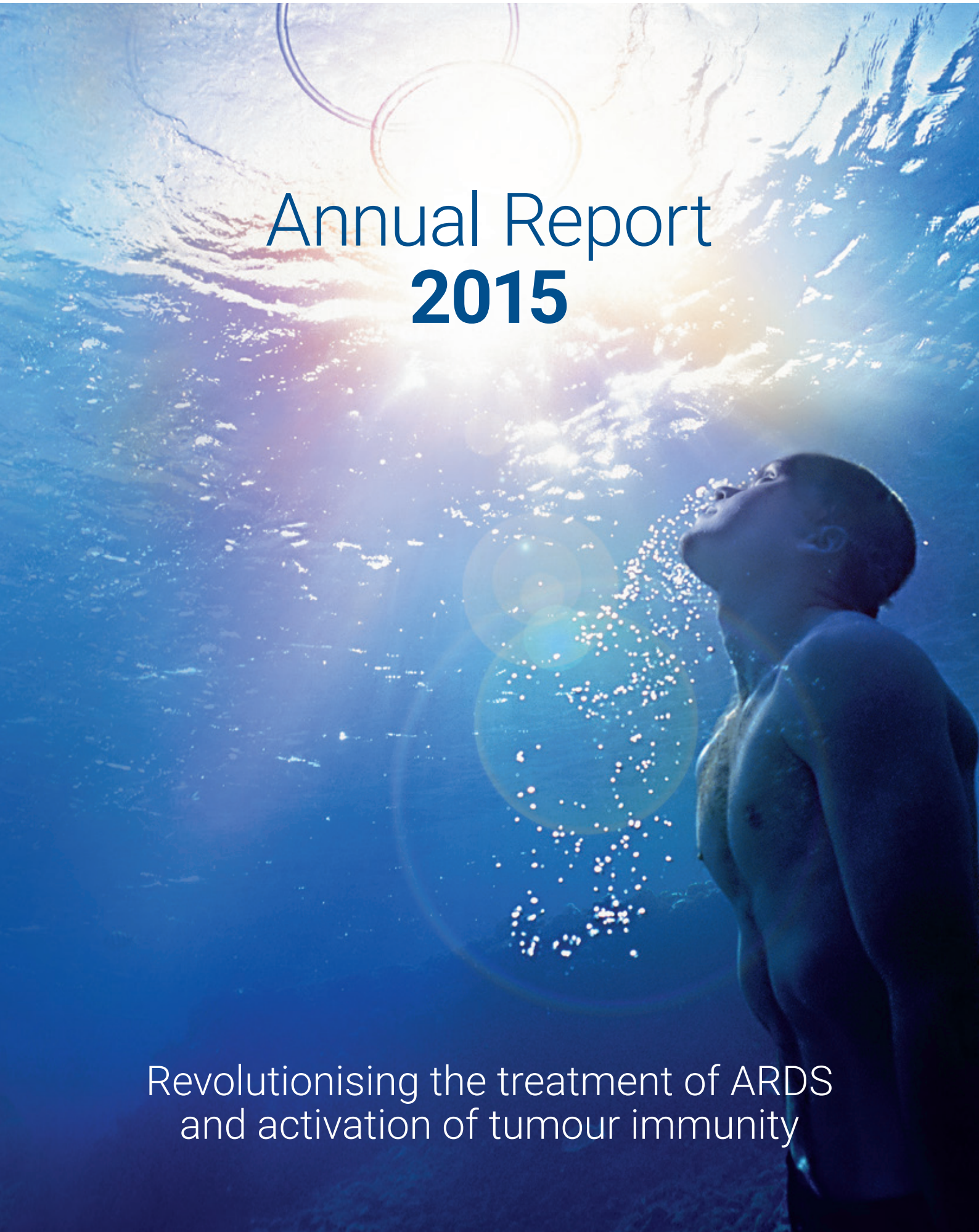
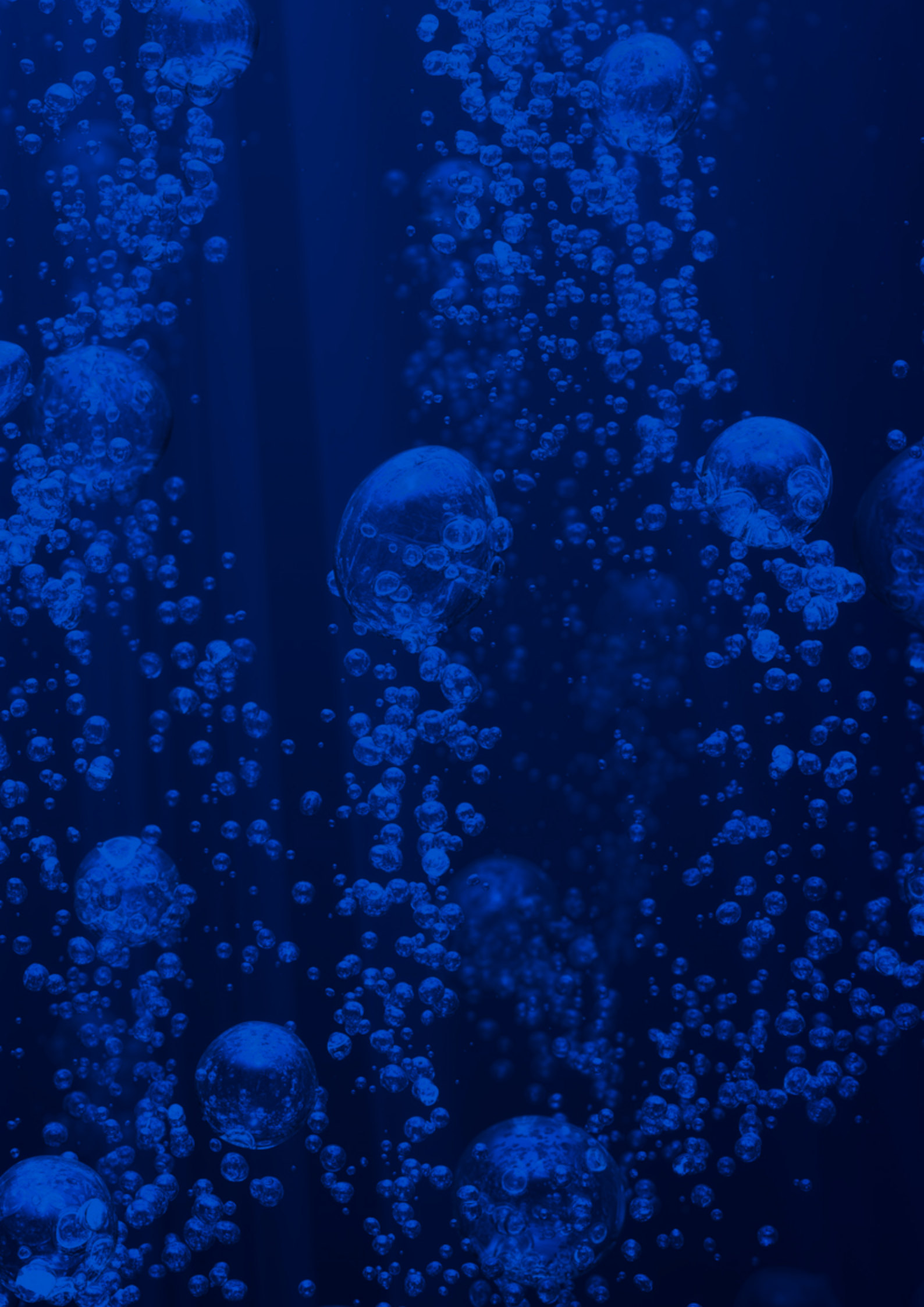
FARON

Pharmaceuticals



Annual Report 2015

Revolutionising the treatment of ARDS and activation of tumour immunity



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FARON PHARMACEUTICALS

Saving Lives

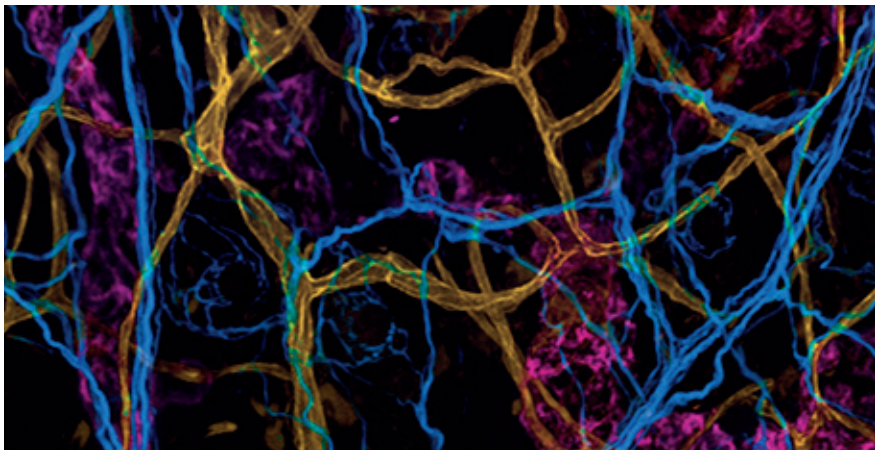
Faron Pharmaceuticals Ltd is a drug discovery and development company focused on creating novel treatments for medical conditions with significant unmet needs. Faron is based in Turku, Finland. The Company has identified several molecular mechanisms involved in the control of endothelial functions as a source of innovations.

Faron currently has a pipeline of products focusing on acute organ traumas, cancer immunotherapy and vascular damage. The Company's lead candidate Traumakine®, has been developed to treat Acute Respiratory Distress Syndrome ("ARDS"), a rare, severe, life-threatening medical condition for which there is currently no approved pharmaceutical treatment. Traumakine® is now in a pan-European pivotal Phase III study (INTEREST).

Besides Traumakine®, Faron's pipeline consists of early stage assets including a pre-clinical anti-Clever-1 antibody named Clevegen®. Clevegen® is focused on converting the immune environment around a tumour from being immune suppressive to immune stimulating and represents a novel immuno-oncology approach. Faron Pharmaceuticals Ltd is listed on London AIM under the ticker 'FARN'.

FARON PHARMACEUTICALS

Endothelial Barrier Is Everything



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

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

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

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

Faron has identified several new endothelial molecules involved in this guidance system and the maintenance of the endothelial barrier. We believe that the control of these molecules provides a unique way to treat many life-threatening conditions with high unmet medical needs. Our two lead indications – acute respiratory lung injury and control of tumour immunity – are both based on the malfunction of the endothelial barrier, both of which we have learned to control.

We hope that our 2015 Annual Report inspires you to explore our technologies, which have originated from world-class academic laboratories and developed by Faron as a novel proprietary treatment for Acute Respiratory Distress Syndrome (ARDS) and tumour immune suppression.

FARON PHARMACEUTICALS

Highlights 2015

TRAUMAKINE

- Established the pivotal pan-European Phase III INTEREST trial for Traumakine® in development for the treatment of Acute Respiratory Distress Syndrome ("ARDS") including 55 hospitals with significant intensive care units in seven European countries (UK, France, Germany, Spain, Italy, Belgium and Finland).
- First Patient recruited in Phase III INTEREST trial in December 2015.
- Entered into agreements with A&B (HK) Company Limited and CMS Pharma Co. Ltd in mainland China, Hong Kong, Macau and Taiwan (the "Greater China Area") to license Traumakine® in May 2015.
- Reported second contract period on the EU FP7 programme for Traumakine® ending 30 November, 2015 triggering next period payments if accepted.

CLEVEGEN

- Entered into a collaboration agreement with the Turku PET Centre, one of the largest positron emission tomography centers in Europe, on the development of novel cancer immunotherapy Clevegen® in June 2015.
- Agreement with Swiss-based Selexis SA for SUREtechnology Platform™ and SURE CHO-M Cell Line™ for use in the development and production of Clevegen® in November 2015.
- Key Publication on Novel Cancer Immunotherapy Mechanism Related to Clevegen® published in Journal of Immunology in November 2015.
- Granted €1.5 million in funding to progress the preclinical development of Clevegen®, Faron´s novel cancer immunotherapy drug candidate. The funding was awarded by Tekes, the Finnish Funding Agency for Innovation in December 2015.

Financial Highlights

- Successful AIM IPO in November 2015, raising €14.2 million in new funds for the Company.
- €5.1 million pre-IPO funding from A&B (HK) Company Limited in May 2015, in conjunction with Traumakine® agreement for Greater China.
- Total equity raised of €19.3 million (net €16.9 million) being used to fund initial pan-European Phase III INTEREST trial in respect of Traumakine® for treatment of Acute Respiratory Distress Syndrome ("ARDS") as well as progressing Clevegen®, the Company's early stage cancer immunotherapy programme.
- Generated €0.5 million (2014: €1.0 million) revenues mainly from milestone payments from Maruishi. In addition the Company recorded grant income of €0.7 million (2014: €0.1 million) from the EU FP7 grant.
- Tekes granted a €1.5 million R&D loan to progress the Clevegen® programme.
- On 31 December 2015 the Company held cash balances of €11.1 million (2014: €0,2 million).
- The operating loss for the financial year ended 31 December 2015 was €6.2 million (2014: €1.4 million loss)
- Net assets on 31 December 2015 were €11.2 million (2014: €0.5 million[1])

Post-Period End Highlights

- On 7th January 2016, Faron announced positive results from the Phase II Japanese study for Traumakine® conducted by Faron's Japanese licensing partner, Maruishi Pharmaceutical Co., Ltd.
- On 1st March 2016 Faron announced a patent application to further strengthen protection for its novel Traumakine® formulation (FP-1201-lyo), seeking exclusivity for the next 20 years which would reinforce Faron's global patent protection strategy for the product.
- Recruitment is on track and Faron anticipates that all 55 sites for the Traumakine® clinical trial will be open in April 2016.

[1] The net assets on 31 December 2014 include the €1.1 million convertible loan that was converted to equity in January 2015.

STRATEGIC REPORT

Addressing Significant Unmet Medical Needs

Faron is a drug discovery and development company focused on creating novel treatments for medical conditions with significant unmet needs. The Company has a pipeline of clinical stage products for the treatment of acute organ traumas, cancer immunotherapy and vascular damage.

Strategy

Faron's strategy is to maximise the potential of its pipeline of drug candidates and to progress the development of its lead product Traumakine®. Faron has identified several new endothelial molecules involved in the maintenance of the endothelial barrier which is a thin layer or membrane of cells that lines blood and lymphatic vessels to separate blood content from tissues. The Company believes that the control of these molecules provides a unique way to treat many life-threatening conditions with high unmet medical needs. Faron collaborates with its strategic partners in research, manufacturing and drug development to bring new pharmaceutical products to market in a timely and cost-effective manner. Faron has formed a core team of leading scientists in capillary biology and diseases arising from vascular leakage. The Company has established links with leading laboratories and clinics based at Turku University in Finland, University College London and other institutions.

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

STRATEGIC REPORT

Chairman´s Statement

Faron has made significant progress with its pipeline in the last year. The small but highly experienced management team is passionate about and committed to their work in life-saving drug development. The Company has chosen to develop new drugs for true unmet medical needs in two critical areas, Acute Respiratory Distress Syndrome (ARDS) and cancer immunotherapy. These two apparently diverse clinical indications are built on Faron's thorough scientific knowledge of the endothelial barrier function and control providing a solid basis to successfully execute the Traumakine® and Clevegen® projects.

Faron's lead drug candidate Traumakine®, now in the pivotal, pan-European Phase III INTEREST trial, is at the heart of the Company's mission. It aims to treat ARDS, an orphan, life-threatening medical condition which currently has no available drug treatment.

ARDS is not common, annually about 370,000 people across Europe and the US are diagnosed, but the condition is serious with about 30 to 45% mortality rate. Data from a Phase I/II study of Traumakine® for ARDS, published in the Lancet, was associated with an 81% reduction in the odds of 28 day mortality rate. We believe that Traumakine® represents a significant opportunity to help ARDS patients, the hospitals that treat these patients and the patients´ families.

Immunotherapy offers enormous potential for cancer treatment by stimulating the patient's own natural immune response to combat the disease. Faron's pre-clinical immunotherapy candidate Clevegen® causes conversion of the immune environment around a tumour from immune suppressive to immune stimulating, by reducing the number of tumour-associated macrophages (TAMs). We believe that Clevegen® is well differentiated from other immunotherapies through its specific targeting of M2 TAMs which facilitate tumour growth, while leaving intact the M1 TAMs that support immune activation against tumours.

In November 2015, Faron was admitted to trading on the AIM market of the London Stock Exchange. The capital raised is devoted to advancing the Company's two programmes and provides a positive start for 2016.

With the AIM listing, I would like to welcome new Shareholders on behalf of the new Board, and thank the previous Board, employees and advisors for a successful 2015. At the time of the listing, the previous Chairman, Matti Manner, stepped down and became Vice-Chairman. We are all indebted to him for his previous leadership. A number of new Board members were appointed at the listing: Dr Jonathan Knowles, Mr Leopoldo Zambeletti, Dr Huaizheng Peng and myself, Dr Frank Armstrong as Chairman. It is a privilege to participate in the ongoing success achieved by Faron. The Board is very grateful to the staff of the Company and particularly to Dr Markku Jalkanen (CEO) and Mr Yrjö Wichmann (CFO) for their commitment and leadership. Faron is an ambitious company and this is reflected in the employees and leadership of the Company.

The Board is committed to delivering the strategy described in the IPO Admission Document. Our key focus is to complete the recruitment for the Phase III INTEREST trial during 2016, as we regard this as a major value inflection point for Shareholders. We also believe that the progress on Clevegen® by our scientific collaborators will provide exciting news in 2016. We will continue to look for opportunities to deliver and enhance value to our Shareholders as well as patients who will benefit from the new drugs Faron is developing.

Dr Frank M Armstrong – Chairman

STRATEGIC REPORT

Operational Review

"We are very excited to become part of the international, publicly quoted biotech sector, which is a key driver in the generation of new pharmaceutical treatments for unmet medical needs."

2015 has been a transformational year for Faron which saw the Company joining AIM in November 2015 and achieving a number of scientific and development milestones. Faron's business growth prospects continue as outlined in the IPO Admission Document in November 2015. We are very excited to become part of the international, publicly quoted biotech sector, which is a key driver in the generation of new pharmaceutical treatments for unmet medical needs.

