December 2016		**2,691**	**32,362**	**(26,652)**	**8,401**
Comprehensive loss for the period		-	-	(21,061)	(21,061)
Transactions with equity holders of the Company					
Issue of ordinary shares, net of transaction costs EUR 1,149 thousand	17	-	15,863	-	15,863
Share options exercised	17,18	-	97	-	97
Warrants exercised	17,18	-	254	-	254
Share-based compensation	17,18	-	-	1,189	1,189
		-	**16,214**	**1,189**	**17,403**
Balance as at 31 December 2017		**2,691**	**48,576**	**(46,524)**	**4,743**

FINANCIAL STATEMENTS

Statement of Cash Flows

€'000	Note	For the year ended 31 December 2017	For the year ended 31 December 2016 (Restated)
Cash flow from operating activities			
Loss before tax		(21,060)	(10,063)
Adjustments for:			
Depreciation and amortisation	8	76	78
Interest expense	9	75	24
Unrealised foreign exchange loss (gain), net	9	290	(627)
Share-based compensation	18	1,189	936
Adjusted loss from operations before changes in working capital		(19,430)	(9,652)
Change in net working capital:			
Prepayments and other receivables		(1,286)	(1,570)
Trade payables		1,175	1,402
Other liabilities		1,189	480
Cash used in operations		(18,352)	(9,340)
Taxes paid	**10**	**(1)**	**(75)**
Interest paid	**9**	**(10)**	**(4)**
Net cash used in operating activities		(18,363)	(9,419)
Cash flow from investing activities			
Payments for intangible assets	12	(90)	(92)
Payments for equipment	12	(8)	-
Net cash used in investing activities		**(98)**	**(92)**
Cash flow from financing activities			
Proceeds from issue of shares	17	17,362	9,330
Share issue transaction cost	17	(1,148)	(811)
Proceeds from borrowings		453	775
Repayment of borrowings	20	(84)	-
Net cash from financing activities		**16,583**	**9,294**
Net increase (+) / decrease (-) in cash and cash equivalents		**(1,878)**	**(217)**
Effect of exchange rate changes on cash and cash equivalents		(290)	627
Cash and cash equivalents at 1 January	16	11,478	11,068
Cash and cash equivalents at 31 December	**16**	**9,310**	**11,478**

FINANCIAL STATEMENTS

Notes to the Financial Statements

1. Corporate information

Faron Pharmaceuticals Ltd. (the "Company") is a clinical stage biopharmaceutical company incorporated and domiciled in Finland, with its headquarters at Joukahaisenkatu 6 B, 20520 Turku, Finland. The Company has two major drug development projects focusing on acute trauma, cancer growth and spread and inflammatory diseases.

The Company is listed on the London Stock Exchange's AIM market since 17 November 2015, with a ticker FARN.

The Board of Directors of the Company approved the financial statements on 5 May, 2018.

2. Summary of significant accounting policies

2.1. Basis of preparation

The financial statements have been prepared in accordance with the International Financial Reporting Standards of the International Accounting Standards Board (IASB) and as adopted by the European Union (IFRS) and the interpretations of the International Financial Reporting Standards Interpretations Committee (IFRS IC). The financial statements have been prepared on a historical cost basis, unless otherwise stated.

The financial statements have been prepared on the basis of a full retrospective application of IFRS 15, Revenue from Contracts with Customers, with the adoption date as of 1 January 2017.

The principal accounting policies applied in the preparation of these financial statements are set out below. The Company has consistently applied these policies to all the periods presented, unless otherwise stated. The areas of the financial statements involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 2.22.

All amounts are presented in thousands of euros, unless otherwise indicated, rounded to the nearest euro thousand.

2.2. Restatements of previously issued financial statements

Subsequent to the original issuance of the Company's financial statements for the year ended 31 December 2016, the Company has adopted new and amended accounting standards as disclosed in note 2.23 and corrected certain prior period errors in its accounting. The 2016 financial statements, as initially reported, have therefore been amended and restated as follows.

1) In the process of adopting IFRS 15 *Revenue from contracts with customers* (see note 2.23) we identified errors in the application of IAS 18, which resulted in the following corrections to our previously issued 2016 financial statements:

   a) Under IAS 18, the Company deferred EUR 750 thousand upfront fee from Korean license partner Pharmbio Korea Inc. ("Pharmbio") as at 31 December, 2016. This was not consistent with the revenue recognition policy that the Company had applied earlier on a license agreement with similar characteristics. Consequently, the Company has recognised the upfront fee in revenue in the accompanied restated financial statements for the year ended 31 December 2016.

   b) The Company entered into a joint purchase agreement with a third party pharmaceutical company whereby they agreed to purchase Active Pharmaceutical Ingredient ('API') from a supplier. Under this arrangement, the Company received cash from the pharmaceutical company that it passed on to the supplier. In 2016, the Company had recognised this cash receipt as revenue and recorded the cost of both Company's and the third party's API in research and development expenses. This has been corrected by reducing revenue by EUR 951 thousand and research and development expenses by the same amount. Further, the related VAT posting of EUR 68 thousand was corrected resulting in an increase in current prepayments and other receivables and decrease in research and development expenses.

   c) The Company has revisited the substance and the accounting treatment of its financing agreement with A&B (HK) Company Limited ("A&B") entered into in May 2015 and concluded that the share subscription by A&B comprised of a linked transaction, whereby A&B simultaneously acquired a license to the Company's intellectual property. Management has assessed that the

consideration received in excess of the estimated fair value of the Company's ordinary shares subscribed for by A&B should have been allocated to the transaction price for the sale of the licensed intellectual property. The Company has determined that the license to intellectual property is a right to use type license and the transaction price should have been recognised in revenue at the point in time when control to the intellectual property transferred in May 2015. Therefore the transaction price for the sale of the licensed intellectual property EUR 690 thousand has been reclassified within equity from the reserve for invested unrestricted equity to accumulated deficit.

2) The Company has corrected amounts in its previous years' accounting for government grants received in the form of direct funding from the European Commission and in the form of indirect government assistance through the below-market rate government loans. The corrections for direct funding from the European Commissions related to the timing of the recognition of the eligible costs and to matching of the grant income to incurred eligible costs. The correction for the below-market rate government loans related to recognition of the grant income based on an accrual basis, instead of recognition upon proceeds received. In addition, the Company has corrected the carrying value of the government loans recognised at amortised cost due to an error in the effective interest rate calculation. These restatements resulted in EUR 369 thousand decrease in prepayments and other receivables with corresponding increase in the accumulated deficit as of 1 January 2016. The other operating income in the comprehensive statement of income for the year ended 31 December 2016 is restated and adjusted by EUR 717 thousand with EUR 1 thousand decrease in financial expense, EUR 629 thousand decrease prepayments in other receivables, EUR 50 thousand increase in the borrowings and EUR 36 thousand increase in other current liabilities. Proceeds from borrowings shown in the statement of cash flows have been adjusted by EUR 34 thousand.

3) The Company has incorrectly capitalised in-process research and development expenditures, which had not met the capitalisation criteria in IAS 38. Consequently, the asset of EUR 718 thousand was derecognised in the balance sheet as of 1 January 2016 and the amortization of EUR 90 thousand has been reversed in the statement of comprehensive income for the financial year ended 31 December 2016.

4) In the balance sheet, EUR 1,212 thousand relating to prepayments to a third party Contract Research Organisations and EUR 24 thousand rental deposits have been reclassified from current prepayments and other receivables to non-current prepayments and receivables as at 1 January 2016 due to the long-term nature of the items.

5) The Company has revised its previous balance sheet classification of inventories and re-classified the balances previously presented as inventory prepayments and finished goods to prepayments and other receivables as such goods are not held for sale in the Company's ordinary course of business, but will be used in the Company's research and development activities. This reclassification totalled to EUR 649 thousand and EUR 1,451 thousand as at 1 January 2016 and 31 December 2016, respectively.

