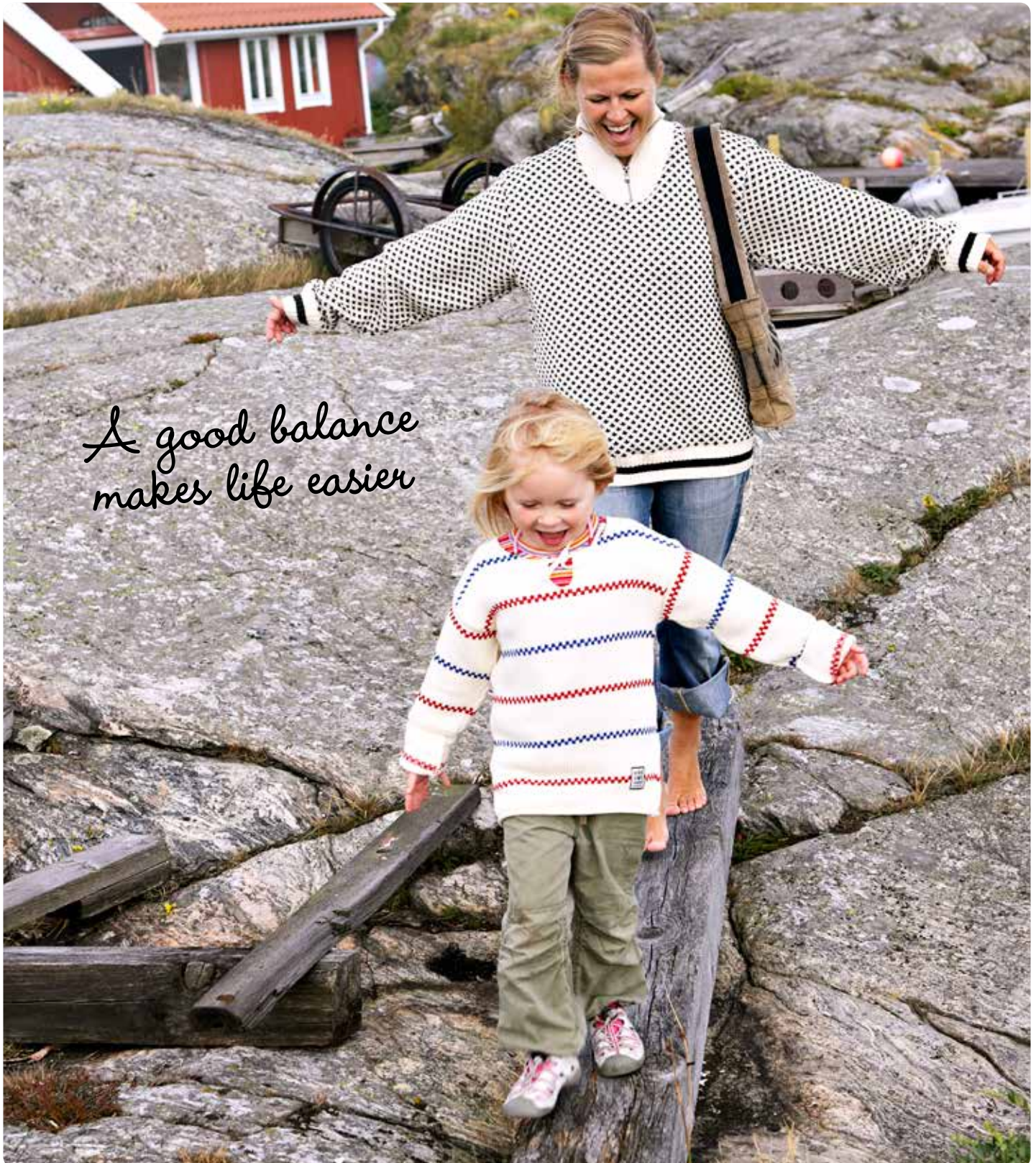


# BioGaia®

ANNUAL REPORT 2014

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*A good balance  
makes life easier*

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## The Annual General Meeting

will be held on Thursday, 7 May 2015,  
4:00 p.m. at Lundqvist & Lindquist Klara  
Strand, Klarabergsviadukten 90, in Stockholm.

