FARON

Annual Report 2019

Faron Pharmaceuticals in brief

Faron (AIM:FARN, First North: FARON) is a clinical stage biopharmaceutical company developing novel treatments for medical conditions with significant unmet needs. The Company currently has a pipeline based on the receptors involved in regulation of immune response in oncology and organ damage. Faron is based in Turku, Finland.

Clevegen, its precision immunotherapy, is a novel anti-Clever-1 antibody with the ability to switch immune suppression to immune activation in various conditions, with potential across oncology, infectious disease and vaccine development. Currently in phase I/II clinical development as a novel macrophage checkpoint immunotherapy for patients with untreatable solid tumours, Clevegen has potential as a single-agent therapy or for use in combination with other immune checkpoint molecules or standard of care therapies.

Traumakine, the Company's pipeline candidate to prevent vascular leakage and organ failures, has completed a phase III clinical trial in Acute Respiratory Distress Syndrome (ARDS). Plans for its future development are being finalised to avoid interfering steroid use together with Traumakine.

We are very pleased to have secured a further EUR 8 million through our series of fundraises in late 2019, further supporting the progress of our pipeline. I would like to thank our new and existing shareholders, and the entire team at Faron, for their continued support.

Dr Markku Jalkanen
Chief Executive Officer

For further information on the Company's progress, development programs and pipeline, please visit Faron´s website www.faron.com.

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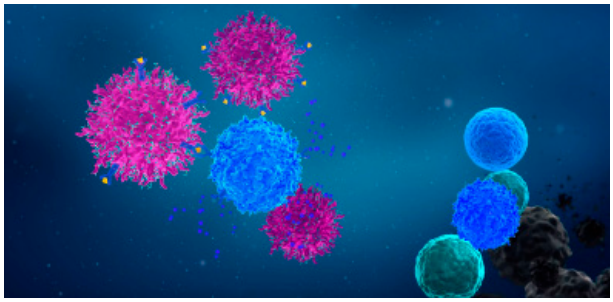


Clevegen
The future of immunotherapy

THE TARGET AND PROGRAMME

Faron's immuno-oncology programme Clevegen revolves around CLEVER-1 (Common Lymphatic Endothelial and Vascular Endothelial Receptor 1), a key immunological switch expressed under immunosuppressive conditions. Pre-clinical studies have proven that CLEVER-1, also known as Stabilin-1 or STAB-1, is involved in cancer growth and spread. Recently, it has become very clear, that CLEVER-1 maintains the immunosuppressive phenotype of tumour associated macrophages (TAMs).

THE SOLUTION

Blocking or silencing CLEVER-1 on human macrophages activates MHC expression and promotes IFN-γ leukocyte cultures. Disruption or inhibition of CLEVER-1 weakens tumour progression in mice.

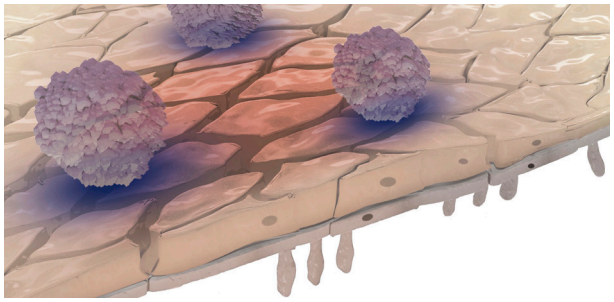
Clevegen is a humanized anti-Clever-1 antibody which targets CLEVER-1 positive TAMs and converts these highly immunosuppressive M2 macrophages to immune stimulating M1 macrophages. This unique macrophage-directed immuno-oncology switch may be used alone or in combination with other cancer treatments. Clevegen also has promise outside immuno-oncology, as it can switch immune suppression to immune activation in various conditions, such as infectious diseases and vaccine development.

Data from Faron's ongoing MATINS trial has shown, that I) in Clevegen, we potentially have the first macrophage immune checkpoint drug which has promoted immune activation of all dosed patients to date; II) Clevegen is safe and well-tolerated, making it a low-risk candidate for combination with existing cancer therapies; III) Clevegen has shown early clinical benefits in patients who have exhausted all other treatment options.

CLINICAL DEVELOPMENT

Faron is currently conducting its first-in-human clinical study MATINS with Clevegen in selected metastatic or inoperable solid tumours. Any significant developments in Faron's programmes are reported on Faron´s website www.faron.com > Media > News and press releases.

Finding an all-encompassing cure for cancer has for decades been an overwhelming medical and scientific challenge. No one can pledge to cure all cancer. We focus on becoming the best in activating immunity by supporting human immune defence mechanisms against tumours. This could help in treating several cancer types, as immune defences are often, if not always, suppressed in cancer patients.



Traumakine
Endothelial barrier is everything

THE TARGET AND PROGRAMME

Faron's Traumakine programme addresses the treatment of Acute Respiratory Distress Syndrome (ARDS) and other ischemic conditions. ARDS is a severe, orphan lung disease characterized by widespread inflammation in the lungs and a sudden failure of the respiratory system. The integrity of vasculature and capillaries, which maintain the supply of oxygen in various organs, is sustained by endothelial cells covering the inner surfaces of blood vessels and forming a barrier between circulation and tissues. The breakdown of this endothelial barrier results in leakage of blood content to tissues. When this happens in lungs (ARDS), the lung air is filled with protein rich fluid and blood cells resulting in respiratory failure.

There are several, seemingly different common causes of ARDS: sepsis, pneumonia, aspiration of fumes, food or stomach contents going into the lungs or significant trauma. There is no pharmaceutical treatment for ARDS, lung-protective mechanical ventilation being the main form of treatment. The reported mortality rate of ARDS is 30 to 45%.

THE SOLUTION

Traumakine is based on the patent-protected use of intravenous interferon beta to prevent capillary leakage in organs under threat of ischemia and inflammation. The active pharmaceutical ingredient in Traumakine is recombinant human IFN beta-1a.

Through extensive research and ex-vivo studies, scientists at Turku University have identified that a molecule called CD73 is an essential entity needed to maintain endothelial barrier function. One of the key findings that led to the development of Traumakine was a discovery that interferon beta-1a 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 so that vascular leaking and escalation of inflammation are reduced.

The European Commission has granted Traumakine an orphan designation. This means Traumakine is intended for the treatment of a disease that is life-threatening and chronically debilitating indication. Also, the FDA has granted Traumakine with Fast Track designation which is a process designed to facilitate the development and expedite the review of drugs to treat serious conditions and fill an unmet medical need.

Furthermore, the UK's Medicines and Healthcare Products Regulatory Agency (MHRA) has granted Promising Innovative Medicines (PIM) designation for Traumakine. PIM designation is granted when a medicine shows early signals, based on evidence to date, that it has potential value in a disease area with significant and urgent unmet need. PIM further qualifies an accompanying application and progression of the medicine towards the next stage in UK's EAMS process.

CLINICAL DEVELOPMENT

Following meticulous pre-clinical research Faron has conducted three clinical studies with Traumakine in the treatment of ARDS. Based on findings from the detailed analysis of INTEREST results, and following discussions with regulators, Faron is continuing clinical development of Traumakine in ARDS.

Any significant developments in Faron's programmes are reported on Faron´s website www.faron.com > Media > News and press releases.

Inducing CD73 expression on vascular endothelium to protect organs under ischemia and inflammation could be a new way to approach the treatment of several life threatening diseases and conditions.

Highlights

Operational (including post period):

CLEVEGEN®

Regulator of major inhibitory immune checkpoints and wholly-owned novel cancer immunotherapy in development

- Part I of the open label phase I/II MATINS trial, initiated across multiple sites through Europe and primarily intended to investigate safety and tolerability, was completed with dose escalation reaching its planned maximum level of 10mg/kg. Clevegen demonstrated good tolerability at all dosing levels (0.1 to 10 mg/kg) without dose limiting toxicity.
- Clevegen promoted immune activation in all dosed patients, measured following treatment with Clevegen and observed as increased circulating CD8+ T-cells and CD8+/CD4+ ratio, decreased regulatory T-cells (T-regs) or a substantial increase in mobile natural killer (NK) cells in the blood.
- Partial responses were observed in two patients. The first, a colorectal cancer (CRC) patient, showed a continuation of lung and lymph node metastasis shrinkage and their tumour load biochemical marker, carcinoembryonic antigen (CEA), also normalised. The second, a heavily pre-treated melanoma patient, showed a reduction in the size of the target lesion tumour (a lung metastasis) by 44 percent and other non-target lesions stabilized. Their biochemical tumour load marker also declined and clearance of pleura fluid was observed.
- Data showing Clevegen's potential early efficacy and good tolerability were presented at the European Society of Medical Oncology (ESMO) 2019 Congress in Barcelona, Spain. At the Society's subsequent Immuno-Oncology Congress 2019 in Geneva, Switzerland, more detailed cell surface biomarker data were presented for the first time showing Clevegen's potential to downregulate a range of inhibitory immune checkpoints commonly targeted by current immuno-oncology (IO) therapies.
- The US Food and Drug Administration (FDA) approved Faron's Investigational New Drug (IND) application for Clevegen, enabling expansion of the MATINS trial into the US.
- CRC and ovarian cancer were selected by the MATINS data monitoring committee as the first and second expansion cohorts in part II of the study. Both cancer types are known to host a significant number of Clever-1 positive tumour-associated macrophages (TAM) which correlates with increased mortality rates.
- New experimental data supporting the immuno-therapeutic blockade of Clever-1 as an alternative to, or in combination with PD-1 checkpoint inhibition to reactivate immunity against immunosuppressive tumours were published in Clinical Cancer Research, a journal of the American Association for Cancer Research.
- Several new patent filings were carried out during the period to further strengthen the existing IP around Clevegen use in conditions where harmful immune suppression causes serious diseases.
- *bexmarilimab* is under consideration by the World Health Organization as the Proposed International Nonproprietary Name.
- Manufacturing was established to supply drug product for cohort expansions in part II of the MATINS study.
- Partnering discussions continued with the aim of supporting expansion of clinical development and exploring the potential of Clevegen in combination with existing immunotherapies and other cancer therapies.

TRAUMAKINE®

in development for the treatment of organ failures

- Faron remains focused on developing Traumakine as a treatment for acute respiratory distress syndrome (ARDS) taking into account the high levels of concomitant corticosteroids used as a standard of care for ARDS and some ruptured abdominal aorta aneurysm (RAAA) patients.
- Following feedback from the FDA regarding trial design, Faron submitted an amended protocol to the FDA, reflecting the FDA's feedback that further studies with interferon-beta (IFN-beta) should exclude the use of overlapping corticosteroids since they are likely to block the desired therapeutic effect of Traumakine and may have a potentially deleterious impact on patient outcomes.
- The FDA accepted Faron's proposed study protocol for the new Traumakine trial, which excludes the use of concomitant corticosteroids and which will be split in two steps. The first step will commence with INTEGRITY, a pilot randomised and placebo controlled study, which will serve as final adjustment for adequate statistical powering and sample size justification for the pivotal second step, CALIBER.
- The Company envisages that further Traumakine trials are likely to be funded through a third party.
- Top-line data from the phase III ARDS trial with Japanese partner Maruishi Pharmaceutical Co., Ltd were, as expected, consistent with the INTEREST study results, showing that treatment with Traumakine did not result in reduced mortality or an increased number of ventilator-free survival days when compared to placebo. In the study, very high concomitant corticosteroids use (77%) was observed.
- A phase I study in healthy volunteers (pharmaco-kinetic/dynamic YODA study), examining the administration and concomitant use of corticosteroids with Traumakine, confirmed observations previously seen in the INTEREST study. Traumakine produced the expected levels of bioactivity, suggesting drug formulation was not a factor in the outcome of that trial and that concomitant corticosteroids use interferes in the desired IFN-beta effect on CD73.
- Interim results from the phase II INFORAAA study examining the effect of Traumakine on mortality (predominantly for multi-organ failure, MOF) and on pharmacodynamic biomarkers in surgically operated RAAA patients, showed biomarker (MxA and CD73) responses indicating a good IFN-beta response from Traumakine. A trend towards reduction of mortality was seen in patients increasing their CD73 plasma levels.
- Based on the advice from the INFORAAA independent data monitoring committee and investigators, the Company decided to close the INFORAAA trial, as unexpected high use of concomitant corticosteroids prevent the scientific implementation of the INFORAAA protocol.
- Faron filed a request for arbitration with the Arbitration Institute of the Stockholm Chamber of Commerce seeking damages from Rentschler Biopharma SE for terminating the API manufacturing process for Traumakine.
- It is the understanding of the Company that the current API manufacturing process used to manufacture Traumakine requires significant upgrading to secure MAA/BLA approval. Various options for manufacturing are currently being explored.

AOC3 ANTAGONIST PLATFORM TECHNOLOGY

- In March 2020, Faron acquired rights for the potential new use of AOC3 inhibitors. Faron will be responsible for the future development of the AOC3 protein inhibitor and for the management, prosecution maintenance and filing of patent applications.

CORPORATE

- Yrjö Wichmann took up the new position of Vice President, Financing and Investor Relations and Toni Hänninen was appointed as Faron's new Chief Financial Officer.
- Faron's shares were listed on Nasdaq First North Growth Market Helsinki as of 3 December 2019.

FINANCIAL

- On 31 December 2019, the Company held cash balances of €7.1 million (2018: €4.1 million).
- Loss for the period for the financial year ended 31 December 2019 was €13.3 million (2018: €20.1 million loss).
- Net assets on 31 December 2019 were €1.6 million (2018: €0.4 million).
- During the period, in November, August, May and March 2019, the Company successfully raised a total of €15.6 million gross (€14.5 million net) from new and existing shareholders, employees and Company Directors through issuance of total of 12,262,853 new ordinary shares. The majority of these proceeds are being used to advance Clevegen through the MATINS trial, further Traumakine development through the design and preparation of the next clinical trials and advance partnering discussions in respect of both Traumakine and Clevegen.

Financial
Consolidated key figures, IFRS

€'000	Unaudited 7–12/2019 6 months	Unaudited 7–12/2018 6 months	1–12/2019 12 months	1–12/2018 12 months
Revenue	0	(1)	0	19
Research and Development expenses	(5,255)	(4,762)	(10,237)	(16,463)
General and Administrative expenses	(1,688)	(1,378)	(3,049)	(3,750)
Loss for the period	(6,850)	(6,026)	(13,262)	(20,086)
Loss per share EUR	(0.18)	(0.20)	(0.36)	(0.65)
Number of shares at end of period	43,290,747	31,027,894	43,290,747	31,027,894
Average number of shares	38,551,293	30,749,648	36,850,577	30,749,648

€'000	Unaudited 30 Jun 2019	Unaudited 30 Jun 2018	31 Dec 2019	31 Dec 2018
Cash and cash equivalents	2,892	11,168	7,059	4,067
Equity	(1,761)	6,722	1,610	369
Balance sheet total	5,103	16,716	10,209	8,002

Chairman's Statement

2019 was a significant year for Faron. The highly experienced management team made significant progress executing the Company's strategy and maintaining momentum in the delivery of its novel pipeline.