6) The Company has corrected the effects of certain prior period cut-off errors related to charges by vendors and their sub-contractors in its restated financial statements resulting in an increase of EUR 241 thousand in non-current other liabilities, EUR 600 thousand increase in other current liabilities, EUR 184 thousand increase in trade payables, EUR 19 thousand increase in prepayments and other receivables and corresponding increase of EUR 1,006 thousand in accumulated deficit as at 1 January 2016. The cut-off correction of EUR 580 thousand was recorded to research and development expenses in the statement of comprehensive income for the year ended 31 December 2016, with corresponding increase in other current liabilities of EUR 245 thousand, increase in other non-current liabilities of EUR 373 thousand and decrease in trade payables of EUR 38 thousand

7) The Company's expense for the effects of the Option Plan 2015, accounted for as an equity-settled plan, has been misstated. The misstatements relate to the valuation of the Option Plan and to errors in accruing for the share-based compensation expense and determination of the grant and service inception dates. As a result, the cumulative expense and corresponding increase of EUR 267 thousand has been recognised to the accumulated deficit as of 1 January 2016, with no impact in total accumulated deficit. The expense for the share-based compensation was increased by EUR 456 thousand in the statement of comprehensive income for the year ended 31 December 2016 with the corresponding increase in accumulated deficit. The Company has also revised the presentation of share-based compensation of EUR 954 thousand in the balance sheet as at 31 December 2016 from reserve for invested unrestricted equity to accumulated deficit.

8) The Company has corrected the proceeds from borrowings in the statement of cash flow for the financial year ended 31 December 2016 by EUR 339 thousand to reflect gross proceeds received. The cash flows for the withdrawal of the borrowings in the form of R&D loans were previously presented net of grant benefit. In addition, the Company has revised the presentation of the statement of cash flows for the financial year ended 31 December 2016 relating to unrealised foreign exchange gains amounting to EUR 627 thousand, interest expense of EUR 24 thousand and the interest paid of EUR 357 thousand, previously presented on a combined basis as financial items. The Company corrected its presentation to disclose share issue transaction cost and the proceeds from issue of shares on a gross basis.

Statement of comprehensive income:

€'000	Reference within note 2.2	As originally reported 2016	Restatement	Amount as adjusted 2016
Revenue	1a, 1b	1,153	(201)	952
Other operating income	2	1,742	(717)	1,025
Research and development expenses	1b, 3, 6, 7	(9,592)	369	(9,223)
General and administrative expenses	7	(2,161)	(296)	(2,457)
Operating loss		**(8,858)**	**(845)**	**(9,703)**
Financial expense	2	(361)	1	(360)
Financial income		0	-	0
Loss before tax	**1, 2, 3, 6, 7**	**(9,219)**	**(844)**	**(10,063)**
Tax expense		(75)	-	(75)
Loss for the period	**1, 2, 3, 6, 7**	**(9,294)**	**(844)**	**(10,138)**
Comprehensive loss for the period attributable to the equity holders of the Company	**1, 2, 3, 6, 7**	**(9,294)**	**(844)**	**(10,138)**
Loss per ordinary share				
Basic and diluted loss per share, euro		(0.39)		(0.42)

Balance sheet:

€'000	Reference within note 2.2	As originally reported, as at 31 December 2016	Restatement	Amount as adjusted, as at 31 December 2016	As originally reported, as at 31 December 2015	Restatement	Amount as adjusted, as at 1 January 2016
Assets							
Non-current assets							
Machinery and equipment		21	-	21	28	-	28
Intangible assets	3	933	(629)	304	1,001	(718)	283
Prepayments and other receivables	4, 5	-	1,475	1,475	-	1,885	1,885
Total non-current assets		**954**	**846**	**1,800**	**1,029**	**1,167**	**2,196**
Current assets							
Inventories	5	1,451	(1,451)	-	649	(649)	-
Prepayments and other receivables	2, 4, 6	3,404	(935)	2,469	2,076	(1,587)	489
Cash and cash equivalents		11,478	-	11,478	11,068	-	11,068
Total current assets		**16,333**	**(2,386)**	**13,947**	**13,793**	**(2,236)**	**11,557**
Total assets		**17,287**	**(1,540)**	**15,747**	**14,822**	**(1,069)**	**13,753**
Equity and liabilities							
Capital and reserves							
Share capital		2,691	-	2,691	2,691	-	2,691
Reserve for invested unrestricted equity	1c	34,006	(1,644)	32,362	24,533	(690)	23,843
Accumulated deficit	1c, 2, 3, 6, 7	(25,814)	(838)	(26,652)	(16,046)	(1,404)	(17,450)
Total equity		**10,883**	**(2,482)**	**8,401**	**11,178**	**(2,094)**	**9,084**
Non-current liabilities							
Borrowings	2	2,033	50	2,083	1,446	-	1,446
Other liabilities	6	-	614	614	-	241	241
Total non-current liabilities		**2,033**	**664**	**2,697**	**1,446**	**241**	**1,687**
Current liabilities							
Borrowings		93		93	245	-	245
Trade and other payables	6	1,874	147	2,021	436	184	620
Other current liabilities	1a, 2, 6	2,404	131	2,535	1,517	600	2,117
Total current liabilities		**4,371**	**278**	**4,649**	**2,198**	**784**	**2,982**
Total liabilities		**6,404**	**942**	**7,346**	**3,644**	**1,025**	**4,669**
Total equity and liabilities		**17,287**	**(1,540)**	**15,747**	**14,822**	**(1,069)**	**13,753**

Statement of cash flows:

€'000	Reference within note 2.2	As originally reported as at 31 December 2016	Restatement	Amount as adjusted, as at 31 December 2016
Cash flow from operating activities				
Loss before tax	1, 2, 3, 6, 7	(9,219)	(844)	(10,063)
Adjustments for				
Depreciation and amortisation	3	168	(90)	78
Financial items	8	361	(361)	-
Interest expense	8	-	24	24
Unrealised foreign exchange gain, net	8	-	(627)	(627)
Share-based compensation	7	480	456	936
Adjusted loss from the operations before changes in working capital		(8,210)	(1,442)	(9,652)
Change in net working capital:				
Prepayments and other receivables	2, 5, 6	(1,330)	(240)	(1,570)
Inventories	5	(802)	802	-
Trade and other liabilities	1a, 2, 6	2,325	(443)	1,882
Cash used in operations		(8,017)	(1,323)	(9,340)
Taxes paid		(75)	-	(75)
Interest paid	8	(361)	357	(4)
Net cash used in operating activities		**(8,453)**	**(966)**	**(9,419)**
Cash flow from investing activities				
Payments for intangible assets		(92)	-	(92)
Net cash used in investing activities		**(92)**	**-**	**(92)**
Cash flow from financing activities				
Proceeds from issue of shares	8	8,519	811	9,330
Share issue transaction cost	8	-	(811)	(811)
Proceeds from borrowings	2	436	339	775
Net cash from financing activities		**8,955**	**339**	**9,294**
Net increase (+) / decrease (-) in cash and cash equivalents		(410)	(627)	(217)
Effect of exchange rate changes on cash and cash equivalents	8	-	627	627
Cash and cash equivalents at 1 January		11,068		11,068
Cash and cash equivalents at 31 December		**11,478**		**11,478**

Accordingly, these restated financial statements as of 31 December 2016 and for the year ended 31 December 2016 have been approved and authorized for issue by the Company's Board of Directors on 5 May 2018. The Company's previously issued financial statements were approved and authorized for issue by the Board of Directors on 28 March 2017.

2.3. Going concern

The Company has incurred net losses since its inception and for the years ended 31 December 2017 and 2016, the Company reported losses of EUR 21,061 thousand and EUR 10,138 thousand, respectively. In addition to its normal R&D and corporate activities, the Company is, as a late clinical stage drug development company, already making early preparations for the commercialization of its lead product Traumakine. With its pre-clinical product candidate, Clevegen, the Company will advance the development through clinical trials. Both these activities require substantial amounts of funds.

The Company has primarily relied upon financing its development operations with funds that the Company has raised from share issues. In September 2016, the Company raised a total of EUR 8,519 thousand and during 2017, the Company had two separate issues raising a total of EUR 16,214 thousand (Note 17). In addition to equity financing, the Company has obtained funding from license agreements and public R&D loans and grants.