The annual report will be distributed to all shareholders.

The year-end report, annual report and quarterly reports are also published in English. All financial information is published on [www.biogaia.com](http://www.biogaia.com) and can be ordered from BioGaia's head office, + 46 9 555 293 00, or through [info@biogaia.se](mailto:info@biogaia.se).





# Highlights of 2014

## ► QUARTER 1

New studies show that

- colic can be prevented
- common infections in children can be prevented
- no significant differences in diabetes study.

Launches

- drops with Vitamin D in Greece, Slovenia and Germany
- drops and oral rehydration product in Libya
- infant formula with *Lactobacillus reuteri* Protectis in Ukraine, Russia and the CIS countries
- oral health tablets in Greece
- drops and digestive health tablets with strawberry flavour in Norway
- drops with Vitamin D and digestive health tablets with Vitamin D in Hungary.

BioGaia receives contingent consideration pertaining to license revenue from Nestlé of EUR 10.8 million (SEK 95.4 million).

New extended agreement with Nestlé.

## ► QUARTER 2

Launches

- oral rehydration product with orange flavour in Greece
- drops and Gastrus digestive health tablets in South Korea and China
- digestive health tablets with Vitamin D in Estonia and Lithuania
- drops med with Vitamin D and K in Italy.

Agreements for the sale of drops in India and the UK.

Decision to expand the subsidiary TwoPac's production plant in Eslöv.

## ► QUARTER 3

Launches

- relaunch of digestive health tablets in Brazil
- oral rehydration product in France
- oral health tablets in Cyprus.

## ► QUARTER 4

Studies

- Infants with colic cry less with BioGaia's drops
- BioGaia Protectis tablets are effective in constipated adults.

Launches

- drops in Brazil
- drops with Vitamin D in Ukraine and Croatia
- oral rehydration product in Belgium
- infant formula with *Lactobacillus reuteri* Protectis in Switzerland.

Decision to invest in MetaboGen AB.

## ► Key events after the end of the year

Agreement for the sale of drops in Vietnam.

Launches

- Nestlé launches infant formula products with *Lactobacillus reuteri* Protectis for children above the age of one year.

## 5-year overview

Key ratios	2014	2014 <sup>1)</sup>	2013	2012	2012 <sup>1)</sup>	2011	2010
Net sales, SEK M	481.8	386.4	315.9	645.2	289.2	315.0	236.0
Net sales Paediatrics, SEK M	409.1	313.7	238.6	E/T	E/T	E/T	E/T
Net sales Adult Health, SEK M	69.4	69.4	75.6	E/T	E/T	E/T	E/T
Net sales of finished consumer products, SEK M	303.6	303.6	256.2	237.6	237.6	215.4	165.6
Net sales of component products, SEK M	176.1	80.7	58.6	406.6	50.6	97.7	68.6
Operating profit, SEK M	196.9	101.5	81.7	428.1	72.1	103.2	56.3
Profit before tax, SEK M	192.5	97.1	83.8	442.2	86.2	108.9	69.7
Profit after tax, SEK M	148.0	73.6	64.2	329.9	63.7	76.4	47.2
Sales growth, %	53	22	9	105	-8	33	16
Operating margin, %	41	26	26	66	25	33	24
Equity/assets ratio, %	83	84	83	88	82	82	82
Average number of employees	90	90	82	70	70	61	45

1) Excluding license revenue from Nestlé (for more information, see administration report).