The main reason for the IPO was to help us execute the further development of our exciting pipeline projects, Traumakine® and Clevegen®. The pre-IPO round in May 2015 allowed us to initiate preparation for the pivotal, pan-European Phase III INTEREST trial for Traumakine® and the proceeds from the IPO round enabled full execution of all the required agreements to open study sites. We can now fully utilise the €6.0 million EU grant to support this final step of Traumakine® development in Europe.

Traumakine® Development

Faron's lead drug Traumakine® is currently in Phase III development for the treatment of Acute Respiratory Distress Syndrome ("ARDS"). ARDS is a severe, life-threatening medical condition characterised by widespread capillary leakage and inflammation in the lungs, most often as a result of sepsis, pneumonia or significant trauma. Currently there are no pharmacological treatments for ARDS, an orphan disease with a high, 30 to 45% mortality rate. Traumakine® has been granted Orphan Drug Designation in Europe which allows a period of 10 years of market exclusivity following marketing approval by the EMA.

"Traumakine® has been granted Orphan Drug Designation in Europe which allows a period of 10 years of market exclusivity following marketing approval by the EMA."

In December 2015, the first patient was recruited into the Traumakine® pan-European Phase III INTEREST trial. The recruitment of the first patient, so soon after the Company's recent IPO is consistent with the anticipated timeline of 12 to 18 months required to complete recruitment for the pivotal Phase III trial for Traumakine®. The Phase III INTEREST trial is being led by Professor Geoff Bellingan from University College London Hospital and Professor Marco Ranieri from the University of Rome. Subject to the completion of successful Phase III INTEREST trial and achievement of regulatory approvals, Traumakine® could be the first effective, mechanistically-targeted, disease-specific pharmacotherapy for ARDS patients.

To date, Faron has entered into agreements with two pharmaceutical companies to carry out the clinical development and commercialisation of Traumakine® in Japan and the Greater China Area. Faron owns the IPR and marketing rights in respect of Traumakine® in all other territories.

A&B (HK) Company Limited and CMS Pharma Co. Ltd – In May 2015, Faron entered into a licence and asset transfer agreement with A&B (HK) for the commercialisation of Traumakine® in the Greater China Area. It is intended that A&B (HK)'s commercialisation activities of Traumakine® will be conducted by a member of the CMS Group, a rapidly growing pharmaceutical group listed on the Hong Kong Stock Exchange. Alongside this agreement, A&B (HK) provided equity funding of €5.1 million in aggregate. CMS Pharma Co. Ltd owns the right to import, register, market, distribute, promote and sell Traumakine® in the Greater China Area.

Maruishi Pharmaceutical Co., Ltd – In 2011 Faron licensed to Maruishi, a Japanese pharmaceutical company, the rights to develop and commercialise Traumakine® in Japan. In January 2016, Faron announced that Maruishi had obtained positive results from the Phase II Japanese study for Traumakine®. Based on these results Maruishi is now planning a pivotal clinical trial to be conducted in Japan.

Clevegen® Development

One of Faron's key areas of focus is to develop a cancer treatment that supports the hosts' immune defences against tumours, as these are often suppressed in cancer patients. Faron's second most advanced drug development project, Clevegen®, revolves around Clever-1, a cell surface molecule involved in cancer growth and spread. The active pharmaceutical ingredient of Clevegen® is a humanised anti-Clever-1 antibody.

In June 2015, Faron entered into a collaboration agreement with the Turku PET Centre, one of the largest positron emission tomography centres in Europe, for the development of Clevegen®. The PET project will assist Faron in optimising the use of Clevegen® for cancer treatment, as well as guide diagnosis, pre-clinical and clinical development and measure potentially novel clinical end points to demonstrate efficacy.

In November 2015, the Journal of Immunology, the highly ranked journal of the American Association of Immunology, published data on Clever-1 function related to Faron's novel cancer immunotherapy antibody Clevegen®.

Following this, in December 2015, Faron was granted €1.5 million funding from Tekes, the Finnish Funding Agency for Innovation, to progress the pre-clinical development of Clevegen®. The funding is a government loan ("Loan"), which covers 50% of the budgeted cost of the pre-clinical development of Clevegen®.

Future Outlook

The key aim for Faron in 2016 is the completion of the Phase III INTEREST trial recruitment. We anticipate that all 55 sites will be open in April 2016 and the observed recruitment is already higher than the anticipated 0.5 patients/site/month. We therefore reiterate that the INTEREST trial results should be available in H2 2017. We also expect our contracted, scientific collaborators to generate exciting new data on Clever-1 function in tumour immune suppression.

Markku Jalkanen – CEO

"Subject to the completion of successful Phase III INTEREST trial and achievement of regulatory approvals, Traumakine® could be the first effective, mechanistically-targeted, disease-specific pharmacotherapy for ARDS patients."

STRATEGIC REPORT

Financial Review

Key Performance Indicator

Faron is a late clinical stage drug development company with no recurring sales and thus the primary Key Performance Indicators (KPI) followed by the Board focus on cash balances and other related information. During 2015, the Company generated €10.8 million free cash flow mainly due to the successful fundraising. The Board will consider the appropriateness of monitoring additional KPIs as the Company's operations advance.

Revenue and Other Operating Income

The Company's revenue was €0.5 million for the year ended 31 December 2015 (2014: €0.9 million), which comprised of milestone income from license partner Maruishi and sale of excess API (Active Pharmaceutical Ingredient) material. The Company also recorded €0.7million (2014: €0.1 million) of other operational income. This comprised of income recognised from the European Commission FP7 grant in support of the Traumakine® programme. There were no new sources of other operating income during the year.

Share-based Compensation

As part of the IPO process, a number of options were awarded to Directors and key personnel. This had no cash impact on the results for the year, however accounting standards require this share based compensation to be recognised in the Consolidated Statement of Comprehensive Income, resulting in a charge of €0.5 million (2014: €0.0 million).

Taxation

The Company's tax credit for the fiscal year 2015 can be recorded only after the Finnish tax authorities have approved the tax report and confirmed the amount of tax-deductible losses for 2015. The total amount of cumulative tax losses carried forward approved by tax authorities on 31 December 2015 was €5.7 million (2014: €3.2 million). These losses can be utilised during the years 2019 to 2024 by offsetting them against profits. In addition, Faron has €2.8 million research and development costs incurred in the financial years 2010 and 2011 that have not yet been deducted in its taxation. This amount can be deducted over an indefinite period at the Company's discretion.

Losses

Loss before income tax was €6.2 million (2014: €1.4 million). Net loss for the year was €6.2 million (2014: €1.4 million), representing a loss of €0.30 per share (2014: €0.09 per share) (adjusted for the changes in share capital).

Cash Flows

The Company had a net cash inflow of €10.8 million for the year ended 31 December 2015, compared to a net cash inflow of €0.2 million for the previous year. Cash used by operating activities increased by €6.8 million to €7.1 million for the year, compared to €0.4 million for the year ended 31 December 2014. This was driven by an increase in research and development investments, as well as an overall increase in general and administration costs.

Net cash inflow from financing activities increased by €17.3 million to €18.1 million for the year due to the receipt of net proceeds of €18.1 million from an equity placings completed in May-June 2015 and the IPO in November 2015.

Financial Position

As at 31 December 2015, total cash and cash equivalents held were €11.1 million (2014: €0.2 million).

Headcount

Average headcount of the Company for the year was 6 (2014: 5). The increase in headcount is attributable to the commencement of the Phase III INTEREST trial.

Shares and Share Capital

On 24 February 2015, the number of Ordinary Shares was increased to 1,623,791 by the issue of 78,166 new Ordinary Shares at a subscription price of €14.40. The shares were issued due to conversion of the 2014 convertible loan, which so became fully converted. The subscription price was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased. The conversion did not have a cash effect in 2015;

On 19 May 2015, the number of Ordinary Shares was increased to 1,843,356 by the issue of 219,565 new Ordinary Shares at a subscription price of €15.41. The subscription price was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased;

On 9 June 2015, the number of Ordinary Shares was increased to 1,926,555 Ordinary Shares by the issue of 83,199 new Ordinary Shares at a subscription price of €20.03. The subscription price was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased;

By resolution of the Extraordinary General Meeting held on 15 September 2015, the number of Ordinary Shares was increased to 19,265,550 by the issue of 17,338,995 new Ordinary Shares to the Shareholders without payment in proportion to their holdings so that nine Ordinary Shares were issued for each existing Ordinary Share (the "Share Split");

By resolution of a Board Meeting held on 16 September 2015, the Company issued 151,400 warrants (each warrant representing an entitlement to subscribe for one Ordinary Share) to Whitman Howard (which were subscribed on 16 September 2015). The warrants are divided into two tranches: in the first tranche, 109,800 warrants with a subscription price of €1.55 ("A Warrants"), and in the second tranche, 41,600 warrants with a subscription price of €2.01 ("B Warrants"). Any "A" Warrants shall be exercised during the subscription period commencing on 2 November 2015 and ending on 7 May 2018. Any "B" Warrants shall be exercised during the subscription period commencing on 2 November 2015 and ending on 28 May 2018;

By resolution of the Extraordinary General Meeting held on 15 September 2015, the Company adopted the 2015 Share Option Plan and granted the Options detailed in Directors´ Remuneration Report set out in the Annual Report and Accounts.

By resolution of a Board Meeting held on 11 November 2015, the Company resolved to issue (i) 2,417,113 Ordinary Shares without payment into treasury, in order for such Ordinary Shares to be transferred to Placees pursuant to the Placing on a delivery versus payment basis on Admission, (ii) 44,044 Ordinary Shares and VCT shares and EIS shares pursuant to the placing, and (iii) 1,384,997 Ordinary Shares as subscription shares pursuant to the subscription.

Pre-IPO Financing

In May – June 2015 the Company raised a total of €5,049,972 issuing a total of 302,764 new shares to A&B (HK) Company Limited in two separate tranches with an average subscription price of €16.68 . After the Share Split the number of shares increased to 3,027,640 and the average subscription price was €1.67. A&B is a Hong Kong company, which is related to CMS by virtue of both having a common controlling shareholder.

IPO

The Company was admitted to trading on AIM in November 2015 alongside the issue of 3,846,154 new shares with a subscription price of 260 pence, or €1.83, per share raising £10,000,000, or €14,210,967. A total of 16 investors participated in the IPO of which 12 were new investors in the Company. The majority of the funds raised and the new investors were from the UK. At 31 December 2015, the Company had issued a total of 23,111,704 shares. All shares are ordinary shares with equal rights.

Money Raised to Date

To date, the Company has been funded with a total of approximately €32.8 million, made up of a combination of equity, debt and grant funding, which has been used to develop the Company's products and intellectual property. The Company has also generated revenues of €3.3 million to date through the receipt of milestone payments pursuant to certain of its licensing arrangements and the sale of surplus raw materials.

Yrjö E K Wichmann – CFO

STRATEGIC REPORT

Principal Risks and Uncertainties

Faron is a late clinical stage biopharmaceutical company and, in common with other companies operating in this field, is subject to a number of risks and uncertainties. The principal risks and uncertainties identified by Faron for the year ended 31 December 2015 are below.

Research and Development

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

Commercial

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

Dependence on Key Personnel and Scientific and Clinical Collaborators

The Company's success is highly dependent on the expertise and experience of the Directors and the key Management. Whilst the Company has entered into employment and other agreements with each of these key personnel, the retention of such personnel cannot be guaranteed. Should key personnel leave or no longer be party to agreements or collaborations with the Company, the Company's business prospects, financial condition and/or results of operations may be materially adversely

affected. To develop new products and commercialise its current pipeline of products, the Company relies, in part, on the recruitment of appropriately qualified personnel, including personnel with a high level of scientific and technical expertise. There is currently a shortage of such personnel in the pharmaceutical industry, meaning that the Company is likely to face significant competition in recruitment. The Company may be unable to find a sufficient number of appropriately highly-trained individuals to satisfy its growth rate which could affect its ability to develop as planned.

Regulatory Environment

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

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

Intellectual Property and Proprietary Technology

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

Despite precautions taken by the Company to protect its products, unauthorised third parties may attempt to copy, or obtain and use the Company's IPR and other technology that is incorporated into its pharmaceutical products. In

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

The Directors do not believe that its lead pharmaceutical drug candidates, future drug candidates in development, and proprietary processes for generating those candidate compounds infringe the IPR of any third parties although shareholders should note the risk factor headed "US Patent owned by Biogen" in the Admission Document dated 18 November 2015. However, it is impossible to be aware of all third party intellectual property. The Company's research has included searching and reviewing certain publicly available resources which are examined by senior levels of management in order to keep abreast of developments in the field.

Financial

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

Operational

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

This report was approved by the Board on 9 March 2016 and signed on its behalf.

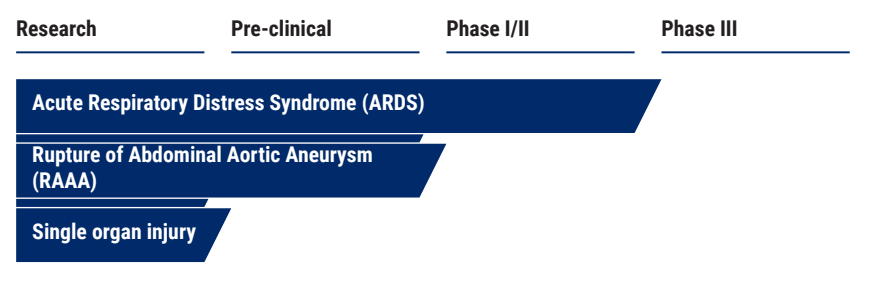
PIPELINE

Revolutionising the Treatment of ARDS and Activation of Tumour Immunity

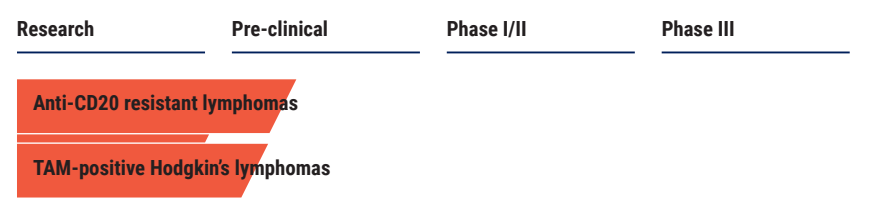
Faron has identified several molecular mechanisms involved in the control of endothelial functions as a source of innovation. The Company currently has a pipeline focusing on acute organ traumas, cancer immunotherapy and vascular damage.

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

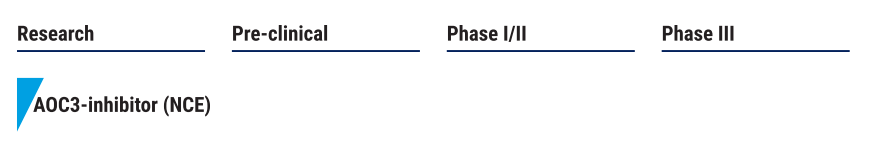
Traumakine® is Faron's spearhead project



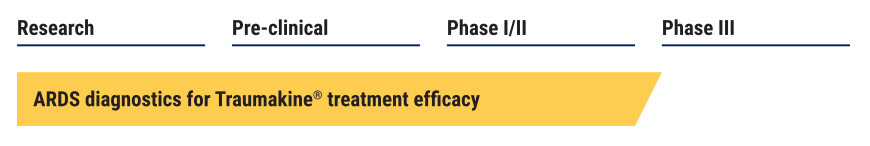
Clevegen®



Farbetic



D-ARDS



TRAUMAKINE

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

PIPELINE: TRAUMAKINE®

Acute Respiratory Distress Syndrome ARDS

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

ARDS is the leading cause of respiratory failure in intensive care unit patients requiring mechanical ventilation. Despite progress in critical care medicine ARDS is currently associated with a mortality rate of 30 to 45% depending on the severity of the condition. Although ARDS mortality has decreased in the last decade due to improvements in supportive care and in the treatment of the underlying conditions, it still remains high.

Currently, patients suffering from ARDS are generally treated with lung-protective mechanical ventilation. This treatment is accompanied by ancillary support such as positioning, fluid management, and food restrictions. Extra corporeal support may also be provided depending on the severity of the condition. Complications which can also arise whilst a patient is being treated for ARDS include the development of infections, pneumothorax, lung scarring and blood clots which can develop into a pulmonary embolism. Patients who recover from ARDS may suffer other consequences of ARDS after being discharged from the intensive care unit. A recovering patient's quality of life may be adversely affected by permanent damage to the lungs, respiratory problems, scar tissue, muscle weakness and depression, all of which can have an adverse effect on the patient's quality of life.