The financial information in these financial statements has been prepared on a going concern basis, which assumes that the Company will continue in operational existence for the foreseeable future. After review of the future operating costs of the Company in conjunction with the cash held at 31 December 2017 and the net proceeds of approximately EUR 15,863 thousand received following the completion of a fund-raising in February 2018, management believes the Company has sufficient funds to continue as a going concern for the foreseeable future (Note 25).

Once the Company has received the marketing approval from the relevant regulatory agencies for products developed in-house that the Company intends to commercialise, the Company would either take the approved product to the markets itself or seek to form partnerships with global, regional or local pharmaceutical companies that have the necessary marketing and distribution capabilities and resources. In case of choosing to market the product itself, the Company would need to secure necessary funding to cover the costs of taking the product through the approval, pricing and regional registering process in addition to required marketing costs. In absence of collaboration agreement, such funding could come from various sources in form of debt or equity funding or as a combination of the before-mentioned.

2.4. Foreign currency transactions and balances

Functional and presentation currency

The financial statements are presented in euro, which is the Company's functional and presentation currency.

Transaction currency

Transactions in foreign currencies are translated at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the exchange rates ruling at the reporting date. Foreign exchange differences arising on translation are recognised in the statement of comprehensive income, within financial income and expenses. Non-monetary assets and liabilities denominated in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction.

2.5. Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker. The Chief Executive Officer, reviewing the operating results regularly to make decisions about the allocation of resources and to assess overall performance, is identified as the chief operating decision maker. The Chief Executive Officer manages the Company as one integrated business and hence, the Company has one operating and reportable segment.

2.6. Revenue recognition

The Company's revenue for 2016 consists of the upfront fee from the license agreement with Pharmbio and the sale of investigational medicinal products to Maruishi. There was no revenue recognised in 2017. The Company adopted IFRS 15 Revenue from Contracts with Customers effective 1 January 2017 and has applied the single, principles based five-step model to all contracts with customers provided by IFRS 15 as follows:

1. Identify the contract with a customer
2. Identify the performance obligations in the contract
3. Determine the transaction price
4. Allocate the transaction price to the performance obligations in the contract
5. Recognise revenue when (or as) the entity satisfies a performance obligation (over time or at a point in time).

Revenue from licensing agreements

According to IFRS 15, performance obligation is a promise to provide a distinct good or service or a series of distinct goods or services. Goods and services that are not distinct are bundled with other goods or services in the contract until a bundle of goods or services that is distinct is created. A good or service promised to a customer is distinct if the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer and the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract.

The Company's existing license agreements with Maruishi in Japan, with A&B in Greater China and with Pharmbio in Republic of Korea each include only one performance obligation, which is the grant of the license to use of its intellectual property ("IP"). After the Company has granted the license, it does not have an obligation to participate or provide additional services to its customers. The transaction price for the grant of the license to use the Company's IP comprises of fixed and variable payment streams and the grant of the license is considered to be a right to use IP. Upfront fees earned, are recognised as revenue at a point in time, upon transfer of control over the license to the licensee. Revenue from variable consideration, which are contingent on achievements of future milestones are recognised as revenue when it is highly probable the revenue will not reverse, that is when the underlying contingencies have been resolved. For future royalty payments associated with a license, the Company applies the IFRS 15 exception for sales-based royalties and recognises the revenue only when the subsequent sale occurs.

In addition, there is a potential performance obligation regarding future manufacturing. The Company has tentatively agreed on supply and manufacture of the drug product to its licensees. The terms including quantities and commercial terms for the future supply will be subject to separate negotiations.

For further information on revenue recognition, see Notes 2.22 and 3.

2.7. Recognition of government grants

The direct government grants are recognised as other operating income at the same time as the underlying expenditure is incurred, provided that there is reasonable assurance that the Company will receive the grant and complies with the conditions of such grant. Direct grant payments received in advance of the incurrence of the expenditure that the grant is intended to compensate are deferred at the reporting date and presented under advances received on the balance sheet.

The indirect government assistance in the form of below-market interest government loans is recognised as grant income and recorded as other operating income in the same period in which the company recognises the expenses for which the benefit is intended to compensate. Grant income is measured as the difference between the initial carrying value of the loan and the proceeds received.

2.8. Research and development expenses

Research and development costs are expensed as incurred and presented under research and development expenses in the statement of comprehensive income. Research and development expenses include costs for outsourced clinical trial services, materials and services, employee benefits and other expenditure directly attributable to the Company's research and development activities. The Company's research and development expenses are directly related to the Company's development projects and may therefore fluctuate strongly from year to year.

Capitalization of expenditure on the development of the Company's products commences from the point at which technical and commercial feasibility of the product can be demonstrated and it is probable that future economic benefits will result from the product once completed. As at 31 December 2017, considering the development stage of the Company's drug candidates, no internally developed assets related to Company's development activities had met these criteria and had therefore not been recognised. The uncertainties inherent in developing pharmaceutical products prohibits the capitalization of internal development expenses as an intangible asset until the marketing approval has been received from the relevant regulatory agencies.

2.9. Employee benefits

The Company's employee benefits consist of short-term employee benefits, post-employment benefits (defined contribution pension plans) and share-based compensation. Short-term employee benefits are charged to the statement of comprehensive income in the year in which the related service is provided. Under defined contribution plans, the Company's contributions are recorded as an expense in the accounting period to which they relate and the Company does not have any further obligations once the contributions have been paid.

2.10. Share-based compensation

The options and warrants granted under share-based incentive programs are measured at fair value at earlier of the grant date or the service commencement date, using the Black-Scholes

valuation model. The options, for which the option exercise price is determined later, right before the vesting, an estimate is used to determine the fair value at service commencement date and the estimate is subsequently revised until the options become granted.

The share-based compensation expense is recognised on a straight-line basis over the vesting period together with a corresponding increase in equity, based on the Company's estimate of equity instruments that will eventually vest. At each reporting date, the Company revises its estimate of the number of equity instruments that are expected to vest and its estimate of the grant date fair value for the options with earlier service commencement date. The exercise price paid by the option or warrant holder to subscribe the Company's shares is recognised in the reserve for invested unrestricted equity.

2.11. Loss per share

Basic loss per share is calculated by dividing the loss for the period with the weighted average number of ordinary shares during the year.

Since the Company has reported losses, inclusion of unexercised options and warrants would decrease the loss per share and therefore not taken into account in diluted loss per share calculation.

2.12. Income tax

Income tax expense for the period consists of current and deferred taxes. Tax is recognised in the statement of comprehensive income, except for the income tax effects of items recognised in other comprehensive income or directly in equity, which is similarly recognised in other comprehensive income or equity.

Deferred taxes are recognised using the liability method on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred taxes are determined using tax rates enacted or substantively enacted by the balance sheet date in the respective countries and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable income will be available against which the temporary differences can be utilized.

2.13. Machinery and equipment

The Company's machinery and equipment comprise of office furniture and equipment, which is stated at historical cost less depreciation and any impairment losses. The historical cost includes expenditure that is directly attributable to the acquisition of the machinery and equipment.

Depreciation is calculated using the straight-line method over the asset's estimated useful life of four years. Depreciation is recorded to the costs of the asset function.

2.14. Intangible assets

The Company's intangible assets comprise of capitalized patent costs arising in connection with the preparation, filing and obtaining of patents. Patent cost are amortised on a straight-line basis over the useful lives of the patents of ten years.

2.15. Impairment of non-financial assets

Assets that are subject to depreciation or amortisation are reviewed for impairment whenever there are indications that the carrying amount may not be recoverable.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. The value in use represents the discounted future net cash flows expected to be derived from the asset.

2.16. Inventories

Inventories are stated at the lower of cost and net realizable value. The cost includes all costs of direct materials and external services associated with the process of manufacturing of the goods sellable upon obtaining the regulatory marketing approval. The cost of inventories is fully written down, with a corresponding charge recognised in research and development expenses until such approval has been obtained. When marketing approval from the relevant regulatory authority is received, the write-down is reversed to net realisable value, which may not exceed the original cost.

2.17. Financial assets

The Company's financial assets comprise of other receivables and cash and cash equivalents, which are all classified to the category "loans and receivables". Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the reporting date, which are classified as non-current assets.

