midatech pharma

# Streamlined for success

**Annual Report & Accounts** 2018

# MIDATECH PHARMA IS AN R&D COMPANY FOCUSED ON DELIVERING INNOVATIVE ONCOLOGY AND RARE DISEASE PRODUCTS TO PATIENTS.

**We are developing a range of new or improved chemotherapeutics and immunotherapeutics, using our three proprietary platform drug delivery technologies, with the aim of improving patients' lives.**

**Cash and deposits**
£2.34m

**Total revenue**
£1.94m
**+96%**

**Statutory Revenue**
£0.15m
**+0%**

**Net loss**
from continuing operations
£10.37m

**Tax credit**
£1.95m

**Loan repayments**
£5.25m

For more information and the latest share price, go to:
**www.midatechpharma.com/investors**

## Financial highlights

- Total revenue[1] for the year from continuing operations up 96% to £1.94m (2017: £0.99m, 2016: £1.32m).
- Statutory Revenue[2] for 2018 was the same as the prior year at £0.15m (2017: £0.15m, 2016: £0.78m).
- £2.34m cash and deposits at 31 December 2018 (2017: £13.20m, 2016: £17.61m).
- Net loss from continuing operations of £10.37m (2017: £11.71m, 2016: £6.16m) with net cash outflow in the year of £10.88m (2017: £4.15m outflow, 2016: £0.97m inflow).
- Tax credit receivable of £1.95m (2017: £1.20m, 2016: £1.44m).
- Repayment of outstanding loan with MidCap Financial Trust of £5.25m (excluding early redemption fees).

## Operational highlights including post period end highlights

- MTD201 Q-Octreotide for neuroendocrine tumours and acromegaly: conducted first in-human clinical trial with data read-out in August 2018, indicating that MTD201 compares favourably with the leading product in the market.
- MTX110 for DIPG childhood brain cancer: commenced first in-human clinical trial in May 2018 at University of California San Francisco (study ongoing).
- Sale of US commercial operation, Midatech Pharma US, Inc. ('MPUS') on 1 November 2018, to Barings LLC, effected through Kanwa Holdings LP, which was established solely for the purpose of acquiring MPUS. This achieved proceeds of £10.20m before deal costs.
- Closure of the Group's research and development facility in Abingdon in December 2018, with ongoing gold nanoparticle research activities incorporated into the Group's Cardiff and Bilbao sites.
- Following the year end, strategic investment in the Company by China Medical System ('CMS') of £8m plus agreement to licence the Group's pipeline products in the Greater China Area and certain South East Asian countries.
- In conjunction with the subscription by CMS, the Company concluded a successful Placing and Open Offer, raising an additional £5.4m, approved by shareholders on 25 February 2019.
- Appointment of Dr Craig Cook as Chief Executive Officer, effective from 1 June 2018.

(1) Total revenue represents collaboration income from continuing operations plus grant revenue.

(2) Statutory Revenue represents total revenue, excluding grant revenue.

## Contents

# MIDATECH PHARMA AT A GLANCE

**Midatech is focussed on developing products based on our proprietary drug delivery platform technologies to target diseases with high unmet medical need.**

**Granted patents**
107

**Employees**
59

**Midatech Limited formed in**
2000

**Estimated Octreotide market**
£2bn
**(p.a)**

## Overview

Midatech Pharma is focussed on the research and development of medicines for rare cancers, via in-house and partnered programmes. We take existing therapies and 'make them better', using our three proprietary platform drug delivery technologies to improve the bio-delivery and bio-distribution of drugs, through either sustained delivery (Q-Sphera™), direct delivery (MidaSolve™), or targeted delivery (MidaCore™).

Listed on AIM and NASDAQ, Midatech is headquartered in the UK and employs 59 people. We have an R&D facility in Cardiff and a manufacturing site in Bilbao, Spain.

Following the recent sale of Midatech Pharma US, we have now fully focussed our resources and activities on using our technologies to establish our fast-to-market oncology and rare disease product pipeline programmes. These are currently in various stages of pre-clinical and clinical development.

36
**Patent families**

## Platform technologies

Midatech's R&D activities utilise our three proprietary platform technologies, designed to allow the delivery of existing therapeutic drugs to the right place at the right time, in the treatment of rare cancers or orphan diseases:

### Q-Sphera™

Our disruptive polymer microsphere technology is used for sustained delivery to prolong and control the release of therapeutics over an extended duration, from weeks to months.

### MidaSolve™

Our innovative nanosaccharide technology is used to dissolve otherwise insoluble drugs so that they can be administered in liquid form, directly and locally into tumours.

### MidaCore™

Our leading-edge gold nanoparticle ('GNP') technology is used for targeting sites of disease using either (i) **chemotherapy** – improved and targeted delivery of existing chemotherapeutic agents to tumour sites, as well as (ii) **immunotherapy** – enhanced uptake of new immuno-moieties by immune cells that can then mount an attack against cancer cells.

## R&D pipeline

The Company's research and development is focussed on developing a range of high value therapeutics based on its three drug delivery technology platforms (Q-Sphera™, MidaSolve™ and MidaCore™).

### Clinical:

**We have two key therapeutic products in clinical development:**

**MTD201 (Q-Octreotide)**

a long-acting dose of octreotide for the treatment of acromegaly and neuroendocrine tumours; based on our Q-Sphera™ technology for sustained delivery.

**MTX110**

a treatment for diffuse intrinsic pontine glioma ('DIPG'), an ultra-rare brain cancer suffered by children, based on our MidaSolve™ technology for direct delivery.

In addition to these two priority programmes, a further programme in the clinic is MTX102, an EU funded project seeking to develop a vaccine for Type I Diabetes, based on our MidaCore™ technology for targeted delivery and uptake by the immune system.

### Pre-clinical:

**MTD201 and MTX110 are expected to be the priority focus for Midatech in the near term, however, the Company has additional, in-house preclinical programmes, which, pending further funding, the Company may progress in due course, including:**

**MTR103**

for the treatment of glioblastoma multiforme ("GBM") brain cancer, using MidaSolve™ technology to deliver drugs directly into the tumour.

**MTD119**

a targeted GNP therapy treatment using the Company's MidaCore™ technology for the treatment of hepatocellular carcinoma.

### Intellectual property

We have a strong intellectual property base, with 107 granted patents, 83 applications in-process and 36 patent families, covering a range of technologies.

See our R&D Pipeline on **pages 10 and 11**

# INVESTMENT PROPOSITION

**Midatech offers the potential for rapid revenue growth through its exciting pipeline of products, that seek to improve the efficacy of existing therapeutic agents, each targeting significant markets. This de-risked strategy, i.e. having multiple programmes based on already approved agents and so not being reliant on proving the efficacy of new drug compounds, is supported by a strong IP portfolio and an ambitious, energised and highly experienced leadership team.**


## Multiple wholly-owned programmes with potential to reach the market in the next few years

- Our three drug delivery technologies are all in clinical testing
- Our two lead product development programmes are progressing on schedule
- Focussed on fast-to-market cancer and rare disease products
- Key validation milestones achieved for our drug delivery technology platforms, with all having entered the clinic
- We create valuable assets that can be monetised as they move through development and beyond, commercialised in-house or licensed to partners

Read more on **page 8**

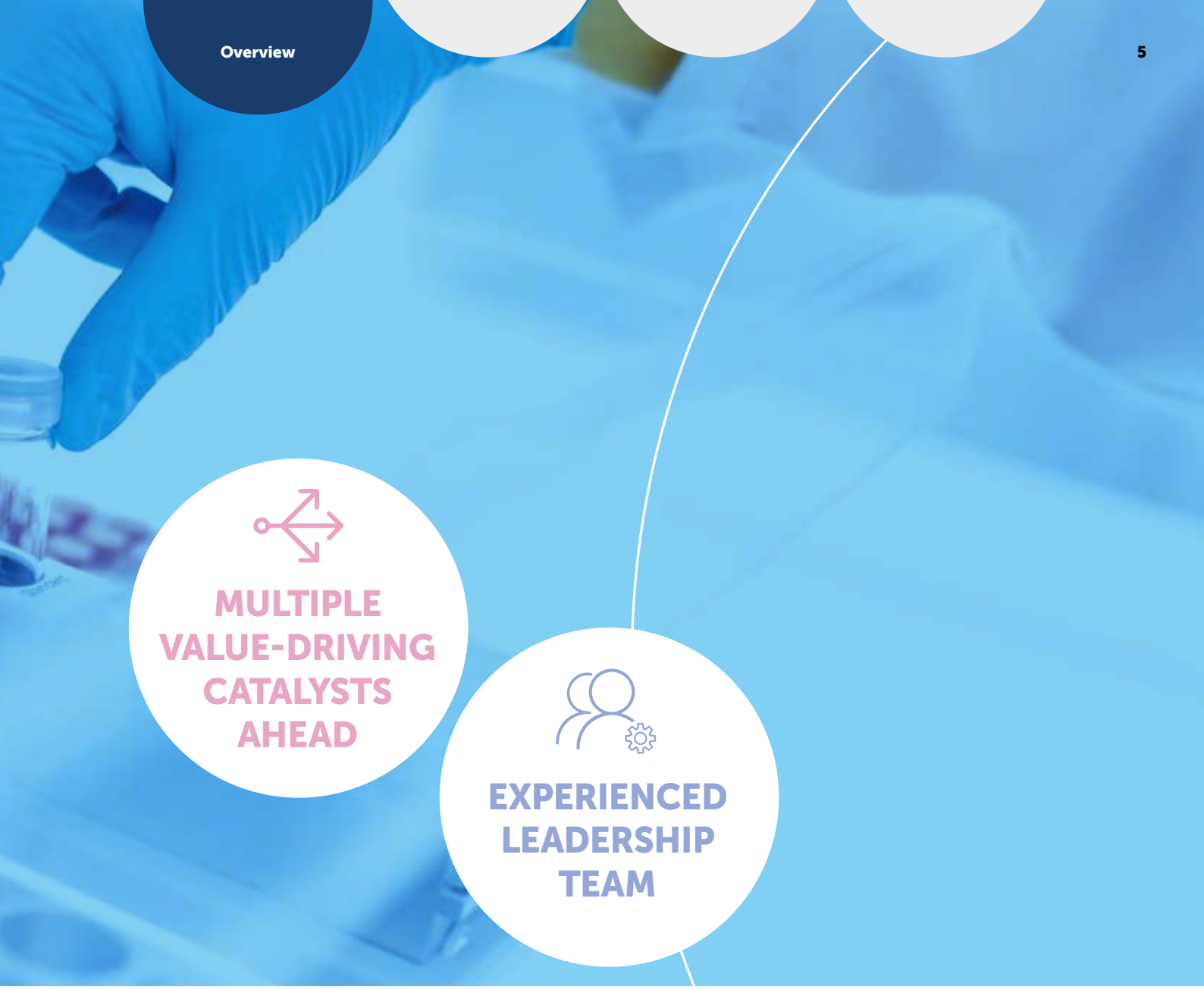
## Attractive target markets with limited competition

- We are addressing rare cancers and diseases with unmet clinical need that, without our technologies, would be impossible or difficult to treat
- Each of our niche cancer therapies has revenue potential ranging from $50m to in excess of $100m per year
- The estimated global market for our lead MTD201 product is worth in excess of $2 billion per year

Read more on **page 10**

## Reduced technical and regulatory risk

- Our platform technologies use proprietary drug delivery mechanisms that seek to improve bio-distribution, safety and efficacy of existing, approved therapeutic agents
- We have multiple programmes and opportunities based on our platform technologies




## Multiple value-driving catalysts ahead

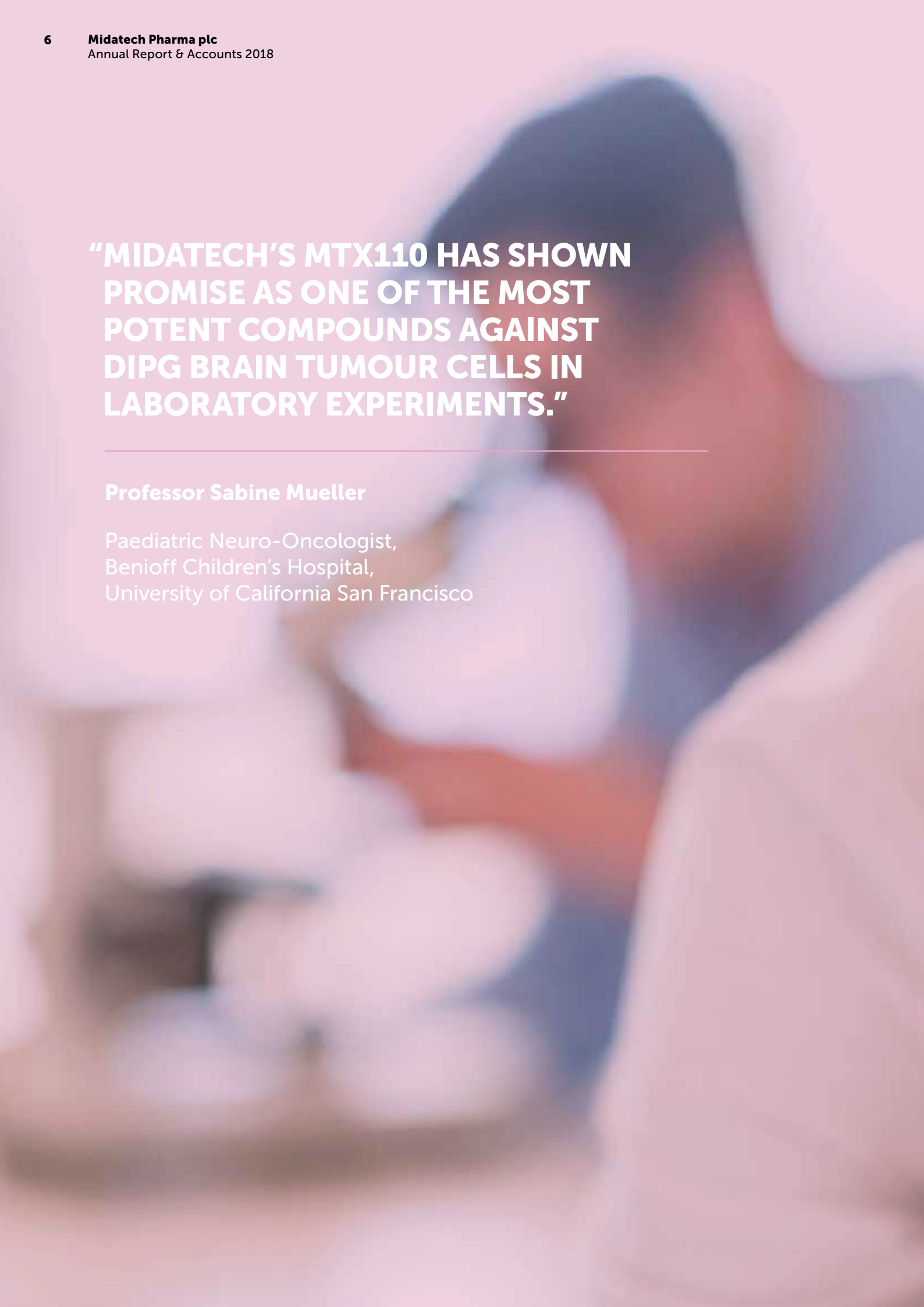
- Our platform technologies, all of which have now successfully entered the clinic, are compelling sources of future, innovative therapies, extending beyond the current lead programmes

Read more on **page 18**

## Experienced leadership team; clear on what needs to be done and how to do it

- Our leadership team has more than 60 years of combined pharmaceutical industry experience, including senior roles in Shire, Novartis, GSK and others
- The Board was enhanced with the promotion of Craig Cook to CEO with effect from June 2018. Prior to his appointment as CEO, Craig was Chief Operating Officer and Head of R&D for the Group

Read more on **page 32**



**"MIDATECH'S MTX110 HAS SHOWN PROMISE AS ONE OF THE MOST POTENT COMPOUNDS AGAINST DIPG BRAIN TUMOUR CELLS IN LABORATORY EXPERIMENTS."**

**Professor Sabine Mueller**

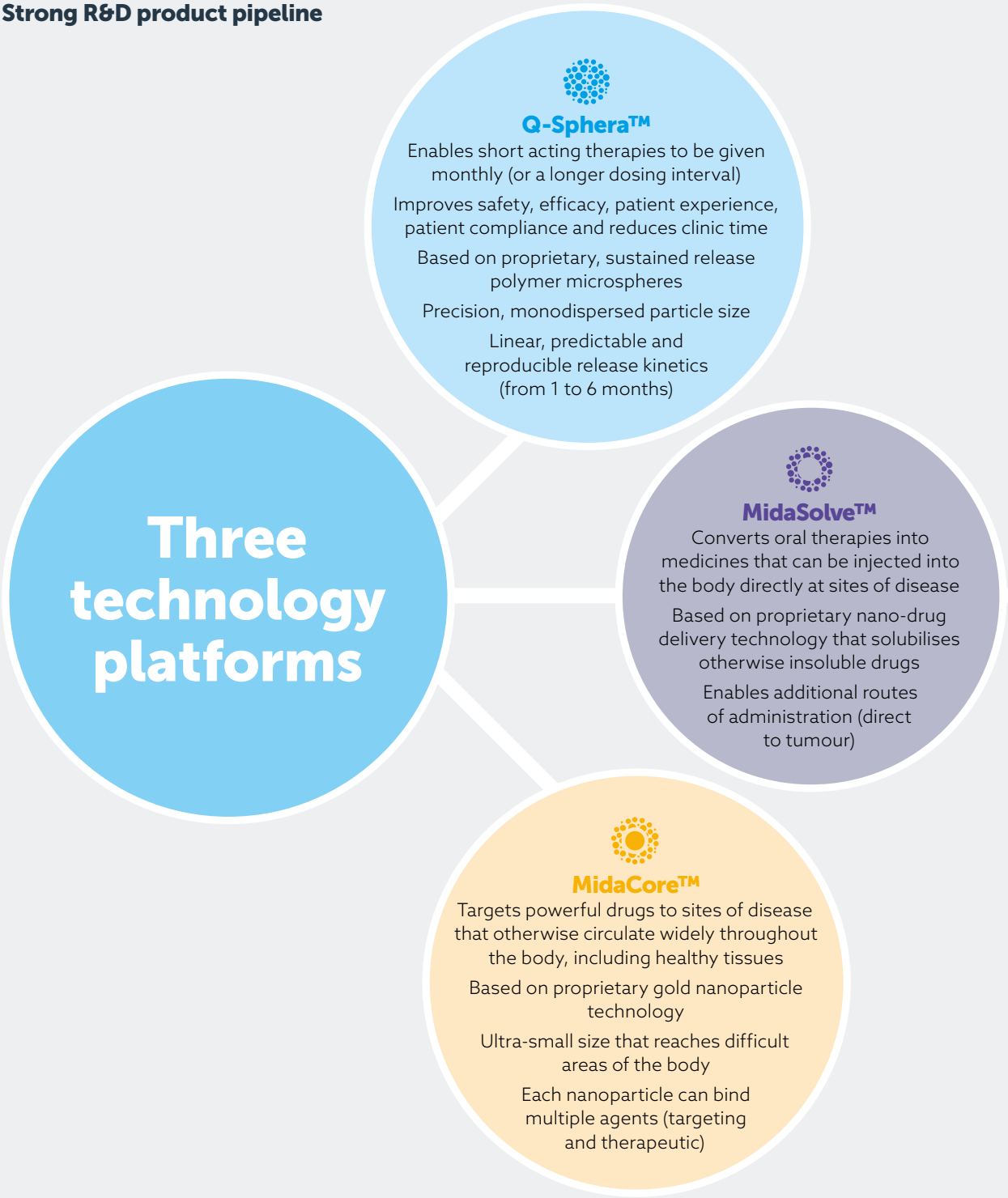
Paediatric Neuro-Oncologist,
Benioff Children's Hospital,
University of California San Francisco

## Strategic Report

# OUR BUSINESS MODEL

**Midatech is now an R&D company focussed on advancing our balanced product pipeline, primarily in-house and with selected partnerships as appropriate.**

## Strong R&D product pipeline



## Our value chain

### Research & development

R&D facility in Cardiff, UK with 13 scientific personnel

Creation of additional pipeline assets and licensing opportunities

### Manufacturing

Licenced in-house manufacturing facility in Bilbao, Spain, employing 38 scientific and other personnel, producing Q-Sphera™ sustained release, MidaSolve™ and MidaCore™ products

Keeps intellectual property and know-how in-house

Maintains control over costs and timelines

### Commercialisation (future strategy)

Driving lead programmes and platforms through the clinic and towards in-house commercialisation and out-licensing opportunities with pharmaceutical partners

Significant and, established target markets with unmet needs that, together with our unique products and technologies, are compelling for prospective licensees

## Value creation

R&D focussed Group with in-house manufacturing

Delivering on clinical milestones, with strong data and compelling pipeline for our proprietary drug delivery platforms all of which are now into the clinic

A rich R&D pipeline with close-to-market programmes and an exciting upcoming value-creating 18-24 months anticipated for programmes, platforms and the Company through 2020

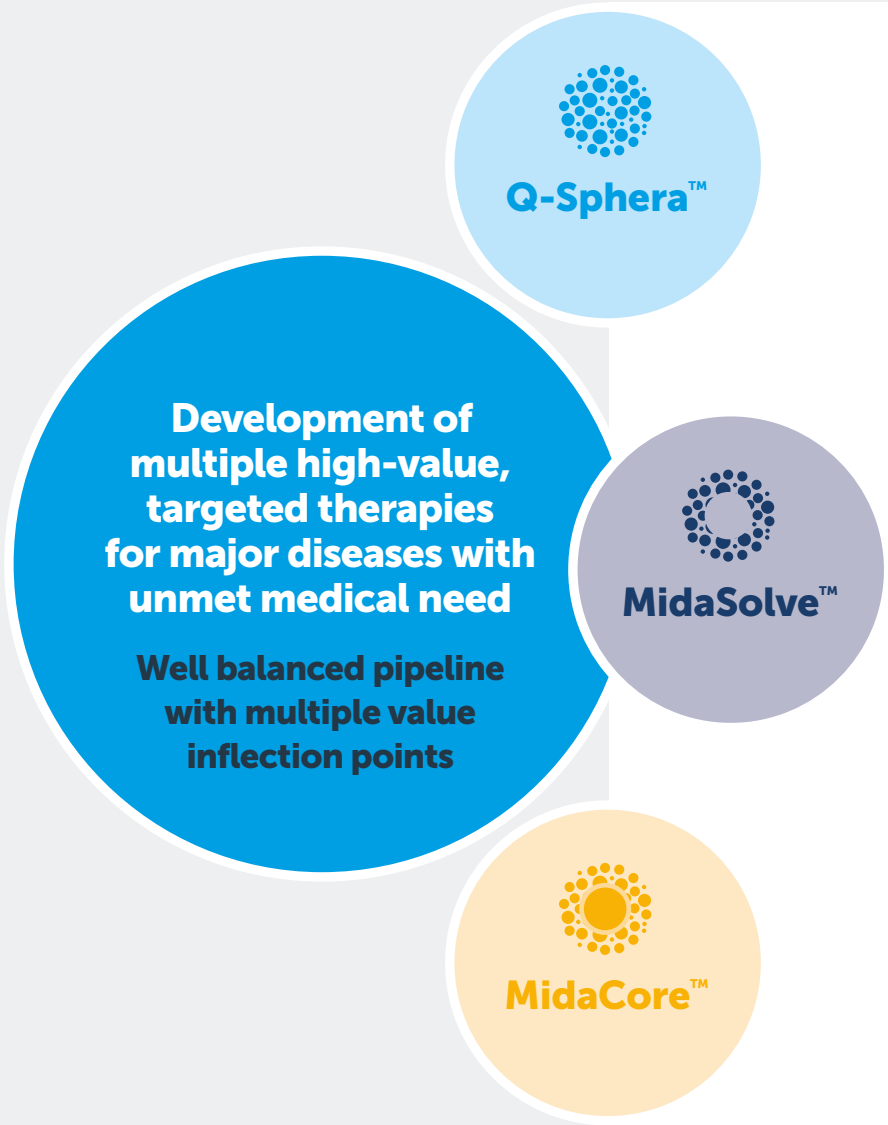
Three proprietary platform technologies, providing a compelling basis for a rich pipeline of therapies for rare cancers with unmet medical need

Scope to work with partners for R&D collaborations and/or licensing and royalty deals

# OUR DEVELOPMENT PIPELINE

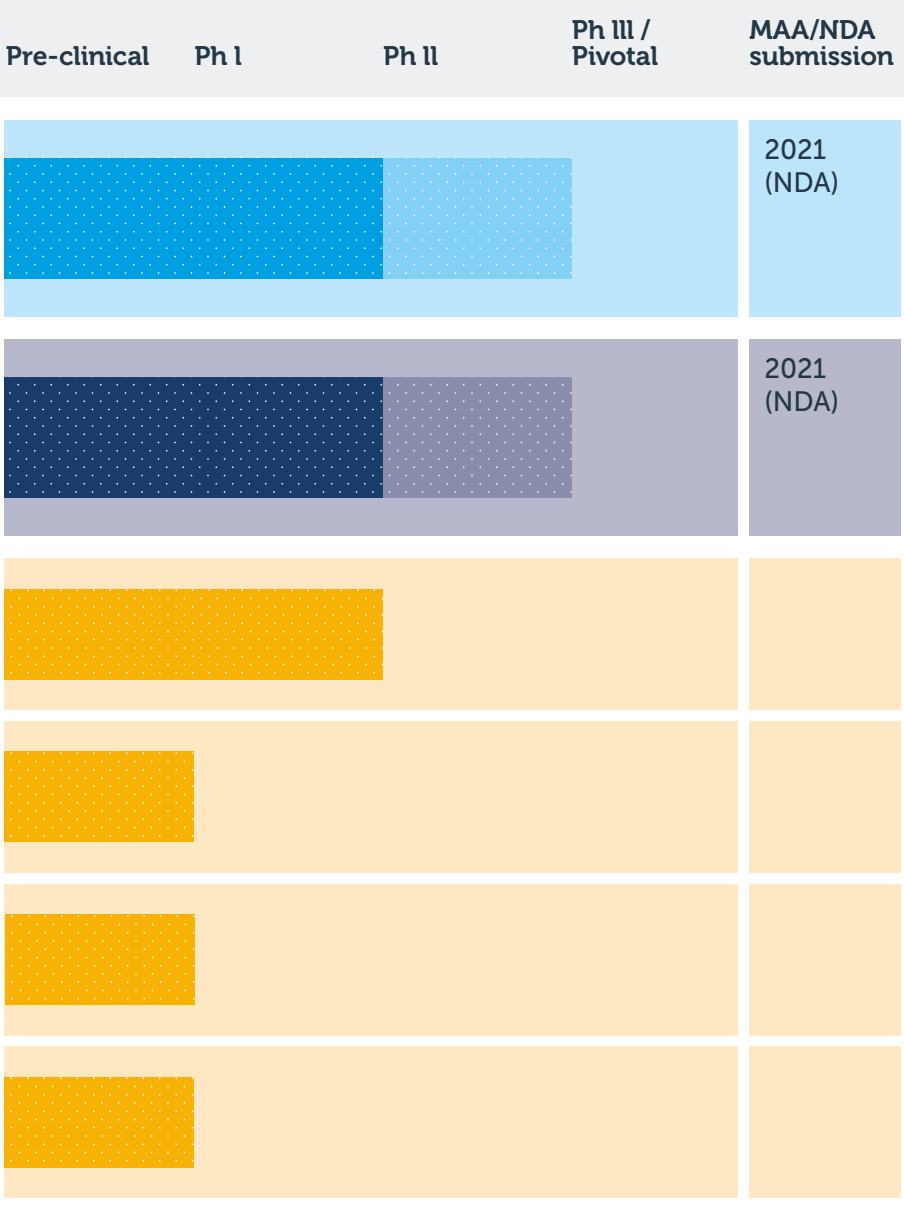
## Midatech is advancing the development of multiple, high value, therapies.

**We commenced first in-human studies for two of our lead programmes during 2018: MTD201 for neuroendocrine tumours and acromegaly, using our Q-Sphera™ sustained release technology, and MTX110 for childhood brain cancer based on our MidaSolve™ technology. These programmes are the focus for the next 12–24 months however, the Company has additional pipeline programmes at various stages of development, using our three platform technologies.**




| Programme and indication | |
|---|---|
| **MTD201** Carcinoid cancer, and acromegaly | |
| **MTX110** Brain cancer children (DIPG) | |
| **MTX102** Type 1 autoimmune diabetes vaccine | |
| **MTD119** Liver cancer, 'all comer' cancers | |
| **MTR111/116** Brain cancer vaccine | |
| **MTX114** Psoriasis immunotherapy | |

## Target product profile, USP and addressable market



# OUR VISION AND STRATEGY

**We have transformed Midatech into an R&D focussed organisation, building shareholder value based on our three proprietary platform technologies and fast-to-market products for rare cancers.**

## OUR VISION

**To profitably use our proprietary platform technologies to improve patients' lives and, in so doing, create value for all stakeholders.**

### Streamlined R&D business following sale of US commercial operation

Midatech acquired Dara BioSciences, Inc. in December 2015 as its US commercial operation. Subsequently renamed Midatech Pharma US, Inc. ('MPUS'), the business focussed on commercialising oncology supportive care products in the US which help patients manage the impact of their cancer as well as the side effects of their cancer therapy.

Following the fundraise in October 2017, the Board committed to assess the market value of certain of the Group's assets in order to drive long term value for the Group without, where possible, a reliance on equity funding. The Board was determined to take action to ensure that the Group was not required to significantly delay, scale back or discontinue the development or commercialisation of its key R&D pipeline products. In order to achieve this strategy, in early 2018, the Board initiated a formal process, seeking buyers of MPUS. This process resulted in a number of offers and in November 2018 we concluded the sale of the US business to Kanwa Holdings LP for initial consideration of $13.0m and up to $6.0m in contingent consideration payable on the achievement of certain MPUS product revenue targets for 2018 and 2019. The targets for 2018 were not achieved. Kanwa Holdings is a limited partnership established for the purposes of acquiring MPUS and is owned by funds managed by or through Barings LLC. The sale of MPUS resulted in net proceeds of approximately $4.2m being received by the Company after transaction fees and after repayment of the Company's outstanding loan to MidCap Financial of $7.7m.

This disposal generated cash for the business and, crucially, it also enabled management to focus exclusively on the key R&D pipeline products which, the Board believes, represent the real value of the business. The progress made on the R&D pipeline during 2018, with the key MTD201 and MTX110 programmes commencing crucial clinical trials, and the MTD201 pilot study producing compelling clinical data, represents a validation of this change in strategy.