Treating ARDS

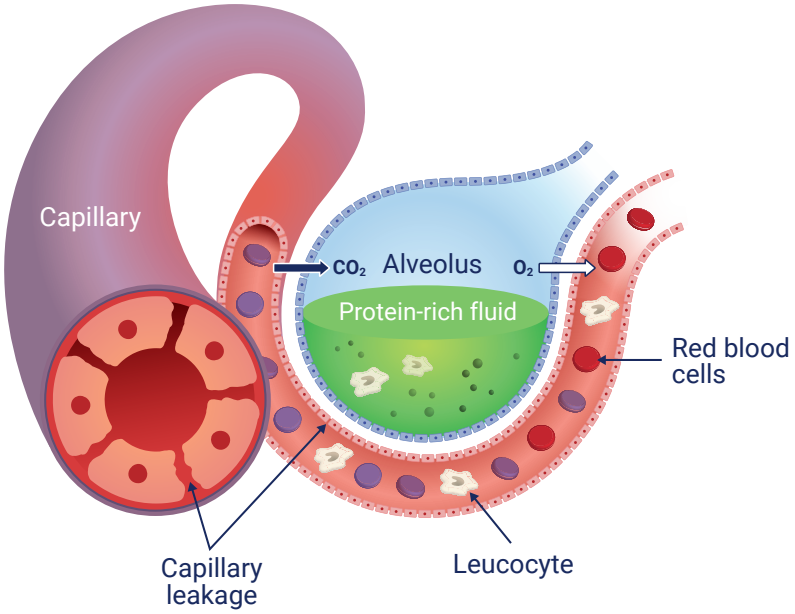
Supply of oxygen and nutrients to individual cells of various organs are maintained by vasculature and especially by the long and thin blood vessels called capillaries. Their integrity is sustained by endothelial cells covering the inner surfaces of these vessels and by forming a barrier between circulation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

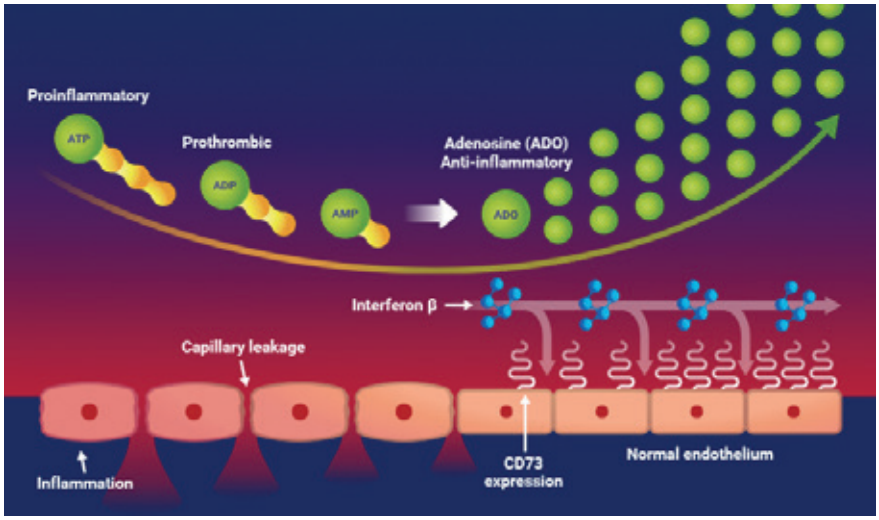
The key molecule to maintain endothelial barrier and lung function is CD73, an endothelial ectoenzyme, which can produce local adenosine. Traumakine's active pharmaceutical ingredient, interferon-beta increases CD73 expression resulting in increased local adenosine. Subsequently high local adenosine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

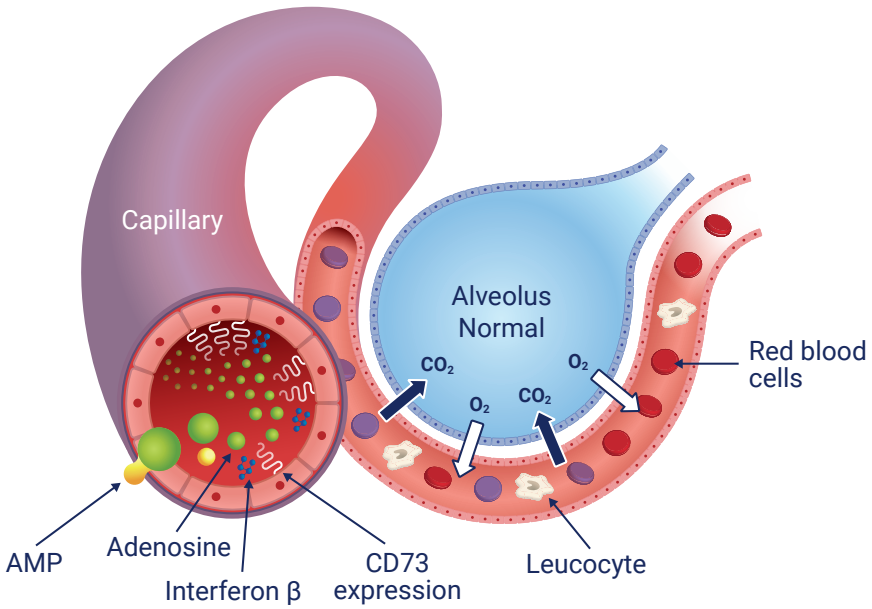
"ARDS is the leading cause of respiratory failure in intensive care unit patients requiring mechanical ventilation."

ARDS

- **A severe, life-threatening medical condition, most often as a result of sepsis, pneumonia or significant trauma**
- **Orphan lung disease with no available drug treatment**
- **The leading cause of respiratory failure in intensive care unit patients who require mechanical ventilation**
- **Annual ARDS incidence in Europe is 170,000 and in the US nearly 200,000 patients**
- **High mortality rate of 30 to 45% and survivors suffer long-term mental and physical problems**

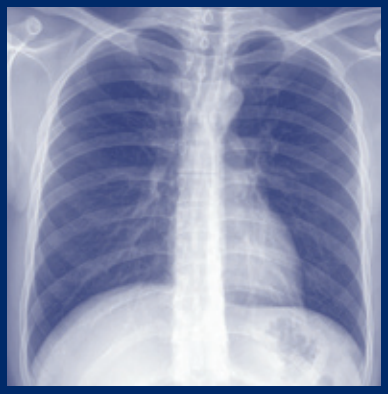






ARDS lung

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



Normal lung

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

Traumakine® Clinical Programme

The clinical programme of Faron´s lead candidate Traumakine® addresses the treatment of Acute Respiratory Distress Syndrome ARDS. The scientific rationale for Traumakine® treatment is based on the use of interferon beta for the restoration of the endothelial barrier function in ARDS patients. Traumakine® (FP-1201-lyo) is based on a patent-protected use of interferon beta to prevent leakage of vascular beds in acute lung injuries. The active pharmaceutical ingredient in Traumakine® is recombinant human IFN beta-1a. Traumakine® has commenced a pan-European Phase III trial in respect of the treatment of ARDS. The first patient in the "INTEREST" study was enrolled in December 2015.

The first clinical trial in the Traumakine® programme was a phase I/II open-label study to assess the safety, tolerability and preliminary efficacy of interferon beta in the treatment of patients with ARDS. This study consisted of dose escalation (Phase I) and dose expansion (Phase II) phases. In the dose escalation phase, four interferon beta levels were tested. The dose expansion phase was conducted using the optimal tolerated dose.

A total of 37 ARDS patients were treated at nine hospitals in the UK with highly encouraging results. Interferon beta was found to be safe and well tolerated in ARDS patients and the optimal tolerated dose was established. The selected pharmacodynamic marker for interferon beta bioactivity showed clear dose response and the treatment target molecule (CD73) levels were induced during the dosing period. Most importantly, interferon beta treatment significantly reduced the all-cause mortality at day 28, the primary end point of the study, compared to the control cohort[1]. Traumakine® was associated with an 81% reduction in odds of 28-day mortality. Comparable results were obtained from Traumakine® Phase II Japanese study conducted by Faron´s Japanese licensing partner Maruishi Pharmaceutical Co., Ltd. in Japan, as announced in January 2016.

Ongoing Phase III INTEREST Study

The presently ongoing, clinical trial is a Phase III double-blind, randomised, parallel-group comparison of efficacy and safety of interferon beta and placebo in the treatment of patients with moderate to severe ARDS. The study named INTEREST is to be conducted in 55 hospitals in Belgium, Finland, France, Germany, Italy, Spain and UK and 300 ARDS patients in total will be recruited. INTEREST has received €6 million funding from the European Union Seventh Framework Programme (FP7).

Mechanism of Action

The mechanism behind Traumakine's action was invented by scientists at Turku University during the period 1995 to 2003. Through extensive research and ex-vivo studies, it was identified that a molecule called CD73 is an essential entity needed to maintain the endothelial barrier function. CD73 is an ectoenzyme capable of breaking down extracellular AMP to produce locally active adenosine. Adenosine maintains the endothelial barrier and downregulates inflammation escalation, preventing both early vascular leakage and escalation of inflammation, which are the two early patho-physiological events leading to Acute Respiratory Distress Syndrome (ARDS).

One of the key findings that led to the development of Traumakine®, was a discovery that interferon beta could enhance CD73 expression and therefore could be used to treat a range of vascular leakage conditions including ARDS. Traumakine® works by enhancing lung CD73 expression and increasing production of anti-inflammatory adenosine such that vascular leaking and escalation of inflammation are reduced.

Recombinant human IFN beta-1a is an approved treatment for patients with relapsing remitting MS and the safety profile of recombinant human IFN beta-1a in such patients is well characterised.

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

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

PIPELINE: TRAUMAKINE®

The INTEREST Study

The INTEREST Study (protocol FPCLI002) is a Phase III clinical study to investigate efficacy and safety of FP-1201-lyo (recombinant human interferon beta-1a) in patients with moderate or severe Acute Respiratory Distress Syndrome (ARDS). This study is planned according to our earlier results from the UK clinical trial, which demonstrated a significant reduction in mortality of ARDS patients and has been published in the Lancet Respiratory Medicine (Bellingan et al., 2014). In the double-blinded and randomised INTEREST Study pivotal effectiveness and safety of FP-1201-lyo is compared to placebo. Both treatment groups also receive standard supportive care.

The primary objective of the INTEREST Study is to demonstrate the efficacy of FP-1201-lyo in improving the clinical course and outcome based on survival and need for mechanical ventilation in patients with moderate or severe ARDS. Other study objectives are to assess the safety and efficacy of FP-1201-lyo compared to placebo, in regard to e.g. mortality, organ failure, need for mechanical ventilation and vasoactive support, length of the stay in ICU and hospital as well as quality of life and pharmacoeconomic parameters.

55 Intensive Care Units in Seven European Countries

Totally about 55 hospitals in seven countries within the European Union – Belgium, Finland, France, Germany, Italy, Spain, UK – participate in the INTEREST Study. A total of 300 adult patients with moderate or severe ARDS will be enrolled (in average six patients per hospital).

Faron Pharmaceuticals runs the study in collaboration with external research service providers. INTEREST has received funding from the European Union Seventh Framework Programme (FP7) under the Traumakine® project name.

First Patient Enrolled in December 2015

The first approvals from competent authorities and favourable opinions from independent ethics committees to conduct the study were obtained during the end of 2015. The first patient was enrolled in December 2015. The majority of the hospital sites are ready to start the study during the first quarter of 2016. The enrolment period is estimated to last 12–18 months.

The patients enrolled in the study are screened from patients who have been

admitted to intensive care units (ICU) at the participating hospitals. To further ensure appropriate patient enrolment into the study across all hospitals the study design incorporates an eligibility process via the electronic data capture system, involving an independent medical monitor. After all screening procedures have successfully been performed and eligibility for inclusion in the study has been confirmed the patient can be randomised into the study.

Following randomisation, the patients will be treated daily with FP-1201-lyo 10 µg or placebo for 6 days and will undergo daily assessments while in the ICU for a maximum of 28 days. The patients are followed up at 3, 6 and 12 months after enrolment. Information on the need for ventilator support as well as for hospital and ICU care is collected during this follow-up period. Other collected data include e.g. respiratory and neurological functions and quality of life.

The main analysis and clinical study report will be written on the data from the 6 months long-term follow-up. The data from the extended follow-up period from 6–12 months will be reported separately in an addendum to the clinical study report.

Safety Monitoring

An Independent Data Monitoring Committee has been established in order to monitor safety in this study. This safety review committee will periodically conduct an independent unblinded review of safety data generated during the study.

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

More details on the study can be found on www.clinicaltrialsregister.eu (reference EudraCT No. 2014-005260-15) and clinicaltrials.gov (reference NCT02622724).

The mode of action of FP-1201-lyo is described on the video found at Faron web pages (www.faronpharmaceuticals.com).

INTEREST Study

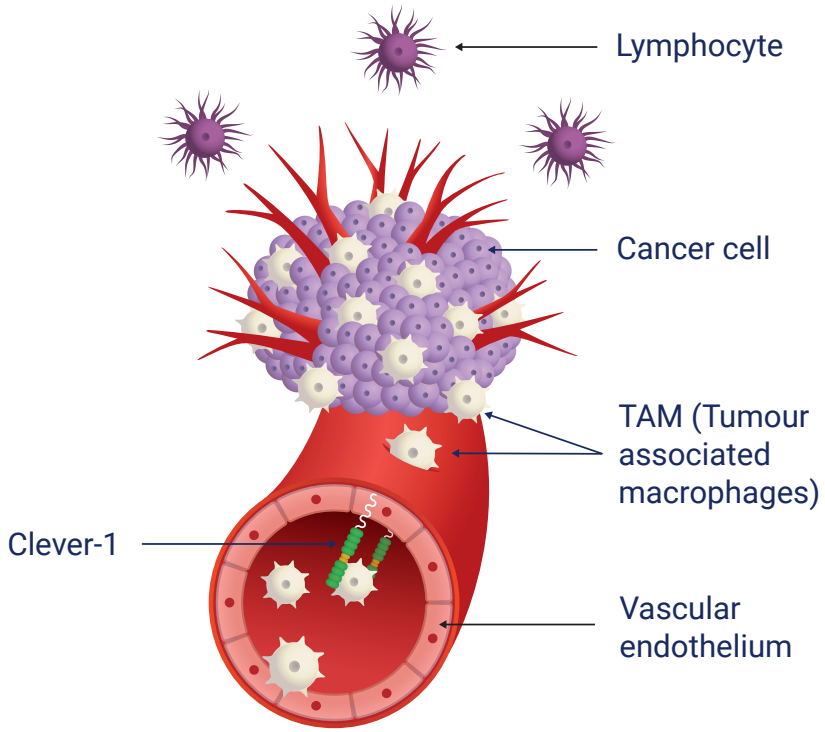
- **Pivotal Phase III trial for Traumakine® in development for the treatment of Acute Respiratory Distress Syndrome ARDS**
- **Conducted in 55 ICUs (Intensive Care Units) in seven European countries**
- **300 adult patients with moderate to severe ARDS will be enrolled in the study**
- **First patient enrolled in December 2015**
- **The enrolment period is estimated to last 12–18 months**
- **Subject to the study results and achievement of regulatory approvals Traumakine® could be the first effective, disease-specific pharmacotherapy for patients suffering from ARDS**

CLEVEGEN

One of Faron's key areas of focus is to develop a cancer treatment to support the hosts' immune defences against tumours, as these are often suppressed in cancer patients. Our second most advanced drug development project, Clevegen®, revolves around Clever-1, a cell surface molecule involved in cancer growth and spread. The active pharmaceutical ingredient of Clevegen® is a humanised anti-Clever-1 antibody.

PIPELINE: CLEVEGEN®

Mechanism of Action

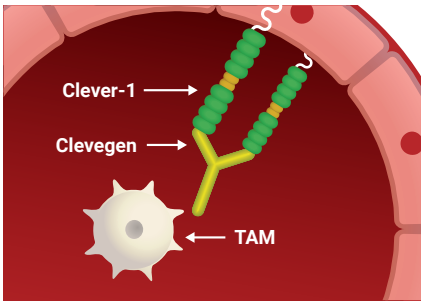


All tumours are infiltrated by immune cells, for example macrophages, neutrophils, T cells, dendritic cells, mast cells, myeloid derived suppressor cells and natural killer cells. Depending on the immune cells stimulated and activated, they can either have a protective effect for the host through suppression of tumour growth or deleterious effect by promoting tumour growth, invasion, metastasis and angiogenesis. Tumour associated macrophages (TAMs) have emerged as an essential constituent of the tumour environment, with influence over many aspects of cancer (proliferation and survival) as well as interaction with surrounding elements (angiogenesis, escape from antitumour specific immunity). When TAMs populate a tumour, one of the very significant influences they exert over it, is a strong increase in immune suppression. Clever-1-positive TAMs represent one major macrophage population involved in the elimination of host immune activity against the tumour cells. Clevegen® is an anti-Clever-1 antibody which targets and eliminates Clever-1-positive TAMs from cancer patients.

Clevegen® has two significant ways to intervene in the TAM's role in tumour growth and spread: prevent TAM infiltration into a tumour and block TAM-to-Tumour cell interaction responsible for TAM transformation into tumour supportive cell types.

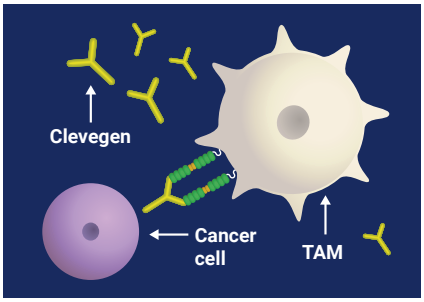
"Clever-1-positive TAMs represent one major macrophage population involved in the elimination of host immune activity against the tumour cells."

"Clevegen® has two significant ways to intervene in the TAM role in tumour growth and spread: prevent TAM infiltration into a tumour and block TAM-to-Tumour cell interaction responsible for TAM transformation into tumour supportive cell types."



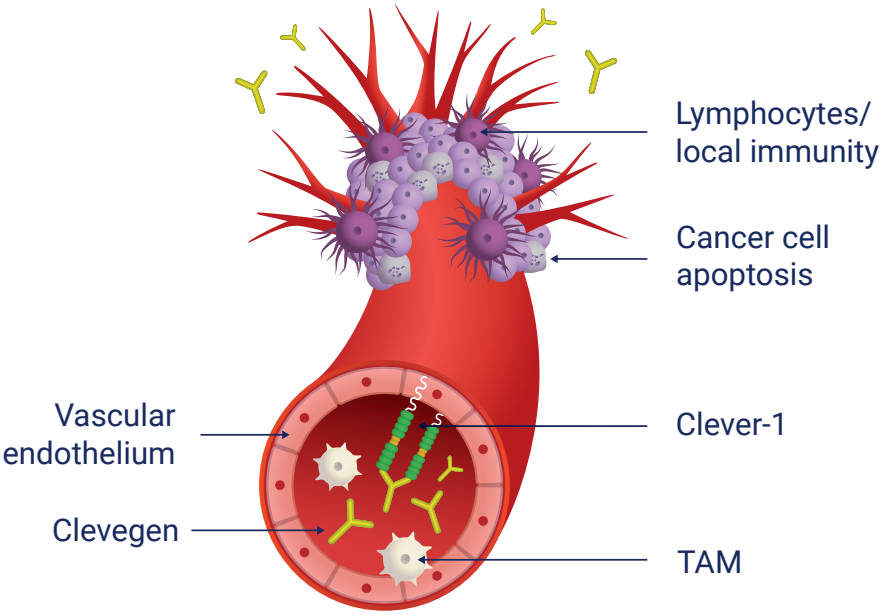
Blocking TAM Infiltration into a Tumour

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



Blocking TAM – Tumour Cell Interaction

Clevegen® prevents tumour cells – TAM interactions as shown on the picture. Through this action, the anti-Clever-1 antibody prevents further transformation of Clever-1 positive TAMs to tumour supportive phenotype.