Other receivables consist mainly of the deferred grant income from the European Union for which the grant payment

has not been received, carried at the amount expected to be received according to the terms and conditions of the grant.

Cash and cash equivalents comprise cash on hand and at banks.

2.18. Financial liabilities

The Company's financial liabilities comprise of interest bearing borrowings, trade payables, other non-current and current liabilities.

Borrowings are initially recognised at fair value, less any directly attributable transaction costs. Subsequently borrowings are carried at amortised cost using the effective interest method. Borrowings are presented as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting period. Borrowings are not derecognised until the liability has ceased to exist, that is, when the obligation identified in a contract has been fulfilled or cancelled or is no longer effective.

Borrowings comprise of three government loans with a below-market rate of interest from The Finnish Funding Agency for Technology and Innovation ("Tekes", currently "Business Finland"), of which two have been fully drawn down before the Company's date to transition to IFRS. Accordingly, the Company has utilized the IFRS 1 exemption and not accounted for the below-market grant separately for these two loans, which are carried at amortised cost.

The government loan originated after the date of transition to IFRS was initially recognised and measured at fair value and subsequently at amortised cost over the loan period by using the effective interest method. The grant component of the loan, which is the benefit of the below-market interest rate, is measured as the difference between the initial fair value of the loan and the proceeds received.

Trade payables and other liabilities are classified as current liabilities, unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting period, in which case they are classified as non-current liabilities. The carrying amount of trade payables and other current liabilities are considered to be the same as their fair values, due to their short-term nature. Non-current liabilities are initially measured at fair value and subsequently at amortised cost.

2.19. Equity

The Company's equity comprises of share capital, reserve for invested unrestricted equity and accumulated deficit. The proceeds from issuance of new ordinary shares, less incremental costs directly attributable to the issue, are credited to the reserve for invested unrestricted equity, in accordance with the terms and conditions of the share issue.

The accumulated deficit comprises of the accumulated profits and losses of the Company since the inception.

2.20. Leases

The Company as lessee

Leases of equipment, where substantially all the risks and rewards of ownership, are classified as finance leases. Assets leased under finance leases are capitalized at the inception of the lease at the lower of the fair value of the leased property and the present value of the minimum lease payments. Lease obligations are included in current and non-current financial liabilities based on their maturity, net of finance charges. The interest element of the payments is expensed. An asset recognised under a finance lease is depreciated over its useful life.

Leases where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the lease term. The Company has no finance leases.

2.21. Provisions and contingent liabilities

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. The Company does not have provisions at the end of the reporting periods presented in these financial statements.

A contingent liability is a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence of uncertain future events not wholly within the control of the entity. Such present obligation that probably does not require settlement of a payment obligation and the amount of which cannot be reliably measured is also considered to be a contingent liability. Contingent liabilities are disclosed in the notes to the financial statements.

2.22. Critical accounting estimates and significant management judgements in applying accounting policies

Revenue recognition

The Company early adopted IFRS 15 on 1 January 2017 with full retrospective application. In determining the amounts to

be recognised as revenue, the Company uses its judgement in the following main issues:

- Identifying the performance obligations in the license agreements and determining whether the license provided is distinct - based on the Company's analysis, the license is distinct as the licensee is able to benefit from the license on its own at its current stage and the licensee has the responsibility for the development in that territory. The management has determined that the provision of data and information generated by the Company in connection with its own development activities to facilitate the licensees' territory-specific development efforts is immaterial (perfunctory) to the grant of the license to the IP and does not constitute a separate performance obligation.

- Management has concluded that the license meets the criteria to be classified as a right to use, as the license granted provides at the outset of the contract all necessary documents and knowhow to utilize the license. The contract does not define activities that would significantly affect the intellectual property to which the licensee has rights after the date of granting.

Share-based compensation

The Company recognises expenses for share-based compensation. For share options and warrants management estimates certain factors used in the option pricing model, including volatility, vesting date of options and number of options and warrants likely to vest. If these estimates vary from actual occurrence, this will impact the value of the share-based compensation. Further details of the Company's estimation of share-based compensation are disclosed in note 18.

Clinical trial accruals

Quantification of the accruals related the clinical trials require significant management judgement. The services invoiced by Contract Research Organisations consist of contributions of various independent subcontractors and the actual tasks completed may be reported with significant delays. Also the clinical study sites, which are mainly public sector hospitals, may invoice their costs with long delays. These factors combined result in a complicated task of defining on which period the cost belongs to and requires management to make assumptions when defining the right timing of the delivered services.

2.23. New and amended standards and interpretations adopted by the Company

- In May 2014, the IASB issued IFRS 15, *Revenue from Contracts with Customers*, which establishes principles for reporting information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard replaces IAS 18, *Revenue*, and IAS 11, *Construction Contracts*, and related interpretations. The Company adopted IFRS 15, and all related amendments, on 1 January 2017 on a full retrospective basis. The 2016 comparatives, in respect of IFRS 15, have been presented on a full retrospective basis as required. For further information of the Company's adoption of IFRS 15, see Note 2.2.

- In January 2016, the IASB issued *Recognition of Deferred Tax Assets for Unrealised Losses (Amendments to IAS 12)* which amended IAS 12, *Income Taxes*. The amendments primarily were issued to clarify the recognition of deferred tax assets for unrealized losses related to debt instruments measured at fair value. The Company adopted these amendments on 1 January 2017 and it did not have a material impact on the Company's financial statements.

- In January 2016, the IASB issued *Disclosure Initiative (Amendments to IAS 7)* which amended IAS 7, *Statement of Cash Flows*. The amendments require entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities. The Company adopted these amendments on 1 January 2017, which did not have a material impact on the Company's financial statements. The enhanced presentation requirements under the amendments are disclosed in Note 19.

2.24. New standards and interpretations issued not yet effective

- In July 2014, the IASB published the final version of IFRS 9, *Financial Instruments*, which reflects all phases of the financial instruments project and replaces IAS 39, *Financial Instruments: Recognition and Measurement*, and all previous versions of IFRS 9, *Financial Instruments*. IFRS 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities, introduces new rules for hedge accounting and a new impairment model for financial assets. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application

permitted. The Company will apply IFRS 9 retrospectively as required by the standard, but will not restate comparative financial information. Upon adoption on 1 January 2018, the Company does not expect IFRS 9, Financial Instruments to have a material impact on the financial statements, as the most significant financial instrument the Company holds is cash and cash equivalents and the standard will not materially impact the classification or measurement of cash and cash equivalents.

- In June 2016, the IASB issued three amendments to IFRS 2, Share-based Payment, in relation to the classification and measurement share-based compensation transactions. The amendments clarify how to account for certain types of share-based payment transactions and provide requirements on the accounting for:
  - The effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments;
  - Share-based payment transactions with a net settlement feature for withholding tax obligations; and
  - A modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled

The amendments are effective for accounting periods beginning on or after 1 January 2018. The amendments are required to be applied without restating prior periods, but retrospective application is permitted if elected for all three amendments and other criteria are met. The Company does not expect the amendments to IFRS 2, *Share-based Payment*, to have any material impact on the Company's financial statements.

- In January 2016, the IASB published IFRS 16, *Leases*, its new leasing standard, which will replace the current guidance in IAS 17, *Leases*, and related interpretations IFRIC 4, SIC-15 and SIC-27. The new standard will result in almost all leases being recognised on the balance sheet, as the distinction between operating and finance leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The only exceptions are short-term and low-value leases. The standard applies to annual periods beginning on or after 1 January 2019, with earlier application permitted. As a result of the new standard, the Company will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset. The Company is continuing to assess the impact of the new Leasing standard. The new standard is not expected to have a material impact on the Company's balance sheet upon adoption (for more information on operating leases see Note 23).

There are no other IFRS or IFRIC interpretations that are not effective that are expected to have a material impact on the Company.

3. Revenue

The Company has entered into exclusive license agreements with Maruishi in Japan, with A&B in Greater China and with Pharmbio in the Republic of Korea for the development, commercialization and supply of Traumakine and is entitled to related milestone payments. The Company retains rights to Traumakine in the rest of the world. The license partners are responsible for all regulatory activities and needed clinical activities necessary for commercialization in respective territories. Under the license agreements, the Company is also entitled to receive royalty payments based on the product sales in territories, but such royalties have not been earned or recognised to revenue during the periods presented.