### Future commercial strategy

Midatech intends to adopt a variable approach to the commercialisation of its development assets. Where target markets are large and well-established, such as for MTD201, the Company intends to out-license to a pharmaceutical partner for commercialisation with direct sales through co-promotion agreements in certain, major territories. In the case of MTX110 and other products where the target market may be accessed with a small focussed sales operation, the Company intends to sell the product directly, potentially with partners in some territories. In this way the Company seeks to maximise value for shareholders without committing to establish a full-scale commercial operation.

Our platform drug delivery technologies are used to generate our own proprietary pharmaceutical assets that can then be licensed as they progress through various development phases, or retained in-house as appropriate. At certain value inflection points the products can be licensed outright to a pharmaceutical partner that would in turn develop them into a product for regulatory approval and subsequent sale. In certain indications, Midatech could create our own pharmaceutical assets and then subsequently opt to retain, develop and commercialise them in-house, rather than partnering them.

From a technology perspective, the nature of the Company's technology platforms – Q-Sphera™, MidaSolve™, and MidaCore™ – are such that Midatech can license the platforms and provide related services to a pharmaceutical partner that would in-turn create, develop and commercialise its own pharmaceutical products.

# OUR STRATEGY

**With the change in strategy, Midatech is now fully focussed on delivering its R&D programmes.**

## Progress development of in-house oncology products

### Progress in 2018

Our two key programmes, MTD201 and MTX110, both reached the clinic in May 2018. The pilot phase of the MTD201 study generated compelling data and MTX110 is progressing well through the safety phase of its clinical trial.

Work in our Spanish manufacturing facility enabled us to produce the material required for the clinical trials and development is ongoing for the next stage of the MTD201 clinical programme.

With the closure of our Abingdon R&D facility in December 2018, ongoing MidaCore™ activities have been incorporated into the Cardiff and Bilbao sites. Whilst existing programmes will be maintained, no new MidaCore™ R&D will be initiated until substantial progress has been made with MTD201.

In February 2018, the MTD119 drug candidate for liver cancer, was granted Orphan Drug Designation by the European Medicines Agency.

### Priorities for 2019

**MTD201:** Following the successful pilot study, we are evaluating the optimal design for the subsequent development programme which we anticipate will commence in H2 2019.

Commence commercial manufacturing scale-up is a key activity for MTD201 in 2019, required prior to filing for marketing approval.

Subject to regulatory acceptance of the proposed trial design, successful outcome of the trial and successful scale-up of manufacturing, the intention is to file for marketing authorisation in 2021.

**MTX110:** We expect the safety phase of the ongoing first in-human study for childhood brain cancer to conclude in H1 2019, with the efficacy phase to commence shortly thereafter. The objective of this study is to evaluate overall survival after 12 months.

**MTX102:** This long term Phase I clinical safety study, evaluating our immuno-tolerising GNP based peptide vaccine for Type 1 Diabetes, is expected to read out in H1 2019.

We plan to focus our efforts and resources on the key MTD201 and MTX110 programmes, outlined above, and due to limited resources, do not intend to undertake further, significant R&D during 2019 on our other, MidaCore™-based programmes, including MTD119, MTR111 and MTR116.

## Drive development of partner programmes

### Progress in 2018

Key validation for our three platform technologies, all now having entered the clinic, which creates the potential for new partnerships and programmes in the near future.

Our collaboration with Emergex continued to make good progress, evaluating GNP-conjugated constructs for Emergex's GNP-based anti-viral vaccination programme.

We were pleased to announce in December 2018, a new Q-Sphera™ microsphere technology partnership with a major regional pharmaceutical partner. This feasibility work will be undertaken during 2019.

### Priorities for 2019

Our primary focus remains the advancement of our in-house products towards commercialisation, however, we will continue to support the Emergex collaboration as required, and look forward to developing new collaborations, such as the ongoing Q-Sphera™ project which we hope will develop into a major partnership.

We will continue to evaluate other, prospective partnerships where these can add value to the Group without distracting from the priority in-house R&D programmes.

# SPOTLIGHT ON KEY PROGRAMMES

## **MTD201** FOR NEUROENDOCRINE TUMOURS AND ACROMEGALY

**Treatment for neuroendocrine tumours and acromegaly using our Q-Sphera™ sustained release technology. With its favourable clinical profile, enhanced dose flexibility and improved injectability, MTD201 will provide an alternative to the market leading Sandostatin® LAR®, the current standard of care.**

### Benefits

Enhanced clinical profile with consistent, predictable and reproducible release kinetics of the active drug into the body

Simple, quick and reliable reconstitution, reducing clinical preparation time and improving patient convenience

Compared to current therapeutics, MTD201 is administered through a smaller needle, hence is less painful and irritating for patients

Minimal wastage due to improved product stability, simpler reconstitution process and no needle blockages, hence no wastage of expensive product

All made possible by our Q-Sphera™ technology: precision, uniform particles allows high drug loading, accurate and consistent drug release, homogeneity, and minimal/no burst release thereby reducing potential for side effects

### Indications

Neuroendocrine tumours ("NETs") and acromegaly

NETs are slow growing tumours derived from neurological, hormonal secreting cells

Acromegaly is a tumour of the pituitary gland in the brain that produces excessive growth hormone

Both are debilitating conditions with significant morbidity and mortality

Octreotide is the mainstay of medical treatment for both neuroendocrine tumours and acromegaly

### Addressable market

Significant opportunity for MTD201 to enter an estimated global market in excess

£2 billion

dominated by Sandostatin® LAR® and Somatuline®

### Progress in 2018

Initial human bioequivalence trial commenced in May 2018 and completed in August, with favourable data

MTD201 compares favourably to SLAR, the leading product in the market, in terms of clinical release profile, therapeutic effect and patient experience

### Next steps

Finalise go-to-market strategy and the resources required to develop MTD201 as either a differentiated product, an interchangeable product with SLAR or potentially pursue both options

Commence follow-on registration programme in H2 2019

Scale-up manufacturing to commercial volumes

Filing for marketing authorisation anticipated in 2021

**"The clinically favourable Phase I pharmacokinetic and pharmacodynamic data reported in healthy subjects has shown the potential of Midatech's Q-Sphera™ technology to deliver flexible sustained-release octreotide options. The study indicates MTD201 has the potential to provide additional benefits compared to current standard of care for acromegaly and neuroendocrine cancer patients needing chronic treatment with a somatostatin analogue, including flexible dosing options, simpler reconstitution, fewer errors and wastage, and improved patient experience because of the requirement for fewer injections."**

**Professor Shlomo Melmed, Dean of Medical Faculty, Cedars-Sinai Medical Centre, Los Angeles**

# SPOTLIGHT ON KEY PROGRAMMES

## **MTX110** FOR DIPG

**Treatment for DIPG ultra-orphan childhood brain cancer using MidaSolve™ technology to solubilise otherwise insoluble drugs for direct-to-tumour administration.**

### Benefits

MidaSolve™ technology converts the active drug panobinostat from an oral formulation, not used in DIPG since it cannot cross the blood brain barrier, into a liquid formulation that can be injected directly into the tumour

Enables elevated drug concentrations of solubilised MTX110 to be infused directly into the tumour, while minimising systemic toxicity and peripheral side effects

Panobinostat API, licenced from Novartis in June 2017, demonstrated high potency against DIPG tumour cell lines in animal studies

### Indications

DIPG, brain stem tumours in young children

Universally fatal, with median survival of just nine months

No effective treatment; surgical resection is not possible; radiotherapy and chemotherapy do not improve survival since anti-cancer drugs cannot cross the blood-brain barrier to reach the tumour

### Addressable market

Up to

1,000

patients worldwide per year

Potentially

$100m

market; highly under-served

Adult form of DIPG – Glioblastoma Multiforme ("GBM") – potential follow-on programme pending further pre-clinical development and data; estimated $3 billion addressable market

**DIPG is a devastating childhood brain cancer with virtually no long term survivors, and for which there are no current therapies other than palliative treatments. Midatech's MTX110 has shown promise as one of the most potent compounds against DIPG brain tumour cells in laboratory experiments, and has also been shown to be well tolerated in an early phase 1 clinical study conducted at the University of California, San Francisco when using a CNS directed delivery strategy referred to as convection enhanced delivery (CED). The combination of a specific CNS directed delivery strategy combined with a promising agent such as MTX110 holds great promise for better outcomes for this devastating disease. It is exciting to be working with the Midatech team on these new therapy options."**

**Associate Adjunct Professor Sabine Mueller, Paediatric Neuro-Oncologist, Benioff Children's Hospital, University of California San Francisco and University Children`s Hospital Zurich, Switzerland**

### Progress in 2018

Commenced US study in human DIPG patients at University of California, San Francisco, with Phase I safety component progressing well

### Next steps

Complete US clinical study; Phase I safety component due to complete H1 2019 followed by commencement of Phase II efficacy study

Commence EU study following regulatory approval

Depending on the outcome, seek accelerated/ conditional approval in the US and EU

Product could receive fast-track approval and be commercially available as early as 2021

### Follow-on product opportunities for MTX110

- In children, other potential indications include high grade gliomas
- In adults, MTX110 represents an exciting treatment prospect for glioblastoma multiforme ("GBM")

  Most common and most aggressive brain cancer, with median survival of around 12 months

  No effective therapies currently exist; fewer than 25% of patients survive beyond 2 years

  Pre-clinical MTX110 programme in GBM underway with promising data so far

**Patients**

1,000

per year

# CHAIRMAN AND CHIEF EXECUTIVE'S STATEMENT

## Rolf Stahel and Craig Cook reflect on a year of significant strategic change for Midatech and discuss next steps for the Group as it enters a landmark phase.

### Highlights

Last year was a year of strategic refocusing of the business, becoming a pure-play R&D company following the divestment of our US commercial operation in November, a major milestone for the Group. Midatech is now focused solely on its R&D pipeline with all resources now directed towards progressing our programmes to unlock their full potential and create valuable assets, by commercialising these ourselves or through license agreements with partners.

To underpin this strategic refocus, two of our key programmes entered the clinic in May 2018 – in carcinoid cancer/acromegaly, and in childhood brain cancer. The first of these in acromegaly completed successfully in September 2018, while the second programme continues to progress on schedule.

More recently, negotiations that commenced in September 2018 and culminated post period in February 2019, the out-licence and £8m investment from leading Chinese speciality pharmaceutical group, China Medical System ("CMS"), has brought a new cornerstone investor and licence partner to Midatech. Securing a partner of the scale and reputation of CMS is a clear validation of the value of our pipeline, our technologies and know-how, and gives us a financial runway for the further development of our current and prospective, future products. This transaction was also key component of a broader fundraise effort that commenced in November 2018 and concluded post period in February 2019, that strengthened the financial position of the Company for the near term future.

**Rolf Stahel**
Chairman

We also sought to rationalise our cost base and simplify our operations, closing our research facility in Abingdon and consolidating our gold nanoparticle research and development operations into our Bilbao and Cardiff sites.

### CMS investment and licence

The relationship with CMS marks a genuine turning point for the Group. Despite Midatech's market capitalisation implying a value of less than £3 million at the time the agreement was reached, CMS has invested £8 million for a 51% stake in the Group, which is a huge vote of confidence in our intellectual property and capabilities.

CMS is looking to add valuable, earlier stage assets, with a strong chance of commercialisation, to its portfolio, and, following extensive due diligence, they see great potential in our products and technologies. Under the terms of the licence agreement, CMS has rights to develop and commercialise the Company's pipeline of products, at its cost, in Greater China and certain countries in South East Asia. This includes promotion through its network of around 4,000 sales staff in China alone. Subject to certain milestones being achieved, Midatech will receive regulatory and sales based payments, as well as royalty payments.

In addition, CMS may identify further product opportunities using Midatech's technologies beyond our current focus. Midatech would undertake the initial development on CMS' behalf, funded by CMS. If such products obtain marketing approval, CMS will own the rights in the territories covered by the agreement and Midatech would retain the rights in the rest of the world, including the US and Europe. Two programmes have already been identified by CMS and preparation for feasibility is underway and, if successful, would be followed by tech-transfer. CMS also provides manufacturing options for Midatech products, with an impressive manufacturing capability and facility based in Shenzhen, China.

**Craig Cook**
Chief Executive Officer

**Estimated global market for MTD201 Q-Octreotide**

£2bn

As we embark on this next phase of Midatech's history, we were pleased to welcome Dr Huaizheng Peng to the Board as a Non-Executive Director. Dr Peng is General Manager of International Investment and Operations at CMS. He brings a wealth of experience, having worked in private equity and investment banking in London prior to joining CMS in 2011.

## Financing activities

We recently initiated a round of fund raising and were pleased to secure £13.4m in February 2019. In addition, the sale of Midatech Pharma US in November 2018, generated net proceeds of approximately US$4.2 million (around £3.4 million) after the repayment of the MidCap loan.

In January 2019 we concluded and agreed terms with the Basque regional government for a €1.5 million loan to support the commercial scale-up for MTD201 and the Q-Sphera™ platform in our Bilbao manufacturing site. This soft loan finance is provided as a reimbursement of costs incurred up to the amount of the loan and follows a related grant worth €450k awarded in 2018.

Separately, in March 2019, we were very pleased to announce that an additional €6.6 million of funding had been conditionally approved under the Spanish Government's Reindus programme, subject to the Company providing a €2.6 million guarantee, which we anticipate will be covered by bank finance. This takes the total public financing facility to €8.5 million in relation to manufacturing scale up costs which are being finally estimated, depending on whether the Company pursues a facility for in-house primary manufacture as well as fill and finish, or in-house primary manufacture with fill and finish outsourced to a CMO.

These facilities are important to our commercial manufacturing scale-up, scheduled over the next 18–24 months in Bilbao and, together with other options under consideration such as strategic manufacturing partnerships, could provide all our manufacturing needs in the medium to long term. For our lead programme MTD201, completion of the commercial manufacturing is required prior to submitting for marketing authorization in the US and EU.

## R&D progress

Our strategy to concentrate on our R&D pipeline has started to bear fruit, with enormous strides made in two of our core programmes, MTD201 and MTX110, which entered human trials during the year. Having previously been hampered by resource and manufacturing challenges, both finally entered the clinic in 2018, and getting positive data for the first of these, MTD201, was a significant development for Midatech which will unlock material value for the Group.

Given their platform nature, each of our technologies has applications in therapies beyond those we are currently working on. For example, with MTD201, we take the same molecule as used in the Novartis product, Sandostatin® LAR® ("SLAR"), and make improvements to the formulation utilising our more efficient and precise manufacturing technology. By applying our patent protected technology to other molecules, we can make existing medicines better, generate new products, and/or give products new patent life. We don't incur typical risks on the side effects or efficacy of the molecule, since these are already approved products, we only need prove that our technology delivers the drug as required.

With the Q-Sphera™ and MidaSolve™ platforms entering the clinic in 2018, via the MTD201 and MTX110 programmes respectively, all three of our platforms are now in human use. Getting these programmes into formal human studies was truly satisfying for the entire Midatech team, and provides a strong foundation and momentum as we take our key research programmes through clinical development. We are well positioned and have a clear strategy to deliver these transformative therapies for patients with devastating oncology and rare diseases.

# CHAIRMAN AND CHIEF EXECUTIVE'S STATEMENT
CONTINUED

### Q-Sphera™: MTD201 (Q-Octreotide)

Last August we completed a Phase I study in healthy human volunteers to compare the bioequivalence of our sustained release MTD201 product and SLAR, the leading incumbent product for the treatment of neuroendocrine tumours and acromegaly. The results were very encouraging, with the next step being a follow-on, pivotal programme.

Following feedback from the FDA on the study design and regulatory route, we have clear sight of what needs to be done and the resources required. With the enhanced product performance characteristics of the Q-Sphera™ technology, our options are to either pursue a differentiated product with a distinct clinical profile compared to SLAR, or to establish an interchangeable alternative to SLAR. Based on extensive regulatory, opinion leader and partner input, the differentiated product route may provide the more valuable, de-risked development programme. It is our intention to, in the near future, finalise the decision to pursue a differentiated versus equivalent product (or indeed both options) and file for clinical trial approval thereafter. The next programme is expected to commence in H2 2019. Subject to the successful outcome of the study and commercial scale-up of MTD201 production, we plan to submit marketing authorisation applications in 2021.

### MidaSolve™: MTX110

Our MTX110 product for childhood brain cancer ("DIPG") based on our MidaSolve™ technology is an important part of our pipeline. DIPG is a rare and terminal condition, and MTX110 may be an important advancement in transforming patient outcomes. The programme is progressing on track and we expect interim data for the Phase I dose-escalating and safety components of the study in 2019. Results to date have been encouraging and show that the therapy is well tolerated. This phase will also establish the recommended dose to be used in the follow-on Phase II efficacy component of the study programme, with the objective of assessing patient survival rates after 12 months. It would be wonderful to make a difference to patients and families dealing with this shattering disease.

We recently agreed with Novartis to expand the scope of the current panobinostat license to include any direct routes of administration for treatment of brain cancers. The original license with Novartis covered the administration of MTX110 via a technique called Convection Enhanced Delivery ("CED"), where MTX110 is infused under slight positive pressure directly into the brain tumour, and then diffuses through and around it. The expanded license agreement with Novartis enables us to evaluate MTX110 for additional routes of administration and other brain cancers in children and adults.

We are evaluating other indications in which MTX110 might make a difference. Our pre-clinical work on GBM adult brain cancer is ongoing, and there are also potential applications for solubilised therapeutics in other childhood brain cancers.

Subject to further favourable results from the studies, we could pursue accelerated approval, a fast track process reserved for orphan conditions where there are no existing treatments.

### MidaCore™

Whilst we have directed our resources to the MTD201 and MTX110 products, there are several early phase programmes based on the MidaCore™ gold nanoparticle targeted delivery platform that may be progressed subject to receiving further funding. These include: MTD119, a targeted therapy for treatment of hepatocellular carcinoma, and MTX114, a topical treatment for psoriasis. We also expect to complete an EU funded Phase I programme for MTX102, evaluating a MidaCore™ based vaccine for diabetes. Finally, under our collaboration with Emergex, where they are using our MidaCore™ gold nanoparticle technology to develop vaccines for infectious viral illnesses such as Ebola and Dengue Fever, we anticipate their projects moving forward into clinical development.

## Technology partnerships

Given that all our technology platforms are now 'validated' in humans, business development will be an important focus this year as we drive our lead programmes and platforms through the clinic and towards further licensing opportunities, particularly for MTD201 but also for our three technology platforms, Q-Sphera™, MidaSolve™ and MidaCore™. The timing is ideal to pursue opportunities that expand the platforms through partnerships with other pharmaceutical or biotech companies, where they are either interested in our current programmes or where they may have an indication they want to develop in combination with our platforms. We will pursue a dual strategy, to commercialise our own programmes in-house and also expand the platforms to get traction in the market.

## Operational changes

During 2018, we divested the US commercial operation, cut administrative costs and closed our Abingdon R&D site. These changes were accompanied by a refocussing of resources on our clinical programmes and raising additional funds, all while continuing to diligently manage our cash resources.

Our principal focus now is on obtaining registration data for MTD201 and MTX110, further developing our platforms, transitioning our Bilbao manufacturing capabilities from research and clinical scale to commercial scale, and ensuring we have the financial runway to achieve these objectives. Future submission of any New Drug Application to the FDA for the approval of MTD201 will require both clinical data, as well as manufacturing data from our first commercial batch to come out of Bilbao, which will be our priority for the next 18-24 months. We have commenced scale-up, but additional funds will be needed to accelerate and deliver our plans. We already have the €1.5 million loan from the regional Basque government, provided as a reimbursement of costs incurred up to the amount of the loan, and conditional approval from the Spanish Ministry of Industry for an additional loan of €6.6 million. We have also applied for funding from the EU Horizon 2020 scheme.

The decisions to close our Abingdon site and divest our US business were both very difficult but ultimately necessary in order to secure the future of the Group. In particular, the decision to close Abingdon and to make talented and valued colleagues redundant was immensely hard, but the changes were vital to secure the necessary investment and put the business on a stronger footing.

The Midatech team is impressive, demonstrating great talent, commitment, work ethic, expertise and experience. The team is driven by the opportunity to make a real difference for patients suffering from these devastating diseases. There is enormous energy and momentum in our drive to advance our products towards commercialisation.

The recent successful fundraise in 2019 has also allowed us to stabilise the financial position of the Company, thus allowing the teams to focus on the priorities at hand without distraction. However, the Board will continue to review additional opportunities and needs for both dilutive and non-dilutive funding as they arise.

Motivation is high, and we are grateful to the entire team, including the recently departed Non-Executive Directors, for their loyalty, drive and belief in making Midatech a success story.

## Outlook

We believe the Company has entered a new chapter in its growth as a streamlined R&D focused business with in-house manufacturing. We are now delivering on clinical milestones, with strong clinical data, and a compelling pipeline for our proprietary drug delivery platforms, all of which are now into the clinic. This sets up a, hopefully, value creating 18–24 months, rich in news flow and milestones for our programmes, platforms and the Company, through 2019 and 2020.

Whilst we are seeking to optimise our plans and fund the balance of manufacturing costs, the recent fundraise gives us the resources to take Midatech through a number of value catalysts. It reflects the potential that our important existing investors see in Midatech and has brought a new and very supportive new cornerstone investor and licensee in CMS, with a significant validating license deal completed. The agreement with CMS has also given us an anchor for the future development of our pipeline. Coupled with the proceeds from the fundraise concluded in February 2019, this has transformed the prospects of the Group by providing additional resource to unlock the value in our platform technologies and products. In particular, this investment will allow the Company to press ahead with confidence in bringing the MTD201 and MTX110 programmes to their next value level and thereby also further advance the value of our platform technologies.

We look forward to an exciting period ahead and, on behalf of the Board, we would like to thank our loyal investors, new investors, and our exceptional management and staff as we look forward to the next phase of value creation.

**Rolf Stahel**
Chairman

**Dr Craig Cook**
Chief Executive Officer

23 April 2019

# FINANCIAL REVIEW

**2018 was a year of significant change with the sale of the US commercial operation coupled with a new R&D focus and, following the recently completed fundraise, we have the resources to deliver on the strategic priorities for 2019 and beyond.**

**Nicholas Robbins-Cherry**
Chief Financial Officer

## Introduction

Midatech Pharma plc (the 'Company') was incorporated as a company on 12 September 2014 and is domiciled in England and Wales.

Following the fundraise completed in October 2017, the Board of Midatech reviewed a range of options to meet the future cash flow needs of the business, including non-dilutive financing and other strategic alternatives. As part of this process, the Board evaluated the possible sale of its US commercial operation, Midatech Pharma US, Inc. ('MPUS') and concluded that such a transaction would optimise shareholder value and also provide the Group with a certain amount of additional funding. Furthermore, selling MPUS would streamline the Midatech business and allow management to completely concentrate on advancing the Company's R&D pipeline to maximise the value of the business.

In furtherance of this strategy, the Company appointed a specialist life sciences advisory firm and initially sought buyers of MPUS on a confidential and measured basis, resulting in two indicative offers being received. Following this exploratory process, the sale process was expanded in order to maximise value from MPUS. This resulted in a significant number of potentially interested parties and additional offers, one of which was from Barings LLC ('Barings') for an initial cash sum of $13m plus an earn out of up to $6m dependant on the revenue performance of certain products of MPUS in 2018 and 2019. The targets for 2018 were not achieved.

The Board considered the terms of the various offers and concluded that the offer from Barings represented the maximum realisation of the value of MPUS for the benefit of its shareholders. Following approval by Midatech's shareholders, the sale to Barings was completed on 1 November 2018. The sale was effected through a limited partnership, Kanwa Holdings LP, which was established solely for the purpose of acquiring MPUS.

As a result of the sale of MPUS the Company was required to repay the outstanding loan due to MidCap Financial of £5.25m plus early redemption fees. This was done immediately prior to completion.

## Financial analysis

With the sale of the US commercial operation, Midatech's KPIs focus on the key areas of R&D spend, operating results and cash management. These measures provide information on the core R&D operation. Additional financial and non-financial KPIs, including further KPIs in respect of the research and development programmes, are being considered and may be adopted in due course.

For the year ended 31 December 2018, Midatech generated consolidated total gross revenue of £1.94m (2017: £0.99m), an increase of 96% on the prior year. Statutory Revenue for the year was the same as the prior year, £0.15m (2017: £0.15m).

In 2017, there was a charge to the Income Statement of £1.50m resulting from the impairment of the in-process research and development intangible asset associated with the product, Opsisporin, a sustained release treatment for uveitis, an inflammatory condition of the eye. As noted at the time, the product still has merit and when the Group has the available resources, development may be continued. There was no requirement for any impairment charge in 2018.

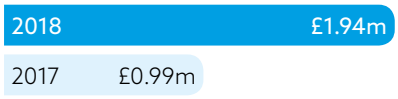
Net cash outflows for the year were £10.88m (2017: outflow of £4.15m). This includes proceeds of £9.26m, before deal costs, arising from the sale of MPUS, and before repayment of the debt owed to MidCap Financial ('MidCap') of £5.25m, plus early redemption penalty. The 2017 outflow of £4.15m was stated after proceeds from a share issue in October 2017 where £5.73m was raised after costs, and receipt of debt finance from MidCap of £5.24m. Adjusting for these exceptional items in 2017, the net cash outflow for 2018 was £14.70m compared to the adjusted outflow for 2017 of £15.12m. Cash management continues to be a critical focus for the Board and senior management.

## Financial analysis continued

### Key performance indicators (from continuing operations)

**Total gross revenue[1]**

£1.94m +96%




**Statutory Revenue**

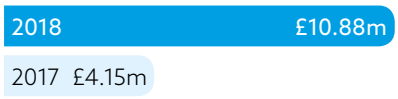
£0.15m +0%


**R&D costs**

£9.36m +12%


**Net cash inflow/ (outflow) for the year**

£10.88m +162%




**Loss from operations before intangible asset impairment charges[2]**

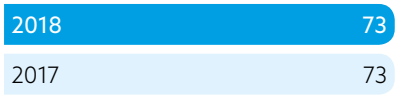
£11.82m +0%


**R&D as % of operating costs[2]**

68%


**Average headcount**

73 +0%




(1) Total gross revenue represents collaboration income from continuing operations plus grant revenue.

(2) 2017 total operating costs and loss from operations are both stated before an intangible asset impairment charge of £1.50m.

**Research and development expenditure**

Research and development costs increased to £9.36m (2017: £8.33m) reflecting ongoing investment in Midatech's R&D programmes. R&D activities were primarily focussed on the MTD201 and MTX110 programmes, with costs for the year reflecting:

- Completion of first in-human Phase I study in healthy volunteers of our product, MTD201, for the treatment of neuroendocrine tumours and acromegaly;
- Commencement of dose-escalating and safety component of a Phase I study in DIPG patients of our product MTX110; and
- Employee termination costs of £275k associated with the closure of the Group's research facility at Milton Park, Abingdon.

**Distribution costs, sales and marketing**

With the sale of MPUS, distribution costs, sales and marketing in 2018, decreased to nil (2017: £0.17m), due to the reclassification to discontinued operations. The 2017 cost in continuing operations related to certain marketing activities associated with the pipeline R&D products.

**Administrative costs**

Midatech's administrative costs increased by 3% on the prior year to £4.39m (2017: £4.27m). The 2018 costs include loan redemption penalties and other costs relating to the early repayment of the debt finance with MidCap Financial.

# FINANCIAL REVIEW
CONTINUED

### Impairment charge

As noted above, there was no impairment charge in 2018 (2017: £1.50m). The prior year charge related to the write down of the Opsisporin in-process research and development.

### Loss from discontinued operations

This comprises the aggregate income statement loss from the MPUS business. The loss for 2018 increased by 7% to £4.66m (2017: £4.36m), however the 2018 loss includes a loss on investment of £1.41m, net of an exchange gain of £3.84m transferred from the foreign exchange reserve, that crystallised with the sale of MPUS, as set out in note 4.

### Staff costs

During the year, the average number of staff for continuing and discontinued operations did not change at 85 (2017: 85). The payroll cost for all operations fell by 7% to £6.15m (2017: £6.60m) however, this includes a net credit to the income statement in respect of share based payments of £36k (2017: charge of £520k). The credit arose due to cancelled options previously awarded to certain employees who left during the year.

### Capital expenditure

During the year, there was no cash expenditure on intangible fixed assets (2017: £0.78m).

The total cash expenditure on property plant and equipment in 2018 was £0.24m (2017: £0.71m), largely in respect of investment in the Group's pharmaceutical development capability in its sustained release facility in Cardiff. Plant and equipment with a net book value of £160k was sold or written off as part of the closure of the Abingdon R&D facility.

### Movement in total assets

Total assets at 31 December 2018 saw a significant reduction on the prior year to £20.44m (2017: £49.22m), reflecting, inter alia, the sale of MPUS. Property plant and equipment decreased by £0.55m, with additions of £0.50m, in respect of the pharmaceutical development capability in Cardiff, as noted above, additional lab equipment, and depreciation of £1.02m, as set out in note 10. Intangible assets decreased, from £27.65m at 31 December 2017 to £12.37m at 31 December 2018 with the disposal of goodwill and product and marketing rights associated with MPUS, as set out in note 11.

Cash and cash equivalents, decreased to £2.34m at year end (2017: £13.20m) principally due to trading losses and repayment of the MidCap loan, offset by cash raised from the sale of MPUS that completed in November 2018.

### Movement in total liabilities

Total liabilities decreased to £3.52m (2017: £14.55m). Total borrowings reduced from £6.55m to £1.25m at 31 December 2018 following repayment of the MidCap loan. Remaining borrowings relates to Spanish government soft loans in Midatech Pharma España, provided under favourable terms to help finance the construction and fit-out of the Company's Bilbao manufacturing facility. Trade and other payables reduced to £2.10m (2017: £8.00m) reflecting the sale of MPUS.

### Other comprehensive income

Other comprehensive income comprises a foreign exchange gain of £1.16m (2017: loss of £1.23m) arising on retranslation of Midatech's non-UK operations and a foreign exchange gain of £3.84m (2017: nil) realised through the loss on the disposal of MPUS.

### Cash flow

Net cash outflow from operating activities for the year was £13.45m (2017: £12.95m). Including the sale of MPUS, there was a net cash inflow from investing activities of £9.04m (2017: outflow of £1.47m). There was a net outflow from financing activities of £6.47m including the repayment of the MidCap loan, early redemption fees, loan interest and finance lease charges (2017: inflow of £10.28m). Overall, there was a net cash outflow for the year, before the effect of exchange rates on cash and cash equivalents, of £10.88m (2017: outflow of £4.15m), resulting in a year end cash balance of £2.34m (2017: £13.20m).

### Capital structure

As at 31 December 2018 Midatech Pharma plc had in issue 61,184,135 Ordinary Shares of 0.005 pence each and 1,000,001 deferred shares of £1.

On 1 August 2018, 100,000 shares were issued to the Midatech Pharma Share Incentive Plan, an employee share incentive trust. No other new shares were issued during the year.