The development programme for Faron's wholly-owned novel precision cancer immunotherapy candidate, Clevegen, has accelerated rapidly. Promising early clinical data continued to give us confidence in the potential of Clevegen as a next-generation immuno-oncology therapy and one that could potentially be used in combination therapy. The strength of the early clinical data generated in 2019 enabled the Clevegen team to quickly identify a group of patients thought most likely to respond to treatment. Selection of the first expansion cohort in colorectal cancer was a significant achievement and is testament to the focus Faron has placed on Clevegen's development this year. The US Food and Drug Administration (FDA) approval of the Company's Investigational New Drug (IND) application for Clevegen was a major development milestone enabling expansion of Clevegen's clinical development in the US.

Harnessing the immune system to fight cancer has transformed the way patients are treated and scientists continue to make new discoveries in the field of immuno-oncology every day. It is exciting to see the Clevegen programme generating such interest in this field, from the scientific community and commercial organisations. The wealth of data generated in 2019 strengthens Faron's confidence in the programme's future.

Alongside Clevegen's development progress in 2019, the Company continued to build on its understanding of the results from Traumakine's INTEREST trial. Data from a late-stage trial undertaken by our Japanese partner Maruishi were consistent with our study results a year earlier and supported our observation that corticosteroid use interferes with Traumakine efficacy. This observation has since been confirmed by the FDA who, following discussions about the future development path for Traumakine, advised that further studies should exclude the concomitant use of steroids. The body of evidence generated during Traumakine's development programme is clearly a matter of interest for opinion leaders involved in the treatment of of acute respiratory distress syndrome (ARDS) patients and the debate around whether corticosteroids have any beneficial role in ARDS patients continues.

Recent guidance from the World Health Organization (WHO) on the clinical management of severe acute respiratory infection related to the novel coronavirus that emerged in China at the end of 2019 advises against the routine use of corticosteroids. The emergence of this novel virus, and the risk of ARDS among infected patients, is a reminder of the need for new treatments to tackle this potentially fatal condition.

During the year our fundraising activities and our listing on the Nasdaq First North Growth Market in Finland received strong shareholder support enabling us to build a more secure financial position for the Company and give the pipeline its greatest chances of success. It was also encouraging to see the Company's share price performance in 2019, its growth reflecting the progress of the business and the strength of Faron's pipeline potential.

On behalf of the Board, I would like to thank all those who have played a part in Faron's progress in 2019 – the management team, staff and Board for their hard work and commitment, our partners and steering committee members for their support and expertise, and the investigators and patients involved in our clinical trials. I would also like to pay particular thanks to our CEO, Markku Jalkanen who, while guiding Faron through difficult circumstances, has successfully led its transition to becoming a leading immunotherapy company.

We look forward to continued progress with our pipeline products Clevegen and Traumakine in 2020.

Dr Frank Armstrong
Chairman
March 19, 2020

Chief Executive Officer's Review

OVERVIEW

Faron is focused on immuno-oncology, organ trauma and vascular damage. Our goal is to save lives by developing unique scientific discoveries into ground-breaking new treatments for hard-to-treat and rare diseases. Our work is rooted in two scientific principles. First, a deep knowledge of the pharmacology of our drug candidates. And second, understanding the science of the targeted conditions at the molecular level, to most effectively influence their underlying causes.

Our focus for 2019 has been to continue to progress our wholly-owned novel precision cancer immunotherapy candidate, Clevegen, through the first-in-human clinical study, MATINS, in selected metastatic or inoperable solid tumours. We have also been working closely with the regulatory authorities to determine the future development pathway for Traumakine in ARDS and organ failures.

CLEVEGEN DEVELOPMENT

We have made significant, and exciting, clinical progress with Clevegen during 2019. Clevegen is our wholly-owned novel precision cancer immunotherapy candidate, which causes conversion of the immune environment around a tumour from immune-suppressive to immune-stimulating by reducing the number and function of tumour-associated macrophages (TAMs). Clevegen is differentiated from other immunotherapies through its specific targeting of M2 TAMs which facilitate tumour growth. Through myeloid cell plasticity, Clevegen can convert these M2 TAMs to M1s, leaving existing M1 TAMs intact and allowing both to support immune activation against tumours. We believe it has the potential to function as a novel macrophage checkpoint immunotherapy both as a monotherapy and in combination with other immuno-oncology therapies or standard of care treatments.

MATINS TRIAL

The MATINS (Macrophage Antibody To INhibit immune Suppression) study is a first-in-human open label phase I/II clinical trial with an adaptive design to investigate the safety and efficacy of Clevegen in selected metastatic or inoperable solid tumours. The selected tumours under investigation are cutaneous melanoma, hepatobiliary/hepatocellular, pancreatic, ovarian and colorectal cancer, all known to host a significant number of Clever-1 positive TAMs. Together these five target groups consist of approximately 2 million annual cases worldwide. Cancer patients with high Clever-1 expression are identified with a simple blood myeloid cell staining with Clevegen ("liquid biopsy").

Part I of the MATINS study was conducted to establish tolerability, safety and dose escalation to optimize dosing. Subjects in Part I of the study received doses of 0.1 mg/kg, 0.3 mg/kg, 1.0 mg/kg, 3.0 mg/kg and 10 mg/kg. All dose levels tested showed good tolerability with no dose limiting toxicity signals and all subjects dosed in the study experienced a switch in their immune cell profiles following treatment with Clevegen towards increased immune activation, observed as increased circulating CD8+ T cells and CD8+/CD4+ ratio, decreased regulatory

T-cells (T-regs) or a substantial increase in mobile natural killer (NK) cells in the blood.

Based on results from the initial part of the MATINS trial, Faron announced in April 2019 that late-stage colorectal cancer (CRC) had been chosen for the first expansion cohort for the second part of the trial. Following the successful conclusion of the dose escalation in Part I, and with approval from the MATINS trial's data monitoring committee (DMC), Faron initiated this first expansion cohort, Part II, in January 2020. A total of 10 late-stage CRC patients are expected to be dosed at the approved initial dose level of 0.3 mg/kg cohort, including two patients who had previously received this dose in the earlier Part I of the study. Furthermore, in January 2020, we announced that ovarian cancer has been selected as the second expansion cohort in the trial. Both these tumour types are known to host a significant number of Clever-1 positive TAMs which correlates with increased mortality rates among these patients.

In November 2019, the FDA approved the Company's Investigational New Drug (IND) application for Clevegen® (FP-1305), enabling expansion of the MATINS trial into the US. We anticipate opening the first site in mid-2020. In due course, we also plan to file applications for Breakthrough Therapy status in the US and PRIME status in Europe, further facilitating regulatory interactions during the development of Clevegen.

Clevegen's ability to down regulate a range of major inhibitory checkpoints reaffirms our belief in its potential as a master regulator of immunity and a highly effective immunotherapy. It indicates that Clevegen treatment could potentially allow increased efficacy of other immuno-oncology therapies through the biomarker analysis of patient's blood cells post Clevegen induced immune activation, finally offering a biological rationale to guide combination therapies. Due to high interest in the potential for new combination therapies in the immuno-oncology field, we are currently engaged in partnering discussions with several parties and hope for a positive outcome from these negotiations during 2020.

TRAUMAKINE DEVELOPMENT

With no currently approved pharmacological treatments available, acute respiratory distress syndrome (ARDS) remains a significant problem for patients and healthcare systems. During 2019, the Company has continued to further understand the correlation between the combined use of corticosteroids and IFN-beta and has been working closely with the regulatory authorities in order to determine the next steps in Traumakine's future development pathway.

In April 2019, Faron announced top-line data from the Phase III trial with Japanese partner Maruishi Pharmaceutical Co., Ltd. Results from this trial were in line with the Company's expectations, and previously announced results observed in the INTEREST trial, showing that treatment with Traumakine did not result in reduced mortality or an increased number of ventilator-free survival days when compared to placebo. In order to further examine the effects of concomitant steroid use and Traumakine, as seen in both the INTEREST trial and the

Japanese study, Faron conducted the pharmacokinetic/dynamic YODA study in healthy volunteers. Results from this study, announced in June 2019, were consistent with the INTEREST data, supporting the conclusion that co-administration of steroids with Traumakine in patients inhibits IFN-beta action.

Also, in June 2019, Faron announced interim results from the Phase II INFORAAA study, which examined the effect of Traumakine on mortality (predominantly for multi-organ failure, MOF) and pharmacodynamic biomarkers of surgically operated ruptured abdominal aorta aneurysm (RAAA) patients. Based on the advice from the INFORAAA independent data monitoring committee and investigators, the Company decided to close the INFORAAA trial, as unexpected high use of concomitant corticosteroids was preventing the scientific implementation of the INFORAAA protocol.

Interestingly, in January 2020, the World Health Organization (WHO) published a recommendation recognising the risk of using corticosteroids on patients with coronavirus. This recommendation aligns with our findings from the post-hoc analysis of the INTEREST study and strengthens our belief that the whole medical community should be more diligent with regard to the combined use of corticosteroids and type I interferons. Faron's scientific network has also confirmed this interaction at a molecular level in lung endothelial cells.

The Company remains committed to progressing Traumakine for the treatment of ARDS and, following the Company's revised protocol submission in February 2020, the FDA have now accepted the protocol design for the next Traumkine study. The study design reflects the feedback and conclusions from the FDA that further studies with IFN beta should exclude the use of concomitant glucocorticoids since they are likely to block the desired therapeutic effect of Traumakine and may have a potentially deleterious impact on patient survival. We are planning to split the clinical development of Traumakine in ARDS into two steps, commencing with INTEGRITY, a pilot randomised and placebo controlled study with approximately 60 patients. The INTEGRITY data will then serve as final adjustment for adequate statistical powering and sample size justification for the pivotal CALIBER study, subjected for FDA review. We expect that the sample size of the CALIBER study will not exceed 200 patients based on the post hoc analysis of the INTEREST trial data. We envisage that future Traumakine trials (including INTEGRITY and CALIBER) are likely to be funded through a third party or parties.

AOC3 ANTAGONIST PLATFORM TECHNOLOGY

In March 2020, Faron announced it had acquired rights for the potential new use of AOC3 inhibitors covered by a recently filed patent application. The AOC3 enzymatic domain, a semicarbazide-sensitive amine oxidase is known to produce hydrogen peroxide, a potent inflammatory mediator. Being expressed by many inflamed vascular endothelial cells, the AOC3 overexpression has been connected with many vascular diseases.

Faron will be responsible for future development of the invention and for the management, prosecution and maintenance of any patent applications as well as for the filing of new patent applications for the AOC3 protein inhibitor. Pre-clinical studies with humanized AOC3 mice and with ex vivo human cells in relation to the Invention are currently ongoing and further information will be provided later in the year.

CORPORATE

On 3 December 2019, Faron started trading on Nasdaq First North Growth Market ("Nasdaq First North"), a multilateral trading facility operated by Nasdaq Helsinki Ltd. The ISIN code of Faron's ordinary shares is FI4000153309 and the trading code on Nasdaq First North is FARON. This is in addition to Faron's listing, since November 2015, on AIM.

In October 2019, Faron received a letter from Rentschler Biopharma SE ("Rentschler") in which Rentschler stated that it was terminating the agreement concerning the API manufacturing for Traumakine. Following a detailed investigation by Faron into the circumstances around manufacturing arrangements, the Company has since concluded that, in its view, Rentschler was in breach of the underlying agreement between the parties. Faron has filed a request for arbitration, funded by a third party on a non-recourse basis, with the Arbitration Institute of the Stockholm Chamber of Commerce seeking damages.

In May 2019, Yrjö Wichmann left his role as the Company's Chief Financial Officer to take up the new position of Vice President, Financing and Investor Relations. Mr Wichmann remains a member of the senior management team but stepped down from the Board with effect from 28 May 2019. We were delighted to welcome Mr Toni Hänninen as Faron's new CFO, effective from 1 June 2019, being responsible for both internal and external reporting.

The Annual General Meeting held on 28 May 2019 resolved the number of members of the Board as six.

Frank Armstrong, Markku Jalkanen, Matti Manner, Leopoldo Zambeletti, Gregory Brown and John Poulos were re-elected to the Board for a term that ends at the end of the next AGM.

FINANCIAL

During the period, the Company successfully raised approximately EUR 15.6 million (gross), EUR 14.5 million (net) from new and existing shareholders, employees and Company Directors. The majority of these proceeds are being used to advance Clevegen through the MATINS trial, further Traumakine development through the design and preparation of the next clinical trials and advance partnering discussions in respect of both Traumakine and Clevegen.

OUTLOOK

Our focus for 2020 will be to continue to expedite Clevegen's clinical development through part II and part III of the MATINS trial and to report these data to regulatory authorities. We will also continue to work in close collaboration with the regulatory authorities in order to progress the INTEGRITY and CALIBER clinical trials and secure Traumakine's future development pathway. We are continuing to make progress with potential partners regarding both Clevegen and Traumakine, whilst also exploring funding opportunities to ensure we can continue to progress both products. I would like to thank our shareholders for their continued belief in the Company and the management team for their hard-work and dedication and look forward to updating the market on our progress throughout the course of the year.

THE BOARD ANTICIPATES THE FOLLOWING PIPE-LINE PROGRESS AND CATALYSTS DURING 2020:

Clevegen:

- Completion of all biomarker analyses from MATINS Part I patients to guide Clevegen dosing
- Initiation of the second expansion cohort, ovarian cancer, during H1-2020
- Initial data from the first expansion cohort (CRC) expected in Q2-2020
- Expansion of the MATINS trial to leading cancer centres in France and Spain in Q2-2020
- Opening of US study sites to facilitate rapid expansion of the MATINS trial in Q2-2020
- Partnering update during 2020

Traumakine:

- Further updates in relation to INTEGRITY and CALIBER during 2020
- Continuation plans to be announced in H2-2020

AOC3 Antagonist Platform Technology:

- Additional information from pre-clinical studies with humanized AOC3 mice and with ex vivo human cells during 2020

Dr Markku Jalkanen
Chief Executive Officer
March 19, 2020

Financial Review

KEY PERFORMANCE INDICATOR

As a clinical stage drug development company, Faron's primary interconnected KPIs are cash burn and cash position. The Company conducted several successful fundraises during 2019. The Company's net cash flow showed €3.0 million positive due to a reduction in expenses and said fundraises. The Board will consider the appropriateness of monitoring additional KPIs as the Company's operations advance.