License agreement and supply agreement with Maruishi

In 2011, the Company entered into a license agreement with Japanese license partner Maruishi. The Company has not recognised revenue for the Maruishi license agreement during the periods presented, but is entitled to receive additional payments upon achievement of certain development or commercial milestones.

In 2014, the Company entered into a separate supply agreement with Maruishi for the delivery of investigational medicinal products to be used in territory-specific clinical studies. During 2016, the Company has recognised revenue of EUR 202 thousand based on physical delivery of the goods.

License agreement with Pharmbio

In 2016, the Company entered into license agreement with Korean license partner Pharmbio and met the upfront at signing. In this connection the Company satisfied the performance obligation for the grant of the license and use of its IP and recognised revenue in the amount of EUR 750 thousand. The Company is entitled to receive additional milestone payments from Pharmbio only if certain development or commercial milestones are achieved.

4. Segment reporting

The Company is a late clinical stage drug discovery and development company. Its operations have been focused on the development of its main drug candidates Traumakine and Clevegen. The Company's chief operating decision maker has been identified as the Chief Executive Officer (CEO).

The CEO manages the Company as one integrated business and hence the Company has one operating and reportable segment.

The Company had no revenue in 2017. In 2016, the Company had revenue of EUR 952 thousand of which EUR 750 thousand from Republic of South-Korea and EUR 202 thousand from Japan. In 2016, the revenue from Maruishi and Pharmbio, each, exceeded 10% of the Company's revenue.

All of the Company's non-current assets are located in Finland.

5. Other operating income

€'000	Year ended 31 December 2017	2016 (Restated)
Grants from the European Union	1,063	873
Grant component of government loans	432	148
Other income	-	4
Total operating income	**1,495**	**1,025**

Grants from the European Union comprise of direct funding from the European Commission under the Seventh Framework Programme for Research and Technological Development to support the Traumakine clinical program. The grant component of government loans comprises of indirect financial benefit from the below-market interest of a loan from the Finnish Funding Agency for Technology and Innovation ("Tekes", currently "Business Finland"), which has been granted to finance the Clevegen clinical development program.

6. Research and development expenses

€'000	Year ended 31 December 2017	2016 (Restated)
Outsourced clinical trials services	(9,392)	(5,218)
Materials and services	(4,727)	(1,594)
Employee benefits	(2,704)	(1,475)
Other R&D costs	(1,315)	(865)
Inventory write-down	(893)	-
Depreciation and amortization	(69)	(71)
Total research and development expenses	**(19,100)**	**(9,223)**

7. Employee benefits

€'000	Year ended 31 December 2017	2016 (Restated)
Salaries	(2,713)	(1,636)
Pension expenses – contribution-based plans	(360)	(219)
Social security contributions	(107)	(90)
Share-based compensation	(1,189)	(936)
Total employee benefit expenses	**(4,369)**	**(2,881)**
Employee benefit expenses by function		
Research and development expenses	(2,704)	(1,475)
General and administrative expenses	(1,665)	(1,406)
Total employee benefit expenses	**(4,369)**	**(2,881)**

The average number of personnel in 2017 was 18 (2016: 10). Share-based compensation information is included in Note 18 and management remuneration information in Note 24.

8. Depreciation and amortisation

€'000	Year ended 31 December 2017	2016 (Restated)
Depreciation and amortisation by type of asset		
Intangible assets - patents	(69)	(71)
Machinery and equipment	(7)	(7)
Total depreciation and amortisation	**(76)**	**(78)**
Depreciation and amortisation by function		
Research and development expenses	(69)	(71)
General and administrative expenses	(7)	(7)
Total depreciation and amortisation	**(76)**	**(78)**

9. Financial income and expenses

€'000	Year ended 31 December 2017	2016 (Restated)
Financial income		
Interest income	-	0
Gains from foreign exchange	7	0
Total financial income	**7**	**0**
Financial expenses		
Interest expenses	(75)	(24)
Losses from foreign exchange	(332)	(333)
Other financial expenses	(1)	(3)
Total financial expenses	**(408)**	**(360)**
Total financial income and expenses, net	**(401)**	**(360)**

Interest expenses consist of paid and accrued interest expenses. The accrued interest expense relates mainly to the government loans (Note 19).

The foreign exchange losses relate to euro value changes of cash balances nominated in Pound Sterling.

Unrealised foreign exchange loss is EUR 290 thousand and gain is EUR 627 thousand for the years ended 31 December 2017 and 2016, respectively.

10. Tax expense

€'000	Year ended 31 December 2017	2016
Tax expense	(1)	(75)
Total tax expense	**(1)**	**(75)**

During the financial year ended 31 December 2016, income tax consists of foreign withholding tax on upfront fee received.

The difference between income taxes at the statutory tax rate in Finland (20%) and income taxes recognised in the statement of comprehensive income is reconciled as follows:

€'000	Year ended 31 December 2017	2016 (Restated)
Loss before tax	(21,060)	(10,063)
Income tax calculated at Finnish tax rate 20%	4,212	2,013
Tax losses and temporary differences for which no deferred tax asset is recognised	(3,974)	(1,937)
Non-deductible expenses and tax exempt income	(238)	(1)
Non-credited foreign withholding taxes	(1)	(75)
Taxes in the statement of comprehensive income	**(1)**	**(75)**

Tax losses and deductible temporary differences for which no deferred assets have been recognised, are as follows:

€'000	Year ended 31 December 2017	2016 (Restated)
R&D expenses not yet deducted in taxation [1]	16,893	47
Tax losses carried forward [2]	25,862	23,527
Deferred tax depreciation on fixed assets	1,628	1,012
Total	**44,383**	**24,586**

1) The Company has incurred research and development costs, mostly during the year ended 31 December 2017, that have not yet been deducted in its taxation. The amount deferred for tax purposes can be deducted over an indefinite period.
2) Tax losses carried forward expire over the period of 10 years. The tax losses will expire as follows:

€'000	2017	2016
Expiry within five years	3,164	1,565
Expiry within 6-10 years	22,698	21,962
Total	**25,862**	**23,527**

The related deferred tax assets have not been recognised in the balance sheet due to the uncertainty as to whether they can be utilized. The Company has a loss history, which is considered a significant factor in the consideration of not recognising deferred tax assets. The total tax value of unrecognised deferred tax assets is EUR 8,877 thousand (2016: EUR 4,917 thousand).

The Company does not have any other deductible or taxable temporary differences. Therefore, no deferred tax assets or liabilities have been recognised in the balance sheet and thus the itemisation of deferred taxes is not provided.

11. Loss per share

Loss per share is calculated by dividing the net loss by the weighted average number of ordinary shares in issue during the year.

€'000	Year ended 31 December 2017	2016 (Restated)
Loss for the period	(21,061)	(10,138)
Weighted average number of ordinary shares in issue	27,887,901	23,979,650
Basic and dilutive loss per share (in €)	**(0.76)**	**(0.42)**

As of 31 December 2016, the Company had two potentially dilutive instruments comprising of share options and warrants.

As of 31 December 2017, the Company had only share options outstanding as the warrants were exercised during the period. Number of potentially dilutive instruments currently outstanding totalled 1,540,900 as of 31 December 2017 (31 December 2016: 1,451,500). Since the Company has reported a net loss, the share options and warrants would have an anti-dilutive effect and are therefore not taken into account in diluted loss per share -calculation. As such, there is no difference between basic and diluted loss per share.