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

Change in Tumour Immunity

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

References:

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

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

Corporate Governance

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

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

CORPORATE GOVERNANCE

Board of Directors

Dr Frank Armstrong

Non-Executive Chairman

Dr Armstrong has held Chief Executive roles with five biotechnology companies (both public and private) including Fulcrum Pharma PLC (AIM). He led Medical Science and Innovation at Merck Serono and was previously Executive Vice President of Product Development at Bayer and Senior Vice President of Medical Research and Communications at Zeneca. Dr Armstrong is currently the Chairman of Xceleron Inc., Summit Therapeutics (AIM and NASDAQ) and Redx Pharma (AIM) and a Non-Executive Director of Actino Pharma, Juniper Therapeutics (NASDAQ) and Mereo Pharma.

Dr Armstrong is a physician and a Fellow of the Royal College of Physicians (Edinburgh). He is also a member of the Scientific Advisory Board of Healthcare Royalty Partners. He was appointed as a Non-Executive Director of the Company in September 2015.

Matti Manner

Non-Executive Vice-Chairman

Mr Matti Manner was appointed as a partner of Brander & Manner Attorneys Ltd in 1980 having previously sat as a judge at Turku Appeal Courts. He has significant experience in national and international business deals, corporate law and mergers and acquisitions having held a number of board memberships throughout his career. Mr Manner joined the Board of the Company as Chairman in 2007 having previously been the Chairman of Faron Ventures Oy from 2002. He is currently Chairman of Turun Osuuskauppa and Ruissalo Foundation and a member of the board of Marva Media Ltd, Satatuote Ltd, YH VS-Rakennuttajat Ltd and Kauppakeskus Mylly Ltd.

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

Dr Markku Jalkanen

Chief Executive Officer

Dr Jalkanen has more than 25 years of experience within biomedical research, biotech development and the biopharmaceutical industry. He was a founding member of the Company and is the Company´s CEO. In addition to his role as CEO of the Company, Dr Jalkanen is an advisor for the only active Finnish life sciences fund – Inveni Capital. Between 1996 and 2002, Dr Jalkanen was the founding CEO and President of BioTie Therapies Corp which has since become the first publically traded Finnish biotech company to have listed on NASDAQ.

Dr Jalkanen has published over 130 peer reviewed scientific publications in various highly ranked international journals.

Dr Jalkanen has held several board memberships for both public and private companies.

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

Dr Juho Jalkanen

Non-Executive Director

Dr Jalkanen is currently a consultant in vascular surgery at Turku University Hospital, having previously held positions as Resident in Surgery at the Hospital District of Southwest Finland, General Hospitals of Raisio and Salo and at Turku University Hospital.

For the period of 2009 to 2012 Dr Jalkanen was a board member of Duodecim Medical Association on Southwest Finland and subsequently joined the Board of the Company in 2013.

Dr Jalkanen obtains degrees from both business and medicine. He has a Master's degree in Economics and Business Administration from the Turku School of Economics, a Medical Doctor's degree from the University of Turku and subsequently became a fully licensed General Practitioner. At the moment Dr Jalkanen is conducting his PhD on the molecular mechanisms of atherosclerosis. He has published six articles in various publications including the International Journal of Biotechnology and Circulation Research.

Dr Jonathan Knowles

Non-Executive Director

Dr Jonathan Knowles has a career spanning over 40 years in the biotech industry. Dr Knowles held a number of research and teaching positions in the early part of his career before founding the molecular biology group within the Biotechnical Laboratory, Helsinki in 1980.

Dr Jonathan Knowles is currently the Chairman of Adaptimmune Therapeutics PLC (NASDAQ) and Immunocore Ltd and serves on the boards of a number of biotech companies in Europe and the USA. He is a trustee of CRUK and Chairman of the Genomics England Access committee. Jonathan Knowles is a visiting Professor at the University of Oxford, a Research Director at FIMM institute in University of Helsinki (20010-2014 FiDiPro Distinguished Professor), and Professor Emeritus at EPFL, Lausanne. He is a member of EMBO and a member of the Board of A*Star in Singapore.

Dr Knowles was appointed as the President of Global Research at F. Hoffman-La Roche Ltd and subsequently the President of Group Research. He was a member of the Genentech Board for 12 years and a member of the Chugai Board for seven years. He was also the Chairman of the Corporate Governance Committee of Genentech. Under his leadership, the company developed and implemented a strategy of highly effective therapies based on personalised healthcare. Dr Knowles retired from his position at F. Hoffman-La Roche Ltd at the end of 2009. Prior to joining Roche, Dr Knowles was the Head of the Glaxo Institute for Molecular Biology in Geneva and subsequently the Research Director for Glaxo Wellcome Europe.

Dr Knowles was, for 5 years, the Chairman of the Hever Group and the Chairman of the Research Directors' Group of EFPIA (European Federation of Pharmaceutical Industry Associations) and was the first Chairman of the Board of the Innovative Medicines Initiative, a unique public-private partnership between 28 pharmaceutical companies and the European Commission with the participation of over 200 academic institutions in Europe with a budget of more than 5 billion euros over ten years.

Dr Knowles obtained a Bachelor of Science in Biological Sciences from the University of East Anglia, Norwich and subsequently received a PhD in Mitochondrial Genetics from the University of Edinburgh. Dr Knowles was appointed as a Non-Executive Director of the Company in September 2015.

Dr Huaizheng Peng

Non-Executive Director

Dr Peng is a General Manager of China Medical System Holdings, a specialty pharmaceutical company listed on the Hong Kong Stock Exchange. He is in charge of international operations for the Company, including pharmaceutical asset acquisition/product licensing-in/out, international business development, outbound investment and asset management, among others. Dr Peng served as an independent Non-Executive Director of China Medical System Holdings Ltd for three years, and the Company was admitted to trading on AIM (between 2007 and 2010).

Dr Peng was a partner of Northland Bancorp, a private equity firm. Before that, he worked as a head of life sciences and as a director of corporate finance at Seymour Pierce, a London-based investment bank and stockbroker. In addition, he was a Non-Executive Director of China Medstar, an AIM listed medical device company. Earlier in his career Dr Peng was a senior portfolio manager, specialising in global life science and Asian technology investment at Reabourne Technology Investment Management Limited.

Dr Peng received his Bachelor´s degree in medicine from Hunan Medical College (now Central South University Siangya School of Medicine) in Changsha, Hunan Province, China and subsequently he obtained a Master´s degree in medicine from Hunan Medical College. Dr Peng was awarded his PhD in molecular pathology from University College London (UCL) Medical School and subsequently practiced as a clinical lecturer there. Dr Peng was appointed as a Non-Executive Director of the Company in September 2015.

Leopoldo Zambeletti

Non-Executive Director

During a 19-year career as an investment banker, Mr Zambeletti led the European Healthcare Investment team at JP Morgan for eight years before taking up the same position at Credit Suisse for a further five years. Since 2013 he has been an independent strategic advisor to life science companies on merger and acquisitions, out-licencing deals and financing strategy. He is a Non-Executive Director at Advanced Accelerator Applications, Qardio, Summit Therapeutics PLC (NASDAQ and AIM) and Nogra Pharma. Mr Zambeletti started his career at KPMG as an auditor.

Mr Zambeletti received a BA in Business from Bocconi University in Milan, Italy. He serves as a trustee to Barts and the London Charity, which helps to fund the hospitals of the Barts NHS Trust including St Bartholomew, the Royal London and the London Chest Hospitals. He is the founder of the cultural initiative 5×15 Italy. Mr Zambeletti was appointed as a Non-Executive Director of the Company in September 2015.

Yrjö E K Wichmann

Chief Financial Officer

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

Mr Wichmann is a member of the Investment Committee at Dasos Timberland Fund I and II and a member of the Innovation Board of Helsinki University, which advises the rector and the board of the university in research commercialisation. The Innovation Board also oversees the venture capital portfolio of Helsinki University Funds valued at approximately €30 million. Mr Wichmann is also a member of the board of Bioretec Oy.

Mr Wichmann obtained a Masters in Economics from Helsinki University. He was appointed as an Executive Director of the Company in 2015.

CORPORATE GOVERNANCE

Directors' Report

For the year ended 31 December 2015.

The Directors present their report together with the audited financial statements for the year ended 31 December 2015.

Directors

The Directors of the Company were:

Executive
Dr Markku Jalkanen, PhD, Chief Executive Officer
Mr Yrjö E K Wichmann, MSc, Chief Financial Officer (Appointed 15 September 2015)

Non-Executive
Dr Frank M Armstrong, FRCPE, FFPM, Chairman (Appointed 15 September 2015)
Mr Matti Manner, LL.M., Vice-Chairman
Dr Risto Lammintausta, MD, PhD, Vice-Chairman (Resigned 15 September 2015)
Dr Juho Jalkanen, MD, MSc, Non-Executive Director
Dr Jonathan Knowles, PhD, Non-Executive Director (Appointed 15 September 2015)
Dr Huaizheng Peng, MD, PhD, Non-Executive Director (Appointed 15 September 2015)
Mr Frans Wuite, MSc, Non-Executive Director (Resigned 15 September 2015)
Mr Leopoldo Zambeletti, BA, Non-Executive Director (Appointed 15 September 2015)

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

	Issued Share Capital		Share options	
Executive	**Ordinary shares**	**Percentage held**	**Ordinary shares**	**Exercise prise, pence**
Markku Jalkanen[1]	2 873 390	12.4%	80 000	260
Juho Jalkanen[2]	1 082 570	4.7%	20 000	260
Matti Manner	480 900	0.3%	20 000	260
Yrjö Wichmann	69 440	0.3%	30 000	260
Leopold Zambeletti	13 461	0.1%	20 000	260
Frank Armstrong[3]	3 846	0.0%	40 000	260
Jonathan Knowles	3 846	0.0%	20 000	260
Huaizheng Peng	0	0.0%	20 000	260
	4 527 453	19.6%	250 000	

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

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

Principal risks and uncertainties

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

Results and dividends

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

The Company's loss for the financial year after taxation and other comprehensive losses was € 6.2 million (2014: €1.4 million loss).

The Company has no distributable equity and thus the Directors do not recommend the payment of a dividend (2014: nil).

Financial information

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

Financial Key Performance Indicators ('KPIs')

For a review of the Company's KPIs please see Statement of Cash Flows.

Research and development

Details of Company's key research and development programmes can be found in the Strategic Report and the detailed programme sections. Further information is also available on the Company website, www.faronpharmaceuticals.com.

Post balance sheet events

No events occurred after the balance sheet date that would have a material impact on the result or financial position of the Company.

Financial instruments and management of liquid resources

The Company's principal financial instrument comprises cash, and this is used to finance Company's operations. The Company has also other financial instruments such as leasing facilities that arise directly from its operations. The Company has a policy, which has been consistently followed, of not trading in financial instruments and to minimise currency exposure by actively matching currency expenses and income to the extent possible. The Company's cash is held on bank accounts in reputable banks in Finland and UK. The Group's treasury policy is reviewed annually. See Note 1.16 Financial assets and Note 2 Principles of financial risk management in the Notes to the Financial Statements for IFRS disclosure regarding financial instruments.

Substantial shareholdings

On 31 December 2015 the Company had been notified of the following holdings of more than 3% or more of the issued share capital of the Company.

Name	Number of shares	%
A&B (HK) Company Limited	3,408,409	14.75
Marko Salmi	3,389,570	14.67
Tom-Erik Lind	2,552,523	11.04
Aviva Investors Global Services Limited	2,305,769	9.98
Markku Jalkanen	1,794,890	7.77
Juho Jalkanen*	1,082,570	4.68
Sirpa Jalkanen	1,078,500	4.67
Maija-Leena Hollmén**	1,078,500	4.67
Katriina Peltola***	1,078,500	4.67
Timo Syrjälä****	924,676	4.00

* Held by Juho Jalkanen and connected parties.
** Held by Maija-Leena Hollmén and connected parties.
*** Held by Katriina Peltola and connected parties.
**** of which, 520,830 are held directly by Timo Syrjälä and 403,846 are held by Acme Investments SPF S.à.r.l., an entity which is wholly owned by Timo Syrjälä.

Annual General Meeting

The AGM will be held on 26 May 2016 and further details will be provided to Shareholders in advance of the meeting.

Independent auditors

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

Disclosure and information to auditors

Each of the current Directors hereby confirms that:

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

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

On behalf of the Board
Frank M Armstrong
Chairman
9 March 2016

CORPORATE GOVERNANCE

Corporate Governance Report

The Board

At 31 December 2015, the Board comprised six Non-Executive Directors, and two Executive Directors.
The composition of the Board of Directors as well as Directors' biographies are described on pages Board of Directors.

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

All key operational and investment decisions are subject to Board approval.

The roles of Chief Executive Officer and Non-Executive Chairman are well defined and clearly separated. The Chairman oversees the Board´s work, ensures that the Board's decision-making is balanced and that the Non-Executive Directors have all relevant information on matters to be decided. The Chief Executive Officer is responsible for implementing the strategy of the Board and managing the day-to-day business activities of the Company. The management of the Company prepares a monthly management and financial accounts pack, which is distributed to the Board every month in advance of Board meetings.

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

Performance evaluation

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

Board committees

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

Remuneration Committee

The Remuneration Committee comprises Frank Armstrong as Chairman together with Huaizheng Peng and Leopoldo Zambeletti. The committee is responsible for the review and recommendation of the scale and structure of remuneration for senior management, including any bonus arrangements or the award of share options with due regard to the interests of the Shareholders and the performance of the Company. The Remuneration Committee did not hold any meetings during 2015.

Attendance at Board meetings

During 2015 the Board held 15 meetings. The table below lists the Directors attendance to the Board meetings during the year:

		Period	
	Joined Board	Before EGM 15 Sep 2015	After EGM 15 Sep 2015
Executive Directors			
Dr Markku Jalkanen	24.10.2006	11/11	4/4
Mr Yrjö E K Wichmann	15.09.2015		4/4
Non-Executive Directors			
Dr Frank M Armstrong	15.09.2015		4/4
Mr Matti Manner	24.10.2006	11/11	4/4
Dr Juho Jalkanen	18.06.2013	11/11	4/4
Dr Jonathan Knowles	15.09.2015		1/4
Dr Risto Lammintausta	08.05.2009	10/11	
Dr Huaizheng Peng	15.09.2015		4/4
Mr Frans Wuite	30.03.2011	9/11	
Mr Leopoldo Zambeletti	15.09.2015		2/4

Audit Committee

The Audit Committee, which comprises Leopoldo Zambeletti as Chairman together with Frank Armstrong and Huaizheng Peng, meets not less than twice a year. The committee is responsible for making recommendations to the New Board on the appointment of auditors and the audit fee and for ensuring that the financial performance of the Company is properly monitored and reported. In addition, the Audit Committee will receive and review reports from management and the auditors relating to the Interim Report, the Annual Report and accounts and the internal control systems of the Company. The Audit Committee did not hold any meetings during 2015.

Nomination Committee

The Nomination Committee comprises of Matti Manner as Chairman together with Frank Armstrong and Jonathan Knowles. The Nomination Committee monitors the size and composition of the Board and the other Board committees and is responsible for identifying suitable candidates for Board membership. The Nomination Committee did not hold any meetings during 2015.

Risk management and internal control

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

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

Corporate Social Responsibility

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

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

Relations with Shareholders

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

Compliance with the Principles of the QCA Code

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

CGR = Corporate Governance Report

CORPORATE GOVERNANCE

Directors' Remuneration Report

Audited Information
Remuneration policy for Executive Directors

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

The remuneration of the Executive Directors during the year 2015 is set out below.

For the year ended 31 December 2015.

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

Basic salary

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

Bonuses

Annual bonuses are based on achievement of Company's strategic and financial targets, and personal performance objectives. The Non-Executive Directors believe that bonuses are an incentive to achieve the targets and objectives, and represent an important element of the total compensation of the Executive Directors; they have established that the annual bonus potential will be up to 40% for the Executive Directors. On 9 Febuary 2016 the Chief Executive Officer was awarded a bonus representing 40% and the Chief Financial Officer was awarded a bonus representing 30% of his 2015 gross basic salary.

Longer term incentives

In order to further incentivise the Executive Directors and employees, and align their interests with Shareholders, the Extraordinary General Meeting of the Company approved a share option plan and granted share options to the members of the Board under this option plan. Details of the option plan are in the table below.

Pension

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

Other benefits

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

Executive Directors' service contracts and termination provisions

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

The details of the Directors' contracts are summarised below:

		Date of contract	Notice period
Markku Jalkanen	CEO	16.09.2015	6 months[1]
Yrjö E K Wichmann	CFO	16.09.2015	6 months[1]

[1]The 6 months' notice period starts after a fixed 12 months' period from Admission, i.e. from 18 November 2016.

Non-Executive Directors' service contracts and remuneration

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

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

Current contracts are summarised below:

Non-Executive Directors' Contracts	Contracts	Date of Contract
Frank M Armstrong	Chairman	16.09.2015
Matti Manner	Vice-Chairman	16.09.2015
Juho Jalkanen	member	16.09.2015
Jonathan Knowles	member	16.09.2015
Huaizheng Peng	member	16.09.2015
Leopoldo Zambeletti	member	16.09.2015

The appointments of Non-Executive Directors are terminable with immediate effect in accordance with the Articles of Association and pursuant to the Finnish Companies Act, through a resolution of Shareholders at a General Meeting on any grounds. The Non-Executive Directors may resign as a Director by delivering three months' notice to the Registered Office of the Company or through tendering such resignation at a meeting of the Board, after a fixed 6 months' period from Admission.

Audited Information
Directors' remuneration

The Directors received the following remuneration during the year:

	Salaries and fees	Bonus 2015	Taxable benefits	Total
Executive				
Markku Jalkanen	150 300,00	63 512,00	12 720,00	226 532,00
Yrjö E K Wichmann	126 666,00	38 202,00	674,00	165 542,00
Non-Executive				
Frank M Armstrong[1]	21 400,00	-	-	21 400,00
Matti Manner	25 709,90	-	-	25 709,90
Juho Jalkanen	22 123,18	-	-	22 123,18
Jonathan Knowles[1]	10 260,27	-	-	10 260,27
Risto Lammintausta[2]	11 862,90	-	-	11 862,90
Huaizheng Peng[1]	10 260,27	-	-	10 260,27
Frans Wuite[2]	10 862,90	-	-	10 862,90
Leopoldo Zambeletti[1]	11 726,03	-	-	11 726,03
	401 171,46	101 714,00	13 394,00	516 279,46

[1] Joined the Board on 15 September 2015
[2] Resigned from the Board on 15 September 2015

Directors' share options

Aggregate remunerations disclosed above do not include any amounts for the value of options to acquire Ordinary Shares in the Company granted to or held by the Directors.