REVENUE AND OTHER OPERATING INCOME

The Company's revenue was €0.0 million for the year ended 31 December 2019 (2018: €nil).

The Company recorded €0.2 million (2018: €0.2 million) of other operating income. This consisted of the reimbursement of already occurred legal expenses by the third-party recovery services provider as announced by the Company on 30 December 2019.

RESEARCH AND DEVELOPMENT COSTS

The R&D costs decreased by €6.3 million from €16.5 million in 2018 to €10.2 million in 2019. The costs of outsourced clinical trial services were reduced by €3.4 million from €5.3 to €1.9 million. The cost of materials and services used in the R&D was reduced by €1.7 million from €7.3 to €5.6 million.

GENERAL AND ADMINISTRATION COSTS

Administrative expenses decreased by €0.8 million from €3.8 million in 2018 to €3.0 million in 2019. The decrease was mainly due to the €1.4 million decrease in external costs related to the development of internal financial and reporting processes during 2018, but this was partially offset by an increase of €0.7 million in the other administrative expenses.

TAXATION

The Company's tax credit for the fiscal year 2019 can be recorded only after the Finnish tax authorities have approved the tax report and confirmed the amount of tax-deductible. The total amount of cumulative tax losses carried forward approved by tax authorities on 31 December 2019 was €16.1 million (2018: €11.2 million). The Company estimates that it can utilise most of these during the years 2020 to 2028 by offsetting them against future profits. In addition, Faron has €58.6 million of R&D costs incurred in the financial years 2010 - 2019 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 €13.3 million (2018: €20.1 million). Net loss for the year was €13.3 million (2018: €20.1 million), representing a loss of €0.31 per share (2018: €0.65 per share) (adjusted for the changes in number of issued shares).

CASH FLOWS

Net cash flow was €3.0 million positive for the year ended 31 December 2019 (2018: €5.3 million negative). Cash used for operating activities decreased by €9.0 million to €11.5 million for the year, compared to €20.5 million for the year ended 31 December 2018. This decrease was mostly driven by a decrease in R&D investments.

Net cash inflow from financing activities was €14.5 million (2018: €15.5 million) due to the successful equity placings completed in during 2019.

FUNDRAISING

During the period, 1 January to 31 December 2019, the Company successfully raised a total of €15.6 million gross (€14.5 million net) across several fundraises from new and existing shareholders, employees and Company Directors. The majority of these proceeds are being used to advance Clevegen through the MATINS trial, further Traumakine development through the design and preparation of the next clinical trials and advance partnering discussions in respect of both Traumakine and Clevegen.

- In March 2019, €3.1 million gross (€2.9 net) through issuance of new ordinary shares.
- In May 2019, €1.3 million gross (€1.3 net) through issuance of new ordinary shares.
- In August 2019, €2.5 gross (€2.2 net) million through issuance of new ordinary shares.
- In November 2019, €8.7 million gross (€8.0 net) through issuance of new ordinary shares.

FINANCIAL POSITION

As at 31 December 2019, total cash and cash equivalents held were €7.1 million (2018: €4.1 million). The Company continues to exercise tight cost control to keep the cash burn as low as possible for preservation of existing resources.

GOING CONCERN

As part of their going concern review, the Directors have followed the Finnish Limited Liability Companies Act, the Finnish Accounting Act and the guidelines published by the Financial Reporting Council entitled "Guidance on the Going Concern Basis of Accounting and Reporting on Solvency and Liquidity Risks – Guidance for directors of companies that do not apply the UK Corporate Governance Code". The Company and its subsidiaries (the "Group") are subject to a number of risks similar to those of other development stage pharmaceutical companies. These risks include, amongst others, generation of revenues in due course from the development portfolio and risks associated with research, development, testing and obtaining related regulatory approvals of its pipeline products. Ultimately, the attainment of profitable operations is dependent on future uncertain events which include obtaining adequate financing to fulfil the Group's commercial and development activities and generating a level of revenue adequate to support the Group's cost structure.

The Group made a net loss of €13.3 million during the year ended 31 December 2019. It had total equity of €1.6

million including an accumulated deficit of €80.0 million. As at that date, the Group had cash and cash equivalents of €7.1 million.

The Directors have prepared detailed financial forecasts and cash flows looking beyond 12 months from the date of the approval of these financial statements. In developing these forecasts, the Directors have made assumptions based upon their view of the current and future economic conditions that are expected to prevail over the forecast period. The Directors estimate that the cash held by the Group together with known receivables will be sufficient to support the current level of activities into the fourth quarter of 2020. The Directors are continuing to explore sources of finance available to the Group and they believe they have a reasonable expectation that they will be able to secure sufficient cash inflows for the Group to continue its activities for not less than 12 months from the date of approval of these financial statements; they have therefore prepared the financial statements on a going concern basis.

Because the additional finance is not committed at the date of issuance of these financial statements, these circumstances represent a material uncertainty that may cast significant doubt on the Company's ability to continue as going concern. Should the Group be unable to obtain further finance such that the going concern basis of preparation were no longer appropriate, adjustments would be required, including to reduce balance sheet values of assets to their recoverable amounts, to provide for further liabilities that might arise.

HEADCOUNT

Average headcount of the Company for the year was 24 (2018: 25).

SHARES AND SHARE CAPITAL

During the period 1 January to 31 December 2019, the Company, using the share authorities granted at the Annual General Meetings held on 31 May 2018 and on 28 May 2019, as well as at an Extraordinary General Meeting held on 25 October 2019, issued a total of 12,262,853 new ordinary shares.

- On 28 March 2019, 4,448,625 shares at an issuance price of € 0.7020 (£0.60) per share.
- On 13 May 2019, 1,757,375 shares at an issuance price of € 0.7598 (£0.65) per share.
- On 5 August 2019, 941,840 shares at an issuance price of € 1.1900 (£1.06) per share.
- On 27 August 2019, 1,179,513 shares at an issuance price of € 1.1900 (£1.06) per share.
- On 12 November 2019, 3,935,500 shares at an issuance price of €2.1980 (£1.90) per share.

The subscription price net of costs was credited in full to the Company's reserve for invested unrestricted equity, and the share capital of the Company was not increased.

The Company has no shares in treasury; therefore at the end of 2019 the total number of voting rights was 43,290,747.

LEGAL PROCEEDINGS

As announced by the Company on 2 October 2019 and 30 December 2019, the Company has received a letter from Rentschler Biopharma SE in which Rentschler stated that it terminates the agreement concerning the Traumakine API manufacturing. The Company considers that this statement is without merit and has filed a request for arbitration to seek damages. To fund the proceedings, the Company has entered into a litigation funding agreement with a third-party recovery services provider which, in the event of success, would receive a typical portion of any damages awarded.

Toni Hänninen
Chief Financial Officer
March 19, 2020

Risks and Uncertainties

Faron is a late clinical stage biopharmaceutical company and, similarly to 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 2019 are below.

RESEARCH AND DEVELOPMENT

Faron's main products are in clinical development however, they may not be successful in clinical trials and the Company 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). Conversion of cutting-edge scientific research into clinical development programmes of novel compounds and drugs where there is limited amount of guidance and no previous examples involves a high degree of uncertainty. This uncertainty, combined with Faron's lean organisation, could result in situations where the Company needs to make rapid alterations to its development projects without full visibility to all the downstream consequences. Additionally, drug development is a highly regulated environment which in itself presents technical risk through the need for study designs and data to be accepted by regulatory agencies. As part of the development risk, the manufacturing of the Company's intended products would become impossible or products would be supplied in lower quantities than needed.

COMMERCIAL PRODUCTS AND MANUFACTURING

The biotechnology and pharmaceutical industries in which Faron operates are very competitive. The Company's competitors include major multinational pharmaceutical companies, biotechnology companies and research institutions. Many of which have substantially greater financial, technical and operational resources, such as larger research and development resources and staff. It may have a material adverse impact on the Company if its competitors succeed in developing, acquiring or licensing drug product candidates that are more effective or less costly than any of the product candidates which the Company is currently developing or which it may develop. Furthermore, there can be no guarantee that the Company will be able, or that it will be commercially advantageous for the Company, to monetise the value of its intellectual property through entering into licensing or other co-operation deals with pharmaceutical companies.

There can be no assurance that the Company's proposed products will be capable of being manufactured in sufficient quantities and standards for clinical trials or in commercial quantities, in compliance with regulatory requirements and at an acceptable cost or within an acceptable timeframe.

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 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 conditions and/or results of operations may be materially adversely affected. To develop new products and commercialise its current pipeline, 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.

Furthermore, 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 and has entered into contractual arrangements with these individuals with the aim of securing their services. 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 shares of the Company.

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 patents, patent applications, confidential business know-how and trade secrets, and trademarks. 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 the Company's lead pharmaceutical drug candidates, future drug candidates in development, and proprietary processes for generating those candidate compounds infringe the IPR of any third parties. However, it is impossible to be aware of all third party intellectual property. The Company's research has included searching and reviewing certain publicly available resources, which are examined by senior levels of management in order to keep abreast of developments in the field.

FINANCIAL

The Company has incurred significant losses since its inception and does not have any approved or revenue-generating products. The Company expects to incur losses for the foreseeable future, and there is no certainty that the business will generate a profit. The Company is highly dependent on equity and public grant and loan financing. 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. The Company operates internationally, and it is thus exposed in various currencies and fluctuation in their relative values. Even though the Company seeks to hedge currency positions there is no guarantee that it will be successful.

OTHER RISKS RELATED TO OPERATIONS

While operating with multiple vendors and other external suppliers, the Company regularly delivers and receives information and data through multiple channels. Some of these are trade secrets or of confidential nature. Even though the Company uses all reasonably available means to secure the data and the channels used, there is no certainty that full data security can be obtained.

The Company is publicly listed and as such subject to various securities laws in multiple jurisdictions. The Company uses significant amount of both internal and external resources to secure that all its operations and external communication are conducted in accordance to these regulations. Whilst the Company will take every effort to ensure that the Company and its partners comply with all applicable securities laws and requirements, there can be no guarantee of this.

This report was approved by the Board on 19 March 2020.

Corporate Governance

CHAIRMAN'S INTRODUCTION TO GOVERNANCE

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

As Chairman of the Board, I oversee the adoption, delivery and communication of Faron's corporate governance model. In this role, I endeavour to foster a positive governance culture throughout the Company, seeing that ultimate responsibility for the quality of, and Faron's approach to, corporate governance lies with me.

Faron is not required to comply with the UK Corporate Governance Code by virtue of being an AIM and Nasdaq First North Growth Market quoted company. The Board does, however, seek to apply the QCA Corporate Governance Code (as devised by the Quoted Companies Alliance in consultation with a number of significant institutional small company investors) in its updated form.

In 2019, Yrjö Wichmann left his role as the Company's Chief Financial Officer to take up the new position of Vice President, Financing and Investor Relations. Mr Wichmann remains a member of the senior management team but stepped down from the Board. Toni Hänninen was appointed as Faron's new CFO, being responsible for both internal and external reporting. Otherwise, no significant changes in governance arrangements occurred during the year.

As described below, the Board continues to promote a healthy corporate culture that is based on ethical values and behaviours consistent with the Company's objectives, strategy and business model described on the Company's website and with the description of principal risks and uncertainties set out in this document. As good corporate governance is fundamentally about culture, rather than procedure, Faron's corporate culture is monitored on a regular basis, and appropriate action is taken if, and to the extent, deemed necessary.

Dr Frank Armstrong
Non-Executive Chairman
March 19, 2020

Compliance

COMPLIANCE WITH THE PRINCIPLES OF THE QCA CODE

The Principles of the QCA Code	Comply/Explain	Disclosure in the 2019 Report
1. Establish a strategy and business model which promote long-term	Comply	Pages 4, 5 and 12 to 15
2. Seek to understand and meet shareholder needs and expectations	Comply	Pages 37 to 39
3. Take into account wider stakeholder and social responsibilities and their implications for long-term success	Comply	Page 39
4. Embed effective risk management, considering both opportunities and threats, throughout the organisation	Comply	Pages 19 to 21
5. Maintain the board as a well-functioning, balanced team led by the chair	Comply	Pages 28 to 29 and 40 to 41
6. Ensure that between them the directors have the necessary up-to-date experience, skills and capabilities	Comply	Pages 24 to 28
7. Evaluate board performance based on clear and relevant objectives, seeking continuous improvement	Comply	Page 28
8. Promote a corporate culture that is based on ethical values and behaviours	Comply	Page 22
9. Maintain governance structures and processes that are fit for purpose and support good decision-making by the board	Comply	Pages 22 and 24
10. Communicate how the company is governed and is performing by maintaining a dialogue with shareholders and other relevant stakeholders	Comply	Pages 28 and 30 to 36

Board of Directors

On 28 May 2019, at the Company's Annual General Meeting, the number of Directors was confirmed as six, with Frank Armstrong, Markku Jalkanen, Matti Manner, Leopoldo Zambeletti, Gregory Brown and John Poulos re-elected to the Board for a term that ends at the end of the next AGM. At the meeting of the Board held following the AGM, Frank Armstrong was re-elected Chairman of the Board and Matti Manner was re-elected Vice-Chairman of the Board. The Board comprises five non-executive directors and one executive director. Brief biographical details for the Directors can be found on the following pages. During 2019, the Board held 22 meetings.

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, to review the strategy and activities of the business, and to advise on management appointments. The Board sees to the administration of the Company and the organisation of its operations, being responsible for the appropriate arrangement of the control of the Company accounts and finances.

All key operational and investment decisions are subject to full Board approval. The management of the Company prepares a monthly management and financial accounts pack, which is distributed to the Board every month and in advance of Board meetings. In individual cases the Board may decide in a matter falling within the general competence of the Chief Executive Officer.

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 Chairman sees to it that the Board meets when necessary.

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 Chief Executive Officer, reviewing the operating results regularly to make decisions about the allocation of resources and to assess overall performance, is the chief operating decision-maker.

The Board considers there to be sufficient independence of 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 their appointment to the Board. Under the Finnish Limited Liability Companies Act and the Company's Articles of Association, the Directors are elected by the shareholders at general meetings annually. Under the 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.