As noted above, following the year end, 348,215,478 new ordinary shares were issued on 26 February 2019 to subscribers in a Subscription, Placing and Open Offer. This raised proceeds of £13.4m before expenses and the new shares were admitted to AIM on 26 February 2019, described in note 32.

# RISK MANAGEMENT

## The Group has formal procedures to monitor and manage risk.

### Principal risks and uncertainties

The Directors consider the principal risks facing the business to be as follows:

#### Regulation

Midatech operates in a highly-regulated sector.

Government authorities in the United Kingdom, United States and in other countries and jurisdictions, including the European Union, extensively regulate, among other things, the research, development, testing, manufacture, quality control, approval, distribution, sale, marketing, post-approval monitoring and reporting of pharmaceutical products. The processes for obtaining regulatory approvals, along with subsequent compliance with applicable statutes and regulations require the expenditure of substantial time and financial resources.

The Group's manufacturing facility in Bilbao operates under the current Good Manufacturing Practice ('cGMP') guidelines for Investigational Medicinal Products and has been licensed to manufacture non-sterile products based on our MidaCore™ gold nanoparticle technology platform since March 2011, with indefinite validity (subject to passing regular inspections). The facility was refurbished in 2014 to enable the manufacture of sterile products and the additional certification of the facility to include production of sterile material was confirmed in February 2016. A further upgrade was carried out to enable the production of sustained release formulations, based around Midatech's Q-Sphera™ technology platform. The regulatory licence for the manufacture of these products was issued in late 2017 by the Spanish Medicines Agency 'AEMPS'. AEMPS has indicated that it will re-inspect the facility during 2019 with a view to issuing a single licence covering all aspects of manufacture subject to a successful inspection. Without this licence, the Group would be unable to manufacture its products in-house and would be required to seek an external contract manufacturing organisation.

Midatech performs its investigational work in accordance with the European Commission recommendation on a Code of Conduct for responsible nanosciences and nanotechnologies research.

The Group's manufacturing health and safety control in its Spanish facility is subcontracted to a specialist provider and complies with all Spanish employee and work regulations.

Waste solutions and products are suitably disposed of under contract with a licensed provider for this purpose. Prior to disposal, hazardous waste materials are stored under appropriate conditions. Solvents and other inflammable reagents are stored in appropriate fire containment storage cabinets.

#### Competition and Technological Advances

Midatech's Q-Sphera™ sustained release technology relies on a novel manufacturing process that, the Directors believe, is unique in the pharmaceutical industry. Competing sustained release technologies are well established in the market, however, the Q-Sphera™ platform has the potential for improved drug delivery kinetics and manufacturing efficiency.

The Group's MidaSolve™ technology is employed for increasing the aqueous solubility of small molecule cancer therapeutics to enable parenteral administration. This platform relies on internal know-how that uniquely applies prevailing chemistry techniques to enhance the solubility of certain insoluble agents.

The Group's MidaCore™ drug nanoconjugate platform is among the latest generation of nanomedicine technologies. Liposomes followed by various polymeric nanoparticles were the first nanotechnologies and now inorganic nanoparticles like Midatech GNPs are a rapidly emerging technology within the nanomedicine market.

Commercial success of Midatech's portfolio of development product candidates depends in part on the market's acceptance of these products and technologies. There can be no guarantee that this acceptance will be forthcoming or that Midatech's technologies will succeed as an alternative to competing products. Furthermore, demand for Midatech's products may decrease if competitor products are introduced with perceived advantages over Midatech's product candidates.

The speed and nature of technological change means that physical science is always evolving and new competition and alternatives are always a possibility, however, the Directors believe that Midatech has established competitive advantage over its peers. As a result of the combination of its platform technologies, intellectual property and proprietary know-how, the Group has a protected position in the sustained release, solubility enhancement and nanoparticle spaces which allows the potential for highly differentiated drugs serving high unmet needs, such as orphan oncology, to be rapidly and independently manufactured and scaled.

# RISK MANAGEMENT
CONTINUED

### Clinical development and regulatory risk

There can be no guarantee that any of the Group's products will be able to obtain or maintain the necessary regulatory approvals in any or all of the territories in respect of which applications for such approvals are made. Where regulatory approvals are obtained, there can be no guarantee that the conditions attached to such approvals will not be considered too onerous by the Group or its distribution partners in order to be able to market its products effectively. The Group seeks to reduce this risk by developing products using safe, well-characterised active compounds, by seeking advice from regulatory advisers, consulting with regulatory approval bodies and by working with experienced distribution partners.

## Financial risk management objectives and policies

The Group is exposed to a variety of financial risks which result from both its operating and investing activities. The Board is responsible for coordinating the Group's risk management and focuses on actively securing the Group's short to medium term cash flows.

### Finance risk

The Group enters into very few transactions involving significant complexity, potential material financial exposure or atypical risk. The Group does not actively engage in the trading of financial assets and has no financial derivatives other than an equity settled derivative financial liability as set out in note 20.

### Funding risk

The Group continues to incur substantial operating expenses. The IPO in December 2014 and subsequent fundraises in October 2016, October 2017 and most recently in February 2019, allowed the Group to advance the development pipeline products towards future value inflection points. However, until the Group generates positive net cash inflows from the out-licence or commercialisation of its development products it is expected to have to seek additional funding, whether through the injection of further equity capital from share issues, grants or debt finance. The Group may not be able to generate positive net cash inflows in the future or be able to attract such additional funding as may be required, either at all, or on suitable terms. In such circumstances the development programmes may be delayed or cancelled and business operations cut back.

The Group seeks to reduce this risk by keeping a tight control on expenditure, avoiding long term supplier contracts (other than for clinical trials), prioritising development spend on products closest to potential revenue generation, obtaining government grants (where possible), maintaining a focussed portfolio of products under development and by keeping shareholders informed of progress.

## Political landscape and external risk

In the referendum in June 2016, voters approved the United Kingdom's exit from the European Union (commonly referred to as 'Brexit'). On 29 March 2017, the United Kingdom formally initiated its withdrawal from the European Union by triggering Article 50 of the Treaty of Lisbon. The process of negotiation with EU member states in order to determine the future terms of the UK's relationship with the EU is ongoing. This has led to a period of uncertainty and volatility particularly in relation to UK financial and banking markets and recent events in the UK Parliament have done little to clarify the eventual outcome of the Brexit process. As the Brexit process unfolds, asset valuations, currency exchange rates and credit ratings may be especially subject to increased market volatility.

Depending on the terms of Brexit, Midatech may face a new regulatory landscape and challenges that may have a material adverse effect on it and its operations. Midatech's manufacturing infrastructure is located in Bilbao, Spain, and when the UK ceases to be a member of the EU, Midatech's ability to integrate its UK and Spanish operations could be adversely affected. For example, depending on the terms of Brexit, Midatech could become subject to export tariffs and regulatory restrictions that could increase the costs and time related to doing business in Spain. Conversely, having a long-established presence inside the EU may become increasingly beneficial providing tariff-free access to the European market and to EU grant funding.

In the United States, President Trump has proposed or sought to implement various policies, including reforming the US Food and Drug Administration that regulates, inter alia, the development, manufacture and sale of pharmaceutical products, repealing the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010 (the 'Affordable Care Act') and changing the manner in which drug prices are negotiated by the US national social insurance Medicare programme. Notwithstanding these possible reforms, we do not expect this administration to have a significant impact on the Midatech business given our development product portfolio, but changes in United States social, political, regulatory and economic conditions or in laws and policies governing foreign trade, importation, manufacturing, development, registration and approval, commercialisation and reimbursement of our products in the United States could adversely affect our business.

## Risk mitigation

The Group has formal procedures to monitor and mitigate risk. Some of the principal risks facing the Group include:

| Risk | Description | Mitigation | Change |
|---|---|---|---|
| **Availability of funding** | Until the Group generates positive net cash inflows from the commercialisation of its development products it may be required to seek additional funding, whether through the injection of further equity capital from share issues, grant or debt finance. The Group may not be able to generate positive net cash inflows in the future or be able to attract such additional funding as may be required, either at all, or on suitable terms. In such circumstances the development programmes may be delayed or cancelled and business operations cut back. | • Fundamentals such as executing the strategy, achieving R&D milestones, on time and in budget, achieving product approvals and containing costs will drive shareholder value that both satisfies current shareholders and attracts new shareholders in the future<br>• The successful fundraise concluded in February 2019 provides sufficient working capital to allow for the delivery of significant, value-driving R&D milestones<br>• Dual NASDAQ and AIM listings will likely provide access to additional funding sources | Decreased risk |
| **Competition / technological progression** | Although R&D is directed towards areas of currently unmet medical need, existing and prospective competitors may have superior capabilities, and/or alternative products may become available. There is a risk of our products losing commercial viability in the fast-moving biotechnology sector. | • Keep a watching brief on drug delivery industry developments and academic outputs to identify generic competition and disruptive technology and products early<br>• Protect our own technologies and products as broadly as possible with patents and trademarks<br>• Review commercial relevance of the Group's technology platforms regularly<br>• Direct innovation effort towards identified strengths and USPs<br>• Examine opportunities to diversify the pipeline by adding additional non-sustained release and non-GNP projects | No change |

# RISK MANAGEMENT
## CONTINUED

| Risk | Description | Mitigation | Change |
|---|---|---|---|
| **Obtaining / maintaining regulatory approval** | There can be no certainty that our products will receive regulatory approvals in the countries where we intend to operate, either within the timescale envisaged or at all. Regulations may also change after approval has been granted and subsequent regulatory difficulties with products may result in impositions against us. | • Develop products using safe, well-characterised active compounds<br>• Seek early scientific and regulatory advice<br>• Track the changing regulatory environment to ensure that we remain in compliance with all regulations and expectations |  No change |
| **Commercial viability of products** | There can be no assurance that our products will be commercially viable; the amounts and costs of production may not be acceptable for commercial use, or superior products may be developed. The ability to sell products at an acceptable cost would also be affected by healthcare reform and by access to appropriate sales channels and infrastructure in individual countries where we plan to operate. | • Maintain a detailed understanding of in-house platform technologies to maximise successful application thereof in Midatech therapeutic areas, whether in relation to chemistry, manufacturing, development or commercialisation<br>• Have clear go/no-go decision criteria allowing early identification of projects unlikely to succeed<br>• Portfolio management to balance higher risk projects with lower risk projects<br>• Hold Scientific and Therapeutic Advisory Board meetings to review the viability of the pipeline and allocate resources accordingly |  No change |
| **Dependence on in-house manufacturing capability** | We operate our own in-house manufacturing facility, capable of producing products based on each of our three technology platforms. As we scale-up from clinical to commercial batch sizes, there can be no assurance that the Group's development products will be capable of being manufactured in sufficient quantities, in compliance with regulatory requirements and at an acceptable cost or within an acceptable timeframe. | • Early involvement of experienced and suitably qualified organisations and individuals to plan and manage the commercial scale-up process<br>• Commitment of appropriate resources to ensure the scale-up plan can be properly executed<br>• Review of external contract manufacturing organisation and other alternatives to in-house manufacture.<br>• Clear go/no-go decision criteria to determine the optimal manufacturing route |  Increased risk |

| Risk | Description | Mitigation | Change |
|---|---|---|---|
| **Dependence on suppliers, partners and customers** | We source materials from certain suppliers, depend on contract research organisations to undertake clinical research, and have collaboration agreements with various partners for aspects of the product development and commercialisation processes. | • Identify and maintain relationships with alternative suppliers, particularly for critical materials<br>• Seek partnerships with companies of diverse interests and sizes<br>• Hold regular dialogue with partners to increase understanding of respective interests<br>• Optimise the portfolio mix and number of projects, and improve R&D productivity to expand the pipeline |  <br>No change |
| **Dependence on key personnel** | We depend on our senior management team, and on the recruitment and retention of skilled individuals to undertake product development. Recent organisational changes have the potential to have adversely impacted morale and staff retention. | • Utilise the Group's appraisal system to encourage two-way communication with individuals<br>• Implementation of PerformanceHub, employee management system and regular employee engagement surveys intended<br>• Utilise HR function to:<br>– Identify and deal with any issues as they emerge<br>– Develop succession planning<br>– Ensure stimulating and open culture and environment<br>– Identify and develop talent, both internally and externally |  <br>Increased risk |

This Strategic Report was approved by the Board on 23 April 2019 and signed on its behalf.

**Nick Robbins-Cherry**
Chief Financial Officer

**"MTD201 HAS THE POTENTIAL TO PROVIDE ADDITIONAL BENEFITS COMPARED TO CURRENT STANDARD OF CARE FOR ACROMEGALY AND NEUROENDOCRINE CANCER PATIENTS NEEDING CHRONIC TREATMENT."**

**Professor Shlomo Melmed**

Dean of Medical Faculty,
Cedars-Sinai Medical Centre,
Los Angeles

## Governance

# BOARD OF DIRECTORS

## As at 31 December 2018 the Board consisted of two Executive Directors and six Non-Executive Directors.

Following the investment in the Company by China Medical System and other investors in February 2019, three Non-Executive Directors, Pavlo Protopapa, Michele Luzi and John Johnston stepped down and a new Non-Executive Director, Huaizheng Peng, was appointed. As of the date of this Report, the Board consisted of two Executive Directors and four Non-Executive Directors. Brief biographies of the current Directors are set out below.

The Directors believe that the new streamlined Board comprised of industry experts gives Midatech Pharma plc a strong and proven Executive and Senior Management team to drive the business forward.

### CRAIG COOK

**Chief Executive Officer (52)**

Dr Cook has more than 15 years of international experience in the pharma, biomedical and high technology sectors including roles across a range of therapeutic areas, such as neurology, inflammatory, immunology, and endocrine, covering both drug development and medical affairs. He has established and led several healthcare initiatives, and held increasingly senior appointments at Johnson & Johnson, Eli Lilly, Novartis Pharma, and Serono Biotech. Dr Cook was lead adviser for Ippon Capital SA's life sciences practice.

He is a qualified physician, has a BSc in Pharmacology, Diploma in Anaesthesiology, and MBA from the London Business School. He joined Midatech in 2014 as Chief Operating Officer and Chief Medical Officer and was appointed as Chief Executive Officer on 1 June 2018.

### NICHOLAS (NICK) ROBBINS-CHERRY

**Chief Financial Officer (49)**

Mr Robbins-Cherry is a Chartered Accountant and MBA with extensive commercial and finance experience gained in the life sciences, technology and consulting sectors, including roles at CACI Limited, Johnson & Johnson and ICI PLC. Mr Robbins-Cherry has a strong track record in mergers and acquisitions and of managing complex multi-national businesses. He qualified with Coopers & Lybrand (now PwC) and has a BSc in Pharmacology.

### ROLF STAHEL

**Non-Executive Chairman (75)**

Mr Stahel has approximately 40 years of experience in the pharmaceutical industry, of which around 20 years were spent at Chief Executive and Board level in public (United Kingdom, Switzerland and United States) and private life science companies registered in Europe, the United States and Asia. Mr Stahel joined Shire as CEO in 1994 following a 27-year career at Wellcome plc (now GlaxoSmithKline). He is currently the Non-Executive chairman of Ampha Limited and was previously the Non-Executive chairman of Ergomed plc, Connexios Life Sciences Pvt Limited, EUSA Pharma Inc., Cosmo Pharmaceuticals SpA, PowderMed Limited and Newron Pharmaceuticals SpA.

## SIMON TURTON

**Senior Independent Non-Executive Director (51)**

Dr Turton previously headed Warburg Pincus' healthcare investing activities in Europe and was a principal at Index Ventures in Geneva. He has over 10 years of experience investing in biopharma companies following a ten-year career in the international pharmaceutical industry incorporating roles in research, business development and general management. Dr Turton has an MBA from INSEAD and a Ph.D. in pharmacy from the University of London. He has been a board director of private and public biomedical companies: Archimedes Pharma, Eurand, ProStrakan and Tornier. Dr Turton was most recently Chairman of Q Chip prior to its acquisition by the Group. He is currently CEO of Gensmile, a new dental corporate building a group of dental clinics in the UK.

## SIJMEN DE VRIES

**Non-Executive Director (59)**

Dr de Vries has extensive senior level experience in both the pharmaceutical and biotechnology industry. He is currently CEO of Pharming group N.V., the Euronext-listed pharmaceutical company. Dr de Vries was previously CEO of both Switzerland-based 4-Antibody and Morphochem AG, and prior to this he worked at Novartis Pharma, Novartis Ophthalmics and at SmithKline Beecham Pharmaceuticals Plc, where he held senior business and commercial positions. Dr de Vries holds an MD degree from the University of Amsterdam and a MBA in General Management from Ashridge Management College (UK).

## HUAIZHENG PENG

**Non-Executive Director (56)**

Dr Peng serves as General Manager of International Investment and Operations for China Medical System Holdings Limited, a specialty pharmaceutical company listed on the Hong Kong Stock Exchange. He served as an independent Non-executive Director in the firm for three years, and that company was admitted to trading on AIM (between 2007 and 2010). Dr Peng worked as a head of life sciences and as a director of corporate finance at Seymour Pierce, a London-based investment bank and stockbroker. In addition, he is Non-Executive Director of Destiny Pharma (an AIM listed drug development company) and Helius Medical Technology (a NASDAQ listed company), as well as some private pharmaceutical companies in Europe and in the USA. He was Non-Executive Director of China Medstar and Faron Pharmaceuticals, AIM listed companies, and NavaMedica, an Oslo listed healthcare company. Dr Peng received his Bachelor´s degree in medicine and Master's degree in medicine from Hunan Medical College (now Central South University Xiangya School of Medicine) in Changsha, Hunan Province, China. He was awarded his PhD in molecular pathology from University College London (UCL) Medical School, London, UK before subsequently practicing as a clinical lecturer there.

# CORPORATE GOVERNANCE
## CHAIRMAN'S INTRODUCTION

### In my capacity as Chairman I am pleased to present the Group's 2019 Corporate Governance Report.

Good corporate governance is a key strategic pillar for the Midatech Group. Since becoming a public company in 2014, we have sought to develop our governance framework above the level required for an AIM listed company of our size adopting many aspects of the UK Corporate Governance Code. With effect from 28 September 2018, all AIM listed companies were required to formally apply a recognised corporate governance code. Midatech has chosen to adopt the principles of the Quoted Companies Alliance Corporate Governance Code for Small and Mid-Sized Quoted Companies (the 'QCA Code'). The QCA Code identifies ten principles to be followed in order for companies to deliver growth in long term shareholder value, encompassing an efficient, effective and dynamic management framework, accompanied by good communication, to promote confidence and trust.

This Corporate Governance Report, together with the Audit Committee and Directors' Remuneration Reports that follow, set out the principles of our governance framework and how the Group has applied the QCA Code. I am very pleased to say that we are able to report full compliance with each of the ten principles of the QCA Code and that our governance framework continues to help ensure that the Group operates effectively and with full regard to Midatech's values and culture.

The appointment of a new CEO during 2018 and the Board reorganisation implemented in early 2019, along with the change in strategic focus for the Group following the sale of the US commercial business, represent important milestones for Midatech and opportunities to further embed good corporate governance. The Board aims to build on the progress made to date and intends to further enhance the role that good governance must continue to occupy in the business.

**Rolf Stahel**
Chairman

> **Good corporate governance is a key strategic pillar for the Midatech Group."**

## Strategy and Business Model

Since the divestment of the US commercial business, Midatech has focussed on its R&D activities. Our pipeline of therapies for rare cancers continues to progress. MTD201, for the treatment of neuroendocrine tumours and acromegaly, and MTX110, for the treatment of the rare children's brain tumour, DIPG, are both now in clinical development with a short path to market. For more information on our strategy please see the Strategic Report on pages 8 to 29, including information about the key challenges posed to the Company in executing its strategy, please see pages 25 and 29 of this Annual Report.

## Board of Directors

As at 31 December 2018 the Board comprised eight Directors, two of whom were Executive Directors and six Non-Executive Directors. With effect from 26 February 2019, three of the Non-Executive Directors resigned after serving on the Board for a number of years. Those who stepped down were Pavlo Protopapa, Michele Luzi and John Johnston. Also on 26 February 2019, the Board welcomed a new Non-Executive member, Dr Huaizheng Peng, who joined Midatech following the investment by China Medical System ('CMS'). The current Board reflects a very high level of experience in the pharmaceutical sector and is ideally positioned to help guide the Group as it takes its development products to market.

Dr Peng is a representative of CMS, but the Group regards the other Non-Executive Directors as independent. No remuneration is paid to either the Chairman or Non-Executive Directors in the form of shares. Sijmen de Vries and former Non-Executive Director, Michele Luzi, both hold share options granted by Midatech Limited, prior to the incorporation of Midatech Pharma plc in 2014.

The Company's shares are also listed on the NASDAQ Capital Market in the form of American Depositary Receipts ('ADRs'). Following a consolidation process, with effect from 8 April 2019, each ADR represents the right to receive twenty ordinary shares from the previous ratio of one ADR representing 2 ordinary shares. This consolidation process did not affect the total number of ordinary shares in issue, but it did reduce the number of ADRs. The Company's status as a Foreign Private Issuer means that we are permitted to follow English corporate law and the Companies Act 2006 with regard to certain aspects of corporate governance; such practices differ in significant respects from the corporate governance requirements applicable to US companies on NASDAQ.

The Board is responsible for inter alia, formulating and monitoring Group strategy, approving financial plans and reviewing performance, as well as complying with legal, regulatory and corporate governance matter and approving interim and annual financial statements. There is a schedule of matters reserved for the Board.

The Board meet regularly to consider strategy, performance and the framework of internal controls. To enable the Board to discharge its duties, all Directors receive appropriate and timely information. Briefing papers are distributed to all Directors in advance of Board meetings.

The Company has established audit, remuneration, nomination and disclosure committees of the Board with formally delegated duties and responsibilities.

## The Audit Committee

The Audit Committee assists the Board in discharging its responsibilities with regard to financial reporting, the external audit and internal controls. This includes: reviewing and monitoring the integrity of the Group's annual and interim financial statements, advising on the appointment of external auditors, reviewing and monitoring the extent of any non-audit work undertaken by external auditors, overseeing the Group's relationship with its external auditors, reviewing the effectiveness of the external audit process and reviewing the effectiveness of the Group's internal control review function. The ultimate responsibility for reviewing and approving the annual report and accounts and the half-yearly reports remains with the Board.

Prior to the Board changes announced on 26 February 2019, the Audit Committee was chaired by Pavlo Protopapa, a qualified accountant, and its other members were Simon Turton and John Johnston. The Audit Committee meet not less than twice a year. During 2018, the Audit Committee met four times. Following the Board changes, the Audit Committee is chaired by Simon Turton who is considered to have significant, recent and relevant financial experience, and its other members are Sijmen de Vries and Rolf Stahel.

The Report of the Audit Committee for the year ended 31 December 2018 can be found on page 37.

# CORPORATE GOVERNANCE
CONTINUED

## The Remuneration Committee

The Remuneration Committee assists the Board in carrying out its responsibilities in relation to remuneration, including making recommendations to the Board on the Group's policy on executive remuneration, setting the over-arching principles, parameters and governance framework of the Group's remuneration policy and determining the individual remuneration and benefits package of each of the Executive Directors and the Group Secretary, including any payment of a discretionary bonus and the award of all share options. The Remuneration Committee ensures compliance with the QCA Code in relation to remuneration wherever possible.

The Remuneration Committee is chaired by Sijmen de Vries, and its other members are Simon Turton and Rolf Stahel. Prior to the Board changes announced on 26 February 2019, Michele Luzi was also a member. The Remuneration Committee is required to meet at least twice a year. During 2018 the Remuneration Committee met on three occasions.

The Directors Remuneration Report for the year ended 31 December 2018 can be found on page 39.

## The Nomination Committee

The Nomination Committee assists the Board in discharging its responsibilities relating to the composition and make-up of the Board and any committees of the Board. It is responsible for periodically reviewing the Board's structure and identifying potential candidates to be appointed as Directors or committee members as the need may arise. The Nomination Committee is responsible for evaluating the balance of skills, knowledge and experience and the size, structure and composition of the Board and committees of the Board, retirements and appointments of additional and replacement Directors and committee members and will make appropriate recommendations to the Board on such matters.

The Nomination Committee is chaired by Rolf Stahel and its other members are all members of the Board. The Nominations Committee was formally convened twice during 2018.

## Going concern

As disclosed in the Directors' Report on page 46 the Group financial statements have been prepared on the going concern basis as the Directors believe that the Group will be able to access adequate resources to continue in operational existence for the foreseeable future. Following the fundraise, approved by shareholders on 26 February 2019, the Directors consider it is appropriate to continue to adopt the going concern basis in preparing the financial statements.

## Relationship with shareholders

The Directors seek to build and maintain a mutual understanding of objectives between the Company and its shareholders. The Company reports formally to shareholders in its Annual Report and Interim Statements setting out details of the Group's activities. In addition, the Company keeps shareholders informed of events and progress through the issue of regulatory news in accordance with the AIM Rules for Companies ("AIM Rules") of the London Stock Exchange and the Foreign Private Issuer reporting requirements as set out in Rules 13a-16 or 15d-16 of the United States Securities Exchange Act of 1934. There is regular dialogue with financial stakeholders with the intention of providing transparent communication. The Chief Executive and Chief Financial Officer meet with institutional shareholders following interim and final results. The Company also maintains investor relations pages and other information regarding the business, the Group's products and activities on its website at www.midatechpharma.com.

The Annual Report is made available to shareholders at least 21 days before the Annual General Meeting ('AGM') along with notice of the AGM. Directors are required to attend the AGM, unless unable to do so for personal reasons or due to pressing commercial commitments, and shareholders are given the opportunity to vote on each separate resolution proposed at the AGM. The Company counts all proxy votes and will indicate the level of proxies lodged for each resolution after it has first been dealt with by a show of hands.

**Rolf Stahel**
Chairman

# AUDIT COMMITTEE REPORT

## On behalf of the Board, I am pleased to present the Audit Committee Report for the year ended 31 December 2018.

**The Committee plays a key role for the Board, monitoring and reviewing all aspects of the Group's financial reporting, risk management procedures and internal controls.**

The following report provides an overview of the work undertaken by the Committee during the year. The most significant topics considered by the Committee during the year included the carrying value of goodwill and intangibles, revenue recognition, accounting for the disposal of MPUS and discontinued operations, and going concern. The Committee also reviewed the principal risk and mitigation disclosures which are set out on pages 25 to 29.

**Simon Turton**
Chairman of the Audit Committee

### The Audit Committee

The Committee, which reports to the Board, is responsible for overseeing the Group's financial reporting process as well as monitoring the effectiveness of internal control, risk management and conduct of the external audit. It also monitors the independence of the external auditors and the provision of non-audit services, if any. Prior to the Board changes announced on 26 February 2019, the Audit Committee was chaired by Pavlo Protopapa, a qualified accountant, and its other members were Simon Turton and John Johnston. Following the Board changes, the Audit Committee is chaired by Simon Turton who is considered to have significant, recent and relevant financial experience, and its other members are Sijmen de Vries and Rolf Stahel.

The Committee's meetings were also attended (by invitation) by the Chief Financial Officer, Group Financial Controller and senior representatives of the external auditor, BDO LLP ('BDO'). The Committee met twice during 2018.

### External Auditor

The Committee oversees the relationship with BDO and is responsible for developing and monitoring the Group's policy on external audit and for monitoring the external auditor's independence. BDO has direct access to the Committee Chairman should they wish to raise any matters outside of formal Committee meetings.

The Committee monitors the external auditor's effectiveness on an ongoing basis, taking into account the views of management that BDO provides a good-quality audit service. The Committee is satisfied that BDO remains independent and objective and that the Group is receiving a robust audit. However, BDO has audited the Group since 2014 and the company's operations have changed significantly in the last 12 months. In light of this, the Committee has decided that, as a matter of good practice, the Group audit should be put out to tender. BDO has been invited to participate in this process and the Board intends to make a recommendation to shareholders at the next Annual General Meeting to either reappoint BDO or appoint a new firm.

### Non-audit services

During the year there were no non-audit services provided by BDO.

The total fees charged by BDO in the year are shown in note 5.

### Internal audit

The annual review of internal control and financial reporting procedures did not highlight any issues warranting the introduction of an internal audit function. It was concluded, given the current size and transparency of the operations of the Group and the robustness of the Group's accounting and business management systems, that an internal audit function was not required, however this remains a matter for ongoing review.

# AUDIT COMMITTEE REPORT
CONTINUED

## Risk management and internal controls

The Board has collective responsibility for risk management and is assisted by the Audit Committee in monitoring the principal risks and uncertainties faced by the Group, including those specific to the pharmaceutical sector, as well as other micro and macroeconomic factors. The Board also considers risks specific to the Group such as those relating to progress of the R&D programmes, the Spanish manufacturing operation and personnel.

The Board is responsible for reviewing and maintaining the Group's system of internal control and for monitoring its effectiveness. The system of internal control is designed to manage, rather than eliminate, the risk of failure of the achievement of business objectives and can only provide reasonable but not absolute assurance against material misstatement or loss.

The Audit Committee continues to monitor and review the effectiveness of the system of internal control and report to the Board when appropriate with recommendations.

The main features of the internal control system are outlined below:

- A strong control environment exists, facilitated by the use of SAP Business One accounting and business management software, that supports a comprehensive and auditable purchasing control and approvals process. This is supplemented by the close management of the business by the Executive Directors and Senior Management Team. The Group has a defined organisational structure with delineated responsibilities and approval limits.
- The Board and Committees of the Board have schedules of matters expressly reserved for their consideration. Matters reserved for the Board include acquisitions and disposals, major capital projects, treasury and risk management policies and approval of budgets.
- The Group utilises a detailed budgeting and forecasting process. Detailed budgets are prepared annually by the Senior Management Team before submission to the Board for approval. Budgets are updated to reflect significant, known changes in the business. Actual results, the cash position and future cash flow projections are all monitored against annual budgets in detail on a monthly basis, with variances highlighted to the Board and investigated.

Financial risks are identified and evaluated for each major transaction for consideration by the Board and senior management.

- Standard financial control procedures are operated throughout the Group to ensure that the assets of the Group are safeguarded and that proper accounting records are maintained.
- A risk review process has been developed whereby the Chief Financial Officer presents a report to the Board each year on the key business risks.

# DIRECTORS' REMUNERATION REPORT

## On behalf of the Board, I am pleased to present the Remuneration Report for the year ended 31 December 2018, which sets out the remuneration policy for the Directors and the amounts earned during the year.

**The Remuneration Committee welcomes feedback on any aspect of Group remuneration and remuneration policy as disclosed in this report.**

**Sijmen de Vries**
Chairman of the Remuneration Committee

## The Remuneration Committee

The Remuneration Committee assists the Board in carrying out its responsibilities in relation to remuneration, including making recommendations to the Board on the Group's policy on executive remuneration, setting the over-arching principles, parameters and governance framework of the Group's remuneration policy and determining the individual remuneration and benefits package of each of the Executive Directors and the Group Secretary.

The Remuneration Committee ensures compliance with the QCA Code in relation to remuneration wherever possible.