A share option plan was adopted by the Company at the Extraordinary General Meeting held on 15 September 2015. The option plan allows the Company to offer options for subscription free of charge to members of the Board, and to such officers and employees of the Company as the Board sees fit. Each option will entitle the holder of the option to subscribe for one Ordinary Share.

Under the terms of the option plan, an aggregate maximum number of 1,600,000 options may be granted, such aggregate being made up of a maximum of 400,000 "A" options, the subscription period for which ends on 31 December 2015 (such options exercisable between 2 November 2015 and 30 September 2021), a maximum of 400,000 "B" options to be subscribed for between 8 October 2016 and 30 September 2019 (exercisable between 8 October 2016 and 30 September 2021), a maximum of 400,000 "C" options to be subscribed for between 8 October 2017 and 30 September 2019 (exercisable between 8 October 2017 and 30 September 2021), and a maximum of 400,000 "D" options to be subscribed for between 8 October 2018 and 30 September 2019 (exercisable between 8 October 2018 and 30 September 2021).

The exercise price for Ordinary Shares based on "A" options shall be the euro equivalent to the Placing Price. The exercise price for Ordinary Shares based on "B", "C" and "D" options shall be determined by the euro equivalent to the average share price of the publicly traded Ordinary Shares of the Company on AIM between 1 July and 30 September of 2016, 2017 and 2018 respectively.

The exercise price will be disclosed in euros based on the exchange reference rate published by the European Central Bank on the last day of the period for determination of the subscription price, and rounded to the nearest euro cent.

Details of these options are as follows:

Directors' share options[1]	Date of grant of A options	At 1 Jan 2015	Granted during the period	Cancelled during the period	At 31 Dec 2015	Price per share (p)	Date from which exer-cisable	Expiry date
Markku Jalkanen	16.09.2015	0	80 000	0	80 000	260	02.11.2015	30.09.2021
Yrjö E K Wichmann	16.09.2015	0	30 000	0	30 000	260	02.11.2015	30.09.2021
Frank M Armstrong[2]	16.09.2015	0	40 000	0	40 000	260	02.11.2015	30.09.2021
Matti Manner	16.09.2015	0	20 000	0	20 000	260	02.11.2015	30.09.2021
Juho Jalkanen	16.09.2015	0	20 000	0	20 000	260	02.11.2015	30.09.2021
Jonathan Knowles[2]	16.09.2015	0	20 000	0	20 000	260	02.11.2015	30.09.2021
Risto Lammintausta[3]		0		0	0			
Huaizheng Peng[2]	16.09.2015	0	20 000	0	20 000	260	02.11.2015	30.09.2021
Frans Wuite[3]		0		0	0			
Leopoldo Zambeletti[2]	16.09.2015	0	20 000	0	20 000	260	02.11.2015	30.09.2021

[1] Additionally, the Directors have the right to subscribe equal amounts of "B", "C" and "D" Options (conditional on them continuing to remain in their respective Director roles at the time of commencement of the relevant subscription period).
[2] Joined the Board on 15 September 2015
[3] Resigned from the Board on 15 September 2015

Directors' shareholdings

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

	Issued Share Capital		Share options	
	Ordinary shares	Percentage held	Ordinary shares	Exercise price, pence
Executive				
Markku Jalkanen[1]	2 873 390	12,4%	80 000	260
Juho Jalkanen[2]	1 082 570	4,7%	20 000	260
Matti Manner	480 900	2,1%	20 000	260
Yrjö E K Wichmann	69 440	0,3%	30 000	260
Leopoldo Zambeletti	13 461	0,1%	20 000	260
Frank M Armstrong[3]	3 846	0,0%	40 000	260
Jonathan Knowles	3 846	0,0%	20 000	260
Huaizheng Peng	0	0,0%	20 000	260
	4 527 453	19,6%	250 000	

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

CORPORATE GOVERNANCE

Statement of Directors' Responsibilities

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

The Board of Directors and the CEO are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, as well as for the preparation of financial statements and the report of the Board of Directors that give a true and fair view in accordance with the laws and regulations governing the preparation of the financial statements and the report of the Board of Directors in Finland. The Board of Directors is responsible for the appropriate arrangement of the control of the Company's accounts and finances, and the CEO shall see to it that the accounts of the Company are in compliance with the law and that its financial affairs have been arranged in a reliable manner.

In accordance with the rules of the London Stock Exchange for companies trading securities on the AIM, the Company is also required to prepare annual accounts and financial statements under IFRS.

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

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

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

Website publication

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

On behalf of the Board
Frank M Armstrong
Chairman
9 March 2016

FINANCIAL STATEMENTS

Statement of Comprehensive Income

Stated in euro	Note	Year ended 31 Dec 2015 €'000	Year ended 31 Dec 2014 €'000
Revenue	3; 4	520	906
Cost of sales		(25)	(425)
Gross profit		496	481
Other operating income	5	701	111
Administrative expenses	6; 7	(3 061)	(349)
Research and development expenses	6; 7	(3 971)	(1 471)
Operating result		(5 835)	(1 228)
Financial income	2; 8	0	15
Financial expenses	2; 8	(311)	(146)
Net financial costs		(311)	(130)
Loss before income taxes		(6 146)	(1 358)
Income tax expense	9	(42)	(6)
Total comprehensive income for the financial year		**(6 188)**	**(1 364)**
Total comprehensive income, attributable to:			
Equity holders of the Company		(6 188)	(1 364)
Loss per share attributable to equity holders of the Company	**10**		
Basic and diluted loss per share, euro		(0,30)	(0,09)

FINANCIAL STATEMENTS

Balance Sheet

Stated in euro	Note	Year ended 31 Dec 2015 €'000	Year ended 31 Dec 2014 €'000
Assets			
Non-current assets			
Property, plant and equipment	11	28	0
Intangible assets	11	1 001	1 184
		1 029	**1 184**
Current assets			
Inventories	12	649	699
Trade and other receivables	13	2 074	40
Cash and cash equivalents	14	11 068	242
		13 791	**980**
Total assets		**14 821**	**2 165**
Equity and liabilities			
Capital and reserves attributable to equity holders of the Company			
Share capital		2 691	1 416
Unregistered share capital		1 275	(1 364)
Reserve for invested non-restricted equity		24 533	6 453
Retained earnings		(16 046)	(10 332)
Total equity	**15; 16**	**11 178**	**(1 188)**
Non-current liabilities			
Interest-bearing financial liabilities	17	1 446	1 691
		1 446	**1 691**
Current liabilities			
Interest-bearing financial liabilities	18	245	-
Non-interest-bearing financial liabilities	18	436	9
Other current liabilities	18	1 517	1 652
		2 197	1 662
Total liabilities		**3 643**	**3 352**
Total equity and liabilities		**14 821**	**2 165**

FINANCIAL STATEMENTS

Statement of Cash Flows

Stated in euro	Year ended 31 Dec 2015 €'000	Year ended 31 Dec 2014 €'000
Cash flow from operating activities		
Loss(-) / profit(+) attributable to equity holders of the Company	(6 188)	(1 364)
Adjustments for		
Depreciation and amortisation	262	60
Financial items	298	130
Income taxes	42	6
Non-cash items (options granted)	474	
Change in net working capital:		
Trade and other receivables	(2 035)	6
Inventories	50	400
Trade and other current liabilities	278	510
Interest and other financial costs paid	(285)	(146)
Interest and other financial income received	0	15
Income taxes paid	(42)	(6)
Net cash used in/from operating activities (A)	**(7 146)**	**(389)**
Cash flow from investment activities		
Investments in machinery and equipment and intangible assets	(107)	(152)
Net cash from/used in investing activities (B)	**(107)**	**(152)**
Cash flow from financing activities		
Proceeds from issue of share capital/issue, net	18 080	
Proceeds from issue of convertible notes		1 126
Proceeds from current borrowings		
Proceeds from non-current borrowings		245
Repayment of current borrowings		(588)
Net cash used in financing activities (C)	**18 080**	**783**
Net increase(+) / decrease (-) in cash and cash equivalents (A+B+C)	**10 827**	**242**
Cash and cash equivalents at 1 January	242	(0)
Cash and cash equivalents at 31 December	**11 068**	**242**

FINANCIAL STATEMENTS

Statement of Changes in Equity

Stated in euro	Share capital €'000	Unregistered share capital €'000	Reserve for invested non-restricted equity €'000	Retained earnings €'000	Total equity €'000
Balance at 31 December 2012	**1 296**		**5 328**	**(7 460)**	**(837)**
Total comprehensive income for the financial year 2013				(1 515)	(1 515)
Transactions with equity holders of the Company, recognised directly in equity					
Conversion of convertible debt				7	7
Issue of ordinary shares for cash	120	1 275			1395
	120	1 275		(1 508)	(112)
Balance at 31 December 2013	**1 416**	**1 275**	**5 328**	**(8 968)**	**(949)**
Total comprehensive income for the financial year 2014				(1 364)	(1 364)
Transactions with equity holders of the Company, recognised directly in equity					
Increase of share capital[1]	1 275	(1 275)			
Conversion of convertible notes			1 126		1 126
	1 275	(1 275)	1 126		
Balance at 31 December 2014	**2 691**		**6 453**	**(10 332)**	**(1 188)**
Total comprehensive income for the financial year 2015				(6 188)	(6 188)
Transactions with equity holders of the Company, recognised directly in equity					
Share base payment				474	474
Increase of share capital			19 261		19 261
Transaction costs on share capital issued			(1 181)		(1 181)
Conversion of convertible notes					
			18 080	(5 714)	12 366
Balance at 31 December 2015	**2 691**		**24 533**	**(16 046)**	**11 178**

For further information on the convertible notes and other equity transactions see Note 15 Equity and reserves.

[1]Unregistered increase in share capital at 31 December 2013.

FINANCIAL STATEMENTS

Notes

NOTE 1
1. Summary of significant accounting policies

1.1 Corporate information

Faron Pharmaceuticals Ltd ("Faron" or the "Company") is a Finnish limited liability company organised under the laws of Finland and domiciled in Turku, Finland. The Company's registered address is Joukahaisenkatu 6 B, 20520 Turku, Finland.

The former parent company of Faron Pharmaceuticals Ltd, Faron Ventures Ltd, merged into Faron Pharmaceuticals Ltd as at 31 December 2013. Faron has no interests in other entities. The shares of Faron are held by multiple Shareholders.

Faron is a privately owned clinical stage drug discovery and development company. Currently Faron has three major drug development projects focusing on:

- acute trauma
- inflammatory diseases; and
- cancer growth and spread.

Faron's lead product FP-1201, also known as Traumakine®, successfully completed a Phase I/II trial in the UK to treat vascular leakage in ARDS[1] patients, and has subsequently commenced a pan-European pivotal Phase III study (INTEREST) during 2015. INTEREST recruited its first patient in late December 2015. Faron has been granted orphan drug status for the treatment of ARDS with interferon-beta by the EU Commission and European Medicines Agency (EMA) under the registration number EU/3/07/505. Faron has also been granted several patents in the USA, Europe and Japan, and has several pending applications in other territories for the use of interferon-beta to treat various ischemic conditions.

The Board of Directors of Faron approved the publishing of these financial statements in its meeting on 9 March 2016. According to the Finnish Limited Liability Companies' Act, Shareholders have the right to approve or reject the financial statements at the Annual General Meeting held after the publication of the financial statements.

The principal accounting policies applied in the preparation of these financial statements are set out below.

1.2 Basis of preparation

These are Faron's full year financial statements prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and as published by the International Accounting Standards Board (IASB) and in force as at 31 December 2015. In the EU IFRS standards and their interpretations are adopted in accordance with the procedure laid down in regulation (EC) No 1606/2002 of the European Parliament and of the Council. Faron has consistently applied these policies to each year presented, unless otherwise stated. The Company has not applied any standard, interpretation or amendment thereto before its effective date.

Faron's date of transition to IFRS is 1 January 2012. The Company has applied IFRS 1 First-time Adoption of International Financial Reporting Standards in preparing these financial statements. Until 31 December 2011 Faron's separate financial statements were prepared in accordance with Finnish Accounting Standards (FAS).

The financial statements are prepared under the historical cost convention, except as disclosed in the accounting policies below.

The financial year of Faron is the calendar year ending 31 December. The figures in the financial statements are presented in thousands of euro unless otherwise stated. All figures presented have been rounded, and consequently the sum of individual figures may deviate from the presented aggregate figure.

The Company has not had any other comprehensive income in those years presented in these financial statements.

Faron's financial statements are prepared on a going concern basis. It is the intention of the Company to continue the development of the products to the point where they can be either licensed at attractive terms to internationally active pharmaceutical companies who have the means to further develop these products, or to develop the products in-house until receipt of marketing approval from the relevant regulatory agencies is obtained. After such approval, Faron would primarily seek to form partnerships with strong global, regional or local pharmaceutical companies that have the necessary marketing and distribution capabilities and resources. In such partnerships, Faron will typically grant geographically limited licenses for products in exchange for contractually agreed payments, license fees and royalties on future product sales. In some cases, one element of such an agreement may include a collaboration in which Faron will also receive funding

for R&D services provided at a cost plus basis. In addition to its normal R&D and corporate activities, Faron seeks, as a clinical stage drug discovery and development company, to advance the development of its lead compounds through clinical trials. The Company conducts these clinical trials either together with development partners or by itself, however, in both cases these activities require substantial funding. Faron primarily relies upon financing its activities through equity financing, license agreements and public R&D loans and grants.

The preparation of financial statements under IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the end of the reporting period as well as the reported amounts of income and expenses during the reporting period. These estimates and assumptions are based on historical experience and other justified assumptions that are believed to be reasonable under the circumstances at the end of the reporting period and the time when they were made. Although these estimates are based on management's best knowledge of current events and actions, actual results may ultimately differ from those estimates. The estimates and underlying assumptions are reviewed on an ongoing basis and when preparing the financial statements. Changes in accounting estimates may be necessary if there are changes in the circumstances on which the estimate was based, or as a result of new information or more experience. Such changes are recognised in the period in which the estimate is revised.

The key assumptions about the future and key sources of estimation uncertainty that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next 12 months are described in more detail in Note 1.20 below.

1.3 Foreign currency transactions and balances

The Company's presentation and functional currency is euro. Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement within financial items.

1.4 Revenue recognition

Pharmaceutical companies collect revenues in many ways depending on the stage of the drug development process. The Company's main sources of revenue have been upfront payments (one-off license payments), revenues from product sales and milestone payments in accordance with the license agreements in place. Revenue is recognised when the amount of revenue can be measured reliably; when it is probable that the future economic benefits will flow to the Company; and when specific criteria have been met for each of the Company's activities as described below.

1.4.1 Revenue from sales of goods

Revenue from the sale of goods is recognised when the significant risks, rewards and control usually associated with ownership of the goods have been transferred to the buyer. In the period 1 January 2013 to 31 December 2015 Faron has generated revenues from sales of excess inventory (interferon-beta).

1.4.2 Recognition of revenue from upfront payments

Upfront license fees, including signing fees, are usually received when a license is granted. They are deferred and recognised as revenue over the relevant contract period on a basis that is consistent with the services delivered over the relevant contract period.

1.4.3 Recognition of revenue from milestone payments

Revenue associated with performance milestones is recognised based on achievement of the deliverables as defined in the respective agreements. Refundable milestone payments are recorded as deferred income and recognised as revenue at the point of time when the underlying performance obligations have been fulfilled. Non-refundable milestone payments are recognised as revenue when:

- the customer has verifiably accepted that the milestone has been reached;
- Faron has no further performance obligations; and
- there is a reasonable assurance that these receivables can and will be collected.

1.5 Other operating income

Other operating income includes income from activities outside the ordinary business of Faron, such as recognition government grants, service charge income and gains from disposals of non-current assets.

1.6 Research and development costs

All costs related to research activities are presented under the heading research and development expenses in the income statement. Research and development expenses include salaries and other expenditure directly attributable to Faron's

research and development activities. Furthermore, costs attributable to supporting the research and development activities, such as rental expenses for facilities, are included. Research and development expenses are directly related to the development phases of Faron's projects and may therefore fluctuate strongly from year to year.

No internal development expenses related to Company's products and product candidates have yet been capitalised as management considers that the uncertainties inherent in developing pharmaceutical products prohibits the capitalisation of internal development expense as an intangible asset until marketing approval has been received from the relevant regulatory agencies.

Costs incurred on internal development projects are recognised as intangible assets as at the date that the internal development project meets the criteria for recognition. See 1.12.2 Intangible assets.

1.7 Employee benefits

Faron's employee benefits currently consist of short-term employee benefits and post-employment benefits (defined contribution pension plans).

Short-term employee benefits, i.e. salaries, social security contributions, paid annual leave and sick leave, bonuses and non-monetary benefits, are accrued in the year in which the related service is provided. A liability is recognised for the amount expected to be paid if Faron has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

A defined contribution plan is a pension plan under which Faron pays fixed contributions into a separate entity. Faron has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods. The contributions are recognised as employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

1.8 Share based payments

Share-based incentive programmes under which Board members and Key employees have the option to purchase shares in the Company (equity-settled share-based payment arrangements) are measured at the equity instrument's fair value at the grant date.

The cost of equity-settled transactions is determined by the fair value at the date of grant using the Black-Scholes valuation model. The cost is recognised together with a corresponding increase in equity over the vesting period being the period in which the performance and service conditions are fulfilled. The fair value determined at the grant date of the equity-settled share-based payment is expensed on a straight line basis.

No expense is recognised for grants that do not ultimately vest. The assumptions and best estimates for calculating the fair value of share-based payment transactions are disclosed in the notes.

1.9 Operating result

IFRS allows the use of additional line items and subtotals in the income statement. Faron has defined its operating result to be a relevant subtotal in understanding the Company's financial performance. Faron's, operating result is the net sum which is formed by adding other operating income to revenue and then deducting research and development expenses as well as administrative expenses. All other items of the income statement are presented below the operating result.