Dr Frank Armstrong

Non-Executive Chairman

Dr Armstrong has held Chief Executive roles with five biotechnology companies (both public and private) including FulcrumPharma PLC (AIM) and CuraGen (NASDAQ). 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 Caldan Therapeutics and a Director of Newcells Biotech. He is a member of the Senior Advisory Board at Healthcare Royalty Partners and an SAB Member at Epidarex Capital. Dr Armstrong is a Member of the Court of the University of Edinburgh. Dr Armstrong is a physician and a Fellow of the Royal College of Physicians (Edinburgh).

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

Matti Manner

Non-Executive Vice-Chairman

Mr Matti Manner was appointed as a partner of Brander & Manner Attorneys Ltd in 1980 having previously sat as a judge at Turku Appeal Courts. He has significant experience in national and international business deals, corporate law and mergers and acquisitions having held a number of board memberships throughout his career. Mr Manner joined the Board of the Company as Chairman in 2007 and has served as Vice-Chairman since October 2015, having previously been the Chairman of Faron Ventures Oy from 2002.

He is currently Chairman of Turun Osuuskauppa and Ruissalo Foundation and a member of the board of Marva Media Ltd, Satatuote Ltd, YH VS-Rakennuttajat Ltd, Kauppakeskus Mylly Ltd and Nurmi-Yhtiöt Oy. Mr Manner has experience of several trustee posts including the Presidency of the Finnish Bar (Lawyers) Association during the period of 1998 to 2004. Mr Manner obtained a Master of Laws from the University of Turku. He became an honorary Chief Justice in Finland in 2013.

Dr Markku Jalkanen

Chief Executive Officer

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

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

Dr Jalkanen has held several board memberships for both public and private companies including Inveni Capital Management, Meddia Ltd and Priaxon AG.

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.

Dr Gregory B. Brown

Non-Executive Director

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

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

John Poulos

Non-Executive Director

Mr John Poulos has a wealth of expertise in global corporate life sciences, having spent 38 years working for AbbVie and Abbott. Mr Poulos served as Vice President, Head of Business Development and Acquisitions for AbbVie from 2013 until 2016. John was also Group Vice President, Head of Pharmaceutical Licensing and Acquisitions for Abbott from 2005 until 2012. During his career with AbbVie and Abbott, John was instrumental in the negotiation of numerous acquisitions, including Knoll/BASF Pharma in 2001 for $6.9 billion, Kos Pharmaceuticals in 2006 for $3.7 billion, Solvay in 2010 for $6.2 billion and Pharmacyclics in 2015 for $21 billion.

Mr Poulos is currently an Operating Advisor with Linden Capital Partners, a private equity firm focused exclusively on healthcare.

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

Leopoldo Zambeletti

Non-Executive Director

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

He is a Non-Executive Director of Philogen, Nogra Pharma and the The Meatless Farm. Mr Zambeletti started his career at KPMG as an auditor.

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

PERFORMANCE EVALUATION

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

In the Board performance evaluation process adopted by the Company, Board, committee and individual effectiveness is considered against the criteria of creating and running an effective Board, professional development, strategic foresight, stewardship, managing management, value creation and corporate culture.

In the most recent Board assessment, opportunities for Board members to engage in professional development and benchmarking of the Company's performance against its peers were identified as areas meriting further discussion by the Board.

The Directors have reviewed the results of the Board self-assessment exercise and agreed a series of actions in that regard, including a new peer group review to be carried out in 2020.

BOARD COMMITTEES

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

Under the Finnish Limited Liability Companies Act, Board committees do not, generally speaking, have a formal legal status or independent decision-making powers; rather, their role is to provide support in the preparation of the decision-making. The responsibility for the decisions remains with the Board even if the matter has been delegated to a committee.

At the Board meeting held following the AGM on 28 May 2019, the Board of Directors re-elected the Chairmen and elected the other members of the Board committees.

REMUNERATION COMMITTEE

As of 28 May 2019, the remuneration committee comprises Frank Armstrong as Chairman together with John Poulos and Leopoldo Zambeletti. The remuneration committee has the task of advising on and making recommendations to the Board in relation to the remuneration paid to the Directors and supervising the development of any other remuneration or reward systems of the Company. During 2019, the remuneration committee held two meetings.

AUDIT COMMITTEE

The audit committee, which comprises Leopoldo Zambeletti as Chairman together with Matti Manner and Gregory Brown, meets not less than twice a year. The audit committee has the task of supervising and developing the internal audit of the Company and advising and making recommendations to the Board on related issues. During 2019, the audit committee held three meetings.

NOMINATION COMMITTEE

The nomination committee comprises Matti Manner as Chairman together with Frank Armstrong. The nomination committee has the task, in co-operation with the Board, of advising on and making recommendations to the Board on issues relating to the composition and nomination of the Board. During 2019, the nomination committee held two meetings.

The nomination committee considers succession planning for Directors and other senior executives in the course of its work, bearing in mind the challenges and opportunities facing the Company and the skills and expertise needed on the Board in the future, and makes recommendations to the Board concerning formulating plans for succession for both Executive and Non-Executive Directors and in particular for the key roles of Chairman and Chief Executive Officer.

Attendance at Board Meetings

During 2019 the Board held 22 meetings. The table below lists the Directors' attendance at the Board and Committee meetings during the year.

The Directors' attendance during the year ended 31 December 2019

	Board	Audit Committee	Remuneration Committee	Nomination Committee
Executive directors				
Jalkanen Markku	22			
Wichmann Yrjö(*)	8(8)			
Non-Executive Directors				
Armstrong Frank	18		2(2)	2(2)
Manner Matti	20	2(3)		2(2)
Brown Gregory	21	3(3)		
Poulos John	20		2(2)	
Zambeletti Leopoldo	17	3(3)	1(1)	

(*) Resigned from the Board on 28 May 2019

Remuneration Report

Remuneration Policy for Directors

The Remuneration Committee sets the remuneration policy that aims to align Director remuneration with shareholders' interests and attract and retain the best talent for the benefit of the Company. No Director is involved in discussions relating to their own remuneration. This report sets out Faron's remuneration policy for the Executive and Non-Executive Directors. The remuneration of the Directors during the year ended 31 December 2019 is set out below:

BASIC SALARY

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

In 2019, no increments in the salaries were made.

BONUSES

Executive Directors' annual bonuses are based on the achievement of the 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 50% for the Executive Directors.

In 2019, the Chief Executive Officer voluntarily waived any bonus for the preceding financial year.

LONGER TERM INCENTIVES

In order to further incentivise the Executive Directors and employees, and align their interests with shareholders, the Extraordinary General Meeting of the Company on 15 September 2015 approved a share option plan and granted share options to the members of the Board under this option plan. At the AGM held on 28 May 2019, the Company authorised the Board to implement a new share option plan for the employees and Directors of, and persons providing services to, the Company's group. Rules of that new option plan were approved by the Board on 20 November 2019. Details of these option plans are on page 52.

PENSION

Faron has a law-defined contribution plan under which it pays fixed contributions into a separate entity. The plan covers all the employees of Faron including the Executive Directors. Faron has no legal or constructive obligations to pay further contributions if the fund does not hold

sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

OTHER BENEFITS

The Chief Executive Officer and some employees have the possibility to take a company car allowance, which is part of their gross salary. All employees including Executive Directors 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 concluded for an indefinite term.

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

	Date of contract	Notice period
Jalkanen Markku, CEO	16.09.2015	6 months
Wichmann Yrjö(*), CFO(**)	16.09.2015	6 months

(*) Resigned from the Board on 28 May 2019
(**) Vice President, Financing and Investor Relations from 1 June 2019

NON-EXECUTIVE DIRECTORS' SERVICE CONTRACTS AND REMUNERATION

The remuneration and compensation payable to the members of the Board including the Non-Executive Directors is 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 go 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.
With the exception of share options disclosed below, the Non-Executive Directors do not receive any pension, bonus or benefit 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	Independence	Contract	Date of Contract
Armstrong Frank	Independent	Chairman	16.09.2015
Manner Matti	Non-independent(*)	Vice-chairman	16.09.2015
Brown Gregory	Independent	Member	16.05.2017
Poulos John	Independent	Member	16.05.2017
Zambeletti Leopoldo	Independent	Member	16.09.2015

(*) Has served as a director for more than 10 consecutive years

The appointments of Non-Executive Directors are terminable with immediate effect, in accordance with the Company's Articles of Association and pursuant to the Finnish Limited Liability 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.

The Directors received the following remuneration during the year

€	Salaries and fees	Bonus	Taxable benefits	Total
Executive Directors				
Jalkanen Markku	257,400		16,080	273,480
Wichmann Yrjö(*)	180,769	11,346	1,041	193,156
Non-Executive Directors				
Armstrong Frank	73,800			73,800
Manner Matti	42,300			42,300
Brown Gregory	40,700			40,700
Poulos John	40,600			40,600
Zambeletti Leopoldo	41,400			41,400

(*) Resigned from the Board on 28 May 2019

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. Option Plan 2015 was adopted by the Company at the Extraordinary General Meeting held on 15 September 2015 and amended in the Annual General Meeting of 16 May 2017. Option Plan 2015 allowed 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 entitles the holder of the option to subscribe for one ordinary share in the Company. Under the terms of Option Plan 2015, an aggregate maximum number of 1,800,000 options could be granted, such aggregate being made up of a maximum of 400,000 "2015A" options, the subscription period for which ended on 9 June 2016, a maximum of 400,000 "2015B" options, the subscription period for which ended on 30 September 2019, a maximum of 500,000 "2015C" options, the subscription period for which ended on 30 September 2019, and a maximum of 500,000 "2015D" options, the subscription period for which ended on 30 September 2019, all such options being exercisable until 30 September 2021.

The exercise price for ordinary shares based on "2015A" options is €3.71. The exercise price for ordinary shares based on "2015B" options is €2.90. The exercise price for ordinary shares based on "2015C" options is €8.39. The exercise price for ordinary shares based on "2015D" options is €1.09.

Total options	At 1 January 2019	Granted during the period	Cancelled during the period	At 31 December 2019	Average subs. price per shares, €
Jalkanen Markku	240 000	80 000	0	320 000	4,02
Wichmann Yrjö	90 000	30 000	0	120 000	4,02
Armstrong Frank	120 000	40 000	0	160 000	4,02
Manner Matti	60 000	20 000	0	80 000	4,02
Brown Gregory	20 000	20 000	0	40 000	4,74
Poulos John	20 000	20 000	0	40 000	4,74
Zambeletti Leopoldo	60 000	20 000	0	80 000	4,02
	610 000	**230 000**	**0**	**840 000**	

Details of these options are as follows

2015A options	Date of grant	At 1 January 2019	Granted during the period	Cancelled during the period	At 31 December 2019	Subscription price per share, €	Date from which exercisable	Expiry date
Jalkanen Markku	16.09.2015	80 000	0	0	80 000	3,71	02.11.2015	30.09.2021
Wichmann Yrjö	16.09.2015	30 000	0	0	30 000	3,71	02.11.2015	30.09.2021
Armstrong Frank	16.09.2015	40 000	0	0	40 000	3,71	02.11.2015	30.09.2021
Manner Matti	16.09.2015	20 000	0	0	20 000	3,71	02.11.2015	30.09.2021
Brown Gregory	-	0	0	0	0	-	-	-
Poulos John	-	0	0	0	0	-	-	-
Zambeletti Leopoldo	16.09.2015	20 000	0	0	20 000	3,71	02.11.2015	30.09.2021
		190 000	**0**	**0**	**190 000**			

2015B options	Date of subscription	At 1 January 2019	Granted during the period	Cancelled during the period	At 31 December 2019	Subscription price per share, €	Date from which exercisable	Expiry date
Jalkanen Markku	18.11.2016	80 000	0	0	80 000	2,90	08.10.2016	30.09.2021
Wichmann Yrjö	18.11.2016	30 000	0	0	30 000	2,90	08.10.2016	30.09.2021
Armstrong Frank	18.11.2016	40 000	0	0	40 000	2,90	08.10.2016	30.09.2021
Manner Matti	18.11.2016	20 000	0	0	20 000	2,90	08.10.2016	30.09.2021
Brown Gregory	-	0	0	0	0	-	-	-
Poulos John	-	0	0	0	0	-	-	-
Zambeletti Leopoldo	18.11.2016	20 000	0	0	20 000	2,90	08.10.2016	30.09.2021
		190 000	**0**	**0**	**190 000**			

2015C options	Date of subscription	At 1 January 2019	Granted during the period	Cancelled during the period	At 31 December 2019	Subscription price per share, €	Date from which exercisable	Expiry date
Jalkanen Markku	16.11.2017	80 000	0	0	80 000	8,39	08.10.2017	30.09.2021
Wichmann Yrjö	16.11.2017	30 000	0	0	30 000	8,39	08.10.2017	30.09.2021
Armstrong Frank	16.11.2017	40 000	0	0	40 000	8,39	08.10.2017	30.09.2021
Manner Matti	16.11.2017	20 000	0	0	20 000	8,39	08.10.2017	30.09.2021
Brown Gregory	16.11.2017	20 000	0	0	20 000	8,39	08.10.2017	30.09.2021
Poulos John	16.11.2017	20 000	0	0	20 000	8,39	08.10.2017	30.09.2021
Zambeletti Leopoldo	16.11.2017	20 000	0	0	20 000	8,39	08.10.2017	30.09.2021
		230 000	**0**	**0**	**230 000**			

2015D options	Date of subscription	At 1 January 2019	Granted during the period	Cancelled during the period	At 31 December 2019	Subscription price per share, €	Date from which exercisable	Expiry date
Jalkanen Markku	21.05.2019	0	80 000	0	80 000	1,09	08.10.2018	30.09.2021
Wichmann Yrjö	21.05.2019	0	30 000	0	30 000	1,09	08.10.2018	30.09.2021
Armstrong Frank	21.05.2019	0	40 000	0	40 000	1,09	08.10.2018	30.09.2021
Manner Matti	21.05.2019	0	20 000	0	20 000	1,09	08.10.2018	30.09.2021
Brown Gregory	21.05.2019	0	20 000	0	20 000	1,09	08.10.2018	30.09.2021
Poulos John	21.05.2019	0	20 000	0	20 000	1,09	08.10.2018	30.09.2021
Zambeletti Leopoldo	21.05.2019	0	20 000	0	20 000	1,09	08.10.2018	30.09.2021
		0	**230 000**	**0**	**230 000**			

At 31 December

2019	Issued Share Capital		Share Options	
	Ordinary shares	Percentage held	Ordinary shares	Average exercise price, €
Executive				
Jalkanen Markku[1]	3,194,290	7.38	320,000	4.02
Wichmann Yrjö(*)[2]	131,294	0.30	120,000	4.02
Non-Executive				
Armstrong Frank	64,792	0.15	160,000	4.02
Manner Matti[3]	551,035	1.27	80,000	4.02
Brown Gregory B	46,490	0.11	40,000	4.74
Poulos John	0	0.0	40,000	4.74
Zambeletti Leopoldo	17,461	0.04	80,000	4.02
	3,874,068	**8.95**	**840,000**	

(*) Resigned from the Board on 28 May 2019

(1) of which 2,020,565 are held by Markku Jalkanen directly and 1,173,725 are held by Markku Jalkanen's wife Sirpa Jalkanen and her related party
(2) of which 81,437 are held by Yrjö Wichmann directly and 49,857 are held by his spouse
(3) of which 528,890 are held by Matti Manner directly and 22,145 are held by his spouse

Corporate Governance Statement

For the Year Ended 31 December 2019

COMMUNICATING WITH SHAREHOLDERS

The Company acknowledges that effective communication with shareholders on strategy and governance is an important part of its responsibilities. Interim and final results are communicated via formal meetings with roadshows, participation in conferences and additional dialogue with key investor representatives held in the intervening periods. Faron recognises the Annual General Meeting as an opportunity to meet shareholders.