The Remuneration Committee is chaired by Sijmen de Vries, and its other members are Simon Turton and Rolf Stahel. Prior to the Board changes announced on 26 February 2019, Michele Luzi was also a member.

## Policy on Executive Directors' remuneration

Executive remuneration packages are designed to attract and retain executives of the necessary skill and calibre to run the Group, with reference to benchmarking comparable groups. The Remuneration Committee recommends remuneration packages to the Board by reference to individual performance. It also uses the knowledge and experience of the Committee members, published surveys relating to AIM companies and the pharmaceutical industry, as well as advice and external benchmarking from a UK remuneration specialist company and market changes generally. The Remuneration Committee has responsibility for recommending any long term incentive schemes.

The Board determines whether or not Executive Directors are permitted to serve in roles with other companies. Such permission is only granted where a role is on a strictly limited basis, where there are no conflicts of interest or competing activities and providing there is no adverse impact on the commitments required to the Group. Earnings from such roles are not disclosed to the Group.

There are four main elements of the remuneration package for Executive Directors and staff:

### (i) Basic salaries and benefits in kind

Basic salaries are recommended to the Board by the Remuneration Committee, taking into account the performance of the individual and the rates for similar positions in comparable companies. Benefits in kind comprising death in service cover and private medical insurance are available to staff and Executive Directors. Benefits in kind are non-pensionable.

### (ii) Share options and other share-based incentives

The Group currently operates two distinct share option schemes for employees including the Executive Directors, to motivate those individuals through equity participation. The choice of scheme depends on the location of the individual:

a) Approved share options awarded to UK based staff under the 2014 Midatech Pharma plc Enterprise Management Incentive Scheme (the 'UK Plan'); and

b) Unapproved share options awarded to non-UK staff.

Prior to the Company's IPO in December 2014, some unapproved share options were granted to certain staff and key consultants however, since then, the award of unapproved share options has been limited to employees of Midatech Pharma España SL and Midatech Pharma US, Inc. prior to the sale of that business. Exercise of all share options under the schemes is subject to specified exercise periods and compliance with the AIM Rules.

# DIRECTORS' REMUNERATION REPORT
CONTINUED

## Policy on Executive Directors' remuneration
continued

The schemes are overseen by the Remuneration Committee, which recommends all grants of share options to the Board based on the Remuneration Committee's assessment of personal performance and specifying the terms under which eligible individuals may be invited to participate. The quantum of any award made since 2016 is made with reference to a fixed percentage of base salary dependent upon the position of the employee within the Group. The exercise price of all awards is the volume weighted average price for the 20 days prior to the date of the Board meeting at which the award is made.

The QCA Code requires a significant proportion of the total remuneration package of Executive Directors to comprise performance related remuneration and should be designed to align Executive Directors' interests with those of the shareholders. The Remuneration Committee currently considers that the best alignment of these interests is through the continued use of performance-based incentives through the award of share options or other share-based arrangements.

### (iii) Bonus scheme

The Group has a discretionary bonus scheme for staff and Executive Directors. Bonus payments are based on a fixed on-target percentage of base salary dependent upon the position of the employee within the Group. The bonus is moderated depending on the achievement of corporate and personal objectives.

Specific details of the objectives used to measure performance are considered commercially sensitive and hence are not disclosed in detail, however, the corporate and personal objectives for 2018, used to determine bonus payments, included the following:

- commencement of various clinical studies for lead programmes;
- divestment of the US business; and
- cost containment measures and a successful re-financing of the Company.

Each specific objective had an associated bonus weighting. The Remuneration Committee reviews actual performance against each objective and applies the appropriate weighting to individuals' maximum potential bonus in order to determine the amount payable. The maximum amount payable against these objectives is 100% of the individual's fixed, on-target percentage of base salary.

The Remuneration Committee and the Board seek to set objectives that encourage optimal, short term financial performance and maximise potential progress with the R&D portfolio thereby creating medium and long term improvements in stakeholder value.

### (iv) Pension contributions

The Group pays a defined contribution to the pension schemes of Executive Directors and other employees. The individual pension schemes are private, and their assets are held separately from the Group.

### Loss of office

The Group has no specific policy on loss of office other than to ensure that employees and Directors are compensated in accordance with their contractual entitlements. With the closure of the Abingdon R&D facility, all affected staff were offered pay in lieu of notice and statutory redundancy appropriate to their employment contracts and service with Midatech.

### Review of Executive Remuneration

Major progress was made during the year, including the commencement of first in-human clinical trials for two key pipeline R&D programmes, with one ongoing at year end and positive data having been generated from the other, and the sale of the US commercial business. Despite these achievements, given the Group's cash situation at year end, the remuneration committee proposed, and the Board of Directors unanimously agreed that there would not be an award of any cash bonus.

Furthermore, the reduction in the base salaries for the Executive Directors and remuneration for the Non-Executive Directors, implemented from 1 October 2017 as part of a broader cost cutting exercise, continued to be in force.

## Service contracts

Set out below are summary details of the service agreements and letters of appointment entered into between the Company and the Directors:

### Executive Directors

**Dr Craig Cook**

*(Chief Executive Officer)*

Dr Cook entered into a service agreement with the Company to act as Chief Executive Officer on 1 June 2018. His continuous employment with the Group commenced 1 January 2014. His appointment is terminable upon six months' notice.

**Nick Robbins-Cherry**

*(Chief Financial Officer)*

Mr Robbins-Cherry entered into a service agreement with the Company to act as Finance Director on 2 December 2014 and has since been appointed as the Group's Chief Financial Officer. Mr Robbins-Cherry's continuous employment with the Group commenced 4 February 2014. Mr Robbins-Cherry retired by rotation prior to the Company's Annual General Meeting held on 3 May 2017 during which he was re-elected by the Company's members. His appointment is terminable upon six months' notice.

### Relative importance of spend on pay

The total amount paid by the Group in remuneration to all employees, as disclosed in note 6, is as follows:

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Remuneration | 6,145 | 6,599 | 7,492 |

No dividends to shareholders have yet been paid.

### Chief Executive Officer remuneration

The total remuneration paid to Dr Craig Cook, since his appointment as Chief Executive Officer, and to Dr Jim Phillips, the previous Chief Executive Officer including a payment in 2018 on termination of his employment of £99k, is as follows:

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Craig Cook | 146 | – | – |
| Jim Phillips | 214 | 310 | 477 |

Midatech has chosen to provide disclosure on executive pay in line with initiatives such as the 2011 Dodd-Frank Wall Street Reform and Consumer Protection Act in the United States, where the US Securities and Exchange Commission was charged with drawing up rules for mandatory disclosure of pay ratios. The emoluments paid to the Chief Executive Officer, Dr Craig Cook, taken from the date of his appointment as CEO, is a multiple of 2.4 times the average amount paid to staff in the Midatech Group (2017: the then CEO, Dr Jim Phillips was paid 4.0 times the average employee remuneration).

The average amount paid per employee for all operations in the year, excluding share based payment charges, increased by 2% (2017: decrease of 18%).

No performance related share options vested during the year.

### Non-Executive Directors

The service contracts of the Non-Executive Directors are made available for inspection at the AGM.

**Rolf Stahel**

*(Non-Executive Chairman)*

Mr Stahel entered into an agreement with Midatech Limited on 13 April 2014 and was subsequently appointed Chairman with effect from 1 March 2014. Mr Stahel subsequently entered into a revised appointment agreement with the Company on 2 December 2014. Mr Stahel retired by rotation prior to the Company's Annual General Meeting held on 3 May 2017 during which he was re-elected by the Company's members. The appointment is terminable upon the election of the Board.

**Simon Turton**

*(Senior Independent Non-Executive Director)*

Dr Turton entered into a Non-Executive Director appointment letter with Midatech Limited on 2 December 2014. Dr Turton was originally appointed as chairman of Q Chip Limited on 24 March 2014 (subsequently terminated on 2 December 2014). Dr Turton retired by rotation prior to the Company's Annual General Meeting held on 27 June 2018 during which he was re-elected by the Company's members. The appointment is terminable upon the election of the Board.

**Sijmen de Vries**

*(Non-Executive Director)*

Dr de Vries entered into a Non-Executive Director appointment letter with the Company on 2 December 2014. Dr de Vries was originally appointed as a Non-Executive Director of Midatech Limited on 29 October 2004 (subsequently terminated on 2 December 2014). Dr de Vries retired by rotation prior to the Company's Annual General Meeting held on 26 May 2015 during which he was re-elected by the Company's members. The appointment is terminable upon the election of the Board.

# DIRECTORS' REMUNERATION REPORT
CONTINUED

## **Service contracts** continued

**Huaizheng Peng**
*(Non-Executive Director)*

Dr Peng entered into a Non-Executive Director appointment letter with the Company on 26 February 2019 following the investment in the Company by China Medical System Holdings.

**Michele Luzi**
*(Non-Executive Director)*

Mr Luzi entered into a Non-Executive Director appointment letter with the Company on 2 December 2014. Mr Luzi was originally appointed as a Non-Executive Director of Midatech Limited on 20 August 2010 (subsequently terminated on 2 December 2014). Mr Luzi retired by rotation prior to the Company's Annual General Meeting held on 27 June 2018 during which he was re-elected by the Company's members. Mr Luzi resigned from the Board on 26 February 2019.

**Pavlo Protopapa**
*(Non-Executive Director)*

Mr Protopapa entered into a Non-Executive Director appointment letter with the Company on 2 December 2014. Mr Protopapa was originally appointed as a Non-Executive Director of Midatech Limited on 5 December 2013 (subsequently terminated on 2 December 2014). Mr Protopapa retired by rotation prior to the Company's Annual General Meeting held on 3 May 2017 during which he was re-elected by the Company's members. Mr Protopapa resigned from the Board on 26 February 2019.

**John Johnston**
*(Non-Executive Director)*

Mr Johnston entered into a Non-Executive Director appointment letter with the Company on 2 December 2014. Mr Johnston retired by rotation prior to the Company's Annual General Meeting held on 27 June 2018 during which he was re-elected by the Company's members. Mr Johnston resigned from the Board on 26 February 2019.

## Policy on Non-Executive Directors' remuneration

The Non-Executive Directors receive a fee for their services as a director, which is approved by the Board, giving due consideration to the time commitment and responsibilities of their roles and of current market rates for comparable organisations and appointments. Non-Executive Directors are reimbursed for travelling and other incidental expenses incurred on Group business in accordance with the Group expenses policy.

The Board encourages the ownership of Midatech shares by Executives and in normal circumstances does not expect Directors to undertake dealings of a short term nature. Non-Executive Directors are preferred to remain independent to the extent that they do not trade in the Company's shares themselves.

The emoluments of the Directors of Midatech Pharma plc are set out below. No emoluments were paid to any Director by any other Group company:

| | Salary and fees £ | Bonus £ | Pensions £ | 2018 total | 2017 £ | 2016 £ |
|---|---|---|---|---|---|---|
| **Non-Executive Directors** | | | | | | |
| Rolf Stahel[1] | 95,000 | – | – | 95,000 | 99,980 | 99,980 |
| Simon Turton | 30,400 | – | – | 30,400 | 36,100 | 36,100 |
| Sijmen de Vries | 30,400 | – | – | 30,400 | 36,100 | 36,100 |
| Huaizheng Peng | – | – | – | – | – | – |
| Michele Luzi | 30,400 | – | – | 30,400 | 36,100 | 36,100 |
| Pavlo Protopapa | 30,400 | – | – | 30,400 | 36,100 | 36,100 |
| John Johnston | 30,400 | – | – | 30,400 | 36,100 | 36,100 |

| | Salary and fees £ | Bonus £ | Pensions £ | 2018 total | 2017 £ | 2016 £ |
|---|---|---|---|---|---|---|
| **Executive Directors** | | | | | | |
| Craig Cook[2] [3] | 145,939 | – | 12,833 | 158,772 | – | – |
| Jim Phillips[2] [4] | 209,117 | – | 4,165 | 213,282 | 299,157 | 309,157 |
| Nick Robbins-Cherry[2] | 155,000 | – | 17,600 | 172,600 | 177,350 | 188,350 |
| Directors' remuneration | 757,056 | – | 34,598 | 791,654 | 756,987 | 777,987 |

(1) Mr Stahel elected to forego additional fees of £40,860 due in respect of 2018, in recognition of the financial situation of the Company.

(2) Following changes to the annual allowance for tax free pension contributions, the Executive Directors both receive part of their contractual pension entitlement in the form of a taxable payment with salary.

(3) Amounts paid to Dr Cook relate to the period since 1 June 2018 on his appointment as Chief Executive Officer.

(4) Remuneration paid to Dr Phillips includes a payment of £99k on termination of his appointment.

Share-based payment expense of £146k in respect of Dr Cook and Mr Robbins-Cherry was charged to the income statement during the year (in respect of Dr Phillips and Mr Robbins-Cherry for 2017: £388k). In addition to the amounts stated above, Dr Cook received a benefit in kind of £1.2k.

Details of the payments to other related parties are disclosed in note 29.

## Directors' interests in shares

| | 31 December 2018 | | 31 December 2017 | |
|---|---|---|---|---|
| | Beneficial Interests | Non-Beneficial Interests | Beneficial Interests | Non-Beneficial Interests |
| **Non-Executive Directors** | | | | |
| Rolf Stahel[1] | 599,942 | – | 599,942 | – |
| Simon Turton | 269,413 | – | 269,413 | – |
| Sijmen de Vries | 38,802 | 59,150 | 38,802 | 59,150 |
| Huaizheng Peng | – | – | – | – |
| Michele Luzi | 131,344 | 69,328 | 131,344 | 69,328 |
| Pavlo Protopapa | 60,000 | 1,649,334 | 60,000 | 1,649,334 |
| John Johnston | 54,981 | – | 54,981 | – |
| **Executive Directors** | | | | |
| Craig Cook | 10,000 | – | 10,000 | – |
| Jim Phillips | – | – | 59,896 | – |
| Nick Robbins-Cherry | 500 | – | 500 | – |

(1) At 31 December 2018, 244,880 of Rolf Stahel's shares were subject to restrictions preventing their disposal or transfer to another party. These restrictions fall away on the following events:

a) 122,440 shares become unrestricted when the market capitalisation of the Company achieves £155m.

b) 122,440 shares become unrestricted when the market capitalisation of the Company achieves £213m.

# DIRECTORS' REMUNERATION REPORT
CONTINUED

## Directors' interests in share options

Other than as shown in the table and note above, no Director had any interest in the shares of the Company or in any subsidiary company.

The Board uses share options to align Executive Directors' and employees' interests with those of shareholders in order to provide incentives and reward them based on improvements in Group performance.

| | 31 December 2018 Options Held over Ordinary shares | 31 December 2017 Options Held over Ordinary shares |
|---|---|---|
| **Non-Executive Directors** | | |
| Rolf Stahel | – | – |
| Simon Turton | – | – |
| Sijmen de Vries | 14,000 | 17,000 |
| Huaizheng Peng | – | – |
| Michele Luzi | 18,796 | 18,796 |
| Pavlo Protopapa | – | – |
| John Johnston | – | – |
| **Executive Directors** | | |
| Craig Cook | 961,000 | 961,000 |
| Jim Phillips | – | 1,740,000 |
| Nick Robbins-Cherry | 555,000 | 555,000 |

All share options were granted with an exercise price at or above market value on the date of grant. As detailed below, some of the share options vest when the Company's share price achieves certain targets. Otherwise the main vesting condition of all share options is that the Director or employee remains employed with the Group as at the date of exercise or continues to provide consultancy services as at the date of exercise. The share options of the Directors (included in totals in note 27) are set out below:

| | Grant Date | Number Awarded | Exercise Price/ Share £ | Vesting Criteria | Expiry Date £ |
|---|---|---|---|---|---|
| **Non-Executive Directors** | | | | | |
| Michele Luzi[1] | 20/04/2012 | 18,796 | 4.19 | Fully vested | 20/04/2022 |
| Sijmen de Vries | 20/04/2012 | 4,000 | 4.19 | Fully vested | 20/04/2022 |
| | 30/06/2014 | 10,000 | 0.075 | Share price[2] | 30/06/2024 |
| **Executive Directors** | | | | | |
| Craig Cook | 01/07/2014 | 360,000 | 0.075 | Share price[2] | 30/06/2024 |
| | 31/10/2016[4] | 150,000 | 2.68 | Time based[3] | 02/12/2025 |
| | 19/12/2016 | 210,000 | 1.21 | Time based[3] | 07/12/2026 |
| | 15/12/2017 | 241,000 | 0.46 | Time and price based[5] | 15/12/2027 |

| | Grant Date | Number Awarded | Exercise Price/ Share £ | Vesting Criteria | Expiry Date £ |
|---|---|---|---|---|---|
| **Executive Directors** continued | | | | | |
| Nick Robbins-Cherry | 30/06/2014 | 60,000 | 0.075 | Share price[2] | 30/06/2024 |
| | 31/10/2016[4] | 125,000 | 2.68 | Time based[3] | 02/12/2025 |
| | 19/12/2016 | 168,000 | 1.21 | Time based[3] | 07/12/2026 |
| | 15/12/2017 | 202,000 | 0.46 | Time and price based[5] | 15/12/2027 |

(1) Share options held by Michele Luzi were granted as part of a 2011 investment round in Midatech Limited.

(2) For those options noted as vesting based on share price; 50% vest when the share price reaches £5.31 per share, a further 25% vests when the share price reaches £13.72 and the remaining 25% when the share price reaches £18.86.

(3) 25% of the options vest 12 months after the grant date, followed by vesting of 12 equal quarterly tranches, over a subsequent three-year period.

(4) Share option award relates to 2015 but the acquisition of DARA BioSciences and other activities during that year meant that there was insufficient time during Open periods to make the awards until 2016.

(5) 25% of the options become eligible to vest 12 months after the grant date, followed by 12 equal quarterly tranches becoming eligible to vest, over a subsequent three-year period. All vesting subject to the 20-VWAP share price reaching £1 at any time during the life of the option.

## Total shareholder return performance

The graph below illustrates the daily movements of the Company's AIM share price compared to the value of the Datastream UK Pharma & Bio share index, rebased to the Company's share price at IPO in December 2014.

DS-UK Pharma & Bio rebased to Midatech Pharma plc


Source: Thomson Reuters Datastream as at 14.02.19

**Sijmen de Vries**

Chairman of the Remuneration Committee

# DIRECTORS' REPORT

## The Directors present their report and the consolidated financial statements of the Group for the year ended 31 December 2018.

### Directors

The Directors during the year were:

- Rolf Stahel
- Simon Turton
- Sijmen de Vries
- Michele Luzi (resigned 26 February 2019)
- Pavlo Protopapa (resigned 26 February 2019)
- John Johnston (resigned 26 February 2019)
- Craig Cook (appointed 1 June 2018)
- James Phillips (resigned 31 May 2018)
- Nick Robbins-Cherry

In addition, Huaizheng Peng was appointed as Non Executive Director on 26 February 2019 following the investment in the Company by China Medical System Holdings.

### Research and development

The Group is continuing to develop products within its chosen areas of therapeutic focus.

### Matters covered in the Strategic Report

Details of the Group's financial instruments are presented in note 21 and future developments and policies are given in the Strategic Report.

### Dividend

The Directors are not recommending the payment of a dividend at this time due to the level of maturity of the Group.

### Post balance sheet events

On 29 January 2019, the Company announced that it had signed a licence agreement with China Medical System Holdings Limited ('CMS') for the development and commercialisation of the Group's pipeline of products in Greater China and certain South East Asian Countries. Once the Group's development products are approved in certain territories, including the US or EU, under the terms of this agreement, Midatech intends to manufacture and supply its products to CMS. CMS will be responsible for funding the development and commercialisation of the Group's product in the territories covered by the licence. Subject to certain milestones being achieved, the Company will be eligible to receive regulatory and sales-based milestone payments as well as royalty payments.

The Company also announced that, in parallel with the licence agreement, CMS intended to invest £8m by way of a Subscription for new shares. Under the terms of this Subscription, for each new share issued, CMS would also receive one warrant over one additional share with an exercise price of 50 pence per share.

On 4 February 2019, the Company announced that, following a Placing of "Units" with new and existing institutional investors, a further £4.65m had been raised, before expenses. Each Unit comprised one ordinary share and one warrant on the same terms as the CMS subscription. Following the results of the Placing, the Company launched an Open Offer to existing shareholder to subscribe for Units to raise additional gross proceeds of up to £0.75m.

At a general meeting of the Company's shareholders held on 26 February 2019, the Subscription, Placing and Open Offer were approved. As a result, the Company raised a total of £13.4m or £12.5m after expenses. Shareholders also voted to approve the Panel Waiver granted by the Takeover Panel in respect of the obligation by CMS (acting with a Concert Party) to make a mandatory general offer pursuant to Rule 9 of the Takeover Code. Following the general meeting, CMS held 51% of the issued share capital of the Company.

At the general meeting Michele Luzi, Pavlo Protopapa and John Johnston resigned from the Board and Huaizheng Peng was appointed as Non-Executive Director of the Company.

### Directors' and officers' liability insurance

The Company has, as permitted by s234 and 235 of the Companies Act 2006, maintained insurance cover on behalf of the Directors and Company Secretary indemnifying them against certain liabilities which may be incurred by them in relation to the Company.

## Employees

Midatech recognises the essential importance of employees to the success of the business and ensures that they are fully informed of events that directly affect them and their working conditions. Information on matters of concern to employees is given in briefings that seek to provide a common awareness on the part of all employees of the financial and economic factors affecting the Group's performance.

## Disabled employees

Applications for employment by disabled persons are given full and fair consideration for all vacancies in accordance with their particular aptitudes and abilities. It is the policy of the Group that training and promotion opportunities should be available to all employees.

## Directors' responsibilities

The Directors are responsible for preparing the Directors' Report, Strategic Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union, and the Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company and of the profit or loss of the Group for that period. The Directors are required to prepare financial statements in accordance with the rules of the London Stock Exchange for companies trading securities on the Alternative Investment Market. The Directors are also required to prepare and file a Form 20-F in accordance with the rules of the US Securities and Exchange Commission which require the financial statements to also be prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IASB).

In preparing these financial statements, the Directors are 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 and as issued by the International Accounting Standards Board (IASB), subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the financial statements comply with the requirements of the Companies Act 2006. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

## Directors' statement as to the disclosure of information to auditors

All of the current directors have taken all steps that they ought to have taken to make themselves aware of any information needed by the Group's auditors for the purposes of their audit and to establish that the auditors are aware of that information. The Directors are not aware of any relevant audit information of which the auditors are unaware.

## Website publication

The Directors are responsible for ensuring the Annual Report and the financial statements are made available on a website. Financial statements are published on the Group's website in accordance with legislation in the United Kingdom governing the preparation and dissemination of financial statements, which may vary from legislation in other jurisdictions. The maintenance and integrity of the Group's website is the responsibility of the Directors. The Directors' responsibility also extends to the ongoing integrity of the financial statements contained therein.

By order of the Board

**Nick Robbins-Cherry**
Chief Financial Officer

23 April 2019

**"THE COMBINATION OF A SPECIFIC CNS DIRECTED DELIVERY STRATEGY COMBINED WITH A PROMISING AGENT SUCH AS MTX110 HOLDS GREAT PROMISE FOR BETTER OUTCOMES FOR THIS DEVASTATING DISEASE."**

**Professor Sabine Mueller**

Paediatric Neuro-Oncologist,
Benioff Children's Hospital,
University of California San Francisco

## Financial Statements

# INDEPENDENT AUDITOR'S REPORT

To the members of Midatech Pharma plc

## Opinion

We have audited the financial statements of Midatech Pharma plc (the 'parent company') and its subsidiaries (the 'group') for the year ended 31 December 2018 which comprise the consolidated statement of comprehensive income, the consolidated , the consolidated statement of cash flows, the consolidated statement of changes in equity, the parent company balance sheet, the parent company statement of changes in equity and notes to the financial statements, including a summary of significant accounting policies.

The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 102, The Financial Reporting Standard in the United Kingdom and Republic of Ireland (United Kingdom Generally Accepted Accounting Practice).

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2018 and of the group's loss for the year then ended;
- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

## Separate opinion in relation to IFRSs as issued by the IASB

As explained in note 1 to the group financial statements, the group in addition to complying with its legal obligation to apply IFRSs as adopted by the European Union, has also applied IFRSs as issued by the International Accounting Standards Board (IASB).

In our opinion the group financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2018 and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with IFRSs as issued by the IASB.

## Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the group and the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the Directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the group's or the parent company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

## Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) we identified, including those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

**Presentation and disclosure of discontinued operations of Midatech Pharma US, Inc.**

| **Key audit matter** | **How our audit addressed the key audit matter** |
|---|---|
| See also note 4 (Discontinued operations) for further details.<br><br>On 1 November 2018 the group disposed of Midatech Pharma US, Inc. ("MPUS") a wholly owned subsidiary.<br><br>The results of the group are presented separately for continuing operations and the discontinued operations for the MPUS component in both the current and comparative periods. The disposal of MPUS represented the closure of the group's commercial operating segment.<br><br>The loss on disposal of MPUS is also disclosed within the loss on discontinued operations in the consolidated statement of comprehensive income.<br><br>Given the amounts recorded as discontinued operations are material to the financial statements and the significant impact on the financial statements of their presentation and disclosure, we identified this as a key audit matter. | Our audit procedures included:<br><br>• MPUS has been subject to a full scope audit to the date of disposal as it has been identified as a significant component of the group. This enabled us to verify the amounts recorded within the losses arising from discontinued operations.<br><br>• We have considered the loss on disposal of MPUS through a review of the carrying value at the date of disposal and the fair value of the consideration receivable.<br><br>• We have evaluated the completeness and accuracy of the disclosure of discontinued operations in the statement of comprehensive income, cashflow statement and the notes to the financial statements with respect to the relevant accounting standard. |

# INDEPENDENT AUDITOR'S REPORT CONTINUED

To the members of Midatech Pharma plc

## Our application of materiality

We apply the concept of materiality both in planning and performing our audit, and in evaluating the effect of misstatements. We consider materiality to be the magnitude by which misstatements, including omissions, could influence the economic decisions of reasonable users that are taken on the basis of the financial statements. Importantly, misstatements below these levels will not necessarily be evaluated as immaterial as we also take account of the nature of identified misstatements, and the particular circumstances of their occurrence, when evaluating their effect on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as follows:

| | Group | Parent company |
|---|---|---|
| **Overall materiality** | £400,000 (2017: £750,000) | £200,000 (2017: £425,000) |
| **How we determined it** | Materiality was based on 3% of total operating expenses. | Materiality for the parent company financial statements was based on 3% of net assets. |
| **Rationale for benchmark applied** | Total operating expenses is considered the most appropriate measure in assessing the performance of the group given its pre-tax loss position, stage of development and level of activities during the year. | We considered an asset based measure to best reflect the nature of the parent company which acts as a parent holding company for the group. |

In considering individual account balances and classes of transactions we apply a lower level of materiality (performance materiality) in order reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceed materiality.

Performance materiality was set at £280,000 (2017: £525,000) for the group, representing 70% of materiality. The level was set taking into account a number of factors including our past experience of adjusted and unadjusted errors, complexity of the audit and controls within the group. The same percentage was applied to each component materiality including the parent company.

Where financial information from components was audited separately, component materiality levels were set for this purpose at lower levels varying from 50% to 87% (2017: 15% to 57%) of group materiality.

We agreed with the Audit Committee that we would report to the committee all individual audit differences in excess of £12,000 (2017: £30,000), being 4% (2017: 4%) of group materiality. We also agreed to report differences below this threshold that, in our view, warranted reporting on qualitative grounds.

## An overview of the scope of our audit

Our group audit scope focussed on the group's principal operating locations and legal structure. The group has operating entities based in the UK, Spain, the US and Australia. The UK, US and Spanish entities were deemed significant components.

The UK subsidiaries were subject to full scope audits by the group auditor.

For the US component the BDO network firm in the US completed a full scope audit, up to the date of disposal of the component, in line with group reporting instructions issued by the group auditor.

The Spanish component was subject to a full scope audit by the group auditor. The group audit team were assisted by staff from the BDO network firm in Spain who performed audit procedures on behalf of the group audit team. The group auditor attended a completion meeting in Spain with local and group management.

The Australian entity was deemed a non-significant component on which we performed analytical review procedures.

## Other information

The Directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

## Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

## Matters on which we are required to report by exception

In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the Directors' report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

## Responsibilities of Directors

As explained more fully in the Directors' responsibilities statement, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Directors 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 Directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

# INDEPENDENT AUDITOR'S REPORT CONTINUED

To the members of Midatech Pharma plc

## Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about 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 ISAs (UK) will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

## Use of our report

This report is made solely to the parent company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the parent company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Parent company and the parent company's members as a body, for our audit work, for this report, or for the opinions we have formed.

**Christopher Pooles (Senior Statutory Auditor)**
For and on behalf of BDO LLP, Statutory Auditor
Reading, UK

23 April 2019

BDO LLP is a limited liability partnership registered in England and Wales (with registered number OC305127).

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2018

| | Note | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|---|
| Revenue | 3 | 149 | 149 | 776 |
| Grant revenue | | 1,789 | 840 | 547 |
| Total revenue | | 1,938 | 989 | 1,323 |
| Research and development costs | | (9,359) | (8,329) | (7,730) |
| Distribution costs, sales and marketing | | – | (170) | – |
| Administrative costs | | (4,394) | (4,266) | (3,245) |
| Impairment of intangible assets | 11 | – | (1,500) | – |
| **Loss from operations** | 5 | **(11,815)** | **(13,276)** | **(9,652)** |
| Finance income | 7 | 2 | 415 | 1,337 |
| Finance expense | 7 | (587) | (109) | (73) |
| **Loss before tax** | | **(12,400)** | **(12,970)** | **(8,388)** |
| Taxation | 8 | 2,032 | 1,265 | 2,227 |
| **Loss from continuing operations** | | **(10,368)** | **(11,705)** | **(6,161)** |
| Loss from discontinued operations net of tax | 4 | (4,662) | (4,359) | (14,001) |
| **Loss for the year attributable to the owners of the parent** | | **(15,030)** | **(16,064)** | **(20,162)** |
| **Other comprehensive income:** | | | | |
| *Items that will or may be reclassified subsequently to profit or loss when specific conditions are met:* | | | | |
| Exchange gains/(losses) arising on translation of foreign operations | | 1,156 | (1,233) | 3,228 |
| Exchange gain realised on disposal of subsidiaries | 4 | (3,842) | – | – |
| **Total other comprehensive (loss)/income, net of tax** | | **(2,686)** | **(1,233)** | **3,228** |
| **Total comprehensive loss attributable to the owners of the parent** | | **(17,716)** | **(17,297)** | **(16,934)** |
| **Loss per share** | | | | |
| Continuing operations | | | | |
| Basic and diluted loss per ordinary share - pence | 9 | 17p | 23p | 17p |
| Discontinued operations | | | | |
| Basic and diluted loss per ordinary share - pence | 9 | 8p | 8p | 39p |

The notes form an integral part of these consolidated financial statements.

# CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 31 December 2018

| Company number 09216368 | Note | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|---|
| **Assets** | | | | |
| **Non-current assets** | | | | |
| Property, plant and equipment | 10 | 1,983 | 2,529 | 2,766 |
| Intangible assets | 11 | 12,374 | 27,647 | 31,172 |
| Other receivables due in greater than one year | 14 | 469 | 465 | 448 |
| | | **14,826** | **30,641** | **34,386** |
| **Current assets** | | | | |
| Inventories | 16 | – | 941 | 817 |
| Trade and other receivables | 14 | 1,323 | 3,242 | 2,439 |
| Taxation | | 1,952 | 1,196 | 1,439 |
| Cash and cash equivalents | 15 | 2,343 | 13,204 | 17,608 |
| | | **5,618** | **18,583** | **22,303** |
| **Total assets** | | **20,444** | **49,224** | **56,689** |
| **Liabilities** | | | | |
| **Non-current liabilities** | | | | |
| Borrowings | 18 | 884 | 6,185 | 1,620 |
| Deferred tax liability | 19 | – | – | – |
| Provisions | | 165 | – | – |
| | | **1,049** | **6,185** | **1,620** |
| **Current liabilities** | | | | |
| Trade and other payables | 17 | 2,103 | 8,002 | 8,407 |
| Borrowings | 18 | 368 | 361 | 538 |
| Derivative financial liability – equity settled | 20 | – | – | 400 |
| | | **2,471** | **8,363** | **9,345** |
| **Total liabilities** | | **3,520** | **14,548** | **10,965** |
| **Issued capital and reserves attributable to owners of the parent** | | | | |
| Share capital | 23 | 1,003 | 1,003 | 1,002 |
| Share premium | 24 | 52,939 | 52,939 | 47,211 |
| Merger reserve | 24 | 53,003 | 53,003 | 53,003 |
| Foreign exchange reserve | 24 | (301) | 2,385 | 3,618 |
| Accumulated deficit | 24 | (89,720) | (74,654) | (59,110) |
| **Total equity** | | **16,924** | **34,676** | **45,724** |
| **Total equity and liabilities** | | **20,444** | **49,224** | **56,689** |

The financial statements were approved and authorised for issue by the Board of Directors on 23 April 2019 and were signed on its behalf by:

**Nick Robbins-Cherry**
Chief Financial Officer

The notes form an integral part of these consolidated financial statements.

# CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2018

| | Note | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|---|
| **Cash flows from operating activities** | | | | |
| Loss for the year | | (15,030) | (16,064) | (20,162) |
| *Adjustments for:* | | | | |
| Depreciation of property, plant and equipment | 10 | 1,016 | 983 | 772 |
| Amortisation of intangible fixed assets | 11 | 434 | 1,577 | 3,583 |
| Loss on disposal of fixed assets | | 165 | 27 | – |
| Net interest (income)/expense | 7 | 585 | (249) | (1,264) |
| Impairment of intangible assets | 12 | – | 1,500 | 11,413 |
| Share-based payment expense | 5 | (36) | 520 | 203 |
| Taxation | 8 | (2,032) | (1,265) | (9,160) |
| Loss on sale of subsidiary | 4 | 1,407 | – | – |
| Foreign exchange losses | | 130 | – | – |
| **Cash flows from operating activities before changes in working capital** | | **(13,361)** | **(12,971)** | **(14,615)** |
| Decrease/(Increase) in inventories | | 347 | (202) | (237) |
| Decrease/(Increase) in trade and other receivables | | 1,030 | (968) | (242) |
| (Decrease)/Increase in trade and other payables | | (2,995) | (267) | 358 |
| Increase in provisions | | 165 | – | – |
| **Cash used in operations** | | **(14,814)** | **(14,408)** | **(14,736)** |
| Taxes received | | 1,364 | 1,455 | 1,650 |
| **Net cash used in operating activities** | | **(13,450)** | **(12,953)** | **(13,086)** |
| **Investing activities** | | | | |
| Purchases of property, plant and equipment | 10 | (244) | (707) | (1,347) |
| Purchase of intangibles | 11 | – | (778) | (19) |
| Disposal of subsidiary, net of cash disposed | 4 | 9,259 | – | – |
| Proceeds from disposal of fixed assets | | 25 | – | – |
| Interest received | | 2 | 15 | 164 |
| **Net cash generated from/(used in) investing activities** | | **9,042** | **(1,470)** | **(1,202)** |
| **Financing activities** | | | | |
| Interest paid | | (587) | (111) | (74) |
| Payments to finance lease creditors | | (64) | (25) | (69) |
| Repayment of borrowings | | (5,821) | (552) | (235) |
| New bank loan | | – | 5,237 | 65 |
| Share issues net of costs | 23 | – | 5,728 | 15,568 |
| **Net cash generated from/(used in) financing activities** | | **(6,472)** | **10,277** | **15,255** |
| **Net (decrease)/increase in cash and cash equivalents** | | **(10,880)** | **(4,146)** | **967** |
| **Cash and cash equivalents at beginning of year** | | **13,204** | **17,608** | **16,175** |
| Exchange (losses)/gains on cash and cash equivalents | | 19 | (258) | 466 |
| **Cash and cash equivalents at end of year** | 15 | **2,343** | **13,204** | **17,608** |

The notes form an integral part of these consolidated financial statements.

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2018

| | Share capital £'000 | Share premium £'000 | Merger reserve £'000 | Foreign exchange reserve £'000 | Accumulated deficit £'000 | Total equity £'000 |
|---|---|---|---|---|---|---|
| **At 1 January 2018** | **1,003** | **52,939** | **53,003** | **2,385** | **(74,654)** | **34,676** |
| Loss for the year | – | – | – | – | (15,030) | (15,030) |
| Reclassification of foreign exchange on disposal | – | – | – | (3,842) | – | (3,842) |
| Foreign exchange translation | – | – | – | 1,156 | – | 1,156 |
| **Total comprehensive loss** | **–** | **–** | **–** | **(2,686)** | **(15,030)** | **(17,716)** |
| Share-based payment charge | – | – | – | – | (36) | (36) |
| **Total contribution by and distributions to owners** | **–** | **–** | **–** | **–** | **(36)** | **(36)** |
| **At 31 December 2018** | **1,003** | **52,939** | **53,003** | **(301)** | **(89,720)** | **16,924** |

| | Share capital £'000 | Share premium £'000 | Merger reserve £'000 | Foreign exchange reserve £'000 | Accumulated deficit £'000 | Total equity £'000 |
|---|---|---|---|---|---|---|
| **At 1 January 2017** | **1,002** | **47,211** | **53,003** | **3,618** | **(59,110)** | **45,724** |
| Loss for the year | – | – | – | – | (16,064) | (16,064) |
| Foreign exchange translation | – | – | – | (1,233) | – | (1,233) |
| **Total comprehensive loss** | **–** | **–** | **–** | **(1,233)** | **(16,064)** | **(17,297)** |
| Shares issued on 16 October 2017 – note 15 | 1 | 6,157 | – | – | – | 6,158 |
| Costs associated with share issue – note 15 | – | (429) | – | – | – | (429) |
| Share option charge | – | – | – | – | 520 | 520 |
| **Total contribution by and distributions to owners** | **1** | **5,728** | **–** | **–** | **520** | **6,249** |
| **At 31 December 2017** | **1,003** | **52,939** | **53,003** | **2,385** | **(74,654)** | **34,676** |

| | Share capital £'000 | Share premium £'000 | Merger reserve £'000 | Shares to be issued £'000 | Foreign exchange reserve £'000 | Accumulated deficit £'000 | Total equity £'000 |
|---|---|---|---|---|---|---|---|
| **At 1 January 2016** | **1,002** | **31,643** | **52,803** | **200** | **390** | **(39,151)** | **46,887** |
| Loss for the year | – | – | – | – | – | (20,162) | (20,162) |
| Foreign exchange translation | – | – | – | – | 3,228 | – | 3,228 |
| **Total comprehensive loss** | **–** | **–** | **–** | **–** | **3,228** | **(20,162)** | **(16,934)** |
| **Transactions with owners** | | | | | | | |
| Shares issued on 31 October 2016 – note 15 | – | 16,673 | – | – | – | – | 16,673 |
| Costs associated with share issue – note 15 | | (1,105) | | | | | (1,105) |
| Share option charge | – | – | – | – | – | 203 | 203 |
| Shares issued as deferred consideration for business combination | – | | 200 | (200) | – | – | – |
| **Total contribution by and distributions to owners** | **–** | **15,568** | **200** | **(200)** | **–** | **203** | **15,771** |
| **At 31 December 2016** | **1,002** | **47,211** | **53,003** | **–** | **3,618** | **(59,110)** | **45,724** |

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS

For the year ended 31 December 2018

## 1 Accounting policies

### General information

Midatech Pharma plc (the 'Company') is a company registered and domiciled in England and Wales. The Company was incorporated on 12 September 2014.

The Company is a public limited company, which has been listed on the Alternative Investment Market ('AIM'), which is a submarket of the London Stock Exchange, since 8 December 2014.

In addition, since 4 December 2015 the Company has American Depository Receipts ('ADRs') registered with the US Securities and Exchange Commission ('SEC') and is listed on the NASDAQ Capital Market.

### Basis of preparation

The Group was formed on 31 October 2014 when Midatech Pharma plc entered into an agreement to acquire the entire share capital of Midatech Limited and its wholly owned subsidiaries through the issue equivalent of shares in the Company which took place on 13 November 2014.

These financial statements have been prepared in accordance with International Financial Reporting Standards, International Accounting Standards and Interpretations (collectively IFRS) issued by the International Accounting Standards Board (IASB) and as adopted by the European Union ('adopted IFRSs') and are presented in £'000's Sterling.

The principal accounting policies adopted in the preparation of the financial statements are set out below. The policies have been consistently applied to all the periods presented.

### Reclassification of 2017 research and development costs and administrative costs – continuing operations

In 2017 the impairment charge of £1.5m against the Opsisporin IPRD intangible asset was disclosed separately on the face of the statement of comprehensive income. In doing so the impairment charge was deducted from administrative costs rather than research and development costs in error. This reclassification has no impact on the loss before tax or the net assets of the group in any year presented.

| | 2017 reclassification continuing operations | 2017 original basis continuing operations |
|---|---|---|
| Research and development costs | 8,329 | 9,829 |
| Distribution costs, sales and marketing | 170 | 170 |
| Administrative costs | 4,266 | 2,766 |
| Impairment | 1,500 | 1,500 |
| | 14,265 | 14,265 |

As a result of the transfer of the Company's Zuplenz® product to MPUS during the year and the subsequent disposal of the commercial operation, management undertook a further review of the classification of certain expenses between the R&D pipeline and commercial segments which resulted in a transfer of £0.70m in 2017 (£0.45m in 2016) from the R&D pipeline to the discontinued commercial segment.

In addition, as a result of management's review, it was found that in 2017 £1.17m (2016: £0.96m) of depreciation and amortisation had been classified to administrative costs in the segment analysis, note 3, but should have been classified to research and development in the amount of £0.97m (2016: £0.76m) and distribution costs, sales and marketing in the amount of £0.20m (2016: £0.20m). The segment note comparatives for 2017 and 2016 have therefore been reclassified.

This reclassification only impacted the segmental analysis and there was no impact on the consolidated statement of comprehensive income. Further analysis is provided in note 3.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 1 Accounting policies continued

### Adoption of new and revised standards

The group adopted IFRS 9 and IFRS 15 on their effective date of 1 January 2018, further details of the impact of the application of these standards can be found within the Financial Asset and Liabilities and Revenue accounting policies.

There is one new standard that is not effective until 1 January 2019, and therefore was not applied in preparing these financial statements.

#### IFRS 16 Leases

IFRS 16 was issued in January 2016 and it replaces IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases-Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognize a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognize the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

Lessees will be also required to re-measure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognize the amount of the re-measurement of the lease liability as an adjustment to the right-of-use asset.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs.

During 2018 the Group assessed the potential effect of IFRS 16 on its consolidated financial statements. Adoption of IFRS 16 will result in the Group recognising right-of-use assets and lease liabilities for all contracts that are, or contain, a lease. For leases currently classified as operating leases, under current accounting requirements the Group does not recognise related assets or liabilities, and instead spreads the lease payments on a straight-line basis over the lease term, disclosing in its annual financial statements the total commitment.

The Board has decided it will apply the modified retrospective adoption method in IFRS 16, and, therefore, will only recognise leases on balance sheet as at 1 January 2019. In addition, it has decided to measure right-of-use assets by reference to the measurement of the lease liability on that date. This will ensure there is no immediate impact to net assets on that date. At 31 December 2018 operating lease commitments amounted to £577k, as set out in note 25. At 1 January 2019, the Group will record a lease liability of £544k in its accounts, reflecting a 4% discount rate on the lease commitment. A corresponding right-of-use asset of £394k has been recognised by the Group in respect of two of its leases, based upon the present value of future payments under these leases.

In respect of the remaining £142k, the Group has entered into a sublease agreement to mitigate the impact of an otherwise onerous lease on the closure of its Abingdon site. This has been recognised as a lease receivable as the Group has determined that the sublease meets the definition of a finance lease under the transitional provisions of IFRS16 and therefore, no right-of-use asset is recognised.

Upon adoption of the new standard, instead of recognising an operating expense for its operating lease payments, the Group will instead recognise interest on its lease liabilities and amortisation on its right-of-use assets. Given the nature of the leases involved and assuming the current low interest rate environment continues, the Group does not currently expect the effect on loss from operations to be significant.

Refer to note 25 for further information on the Group's operating leases.

There are no other IFRS standards or interpretations not currently effective that would be expected to have a material impact on the Group.

## Basis for consolidation

The Group financial statements consolidate those of the parent company and all of its subsidiaries. The parent controls a subsidiary if it has power over the investee to significantly direct the activities, exposure, or rights to variable returns from its involvement with the investee, and the ability to use its power over the investee to affect the amount of the investor's returns. All subsidiaries have a reporting date of 31 December.

All transactions and balances between Group companies are eliminated on consolidation, including unrealised gains and losses on transactions between Group companies. Where unrealised losses on intra-Group asset sales are reversed on consolidation, the underlying asset is also tested for impairment from a Group perspective. Amounts reported in the financial statements of subsidiaries have been adjusted where necessary to ensure consistency with the accounting policies adopted by the Group.

The loss and other comprehensive income of Midatech Pharma US, Inc. (formerly DARA Biosciences, Inc) acquired in December 2015 is recognised from the effective date of acquisition i.e. 4 December 2015 through to the date of sale on 1 November 2018. Similarly, the loss and other comprehensive income of Zuplenz®, acquired as a business by Midatech Pharma plc, is recognised from 24 December 2015 until 31 October 2018 (up to the formal completion of the sale of MPUS on 1 November 2018).

Discontinued operations are presented in the consolidated statement of comprehensive income as a single line which comprises the post-tax profit or loss of the discontinued operation along with the post-tax gain or loss recognised on the re-measurement to fair value less costs to sell or on disposal of the assets or disposal groups constituting discontinued operations.

The consolidated financial statements consist of the results of the following entities:

| Entity | Summary description |
|---|---|
| Midatech Pharma plc | Ultimate holding company |
| Midatech Limited | Trading company |
| Midatech Pharma (Espana) SL (formerly Midatech Biogune SL) | Trading company |
| PharMida AG | Dormant |
| Midatech Pharma (Wales) Limited (formerly Q Chip Limited) | Trading company |
| Midatech Pharma US, Inc. (formerly DARA Biosciences, Inc.) (until 1 November 2018) | Trading company |
| Dara Therapeutics, Inc. (until 1 November 2018) | Dormant |
| Midatech Pharma Pty | Trading company |

## Going concern

The Group and parent company are subject to a number of risks similar to those of other development and early-commercial stage pharmaceutical companies. These risks include, amongst others, generation of revenue from the development portfolio and risks associated with research, development, testing and obtaining related regulatory approvals of its pipeline products. Ultimately, the attainment of profitable operations is dependent on future uncertain events which include obtaining adequate financing to fulfil the Group's commercial and development activities and generating a level of revenue adequate to support the Group's cost structure.

The Group has experienced net losses and significant cash outflows from cash used in operating activities over the past years as it develops its portfolio. As at 31 December 2018 the Group had total equity of £16.92m which includes an accumulated deficit of £89.72m, it incurred a net loss for the year to 31 December 2018 of £15.03m and used cash in operating activities of £13.45m for the same year. As at 31 December 2018, the Group had cash and cash equivalents of £2.34m.

The long term viability of the Group is dependent on its ability to generate cash from operating activities, to raise additional capital to finance its operations and to successfully obtain regulatory approval to allow marketing of the Group's development products. The Group's failure to raise capital as and when needed could have a negative impact on its financial condition and ability to pursue its business strategies.

Following the year end, Midatech concluded a fundraise in a Subscription, Placing and Open Offer. This raised proceeds of £13.4m before expenses and the new shares were admitted to AIM on 26 February 2019.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 1 Accounting policies continued

The Directors have prepared cash flow forecasts and considered the cash flow requirement for the Group for the next five years. These forecasts show that the Group has sufficient cash resources for at least the next 12 months from the date of approval of these consolidated financial statements. The Directors therefore consider it appropriate to continue to adopt the going concern basis in preparing the financial information.

### Revenue

The Group's income streams include milestone income from research and development contracts. Milestone income is recognised as revenue in the accounting period in which the milestones are achieved. Milestones are agreed on a project by project basis and will be evidenced by set deliverables.

#### Application of IFRS 15 Revenue from Contracts with Customers

The Group implemented the new standard from 1 January 2018 and applied the modified retrospective method, which required the recognition of the cumulative effect of initially applying IFRS 15 as at 1 January 2018, to accumulated deficit and not restate prior years.

The Group performed a full assessment of the impact of IFRS 15, taking advantage of the practical expedient not to apply IFRS 15 to any contracts completed at 1 January 2018, and has transitioned to the new standard through means of a consideration of the cumulative impact as at 1 January 2018. If IFRS 15 had been applied in the financial statements for the year ended 31 December 2017 and the 12-month period to 31 December 2018, the Directors do not consider that there would have been any material change to revenue recognised on the basis that all performance obligations were satisfied prior to the relevant reporting dates.

In respect of the application of IFRS 15, there is no change in the revenue recognition for services performed, which continue to be recognised over time as a reasonable assessment of the extent to which the performance obligations have been delivered; future revenues which may arise from collaboration agreements with third parties will be recognised when they become due, dependant on the nature of the revenue earned. This policy will be clarified in future financial reports once the nature of any future revenue is known. There were no material judgements applied in applying IFRS 15.

Historically, revenue from the sales of goods by Midatech Pharma US, Inc. ('MPUS') was recognised when the significant risks and rewards of ownership were transferred to the buyer and it was probable the previously agreed payment would be received. These criteria were considered to be met when the goods were delivered to the buyer. Revenue represented the full list price of products shipped to wholesalers and other customers less product returns, discounts, rebates and other incentives based on the sales price.

Sales to wholesalers provide for selling prices that were fixed on the date of sale, although MPUS offered certain discounts to group purchasing organisations and governmental programmes. The wholesalers took title to the product, bore the risk and rewards and had ownership of the inventory. MPUS had sufficient experience with their material wholesaler distribution channel to reasonably estimate product returns from its wholesalers while the wholesalers were still holding inventory.

Following the adoption of IFRS 15 on 1 January 2018, revenue from sales of goods by MPUS were recognised when all performance obligations were met. These criteria were considered to be met when the goods were delivered to the buyer. Revenue represented the full list price of products shipped to wholesalers and other customers less product returns, discounts, rebates and other incentives based on the sales price.

### Grant revenue

Where grant income is received, which is not a direct re-imbursement of related costs and at the point at which the conditions have been met for recognition as income, this has been shown within grant revenue.

### Government grants and government loans

Where government grants are received as a re-imbursement of directly related costs they are credited to research and development expense in the same period as the expenditure towards which they are intended to contribute.

The Group receives government loans that have a below-market rate of interest. These loans are recognised and measured in accordance with IFRS 9. The benefit of the below-market rate of interest is measured as the difference between the initial carrying value of the loan discounted at a market rate of interest and the proceeds received.

The difference is held within deferred revenue as a government grant and is released as a credit to grant income or to research and development expense in line with the expenditure to which it relates. In a situation where the proceeds were invested in plant and equipment, the deferred revenue is credited to research and development within the income statement in line with the depreciation of the acquired asset.

### Business combinations and externally acquired intangible assets

Business combinations are accounted for using the acquisition method at the acquisition date, which is the date at which the Group obtains control over the entity. The cost of an acquisition is measured as the amount of the consideration transferred to the seller, measured at the acquisition date fair value, and the amount of any non-controlling interest in the acquiree. The Group measures goodwill initially at cost at the acquisition date, being:

- the fair value of the consideration transferred to the seller, plus;
- the amount of any non-controlling interest in the acquiree, plus;
- if the business combination is achieved in stages, the fair value of the existing equity interest in the acquiree re-measured at the acquisition date, less; and
- the fair value of the net identifiable assets acquired and assumed liabilities.

Acquisition costs incurred are expensed and included in administrative costs. Any contingent consideration to be transferred by the acquirer is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration, whether it is an asset or liability, will be recognised either as a profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it is not re-measured.

An intangible asset, which is an identifiable non-monetary asset without physical substance, is recognised to the extent that it is probable that the expected future economic benefits attributable to the asset will flow to the Group and that its cost can be measured reliably. The asset is deemed to be identifiable when it is separable or when it arises from contractual or other legal rights.

Externally acquired intangible assets other than goodwill are initially recognised at cost and subsequently amortised on a straight-line basis over their useful economic lives where they are in use. The amortisation expense is included within the distribution costs, sales and marketing in the consolidated statement of comprehensive income. Goodwill is stated at cost less any accumulated impairment losses.

The amounts ascribed to intangibles recognised on business combinations are arrived at by using appropriate valuation techniques (see section related to critical estimates and judgements below).

In-process research and development ('IPRD') programmes acquired in business combinations are recognised as assets even if subsequent expenditure is written off because the criteria specified in the policy for development costs below are not met. IPRD is subject to annual impairment testing until the completion or abandonment of the related project. No further costs are capitalised in respect of this IPRD unless they meet the criteria for research and development capitalisation as set out below.

As per IFRS 3, once the research and development of each defined project is completed, the carrying value of the acquired IPRD is reclassified as a finite-lived asset and amortised over its useful life.

The product and marketing rights recognised in 2017 related to various licenses, the Group held via its US subsidiary. These rights were disposed of with the sale of the subsidiary.

The significant intangibles recognised by the Group and their useful economic lives are as follows:

| | |
|---|---|
| Goodwill | – Indefinite life |
| IPRD | – In process, not yet amortising |
| IT and website costs | – 4 years |
| Product and marketing rights | – Between 2 and 12 years |

The useful economic life of IPRD will be determined when the in-process research projects are completed. Amortisation of product and marketing rights ceased in June 2018 when the US entity was classified as held for sale.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 1 Accounting policies continued

### Internally generated intangible assets (development costs)

Expenditure on the research phase of an internal project is recognised as an expense in the period in which it is incurred. Development costs incurred on specific projects are capitalised when all the following conditions are satisfied:

- completion of the asset is technically feasible so that it will be available for use or sale;
- the Group intends to complete the asset and use or sell it;
- the Group has the ability to use or sell the asset and the asset will generate probable future economic benefits (over and above cost);
- there are adequate technical, financial and other resources to complete the development and to use or sell the asset; and
- the expenditure attributable to the asset during its development can be measured reliably.

Judgement is applied when deciding whether the recognition criteria are met. Judgements are based on the information available. In addition, all internal activities related to the research and development of new projects are continuously monitored by the Directors. The Directors consider that the criteria to capitalise development expenditure are not met for a product prior to that product receiving regulatory approval in at least one country.

Development expenditure not satisfying the above criteria, and expenditure on the research phase of internal projects are included in research and development costs recognised in the Consolidated Statement of Comprehensive Income as incurred. No projects have yet reached the point of capitalisation.

### Impairment of non-financial assets

Assets that have an indefinite useful life, for example goodwill, or intangible assets not ready for use, such as IPRD, are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate 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 to sell and value in use. An impairment charge of £1.5m was recognised in 2017 against the IPRD of the Midatech Pharma (Wales) Ltd cash generating unit within continuing operations.

An impairment charge of £11.4m was recognised in 2016 against the product rights of the Midatech Pharma US cash generating unit within discontinued operations.

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). After the disposal of the US operation on 1 November 2018, the group at 31 December 2018 had only one cash generating unit (2017: two, 2016: two), as set out in note 12. Non-financial assets other than goodwill that suffered impairment are reviewed for possible reversal of impairment at each reporting date.

Impairment charges are included in profit or loss, except, where applicable, to the extent they reverse gains previously recognised in other comprehensive income. An impairment loss recognised for goodwill is not reversed.

### Patents and trademarks

The costs incurred in establishing patents and trademarks are either expensed in accordance with the corresponding treatment of the development expenditure for the product to which they relate or capitalised if the development expenditure to which they relate has reached the point of capitalisation as an intangible asset.

### Joint arrangements

The Group is a party to a joint arrangement when there is a contractual arrangement that confers joint control over the relevant activities of the arrangement to the Group and at least one other party. Joint control is assessed under the same principles as control over subsidiaries.

The Group classifies its interests in joint arrangements as either:

- Joint ventures: where the Group has rights to only the net assets of the joint arrangement; or
- Joint operations: where the Group has both the rights to assets and obligations for the liabilities of the joint arrangement.

In assessing the classification of interests in joint arrangements, the Group considers:

- the structure of the joint arrangement;
- the legal form of joint arrangements structured through a separate vehicle;
- the contractual terms of the joint arrangement agreement; and
- any other facts and circumstances (including any other contractual arrangements).

## Foreign currency

Transactions entered into by subsidiary entities in a currency other than the currency of the primary economic environment, in which they operate, are recorded at the rates ruling when the transactions occur. Foreign currency monetary assets and liabilities are translated at the rates ruling at the reporting date. Exchange differences arising on the retranslation of unsettled monetary assets and liabilities are recognised immediately in profit or loss.

The presentational currency of the Group is Pounds Sterling, and the reporting currency is also Pounds Sterling. Foreign subsidiaries use the local currencies of the country where they operate. On consolidation, the results of overseas operations are translated into Pounds Sterling at rates approximating to those ruling when the transactions took place. All assets and liabilities of overseas operations, including goodwill arising on the acquisition of those operations, are translated at the rate ruling at the reporting date. Exchange differences arising on translating the opening net assets at opening rate and the results of overseas operations at actual rate are recognised in other comprehensive income and accumulated in the foreign exchange reserve.

Exchange differences recognised in the profit or loss of Group entities on the translation of long term monetary items forming part of the Group's net investment in the overseas operation concerned are reclassified to other comprehensive income and accumulated in the foreign exchange reserve on consolidation.

On disposal of a foreign operation, the cumulative exchange differences recognised in the foreign exchange reserve relating to that operation up to the date of disposal are transferred to the consolidated statement of comprehensive income as part of the profit or loss on disposal.

## Financial assets and liabilities

### Application of IFRS 9 Financial Instruments

The Group adopted IFRS 9, which addresses the classification, measurement and de-recognition of financial assets and financial liabilities, on 1 January 2018, considering the cumulative impact at this date in assessing whether an adjustment to opening reserves is required. The Group applies the simplified approach and records lifetime expected losses on all trade receivables.

This standard had no material financial impact on either the current or comparative period and there were no changes recorded in the carrying value of any financial assets or liabilities. Whilst the adoption of IFRS 9 has had no material impact, the Group's policy on provisions has now changed from an incurred to expected loss basis.

### Assets at amortised cost

The Group does not have any financial assets which it would classify as fair value through profit or loss. Therefore, all financial assets are classed as assets at amortised cost as defined below.

These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise principally through the provision of goods and services to customers (e.g. trade receivables), but also incorporate other types of contractual monetary asset. They are initially recognised at fair value plus transaction costs that are directly attributable to their acquisition or issue, and are subsequently carried at amortised cost using the effective interest rate method, less provision for impairment.

For impairment provisions, the Group applies the IFRS 9 simplified approach to measure expected credit losses using a lifetime expected credit loss provision for trade receivables to measure expected credit losses on a collective basis. Trade receivables are grouped based on a similar credit risk and ageing. Based on the scale of this area, our historic treatment is not materially different to the simplified approach under IFRS 9.

The expected loss rates are based on the Group's historic credit losses experienced over the three-year period prior to the period end. The historic loss rates are then adjusted for current and forward-looking information on macroeconomic factors.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 1 Accounting policies continued

The Group's assets at amortised costs comprise trade and other receivables and cash and cash equivalents in the consolidated statement of financial position.

Cash and cash equivalents include cash in hand, deposits held at call with original maturities of three months or less.

### Financial liabilities

The Group classifies its financial liabilities into one of two categories, depending on the purpose for which the liability was acquired.

#### Fair value through profit and loss ('FVTPL')

The Group assumed fully vested warrants and share options on the acquisition of DARA Biosciences, Inc. The number of ordinary shares to be issued when exercised is fixed, however the exercise prices are denominated in US Dollars being different to the functional currency of the parent company. Therefore, the warrants and share options are classified as equity settled derivative financial liabilities recognised at fair value through the profit and loss account.

The financial liabilities were valued using the Black-Scholes option pricing model. Financial liabilities at FVTPL are stated at fair value, with any gains or losses arising on re-measurement recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability and is included in the 'finance income' or 'finance expense' lines item in the income statement. Fair value is determined in the manner described in note 21.

Other financial liabilities include the following items:

- Borrowings are initially recognised at fair value net of any transaction costs directly attributable to the issue of the instrument. Such interest-bearing liabilities are subsequently measured at amortised cost using the effective interest rate method, which ensures that any interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the consolidated statement of financial position. Interest expense in this context includes initial transaction costs and premium payable on redemption, as well as any interest or coupon payable while the liability is outstanding.
- Government loans received on favourable terms below market rate are discounted at a market rate of interest. The difference between the present value of the loan and the proceeds is held as a government grant within deferred revenue and is released to research and development expenditure or grant income in line with when the asset or expenditure is recognised in the income statement.
- Trade payables and other short term monetary liabilities are initially recognised at fair value and subsequently carried at amortised cost using the effective interest method.

### Share capital

Financial instruments issued by the Group are classified as equity only to the extent that they do not meet the definition of a financial liability or financial asset. The Group has two classes of share in existence:

- ordinary shares of £0.00005 each are classified as equity instruments;
- deferred shares of £1 each are classified as equity instruments.

### Retirement benefits: defined contribution schemes

Contributions to defined contribution pension schemes are charged to the consolidated statement of comprehensive income in the year to which they relate.