12. Intangible assets and machinery and equipment

€'000	Intangible assets	Machinery and equipment
Book value 1 January 2016 (restated)		
Acquisition cost (restated)	348	32
Accumulated depreciation/amortisation	(65)	(4)
Book value 1 January 2016 (restated)	**283**	**28**
Additions	92	0
Depreciation/amortisation (restated)	(71)	(7)
Book value 31 December 2016 (restated)	**304**	**21**
As at 31 December 2016 (restated)		
Acquisition cost	440	28
Accumulated depreciation/amortisation	(136)	(7)
Book value 31 December 2016 (restated)	**304**	**21**
Book value on 1 January 2017	**304**	**21**
Additions	90	8
Depreciation/amortisation	(69)	(7)
Book value 31 December 2017	**325**	**22**
As at 31 December 2017		
Acquisition cost	530	36
Accumulated depreciation/amortisation	(205)	(14)
Book value 31 December 2017	**325**	**22**

13. Non-current prepayments and other receivables

€'000	As at 31 December 2017	2016 (Restated)
Prepayments for API	1,192	1,451
Production supplies	86	-
Other receivables	32	24
Total non-current prepayments and other receivables	**1,310**	**1,475**

Prepayments for API consist of payments remitted to manufacturer for API to be consumed in the Company's development activities. Other receivables consist of restricted cash in the form of security deposits for rental agreements.

14. Inventories

€'000	As at 31 December 2017	2016 (Restated)
Work in process	893	-
Write-down of inventory	(893)	-
Total inventories	**-**	**-**

Inventories purchased prior to regulatory marketing approval are recognised as inventory but are subject to full write-down. Write-downs of inventories to net realisable value amounted to EUR 893 thousand (2016 nil). These were recognised as research and development expenses. The Company has not reversed any previous inventory write-downs.

15. Current prepayments and other receivables

€'000	As at 31 December 2017	2016 (Restated)
Prepayments	1,594	1,200
Grant receivable	1,063	160
Receivable for production defects	434	-
VAT receivable	404	342
Receivable for joint purchase agreement	-	474
Other receivables	425	293
Total current prepayments and other receivables	**3,920**	**2,469**

The majority of prepayments consist of the Clinical Service Agreements with Contract Research Organisations, which are or were current service providers in different clinical trials. Grant receivable consist of the grant income from the European Union for which the grant payment has not been received.

16. Cash and cash equivalents

€'000	As at 31 December 2017	2016
Bank accounts	9,310	11,478
Total cash and cash equivalents	**9,310**	**11,478**

17. Shareholders' equity

Movements in number of shares, share capital and reserve for invested unrestricted equity were as follows.

€'000	Total registered shares (pcs)	Share capital	Reserve for unrestricted equity
1 January 2016	**23,111,704**	**2,691**	**23,843**
Issue of new shares, net of transaction costs	3,200,000	-	8,519
31 December 2016	**26,311,704**	**2,691**	**32,362**
1 January 2017	**26,311,704**	**2,691**	**32,362**
Issue of new shares, net of transaction costs	2,672,340	-	15,863
Exercise of warrants	151,400	-	254
Exercise of options	29,100	-	97
31 December 2017	**29,164,544**	**2,691**	**48,576**

On 23 September 2016, the number of shares was increased to 26,311,704 following the issue of 3,200,000 new shares. On 1 March 2017, the number of shares was increased to 27,734,044 following the issue of 1,422,340 new shares. On 27 April 2017, the number of shares was increased to 27,787,034 following the issue of 52,990 new shares due to exercise of warrants. On 31 May 2017, the number of shares was increased to 27,914,544 following the issue of 127,510 new shares due to exercise of warrants and options and on 11 October 2017, the number of shares was increased to 29,164,544 following the issue of 1,250,000 new shares.

The Company has one class of ordinary shares. The shares have no par value. Each share entitles the holder to one vote at the Annual General Meeting and equal dividend. All shares are fully paid.

The subscription price for the shares is recorded to the share capital, unless the Board has made a resolution to record the subscription price in the reserve for invested unrestricted equity. If the shares of a Finnish limited liability company have no par value according to its articles of association, the Finnish Limited Liability Companies Act allows companies the recognition of the proceeds from share issuance to the reserve for invested unrestricted equity. In such situations the board of a company can choose on a subscription by subscription basis, how much of the issue, if anything, is recorded in share capital and how much to the reserve for invested unrestricted equity that is distributable. During 2016 and 2017, the Board recognised all relevant transactions in the invested unrestricted equity reserve.

18. Share options and warrants

Option Plan 2015

The Option Plan 2015 was approved at the Company's extraordinary shareholders' meeting on 15 September 2015 as part of the Company's incentive scheme determined by the Board of Directors. The share options are granted to the members of the Board of Directors and the management team and other management and employees for no consideration. The annual general meeting on 10 May 2017 resolved to amend, due to the increase in the number of employees in the Company and the increase in the number of members of the Board of Directors, the Option Plan so that a maximum total of 500,000 C options and a maximum total of 500,000 D options may be offered under initial Option Plan terms and conditions. The share options have a service condition and are forfeited in case the employee leaves the Company before the share options vest, unless the Board of Directors approves otherwise. After the beginning of the share subscription period, the vested options may be freely transferred or exercised. The fair value of the options has been determined by using the Black & Scholes option valuation model and expensed over the vesting period. Grant dates for the share options may vary depending on the date when the Company and the employees agree to the key terms and conditions of the Option Plan. The maximum number of share options that can be awarded under the Option Plan is 1.800.000 in four different tranches designated as A options, B options, C options and D options. Each share option entitles the holder of the option to subscribe for one ordinary share in the Company.

The exercise price for ordinary shares based on A options is euro equivalent of the Company's share subscription price in the Company's initial public offering on the AIM market place of the London Stock Exchange on 17 November 2015. The exercise price for ordinary shares based on B options, C options and D options is euro equivalent of the exercise price determined based on the Company's average share price on the AIM market place during 1 July - 30 September 2016, 2017 and 2018, respectively.

Key characteristics and terms of the option plan are listed in the table below.

2015 Option Plan	A options	B options	C options	D options
Maximum number of share options	400,000	400,000	500,000	500,000
Exercise price, EUR	3.71	2.90	8.39	(*)
Dividend adjustment	No	No	No	No
Beginning of subscription period	2 November 2015	8 October 2016	8 October 2017	8 October 2018
End of subscription period	20 September 2021	20 September 2021	20 September 2021	20 September 2021
Vesting conditions	Service until the beginning of the subscription period			

(*) Exercise price will be determined based on euro equivalent of the Company's average share price on the AIM market place during 1 July - 30 September 2018.

Number of share options	For the year ended 31 December 2017 2015 Option Plan A	B	C	D	For the year ended 31 December 2017 2015 Option Plan A	B	C	D
Outstanding at 1 January	400,000	400,000	250,000	250,000	250,000	250,000	250,000	250,000
Granted	-	-	250,000	20,000	150,000	150,000	-	-
Forfeited	-	-	-	-	-	-	-	-
Exercised	(15,000)	(14,100)	-	-	-	-	-	-
Outstanding at 31 December	385,000	385,900	500,000	270,000	400,000	400,000	250,000	250,000
Exercisable at 31 December	385,000	385,900	500,000	-	400,000	400,000	-	-
The weighted average fair value of the share options granted, EUR	-	-	3.23	0.53	1.27	1.43	-	-
The weighted average share price at the date of exercise, EUR	8.83	8.83	-	-	-	-	-	-

Determination of the fair value for the share options granted	2017 2015 Option Plan C	D	2016 2015 Option Plan A	B
Share price at grant date, EUR	4.51-9.39	9.21	2.69-3.38	2.96-4.10
Subscription price, EUR	4.51-8.39	9.21	3.71	2.90-4.10
Volatility, % (*)	42.59-52.57	42.59	50.03-52.57	50.03-52.57
Risk-free interest rate, %	0.01	0.01	0.01	0.01
Expected dividends yield, %	0	0	0	0
Option fair value, EUR	1.42-4.01	2.87	1.00-1.54	1.32-1.57
Effect on earnings 2016, EUR thousand (**)	43	-	191	188
Effect on earnings 2017, EUR thousand (**)	758	25	-	-

(*) Expected volatility was determined as the average volatility of a peer group consisting of ten comparable biotechnology companies listed on London Stock Exchange AIM list.
(**) Effect of share options granted on earnings is calculated based on earlier of the grant date or the service commencement date.

The share-based compensation expense for the Option Plan 2015, was EUR 1,189 thousand in 2017 (EUR 936 thousand in 2016).