As an AIM and First North listed company, Faron complies the Market Abuse Regulation, the AIM Rules for Companies and the Nasdaq First North Growth Market Rulebook. The Company complies with other relevant legislation in all its corporate communications issues.

The Company speaks to the financial community and shareholders only through authorised representatives. In accordance with the Company's disclosure policy, the Chief Executive Officer is the designated person to make public statements. The Chief Executive Officer may delegate this authority to other members of the management team. In addition to the CEO, the Vice President of Financing and Investor Relations is able to communicate externally on behalf of the Company.

The contact details are below:

Faron
email: investor.relations@faron.com

Media and investor relations:

Consilium Strategic Communications
email: faron@consilium-comms.com

SHARE DEALING

The Company has established a share dealing code appropriate to an AIM and First North listed company, and all the Directors of the Company understand the importance of compliance to that code.

ETHICAL VALUES AND CORPORATE CULTURE

Faron is strongly committed to conducting its business affairs with honesty and integrity and in full compliance with all applicable laws, rules and regulations. The Company requires that all employees and Directors comply with all laws, rules and regulations applicable to the Company wherever it does business.

Employees and Directors should endeavour to deal honestly, ethically and fairly with the Company's

collaborators, licensors, licensees, business partners, suppliers, customers, competitors and other employees. Statements regarding the Company's therapies and services must not be untrue, misleading, deceptive or fraudulent.

Employees and Directors act in the best interests of the Company and use the Company's assets and services solely for legitimate business purposes of the Company and not for any personal benefit or the personal benefit of anyone else.

RISK MANAGEMENT AND INTERNAL CONTROL

The principal risks and uncertainties identified by the Board are set out on pages 19 to 21 of the 2019 Report. The Board has put in place internal controls and systems which are designed to manage rather than eliminate risk and provide reasonable but not absolute assurance against material misstatement or loss. A key element of delivering the Company's strategy and managing the risks facing the Company is the employment of a skilled workforce and use of appropriate vendors. The Board reviews the risks and uncertainties facing the Company and the effectiveness of its systems annually.

At present, the Company does not consider it necessary to have an internal audit function due to the small size of the administrative function, the frequent interaction with the auditors and the supervision of the audit committee. The Board is, however, closely following both regulatory and operational developments in this realm and plans to react appropriately if, and to the extent, considered necessary.

There is a monthly review and authorisation of transactions by the Chief Financial Officer and Chief Executive Officer. A comprehensive budgeting process is completed once a year and is reviewed and approved by the Board. The Company's results, compared with the budget, are reported to the Board on regular basis and discussed in detail.

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

REGULATED ADVISORS

The shares of Faron are listed for trading on the London Stock Exchange AIM and Nasdaq First North Growth Market marketplaces, which require the nominating of advisors. Panmure Gordon (UK) Limited is the Company's nominated adviser and broker on AIM and Sisu Partners Oy is the Company's certified advisor on First North.

CORPORATE SOCIAL RESPONSIBILITY

Faron acknowledges that running its business has an effect on society. In particular, the Company has a responsibility to the patients, its employees and contractors as well as the broader community in which it operates.

Faron is committed to taking responsibility for its actions and encourages a positive contribution towards improving standards for patients and its employees, minimising its impact on the environment and improving the quality of the local community.

Faron is committed to maintaining and promoting high standards of business integrity. The Company's values, which incorporate the principles of corporate social responsibility and sustainability, guide its relationships with clients, employees and the communities and environment in which it operates. Faron's approach to sustainability addresses both its environmental and social impacts, supporting its vision to remain an employer of choice, while meeting client demands for socially responsible partners. Faron respects local laws and customs while supporting international laws and regulations.

By putting CSR into practice, Faron is committed, wherever possible, to:

- developing treatments for medical conditions with significant unmet needs
- conducting itself responsibly and in an ethical manner
- creating a positive and supportive working environment
- acting fairly in its dealings with suppliers and other third parties
- minimising the impact on its environment

FARON'S CSR PRINCIPLES

Conduct

The Company aims to adopt the highest professional standards and not to act in such a way as to compromise Faron's integrity. Faron actively promotes respect between its staff members in their dealings with each other and with suppliers and other third parties.

Working Environment

The Company recognises that its staff are its most important resource. Faron actively seeks to offer its staff a positive and healthy working environment and ensure that they have rewarding careers and job satisfaction.

Faron seeks to ensure that all staff have access to the training they need both for their own development and to

enable them to deliver a high-quality work contribution.

Faron considers all staff members to be equal and aims to create a working environment which is free of unlawful discrimination. In this regard, the Company maintain an internal code of conduct based on professionalism and respect.

Suppliers

Faron is committed to eliminating unlawful discrimination and to promoting equality and diversity in its professional dealings with suppliers and other third parties. The Company endeavours to enter into clear and fair contracts with its suppliers.

Environment

Faron is committed to behaving responsibly and to minimising its impact on the environment. In considering the environment, the Company has resolved to include environmental considerations in its business travel and to minimise its consumption of natural resources and manage waste through responsible disposal and reuse and recycling, including paper and ink cartridges.

Responsibility and Review

The Board has overall responsibility for the Company's CSR strategy and for implementing Faron's CSR principles. They have a key role in ensuring the systems and controls Faron has in place are effective. All members of staff have a role to play in complying with the Company's CSR objectives and are encouraged to make further suggestions in relation to initiatives Faron could undertake.

Faron is fully committed to the highest possible standards of openness, honesty and accountability. In line with that commitment, the Company actively encourages all staff members who have serious concerns about any real or perceived departure from the high ethical standard that it sets to voice those concerns openly.

STATEMENT OF RESPONSIBILITIES

Under the Finnish Limited Liability Companies Act and the Finnish Accounting Act, the Company must prepare financial statements in accordance with applicable law and regulations.

The Board 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 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 in Finland. The Board 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 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 IFRS as adopted by the EU, 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 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 statement 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 financial statements are made available on a website. Financial statements are published on the Company's website in accordance with AIM Rule 26, Nasdaq First North Growth Market Rulebook and the recommendations of the QCA's Corporate Governance Code for Small and Medium Sized Companies.

On behalf of the Board

Frank Armstrong
Chairman
March 19, 2020

Directors' Report

For the year ended 31 December 2019

The Directors present their report together with the audited financial statements for the year ended 31 December 2019.

DIRECTORS

During the year ended 31 December 2019 the following persons have been members of the Board of the Company:

Executive

Dr Markku Jalkanen, PhD | Chief Executive Officer
Mr Yrjö Wichmann(*), MSc | Chief Financial Officer(**)

Non-executive

Dr Frank Armstrong, FRCPE, FFPM | Chairman
Mr Matti Manner, LLM | Vice-Chairman
Dr Gregory B Brown | Non-Executive Director
Mr John Poulos | Non-Executive Director
Mr Leopoldo Zambeletti | Non-Executive Director

(*) Resigned from the Board on 28 May 2019
(**) Vice President, Financing and Investor Relations from 1 June 2019

PRINCIPAL RISKS AND UNCERTAINTIES

For a discussion of the principal risks and uncertainties which face Faron please see pages 19 to 21 of this document.

RESULTS AND DIVIDENDS

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

The Company's loss of the financial year after taxation and other comprehensive losses was €13.3 million (2018: €20.1 million).

The Company has no distributable equity and thus the Directors do not recommend the payment of a dividend (2018: nil).

FINANCIAL INFORMATION

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

FINANCIAL KEY PERFORMANCE INDICATORS (KPIs)

For a review of the Group's KPIs please see page 16 Financial Review.

RESEARCH AND DEVELOPMENT

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

FINANCIAL INSTRUMENTS AND MANAGEMENT OF LIQUID RESOURCES

The Company's principal financial instrument comprises cash, and this is used to finance the 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 bank in Finland. The Group's treasury policy is reviewed annually. See note 2.16 'Financial assets', note 19 'Financial assets and liabilities' and note 20, 'Financial risk management' in the notes to the Financial Statements for IFRS disclosure regarding financial instruments.

SUBSTANTIAL SHAREHOLDINGS

On 31 December 2019 the Company had been notified of the following holdings of 3% or more of the issued share capital of the Company.

Timo Syrjälä(*)	6,496,612	15.01%
Tom-Erik Lind	3,547,712	8.20%
A&B (HK) Company Limited	3,408,409	7.87%
Markku Jalkanen(**)	3,194,290	7.38%
Marko Salmi	2,817,736	6.51%
Hargreaves Lansdown Asset Mgt	2,356,781	5.44%

(*) of which 2,680,647 are held directly by Timo Syrjälä directly and 3,815,965 are held by Acme Investments SPF S.à.r.l., an entity which is wholly owned by Timo Syrjälä
(**) of which 2,020,565 are held by Markku Jalkanen directly and 1,173,725 are held by Markku Jalkanen's wife Sirpa Jalkanen and her related party

ANNUAL GENERAL MEETING

The Company held two general meetings in 2019, an Annual General Meeting on 28 May 2019 and an Extraordinary General Meeting on 25 October 2019.

In 2020, the Annual General Meeting will be held on 15 April 2020. 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 Annual General Meeting.

DISCLOSURE AND INFORMATION TO AUDITORS

Each of the current Directors hereby confirms that:
(a) So far as he is aware, there is no relevant audit information of which the auditors are unaware; and
(b) He 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 Armstrong
Chairman
March 19, 2020

Financial Report

Statement of Comprehensive Income

For the year ended 31 December

		Group		Parent	
€'000	Note	2019	2018	2019	2018
Revenue	**3, 4**	**0**	**19**	**0**	**19**
Other operating income	5	185	205	185	205
Research and development expenses	6, 7, 8	(10,237)	(16,463)	(10,237)	(16,463)
General and administrative expenses	6, 7, 8	(3,049)	(3,750)	(3,080)	(3,740)
Operating loss		**(13,101)**	**(19,989)**	**(13,132)**	**(19,979)**
Financial expense	9	(224)	(397)	(215)	(397)
Financial income	9	74	302	77	302
Loss before tax		**(13,251)**	**(20,084)**	**(13,270)**	**(20,074)**
Tax expense	10	(11)	(2)	(9)	(2)
Loss for the period		**(13,262)**	**(20,086)**	**(13,279)**	**(20,076)**
Other comprehensive income		-	-	-	-
Total comprehensive loss for the period		**(13,262)**	**(20,086)**	**(13,279)**	**(20,076)**
Loss per ordinary share					
Basic and diluted loss per share, EUR	11	(0.36)	(0.65)	(0.36)	(0.65)

Balance Sheet

		Group		Parent	
€'000	Note	2019	2018	2019	2018
Assets					
Non-current assets					
Machinery and equipment	12	13	17	13	17
Right-of-use-assets	14	386	-	386	-
Subsidiary shares	23	-	-	18	18
Intangible assets	12	529	525	529	525
Prepayments and other receivables	13	77	636	209	636
Total non-current assets		**1,005**	**1,177**	**1,155**	**1,195**
Current assets					
Prepayments and other receivables	15	2,145	2,759	2,145	2,759
Cash and cash equivalents	16	7,059	4,067	7,058	4,058
Total current assets		**9,204**	**6,825**	**9,203**	**6,817**
Total assets		**10,209**	**8,002**	**10,358**	**8,012**
Equity and liabilities					
Capital and reserves attributable to the equity holders of the Company					
Share capital		2,691	2,691	2,691	2,691
Reserve for invested unrestricted equity		78,916	64,464	78,916	64,464
Accumulated deficit		(79,997)	(66,786)	(80,003)	(66,775)
Translation difference		-	-	-	-
Total equity	**17, 18**	**1,610**	**369**	**1,604**	**380**
Non-current liabilities					
Borrowings	19	2,263	1,887	2,263	1,887
Lease liabilities	14	261	-	261	-
Total non-current liabilities		**2,524**	**1,887**	**2,524**	**1,887**
Current liabilities					
Borrowings	19	163	245	163	245
Lease liabilities	14	135	-	135	-
Trade payables	21	2,967	3,534	3,173	3,533
Other current liabilities	21	2,810	1,967	2,759	1,967
Total current liabilities		**6,075**	**5,745**	**6,230**	**5,744**
Total liabilities		**8,599**	**7,633**	**8,754**	**7,631**
Total equity and liabilities		**10,209**	**8,002**	**10,358**	**8,012**

Parent Company Statement of Changes in Equity

€'000	Note	Share capital	Reserve for invested unrestricted equity	Accumulated deficit	Total equity
Balance as at 31 December 2017		**2,691**	**48,576**	**(46,524)**	**4,743**
Comprehensive loss for the period		-	-	(20,076)	(20,076)
Transactions with equity holders of the Company					
Issue of ordinary shares, net of transaction costs EUR 1,149 thousand	17	-	15,888	-	15,888
Share-based compensation	7,18	-	-	(176)	(176)
		-	**15,888**	**(176)**	**15,712**
Balance as at 31 December 2018		**2,691**	**64,464**	**(66,775)**	**380**
Comprehensive loss for the period		-	-	(13,279)	(13,279)
Transactions with equity holders of the Company					
Issue of ordinary shares, net of transaction costs EUR 1,174 thousand	17	-	14,452	-	14,452
Share-based compensation	7,18	-	-	51	51
		-	**14,452**	**51**	**14,503**
Balance as at 31 December 2019		**2,691**	**78,916**	**(80,003)**	**1,604**