# A successful year with challenges

**HOW DOES THAT GO TOGETHER?** With sales growth of 22 per cent<sup>1</sup> and an operating margin of 26 per cent, 2014 can only be summed up as a successful year. Although one of our most important markets, Ukraine, declined significantly during the year, this negative trend was offset by very strong development in Brazil, where we launched during the autumn. It is gratifying to see that nearly all of our markets are growing at a solid pace and that the BioGaia brand is becoming more and more established, particularly among paediatricians, as the safest and most effective probiotic on the market.

On the other hand, we did face challenges in the form of problems with the stability of the bacteria cultures from one of our suppliers. On delivery the cultures met specifications, but in the finished product the shelf life was shorter than normal. The problem was detected through BioGaia's own control system. We had to devote a lot of time and resources to finding the root of the problem and meeting the immediate need for cultures. Not only did we have to recall a number of products from our partners, which cost us a total of around SEK 11 million, our product developers were not able to focus fully on developing new products but were instead forced to address the acute stability problem. Thanks to our quick initiation of a comprehensive action plan, we now have the stability problem under control. The plan includes both short-term measures and an ambitious development project to build further knowledge in the fermentation area.

Our close collaboration with Nestlé has continued and during the year resulted in a new agreement through which we received the remaining outstanding payments under the agreement from 2012. It will also provide us with royalty payments for which we will carry out a number of clinical studies and develop new products for Nestlé in whole new areas. It is my assessment that the agreement is of great significance for BioGaia's future development.

**POSITIVE RESULTS FROM CLINICAL STUDIES** Clinical studies are our most important marketing tool and a number of new studies with our products were published during the year. Two of these concerned children with colic, one that showed significant positive results and one with neutral results. However, the neutral study, in which we only provided the researchers with study product and placebo, was so poorly executed that we could easily explain the results to our distributors, and they in turn to the paediatricians they visit. We now have a total of four positive colic studies, which is more than enough to convince doctors that the product works.

We also obtained results from a study on small children showing that *Lactobacillus reuteri* Protectis can prevent infections and reduce the number of doctor's visits and the use of antibiotics. These are exceptionally satisfying findings that in a longer perspective can give us additional opportunities to work more with prevention of infections. There is a vital and urgent debate underway regarding reduction of antibiotic use, and I welcome a discussion with a wider scope that also evaluates preventative initiatives other than the development of new antibiotics to treat already existing infections.

Another area where we now have convincing data is con-

stipation, which will open new opportunities to position our products also in this area.

Unfortunately, we obtained neutral results in our diabetes study and have consequently decided not to continue investing in this area for the time being.

**DRUG INVESTMENT IN IBT MOVING FORWARD** Our subsidiary IBT was formed to develop a drug to prevent NEC, a fatal disease that often affects premature newborns. And the company is now going from strength to strength. We have been granted orphan drug status in both the USA and Europe, started development of the manufacturing process and hired a bank to help us secure financing through a license with a pharmaceutical company. During the year, consolidated profit was charged with costs of SEK 6.7 million related to IBT.

**TWOPAC INVESTING FURTHER** Our manufacturing company TwoPac is working intensively to receive GMP approval from the Swedish Medical Products Agency at the same time as new machinery and products are being developed at a rapid rate. In June 2014 a decision was made for TwoPac to build another production plant adjacent to the existing facility in Eslöv. The investment is estimated at SEK 16 million. I am certain that the steps we are taking in TwoPac will be decisive in enabling us to maintain our innovation rate and gain entrance to markets with rigorous regulatory requirements.

**METABOGEN – RESEARCH AT THE CUTTING EDGE** Towards the end of the year we decided to invest SEK 12 million in the Gothenburg-based company MetaboGen AB, which was founded by the highly successful professors *Fredrik Bäckhed* and *Jens Nielsen*. The company conducts research on the so-called microbiome, which is the collective genetic material contained by the large number of bacteria in the gut flora. The assumption is that the microbiome affects the onset of various diseases and that by altering its composition, it is possible to positively impact health. We see this as a natural expansion of the probiotic concept and want to be at the cutting edge of this exciting development. Major corporations such as Johnson & Johnson and Nestlé are investing aggressively in this area.