1.10 Loss per share

Basic loss per share is calculated by dividing the net loss attributable to Shareholders by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the Company and held as treasury shares.

Diluted loss per share is calculated by adjusting the weighted average number of ordinary shares outstanding assuming conversion of all dilutive potential ordinary shares.

1.11 Income taxes

The income tax expense for the period consists of current and deferred taxes. Tax is recognised in the income statement, except for the income tax effects of items recognised in other comprehensive income or directly in equity, which is similarly recognised in other comprehensive income or equity. The current income tax charge is calculated on the basis of the tax rates and laws enacted or substantively enacted in the countries where Faron operates and generates taxable income. Management establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities. Deferred tax is provided using the liability method on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, deferred tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss. Faron's major temporary differences arise from tax losses carried forward and research expenditure incurred not yet deducted for tax purposes.

Deferred tax liability tax is generally provided for in full. Deferred tax assets are recorded up to the amount that represents probable taxable income received in the future and against which temporary differences can be utilised. The amount and probability of the utilisation of deferred tax assets are reviewed at the end of each reporting period.

Deferred taxes are determined using tax rates (and laws) enacted or substantively enacted by the balance sheet date in the respective countries and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

1.12 Equipment and intangible assets

1.12.1 Equipment

Currently Faron does not own any land or buildings. Equipment that Faron owns comprises of mainly office equipment and personal computers. Equipment is stated at historical cost less depreciation and any impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Repairs and maintenance costs are expensed as incurred.

Depreciation is calculated using the straight-line method to allocate each item's cost to its residual value over its estimated useful life.

The depreciation expense is included in the costs of the functions using the asset.

1.12.2 Intangible assets

Faron's intangible assets include patents and internally developed intellectual property ("documentation-related assets"). An intangible asset is recognised only if it is probable that the future economic benefits attributable to the asset will flow to Faron and the cost of the asset can be measured reliably. All other expenditure is expensed as incurred. These intangible assets are initially recognised at cost. Cost comprises the purchase price and all costs directly attributable to bringing the asset ready for its intended use. Subsequently intangible assets are carried at cost less amortisation and any accumulated impairment losses.

Internally generated intangible assets arising from development are recognised if, and only if, all the criteria for recognition are fulfilled:

- it is technically feasible to complete the intangible asset so that it will be available for use;
- there is an ability to use or sell the intangible asset;
- it can be demonstrated how the intangible asset will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use or sell the intangible asset are available; and
- the expenditure attributable to the intangible asset during its development can be reliably measured.
- The internally developed documentation asset is related to the re-development of the Active Pharmaceutical Ingredient, API ("API documentation") The development activities and documentation relate to stability testing of a drug substance (API), that is sellable as such, but the quality and value of which improves as the stability is proven and documented. In addition to its own use, Faron may also, for a fee, license the documentation to companies that can utilise documentation in their own drug candidate approval and registration documentation. Provision of such access does in no way limit Faron's ability to use the documentation in its own application processes or ability to give such access to additional users.

Intangible assets are amortised over their expected or known useful lives on a straight-line basis beginning from the point they are available for use. The estimated useful life is the lower of the legal duration and the economic useful life. The estimated useful lives of intangible assets are regularly reviewed. The estimated useful life for intangible assets is currently 10 years. The effect of any adjustment to useful lives is recognised prospectively as a change of accounting estimate. Intellectual property-related costs for patents are part of the expenditure for the research and development projects.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each financial year.

Internal research costs are those costs incurred for the purpose of gaining new scientific or technical knowledge and understanding. Such costs are always expensed as incurred. Internal development costs are those costs incurred for the application of research findings or other knowledge to plan and develop new products for commercial production. As the drug product development projects undertaken by Faron are subject to technical feasibility, regulatory approval and other uncertainties, these criteria are considered to be met only after Faron has filed its submission to the regulatory authority for final approval after which all subsequent development costs will be capitalised. Before this trigger point all drug product related development costs are typically expensed as incurred. Faron has not capitalised any drug product related development expenditure as the related criteria have not been met yet. Development costs expensed in prior financial years are not capitalised at a later date.

1.13 Impairment of non-financial assets

Assets that are subject to depreciation/amortisation are reviewed for impairment whenever there are any indications

that the carrying amount may not be recoverable. As a clinical stage drug discovery and development company Faron pays attention to the following factors, among others: changes in the legal framework covering patents, rights or licences, change in the useful lives of similar assets, relationship with other intangible or tangible assets and, other factors that indicate that the value of a tangible or an intangible asset has been impaired.

Intangible assets that have an indefinite useful life or intangible assets not ready for use are not subject to amortisation and are tested for impairment annually or 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. The value in use represents the discounted future net cash flows expected to be derived from an asset. Any reductions are reported in the income statement as an impairment loss.

1.14 Government grants

Faron has received government grants from the EU (Commission's FP7 programme).

Grants from governments or similar organisations to support certain projects are accounted for as grants related to income. They are initially recognised at their fair value. Those grants are deferred and recognised in the income statement over the period necessary to match them with the costs that they are intended to compensate, when management has reasonable assurance that the grant will be received and Faron will comply with the conditions attached to that grant. Such grants are presented as other operating income.

Grants for the acquisition of equipment and intangible assets would be deducted from the cost of the asset in question. So far Faron has not received any such grants.

If, at the balance sheet date, the conditions are believed to be fulfilled and the related grant payments are outstanding, grant receivables are shown in the balance sheet.

1.15 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the first-in, first-out (FIFO) method. The cost of finished goods comprises purchase price and other directly attributable costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

Inventories consist of GMP[2] manufactured drug ingredient API (Active Pharmaceutical Ingredient), acquired primarily for research and development purposes to be processed into IMP (Investigational Medicinal Product). However, it also has alternative use, i.e. the ingredient is traded by other companies and consequently may be sold in the market. Faron has sold API over the reporting periods to pharmaceutical companies.

1.16 Financial assets

Faron's financial assets consist principally of cash and cash equivalents.

The classification of a financial asset depends on the purpose for which the financial asset was acquired. Management determines the classification of its financial assets at initial recognition.

Cash and cash equivalents are recognised at cost. They include cash in hand and bank balances if they are readily convertible to known amounts of cash, are not subject to significant changes in value and have a maturity of three months or less from the date of acquisition. Any bank overdrafts are shown within borrowings in current financial liabilities.

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market nor held by the Company for trading. Trade receivables and other financial receivables are included in this category. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period.

Trade receivables are amounts due from customers for signing fees, milestone payments or services performed (including reimbursable costs) in the ordinary course of business. Trade receivables are carried at the original invoice amount less allowances made for doubtful receivables, discounts and rebates and similar allowances, when applicable. Impairment is recognised on doubtful receivables based on individual assessment of potential identified credit risk where there is objective evidence that Faron will not be able to collect all amounts due. Credit losses are recognised in the income statement and presented under costs allocated to functions. Interest income is recognised using the effective interest method and recorded in financial income.

Financial assets are derecognised when Faron loses the rights to receive the contractual cash flows on the financial asset or it transfers substantially all the risks and rewards of ownership outside Faron.

1.17 Financial liabilities and equity

Faron classifies an instrument, or its component parts, on initial recognition as a financial liability or an equity instrument in accordance with the substance of the contractual arrangement and the definitions of a financial liability and an equity instrument.

1.17.1 Bank borrowings

Borrowings are initially recognised at fair value, less any directly attributable transaction costs. Subsequently borrowings are carried at amortised cost using the effective interest method.

Borrowings are presented as current liabilities unless Faron has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting period. Borrowings (or part of the liability) is not derecognised until the liability has ceased to exist, that is, when the obligation identified in a contract has been fulfilled or cancelled or is no longer effective.

Fees paid on the establishment of loan facilities are recognised as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred until the draw-down occurs. To the extent there is no evidence that it is probable that some or all of the facility will be drawn down, the fee is capitalised as a pre-payment for liquidity services and amortised over the period of the facility to which it relates.

1.17.2 Government loans

Faron has two government loans with a below-market rate of interest from Tekes (The Finnish Funding Agency for Technology and Innovation). The loans have been withdrawn before the date to transition to IFRS (i.e. prior to 1 January 2012). Based on the exemption under IFRS 1, Faron has measured the government loans using the previous FAS book value as the carrying amount of the loan and as such has not accounted for the below-market grant separately. Subsequently, the loans are carried at amortised cost using the effective interest rate. In December 2015 Tekes made a positive decision regarding a €1.5 million development loan for funding of the pre-clinical development of Clevegen®. As at 31 December 2015 the loan agreement was not signed.

1.17.3 Convertible notes

Faron analyses the contractual terms and substance of convertible notes to classify each instrument, or its component parts, as a financial liability or an equity instrument.

If the instrument does not contain a contractual obligation to deliver cash or other financial assets, and it can be converted to a fixed amount of the Company's shares, it is classified as equity. If the conversion option is to a variable amount of the Company's shares, and it includes contractual obligation to deliver cash, the instrument is a liability that contains embedded derivatives, and it is therefore classified as a financial liability at fair value through profit or loss in its entirety.

If the instrument is classified as equity, it is recognised at cost and it is not re-measured subsequently. If the instrument is classified as a financial liability at fair value through profit or loss, it is measured initially and subsequently at fair value, and fair value changes are recognised in the income statement as finance income or costs in the period in which they occur. On conversion to equity, the liability is transferred to equity.

All convertible notes have been converted into ordinary shares by the end of January 2015.

1.17.4 Equity

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds of the share issue. The portion of costs attributable to the stock market listing in November 2015, or are otherwise not incremental and directly attributable to issuing new shares, are recorded as an expense in the income statement.

Reserve for invested unrestricted equity is credited with other equity inputs as well as that part of the subscription price of the shares that according to the explicit decision is not to be credited to the share capital.

1.18 Leases

Faron as a lessee

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

Leases where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the lease term.

1.19 Provisions and contingent liabilities

A provision is recognised when Faron has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Faron had no provisions at the end of the reporting periods presented in these financial statements.

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

1.20 Critical accounting estimates and management judgments made in applying accounting policies

1.20.1 Revenue recognition

Due to the nature of the pharmaceutical development business, Faron's collaboration and licence contracts are complex and these contracts often require significant analysis and judgement by management in order to determine the appropriate method of revenue recognition.

Contracts may consist of multiple components with the underlying services and goods delivered at different times over a contract's lifetime representing separate earnings processes. Revenue is allocated to the separate components on a relative fair value basis and revenue is recognised when the criteria for revenue recognition is met for each component. Non-refundable milestones are recognised as revenue when the milestone has been achieved and the Company does not have future obligations. This is normally when the Company is informed by the contract party that the milestone has been achieved. Any milestone payments that have been received but for which earnings process has not been completed are reported as deferred revenue in the balance sheet/statement of financial position and recognised as revenue when the service/goods has been delivered is complete and there are no remaining obligations or contingencies. For some transactions this may result in recognising cash receipts initially as deferred income and then released to income over subsequent financial years on the basis of meeting the conditions further specified in each individual agreement.

1.20.2 Research and development expenses

Faron follows IFRS guidance to determine whether development costs qualify for capitalisation. This determination requires significant judgement. When an internal development project fulfills the criteria for capitalisation, costs incurred are capitalised from that point forward. The in-process development project is then tested for impairment annually and whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. It is Faron's view that drug product related development expenses may not be capitalised until marketing approval has been received from the relevant regulatory agencies, as this is considered to be the first point at which it may be concluded that future revenues can be generated.

According to management's judgement, the internally developed documentation asset that is related to the re-development of the Active Pharmaceutical Ingredient, API ("API documentation"), fulfills the criteria of IFRS for capitalising costs of internally developed intangible assets despite the nature of the Company's operations where capitalisation criteria is traditionally met at the receipt of regulatory approval. The development activities and documentation relate to stability testing of a drug substance (API) that is sellable as such, even though it is primarily used in the development process. The quality and value of the drug substance improves as the stability is proven and documented. In addition to its own use, Faron may also, for a fee, license the documentation to companies that can utilise documentation in their own drug candidate approval and registration documentation. The costs of this internally developed intangible asset have been capitalised as of the criteria for capitalisation was fulfilled.

1.20.3 Deferred taxes

Recognition and measurement of deferred tax assets and deferred tax liabilities include management estimates, especially for deferred tax assets arising from tax losses carried forward. Deferred tax assets are recognised for deductible temporary differences to the extent that it is probable that taxable profit will be available against which deductible temporary differences can be utilised. Various internal and external factors may have favorable or unfavorable effects on the deferred tax assets and liabilities. These factors include, but are not limited to, available tax strategies, changes in tax laws, regulations and/or rates dealing with e.g. recoverability periods for tax loss carry-forwards, changing interpretations of existing tax laws or regulations, future levels of research and development spending and changes in overall levels of pre-tax earnings. Such changes that arise could impact the assets and liabilities recognised in the balance sheet in future periods. All tax liabilities and assets are reviewed at the end of the reporting period and changes are recognised in the income statement. Faron has not recorded any deferred tax assets on tax losses carried forward.

1.20.4 Inventories

Measurement of inventories includes some management estimates. Inventories are measured at lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the

sale. Net realisable value is used in testing the recoverable amount of inventories in order to avoid the inventories being carried in excess of amount expected to be realised from their sale or use.

Management has assessed, that GMP[3] manufactured drug ingredient also fulfills the criteria of IFRS to be classified as inventory. Even though it has been acquired mainly for research and development purposes to be processed into API (Active Pharmaceutical Ingredient) and it is not currently Faron's core business to actively market the ingredient, as it also has alternative use, i.e. the ingredient is traded by other companies and Faron has also traded API, management has recorded the API in its inventory.

1.20.5 Adoption of new and amended standards and interpretations applicable in future financial years

Faron has not yet adopted the new and amended standards and interpretations already issued by the IASB but that are not effective for financial year 2015. The Company will adopt them as of the effective date or, if the date is other than the first day of the financial year, from the beginning of the subsequent financial year. The Company has presented below only the standards that are relevant to the Company and might have impact on its financial statements in its current operations.

*= not yet endorsed for use by the EU as of 31 December 2015.

- IFRIC 21 Levies (effective for financial years beginning on or after 17 June 2014): The interpretation addresses the accounting for a liability to pay a levy recognised in accordance with IAS 37 Provisions, and the liability to pay a levy whose timing and amount is certain. The amendment does not have a material impact on the Company's financial statements.

- Annual Improvements to IFRSs (2010-2012 and 2011-2013 cycles*) (effective for financial years beginning on or after 1 July 2014): The annual improvements process provides a mechanism for minor and non-urgent amendments to IFRSs to be grouped together and issued in one package annually. These amendments cover several standards and their impacts vary standard by standard but the Company considers that they do not have a significant impact on the financial statements of Company.

- Amendments to IAS 1 Presentation of financial statements (effective for financial years beginning on or after 1 January 2016): The amendments clarify guidance in IAS 1 on materiality and aggregation, the presentation of subtotals, the structure of financial statements and the disclosure of accounting policies. The Company is still assessing the possible impact of the amendments to its financial statements.

- IFRS 15 Revenue from contracts with customers* (effective for financial years beginning on or after 1 January 2017): The standard covers revenue recognition and will supersede current revenue recognition standards, IAS 18 and IAS 11. The Company is still to assess the impacts of the standard.

- IFRS 9 Financial Instruments* (effective for financial years beginning on or after 1 January 2018): The standard will replace IAS 39 fully (even though some areas are moved from IAS 39 to IFRS 9 unchanged). Main changes are: Financial assets are classified based on entity's business model. Impairment will be recognised based on expected losses from the first reporting date that the assets measured at amortised cost are on the balance sheet. Hedge accounting will be aligned more closely with risk management. The Company is still to assess the impacts of the standard.

[1] Acute Respiratory Distress Syndrome, ARDS.
[2] GMP = Good Manufacturing Practice.
[3] GMP = Good Manufacturing Practice.

NOTE 2
2.1 Principles of financial risk management

Faron's activities expose it to a variety of financial risks as follows:

In 2015 Faron received new equity, less direct costs, to the amount of EUR 18,080,000. This new capital significantly reduced the liquidity risk for the Company in the near future.

In 2012 the European Commission awarded a EUR 5,963,000 grant to the Faron network (Consortium) to support the FP-1201-lyo clinical Phase III programme ("Traumakine®"). The Consortium consists of the European Commission as a granting agency, Faron as a coordinator and three other participating partners of the Traumakine® programme; University College London Hospital (UCLH), University of Torino and University of Turku. The first payment under the grant, received in 2013, amounted to EUR 1,693,000, of which EUR 660,000 has been recognised as other operating income. The second grant payment, EUR 1,018,000 was received at the end of 2014, of which EUR 110,000 has been recognised as other operating income. In 2015, EUR 701,000 was recognised as other operating income.

During 2014 the Company negotiated a two-year extension to the loan and an equal postponement of the instalments of the first government R&D loan from Tekes, for which the first instalment was originally now due in 2014. Tekes provided Faron with an additional two years to make payment in respect to the first instalment which is now therefore due in 2016. Faron also has had a committed credit limit available, up to EUR 800,000, which was ended in 31 December 2015. The management believes that this credit limit can be reopened if required.

These above mentioned funds and financing sources, in addition to expected milestone payments from Maruishi, in 2016 and income from other commercial agreements, will enable Faron to fund its operating expenses as planned during 2016.

A) Goverment loans (R&D loans from Tekes)

The Finnish Funding Agency for Technology and Innovation (Tekes) has granted two loans to the Company. The total amount had been drawn down by the Company by the end of the year 2011. Both loans are government loans with a below-market rate of interest. The total loan periods are 10 years from the draw-down. The interest rate for these loans is the base rate set by the Finnish Ministry of Finance less 1%, however, the interest rate will not fall below a 3% minimum. Repayment of these loans shall be initiated after 5 years, thereafter loan principals shall be paid back in equal installments over the remaining loan period. In certain circumstances Tekes may, at its own discretion, extend the loan terms, convert the loans into capital loans or exempt the Company from repayment following the general terms of the loans. The loans do not include any covenants. The Company has negotiated with Tekes a two-year extension to the loan and an equal postponement of the installments of the first loan.