### Provisions

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

### Share-based payments

The Group operates a number of equity-settled, share-based compensation plans, under which the entity receives services from employees as consideration for equity instruments (options) of the Group. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted:

- including any market performance conditions (including the share price);
- excluding the impact of any service and non-market performance vesting conditions (for example, remaining an employee of the entity over a specified time period); and
- including the impact of any non-vesting conditions (for example, the requirement for employees to save).

Non-market performance and service conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. Where vesting conditions are accelerated on the occurrence of a specified event, such as a change in control or initial public offering, such remaining unvested charge is accelerated to the income statement.

In addition, in some circumstances employees may provide services in advance of the grant date and therefore the grant date fair value is estimated for the purposes of recognising the expense during the period between service commencement period and grant date.

At the end of each reporting period, the Group revises its estimates of the number of options that are expected to vest based on the non-market vesting conditions. It recognises the impact of the revision to original estimates, if any, in the income statement, with a corresponding adjustment to equity. When the options are exercised, the Company issues new shares. The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium.

### Leased assets

Where substantially all of the risks and rewards incidental to ownership of a leased asset have been transferred to the Group (a 'finance lease'), the asset is treated as if it had been purchased outright. The amount initially recognised as an asset is the lower of the fair value of the leased property and the present value of the minimum lease payments payable over the term of the lease. The corresponding lease commitment is shown as a liability. Lease payments are analysed between capital and interest. The interest element is charged to the consolidated statement of comprehensive income over the period of the lease and is calculated so that it represents a constant proportion of the lease liability. The capital element reduces the balance owed to the lessor.

Where substantially all of the risks and rewards incidental to ownership are not transferred to the Group (an 'operating lease'), the total rentals payable under the lease are charged to the consolidated statement of comprehensive income on a straight-line basis over the lease term. The aggregate benefit of lease incentives is recognised as a reduction of the rental expense over the lease term on a straight-line basis.

### Deferred taxation

Deferred tax assets and liabilities are recognised where the carrying amount of an asset or liability in the consolidated statement of financial position differs from its tax base, except for differences arising on:

- the initial recognition of goodwill;
- the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting or taxable profit; and
- investments in subsidiaries and jointly controlled entities where the Group is able to control the timing of the reversal of the difference and it is probable that the difference will not reverse in the foreseeable future.

Recognition of deferred tax assets is restricted to those instances where it is probable that taxable profit will be available against which the difference can be utilised.

The amount of the asset or liability is determined using tax rates that have been enacted or substantively enacted by the reporting date and are expected to apply when the deferred tax assets or liabilities are recovered or settled.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 1 Accounting policies continued

### Property, plant and equipment

Items of property, plant and equipment are initially recognised at cost. As well as the purchase price, cost includes directly attributable costs.

Depreciation is provided on all items of property, plant and equipment so as to write off their carrying value over their expected useful economic lives. It is provided at the following rates:

| | |
|---|---|
| Fixtures and fittings | – 25% per annum straight line |
| Leasehold improvements | – the shorter of 10% per annum straight line or over the lease term |
| Computer equipment | – 25% per annum straight line |
| Laboratory equipment | – 15% – 25% per annum straight line |

### Inventories

Inventories are stated at the lower of cost or net realisable value. Net realisable value is the market value. In evaluating whether inventories are stated at the lower of cost or net realisable value, management considers such factors as the amount of inventory on hand and in the distribution channel, estimated time required to sell such inventory, remaining shelf life, and current and expected market conditions, including levels of competition.

If net realisable value is lower than the carrying amount a write down provision is recognised for the amount by which the carrying value exceeds its net realisable value.

Inventory is valued at the lower of cost or market value using the FIFO method. Inventory is charged to the income statement as cost of sales as it is sold.

## 2 Critical accounting estimates and judgements

The preparation of these consolidated financial statements requires the Group to make estimates, assumptions and judgments that can have a significant impact on the reported amounts of assets and liabilities, revenue and expenses and related disclosure of contingent assets and liabilities, at the respective dates of our financial statements. The Group bases its estimates, assumptions and judgments on historical experience and various other factors that we believe to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. Management evaluates estimates, assumptions and judgments on a regular basis and makes changes accordingly, and discusses critical accounting estimates with the board of Directors.

The following are considered to be critical accounting policies because they are important to the portrayal of the financial condition or results of operations of the Group and they require critical management estimates and judgments about matters that are uncertain.

### Business combinations

The Directors determine and allocate the purchase price of an acquired business to the assets acquired and liabilities assumed as of the business combination date. The purchase price allocation process requires the use of significant estimates and assumptions, including the estimated fair value of the acquired intangible assets.

While the Directors use their best estimates and assumptions as part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the date of acquisition, our estimates and assumptions are inherently uncertain and subject to refinement. Examples of critical estimates in valuing the intangible assets we have acquired or may acquire in the future include but are not limited to:

- future expected cash flows from in-process research and development;
- the fair value of the property, plant and equipment; and
- discount rates.

### Impairment of goodwill and intangible assets not yet ready for use

Goodwill and intangibles not yet ready for use are tested for impairment at the cash generating unit level on an annual basis at the year end and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a cash generating unit below its carrying value. These events or circumstances could include a significant change in the business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

Application of the goodwill impairment test requires judgment, including the identification of cash generating units, assignment of assets and liabilities to such units, assignment of goodwill to such units and determination of the fair value of a unit and for intangible assets not yet ready for use, the fair value of the asset. The fair value of each cash generating unit or asset is estimated using the income approach, on a discounted cash flow methodology. This analysis requires significant judgments, including estimation of future cash flows, which is dependent on internal forecasts, including for revenues and development costs, estimation of the long term rate of growth for the business, estimation of the useful life over which cash flows will occur and determination of our weighted-average cost of capital.

The carrying value of goodwill was £2.29m and intangibles not yet ready for use was £10.1m as at 31 December 2018 (note 11).

The estimates used to calculate the fair value of a cash generating unit change from year to year based on operating results and market conditions. Changes in these estimates and assumptions could materially affect the determination of fair value and goodwill impairment for each such unit. Based on the analysis performed, there was no impairment of the remaining goodwill after the sale of MPUS in the year ended 31 December 2018 or in 2017, and there was no impairment charge against the IPRD of the Midatech Pharma (Wales) Ltd cash generating unit (£1.5m in 2017). See note 12.

### Share-based payments

The Group accounts for share-based payment transactions for employees in accordance with IFRS 2 Share-based Payment, which requires the measurement of the cost of employee services received in exchange for the options on our ordinary shares, based on the fair value of the award on the grant date.

The Directors selected the Black-Scholes-Merton option pricing model as the most appropriate method for determining the estimated fair value of our share-based awards without market conditions. For performance-based options that include vesting conditions relating to the market performance of our ordinary shares, a Monte Carlo pricing model was used in order to reflect the valuation impact of price hurdles that have to be met as conditions to vesting.

The resulting cost of an equity incentive award is recognised as expense over the requisite service period of the award, which is usually the vesting period. Compensation expense is recognised over the vesting period using the straight-line method and classified in the consolidated statements of comprehensive income.

The assumptions used for estimating fair value for share-based payment transactions are disclosed in note 27 to our consolidated financial statements and are estimated as follows:

- volatility is estimated based on the average annualised volatility of a number of publicly traded peer companies in the biotech sector;
- the estimated life of the option is estimated to be until the first exercise period, which is typically the month after the option vests; and
- the dividend return is estimated by reference to our historical dividend payments. Currently, this is estimated to be zero as no dividend has been paid in the prior periods.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 2 Critical accounting estimates and judgements continued

### Income taxes

Deferred tax assets are recognised for unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgment is required to determine the amount of deferred tax assets that can be recognised based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

In 2018, there were approximately £40.4m of gross unutilised tax losses carried forward (2017: £38.4m, 2016: £27.0m). No deferred tax asset has been provided in respect of these losses as there was insufficient evidence to support their recoverability in future periods.

### Research and development costs

Research and development costs are charged to expense as incurred and are typically made up of salaries and benefits, clinical and preclinical activities, drug development and manufacturing costs, and third-party service fees, including for clinical research organizations and investigative sites. Costs for certain development activities, such as clinical trials, are periodically recognised as intangible assets based on an evaluation of the progress to completion of specific tasks using data such as patient enrolment, clinical site activations, or information provided by vendors on their actual costs incurred. Payments for these activities are based on the terms of the individual arrangements, which may differ from the pattern of costs incurred, and are reflected in the financial statements as prepaid or accrued expenses.

## 3 Segment Information

### Revenue from contracts with customers

#### Geographical analysis of revenue by destination of customer

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Revenue from continuing operations: | | | |
| United Kingdom | 149 | 79 | 491 |
| Rest of Europe | – | 70 | 35 |
| United States | – | – | 250 |
| | **149** | **149** | **776** |
| Revenue from discontinued operations | | | |
| United States | 3,882 | 6,609 | 5,600 |

In 2018, all revenue from continuing operations came from a single customer (2017: 3 customers; 2016: 4 customers). Within revenue from discontinued operations for 2018, reported in the consolidated statement of comprehensive income under loss from discontinued operations, four customers each accounted for at least 10% of revenue from discontinued operations (2017: three customers, 2016: three customers):

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Customer A | 26% | 23% | 25% |
| Customer B | 25% | 7% | – |
| Customer C | 13% | 15% | 19% |
| Customer D | 12% | 20% | 12% |

Following the disposal of the US commercial business, the Group contains one reportable operating segment, Pipeline Research and Development ('Pipeline R&D'). This segment seeks to develop products using the Group's nanomedicine and sustained release technology platforms.

The accounting policies of the reportable segments are consistent with the Group's accounting policies described in note 1. Segment results represent the result of each segment without the allocation of head office expenses, interest expense, interest income and tax.

No measures of segment assets and segment liabilities are reported to the Group's Board of Directors in order to assess performance and allocate resources. There is no intersegment activity and all revenue is generated from external customers.

Both the UK and Spanish entities meet the aggregation criteria and have therefore been presented as a single reportable segment under Pipeline R&D. The research and development activities involve the discovery and development of pharmaceutical products in the field of nanomedicine and sustained release technology. The US operating company is engaged in the sale and marketing of cancer supportive care products and was reported historically under the Commercial segment.

**Segmented results for the year ended 31 December 2018**

| | Pipeline R&D £'000 | Commercial (discontinued) £'000 | Consolidated (including discontinued operations) £'000 |
|---|---|---|---|
| Revenue | 149 | 3,882 | 4,031 |
| Grant revenue | 1,789 | – | 1,789 |
| Total revenue | 1,938 | 3,882 | 5,820 |
| Cost of sales | – | (1,286) | (1,286) |
| Research and development costs | (8,555) | (283) | (8,838) |
| Distribution costs, sales and marketing | – | (4,357) | (4,357) |
| Administrative costs | (4,087) | (872) | (4,959) |
| Loss on disposal of discontinued operations | – | (1,407) | (1,407) |
| Depreciation | (1,011) | (5) | (1,016) |
| Amortisation | (100) | (334) | (434) |
| Loss from operations | (11,815) | (4,662) | (16,477) |
| Finance income | 2 | – | 2 |
| Finance expense | (587) | – | (587) |
| Loss before tax | (12,400) | (4,662) | (17,062) |
| Taxation | 2,032 | – | 2,032 |
| Loss for the year | (10,368) | (4,662) | (15,030) |
| Loss from continuing operations | | | (10,368) |
| Loss from discontinued operations | | | (4,662) |

**Segmented results for the year ended 31 December 2017**

| | Pipeline R&D £'000 | Commercial (discontinued) £'000 | Consolidated (including discontinued operations) £'000 |
|---|---|---|---|
| Revenue | 149 | 6,609 | 6,758 |
| Grant revenue | 840 | – | 840 |
| Total revenue | 989 | 6,609 | 7,598 |
| Cost of sales | – | (926) | (926) |
| Research and development costs (reclassified) | (7,355) | (356) | (7,711) |
| Distribution costs, sales and marketing (reclassified) | (170) | (7,477) | (7,647) |
| Administrative costs (reclassified) | (4,266) | (566) | (4,832) |
| Depreciation | (974) | (9) | (983) |
| Amortisation (reclassified) | – | (1,577) | (1,577) |
| Impairment of intangible assets | (1,500) | – | (1,500) |
| Loss from operations | (13,276) | (4,302) | (17,578) |
| Finance income | 415 | – | 415 |
| Finance expense | (109) | (57) | (166) |
| Loss before tax | (12,970) | (4,359) | (17,329) |
| Taxation | 1,265 | – | 1,265 |
| Loss for the year | (11,705) | (4,359) | (16,064) |
| Loss from continuing operations | | | (11,705) |
| Loss from discontinued operations | | | (4,359) |

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 3 Segment Information continued

**Segmented results for the year ended 31 December 2016**

| | Pipeline R&D £'000 | Commercial (discontinued) £'000 | Consolidated (including discontinued operations £'000 |
|---|---|---|---|
| Revenue | 776 | 5,600 | 6,376 |
| Grant revenue | 547 | – | 547 |
| Total revenue | 1,323 | 5,600 | 6,923 |
| Cost of sales | – | (667) | (667) |
| Research and development costs (reclassified) | (6,968) | (66) | (7,034) |
| Distribution costs, sales and marketing (reclassified) | – | (8,734) | (8,734) |
| Administrative costs (reclassified) | (3,245) | (2,061) | (5,306) |
| Depreciation | (762) | (10) | (772) |
| Amortisation (reclassified) | – | (3,583) | (3,583) |
| Impairment of intangible assets | – | (11,413) | (11,413) |
| Loss from operations | (9,652) | (20,934) | (30,586) |
| Finance income | 1,337 | – | 1,337 |
| Finance expense | (73) | – | (73) |
| Loss before tax | (8,388) | (20,934) | (29,322) |
| Taxation | 2,227 | 6,933 | 9,160 |
| Loss for the year | (6,161) | (14,001) | (20,162) |
| Loss from continuing operations | | | (6,161) |
| Loss from discontinued operations | | | (14,001) |

During 2018, management undertook a further review of the classification of certain expenses between R&D pipeline and commercial segments in 2017 and 2016. This reclassification only impacted the segmental analysis and there was no impact on the consolidated statement of comprehensive income. Further detail is provided in note 1.

**Non-current assets by location of assets**

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Spain | 1,860 | 2,154 | 2,125 |
| United Kingdom | 12,966 | 15,331 | 16,489 |
| United States | – | 13,156 | 15,772 |
| | 14,826 | 30,641 | 34,386 |

All material additions to non-current assets in 2018, 2017 and 2016 were in the Pipeline R&D segment.

## 4 Discontinued operations

During the year the group made the decision to sell its Commercial business based in the US. The sale completed on 1 November 2018 to Barings LLC, a member of the MassMutual Financial Group, for total consideration of up to $19m. This included $6m of consideration contingent payable on the achievement of various net revenue milestones for the MPUS business for the financial years 2018 and 2019. Based on a probability adjusted, discounted cash flow model, the estimate of the contingent consideration receivable at 31 December 2018 was nil.

The statement of cash flows includes the following amounts relating to discontinued operations:

| | 2018 £'000 |
|---|---|
| Cash consideration received | 9,350 |
| Other consideration received | – |
| Total consideration received | 9,350 |
| Cash disposed of | (91) |
| Net cash inflow on disposal of discontinued operation | 9,259 |
| Net assets disposed (other than cash): | 3 |
| Property, plant and equipment | 15,662 |
| Intangibles | 948 |
| Inventory | 629 |
| Trade and other payables | (2,734) |
| Total net assets disposed of (other than cash) | (14,508) |
| Loss on disposal of discontinued operation before and after tax | (5,249) |
| Foreign exchange gain realised on disposal | 3,842 |
| Loss on disposal | (1,407) |

The post-tax loss on disposal of discontinued operations was determined as follows:

| Result of discontinued operations | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Revenue | 3,882 | 6,609 | 5,600 |
| Expenses other than finance costs | (7,137) | (10,911) | (15,121) |
| Finance costs | – | (57) | – |
| Impairment | – | – | (11,413) |
| Loss from discontinued operations before tax | (3,255) | (4,359) | (20,934) |
| Taxation | – | – | 6,933 |
| Loss on disposal of discontinued operations | (1,407) | – | – |
| Loss for the year from discontinued operations after tax | (4,662) | (4,359) | (14,001) |

| Statement of cash flows | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| The statement of cash flows includes the following amounts relating to discontinued operations: | | | |
| Operating activities | (5,368) | (1,654) | 1,251 |
| Investing activities | – | – | (11) |
| Financing activities | (7) | (34) | (35) |
| Net cash flow from discontinued operations | (5,375) | (1,688) | 1,205 |

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 5 Loss from operations

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Loss from operations is stated after charging/(crediting): | | | |
| Changes in inventories of finished goods and work in progress | (976) | 202 | 256 |
| Write down of inventory to net realisable value | – | – | 287 |
| Depreciation of property, plant and equipment | | | |
| – From continuing operations | 1,011 | 974 | 762 |
| – From discontinued operations | 5 | 9 | 10 |
| Amortisation of intangible assets – product and marketing rights | | | |
| – From continuing operations | 100 | 193 | 193 |
| – From discontinued operations | 334 | 1,384 | 3,390 |
| Impairment of intangible assets | – | 1,500 | 11,413 |
| Fees payable to the Company's auditor for the audit of the parent Company | 111 | 110 | 100 |
| Fees payable to the Company's subsidiary auditors for the audits of the subsidiary accounts | 143 | 140 | 139 |
| Fees payable to the Company's auditor for: | | | |
| – Other services | 83 | 100 | 72 |
| Operating lease expense: | | | |
| – Property | 386 | 277 | 385 |
| – Plant and machinery | – | – | 194 |
| Arrangement/penalty fees for loan facility | 469 | 57 | – |
| Foreign exchange(gain)/loss | 212 | (39) | 31 |
| Loss on disposal of property, plant and equipment | 165 | 27 | – |
| Equity settled share-based payment | (36) | 520 | 203 |

Amortisation of product and marketing rights are included with distribution costs, sales and marketing expenses. Amortisation ceased when the assets were reclassified as held for sale on 30 June 2018 and were sold on 1 November 2018.

## 6 Staff costs

Staff costs (including Directors), for continuing and discontinued operations, comprise:

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Staff costs (including Directors) comprise: | | | |
| Wages and salaries | 5,393 | 5,278 | 6,314 |
| Defined contribution pension cost (note 26) | 149 | 158 | 206 |
| Social security contributions and similar taxes | 639 | 643 | 769 |
| Share-based payment | (36) | 520 | 203 |
| | 6,145 | 6,599 | 7,492 |
| Continuing operations | 4,352 | 4,578 | 4,663 |
| Discontinued operations | 1,793 | 2,021 | 2,829 |
| | 6,145 | 6,599 | 7,492 |

## Employee numbers

The average number of staff employed by the Group during the financial year, for continuing and discontinued operations, amounted to:

| | 2018 | 2017 | 2016 reclassified |
|---|---|---|---|
| Research and development | 63 | 62 | 57 |
| General and administration | 16 | 17 | 19 |
| Sales and marketing | 6 | 6 | 8 |
| | 85 | 85 | 84 |

### Key management personnel compensation

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, including the Directors of the Company listed on page 46, and the Chief Operating Officer.

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Wages and salaries | 900 | 811 | 1,054 |
| Defined contribution pension cost | 39 | 68 | 59 |
| Payments made to third parties | 142 | 142 | 142 |
| Social security contributions and similar taxes | 77 | 97 | 152 |
| Benefits in kind | 3 | 3 | 2 |
| Share-based payment | (92) | 388 | 184 |
| | 1,069 | 1,509 | 1,593 |

Emoluments disclosed above include the following amounts in respect of the highest paid Director. Directors' emoluments are disclosed on pages 42 and 43.

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Salary | 110 | 299 | 448 |
| Total pension and other post-employment benefit costs | 4 | 10 | 28 |
| Benefits in kind | 1 | 1 | 1 |
| Termination benefits | 99 | – | – |
| | 214 | 310 | 477 |

None of the Directors have exercised share options during the year (2017: nil, 2016: nil).

During the year 3 Directors (2017: 2, 2016: 2) participated in a defined contribution pension scheme.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 7 Finance income and expense

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| **Finance income** | | | |
| Interest received on bank deposits | 2 | 15 | 164 |
| Gain on equity settled derivative financial liability | – | 400 | 1,173 |
| **Total finance income** | **2** | **415** | **1,337** |

The gain on the equity settled derivative financial liability in 2017 and 2016 arose due to the reduction in the share price and the lapsing of associated warrants and options as set out in note 20.

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| **Finance expense** | | | |
| Bank loans | 587 | 18 | 16 |
| Other loans | – | 91 | 57 |
| **Total finance expense** | **587** | **109** | **73** |

## 8 Taxation

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| **Current tax credit** | | | |
| Current tax credited to the income statement | 1,952 | 1,253 | 1,936 |
| Taxation payable in respect of foreign subsidiary | (67) | – | (25) |
| Adjustment in respect of prior year | 128 | – | – |
| | 2,013 | 1,253 | 1,911 |
| **Deferred tax credit** | | | |
| Reversal of temporary differences | 19 | 12 | 316 |
| **Total tax credit** | **2,032** | **1,265** | **2,227** |

There was no tax charge relating to discontinued operations for 2018 and 2017. For 2016, the reversal of the deferred tax provision, credited to the income statement was £316k.

The reasons for the difference between the actual tax charge for the year and the standard rate of corporation tax in the United Kingdom applied to losses for the year are as follows:

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Loss for the year, continuing and discontinued operations | (15,030) | (16,064) | (20,162) |
| Income tax credit – continuing operations | (2,032) | (1,265) | (2,227) |
| Income tax credit – discontinuing operations | – | – | (6,933) |
| Loss before tax | (17,062) | (17,329) | (29,322) |
| Expected tax credit based on the standard rate of United Kingdom corporation tax at the domestic rate of 19% (2017: 19.25%, 2016: 20.25%) | (3,241) | (3,336) | (5,864) |
| Expenses not deductible for tax purposes | 2,492 | 412 | 1,022 |
| Adjustment in respect of prior period | (129) | – | (435) |
| Additional deduction for R&D expenditure | – | – | 4 |
| Surrender of tax losses for R&D tax refund | (1,955) | (1,196) | (1,503) |
| Reversal of deferred tax on impairment | – | – | (3,421) |
| Unrelieved tax losses and other deductions arising in the period | (220) | (156) | (166) |
| Foreign exchange differences | (26) | (84) | 712 |
| Deferred tax not recognised | 1,047 | 3,095 | 491 |
| Tax credit related to discontinued operations | – | – | (6,933) |
| Total tax credited to the income statement | **(2,032)** | **(1,265)** | **(2,227)** |

The taxation credit arises on the enhanced research and development tax credits accrued for the respective periods.

## 9 Loss per share

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| *Numerator* | | | |
| Loss used in basic EPS and diluted EPS: | | | |
| Continuing operations | (10,368) | (11,705) | (6,161) |
| Discontinued operations | (4,662) | (4,359) | (14,001) |
| *Denominator* | | | |
| Weighted average number of ordinary shares used in basic EPS: | 61,126,053 | 51,317,320 | 36,072,752 |
| Basic and diluted loss per share: | | | |
| Continuing operations – pence | (17p) | (23p) | (17p) |
| Discontinued operations – pence | (8p) | (8p) | (39p) |

The Group has made a loss in the current and previous years presented, and therefore the options and warrants are anti-dilutive. As a result, diluted earnings per share is presented on the same basis for all periods shown.

On 26 February 2019, as a result of a Subscription, Placing and Open Offer, 348,215,478 new ordinary shares were issued, increasing the total number of issued shares to 409,399,613.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 10 Property, plant and equipment

| | Fixtures and fittings £'000 | Leasehold improvements £'000 | Computer equipment £'000 | Laboratory equipment £'000 | Total £'000 |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| **At 1 January 2016** | 1,319 | 1,112 | 354 | 983 | 3,768 |
| Additions | 2 | 715 | 43 | 609 | 1,369 |
| Disposal | – | – | (1) | – | (1) |
| Transfer | (1,125) | – | (122) | 1,247 | – |
| Exchange differences | 32 | 172 | 7 | 211 | 422 |
| **At 31 December 2016** | **228** | **1,999** | **281** | **3,050** | **5,558** |
| Additions | 18 | 41 | 57 | 591 | 707 |
| Disposal | – | – | – | (41) | (41) |
| Exchange differences | 6 | 72 | 4 | 69 | 151 |
| **At 31 December 2017** | **252** | **2,112** | **342** | **3,669** | **6,375** |
| Additions | 4 | 106 | 40 | 353 | 503 |
| Disposals | (5) | (229) | – | (401) | (635) |
| Exchange differences | 2 | 24 | 1 | 30 | 57 |
| **At 31 December 2018** | **253** | **2,013** | **383** | **3,651** | **6,300** |

| | Fixtures and fittings £'000 | Leasehold improvements £'000 | Computer equipment £'000 | Laboratory equipment £'000 | Total £'000 |
|---|---|---|---|---|---|
| **Accumulated depreciation** | | | | | |
| **At 1 January 2016** | **458** | **733** | **180** | **413** | **1,784** |
| Charge for the year | 41 | 134 | 54 | 543 | 772 |
| Transfer | (369) | (96) | (118) | 583 | – |
| Exchange differences | 19 | 101 | 6 | 110 | 236 |
| **At 31 December 2016** | **149** | **872** | **122** | **1,649** | **2,792** |
| Charge for the year | 43 | 330 | 68 | 542 | 983 |
| Disposals | – | – | – | (14) | (14) |
| Exchange differences | 4 | 36 | 2 | 43 | 85 |
| **At 31 December 2017** | **196** | **1,238** | **192** | **2,220** | **3,846** |
| Charge for the year | 43 | 403 | 72 | 499 | 1,016 |
| Disposals | – | (175) | (3) | (421) | (599) |
| Exchange differences | 2 | 19 | 4 | 28 | 53 |
| **At 31 December 2018** | **241** | **1,485** | **265** | **2,326** | **4,317** |
| **Net book value** | | | | | |
| **At 31 December 2018** | **12** | **528** | **118** | **1,325** | **1,983** |
| At 31 December 2017 | 56 | 874 | 150 | 1,449 | 2,529 |
| At 31 December 2016 | 79 | 1,127 | 159 | 1,401 | 2,766 |

Included within the total net book value of tangible fixed assets is £258k (2017: £63k 2016: £33k) in respect of assets held under finance leases and similar hire purchase contracts. The depreciation charge for the year on these assets was £133k (2017: £62k, 2016: £22k). These assets were held as security in respect of their finance lease obligations. Proceeds of £25k were received during the year in relation to the sale of fixed assets.

## 11 Intangible assets

| | In-process research and development £'000 | Product and marketing rights £'000 | Goodwill £'000 | IT/Website costs £'000 | Total £'000 |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| **At 1 January 2016** | **12,600** | **18,321** | **12,456** | **15** | **43,392** |
| Additions | – | – | – | 19 | 19 |
| Foreign exchange | – | 3,160 | 2,032 | – | 5,192 |
| Disposals | – | – | – | (8) | (8) |
| **At 31 December 2016** | **12,600** | **21,481** | **14,488** | **26** | **48,595** |
| Additions | 778 | – | – | – | 778 |
| Foreign exchange | – | (1,625) | (1,044) | 1 | (2,668) |
| **At 31 December 2017** | **13,378** | **19,856** | **13,444** | **27** | **46,705** |
| Disposals | – | (21,022) | (11,808) | – | (32,830) |
| Foreign exchange | – | 1,166 | 655 | 1 | 1,822 |
| **At 31 December 2018** | **13,378** | **–** | **2,291** | **28** | **15,697** |

| | In-process research and development £'000 | Product and marketing rights £'000 | Goodwill £'000 | IT/Website Costs £'000 | Total £'000 |
|---|---|---|---|---|---|
| **Accumulated amortisation** | | | | | |
| **At 1 January 2016** | **1,800** | **243** | **–** | **10** | **2,053** |
| Amortisation charge for the year | – | 3,578 | – | 5 | 3,583 |
| Impairment | – | 11,413 | – | – | 11,413 |
| Foreign exchange | – | 374 | – | – | 374 |
| **At 31 December 2016** | **1,800** | **15,608** | **–** | **15** | **17,423** |
| Amortisation charge for the year | – | 1,574 | – | 3 | 1,577 |
| Impairment | 1,500 | – | – | – | 1,500 |
| Foreign exchange | – | (1,443) | – | 1 | (1,442) |
| **At 31 December 2017** | **3,300** | **15,739** | **–** | **19** | **19,058** |
| Amortisation charge for the year | – | 431 | – | 3 | 434 |
| Disposals | – | (17,103) | – | – | (17,103) |
| Foreign exchange | – | 933 | – | 1 | 934 |
| **At 31 December 2018** | **3,300** | **–** | **–** | **23** | **3,323** |
| **Net book value** | | | | | |
| **At 31 December 2018** | **10,078** | **–** | **2,291** | **5** | **12,374** |
| At 31 December 2017 | 10,078 | 4,117 | 13,444 | 8 | 27,647 |
| At 31 December 2016 | 10,800 | 5,873 | 14,488 | 11 | 31,172 |

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 11 Intangible assets continued

The individual intangible assets, excluding goodwill, which are material to the financial statements are:

| | Carrying amount | | | Remaining amortisation period | | |
|---|---|---|---|---|---|---|
| | 2018 £'000 | 2017 £'000 | 2016 £'000 | 2018 (years) | 2017 (years) | 2016 (years) |
| Midatech Pharma (Wales) Limited acquired IPRD | 9,300 | 9,300 | 10,800 | n/a in process | n/a in process | n/a in process |
| Midatech Pharma US, Inc., product and marketing rights | – | 1,995 | 3,557 | n/a | Between 1 and 3 | Between 1 and 4 |
| Zuplenz® product and marketing rights | – | 2,122 | 2,316 | n/a | 11 | 12 |
| MTX110 acquired IPRD | 778 | 778 | – | n/a in process | n/a in process | – |
| | 10,078 | 14,195 | 16,673 | | | |

## 12 Impairment testing

### Midatech Pharma (Wales) Ltd

Details of goodwill and IPRD allocated to the acquired cash generating unit and the valuation basis are as follows:

| | Indefinite lived | | | | | | |
|---|---|---|---|---|---|---|---|
| | IPRD carrying amount | | | Goodwill carrying amount | | | |
| Name | 2018 £'000 | 2017 £'000 | 2016 £'000 | 2018 £'000 | 2017 £'000 | 2016 £'000 | Valuation Basis |
| CGU – Midatech Pharma (Wales) Ltd | 9,300 | 9,300 | 10,800 | 2,291 | 2,291 | 2,291 | Value in use |

The assets of the Midatech Pharma Wales Ltd ('MPW') CGU were valued as at 31 December 2018, 2017 and 2016 and were found to support the IPRD and goodwill carrying amounts set out above. The IPRD was valued using 12–13 year (2017: 13–14 year), risk adjusted cash flow forecasts, in line with patent life, that have been approved by the Board. A period longer than 5 years is appropriate on the basis that the investment is long term and the development and commercialisation process is typically in excess of 5 years. Beyond the period from product launch and initial market penetration, a long term growth rate of 2% was used.