**AN EXCITING FUTURE** During the year we also succeeded in signing agreements to introduce our products in a few major markets such as the UK and India, where we are now working intensively to ensure successful launches. In light of the potential in these markets and Brazil, where we are off to an excellent start, I am optimistic about 2015 and expect BioGaia to maintain a high rate of growth. At the same time, we are continuing to focus on further clinical studies and product development and are investing in TwoPac and IBT. I therefore anticipate strong growth in the company in both the short and long term.



PETER ROTHSCHILD,  
FOUNDER AND PRESIDENT, BIOGAIA

<sup>1</sup> Excluding license revenue from Nestlé. Including license revenue, growth was 53 per cent and the operating margin was 41 per cent.



# About BioGaia

**BUSINESS CONCEPT** ► BioGaia develops, markets and sells probiotic products with documented health benefits. The products are primarily based on different strains of the lactic acid bacterium *Lactobacillus reuteri* in combination with unique packaging solutions that make it possible to create products with a long shelf life.

► **FOUNDED IN 1990** by Peter Rothschild and Jan Anrwall.

► **PRIMARY POSITIONING** “Clinically Proven Probiotics”. Dietary supplements containing scientifically tested probiotics of a high quality that are sold in pharmacies and similar sales outlets. In most markets, the products are recommended by doctors or other healthcare professionals.

► **PRODUCTS** BioGaia sells products for both children and adults. The Paediatrics business unit accounts for approximately 80 per cent of BioGaia’s net sales and Adult Health for close to 20 per cent. Read more about the products on pages 16-17.

► **SALES** The products are sold by local distribution partners in 90 countries.

► **BIOGAIA AROUND THE WORLD**

- The corporate headquarters with the executive management, administrative functions and departments for marketing and sales are based in Stockholm
- Product development and departments for production and quality control are based in Lund
- Sales offices in Hiroshima, Japan, and Shanghai, China. In Raleigh, USA, there is a laboratory
- Production plant in the subsidiary TwoPac in Eslöv
- Around 60 distribution partners with sales in some 90 countries
- Research collaborations with around 50 universities and hospitals around the world

► **BIOGAIA’S CLASS B SHARE** is quoted on the Mid Cap list of NASDAQ OMX Nordic Exchange Stockholm.



# Organisation

Despite growing sales around the world and in different indication areas, BioGaia's ambition is to preserve the advantages of a small company in the form of short decision-making paths. This is facilitated by BioGaia's business model based on external networks.

Since the autumn of 2013 the company is divided into three business units, Paediatrics, Adult Health and New Business. Support functions have been retained at the central level, but the business units are responsible for product development and sales to their respective target groups. The aim of the reorganisation is to achieve a better focus and more effective decision-making. In 2014 additional adjustments were made and the effects of the new organisation are already starting to emerge.

► **FOUR SUBSIDIARIES** BioGaia Japan and CapAble are the oldest subsidiaries, and were founded in 2006 and 2008, respectively (read more about them on page 28). TwoPac was previously 50 per cent-owned by BioGaia but became a wholly owned subsidiary in mid-2013. In November the same year, the subsidiary Infant Bacterial Therapeutics was formed (read more about IBT on page 4).

► **NUMBER OF EMPLOYEES** 95 employees, of whom 34 are based in Stockholm, 28 in Lund, 22 in Eslöv, three in Raleigh, USA, six in Hiroshima, Japan, and two in Shanghai, China.