Group Statement of Changes in Equity

€'000	Note	Share capital	Reserve for invested unrestricted equity	Translation difference	Accumulated deficit	Total equity
Balance as at 31 December 2017		**2,691**	**48,576**	**-**	**(46,524)**	**4,743**
Comprehensive loss for the period		-	-	-	(20,086)	(20,086)
Transactions with equity holders of the Company						
Issue of ordinary shares, net of transaction costs EUR 1,149 thousand	17	-	15,888	-	-	15,888
Share-based compensation	7,18	-	-	-	(176)	(176)
		-	**15,888**	**-**	**(176)**	**15,712**
Balance as at 31 December 2018		**2,691**	**64,464**	**-**	**(66,786)**	**369**
Comprehensive loss for the period		-	-	-	(13,262)	(13,262)
Transactions with equity holders of the Company						
Issue of ordinary shares, net of transaction costs EUR 1,174 thousand	17	-	14,452	-	-	14,452
Share-based compensation	7,18	-	-	-	51	51
		-	**14,452**	**-**	**51**	**14,503**
Balance as at 31 December 2019		**2,691**	**78,916**	**-**	**(79,997)**	**1,610**

Statement of Cash Flows

As at 31 December		*Group*		*Parent*	
€'000	Note	2019	2018	2019	2018
Cash flow from operating activities					
Loss before tax		(13,251)	(20,084)	(13,270)	(20,074)
Adjustments for:					
Depreciation and amortisation	8	238	100	238	100
Interest expense	9	158	121	155	121
Unrealised foreign exchange loss (gain), net	9	(7)	(36)	(16)	(36)
Tax expense	10	11	-	9	-
Share-based compensation	18	51	(176)	51	(176)
Adjusted loss from operations before changes in working capital		(12,800)	(20,075)	(12,833)	(20,065)
Change in net working capital:					
Prepayments and other receivables		1,173	1,836	1,041	1,836
Trade payables		(567)	338	(360)	337
Other liabilities		731	(2,595)	688	(2,595)
Cash used in operations		(11,463)	(20,496)	(11,464)	(20,487)
Taxes paid	10	(9)	(2)	(9)	(2)
Interest paid	9	(51)	(27)	(51)	(27)
Net cash used in operating activities		**(11,523)**	**(20,525)**	**(11,524)**	**(20,516)**
Cash flow from investing activities					
Payments for acquisition of shares in subsidiaries	23	-	-	(0)	(18)
Payments for intangible assets	12	(100)	(293)	(100)	(293)
Payments for equipment	12	-	(2)	(0)	(2)
Net cash used in investing activities		**(100)**	**(295)**	**(100)**	**(313)**
Cash flow from financing activities					
Proceeds from issue of shares	17	15,627	17,023	15,627	17,023
Share issue transaction cost	17	(1,175)	(1,135)	(1,175)	(1,135)
Proceeds from borrowings	20	307	-	307	-
Repayment of borrowings	20	-	(347)	-	(347)
Payment of lease liabilities	2.19	(151)	-	(151)	-
Net cash from financing activities		**14,608**	**15,541**	**14,608**	**15,541**
Net increase (+) / decrease (-) in cash and cash equivalents		**2,985**	**(5,279)**	**2,984**	**(5,288)**
Effect of exchange rate changes on cash and cash equivalents		7	36	16	36
Cash and cash equivalents at 1 January	16	4,067	9,310	4,058	9,310
Cash and cash equivalents at 31 December	**16**	**7,059**	**4,067**	**7,058**	**4,058**

Notes to the Financial Statement

1. CORPORATE INFORMATION

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

Faron Pharmaceuticals Ltd. is listed on the London Stock Exchange's AIM market since 17 November 2015, with a ticker FARN. On 21 November the company announced it has submitted an application for the listing of its ordinary shares on Nasdaq First North Growth Market, a multilateral trading facility operated by Nasdaq Helsinki Ltd. The first date of trading at Nasdaq First North was 3 December 2019 (trading code FARON).

The Board of Directors of the Company approved the financial statements on 19 March 2020.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

2.1. Basis of Preparation

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

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

The principal accounting policies applied in the preparation of these financial statements are set out below. The Company has consistently applied these policies to all the periods presented, unless otherwise stated. The areas of the financial statements involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 2.21.

The Consolidated Financial Statements incorporate the parent company, Faron Pharmaceuticals Ltd, and all subsidiaries in which it holds over 50% of the voting rights. The subsidiaries established during the financial period are consolidated from the date that control was obtained by the Group.

The subsidiaries are consolidated by using the purchase method. All intragroup transactions, receivables, liabilities and unrealized gains are eliminated in the Consolidated Financial Statements. Faron Pharmaceuticals Ltd holds 100% ownership of all its subsidiaries.

The Consolidated Financial Statements are presented in euro which is the functional currency of the parent company. The statements of comprehensive income and statements of cash flows of foreign subsidiaries, whose functional currency is not euro, are translated into euro each month at the average monthly exchange rates, while the statements of financial position of such subsidiaries are translated at the exchange rate prevailing at the reporting date. Translation differences resulting from the translation of profit for the period and other items of comprehensive income in the statement of comprehensive income and statement of financial position are recognised as a separate component in equity and in other comprehensive income. Also, the translation differences arising from the application of the purchase method and from the translation of equity items cumulated subsequent to acquisition are recognised in other comprehensive income.

All figures presented in notes are group figures if not else stated.

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

2.2. Going Concern

As part of their going concern review the Directors have followed the Finnish Limited Liability Companies Act, the Finnish Accounting Act and the guidelines published by the Financial Reporting Council entitled "Guidance on the Going Concern Basis of Accounting and Reporting on Solvency and Liquidity Risks – Guidance for directors of companies that do not apply the UK Corporate Governance Code". The Company and its subsidiaries (the "Group") are subject to a number of risks similar to those of other development stage pharmaceutical companies. These risks include, amongst others, generation of revenues in due course from the development portfolio and risks associated with research, development, testing and obtaining related regulatory approvals of its pipeline products. Ultimately, the attainment of profitable operations is dependent on future uncertain events which include obtaining adequate financing to fulfil the Group's commercial and development activities and generating

a level of revenue adequate to support the Group's cost structure.

The Group made a net loss of €13.3 million during the year ended 31 December 2019. At the end of the financial year, it had total equity of €1.6 million including an accumulated deficit of €80.0 million. As at that date, the Group had cash and cash equivalents of €7.1 million.

The Directors have prepared detailed financial forecasts and cash flows looking beyond 12 months from the date of the approval of these financial statements. In developing these forecasts, the Directors have made assumptions based upon their view of the current and future economic conditions that are expected to prevail over the forecast period. The Directors estimate that the cash held by the Group together with known receivables will be sufficient to support the current level of activities into the fourth quarter of 2020. The Directors are continuing to explore sources of finance available to the Group and they believe they have a reasonable expectation that they will be able to secure sufficient cash inflows for the Group to continue its activities for not less than 12 months from the date of approval of these financial statements; they have therefore prepared the financial statements on a going concern basis.

Because the additional finance is not committed at the date of issuance of these financial statements, these circumstances represent a material uncertainty that may cast significant doubt on the Company's ability to continue as going concern. Should the Group be unable to obtain further finance such that the going concern basis of preparation were no longer appropriate, adjustments would be required, including to reduce balance sheet values of assets to their recoverable amounts, to provide for further liabilities that might arise.

2.3. Foreign Currency Transactions and Balances

Functional and Presentation Currency

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

Transaction Currency

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

2.4. Segment Reporting

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

2.5. Revenue Recognition

The Group adopted IFRS 15 Revenue from Contracts with Customers effective 1 January 2017 and has applied the single, principles based five-step model to all contracts with customers provided by IFRS 15 as follows:

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

Revenue from Licensing Agreements

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

Faron Pharmaceuticals Ltd.'s existing license agreements with Maruishi in Japan, with A&B in Greater China and with Pharmbio in Republic of Korea each include only one performance obligation, which is the grant of the license to use of its intellectual property ("IP"). After the Company has granted the license, it does not have an obligation to participate or provide additional services to its customers. The transaction price for the grant of the license to use the Company's IP comprises of fixed and variable payment streams and the grant of the license is considered to be a right to use IP. Upfront fees earned, are recognised as revenue at a point in time, upon transfer of control over the license to the licensee.

Revenue from variable consideration, which are contingent on achievements of future milestones are recognised as revenue when it is highly probable the revenue will not reverse, that is when the underlying contingencies have been resolved. For future royalty payments associated with a license, the Group applies the IFRS 15 exception for sales-based royalties and recognises the revenue only when the subsequent sale occurs.

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

For further information on revenue recognition, see notes 2.21 and 3.

2.6. Recognition of Government Grants

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

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

2.7. Research and Development Expenses

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

Capitalization of expenditure on the development of the Company's products commences from the point at which technical and commercial feasibility of the product can be demonstrated and it is probable that future economic benefits will result from the product once completed. As at 31 December 2019, considering the development stage of the Company's drug candidates, no internally developed assets related to Company's development activities had met these criteria and had therefore not been recognised. The uncertainties inherent in developing pharmaceutical products prohibits the capitalization of internal development expenses as an intangible asset until the marketing approval has been received from the relevant regulatory agencies.

2.8. Employee Benefits

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

2.9. Share-based Compensation

The options granted under share-based incentive programs are measured at fair value at earlier of the grant date or the service commencement date, using the Black-Scholes valuation model. The options, for which the option exercise price is determined later, right before the vesting, an estimate is used to determine the fair value at service commencement date and the estimate is subsequently revised until the options become granted. The share-based compensation expense is recognised on a straight-line basis over the vesting period together with a corresponding increase in equity, based on the Group's estimate of equity instruments that will eventually vest. At each reporting date, the Group revises its estimate of the number of equity instruments that are expected to vest and its estimate of the grant date fair value for the options with earlier service commencement date. The exercise price paid by the option or warrant holder to subscribe the Group's shares is recognised in the reserve for invested unrestricted equity.

2.10. Loss per Share

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

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

2.11. Income Tax

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

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

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

2.12. Machinery and Equipment

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

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

2.13. Intangible Assets

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

2.14. Impairment of Non-financial Assets

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

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

2.15. Inventories

Inventories are stated at the lower of cost and net realizable value. The cost includes all costs of direct materials and external services associated with the process of manufacturing of the goods sellable upon obtaining the regulatory marketing approval. The cost of inventories is fully written down.

2.16. Financial Assets

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

Other receivables consist mainly of the deferred grant income from the European Union for which the grant payment has not been received, carried at the amount expected to be received according to the terms and conditions of the grant.

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

2.17. Financial Liabilities

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

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

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

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

between the initial fair value of the loan and the proceeds received.

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

2.18. Equity

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

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

Under the Finnish Limited Liability Companies Act (624/2006, as amended), if the board of directors of a company notices that the company has negative equity, the board must make a register notification on the loss of share capital. However, if the fair value of the assets of the company is otherwise than temporarily notably higher than their book value, the difference between the probable current price and the book value may be taken into account as an addition to equity. During the Period, the Board noticed that the Company had negative equity. The Board reviewed the situation, carried out a survey of the amount of equity and took measures to remedy the financial position of the Company so that, following the placing announced in November 2019, the Company had at the end of the Period positive equity. In ascertaining the financial position of the Company, the Board, exercising special caution, noted that the fair value of the intellectual property assets of the Company related to Clevegen and Traumakine is notably higher than their book value. In making the calculations required under the Limited Liability Companies Act, that difference was taken into account as an addition to equity and, accordingly, no register notification was made.

2.19. Leases

The Company as Lessee

This note explains the impact of the adoption of IFRS 16 Leases on the Group's financial statements. The group has adopted IFRS 16 Leases retrospectively from 1 January 2019, but has not restated comparatives for the 2018 reporting period, as permitted under the specific transition provisions in the standard. The reclassifications and the adjustments arising from the new leasing rules are therefore recognised in the opening balance sheet on 1 January 2019.

On adoption of IFRS 16, the group recognised lease liabilities in relation to leases which had previously been classified as 'operating leases' under the principles of IAS 17 Leases. These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019.

The weighted average lessee's incremental borrowing rate applied to the lease liabilities on 1 January 2019 was 5.0%.

From 1 January 2019, the Group recognises all leases, with the exception of short-term (i.e. lease term less than 12 months) and low value leases, in line with IFRS 16 Leases as right-of-use assets with a corresponding lease liability at the date at which the leased asset is available for use by the Group. A contract is or contains a lease if the Group has the right to control the use of an identified asset for a period of time in exchange for consideration. When determining the lease term, the Group assesses the probability of exercising extension and termination options over the non-cancellable period by considering all relevant facts and circumstances. Right-of-use assets and lease liabilities are initially recognised on the consolidated balance sheet at future fixed lease payments over the lease term. Lease payments are discounted to present value using an effective interest rate. Right-of-use assets are depreciated on a straight-line basis over the lease term and reviewed periodically for indication of impairment. When the future lease payments are revised due to changes in index-linked considerations or the lease term changes, the right-of-use asset and the corresponding lease liability is remeasured. Any differences arising on reassessments are recognised in the consolidated income statement. Interest expense on lease liabilities is presented within Interest expense in the consolidated income statement. In the consolidated cash flow statement, the principal portion of the lease payment is presented in the cash flow from financing activities.

Practical expedients applied in applying IFRS 16 for the first time, the group has used the following practical expedients permitted by the standard:

- accounting for operating leases with a remaining lease term of less than 12 months as at 1 January 2019 as short-term lease
- low-value leasing assets are not included

The effect of adoption IFRS 16 as at January 1, 2019 is as follows:

Assets

- Right-of-use-assets +EUR 523 thousand

Liabilities

- Non-current leasing liabilities +EUR 386 thousand
- Current leasing liabilities +EUR 137 thousand

IFRS 16 also impacts comparability for the following financial information:

- Depreciation expenses have increased significantly and correspondingly rent expenses decreased. Depreciation for right-of-use-assets totalled to EUR 137 thousand, rent expenses totalled EUR 151 thousand. This increased reported EBIT compared with 2018.
- Reported assets on 1 January 2019 have increased by EUR 523 thousand due to recognition of right-of-use-assets.
- Principal payments of lease liabilities are separately presented in the cash flow from financing activities and totalled to EUR 151 thousand.