In 2017 an impairment charge of £1.5m was recorded in the MPW CGU as a result of the impairment of the Opsisporin IPRD, primarily due to a strategic review concluding that the product is outside of Midatech's strategic focus and as a result the decision was made not to continue with the programme at this point. At the same time the carrying value of a component of IPRD was reduced from £1.5m to nil. The resulting charge was shown separately within the consolidated statement of income.

The key assumptions used in the valuation model examining the MPW Ltd cash generating unit include the following:

| Assumptions | 2018 | 2017 | 2016 |
|---|---|---|---|
| Pre-tax discount rate | 17.7% | 17.9% | 18.1% |
| Cumulative probability of success of projects | 81% | 81% | 46% to 81% |

The discount rate is an estimated market-based weighted average cost of capital for the MPW business, determined at the date of acquisition. Cumulative probability of success of projects is the product of the probability of success of each remaining major phase of development for each individual IPRD component. These phase probabilities were determined by management with reference to the risks associated with each remaining development stage.

**Sensitivity analysis**

If any one of the following changes were made to the above key assumptions, the carrying value and recoverable amount would be equal.

| Assumptions | 2018 | 2017 | 2016 |
|---|---|---|---|
| Pre-tax discount rate for all projects | increase to 29.8% | increase to 21.0% | increase to 26.4% |
| Cumulative probability of success of project | 34% | 57% | 53% |

## 13 Subsidiaries

The subsidiaries of Midatech Pharma plc, all of which are 100% owned, either directly or through subsidiaries where indicated, and have been included in these financial statements in accordance with the details set out in the basis of preparation and basis of consolidation note 1, are as follows:

| Name | Registered Office | Nature of Business | Notes |
|---|---|---|---|
| Midatech Limited | Oddfellows House, 19 Newport Road, Cardiff, CF24 0AA | Trading company | |
| Midatech Pharma (España) SL | Parque Tecnológico de Vizcaya, Edificio 800 Planta 2, Derio, 48160, Vizcaya, Spain | Trading company | (a) |
| PharMida AG | c/o Kellerhals, Hirschgässlein 11, 4051 Basel, Switzerland | Dormant | (a) (b) |
| Midatech Pharma (Wales) Limited | Oddfellows House, 19 Newport Road, Cardiff, CF24 0AA | Trading company | |
| Midatech Pharma PTY | c/o Griffith Hack Consulting, 300 Queen Street, Brisbane, QLD 4000, Australia | Trading company | (c) |

Notes:

(a) Wholly owned subsidiary of Midatech Limited.

(b) PharMida AG became dormant in January 2016.

(d) Midatech Pharma PTY was incorporated on 16 February 2015.

## 14 Trade and other receivables

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Trade receivables | 89 | 2,232 | 1,428 |
| Prepayments | 139 | 627 | 586 |
| Other receivables | 1,564 | 848 | 873 |
| **Total trade and other receivables** | 1,792 | 3,707 | 2,887 |
| Less: non-current portion (rental deposit and on bond) | (469) | (465) | (448) |
| Current portion | 1,323 | 3,242 | 2,439 |

Trade and other receivables do not contain any impaired assets. The Group does not hold any collateral as security and the maximum exposure to credit risk at the consolidated statement of financial position date is the fair value of each class of receivable.

Book values approximate to fair value at 31 December 2018, 2017 and 2016.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 15 Cash and cash equivalents and cash flow supporting notes

Cash and cash equivalents for purposes of the consolidated statement of cash flows comprises:

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Cash at bank available on demand | 2,343 | 13,204 | 17,608 |

There were no significant non-cash transactions during the year.

During 2017 and 2016, cash inflows arose from an equity financing transaction, included within financing activities on the face of the cash flow statement.

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Funds raised on Public Offering | – | 6,157 | 16,673 |
| Costs of raising funds on Public Offering | – | (429) | (1,105) |
| | – | 5,728 | 15,568 |

The following changes in bank loan liabilities arose as a result of financing activities during the year:

| | Non-current liabilities, bank loans £'000 | Current liabilities, bank loans £'000 | Total £'000 |
|---|---|---|---|
| **At 1 January 2018** | **5,207** | **11** | **5,218** |
| Cash flows | (5,494) | (7) | (5,501) |
| Foreign Exchange | 287 | | 287 |
| **At 31 December 2018** | **–** | **4** | **4** |

| | Non-current liabilities, bank loans £'000 | Current liabilities, bank loans £'000 | Total £'000 |
|---|---|---|---|
| **At 1 January 2017** | **–** | **23** | **23** |
| Cash Flows | 5,249 | (12) | 5,237 |
| Foreign Exchange | (42) | – | (42) |
| **At 31 December 2017** | **5,207** | **11** | **5,218** |

## 16 Inventories

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Finished goods | – | 941 | 817 |
| Total inventories | – | 941 | 817 |

There was no stock held at 31 December 2018. In 2017 a reserve was maintained against inventory that was not expected to be sold before its sell by date. The resulting charge to the discontinued element of the comprehensive statement of income in 2017 was £151k (2016: £287k).

## 17 Trade and other payables

| Current | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Trade payables | 286 | 2,271 | 3,268 |
| Other payables | – | 1,141 | 1,166 |
| Accruals | 1,025 | 3,090 | 2,003 |
| **Total financial liabilities, excluding loans and borrowings, classified as financial liabilities measured at amortised cost** | **1,311** | **6,502** | **6,437** |
| Tax and social security | 347 | 359 | 670 |
| Deferred revenue and government grants | 445 | 1,141 | 1,300 |
| **Total trade and other payables** | **2,103** | **8,002** | **8,407** |

Book values approximate to fair value at 31 December 2018, 2017 and 2016.

All current trade and other payables are payable within 3 months of the period end date shown above.

### Government grants

The Group received development grant funding from the European Union under the Horizon 2020 'Nanofacturing' project, a European Union funded programme to develop a scalable manufacturing platform for the production of nanopharmaceutical products. Midatech participated in this programme, along with seven other entities, through two Group companies, Midatech Pharma España SL ('MPE'), which acted as project coordinator, and Midatech Limited ('MTL'). The project commenced in February 2015 and completed in January 2019. £1,610k (2017: £840k, 2016: £547k) of revenue has been recognised during the year in relation to this project and £124k (2017: £1.11m, 2016: £1.24m) of the deferred revenue balance relates to funds received but not yet recognised.

### Government grants/loans in Spain

Five tranches of government loans have been received by Midatech Pharma España SL for the finance of research, technical innovation and the construction of their laboratory. The loans are term loans which carry an interest rate below the market rate, and are repayable over periods through to 2022. The loans carry default interest rates in the event of scheduled repayments not being met. On initial recognition, the loans are discounted at a market rate of interest with the credit being classified as a grant within deferred revenue. The deferred grant revenue is released to the consolidated statement of comprehensive income within research and development costs in the period to which the expenditure is recognised.

The debt element of the government loans is designated within note 18 as borrowings, the gross contractual repayment of the loans is disclosed in note 21.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 18 Borrowings

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| **Current** | | | |
| Bank loans | 4 | 11 | 23 |
| Finance lease | 80 | 39 | 31 |
| Government and research loans | 284 | 311 | 484 |
| **Total** | 368 | 361 | 538 |
| **Non-current** | | | |
| Bank loans | – | 5,207 | – |
| Finance lease | 170 | 29 | 52 |
| Government and research loans | 714 | 949 | 1,568 |
| **Total** | 884 | 6,185 | 1,620 |

Book values approximate to fair value at 31 December 2018, 2017 and 2016.

Obligations under finance leases are secured by a fixed charge over the fixed assets to which they relate.

### Midcap Loan Facility

In December 2017, Midatech Pharma entered into a secured loan agreement with Midcap Financial Trust (MidCap). The total facility was for $15m to be drawn down in three separate tranches. Interest was charged on the outstanding balance of the loan at an annual rate of LIBOR plus 7.5% subject to a LIBOR floor of 1.25%. MidCap was granted 247,881 warrants to purchase shares which was equal to 2% of the amount funded divided by the Exercise Price of £0.42. The Exercise Price was calculated as the average closing price for the 30-day period prior to the date of grant. The loan was secured against the assets of the Group.

The first tranche of $7m was drawn down on 28 December 2017 and is disclosed under bank loans. This loan was repaid on 31 October 2018.

## 19 Provisions

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Opening provision at 1 January | – | – | – |
| Provision recognised in the year | 165 | – | – |
| At 31 December | 165 | – | – |

The provision relates to the 'making good' clause on the Abingdon office which was vacated in December 2018. The office has been sub-let for the remaining period of the lease, which is due to terminate in February 2020.

## 20 Derivative financial liability – current

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Equity settled derivative financial liability | – | – | 400 |
| At 1 January/on acquisition – 5 December 2015 | – | 400 | 1,573 |
| Gain recognised in finance income within the consolidated statement of comprehensive income | – | (400) | (1,173) |
| At 31 December | – | – | 400 |

Equity settled derivative financial liability is a liability that is not to be settled for cash. The Group assumed fully vested warrants and share options on the acquisition of DARA Biosciences, Inc. The number of ordinary shares to be issued when exercised is fixed, however the exercise prices are denominated in US Dollars being different to the functional currency of the parent company. Therefore, the warrants and share options are classified as equity settled derivative financial liabilities recognised at fair value through the profit and loss account. The financial liabilities were valued using the Black-Scholes option pricing model. Financial liabilities at FVTPL are stated at fair value, with any gains or losses arising on re-measurement recognised in profit or loss. The net gain or loss recognised in profit or loss incorporated any interest paid on the financial liability and is included in the 'finance income' line item in the income statement. Fair value is determined in the manner described in note 21. A key input in the valuation of the instrument is the Company share price.

At 31 December 2016, some 398,315 options and 16,664 warrants had lapsed. In addition, the share price had fallen to £1.18, which resulted in a gain of £1.17m on re-measurement, which was credited to finance income in 2016.

At 31 December 2017 a further 166,058 options and 489,318 warrants had lapsed and the share price had fallen to £0.36 which results in a gain of £0.40m on re-measurement which was credited to finance income during 2017.

At 31 December 2018 a further 176,935 options and 776,889 warrants had lapsed and the share price had fallen to £0.06. As the liability had already been reduced to zero there was no movement on re-measurement.

## 21 Financial instruments – risk management

The Group is exposed through its operations to the following financial risks:

- Credit risk
- Foreign exchange risk
- Liquidity risk

In common with all other businesses, the Group is exposed to risks that arise from its use of financial instruments. This note describes the Group's objectives, policies and processes for managing those risks and the methods used to measure them. The Board does not believe that its risk exposure to financial instruments, its objectives, policies and processes for managing those risks or the methods used to measure them from previous periods unless otherwise stated in this note has changed in the past year.

### Principal financial instruments

The principal financial instruments used by the Group, from which financial instrument risk arises, are as follows:

- Trade and other receivables
- Cash and cash equivalents
- Trade and other payables
- Accruals
- Loans and borrowings
- Derivative financial liability

A summary of the financial instruments held by category is provided below:

### Financial assets – amortised cost

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Cash and cash equivalents | 2,343 | 13,204 | 17,608 |
| Trade receivables | 89 | 2,232 | 1,428 |
| **Total financial assets** | 2,432 | 15,436 | 19,036 |

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 21 Financial instruments – risk management continued

### Financial liabilities – amortised cost

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Trade payables | 286 | 2,271 | 3,268 |
| Other payables | – | 1,141 | 1,166 |
| Accruals | 1,025 | 3,090 | 2,003 |
| Borrowings | 1,252 | 6,546 | 2,158 |
| **Total financial liabilities - amortised cost** | 2,563 | 13,048 | 8,595 |

### Financial liabilities – fair value through profit and loss – current

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Equity settled derivative financial liability | – | – | 400 |

#### General objectives, policies and processes

The Board has overall responsibility for the determination of the Group's risk management objectives and policies and, whilst retaining ultimate responsibility for them, it has delegated the authority for designing and operating processes that ensure the effective implementation of the objectives and policies to the Group's management.

The overall objective of the Board is to set policies that seek to reduce risk as far as possible without unduly affecting the Group's competitiveness and flexibility. Further details regarding these policies are set out below:

Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets and liabilities;
- Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs that have a significant effect on the recorded fair value that are not based on observable market data.

The fair value of the Group's derivative financial liability is measured at fair value on a recurring basis. The following table gives information about how the fair value of this financial liability is determined, additional disclosure is given in note 20:

| Financial liabilities | Fair value as at 31/12/2018 | Fair value hierarchy | Valuation technique(s) and key input(s) | Significant unobservable input(s) | Relationship of unobservable inputs to fair value |
|---|---|---|---|---|---|
| Equity settled financial derivative liability | – | Level 3 | Black-Scholes option pricing model | Volatility rate of 42.5% determined using historical volatility of comparable companies. | The higher the volatility the higher the fair value. |
| | | | | Expected life between a range of 0.1 and 7.6 years determined using the remaining life of the share options. | The shorter the expected life the lower the fair value. |
| | | | | Risk-free rate between a range of 0.0% and 1.14% determined using the expected life assumptions. | The higher the risk-free rate the higher the fair value. |

| Financial liabilities | Fair value as at 31/12/2017 | Fair value hierarchy | Valuation technique (s) and key input(s) | Significant unobservable input(s) | Relationship of unobservable inputs to fair value |
|---|---|---|---|---|---|
| Equity settled financial derivative liability | – | Level 3 | Black-Scholes option pricing model | Volatility rate of 42.5% determined using historical volatility of comparable companies. | The higher the volatility the higher the fair value. |
| | | | | Expected life between a range of 0.1 and 8.6 years determined using the remaining life of the share options. | The shorter the expected life the lower the fair value. |
| | | | | Risk-free rate between a range of 0.0% and 1.14% determined using the expected life assumptions. | The higher the risk-free rate the higher the fair value. |

Given that the fair value of the equity settled financial derivative liability is nil, it is not sensitive to changes in volatility or expected life. In 2016, if the above unobservable volatility input to the valuation model had been 10% higher while all other variables were held constant, the carrying amount of shares would have increased by £94k. If the above unobservable expected life input to the valuation model had been 1 year shorter while all other variables were held constant, the carrying amount of shares would have decreased by £133k.

Changing the unobservable risk free rate input to the valuation model by 10% higher while all other variables were held constant, would not impact the carrying amount of shares (2017: nil, 2016: increase by £2k).

There were no transfers between Level 1 and 2 in the period.

The financial liability measured at fair value on Level 3 fair value measurement represents consideration relating to a business combination.

### Credit risk

Credit risk is the risk of financial loss to the Group if a development partner or a counterparty to a financial instrument fails to meet its contractual obligations. The Group is mainly exposed to credit risk from amounts due from collaborative partners which is deemed to be low.

Credit risk also arises from cash and cash equivalents and deposits with banks and financial institutions. For banks and financial institutions, only independently rated parties with high credit status are accepted.

The Group does not enter into derivatives to manage credit risk.

The consolidated entity recognises a loss allowance for expected credit losses on financial assets which are either measured at amortised cost or fair value through other comprehensive income. The measurement of the loss allowance depends upon the consolidated entity's assessment at the end of each reporting period as to whether the financial instrument's credit risk has increased significantly since initial recognition, based on reasonable and supportable information that is available, without undue cost or effort to obtain.

Where there has not been a significant increase in exposure to credit risk since initial recognition, a 12-month expected credit loss allowance is estimated. This represents a portion of the asset's lifetime expected credit losses that is attributable to a default event that is possible within the next 12 months. Where a financial asset has become credit impaired or where it is determined that credit risk has increased significantly, the loss allowance is based on the asset's lifetime expected credit losses. The amount of expected credit loss recognised is measured on the basis of the probability weighted present value of anticipated cash shortfalls over the life of the instrument discounted at the original effective interest rate. For financial assets measured at fair value through other comprehensive income, the loss allowance is recognised within other comprehensive income. In all other cases, the loss allowance is recognised in profit or loss.

Quantitative disclosures of the credit risk exposure in relation to financial assets are set out in note 14. This includes details regarding trade and other receivables, which are neither past due nor impaired.

The total exposure to credit risk of the Group is equal to the total value of the financial assets held at each year end as noted above.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 21 Financial instruments – risk management continued

### Cash in bank

The Group is continually reviewing the credit risk associated with holding money on deposit in banks and seeks to mitigate this risk by holding deposits with banks with high credit status.

### Foreign exchange risk

Foreign exchange risk arises because the Group has a material operation located in Bilbao, Spain, and had operations in the US whose functional currencies are not the same as the functional currency of the Group. The Group's net assets arising from such overseas operations are exposed to currency risk resulting in gains or losses on retranslation into sterling. Given the levels of materiality, the Group does not hedge its net investments in overseas operations as the cost of doing so is disproportionate to the exposure.

Foreign exchange risk also arises when individual Group entities enter into transactions denominated in a currency other than their functional currency; the Group's transactions outside the UK to the US, Europe and Australia drive foreign exchange movements where suppliers invoice in currency other than sterling. These transactions are not hedged because the cost of doing so is disproportionate to the risk.

The table below shows analysis of the Pounds Sterling equivalent of year-end cash and cash equivalent balances by currency:

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Cash and cash equivalents: | | | |
| Pounds Sterling | 457 | 6,116 | 10,229 |
| US Dollar | 1,421 | 5,362 | 2,186 |
| Euro | 459 | 1,632 | 5,143 |
| Other | 6 | 94 | 50 |
| **Total** | 2,343 | 13,204 | 17,608 |

The table below shows the foreign currency exposure that gives rise to net currency gains and losses recognised in the consolidated statement of comprehensive income. Such exposures comprise the net monetary assets and monetary liabilities of the Group that are not denominated in the functional currency of the relevant Group entity. As at 31 December 2018, these exposures were as follows:

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Net Foreign Currency Assets/(Liabilities): | | | |
| US Dollar | 1,421 | 4,459 | (206) |
| Euro | 552 | (362) | 2,655 |
| Other | 8 | 95 | 58 |
| **Total** | 1,981 | 4,192 | 2,507 |

### Foreign currency sensitivity analysis

The most significant currencies in which the Group transacts, other than Pounds Sterling, are the US Dollar and the Euro. The Group also trades in other currencies in small amounts as necessary.

The following table details the Group's sensitivity to a 10% change in year-end exchange rates, which the Group feels is the maximum likely change in rate based upon recent currency movements, in the key foreign currency exchange rates against Pounds Sterling:

| Year ended 31 December 2018 | US Dollar £'000 | Euro £'000 | Other £'000 |
|---|---|---|---|
| Loss before tax | – | 168 | – |
| Total equity | 142 | 168 | – |

| Year ended 31 December 2017 | US Dollar £'000 | Euro £'000 | Other £'000 |
|---|---|---|---|
| Loss before tax | 307 | (89) | – |
| Total equity | 307 | (89) | – |

| Year ended 31 December 2016 | US Dollar £'000 | Euro £'000 | Other £'000 |
|---|---|---|---|
| Loss before tax | 521 | (73) | (55) |
| Total equity | 521 | (73) | (55) |

The sale of the Midatech Pharma US, Inc. operation prior to 31 December 2018 resulted in there not being any US Dollar denominated assets or liabilities to report on at year end other than a US Dollar cash balance held by Midatech Pharma PLC. In management's opinion, the sensitivity analysis is unrepresentative of the inherent foreign exchange risk as the year-end exposure does not reflect the exposure during the year.

### Liquidity risk

Liquidity risk arises from the Group's management of working capital. It is the risk that the Group will encounter difficulty in meeting its financial obligations as they fall due. It is the Group's aim to settle balances as they become due.

In Q1 2019, the Company completed a Subscription, Placing and Open Offer which raised £13.4m before costs. The Group's current financial position is such therefore, that the Board does not consider there to be a short term liquidity risk. However, the Board will continue to monitor long term cash projections in light of the development plan and will consider raising funds as required to fund long term development projects. Development expenditure can be curtailed as necessary to preserve liquidity.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 21 Financial instruments – risk management continued

The following table sets out the contractual maturities (representing undiscounted contractual cash-flows) of financial liabilities:

| 2018 | Up to 3 months £'000 | Between 3 and 12 months £'000 | Between 1 and 2 years £'000 | Between 2 and 5 years £'000 | Over 5 years £'000 |
|---|---|---|---|---|---|
| Trade and other payables | 1,311 | – | – | – | – |
| Bank loans | 3 | 2 | – | – | – |
| Finance leases | 22 | 65 | 79 | 117 | – |
| Government research loans | 44 | 240 | 406 | 414 | – |
| **Total** | 1,380 | 307 | 485 | 531 | – |

| 2017 | Up to 3 months £'000 | Between 3 and 12 months £'000 | Between 1 and 2 years £'000 | Between 2 and 5 years £'000 | Over 5 years £'000 |
|---|---|---|---|---|---|
| Trade and other payables | 6,502 | – | – | – | – |
| Bank loans | 120 | 359 | 2,201 | 3,926 | – |
| Finance leases | 16 | 25 | 30 | – | – |
| Government research loans | 43 | 268 | 467 | 545 | 47 |
| **Total** | 6,681 | 649 | 2,698 | 4,471 | 47 |

| 2016 | Up to 3 months £'000 | Between 3 and 12 months £'000 | Between 1 and 2 years £'000 | Between 2 and 5 years £'000 | Over 5 years £'000 |
|---|---|---|---|---|---|
| Trade and other payables | 6,437 | – | – | – | – |
| Bank loans | 3 | 8 | 11 | 4 | – |
| Finance leases | 7 | 26 | 30 | 33 | – |
| Government research loans | – | 449 | 269 | 761 | 393 |
| **Total** | 6,447 | 483 | 310 | 798 | 393 |

More details with regard to the line items above are included in the respective notes:

- Trade and other payables – note 17
- Loans and borrowings – note 28

### Capital risk management

The Group monitors capital which comprises all components of equity (i.e. share capital, share premium, foreign exchange reserve and accumulated deficit).

The Group's objectives when maintaining capital are:

- to safeguard the entity's ability to continue as a going concern; and
- to have sufficient resource to take development projects forward towards commercialisation.

The Group continues to incur substantial operating expenses. Until the Group generates positive net cash inflows from the commercialisation of its products it remains dependent upon additional funding through the injection of equity capital and government funding. The Group may not be able to generate positive net cash inflows in the future or to attract such additional required funding at all, or on suitable terms. In such circumstances the development programmes may be delayed or cancelled and business operations cut back.

The Group seeks to reduce this risk by keeping a tight control on expenditure, avoiding long term supplier contracts (other than clinical trials), prioritising development spend on products closest to potential revenue generation, obtaining government grants (where applicable), maintaining a focussed portfolio of products under development and keeping shareholders informed of progress.

There have been no changes to the Group's objectives, policies and processes for managing capital and what the Group manages as capital, unless otherwise stated in this note, since the previous year.

## 22 Deferred tax

Deferred tax is calculated in full on temporary differences under the liability method using tax rates applicable in the tax jurisdictions where the tax asset or liability would arise.

The movement on the deferred tax account is as shown below:

| | 2018 £'000 | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| Liability at 1 January | – | – | 6,547 |
| Arising on business combination | – | – | – |
| Credited to income on impairment and amortisation of intangibles | – | – | (5,509) |
| Credited to income statement | – | – | (1,740) |
| Foreign exchange gain | – | – | 702 |
| Liability at 31 December | – | – | – |

The movement on the deferred tax account in 2018 is nil (2017: nil, 2016: nil) as the net credit arising on the amortisation of intangible assets and other timing differences has been matched by a reduction in the deferred tax asset recognised on the losses offsetting the liability remaining.

A deferred tax liability arose due to deferred tax on intangible assets acquired in 2015.

An intangible asset was impaired in the financial statements for the year ended 31 December 2016 by £11.4m which resulted in a £4.6m tax credit being recognised in the income statement.

Unused tax losses carried forward, subject to agreement with local tax authorities, were as follows:

| | Gross losses £'000 | Potential deferred tax asset £'000 |
|---|---|---|
| **31 December 2018** | **40,741** | **6,926** |
| 31 December 2017 | 38,377 | 6,639 |
| 31 December 2016 | 26,956 | 5,049 |

With the exception of the £1.7m (2017: £2.6m, 2016: £3.7m) deferred tax asset which qualifies for offset against the deferred tax liabilities arising on the acquisitions of Midatech Pharma (Wales) Limited, the remaining potential deferred tax asset of £7.3m (2017 £9.5m, 2016: £8.1m) has not been provided in these accounts due to uncertainty as to whether the asset would be recovered.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 22 Deferred tax continued

Details of the deferred tax liability are as follows:

| 2018 | Asset £'000 | Liability £'000 | Net £'000 |
|---|---|---|---|
| Business Combinations | **1,690** | **(1,690)** | **–** |

| 2017 | Asset £'000 | Liability £'000 | Net £'000 |
|---|---|---|---|
| Business Combinations | 2,599 | (2,599) | – |

| 2016 | Asset £'000 | Liability £'000 | Net £'000 |
|---|---|---|---|
| Business Combinations | 3,668 | (3,668) | – |

## 23 Share capital

| Authorised, allotted and fully paid – classified as equity | 2018 Number | 2018 £ | 2017 Number | 2017 £ | 2016 Number | 2016 £ |
|---|---|---|---|---|---|---|
| At 1 January | | | | | | |
| Ordinary shares of £0.00005 each | 61,184,135 | 3,059 | 61,084,135 | 3,054 | 48,699,456 | 2,435 |
| Deferred shares of £1 each | 1,000,001 | 1,000,001 | 1,000,001 | 1,000,001 | 1,000,001 | 1,000,001 |
| **Total** | | **1,003,060** | | **1,003,055** | | **1,002,436** |

In accordance with the Articles of Association for the Company adopted on 13 November 2014, the share capital of the Company consists of an unlimited number of ordinary shares of nominal value 0.005 pence each. Ordinary and deferred shares were recorded as equity.

### Rights attaching to the shares following the incorporation of Midatech Pharma plc

#### Shares classified as equity

The holders of ordinary shares in the capital of the Company have the following rights:

(a) to receive notice of, to attend and to vote at all general meetings of the Company, in which case shareholders shall have one vote for each share of which he is the holder; and,

(b) to receive such dividend as is declared by the Board on each share held.

The holders of deferred shares in the capital of the Company:

(a) shall not be entitled to receive notice of or to attend or speak at any general meeting of the Company or to vote on any resolution to be proposed at any general meeting of the Company;

(b) shall not be entitled to receive any dividend or other distribution of out of the profits of the Company.

In the event of a distribution of assets, the deferred shareholders shall receive the nominal amount paid up on such share after the holder of each ordinary share shall have received (in cash or specie) the amount paid up or credited as paid up on such ordinary share together with an additional payment of £100 per share. The Company has the authority to purchase the deferred shares and may require the holder of the deferred shares to sell them for a price not exceeding 1p for all the deferred shares.

| | | Ordinary Shares Number | Deferred Shares Number | Share Price £ | Total consideration £'000 |
|---|---|---|---|---|---|
| **As at 1 January 2016** | | **33,467,504** | **1,000,001** | | **46,840** |
| **2016** | | | | | |
| 1 July 2016 | Deferred consideration re: acquisition of Q Chip Limited | 74,908 | – | 2.67 | 200 |
| 31 October 2016 | Placing and Open Offer (see note 15) | 15,157,044 | – | 1.10 | 16,673 |
| **As at 31 December 2016** | | **48,699,456** | **1,000,001** | | **63,713** |
| **2017** | | | | | |
| 19 May 2017 | Share issue to SIPP trustee (see note 27) | 20,000 | – | 0.00005 | – |
| 16 October 2017 | Placing and Open Offer (see note 15) | 12,314,679 | – | 0.5 | 6,157 |
| 7 November 2017 | Share issue to SIPP trustee (see note 27) | 50,000 | – | 0.00005 | – |
| **As at 31 December 2017** | | **61,084,135** | **1,000,001** | | **69,870** |
| **2018** | | | | | |
| 1 August 2018 | Share issue to SIPP trustee (see note 27) | 100,000 | – | 0.00005 | – |
| **As at 31 December 2018** | | **61,184,135** | **1,000,001** | | **69,870** |

## 24 Reserves

The following describes the nature and purpose of each reserve within equity:

| Reserve | Description and purpose |
|---|---|
| Share premium | Amount subscribed for share capital in excess of nominal value. |
| Merger reserve | Represents the difference between the fair value and nominal value of shares issued on the acquisition of subsidiary companies where the Company has elected to take advantage of merger relief. |
| Shares to be issued | Shares for which consideration has been received but which are not yet issued and which form part of consideration in a business combination. |
| Foreign exchange reserve | Gains/losses arising on retranslating the net assets of overseas operations into sterling. |
| Accumulated deficit | All other net gains and losses and transactions with owners (e.g. dividends) not recognised elsewhere. |

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 25 Leases

The Group had commitments under non-cancellable operating leases as set out below:

| 2018 | Land and buildings £'000 | Other £'000 |
|---|---|---|
| Expiring In one year or less | 383 | 1 |
| Expiring Between one and five years | 189 | 4 |
| | 572 | 5 |

| 2017 | Land and buildings £'000 | Other £'000 |
|---|---|---|
| Expiring In one year or less | 449 | 8 |
| Expiring Between one and five years | 359 | 32 |
| | 808 | 40 |

| 2016 | £'000 | Other £'000 |
|---|---|---|
| Expiring In one year or less | 371 | 7 |
| Expiring Between one and five years | 449 | 28 |
| | 820 | 35 |

A sub lease has been granted on the remaining term of the property lease for the Abingdon office amounting to £156,895.

## 26 Retirement benefits

The Group operates a defined contribution pension scheme for the benefit of its employees. The assets of the scheme are administered by trustees in funds independent from those of the Group.

## 27 Share-based payments

### Share Options

The Group has issued options over ordinary shares under the 2014 Midatech Pharma plc Enterprise Management Incentive Scheme, the Midatech Pharma plc 2016 U.S. Option Plan, which is a sub-plan of the approved UK plan, and unapproved share options awarded to non-UK or non-US staff. In addition, certain share options originally issued over shares in Midatech Limited under the Midatech Limited 2008 unapproved share option scheme or Midatech Limited 2013 approved Enterprise Incentive scheme were reissued in 2015 over shares in Midatech Pharma plc under the 2014 Midatech Pharma plc Enterprise Management Incentive Scheme. Exercise of an option is subject to continued employment.