B) Convertible notes

Faron issued convertible notes in 2014 to strengthen its financial position. These convertible notes were classified in equity, because they contained contractual obligation to deliver cash to the holder only in an event of liquidation of Faron, and the actual conversion rate determined in the contract was fixed. The loan was fully converted to shares in January 2015.

C) Loans

Stated in euro	2015 €'000	2016 €'000	2017 €'000	2018 €'000	Later years €'000	Total €'000
Contractual maturity of loans and their interest payments at 31 Dec						
Non-current financial liabilities						
Government loans						
Repayment of loans	0	245	338	338	770	1 691
Interest expenses	18	16	13	9	9	64
Current financial liabilities						
Government loans, current portion						
Interest expenses						
Bank overdraft facility						
Trade payables	436					436
	453	**260**	**351**	**348**	**779**	**2 191**

The Company intends to finance the repayment of the loans from future cash sources including among others milestone payments from existing agreements, equity issuances and revenue from future lisencing agreements. The loans contain a provision, that if the projects related to the loans turn out to be unsuccesful the lender can forgive the loans either partially or fully.

Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for Faron by failing to discharge an obligation.

Credit risk arises from cash and cash equivalents as well as credit exposures to external parties, including amounts to be invoiced and outstanding receivables.

Currently Faron does business with one external counterparty, Maruishi. Over the coming years, Maruishi funding (milestone payments and reimbursable research expenses) remains critical to Faron's product development programmes and is considered the main area of credit risk. However, this risk is partly mitigated by the fact that Faron's current collaboration partner is a large and internationally reputable pharmaceutical company that is financially solid. These collaborations are normally governed by contractual relationships that typically address and describe remedies for situations in which interests of Faron and the partner are not longer in line.

Faron's cash and cash equivalents are invested primarily in saving and deposit accounts with original maturities of three months or less. These accounts generate a very small amount of interest income. The banks that Faron works with have good (Moody's Aaa) credit ratings.

The Company has not incurred any credit losses over the reporting periods 2012-2015, and management does not expect losses from non-performance by counterparties (for example, Maruishi). Therefore, at present, credit risk is limited.

Faron had no trade receivables by year-end 2012-2014. In the year ended 31 December 2015 there is one invoice which has been outstanding for 2.5 months. No further ageing analysis of trade receivables is presented.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk:

- currency risk
- interest rate risk; and
- other price risk

A) Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument, e.g. a trade receivable, will fluctuate because of changes in foreign exchange rates.

Faron's functional currency is the euro and Faron is exposed to foreign exchange risk arising from currency exposure, currently mainly with respect to the Japanese Yen and pound sterling. The Company receives payments from its main licence partner Maruishi (based in Japan) in Japanese Yen. However, the impact of the foreign exchange risk arising from the Yen exposure is not considered significant in average.

Due to the commencement of the Phase III clinical trials with a UK based Clinical Research Organisation as the main service provider, the Companys' pound sterling denominated expenses and trade payables have become significant. The Company converted most of the pound sterling denominated IPO proceeds into euros immediatelly after the IPO, but held and still holds a sizeable amounts of pound sterling in its pound sterling bank accounts. This forms a natural hedge against euro-pound exchange rate changes, as the funds held in pound sterling roughly match with the estimated pound sterling expenses during 2016. As a result of the sizeable pound sterling holdings, the depreciation of pound sterling against euro had a negative effect on the financial statements. As the exchange rate may move also to other direction during 2016, the management believes that natural hedge strategy best protects the Company from adverse exchange rate changes and this protection overweights short-term currency rate losses.

Other foreign currency denominated trade receivables (and trade payables, if any) are small and short term in nature.The borrowings and other liabilities of Faron are denominated in euro. As the currency exposure and risk is considered significant, the Company established a natural hedging policy to manage the foreign exchange risk against the functional currency of the Company.

B) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Company's interest rate risk arises from long-term borrowings. Faron's borrowings are denominated in euro. The non-current borrowings issued at fixed rates expose the Company to fair value interest rate risk. Interest rate is partially offset by cash held at variable rates which, on the other hand, expose Faron to cash flow interest rate risk. Given that most of the borrowings are government loans with a below-market rate of interest, cash and cash equivalents are very short-term, the impact of interest rate risk on Faron is currently minor, and consequently Faron does not hedge the interest rate risk.

2.2 Capital management

Faron's objectives when managing capital are to safeguard the Company's ability to continue as a going concern and to maintain an optimal capital structure to reduce the cost of capital. The total amount of equity as recognised in the balance sheet is seen and managed as capital by Faron. In order to maintain or adjust the capital structure, Faron may issue new shares or other equity, liability or compound instruments, or sell assets to reduce debt.

To advance the drug development programmes into commercialised pharmaceutical products requires significant financial resources. Faron relies on its ability to fund its operations through three major sources of financing:

1) Equity financing: Faron's funding is partly organised through equity financing. Management monitors liquidity on the basis of the amount of funds. These are reported to the Board regularly.

2) Commercialisation, collaboration and licensing agreements: by entering into said agreements with larger pharmaceutical companies Faron is entitled to receive upfront and milestone-dependent payments from these partners. Activities in the area of business development are targeted at securing such agreements. These activities are integral part of the duties of the management and are monitored by the Board of Directors, which ultimately decides on entering into such agreements.

3) Research and development grants and loans: In addition to the sources of funding described above. Faron also relies on different sources of R&D grants and loans. Various regional, national or EU level institutions provide these funds with the aim of fostering economic and technological progress in the region in which Faron operates. Such funds have been historically available to Faron at substantial levels. Faron is in regular contact with the funding agencies. The availability of such funds in the future cannot be guaranteed.

Faron's Board of Directors approves the operational plans and budget. The Board regularly follows up the implementation of these plans and the financial status.

2.3 Fair value estimation

Some of Faron's accounting policies and disclosures require the measurement of fair values. For Faron this applies primarily to financial assets and liabilities.

For financial instruments that are measured in the balance sheet at fair value, IFRS requires disclosure of fair value measurements by level of the fair value measurement hierarchy. Fair value hierarchy is based on the source of inputs used in determining fair values (used in the valuation techniques) as follows:

- Level 1: fair values are based on quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: fair values are based on market rates and prices, discounted future cash flows etc. Thus inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) are used.
- Level 3: for assets and liabilities in level three, there is no reliable market source available and thus fair value measurement cannot be based on observable market data (unobservable inputs).

When measuring the fair value of an asset or a liability, Faron uses market observable data as far as possible.

NOTE 3
Revenue

In 2014 revenue consisted of income generated from sale of both API and IMP reference materials. In 2015 revenue consisted of milestone income from Maruishi as well as sales of API material samples and analyses materials.

NOTE 4
Segment reporting

Faron is a late clinical stage biotechnology company. Its operations have been focused on the development of its lead drug candidate, Traumakine®. Faron's chief operating decision maker has been identified as the Chief Executive Officer (CEO).

The CEO manages Faron as one integrated business and hence Faron has one operating and reportable segment. Faron's country of operation is Finland.

NOTE 5
Other operating income

Stated in euro	2015 €'000	2014 €'000
Grants from EU	701	111
Grant from Tekes		
Other items		
Total other operating income	701	111

In the year ended 2012, the pan-European "Traumakine®" consortium where Faron Pharmaceuticals is a Coordinator, signed a grant agreement of the EUR 5,963,000 research grant awarded by the European Commission from the Seventh Framework Programme (FP7) to support the FP-1201-lyo clinical Phase III Programme ("Traumakine®"), focusing on a first pharmacological treatment for Acute Respiratory Distress Syndrome (ARDS). The first payment under the grant, received in 2013, amounted to EUR 1,693,000, of which EUR 660,000 has been recognised as other operating income. The second grant payment of EUR 1,018,000 was received at the end of 2014, of which EUR 110,000 has been recognised as other operating income. In 2015, EUR 701,000 was recognised as other operating income.

The Company will defer elements of the grant to the point in which the respective milestones are completed (i.e. the milestones which are set out within the EU Grant agreement). Once these milestones are met, the amount due to the Company is recognised as other operating income.

NOTE 6

Employee benefit expense

Stated in euro	2015 €'000	2014 €'000
Salaries	(940)	(446)
Contributions to defined contribution post-employment plans	(115)	(69)
Social security contributions	(63)	(15)
Share based payments	(474)	
Total employee benefit expenses	**(1,591)**	**(530)**
Average number of personnel		
Finland	6	5
Finland	**6**	**5**

For further information on management remuneration see Note 21 related party transactions. Share based payments are further explained in Note 16.

NOTE 7

Depreciation and amortisation

Stated in euro	2015 €'000	2014 €'000
Depreciation and amortisation allocated to functions		
Research and development	(175)	(60)
Administration	(9)	(0)
Total depreciation and amortisation	(184)	(60)
Depreciation and amortisation by asset categories		
Machinery and equipment	(9)	(0)
Total depreciation	(9)	(0)
Intangible assets		
Patents	(65)	(60)
Other intangible assets	(110)	
Total amortisation	(175)	(60)
Total depreciation and amortisation	**(184)**	**(60)**

The Company has not recorded any impairment losses for the years ended 31 December 2012 to 2015.

NOTE 8
Financial income and expenses

Faron has received two goverment loans for research and development purposes with below-market interest rate from Tekes (The Finnish Funding Agency for Technology and Innovation). Both loans were withdrawn before the date of transition to IFRS (i.e. prior to 1 January 2012). Thus, based on the exemption under IFRS 1, Faron has measured the government loans using the previous FAS carrying amount as the carrying amount of the loan. Subsequently, both loans are carried at amortised cost using the effective interest rate.

Other significant financial expense items are the exchange rate losses when transferring GBP to euro, when issuing the new shares upon Admission to AIM, expenses on loan guarantees, interest on convertible loans and credit limit interest from bank.

See also Note 2 Financial risk management.

Stated in euro	2015 €'000	2014 €'000
Financial income		
Interest from bank balances	0	0
Interest from account receivables		15
Total financial income	0	15
Financial expenses		
Interest on government loans (Tekes)	(18)	(15)
Fair value changes of convertible bonds		
Interest expenses on convertible bonds	(9)	(67)
Interest on bank loans	(10)	(26)
Interest on accounts payables	(1)	(1)
Exchange rate losses	(247)	(1)
Bank guarentee costs and provisions	(27)	(35)
Total financial expenses	(311)	(146)
Total financial income and expenses	**(311)**	**(131)**

NOTE 9

Income taxes

Stated in euro	2015 €'000	2014 €'000
Withholding tax	(42)	(6)
Total income taxes	(42)	(6)

Withholding taxes paid in the year ended 31 December 2014 relate to payments of advisory fees to the non-Finnish members of the Clinical trial Steering Group. Taxes paid in the year ended 31 December 2015 relate to milestone payment from Maruishi.

Stated in euro	2015 €'000	2014 €'000
Reconciliation of effective tax rate *The Finnish corporate tax rate applied was 20%.*		
Loss before income tax	(6 188)	(1 358)
Tax using Faron's domestic corporate tax rate	1 238	272
Current-year losses for which no deferred tax asset is recognised	(1 238)	(272)
Taxes in the income statement		

Items for which Faron has not recognised a deferred tax asset		
R&D expenses not yet deducted in taxation[1]	2 816	2 816
The tax losses carried forward approved by tax authorities[2]	5 663	3 164
Deductible temporary differences for which no deferred assets have been recognised	8 479	5 979

[1] Faron has incurred research and development costs in the financial years ended 31 December 2010 and 2011 that have not yet been deducted in its taxation. The amount can be deducted over an indefinite period with amounts that the Company may freely decide.

[2] These losses expire over the years 2019 to 2024. The amount presented for the year ended 31 December 2015 does not include the deductible temporary difference arisen from the net loss for the financial year 2015 as the related loss has not yet been approved by tax authorities by the time of preparation of these financial statements.

The related deferred tax assets have not been recognised due to the uncertainty as to whether they can be utilised.

NOTE 10
Loss per share

Basic

Basic loss per share is calculated by dividing the loss attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

	2015	2014
Loss attributable to equity holders of the Company (EUR 1,000)	(6 188)	(1 364)
Weighted average number of ordinary shares in issue	20 686 854	15 012 262
Basic (and dilutive) loss per share, EUR	(0,30)	(0,09)
Weighted-average number of ordinary shares		
Issued ordinary shares at 1 January	15 456 250	14 570 680
Effect of shares issued	5 230 604	441 582
Weighted-average number of ordinary shares at 31 December	20 686 854	15 012 262

Diluted

Diluted loss per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares.

	2015	2014
Loss attributable to equity holders of the Company (EUR 1,000)	(6 188)	(1 364)
Interest adjustment	9	67
Convertible loan interest adjusted loss attributable to equity holders	(6 179)	(1 297)
Diluted weighted average number of ordinary shares in issue	20 686 854	15 406 329
Basic loss per share, EUR	(0,30)	(0,09)
Weighted-average number of ordinary shares		
Issued ordinary shares at 1 January	15 456 250	14 570 680
Effect of shares issued	5 230 604	441 582
Weighted-average number of ordinary shares at 31 December	20 686 854	15 012 262
Dilution effect of convertible loans	-	394 067
Diluted weighted-average number of ord. shares at 31 December	20 686 854	15 406 329

NOTE 11
Machinery and equipment and intangible assets

Machinery and equipment

Stated in euro	2015 €'000	2014 €'000
Cost		
Balance at 1 January		
Cost	2	2
Additions	37	
Disposals		
Transfers		
Balance at 31 December	39	2
Accumulated depreciation / amortisation and impairment		
Balance at 1 January	(1)	(1)
Depreciation / amortisation (Note 7)	(9)	(0)
Balance at 31 December	(11)	(1)
Net book value at 1 January	**0**	**1**
Net book value at 31 December	**28**	**0**

Patents

Stated in euro	2015 €'000	2014 €'000
Cost		
Balance at 1 January		
Cost	646	602
Additions	70	44
Disposals		
Transfers		
Balance at 31 December	716	646
Accumulated depreciation / amortisation and impairment		
Balance at 1 January	(369)	(309)
Depreciation / amortisation (Note 7)	(65)	(60)
Balance at 31 December	(434)	(369)
Net book value at 1 January	**277**	**293**
Net book value at 31 December	**283**	**277**

Documentation assets in process

Stated in euro	2015 €'000	2014 €'000
Cost		
Balance at 1 January		
Cost	907	800
Additions		107
Disposals		
Transfers		
Balance at 31 December	907	907
Accumulated depreciation / amortisation and impairment		
Balance at 1 January		
Depreciation / amortisation (Note 7)	(188)	
Balance at 31 December	(188)	
Net book value at 1 January	**907**	**800**
Net book value at 31 December	**719**	**907**

Total intangible assets

Stated in euro	2015 €'000	2014 €'000
Cost		
Balance at 1 January		
Cost	1 553	1 403
Additions	70	152
Disposals		
Transfers		
Balance at 31 December	1 623	1 555
Accumulated depreciation / amortisation and impairment		
Balance at 1 January	(369)	(310)
Depreciation / amortisation (Note 7)	(253)	(60)
Balance at 31 December	(622)	(370)
Net book value at 1 January	**1 922**	**1 714**
Net book value at 31 December	**1 001**	**1 184**

Total machinery and equipment and intangible assets

Stated in euro	2015 €'000	2014 €'000
Cost		
Balance at 1 January		
Cost	1 555	1 405
Additions	107	152
Disposals		
Transfers		
Balance at 31 December	1 662	1 557
Accumulated depreciation / amortisation and impairment		
Balance at 1 January	(370)	(312)
Depreciation / amortisation (Note 7)	(262)	(60)
Balance at 31 December	(632)	(372)
Net book value at 1 January	**1 925**	**1 717**
Net book value at 31 December	**1 029**	**1 185**

Finance leases

The company does not have any finance leases.

Documentation assets

The cost of the documentation arisen in conjunction to the development work of Faron is recorded in intangible assets. This documentation consists of API documentation1 (see Note 1, 1.12.2 Intangible assets for further details).

Faron has completed these assets in 2014.

Orphan drug status

Faron has been granted an orphan drug status for the treatment of ALI/ARDS with interferon beta by the European Commission and the European Medicines Agency (EMA) under the registration number EU/3/07/505. The orphan drug status granted by the EMA entitles the holder an exclusive right for the marketing and sales of drugs within the European Union for 10 years as from the grant date of the approval. This status is transferable. No costs related to this status have been capitalised. Thus the orphan drug status represents an off-balance sheet asset.

NOTE 12
Inventories

Stated in euro	2015 €'000	2014 €'000
Finished goods	649	699
Inventories total	649	699

Inventories consists of deep-frozen bags of active pharmaceutical ingredient used in production of FP-1201-lyo, which have a limited expiry time, which can be extended by conducting additional stability studies.

The cost of inventories is recognised as an expense and included in the line item "Cost of sales" amounted to EUR 100,000 (2014: zero; 2013: zero).

The Company has not recorded any impairment losses in years from 2012 to 2015.

NOTE 13
Current receivables

Stated in euro	2015 €'000	2014 €'000
Trade receivables	37	
Prepayments	1 248	
Accrued items	17	23
Other receivables	773	16
Total trade and other receivables	**2 074**	**40**

The majority of prepayments relate to the Clinical Service Agreement with the clinical research organisation (CRO) GAEA Clinical, which is the main service provider for the INTEREST Study. The other receivables consist mainly of the EU FP7 grant income as described in Note 4.