Warrants

Based on authorization given by the Company's extraordinary shareholders' meeting on September 15, 2015, the Board of Directors approved on 16 September 2015, the issuance of 151,400 warrants that entitle to subscription of a maximum number of 151,400 ordinary shares in the Company. The warrants were issued in exchange for services received from a Company's external advisor as the services were incurred. The warrants were granted in two tranches designated as Warrants A and Warrants B and each warrant entitles the holder of the warrant to subscribe for one ordinary share in the Company. After the beginning of the share subscription period, the vested warrants may be freely transferred or exercised. The fair value of the warrants was determined at the grant date or by using the Black & Scholes valuation model and expensed over the vesting period during 2015.

Tranche	Number of warrants	Share subscription period	Exercise price, EUR
Warrants A	109,800	2 November 2015 – 7 May 2018	1.55
Warrants B	41,600	2 November 2015 – 28 February 2018	2.01

	2017		2016	
Number of warrants	Warrants A	Warrants B	Warrants A	Warrants B
Outstanding at 1 January	109,800	41,600	109,800	41,600
Granted	0	0	0	0
Forfeited	0	0	0	0
Exercised	(109,800)	(41,600)	0	0
Outstanding at 31 December	0	0	109,800	41,600
Exercisable at 31 December	0	0	109,800	41,600
The weighted average share price at the date of exercise, EUR	8.72	8.72	-	-

All of the warrants the Company had issued in 2015, were exercised during 2017.

19. Financial assets and liabilities

€'000	As at 31 December 2017	2016 (Restated)
Loans and receivables		
Other receivables (*)	1,497	634
Cash and cash equivalents	9,310	11,478
Total loans and receivables	10,807	12,112
Financial liabilities measured at amortised cost		
Trade payables	3,196	2,021
Borrowings in form of Tekes R&D loans	2,426	2,176
Total financial liabilities measured at amortised cost	5,622	4,197

*Prepayments are excluded as they are not considered to be financial instruments.

Due to the short-term nature of the other receivables, their carrying amount is considered to equal their fair values.

Borrowings in the form of Tekes R&D loans

Fair value for the Tekes R&D loans is calculated by discounting estimated future cash flows for the loans using appropriate interest rates at the reporting date. The discount rate considers the risk-free interest rate and estimated margin for the Company's own credit risk. Discounted future cash flows are derived from the terms containing the repayment amounts and repayment dates for the principal and the cash payments for interest. Given that some of the inputs to the valuation technique rely on unobservable market data, loan fair values are classified in Level 3.

The fair value of all the Tekes loans was EUR 2,139 thousand (2016 EUR 2,035 thousand).

Tekes R&D loans are granted to a defined product development project and cover a contractually defined portion of the underlying development projects' R&D expenses. The below-market interest rate for these loans is the base rate set by the Ministry of Finance minus three (3) percentage points, subject to a minimum rate of 1%. Repayment of these loans shall be initiated after 5 years, thereafter loan principals shall be paid back in equal instalments over a 5-year period, unless otherwise agreed with Tekes. For more information on contractual maturities of the Tekes R&D loans and interests is provided in the Note 19. The accrued interest on Tekes R&D loans amounted to EUR 65 thousand (2016 EUR 20 thousand).

This section sets out an analysis of net debt and the movements in net debt (calculated as cash and cash equivalents less borrowings) for each of the periods presented.

€'000	As at 31 December 2017	2016 (Restated)
Net debt		
Cash and cash equivalents	9,310	11,478
Tekes R&D loans- repayable within one year	(338)	(93)
Tekes R&D loans- repayable after one year	(2,088)	(2,083)
Net debt	6,884	9,302

€'000	Cash and cash equivalents	Borrowings	Total
Net debt as at 1 January 2016	11,068	(1,691)	9,377
Cash flows	(217)	(775)	(992)
Foreign exchange adjustments	627	-	627
Other non-cash movements	-	290	290
Net debt as at 31 December 2016	**11,478**	**(2,176)**	**9,302**
Cash flows	(1,878)	(369)	(2,247)
Foreign exchange adjustments	(290)	-	(290)
Other non-cash movements	-	119	119
Net debt as at 31 December 2017	**9,310**	**(2,426)**	**6,884**

20. Financial risk management

The operations of the Company expose it to financial risks. The main risk that the Company is exposed to is liquidity risk, with capital management being another important area given the nature of the Company's operations and its financing structure. The Company's risk management principles focus on obtaining funding and managing capital taking into consideration the unpredictability of the financial markets with the aim at minimizing any undesired impacts on the Company's financial performance and position. The Board of Directors define the general risk management principles and approve operational guidelines concerning specific areas including but not limited to liquidity risk, foreign exchange risk, interest rate risk, credit risk, the use of any derivatives and investment of the Company's liquid assets.

(a) Capital management and liquidity risks

The Company's objective when managing capital is to safeguard the Company's ability to continue as a going concern (refer to notes 2.3 and 16).

Significant financial resources are required to advance the drug development programs into commercialized pharmaceutical products. The Company relies on its ability to fund the operations of the Company through three major sources of financing – equity financing, research and development grants and loans and licensing agreements.

The Company has been able to fund its operations with equity and R&D loans. While equity financing has been available in the past (the last such financing was a EUR 15.8 million share issue in February 2018), there can be no assurance that sufficient funds can be secured in order to permit the Company to carry out its planned activities. In general, capital market conditions are volatile. The prevailing financial market situation and the overall investor's sentiment dictate whether the Company is able to secure additional financing in the future, which can be considered a risk. To partly manage this risk, the Company and its management is in constant dialogue with financial investors, investment banks, debt providers and other market participants.

The Company also relies on different sources of research and development grants and loans. These funds, which are provided through regional, national or EU level institutions, have been historically available to the Company. The Company strictly complies with all rules and legal obligations pertaining to these funding programs and is in regular contact with the funding agencies providing these. Availability of such funds in the future cannot be guaranteed and thus this poses a potential risk to the Company's funding in the future.

Finally entering into commercialization, collaboration and licensing agreements with larger pharmaceutical companies entitles the Company to receive up-front and milestone payments related to agreed regulatory or commercial points, as well as royalty payments once commercialization has been successful. Activities in the area of business development are targeted at securing such agreements. Consideration of these activities is part of the management's duties and is monitored by the Board of Directors, which ultimately decides on entering into such agreements.

There can be no assurance that sufficient financing can be secured in order to permit the Company to carry out its planned activities. To protect the continuity of the Company's operations, sufficient liquidity and capital has to be maintained.

The Company aims to have funds to finance its operations for the foreseeable future. The Company can influence the amount of capital by adapting its cost basis considering available financing. Management monitors liquidity on the basis of the amount of funds. These are reported to the Board of Directors on a monthly basis.

The Company's Board of Directors approves the operational plans and budget and monitors the implementation of these plans and the financial status of the Company on a monthly basis.

As at 31 December 2017, the contractual maturity of loans and interests was as follows:

€'000	2018	2019	2020	2021– thereafter	Total
R&D loans					
Repayment of loans	347	338	338	1,403	2,426
Interest expenses	25	21	18	42	106
Total	**372**	**359**	**356**	**1,445**	**2,532**

As at December 31, 2016, the contractual maturity of loans and interest was as follows:

€'000	2017	2018	2019	2020– thereafter	Total
R&D loans					
Repayment of loans	84	347	338	1,407	2,176
Interest expenses	26	25	21	60	132
Total	**110**	**372**	**359**	**1,467**	**2,308**

(b) Market risk

i. Foreign exchange risk

The Company operates internationally but is mainly exposed to translation risk in respect of Pound Sterling ("GBP") denominated cash and cash equivalents balances The Company's policy is not to hedge translation risk. As of 31 December 2017, the Company had cash and cash equivalents of EUR 359 thousand and GBP 7,941 thousand (2016: EUR 6.390 thousand and GBP 4.356 thousand) and the foreign exchange gains and losses recorded arise mainly from the GBP cash balances. The Company is not exposed to significant transaction risk, as the Company mainly operates in its functional currency, the EUR.

ii. Interest rate risk

The Company's interest rate risk arises from Tekes R&D loans, which interest is the base rate defined by the Finnish Ministry of Finance minus three (3) percentage points, subject to minimum rate of 1%. During the periods presented, the interest has been below the minimum level and the Company has paid the minimum interest of 1% on the loans. During the periods presented, the Company has not been exposed to variable interest rate risk and accordingly the Company has not entered into derivative contracts.