Details of all share options granted under the Schemes are set out below:

| Date of grant | At 1 January 2018 | Granted in 2018 | Exercised in 2018 | Forfeited in 2018 | At 31 December 2018 | Exercise Price |
|---|---|---|---|---|---|---|
| 31 December 2008 | 26,122 | – | – | 26,122 | – | £1.425 |
| 31 December 2008 | 3,000 | – | – | 3,000 | – | £3.985 |
| 1 April 2010 | 25,110 | – | – | – | 25,110 | £4.00 |
| 20 August 2010 | 41,766 | – | – | | 41,766 | £4.19 |
| 13 September 2011 | 3,000 | – | – | – | 3,000 | £4.19 |
| 20 April 2012 | 35,796 | – | – | 4,000 | 31,796 | £4.19 |
| 9 May 2014 | 200,000 | – | – | – | 200,000 | £0.075 |
| 30 June 2014 | 880,000 | – | – | 450,000 | 430,000 | £0.075 |
| 11 July 2014 | 2,000 | – | – | – | 2,000 | £0.075 |
| 31 October 2016 | 50,000 | – | – | – | 50,000 | £1.710 |
| 31 October 2016 | 607,600 | – | – | 139,375 | 468,225 | £2.680 |
| 14 December 2016 | 8,000 | – | – | – | 8,000 | £1.550 |
| 14 December 2016 | 10,000 | – | – | – | 10,000 | £1.700 |
| 14 December 2016 | 40,000 | – | – | – | 40,000 | £1.870 |
| 14 December 2016 | 40,000 | – | – | 7,500 | 32,500 | £1.880 |
| 15 December 2016 | 102,000 | – | – | 10,000 | 92,000 | £1.210 |
| 19 December 2016 | 1,104,250 | – | – | 386,875 | 717,375 | £1.210 |
| 15 December 2017 | 1,351,250 | – | – | 433,500 | 917,750 | £0.46 |
| 2 April 2018 | – | 20,000 | – | – | 20,000 | £0.83 |
| 2 April 2018 | – | 90,000 | – | – | 90,000 | £1.21 |
| | **4,529,894** | **110,000** | **–** | **(1,460,372)** | **3,179,522** | |

| | |
|---|---|
| Options exercisable at 31 December 2018 | 2,247,869 |
| Weighted average exercise price of outstanding options at 31 December 2018 | £1.101 |
| Weighted average exercise price of options exercised in 2018 | n/a |
| Weighted average exercise price of options forfeited in 2018 | £0.799 |
| Weighted average exercise price of options granted in 2018 | £0.830 |
| Weighted average remaining contractual life of outstanding options at 31 December 2018 | 5.7 years |

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 27 Share-based payments continued

| Date of grant | At 1 January 2017 | Granted in 2017 | Exercised in 2017 | Forfeited in 2017 | At 31 December 2017 | Exercise Price |
|---|---|---|---|---|---|---|
| 31 December 2008 | 26,122 | – | – | – | 26,122 | £1.425 |
| 31 December 2008 | 3,000 | – | – | – | 3,000 | £3.985 |
| 1 April 2010 | 25,110 | – | – | – | 25,110 | £4.00 |
| 20 August 2010 | 41,766 | – | – | | 41,766 | £4.19 |
| 13 September 2011 | 3,000 | – | – | – | 3,000 | £4.19 |
| 20 April 2012 | 35,796 | – | – | – | 35,796 | £4.19 |
| 9 May 2014 | 200,000 | – | – | – | 200,000 | £0.075 |
| 30 June 2014 | 880,000 | – | – | – | 880,000 | £0.075 |
| 11 July 2014 | 3,000 | – | – | 1,000 | 2,000 | £0.075 |
| 31 October 2016 | 50,000 | – | – | – | 50,000 | £1.710 |
| 31 October 2016 | 607,600 | – | – | – | 607,600 | £2.680 |
| 14 December 2016 | 8,000 | – | – | – | 8,000 | £1.550 |
| 14 December 2016 | 10,000 | – | – | – | 10,000 | £1.700 |
| 14 December 2016 | 3,000 | – | – | 3,000 | – | £1.710 |
| 14 December 2016 | 3,000 | – | – | 3,000 | – | £1.730 |
| 14 December 2016 | 3,000 | – | – | 3,000 | – | £1.740 |
| 14 December 2016 | 40,000 | – | – | – | 40,000 | £1.870 |
| 14 December 2016 | 40,000 | – | – | – | 40,000 | £1.880 |
| 15 December 2016 | 197,000 | – | – | 95,000 | 102,000 | £1.210 |
| 19 December 2016 | 1,110,000 | – | – | 5,750 | 1,104,250 | £1.210 |
| 15 December 2017 | – | 1,351,250 | – | – | 1,351,250 | £0.46 |
| | **3,289,394** | **1,351,250** | **–** | **(110,750)** | **4,529,894** | |

| | |
|---|---|
| Options exercisable at 31 December 2017 | 1,000,469 |
| Weighted average exercise price of outstanding options at 31 December 2017 | £1.003 |
| Weighted average exercise price of options exercised in 2017 | n/a |
| Weighted average exercise price of options forfeited in 2017 | £1.242 |
| Weighted average exercise price of options granted in 2017 | £0.46 |
| Weighted average remaining contractual life of outstanding options at 31 December 2017 | 8.3 years |

| Date of grant | At 1 January 2016 | Granted in 2016 | Exercised in 2016 | Forfeited in 2016 | At 31 December 2016 | Exercise Price |
|---|---|---|---|---|---|---|
| 31 December 2008 | 26,122 | – | – | – | 26,122 | £1.425 |
| 31 December 2008 | 15,500 | – | – | (12,500) | 3,000 | £3.985 |
| 1 April 2010 | 25,110 | – | – | – | 25,110 | £4.00 |
| 20 August 2010 | 41,766 | – | – | | 41,766 | £4.19 |
| 13 September 2011 | 3,000 | – | – | – | 3,000 | £4.19 |
| 20 April 2012 | 35,796 | – | – | – | 35,796 | £4.19 |
| 9 May 2014 | 200,000 | – | – | – | 200,000 | £0.075 |
| 30 June 2014 | 880,000 | – | – | – | 880,000 | £0.075 |
| 11 July 2014 | 5,000 | – | – | (2,000) | 3,000 | £0.075 |
| 31 October 2016 | – | 50,000 | – | – | 50,000 | £1.710 |
| 31 October 2016 | – | 607,600 | – | – | 607,600 | £2.680 |
| 14 December 2016 | – | 8,000 | – | – | 8,000 | £1.550 |
| 14 December 2016 | – | 10,000 | – | – | 10,000 | £1.700 |
| 14 December 2016 | – | 3,000 | – | – | 3,000 | £1.710 |
| 14 December 2016 | – | 3,000 | – | – | 3,000 | £1.730 |
| 14 December 2016 | – | 3,000 | – | – | 3,000 | £1.740 |
| 14 December 2016 | – | 40,000 | – | – | 40,000 | £1.870 |
| 14 December 2016 | – | 40,000 | – | – | 40,000 | £1.880 |
| 15 December 2016 | – | 197,000 | – | – | 197,000 | £1.210 |
| 19 December 2016 | | 1,110,000 | – | – | 1,110,000 | £1.210 |
| | **1,232,294** | **2,071,600** | **–** | **(14,500)** | **3,289,394** | |

| | |
|---|---|
| Options exercisable at 31 December 2016 | 468,194 |
| Weighted average exercise price of outstanding options at 31 December 2016 | £1.234 |
| Weighted average exercise price of options exercised in 2016 | n/a |
| Weighted average exercise price of options forfeited in 2016 | £3.446 |
| Weighted average exercise price of options granted in 2016 | £1.685 |
| Weighted average remaining contractual life of outstanding options at 31 December 2016 | 8.6 years |

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 27 Share-based payments continued

The following information is relevant in the determination of the fair value of options granted during the year 2018 under the equity share based remuneration schemes operated by the Group.

| | 2018 |
|---|---|
| Number of options | 110,000 |
| Option pricing models used | Monte-Carlo |
| Share price | £0.27* |
| Exercise price of options issued in year | £0.83–£1.21 |
| Contractual life | 10 years |
| Expected life | 5 years |
| Volatility | 45.2%** |
| Expected dividend yield | 0% |
| Risk free rate | 1.03% |

* The share price used in the determination of the fair value of the options granted in 2018 was the share price on the date of grant.

** Volatility was calculated with reference to the historic share price volatility of comparable companies measured over a five-year period.

The following information is relevant in the determination of the fair value of options granted during the year 2017 under the equity share based remuneration schemes operated by the Group.

| | 2017 |
|---|---|
| Number of options | 1,351,250 |
| Option pricing models used | Monte-Carlo |
| Share price | £0.41* |
| Exercise price of options issued in year | £0.46 |
| Contractual life | 10 years |
| Expected life | 5 years |
| Volatility | 42.5%** |
| Expected dividend yield | 0% |
| Risk free rate | 0.73% |

* The share price used in the determination of the fair value of the options granted in 2017 was the share price on the date of grant.

** Volatility was calculated with reference to the historic share price volatility of comparable companies measured over a five-year period.

The following information is relevant in the determination of the fair value of options granted during the year 2016 under the equity share based remuneration schemes operated by the Group.

| | 2016 |
|---|---|
| Number of options | 2,071,600 |
| Option pricing models used | Black-Scholes |
| Share price | £1.143–£1.19* |
| Exercise price of options issued in year | £1.21–£2.68 |
| Contractual life | 10 years |
| Expected life | 5 years |
| Volatility | 40%** |
| Expected dividend yield | 0% |
| Risk free rate | 0.63%–0.74% |

* The share price used in the determination of the fair value of the options granted in 2016 was the average of the opening and closing share prices on the date of grant.

** Volatility was calculated with reference to the historic share price volatility of comparable companies measured over a five-year period.

All other share options relate to the Midatech Limited 2008 unapproved share option scheme.

### Share Incentive Plan

In April 2017 the Group set up the Midatech Pharma Share Incentive Plan (MPSIP). Under the MPSIP, Group employees and Directors can acquire ordinary shares in the Company via a salary sacrifice arrangement. Midatech grants matching shares for every share bought. In order to retain these shares, scheme participants must remain employed by the Group for three years from the date of acquisition. All shares purchased by the MPSIP are held by an Employee Benefit Trust that is not under the control of Midatech. Shares must be left in the plan for 5 years to qualify for full income tax and NIC relief.

## 28 Capital commitments

The Group had no capital commitments at 31 December 2018, 31 December 2017 and 31 December 2016.

## 29 Related party transactions

Details of Directors' remuneration are given in the Directors Remuneration Report on page 39 and in note 6.

### Transactions with Monosol RX, LLC

The Directors considered Monosol RX, LLC ('Monosol') to be a related party up to 2 May 2016 by virtue of the fact that Monosol was a shareholder of the Company and a collaborative partner in the MidaSol Therapeutics joint operation. Monosol was also the licensor of the Company's Zuplenz® product. In this capacity, the Group incurred royalty costs, payable to Monosol of £188k, up to the date at which it ceased to be a related party in 2016.

### Transactions with Preci-Health

The Directors consider Preci-Health SA ('Preci-Health) to be a related party up to 31 May 2018 by virtue of the fact that there was a common Director with the Company up to that point in time.

During the year there were no transactions with Preci-Health. During 2017, £44k was invoiced to Preci-Health for research services and credited to revenue. There were no transactions with Preci-Health in 2016.

The Group has not made any allowances for bad or doubtful debts in respect of related party debtors nor has any guarantee been given or received during 2018, 2017 or 2016 regarding related party transactions.

## 30 Contingent liabilities

The Group had no contingent liabilities at 31 December 2018, 31 December 2017 and 31 December 2016.

## 31 Ultimate controlling party

The Directors do not consider that there was an ultimate controlling party at 31 December 2018.

Following the year end, China Medical Systems Holdings Limited and A&B (HK) Company Ltd (collectively, 'CMS'), companies under common control, invested a total of £8m in return for 207,792,206 new ordinary shares, which following admission on 26 February 2019, represents 51% of the issued share capital of the Company (See note 32). Based upon this, CMS is able to exert control over Midatech.

At date of approval of the financial statements, the ultimate controlling party is deemed to be Dr Lam Kong by virtue of the control he has over CMS.

# NOTES FORMING PART OF THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 32 Post balance sheet event

On 29 January 2019, the Company announced that it had signed a licence agreement with China Medical System Holdings Limited ('CMS') for the development and commercialisation of the Group's pipeline of products in Greater China and certain South East Asian Countries. Once the Group's development products are approved in certain territories, including the US or EU, under the terms of this agreement, Midatech intends to manufacture and supply its products to CMS. CMS will be responsible for funding the development and commercialisation of the Group's product in the territories covered by the licence. Subject to certain milestones being achieved, the Company will be eligible to receive regulatory and sales-based milestone payments as well as royalty payments.

The Company also announced that, in parallel with the licence agreement, CMS intended to invest £8m by way of a Subscription for new shares. Under the terms of this Subscription, for each new share issued, CMS would also receive one warrant over one additional share with an exercise price of 50 pence per share.

On 4 February 2019, the Company announced that, following a Placing of 'Units' with new and existing institutional investors, a further £4.65m had been raised, before expenses. Each Unit comprises one ordinary share and one warrant on the same terms as the CMS subscription. Following the results of the Placing, the Company launched an Open Offer to existing shareholders to subscribe for Units to raise additional gross proceeds of up to £0.75m.

At a general meeting of the Company's shareholders held on 26 February 2019, the Subscription, Placing and Open Offer were approved. As a result, the Company raised a total of £13.4m or £12.5m after expenses. Shareholders also voted to approve the Panel Waiver granted by the Takeover Panel in respect of the obligation by CMS (acting with a Concert Party) to make a mandatory general offer pursuant to Rule 9 of the Takeover Code. Following the general meeting, CMS held 51% of the issued share capital of the Company.

Following the general meeting, 348,215,478 new ordinary shares were issued to the subscribers in the Subscription, Placing and Open Offer and the new shares were admitted to AIM on 26 February 2019.

# COMPANY BALANCE SHEET

At 31 December 2018

| Company number 09216368 | Note | 2018 £'000 | 2018 £'000 | 2017 £'000 | 2017 £'000 |
|---|---|---|---|---|---|
| **Fixed assets** | | | | | |
| Intangible assets | 4 | | – | | 2,153 |
| Investments | 5 | | 1,001 | | 7,405 |
| Property, Plant & Equipment | 6 | | 85 | | 230 |
| | | | 1,086 | | 9,788 |
| **Current assets** | | | | | |
| Debtors | 7 | 16,931 | | 34,706 | |
| Cash at bank | | 1,508 | | 5,865 | |
| | | 18,439 | | 40,571 | |
| **Creditors: amounts due falling due within one year** | 8 | (621) | | (1,075) | |
| **Net current assets** | | | **17,818** | | **39,496** |
| **Total assets less current liabilities** | | | 18,904 | | 49,284 |
| **Creditors: amounts due falling after one year** | 9 | | (165) | | (5,207) |
| **Net assets** | | | **18,739** | | **44,077** |
| **Capital and reserves** | | | | | |
| Called up share capital | 10 | | 1,003 | | 1,003 |
| Share premium account | 14 | | 52,939 | | 52,939 |
| Accumulated deficit | 14 | | (35,203) | | (9,865) |
| **Total equity attributable to owners of the parent company** | | | **18,739** | | **44,077** |

The loss for the financial period, of the Company, as approved by the Board, was £24.99m (2017: £4.83m, 2016: £3.34m).

The financial statements were approved and authorised for issue by the Board of Directors on 23 April 2019 and were signed on its behalf by:

**Nick Robbins-Cherry**
Chief Financial Officer

The notes on pages 103 to 108 form part of these financial statements.

# COMPANY STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2018

| | Share capital £'000 | Share Premium £'000 | Accumulated deficit £'000 | Total equity £'000 |
|---|---|---|---|---|
| **At 1 January 2018** | **1,003** | **52,939** | **(9,865)** | **44,077** |
| Loss for the year | – | – | (24,989) | (24,989) |
| **Total comprehensive loss** | **1,003** | **52,939** | **(34,854)** | **19,088** |
| **Transactions with owners** | | | | |
| Share option charge | – | – | (349) | (349) |
| **Total contribution by and distributions to owners** | – | – | (349) | (349) |
| **At 31 December 2018** | **1,003** | **52,939** | **(35,203)** | **18,739** |

| | Share capital £'000 | Share Premium £'000 | Accumulated deficit £'000 | Total equity £'000 |
|---|---|---|---|---|
| **At 1 January 2017** | **1,002** | **47,211** | **(5,407)** | **42,806** |
| Loss for the year | – | – | (4,831) | (4,831) |
| **Total comprehensive loss** | **1,002** | **47,211** | **(10,238)** | **37,975** |
| **Transactions with owners** | | | | |
| Shares issued (net of issue costs) | 1 | 5,728 | – | 5,729 |
| Share option charge | – | – | 373 | 373 |
| **Total contribution by and distributions to owners** | **1** | **5,728** | **373** | **6,102** |
| **At 31 December 2017** | **1,003** | **52,939** | **(9,865)** | **44,077** |

# NOTES FORMING PART OF THE COMPANY FINANCIAL STATEMENTS

For the year ended 31 December 2018

## 1 Accounting policies

### Basis of preparation

Midatech Pharma plc is a company incorporated in England & Wales under the Companies Act. The address of the registered office is given on the contents page and the nature of the Group's operations and its principal activities are set out in the Strategic Report. The financial statements have been prepared in accordance with FRS 102, the Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland ('FRS102').

The preparation of financial statements in compliance with FRS 102 requires the use of certain critical accounting estimates. It also requires Group management to exercise judgement in applying the Group's accounting policies.

### Parent company disclosure exemptions

In preparing the separate financial statements of the parent company, advantage has been taken of the following disclosure exemptions available in FRS 102:

- only one reconciliation of the number of shares outstanding at the beginning and end of the period has been presented as the reconciliations for the Group and the parent company would be identical;
- no cash flow statement has been presented for the parent company;
- disclosures in respect of the parent company's financial instruments and share-based payment arrangements have not been presented as equivalent disclosures have been provided in respect of the Group as a whole; and
- no disclosure has been given for the aggregate remuneration of the key management personnel of the parent company as their remuneration is included in the totals for the Group as a whole.

The following principal accounting policies have been applied:

### Valuation of investments

Investments in subsidiaries are measured at cost less accumulated impairment. Where merger relief is applicable, the cost of the investment in a subsidiary undertaking is measured at the nominal value of the shares issued together with the fair value of any additional consideration paid. Costs of acquisition of investments are capitalised.

### Intangible assets

Externally acquired intangible assets are initially recognised at cost and subsequently amortised on a straight-line basis over their useful economic lives where they are in use. The amortisation expense is included within the administrative cost in the profit and loss account income.

The amounts ascribed to intangibles recognised on business combinations are arrived at by using appropriate valuation techniques.

### Goodwill

Goodwill represents the excess of the cost of a business combination over the fair value of the Group's share of the net identifiable assets of the acquired business at the date of acquisition. Acquisition costs of a business are capitalised within goodwill. Goodwill on acquisitions is included in 'intangible assets'. Goodwill is carried at cost less accumulated amortisation and accumulated impairment losses. Goodwill amortisation is calculated by applying the straight-line method to its estimated useful life. Goodwill is being amortised to 'administrative expenses' over a period of 5 years.

### Impairment of goodwill and intangible assets

Where there is any indication that an asset may be impaired, the carrying value of the asset (or cash-generating unit to which the asset has been allocated) is tested for impairment. 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 (or CGU's) fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (CGUs). Non-financial assets except goodwill that have been previously impaired are reviewed at each reporting date to assess whether there is any indication that the impairment losses recognised in prior periods may no longer exist or may have decreased.

Product marketing rights acquired in business combinations are recognised as assets and are amortised over their useful life.

Product and marketing rights – 13 years

Product and marketing rights were transferred to MPUS prior to the disposal of the subsidiary, at a value of $5.5m.

# NOTES FORMING PART OF THE COMPANY FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 1 Accounting policies continued

### Taxation

Current tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

A deferred tax asset in respect of unutilised tax losses has not been recognised on the basis that the future economic benefit is not certain.

### Going concern

Accounting standards require the Directors to consider the appropriateness of the going concern basis when preparing the financial statements. The Directors are of the opinion that they consider the going concern basis will remain appropriate. The Directors have taken notice of the Guidance on the Going Concern Basis of Accounting and Reporting on Solvency and Liquidity Risk Guidance for directors of companies that do not apply the UK Corporate Governance Code (April 2016). The Directors regard the going concern basis as remaining appropriate as the Group has adequate resources to continue in operational existence for the foreseeable future including a period of at least 12 months from the date of approval of these financial statements. Thus, the Directors continue to adopt the going concern basis of accounting in preparing the annual financial statements.

### Financial assets and liabilities

#### Financial assets

Financial assets, other than investments and derivatives, are initially measured at transaction price (including transaction costs) and subsequently held at cost, less any impairment.

#### Financial liabilities and equity

Financial liabilities and equity are classified according to the substance of the financial instrument's contractual obligations, rather than the financial instrument's legal form. Financial liabilities, excluding convertible debt and derivatives, are initially measured at transaction price (after deducting transaction costs) and subsequently held at amortised cost.

### Depreciation

Depreciation on assets is charged so as to allocate the cost of assets less their residual value over their estimated useful lives, using the straight-line method. The estimated useful lives range as follows:

| | | |
|---|---|---|
| Leasehold Improvements | – | The term of the lease |
| Computer Equipment and Software | – | 4 years |
| Fixtures and Fittings | – | 4 years |

The assets' residual values, useful lives and depreciation methods are reviewed, and adjusted prospectively if appropriate, if there is an indication of a significant change since the last reporting date.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within 'other operating income or losses' in the statement of comprehensive income.

## 2 Staff costs

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Staff costs (including Directors) comprise: | | |
| Wages and salaries | 987 | 717 |
| Defined contribution pension cost | 41 | 42 |
| Social security contributions and similar taxes | 114 | 102 |
| Share-based payment | (349) | 373 |
| | 793 | 1,234 |

### Employee numbers

The average number of staff employed by the Group during the financial year amounted to:

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| General and administration | 4 | 4 |
| | 4 | 4 |

Please also refer to note 6 in the consolidated financial statements regarding Directors' remuneration.

## 3 Loss attributable to shareholders

Under Section 408 of the Companies Act 2006 the Company is exempt from the requirement to present its own profit and loss account. The loss for the financial period, of the holding Company, as approved by the Board, was £24.99m (2017: £4.83m, 2016: £3.34m).

## 4 Intangibles

| | Product and marketing rights £'000 | Goodwill £'000 | Total £'000 |
|---|---|---|---|
| **Cost** | | | |
| **At 1 January 2018** | **2,512** | **53** | **2,565** |
| Transfer to subsidiary company | (2,512) | (53) | (2,565) |
| **At 31 December 2018** | **–** | **–** | **–** |
| **Amortisation** | | | |
| **At 1 January 2018** | **390** | **22** | **412** |
| Charge for year | (390) | (22) | (412) |
| **At 31 December 2018** | **–** | **–** | **–** |
| **Net book value** | | | |
| **At 31 December 2018** | **–** | **–** | **–** |

| | Product and marketing rights £'000 | Goodwill £'000 | Total £'000 |
|---|---|---|---|
| **Cost** | | | |
| **At 1 January 2017** | 2,512 | 53 | 2,565 |
| Additions | – | – | – |
| **At 31 December 2017** | **2,512** | **53** | **2,565** |
| **Amortisation** | | | |
| At 1 January 2017 | **197** | **11** | **208** |
| Charge for year | 193 | 11 | 204 |
| **At 31 December 2017** | **390** | **22** | **412** |
| **Net book value** | | | |
| **At 31 December 2017** | **2,122** | **31** | **2,153** |

# NOTES FORMING PART OF THE COMPANY FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 5 Investments

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Brought forward 1 January** | **7,405** | **7,405** |
| Disposals | (6,404) | – |
| **Total investments at 31 December** | **1,001** | **7,405** |

At 31 December 2018, the Company held share capital in the following subsidiaries and joint arrangements:

| Name | Registered Office or Country of Incorporation | Nature of Business | Proportion held | Notes |
|---|---|---|---|---|
| Midatech Limited | Oddfellows House, 19 Newport Road, Cardiff, CF24 0AA | Trading company | 100% | |
| Midatech Pharma (España) SL | Parque Tecnológico de Vizcaya, Edificio 800 Planta 2, Derio, 48160, Vizcaya, Spain | Trading company | 100% | (a) |
| PharMida AG | c/o Kellerhals, Hirschgässlein 11, 4051 Basel, Switzerland | Dormant | 100% | (a) (b) |
| Midatech Pharma (Wales) Limited | Oddfellows House, 19 Newport Road, Cardiff, CF24 0AA | Trading company | 100% | |
| Midatech Pharma PTY Limited | c/o Griffith Hack Consulting, 300 Queen Street, Brisbane, QLD 4000, Australia | Trading company | 100% | |
| MidaSol Therapeutics GP | Incorporated in the Cayman Islands | Dormant JV | 50% | |
| Syntara LLC | Incorporated in the United States | Dormant JV | 50% | |

Notes:

(a) Wholly owned subsidiary of Midatech Limited.

(b) PharMida AG became dormant in January 2016.

## 6 Property, plant and equipment

| | Fixtures and fittings £'000 | Leasehold improvements £'000 | Computer equipment and software £'000 | Total £'000 |
|---|---|---|---|---|
| **Cost** | | | | |
| **At 1 January 2018** | 5 | 229 | 219 | 453 |
| Disposals | (5) | (229) | – | (234) |
| Additions | – | – | 16 | 16 |
| **At 31 December 2018** | **–** | **–** | **235** | **235** |
| **Depreciation** | | | | |
| **At 1 January 2018** | **3** | **126** | **94** | **223** |
| Disposals | (3) | (174) | – | (177) |
| Charge for year | – | 48 | 56 | 104 |
| **At 31 December 2018** | **–** | **–** | **150** | **150** |
| **Net book value** | | | | |
| **At 31 December 2018** | **–** | **–** | **85** | **85** |

| | Fixtures and fittings £'000 | Leasehold improvements £'000 | Computer equipment and software £'000 | Total £'000 |
|---|---|---|---|---|
| **Cost** | | | | |
| **At 1 January 2017** | 5 | 229 | 175 | 409 |
| Additions | – | – | 44 | 44 |
| **At 31 December 2017** | **5** | **229** | **219** | **453** |
| **Depreciation** | | | | |
| **At 1 January 2017** | **2** | **78** | **44** | **124** |
| Charge for year | 1 | 48 | 50 | 99 |
| **At 31 December 2017** | **3** | **126** | **94** | **223** |
| **Net book value** | | | | |
| **At 31 December 2017** | **2** | **103** | **125** | **230** |

## 7 Debtors

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Amounts due from group companies | 16,676 | 34,270 |
| Other debtors | 145 | 159 |
| Prepayments | 110 | 277 |
| | 16,931 | 34,706 |

## 8 Creditors: amounts due falling due within one year

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Trade creditors | 78 | 329 |
| Accruals | 513 | 717 |
| Other creditors | 30 | 29 |
| Derivative financial liability | – | – |
| | 621 | 1,075 |

Details of the derivative financial liability are provided in note 20 of the consolidated financial statements.

## 9 Creditors: amounts due falling due after one year

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Bank Loan | – | 5,207 |
| Provision | 165 | – |
| | 165 | 5,207 |

Details of the provision are provided in note 19 of the consolidated financial statements and the bank loan in note 18.

## 10 Share capital

| Allotted and fully paid | 2018 Number | 2018 £'000 | 2017 Number | 2017 £'000 |
|---|---|---|---|---|
| Ordinary shares of 0.00005 each | 61,184,135 | 3 | 61,084,135 | 3 |
| Deferred shares of £1 each | 1,000,001 | 1,000 | 1,000,001 | 1,000 |
| Total | | 1,003 | | 1,003 |

Details of shares issued by the Company in the year are given in note 23 of the consolidated financial statements.

# NOTES FORMING PART OF THE COMPANY FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2018

## 11 Capital commitments

The Company had no capital commitments at 31 December 2018 or at 31 December 2017.

## 12 Contingent liabilities

The Company had no contingent liabilities at 31 December 2018, or at 31 December 2017.

## 13 Ultimate controlling party

The Directors do not consider that there was an ultimate controlling party at 31 December 2018. Following the year end, China Medical Systems Holdings Limited and A&B (HK) Company Ltd (collectively, 'CMS') invested a total of £8m in return for 207,792,206 new ordinary shares, which following admission on 26 February 2019, represents 51% of the issued share capital of the Company. Based upon this, CMS is able to exert control over Midatech.

At date of approval of the financial statements, the ultimate controlling party is deemed to Dr Lam Kong by virtue of the control he has over CMS.

## 14 Reserves

The following describes the nature and purpose of each reserve within the equity:

| Reserve | Description and purpose |
|---|---|
| Share premium | Amount subscribed for share capital in excess of nominal value. |
| Accumulated deficit | All other net gains and losses and transactions with owners (e.g. dividends) not recognised elsewhere. |

## 15 Post balance sheet event

On 29 January 2019, the Company announced that it had signed a licence agreement with China Medical System Holdings Limited ('CMS') for the development and commercialisation of the Group's pipeline of products in Greater China and certain South East Asian Countries. Once the Group's development products are approved in certain territories, including the US or EU, under the terms of this agreement, Midatech intends to manufacture and supply its products to CMS. CMS will be responsible for funding the development and commercialisation of the Group's product in the territories covered by the licence. Subject to certain milestones being achieved, the Company will be eligible to receive regulatory and sales-based milestone payments as well as royalty payments.

The Company also announced that, in parallel with the licence agreement, CMS intended to invest £8m by way of a Subscription for new shares. Under the terms of this Subscription, for each new share issued, CMS would also receive one warrant over one additional share with an exercise price of 50 pence per share.

On 4 February 2019, the Company announced that, following a Placing of 'Units' with new and existing institutional investors, a further £4.65m had been raised, before expenses. Each Unit comprises one ordinary share and one warrant on the same terms as the CMS subscription. Following the results of the Placing, the Company launched an Open Offer to existing shareholder to subscribe for Units to raise additional gross proceeds of up to £0.75m.

At a general meeting of the Company's shareholders held on 26 February 2019, the Subscription, Placing and Open Offer were approved. As a result, the Company raised a total of £13.4m or £12.5m after expenses. Shareholders also voted to approve the Panel Waiver granted by the Takeover Panel in respect of the obligation by CMS (acting with a Concert Party) to make a mandatory general offer pursuant to Rule 9 of the Takeover Code. Following the general meeting, CMS held 51% of the issued share capital of the Company.

Following the general meeting, 348,215,478 new ordinary shares were issued to the subscribers in the Subscription, Placing and Open Offer and the new shares were admitted to AIM on 26 February 2019.

# COMPANY INFORMATION

## Directors

Craig Cook
Nick Robbins-Cherry
Rolf Stahel
Simon Turton
Sijmen de Vries
Huaizheng Peng

## Secretary

Nick Robbins-Cherry

## Registered office

Oddfellows House
19 Newport Road
Cardiff
CF24 0AA

## Registered number

09216368

## Auditor

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United Kingdom


**Registered office**

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