NOTE 14
Cash and cash equivalents

Stated in euro	2015 €'000	2014 €'000
Bank balances	11 068	242
Total cash and cash equivalents	11 068	242

NOTE 15
Equity and reserves

Equity and reserves	Number of shares (pcs)	Share capital (1,000 €)	Reserve for invested non-restricted equity (1,000 €)	Total (1,000 €)
In issue at 1 January 2013	1 453 380	1 296	5 328	6 624
Conversion of convertible notes to shares	3 688	120	0	120
Issued for merger consideration	1 000 000	0	0	0
Cancelled in merger	-1 000 000	0	0	0
31 December 2013	1 457 068	1 416	5 328	6 744
Share issues, issued for cash	35 424	1 275	0	1 275
Issue of convertible equity instrument	0	0	1 126	1 126
Warrants issue	53 133	0	0	0
31 December 2014	1 545 625	2 691	6 453	9 144
Share base payments	0	0		0
Convertible issue	78 166			0
Share issues for cash	302 764		5 050	5 050
Total	1 926 555			0
Split 1:10	19 265 550			0
Emission of new shares	3 846 154		13 030	13 030
31 December 2015	23 111 704	2 691	24 533	27 224

Faron Pharmaceuticals Ltd has one class of shares. The shares amounted to 1,545,625 at 1 January 2015. The following increases were made during 2015:

a) On 24 February 2015, the number of Ordinary Shares was increased to 1,623,791 by the issue of 78,166 new Ordinary Shares at a subscription price of €14.40. The shares were issued due to conversion of the 2014 convertible loan, which so became fully converted. The subscription price was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased. The conversion did not have a cash effect in 2015;
On 19 May 2015, the number of Ordinary Shares was increased to 1,843,356 by the issue of 219,565 new Ordinary Shares at a subscription price of €15.41. The subscription price was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased;

b) By a Board resolution on 6 May 2015 and pursuant to an authority granted to the Board at the Annual General Meeting held on 16 March 2015, on 19 May 2015 the number of Ordinary Shares was increased to 1,843,356 Ordinary Shares by the issue of 219,565 new Ordinary Shares at a subscription price of €15.41 per Ordinary Share. The subscription price was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased;

c) By a Board resolution on 28 May 2015 and pursuant to an authority granted to the Board at the Annual General Meeting held on 16 March 2015, on 9 June 2015 the number of Ordinary

Shares was increased to 1,926,555 Ordinary Shares by the issue of 83,199 new Ordinary Shares at a subscription price of €20.03 per Ordinary Share. The subscription price was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased;

d) by a resolution of the Extraordinary General Meeting held on 15 September 2015, on 17 September 2015 the number of Ordinary Shares was increased to 19,265,550 by the issue of 17,338,995 new Ordinary Shares to the Shareholders without payment in proportion to their holdings so that nine Ordinary Shares were issued for each existing Ordinary Share (the "Share Split");

e) by a resolution of a Board Meeting held on 16 September 2015 made pursuant to an authority granted to the Board of Directors at the Extraordinary General Meeting held on 15 September 2015, on 16 September 2015 the Company issued 151,400 warrants (each warrant representing an entitlement to subscribe for one Ordinary Share) to Whitman Howard (which were subscribed for by and issued to Whitman Howard on 16 September 2015). The warrants are divided into two tranches: in the first tranche, 109,800 warrants with a subscription price of [£0.87] ("A Warrants"), and in the second tranche, 41,600 warrants with a subscription price of [£1.43] ("B Warrants"). Any "A" Warrants shall be exercised during the subscription period commencing on 2 November 2015 and ending on 7 May 2018. Any "B" Warrants shall be exercised during the subscription period commencing on 2 November 2015 and ending on 28 May 2018;

f) by a resolution of the Extraordinary General Meeting held on 15 September 2015, the Company adopted the 2015 Share Option Plan and granted the Options detailed in paragraph 5.5 below to the Directors;

g) by a resolution of a Board Meeting held on 11 November 2015 made pursuant to an authority granted to the Board of Directors at the Extraordinary General Meeting held on 15 September 2015, the Company resolved to issue (i) 2,417,113 Ordinary Shares without payment into treasury, in order for such Ordinary Shares to be transferred to Placees pursuant to the Placing on a delivery versus payment basis on Admission, (ii) 44,044 Ordinary Shares as VCT Shares and EIS Shares pursuant to the Placing, and (iii) 1,384,997 Ordinary Shares as Subscription Shares pursuant to the Subscription.

The Company was listed on the London Stock Exchange in November 2015. The share has no nominal value. Each share entitles the holder to one vote at the Annual General Meeting. All shares entitle holders to an equal dividend.

At the 31 December 2015 Faron's share capital, entered in the Finnish trade register, amounted to EUR 2,691,000.

Details on the management shareholding are disclosed in Note 21 Related party transactions.

Nature and purpose of reserves

Share capital

The subscription price of a share received by the Company in connection with share issues is credited to the share capital, unless it is provided in the share issue decision that a part of the subscription price is to be recorded in the fund for invested non-restricted equity. The proceeds received by Faron from the conversion of the convertible bonds have been credited to share capital.

Fund for invested non-restricted equity

The fund for invested non-restricted equity includes other equity investments, for which part of the subscription price of the shares according to the related decision is not to be credited to the share capital and issuance of convertible capital loans.

Faron has not paid any dividends over the years.

NOTE 16
Share options

The Company adopted its 2015 option plan on 15 September 2015 ("Option Plan") as described in full in the Company's Admission Document. Under the Option Plan, options may be granted in four different tranches (A, B, C and D), each of which may be subscribed for and exercised in different periods. Each option will entitle the holder of the option to subscribe for one ordinary share in the Company. An aggregate maximum number of 1,600,000 options may be granted under this plan, such aggregate being made up of a maximum of 400,000 "A" Options, the subscription period for which ends on 31 December 2015 (exercisable between 2 November 2015 and 30 September 2021), a maximum of 400,000 "B" Options to be subscribed for between 8 October 2016 and 30 September 2019 (exercisable between 8 October 2016 and 30 September 2021), a maximum of 400,000 "C" Options to be subscribed for between 8 October 2017 and 30 September 2019 (exercisable between 8 October 2017 and 30 September 2021), and a maximum of 400,000 "D" Options to be subscribed for between 8 October 2018 and 30 September 2019 (exercisable between 8 October 2018 and 30 September 2021).

The terms of the 2015 option plan require that the option holder remains in the Company's service until the beginning of the subscription period. The exercise price for Ordinary Shares based on "A" Options is €3.71. The exercise price for ordinary shares based on tranches "B", "C" and "D" Options shall be determined by the euro equivalent to the average share price of the publicly traded ordinary shares of the Company on AIM between 1 July and 30 September of 2016, 2017 and 2018 respectively.

Faron has no legal or constructive obligation to repurchase or settle the options in cash, accordingly, the arrangements have been classified as equity settled share-based payments.

Transactions during 2015

Option under the 2015 Option Plan

Option tranche	A	B	C	D	Total	Average exercise price in €
Status	Granted	Allocated*	Allocated*	Allocated*		
Outstanding at 1 Jan.	0	0	0	0	0	
Amount	250 000	250 000	250 000	250 000	1 000 000	4.32
Forfeited	0	0	0	0	0	
Exercised	0	0	0	0	0	
Outstanding at 31 Dec.	**250 000**	**250 000**	**250 000**	**250 000**	**1 000 000**	**4.32**

*Subscription for these options is conditional on the Director/employee remaining in their role at the time of commencement of the relevant subscription period.

Warrants

Warrant tranche	A	B	Total	Average exercise price in €
Status	Granted	Granted		
Outstanding at 1 Jan.	0	0	0	
Granted	109 800	41 600	151 400	1.68
Forfeited	0	0	0	
Exercised	0	0	0	
Outstanding at 31 Dec.	**109 800**	**41 600**	**151 400**	**1.68**

During 2015 the Company granted warrants over 151,400 ordinary shares. The warrants are divided into two tranches: in the first tranche, 109,800 warrants with a subscription price of €1.55 (“A Warrants”), and in the second tranche, 41,600 warrants with a subscription price of €2.01 (“B Warrants”). Any “A” Warrants shall be exercised during the subscription period commencing on 2 November 2015 and ending on 7 May 2018. Any “B” Warrants shall be exercised during the subscription period commencing on 2 November 2015 and ending on 28 May 2018.

Calculation of the share-based payment expense in the income statement

Accounting for share-based payments under IFRS 2 requires Faron to take into account all the options and warrants, both granted and allocated. In the calculation of the share-based payment expense the options and warrants were treated as one pool.

The estimated average fair value of options and warrants granted and allocated during the period was €0.96 per option.

Out of 1,151,400 granted and allocated options and warrants, 401,400 were exercisable as at 31 December 2015. None were exercised in 2015. The maximum number of ordinary shares which could be issued in the event of all options under the 2015 option plan being allocated, subscribed for and exercised together with exercise of the outstanding warrants outstanding, amounts to 1,751,400 shares.

The grant date fair value of the options were determined using the Black-Scholes valuation model.The significant inputs into the model were share price, exercise price, volatility and the annual risk-free interest rate as shown in the table below.

Plan and month of grant	Years of vesting	Contractual months remaining	Share price €	Estimated excercise price €	Volatility	Risk-free interest rate
A Options - Sept 2015	2015-2021	69	2.69	3.71	50%	0.01%.
B Options - Sept 2015	2016-2021	69	2.69	4.10	50%	0.01%
C Options - Sept 2015	2017-2021	69	2.69	4.51	50%	0.01%
D Options - Sept 2015	2018-2021	69	2.69	4.96	50%	0.01%
Warrants A - Sept 2015	2015-2018	29	2.69	1.55	50%	0.01%
Warrants B - Sept 2015	2015-2018	29	2.69	2.01	50%	0.01%

The total expense recognised in the income statement for share options is EUR 474,000 in 2015. 2015 is the Company's first year to issue options.

Accounting for share-based payments under IFRS 2 requires Faron management to use judgment in determining whether a transactions settled in entity's own equity instruments include share-based payments. In addition, management uses judgment in determining the attribution model in the financial statements, including, for example, estimates of future forfeitures. Measuring the fair value of equity instruments granted requires management to use judgment on appropriate inputs into option pricing model, e.g. share price at grant date, volatility and interest rates.

NOTE 17
Non-current financial liabilities and other liabilities

Stated in euro	2015 €'000	2014 €'000
Interest-bearing financial liabilities		
Tekes loan	1 446	1 691
Convertible notes		
Total non-current financial liabilities	**1 446**	**1 691**
Other non-current liability		
Total other non-current liabilities		
Total non-current financial liabilities	**1 446**	**1 691**

Further information on Faron's financial liabilities and related arrangements is presented in Note 2 Financial risk management. See also Note 18 Current financial liabilities and other liabilities below.

NOTE 18
Current financial liabilities and other liabilities

Stated in euro	2015 €'000	2014 €'000
Interest-bearing financial liabilities		
Convertible notes		
Goverment loans (current portion)	245	
Bank overdraft facility		
	245	
Non-interest-bearing financial liabilities		
Trade payables	436	9
	436	9
Other liabilities		
Prepayment	973	1 456
Accrued expenses	515	150
Other liabilities	29	46
	1 517	1 652
Total current financial liabilities and other liabilities	**2 198**	**1 662**

The item "Prepayments" above comprises portions of the awarded EU grant, received in 2013 and 2014. For further information, see Note 5 Other operating income.

For the years 2014 and 2015 the major item under "Accrued expenses" are personnel related (short-term employee benefits). In 2014 in addition to the before mentioned, the accrued interest of the convertible notes contributed to the increase of the accrued expenses.

NOTE 19
Carrying amounts and fair values of financial liabilities by measurement categories

During the years presented in these financial statements Faron mainly had financial instruments classified as financial liabilities measured at amortised cost. Fair value information of those measured at fair value is included in note 2.3. The carrying amounts of Faron's financial liabilities are considered to equal their fair values, except for the following:

Faron has elected to apply the exemption provided under IFRS 1 to both goverment loans (Tekes), drawn in 2008 and 2010. The loans are stated at the carrying amount measured using the previous GAAP. The carrying amount and the respective fair value are presented below.

Stated in euro	2015 €'000	2014 €'000
Carrying amount[1]	1 691	1 691

[1] Includes both the non-current and current portions

The fair values of all financial liabilities are within level 2 of the fair value hierarchy. Description of the hierarchy levels are included in note 2.3

NOTE 20
Contingencies and commitments

Stated in euro	2015 €'000	2014 €'000
Financial liabilities, for which mortgages have been issued		
Corporate mortgages	800	800
Corporate mortgages	800	800

The corporate mortgage is a guarantee for the EUR 800,000 credit limit. The credit limit was not renewed after it expired on 31 December 2015.

Operating lease – Faron as a lessee

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

Stated in euro	2015 €'000	2014 €'000
No later than 1 year	82	46
Later than 1 year and no later than 5 years	14	2
Later than 5 years		
Total	96	48

Faron leases equipment under non-cancellable operating leases. The lease terms at the time of the start of the lease agreement are between 3 and 4 years.

The operating facilities used currently are leased under a cancellable operating lease. Faron is required to give a three-month notice for the termination of this agreement.

NOTE 21
Transactions with related parties

Related parties of the Company

Faron's related party comprise of the following:

- Marko Salmi, a private person having significant influence over Faron Pharmaceuticals Oy, following from the shareholding of 17.6%, as at 31 December 2015;
- A&B (HK) Company Limited, an investment company existing under the laws of Hong Kong having significant influence in Faron Pharmaceuticals Oy, given their shareholding of 15.2%, as at 31 December 2015;
- Board of Directors; and
- the Company's key management personnel (see below)
- Faron had no interests in other entities at the end of the reporting periods presented in these financial statements.

Key management personnel

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

- members of the Board of Directors; and
- Management Team comprising CEO Markku Jalkanen, PhD; VP Ilse Piippo, MD, MSc (Pharm); VP Mikael Maksimow, PhD; CFO Yrjö Wichmann MSc (Econ)

Stated in euro	2015 €'000	2014 €'000
Remuneration of key management personnel*		
Salaries and other short-term employee benefits	769	472
Share-based payment	122	
Post-employment benefits (defined contribution plans)		
Total	**891**	**472**

Stated in euro	2015 €'000	2014 €'000
Remuneration to the Board of Directors **		
Salaries and other short-term benefits	124	50
Share-based payment	155	
Total	**279**	**50**

* Presented information for the Management includes the Executive Directors of the Board.

** Presented information for the Board includes only Non-Executive Directors.

Management and Board shareholding

Management* shareholding, 31 December 2015	
Number of shares (pcs)	2 942 830
Shareholding, percentage	12.7%
Board shareholding, 31 December 2015**	
(excluding the shareholding of CEO)	
Number of shares (pcs)	1 584 623
Shareholding, percentage	6.9%
Total number of shares outstanding at 31 December 2015 (pcs)	23 111 704

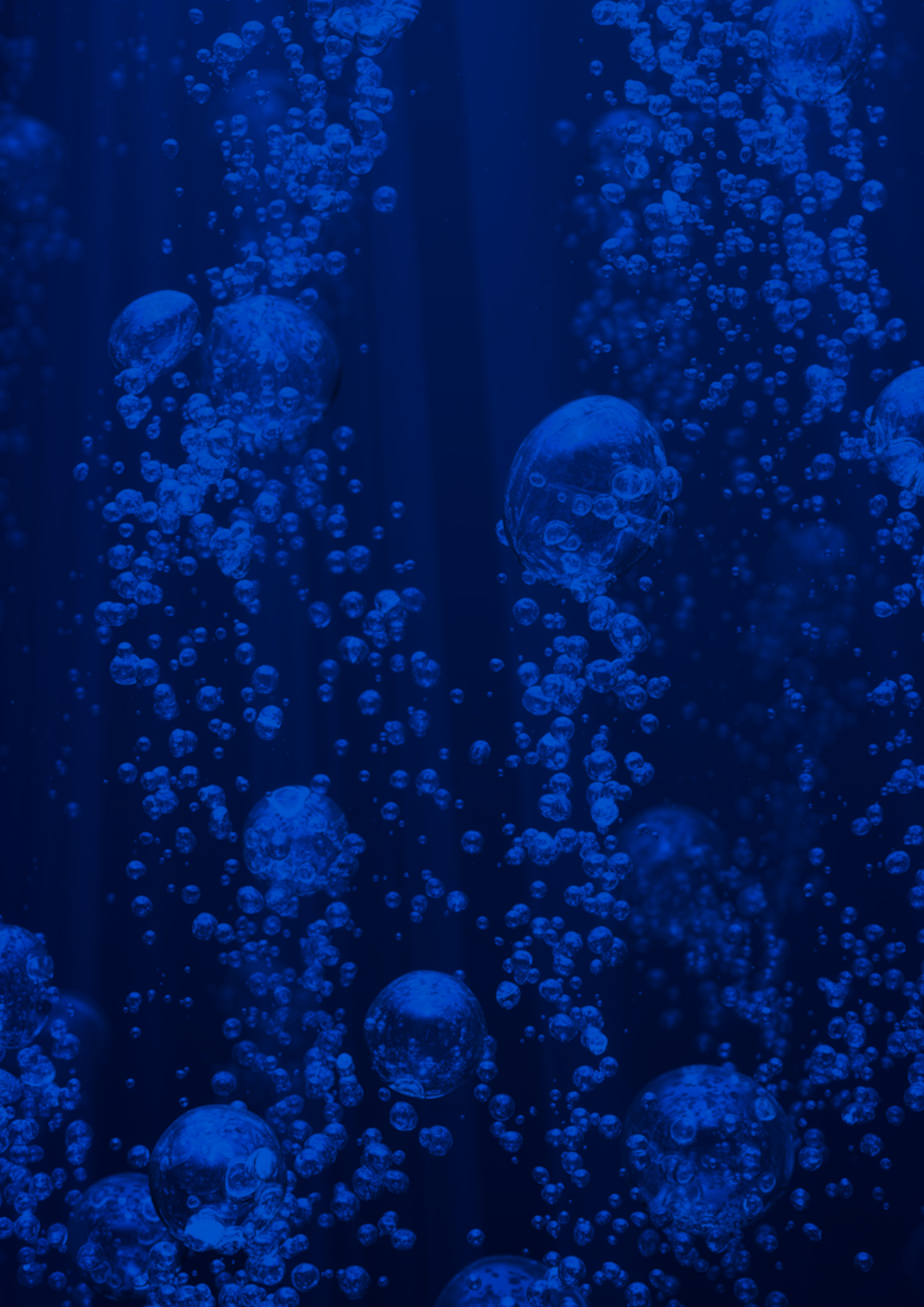
* Presented information for the Management includes the Executive Directors of the Board.
** Presented information for the Board includes only Non-Executive Directors.

Transactions with related parties

Faron has not carried out any transactions with related parties in the financial years presented in these financial statements, except that the former parent company of Faron Pharmaceuticals Ltd, Faron Holding Ltd, merged into its subsidiary Faron Pharmaceuticals Ltd on 31 December 2013.

NOTE 22
Events after the balance sheet date

No events occurred after the balance sheet date that would have a material impact on the result or financial position of the Company.



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