2.20. Provisions and Contingent Liabilities

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

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

2.21. Critical Accounting Estimates and Significant Management Judgements in Applying Accounting Policies

Revenue Recognition

The Group early adopted IFRS 15 on 1 January 2017 with full retrospective application. In determining the amounts to be recognised as revenue, the Group uses its judgement in the following main issues:

- Identifying the performance obligations in the license agreements and determining whether the license provided is distinct - based on the Group's analysis, the license is distinct as the licensee is able to benefit from the license on its own at its current stage and the licensee has the responsibility for the development in that territory. The management has determined that the provision of data and information generated by the Group in connection with its own development activities to facilitate the licensees' territory-specific development efforts is immaterial (perfunctory) to the grant of the license to the IP and does not constitute a separate performance obligation.
- Management has concluded that the license meets the criteria to be classified as a right to use, as the license granted provides at the outset of the contract all necessary documents and knowhow to utilize the license. The contract does not define activities that would significantly affect the intellectual property to which the licensee has rights after the date of granting.

Share-based Compensation

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

Clinical Trial Accruals

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

2.22. New and Amended Standards and Interpretations Adopted by the Group

The group has adopted IFRS 16 Leases retrospectively from 1 January 2019, but has not restated comparatives for the 2018 reporting period, as permitted under the

specific transition provisions in the standard. The reclassifications and the adjustments arising from the new leasing rules are therefore recognised in the opening balance sheet on 1 January 2019.

On adoption of IFRS 16, the group recognised lease liabilities in relation to leases which had previously been classified as 'operating leases' under the principles of IAS 17 Leases. These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019.

Practical Expedients Applied

In applying IFRS 16 for the first time, the group has used the following practical expedients permitted by the standard:

- applying a single discount rate to a portfolio of leases with reasonably similar characteristics
- relying on previous assessments on whether leases are onerous as an alternative to performing an impairment review – there were no onerous contracts as at 1 January 2019
- accounting for operating leases with a remaining lease term of less than 12 months as at 1 January 2019 as short-term leases
- excluding initial direct costs for the measurement of the right-of-use asset at the date of initial application, and
- using hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

The group has also elected not to reassess whether a contract is or contains a lease at the date of initial application. Instead, for contracts entered into before the transition date the group relied on its assessment made applying IAS 17 and Interpretation 4 Determining whether an Arrangement contains a Lease.

3. REVENUE

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

License Agreement and Supply Agreement with Maruishi

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

In 2014, the Company entered into a separate supply agreement with Maruishi for the delivery of investigational medicinal products to be used in territory-specific clinical studies. In 2019 the Company has not recognised revenue from deliveries based on this agreement.

License Agreement with Pharmbio

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

4. SEGMENT REPORTING

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

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

The Group had no revenue in 2019 (EUR 19 thousand in 2018).

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

5. OTHER OPERATING INCOME

€'000	Year ended 31 December 2019	2018
Grants from the European Union	-	191
Other income	185	14
Total operating income	**185**	**205**

Grants from the European Union comprise of direct funding from the European Commission under the Seventh Framework Programme (FP7) for Research and Technological Development to support the Traumakine clinical program. The project funded with the FP7 -funding ended in 2H-2018.

The other income consisted of the reimbursement of already occurred legal expenses by the third-party recovery services provider as announced by the Company on 30 December 2019.

6. BREAKDOWN OF EXPENSES BY FUNCTION

Research and Development Expenses

€'000	Year ended 31 December 2019	2018
Materials and services	(5,604)	(7,311)
Employee benefits	(2,099)	(1,820)
Outsourced clinical trials services	(1,906)	(5,250)
Other R&D costs	(437)	(1,652)
Depreciation and amortization	(191)	(92)
Inventory write-down	-	(338)
Total research and development expenses	**(10,237)**	**(16,463)**

General and Administration Expenses

€'000	Year ended 31 December 2019	2018
Other G&A costs	(1,615)	(917)
Employee benefits	(1,177)	(1,330)
Communication	(210)	(137)
Depreciation and amortization	(47)	(8)
Internal financial and reporting process development	-	(1,358)
Total general and administrative expenses	**(3,049)**	**(3,750)**

7. EMPLOYEE BENEFITS

€'000	Year ended 31 December 2019	2018
Salaries	(2,711)	(2,816)
Pension expenses – contribution-based plans	(417)	(513)
Social security contributions	(97)	3
Share-based compensation	(51)	176
Total employee benefit expenses	**(3,276)**	**(3,150)**
Employee benefit expenses by function		
Research and development expenses	(2,099)	(1,820)
General and administrative expenses	(1,177)	(1,330)
Total employee benefit expenses	**(3,276)**	**(3,150)**

The average number of personnel in 2019 was 24 (2018: 25). Share-based compensation information is included in note 18 and management remuneration information in note 23.

8. DEPRECIATION AND AMORTISATION

€'000	Year ended 31 December 2019	2018
Depreciation and amortisation by type of asset		
Depreciation for right-of-use-assets	(137)	-
Intangible assets - patents	(94)	(92)
Intangible assets	(2)	(1)
Machinery and equipment	(4)	(7)
Total depreciation and amortisation	**(238)**	**(100)**
Depreciation and amortisation by function		
Research and development expenses	(191)	(92)
General and administrative expenses	(47)	(8)
Total depreciation and amortisation	**(238)**	**(100)**

Depreciation expenses have increased due to adoption of IFRS 16.

9. FINANCIAL INCOME AND EXPENSES

€'000	Year ended 31 December 2019	2018
Financial income		
Interest income	-	-
Gains from foreign exchange	74	302
Total financial income	**74**	**302**
Financial expenses		
Interest expenses	(133)	(121)
Losses from foreign exchange	(66)	(274)
Interest expenses from lease liabilities	(23)	-
Other financial expenses	(2)	(2)
Total financial expenses	**(224)**	**(397)**
Total financial income and expenses, net	**(150)**	**(95)**

Interest expenses consist of paid and accrued interest expenses. The accrued interest expense relates mainly to the government loans, see note 19. Interest expenses recognised from lease liabilities totalled to EUR 23 thousand due to adoption of IFRS 16.

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

Unrealised foreign exchange loss is EUR 7 thousand and loss is EUR 36 thousand for the years ended 31 December 2019 and 2018, respectively.

10. TAX EXPENSE

€'000	Year ended 31 December 2019	2018
Tax expense	(11)	(2)
Total tax expense	**(11)**	**(2)**

Income tax consists of foreign corporation tax.

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

€'000	Year ended 31 December 2019	2018
Loss before tax	(13,251)	(20,084)
Income tax calculated at Finnish tax rate 20%	2,650	4,017
Tax losses and temporary differences for which no deferred tax asset is recognised	(2,858)	(4,268)
Non-deductible expenses and tax exempt income	208	251
Non-credited foreign withholding taxes	(11)	(2)
Taxes in the statement of comprehensive income	**(11)**	**(2)**

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

€'000	Year ended 31 December 2019	2018
R&D expenses not yet deducted in taxation[(1)]	58,606	49,063
Tax losses carried forward[(2)]	16,053	11,151
Deferred tax depreciation on fixed assets	-	-
Total	**74,659**	**60,214**

(1) The Group has incurred research and development costs, that have not yet been deducted in its taxation. The amount deferred for tax purposes can be deducted over an indefinite period.

(2) Tax losses carried forward expire over the period of 10 years. The tax losses will expire as follows:

€'000	2019	2018
Expiry within five years	31	1,164
Expiry within 6-10 years	16,022	9,987
Total	**16,053**	**11,151**

The related deferred tax assets have not been recognised in the balance sheet due to the uncertainty as to whether they can be utilized. The Group has a loss history, which is considered a significant factor in the consideration of not recognising deferred tax assets. The total tax value of unrecognised deferred tax assets is EUR 14,932 thousand (2018: EUR 12,043 thousand).

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

11. LOSS PER SHARE

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

€'000	Year ended 31 December 2019	2018
Loss for the period	(13,262)	(20,086)
Weighted average number of ordinary shares in issue	36,850,577	30,749,648
Basic and dilutive loss per share (in €)	**(0.36)**	**(0.65)**

As of 31 December 2019, Faron Pharmaceuticals Ltd. had only share options outstanding. Number of potentially dilutive instruments currently outstanding totalled 1,540,900 as of 31 December 2019 (31 December 2018: 1,540,900). Since the Group has reported a net loss, the share options would have an anti-dilutive effect and are therefore not taken into account in diluted loss per share-calculation. As such, there is no difference between basic and diluted loss per share.

12. INTANGIBLE ASSETS AND MACHINERY AND EQUIPMENT

€'000	Intangible assets	Machinery and equipment
Book value on 1 January 2019	**525**	**17**
Additions	100	-
Disposals	-	-
Depreciation/amortisation	(96)	(4)
Book value 31 December 2019	**529**	**13**
As at 31 December 2019		
Acquisition cost	923	39
Accumulated disposals	-	-
Accumulated depreciation/amortisation	(394)	(26)
Book value 31 December 2019	**529**	**13**
Book value 1 January 2018	**325**	**22**
Additions	293	2
Disposals	-	-
Depreciation/amortisation	(93)	(7)
Book value 31 December 2018	**525**	**17**
As at 31 December 2018		
Acquisition cost	823	39
Accumulated disposals	-	-
Accumulated depreciation/amortisation	(298)	(22)
Book value 31 December 2018	**525**	**17**

13. NON-CURRENT PREPAYMENTS AND OTHER RECEIVABLES

€'000	As at 31 December 2019	2018
Prepayments for API	-	524
Production supplies	38	76
Other receivables	39	36
Total non-current prepayments and other receivables	**77**	**636**

Group has written down prepayments for API due to uncertainty to be consumed in the Group's development activities. Other receivables consist mainly of restricted cash in the form of security deposits for rental agreements.

14. RIGHT-OF-USE-ASSETS AND LEASING LIABILITIES

€'000	31 December 2019	1 January 2019
Right-of-use assets		
Office	366	485
Vehicle	20	39
Total right-of-use assets	**386**	**523**
Lease liabilities		
Long-term leasing liability	261	386
Short-term leasing liability	134	137
Total leasing liabilities	**395**	**523**

There were no additions to right-of-use assets in 2019.

15. CURRENT PREPAYMENTS AND OTHER RECEIVABLES

	Group		*Parent*	
	As at 31 December			
€'000	2019	2018	2019	2018
Prepayments	895	1,814	895	1,814
Other receivables	521	162	521	162
Receivable for production defects	434	434	434	434
VAT receivable	295	349	295	349
Total current prepayments and other receivables	**2,145**	**2,759**	**2,145**	**2,759**

The majority of prepayments consist of the Clinical Service Agreements with Contract Research Organisations, which are current service providers in different clinical trials. Other receivables include the receivables from the third-party recovery services provider as announced by the Group on 30 December 2019.

16. CASH AND CASH EQUIVALENTS

	Group		Parent	
	As at 31 December			
€'000	2019	2018	2019	2018
Bank accounts	7,059	4,067	7,058	4,058
Total cash and cash equivalents	**7,059**	**4,067**	**7,058**	**4,058**

17. SHAREHOLDERS' EQUITY

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

€'000	Total registered shares (pcs)	Share capital	Reserve for unrestricted equity
1 January 2018	**29,164,544**	**2,691**	**48,576**
Issue of new shares, net of transaction costs	1,863,350	-	15,888
31 December 2018	**31,027,894**	**2,691**	**64,464**
1 January 2019	**31,027,894**	**2,691**	**64,464**
Issue of new shares, net of transaction costs	12,262,853	-	14,452
31 December 2019	**43,290,747**	**2,691**	**78,916**

On 19 February 2018, the number of shares was increased to 29,336,744 following the issue of 172,200 new shares, on 21 February 2018, the number of shares was increased to 30,094,744 following the issue of 758,000 new shares and on 26 February 2018 the number of shares was increased to 31,027,894 following the issue of 933,150 new shares.

On 28 March 2019, the number of shares was increased to 35,476,519 following the issue of 4,448,625 new shares, on 13 May 2019 the number of shares was increased to 37,233,894 following the issue of 1,757,375 new shares. On 5 August 2019, the number of shares was increased to 38,175,734 following the issue of 941,840 new shares, on 27 August 2019, the number of shares was increased to 39,355,427 following the issue of 1,179,513 new shares and on 12 November 2019 the number of shares was increased to 43,290,747 following the issue of 3,935,500 new shares.

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

The subscription price for the shares is recorded to the share capital, unless the Board has made a resolution to record the subscription price in the reserve for invested unrestricted equity. If the shares of a Finnish limited liability company have no par value according to its articles of association, the Finnish Limited Liability Companies Act allows companies the recognition of the proceeds from share issuance to the reserve for invested unrestricted equity. In such situations the board of a company can choose on a subscription by subscription basis, how much of the issue, if anything, is recorded in share capital and how much to the reserve for invested unrestricted equity that is distributable. During 2018 and 2019, the Board recognised all relevant transactions in the invested unrestricted equity reserve.

18. SHARE OPTIONS

Option Plan 2015

The Option Plan 2015 was approved at the Company's extraordinary shareholders' meeting on 15 September 2015 as part of the Group's incentive scheme determined by the Board of Directors. The share options are granted to the members of the Board of Directors and the management team and other management and employees for no consideration. The annual general meeting on 16 May 2017 resolved to amend, due to the increase in the number of employees in the Group and the increase in the number of members of the Board of Directors, the Option Plan so that a maximum total of 500,000 C options and a maximum total of 500,000 D options may be offered under initial Option Plan terms and conditions. The share options have a service condition and are forfeited in case the employee leaves the Company before the share options vest, unless the Board of Directors approves otherwise. After the beginning of the share subscription period, the vested options may be freely transferred or exercised. The fair value of the options has been determined using the Black & Scholes option valuation model and expensed over the vesting period. Grant dates for the share options may vary depending on the date when the Company and the employees agree to the key terms and conditions of the Option Plan. The maximum number of share options that can be awarded under the Option Plan is 1.800.000 in four different tranches designated as A options, B options, C options and D options. Each share option entitles the holder of the option to subscribe for one ordinary share in the Company.

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

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

The date of the allocation of D options to the employees and key management is 30 June 2019, which has been used in the option calculations.