(c) Credit and counterparty risk

The Company works with partners and financial institutions with good credit ratings. Management monitors credit ratings of the financial institutions that hold the Company's bank deposits regularly. Further, the Company currently derives its revenue from restricted number of reputable licence partners in specific territories. This risk of concentration of creditors is partly mitigated by the fact that these partners are financially solid. These licence agreements are governed by contractual relationships that typically address and describe remedies for situations in which interests of the Company and the partner are no longer aligned.

21. Other non-current liabilities

€'000	As at 31 December 2017	2016 (Restated)
Clinical trial hospital fees	-	337
Accrued uninvoiced research costs		277
Total	**-**	**614**

22. Trade payables and other current liabilities

€'000	As at 31 December 2017	2016 (Restated)
Trade payables	3,196	2,021
Clinical trial hospital fees	1,241	245
Advances received	976	1,021
Accrued payroll	969	599
Accrued milestone payment	600	600
Accrued research costs	350	-
Other accruals	84	5
Other liabilities	302	65
Total	**7,718**	**4,556**

Advances received comprise mainly received grant payments from European Union for which the related grant income has not yet been recognised or which have not been forwarded to the other participants of the grant consortium. For further information about grant income (Note 5).

Accrued expenses comprise mainly accrued clinical trial fees EUR 1,241 thousand (31 December 2016: EUR 245 thousand), salary accruals EUR 969 thousand (31 December 2016: EUR 599 thousand) and milestone payment EUR 600 thousand (31 December 2016: EUR 600 thousand).

23. Contingencies and commitments

Operating lease – Faron as a lessee

The future aggregate minimum lease payments under non-cancellable operating leases are as follows

€'000	Year ended 31 December 2017	2016
No later than 1 year	172	144
Later than 1 year and no later than 5 years	231	261
Later than 5 years	-	-

The Company's operating lease commitments comprise of rent commitments for leasehold properties and lease commitments for cars, machines and equipment with leases of 3 to 4 years. The Company's operating leases are non-cancellable and they do not include redemption or extension options.

Contractual contingencies

In addition to the accrued milestone payment to a subcontractor of Traumakine of EUR 600 thousand as presented in note 22, the Company has contingent milestone payments of EUR 1,400 thousand to the same party that will become payable only upon the Company achieving certain milestones it its clinical development and obtaining the regulatory approval for Traumakine.

The Company has a contingent contractual liability to a development party for pre-clinical product candidate Clevegen to pay milestone payments. First milestone payment of EUR 427 thousand is contingent to production system reaching certain material yield threshold and the remaining ones upon the Company achieving subsequent regulatory filings and approvals for Clevegen. The milestone payments related to subsequent regulatory filings and approvals for Clevegen are considered to be remote. At the date of these financial statements there is no certainty that the yield threshold will be reached.

24. Related party transactions

The Company identifies the following related parties:

- A&B (HK) Company Limited, an investment company existing under the laws of Hong Kong having significant influence in Faron Pharmaceuticals Oy, given its shareholding of 11.69% and membership on the Board of Directors.
- Members of the Board of Director, and their close family members; and
- Company's key Management team and their close family members

Faron has not had interests in other entities as at and for the years ended December 31, 2016 and 2017.

Key management personnel

The Company's key management personnel consist of the following:

- Members of the Board of Directors
- Management team, including CEO

€'000	Year ended 31 December 2017	2016
Compensation of key management personnel*		
Salaries and other short-term employee benefits	1,668	832
Post-employment benefits	220	159
Share-based payments	883	785
Total	**2,771**	**1,776**

The Management team was awarded 249,850 share options during 2017 (2016: 303,600 share options). At the end of the 2017, the number of outstanding options and share granted to the Management team amounted to 663,450 share options (at the end of 2016: 413,600 share options).

Non-executive Directors were awarded 40,000 share options during 2017, (2016: 0 share options). At the end of 2017, the number of outstanding options and share options granted to the non-executive directors amounted to 600,000 share options (at the end of 2016: 560,000 share options).

Management and Board shareholding

Management* shareholding, 31 December 2017	
Number of shares (pcs)	4,047,740
Shareholding, percentage	13.9%
Board shareholding, 31 December 2017**	
(excluding the shareholding of CEO and CFO)	
Number of shares (pcs)	626,169
Shareholding, percentage	2.1%
Total number of shares outstanding at 31 December 2017 (pcs)	29,164,544

*Presented information for the Management Includes the executive directors of the Board
**Presented information for the Board includes only non-executive directors.

Transactions with related parties

There are no additional related party transactions during 2017 and 2016 than already disclosed.

25. Events after the balance sheet date

On 21 February 2018 Faron announced that the Company raised EUR 15,863 thousand before expenses by way of the placing of 1,863,350 ordinary shares at the Issue Price of GBP 8.05 per share.

During the first quarter 2018, Faron Pharmaceuticals Ltd has registered subsidiaries in the United States of America and in Switzerland.

Mr. Juhana Heinonen was appointed to Chief Commercial Officer and Mrs. Maria Lahtinen to Supplier Management Director, both are members of Company's management team as of January 2018.

On May 5th the preliminary results of the INTEREST -trial were reported to the Board. The Company continues to investigate the results.

Results and dividends

The statement of comprehensive income is on page 49.
The loss for the accounting period was 21,060,638.95 euro (2016: 10,137,447.74 euro).
The Board of Directors does not recommend the payment of a dividend (2016: nil).

Board signatures

Turku, 5 May 2018

Frank Armstrong, Chairman

Markku Jalkanen

Gregory Brown

Jonathan Knowles

Matti Manner

Huaizheng Peng

John Poulos

Yrjö Wichmann

Leopoldo Zambeletti

The Auditor's Note

The report on the audit performed has been issued today

Helsinki, 7 May 2018

PricewaterhouseCoopers
Authorised Public Accountants

Panu Vänskä
Authorised Public Accountant (KHT)

Auditor's Report (Translation of the Finnish Original)

To the Annual General Meeting of Faron Pharmaceuticals Ltd.

Report on the Audit of the Financial Statements

Opinion

In our opinion, the financial statements give a true and fair view of the company's financial performance and financial position in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.

What we have audited

We have audited the financial statements of Faron Pharmaceuticals Ltd (business identity code 2068285-4) for the year ended 31 December 2017. The financial statements comprise the balance sheet, statement of comprehensive income, statement of changes in equity and statement of cash flows and notes.

Basis for Opinion

We conducted our audit in accordance with good auditing practice in Finland. Our responsibilities under good auditing practice are further described in the Auditor's Responsibilities for the Audit of Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the company in accordance with the ethical requirements that are applicable in Finland and are relevant to our audit, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Responsibilities of the Board of Directors and the Managing Director for the Financial Statements

The Board of Directors and the Managing Director are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU. The Board of Directors and the Managing Director are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Board of Directors and the Managing Director are responsible for assessing the company's ability to continue as going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting. The financial statements are prepared using the going concern basis of accounting unless there is an intention to liquidate the company or cease operations, or there is no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance on whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with good auditing practice will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with good auditing practice, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of the Board of Directors' and the Managing Director's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events so that the financial statements give a true and fair view.

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

Other Reporting Requirements

Other Information

The Board of Directors and the Managing Director are responsible for the other information. The other information comprises of the Strategic Report, Directors' Report, Directors' Remuneration Report and the Statement of Responsibilities included in the Annual Report, but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information.

In connection with our audit of the financial statements, our responsibility is to read the reports mentioned above and, in doing so, consider whether the information included in the reports are materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

In our opinion the information given in in the Strategic Report, Directors' Report, Directors' Remuneration report and the Statement of Responsibilities is consistent with the information in the financial statements.

If, based on the work we have performed, we conclude that there is a material misstatement in the reports mentioned above, we are required to report that fact. We have nothing to report in this regard.

Helsinki 7th of May 2018

PricewaterhouseCoopers Oy
Authorised Public Accountants

Panu Vänskä
Authorised Public Accountant (KHT)

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