2015 Option Plan	A options	B options	C options	D options
Maximum number of share options	400,000	400,000	500,000	500,000
Exercise price, EUR	3.71	2.90	8.39	1.09
Dividend adjustment	No	No	No	No
Beginning of subscription period	2 November 2015	8 October 2016	8 October 2017	8 October 2018
End of subscription period	30 September 2021	30 September 2021	30 September 2021	30 September 2021
Vesting conditions	Service until the beginning of the subscription period			

	2019 2015 Option Plan				2018 2015 Option Plan			
Number of share options	**A**	**B**	**C**	**D**	**A**	**B**	**C**	**D**
Outstanding at 1 January	385,000	385,900	500,000	270,000	385,000	385,900	500,000	270,000
Granted	-	-	-	230,000	-	-	-	-
Forfeited	-	-	-	-	-	-	-	-
Exercised	-	-	-	-	-	-	-	-
Outstanding at 31 December	385,000	385,900	500,000	500,000	385,000	385,900	500,000	270,000
Exercisable at 31 December	385,000	385,900	500,000	-	385,000	385,900	500,000	-
The weighted average fair value of the share options granted, EUR	-	-	-	-	-	-	-	-
The weighted average share price at the date of exercise, EUR	3.24	3.67	6.20	3.45	3.24	3.67	6.20	3.45

	2019 2015 Option Plan		2018 2015 Option Plan	
Determination of the fair value for the share options granted	**C**	**D**	**C**	**D**
Share price at grant date, EUR	4.51–9.39	0.62–4.96	4.51–9.39	0.62–4.96
Subscription price, EUR	4.51–8.39	1.09–4.96	4.51–8.39	1.09–4.96
Volatility, %(*)	42.59–52.57	55.60	42.59–52.57	55.60
Interest free rate, %	0.01	0.01	0.01	0.01
Expected dividends yield, %	0	0	0	0
Option fair value, EUR	1.42–4.01	0.11–1.25	1.42–4.01	0.11–1.25

(*) Expected volatility was determined as the average volatility of a peer group consisting of ten comparable biotechnology companies listed on London Stock Exchange AIM list.

There was no effect on earnings 2019 or 2018 based on share options granted.

The share-based compensation expense for the Option Plan 2015, was EUR 51 thousand in 2019 (positive of EUR 176 thousand in 2018).

19. FINANCIAL ASSETS AND LIABILITIES

	Group		Parent	
	As at 31 December			
€'000	2019	2018	2019	2018
Financial assets measured at amortised cost				
Other receivables(*)	334	385	334	385
Cash and cash equivalents	7,059	4,067	7,058	4,058
Total financial assets measured at amortised cost	**7,393**	**4,452**	**7,392**	**4,443**
Financial liabilities measured at amortised cost				
Trade payables	2,967	3,534	3,173	3,533
Borrowings in form of Tekes R&D loans	2,426	2,132	2,426	2,132
Total financial liabilities measured at amortised cost	**5,393**	**5,666**	**5,599**	**5,665**

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

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

Borrowings in the Form of Tekes R&D Loans

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

The fair value of all the Tekes loans was EUR 2,099 thousand (2018 EUR 1,792 thousand).

Tekes R&D loans are granted to a defined product development project and cover a contractually defined portion of the underlying development projects' R&D expenses. The below-market interest rate for these loans is the base rate set by the Ministry of Finance minus three (3) percentage points, subject to a minimum rate of 1%. Repayment of these loans shall be initiated after 5 years, thereafter loan principals shall be paid back in equal instalments over a 5-year period, unless otherwise agreed with Tekes. For more information on contractual maturities of the Tekes R&D loans and interests is provided in the note 19. The accrued interest on Tekes R&D loans amounted to EUR 107 thousand (2018 EUR 79 thousand). Grant payments received in advance of the incurrence of the costs the grant is intended to compensate are deferred at the reporting date and presented under advances received on the balance sheet.

This section sets out an analysis of net debt and the movements in net debt (calculated as cash and cash equivalents less borrowings) for each of the periods presented. Lease liabilities are included in analysis as of 1 January 2019.

	Group		Parent	
	As at 31 December			
€'000	2019	2018	2019	2018
Net debt				
Cash and cash equivalents	7,059	4,067	7,058	4,058
Lease liabilities	(396)	-	(396)	-
Tekes R&D loans- repayable within one year	(163)	(245)	(163)	(245)
Tekes R&D loans- repayable after one year	(2,263)	(1,887)	(2,263)	(1,887)
Net debt	**4,237**	**1,935**	**4,236**	**1,926**

	Group			Parent		
€'000	Cash and cash equivalents	Borrowings	Total	Cash and cash equivalents	Borrowings	Total
Net debt as at 1 Jan 2018	**9,310**	**(2,426)**	**6,884**	**9,310**	**(2,426)**	**6,884**
Cash flows	(5,279)	347	(4,933)	(5,288)	347	(4,941)
Foreign exchange adj.	36	-	36	36	-	36
Other non-cash movements	-	(53)	(53)	-	(53)	(53)
Net debt as at 31 Dec 2018	**4,067**	**(2,132)**	**1,935**	**4,058**	**(2,132)**	**1,926**
Cash flows	2,985	(307)	2,678	2,984	(307)	2,677
Foreign exchange adj.	7	-	7	16	-	16
Lease liability	-	(396)	(396)	-	(396)	(396)
Other non-cash movements	-	13	13	-	13	13
Net debt as at 31 Dec 2019	**7,059**	**(2,822)**	**4,237**	**7,058**	**(2,822)**	**4,236**

20. FINANCIAL RISK MANAGEMENT

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

(a) Capital Management and Liquidity Risks

The Group's objective when managing capital is to safeguard the Group's ability to continue as a going concern (refer to notes 2.2 and 16).

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

Faron Pharmaceuticals Ltd. has been able to fund its operations with equity and R&D loans. While equity financing has been available in the past, there can be no assurance that sufficient funds can be secured in order to permit the Group to carry out its planned activities. In general, capital market conditions are volatile. The

prevailing financial market situation and the overall investor's sentiment dictate whether the Group is able to secure additional financing in the future, which can be considered a risk. To partly manage this risk, the Group and its management is in constant dialogue with financial investors, investment banks, debt providers and other market participants.

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

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

There can be no assurance that sufficient financing can be secured in order to permit the Group to carry out its planned activities. To protect the continuity of the Group's operations, sufficient liquidity and capital has to be maintained. The Group aims to have funds to finance its operations for the foreseeable future. The Group can influence the amount of capital by adapting its cost basis considering available financing. Management monitors liquidity on the basis of the amount of funds. These are reported to the Board of Directors on a monthly basis.

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

As at 31 December 2019, the contractual maturity of loans and interests was as follows:

€'000	2020	2021	2022	2023-thereafter	Total
R&D loans					
Repayment of loans	163	257	564	1,811	2,795
Interest expenses	28	26	21	32	107
Lease liabilities(*)	261	138	11	0	411
Total	**452**	**421**	**596**	**1,843**	**3,313**

(*) These are lease liabilities relating to IFRS 16 adoption on 1 January 2019.

As at 31 December 2018, the contractual maturity of loans and interests was as follows:

€'000	2019	2020	2021	2022-thereafter	Total
R&D loans					
Repayment of loans	245	245	338	1,304	2,132
Interest expenses	23	21	17	23	85
Total	**268**	**265**	**356**	**1,328**	**2,217**

(b) Market Risk

i. Foreign Exchange Risk

The Group operates internationally but is mainly exposed to translation risk in respect of Pound Sterling ("GBP") denominated cash and cash equivalents balances The Group's policy is not to hedge translation risk. As of 31 December 2019, the Group had cash and cash equivalents of EUR 6,611 thousand and GBP 380 thousand (2018: EUR 4,058 thousand and GBP 0 thousand) and the foreign exchange gains and losses recorded arise mainly from the GBP cash balances. The Group is not exposed to significant transaction risk, as the Group mainly operates in its functional currency, the EUR.

ii. Interest Rate Risk

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

(c) Credit and Counterparty Risk

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

21. TRADE PAYABLES AND OTHER CURRENT LIABILITIES

	Group		*Parent*	
	As at 31 December			
€'000	**2019**	**2018**	**2019**	**2018**
Trade payables	2,967	3,534	3,173	3,533
Clinical trial hospital fees	849	268	849	268
Accrued research & development costs	811	749	811	749
Accrued payroll	603	527	558	527
Other liabilities	306	281	300	281
Other accruals	166	142	166	142
Advances received	75	-	75	-
Total	**5,777**	**5,501**	**5,932**	**5,500**

Other liabilities comprise mainly of unpaid prepayment to FP7 -grant consortium members.

22. CONTINGENCIES AND COMMITMENTS

Operating Lease – Faron as a Lessee

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

€'000	Year ended 31 December	
	2019	**2018**
No later than 1 year	68	179
Later than 1 year and no later than 5 years	131	82
Later than 5 years	-	-

The Group's operating lease commitments comprise of lease commitments for machines and equipment with low value leases of 3 to 4 years and one time-limited office rent agreement which will be taken into use in the coming months. The Group's operating leases are non-cancellable and they do not include redemption or extension options. Contingencies and commitments liabilities do not include lease liabilities that are recognised as lease liabilities on the balance sheet.

Contractual Contingencies

The Group has a contingent contractual liability to a development party for pre-clinical product candidate Clevegen to pay additional milestone payments. Second milestone payment of EUR 460 thousand payable when production system reached certain material yield threshold was charged 2019. The remaining ones become payable upon the Group achieving subsequent regulatory filings and approvals for Clevegen.

As announced by the Group on 2 October 2019 and 30 December 2019, Faron Pharmaceuticals Ltd. has received a letter from Rentschler Biopharma SE in which Rentschler terminates the agreement concerning the API manufacturing. The Company considers that this said termination is without merit and has filed a request for arbitration to seek damages. To fund the proceedings, the Company has entered into a litigation funding agreement with a third-party recovery services provider, which in the event of success would receive a typical portion of any damages awarded.

23. RELATED PARTY TRANSACTIONS

Parent and subsidiary relations of Faron Pharmaceuticals Group on 31 December 2019:

	Country	**Group holding %**	**Group voting %**
Companies owned by the parent company			
Faron Europe GmbH	Switzerland	100	100
Faron USA LLC	USA	100	100

The Group identifies the following related parties:

- Members of the Board of Directors, and their close family members; and
- Company's key Management team and their close family members

Faron Pharmaceuticals Ltd. has not had interests in other entities as at, and for the years ended, December 31, 2018 and 2019.

Key Management Personnel

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

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

€'000	Year ended 31 December 2019	2018
Compensation of key management personnel(*)		
Salaries and other short-term employee benefits	1,350	1,535
Post-employment benefits	242	288
Share-based payments	51	(176)
Total	**1,643**	**1,647**

(*) Presented information for the Management includes the executive directors of the Board

The Management team was awarded 265,000 share options during 2019 (2018: 0 share options). At the end of the 2019, the number of outstanding options and share granted to the Management team amounted to 800,680 share options (at the end of 2018: 663,450 share options).

Non-executive Directors were awarded 120,000 share options during 2019, (2018: 0 share options). At the end of 2019, the number of outstanding options and share options granted to the non-executive directors amounted to 400,000 share options (at the end of 2018: 600,000 share options).

Management and Board Shareholding

Management(*) shareholding, 31 December 2019	
Number of shares (pcs)	4,684,920
Shareholding, percentage	10.8 %
Board(**) shareholding, 31 December 2019 (excluding the shareholding of CEO and CFO)	
Number of shares (pcs)	679 778
Shareholding, percentage	1.6 %
Total number of shares outstanding at 31 December 2019 (pcs)	**43,290,747**

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

Transactions with Related Parties

There are no additional related party transactions during 2018 and 2019 than already disclosed.

24. EVENTS AFTER THE BALANCE SHEET DATE

There are no events after the balance sheet date.

Result and Dividends

The statement of comprehensive income is on page 9.

The Group's loss for the accounting period was 13,261,911.93 euro (2018: 20,086,402.06 euro).

The Board of Directors does not recommend the payment of a dividend (2018: nil).

BOARD SIGNATURES

Turku, 19 March 2020

Frank Armstrong
Chairman

Markku Jalkanen

Gregory Brown

Matti Manner

John Poulos

Leopoldo Zambeletti

THE AUDITOR'S NOTE

The report on the audit performed has been issued today
Helsinki, 19 March 2020
PricewaterhouseCoopers Oy
Authorised Public Accountants

Panu Vänskä
Authorised Public Accountant (KHT)

Auditor's Report (Translation of the Finnish Original)

To the Annual General Meeting of Faron Pharmaceuticals Oy

Report on the Audit of the Financial Statements

Opinion

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

What we have audited

We have audited the financial statements of Faron Pharmaceuticals Oy (business identity code 2068285-4) for the year ended 31 December 2019. The financial statements comprise:

- the consolidated balance sheet, statement of comprehensive income, statement of changes in equity, statement of cash flows and notes
- the parent company's balance sheet, statement of comprehensive income, statement of changes in equity, statement of cash flows and notes.

Basis for Opinion

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

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

Independence

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

Material Uncertainty Related to Going Concern

We draw attention to the notes in financial statements on page 7, item 2.2 "Going concern". As mentioned in the note the additional finance is not committed at the date of approval of the financial statements. This together with other items mentioned in the note indicates, that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

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

The Board of Directors and the Managing Director are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, and of financial statements that give a true and fair view in accordance with the laws and regulations governing the preparation of financial statements in Finland and comply with statutory requirements.

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Reg. Domicile Helsinki, Business ID 0486406-8

The Board of Directors and the Managing Director are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the parent company's or the group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the Board of Directors' and the Managing Director's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the parent company's or the group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the parent company or the group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events so that the financial statements give a true and fair view.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

Other Reporting Requirements

Other Information

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

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

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

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

Helsinki 19 March 2020

PricewaterhouseCoopers Oy
Authorised Public Accountants

Panu Vänskä
Authorised Public Accountant (KHT)

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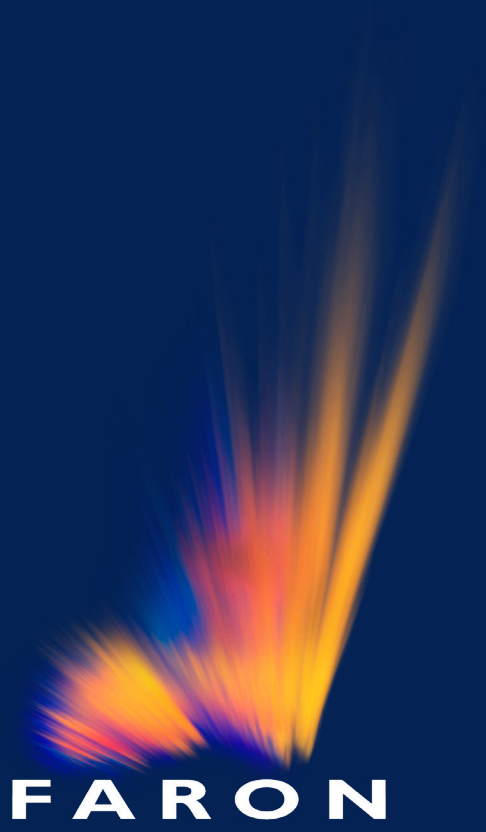
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