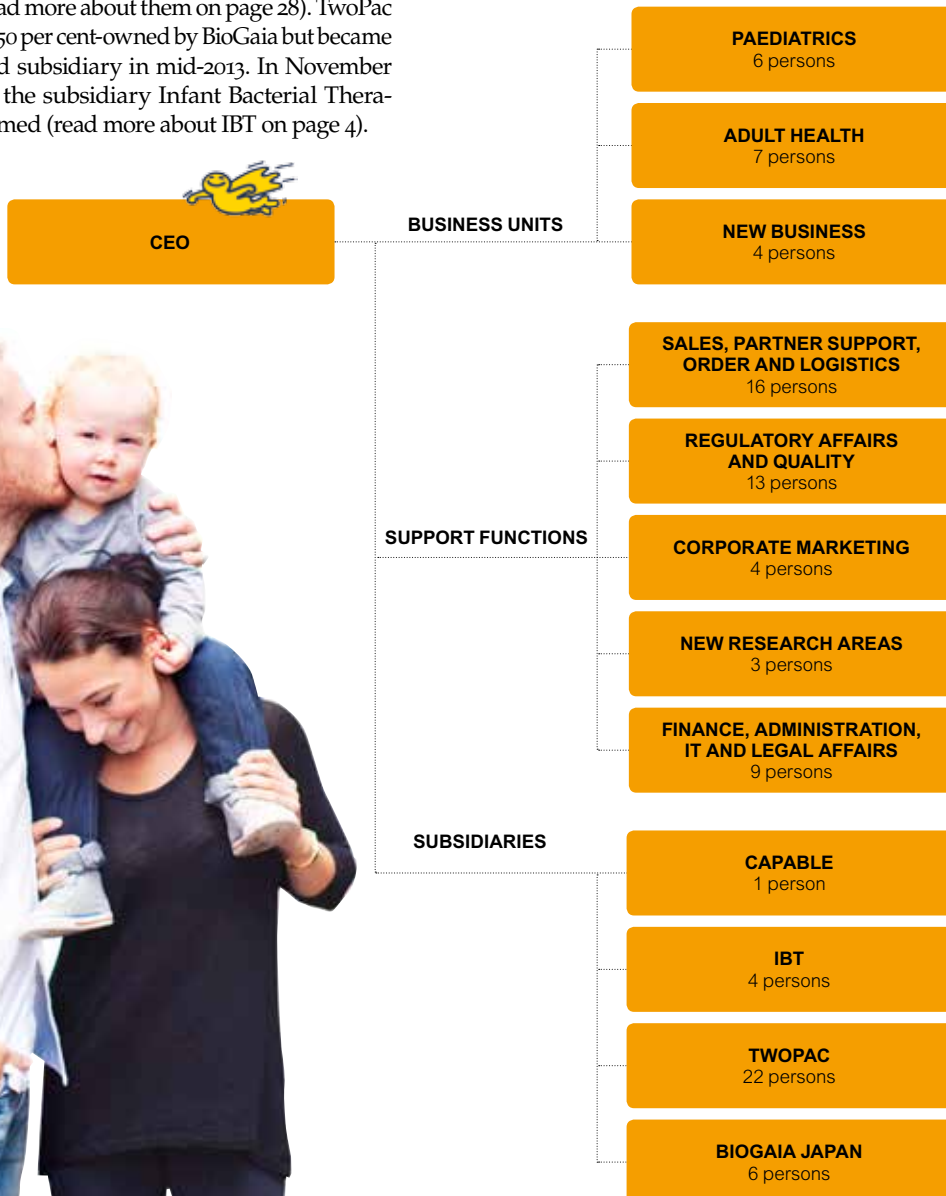
► **NEW HIRES** 17 people, while 7 people left the company.

► **AVERAGE TERM OF SERVICE** 7 years.

► **AVERAGE AGE** 43 years.

► **HIGH LEVEL OF EXPERTISE** Around 70 employees have a university education or the equivalent, and five hold a doctor's degree.

► **LOW SICKNESS ABSENCE** In 2014 the employees had an average of 4.4 sick days, including two people on long-term sick leave. Excluding long-term sick leave, the average number of sick days is 2.4.



# Business model

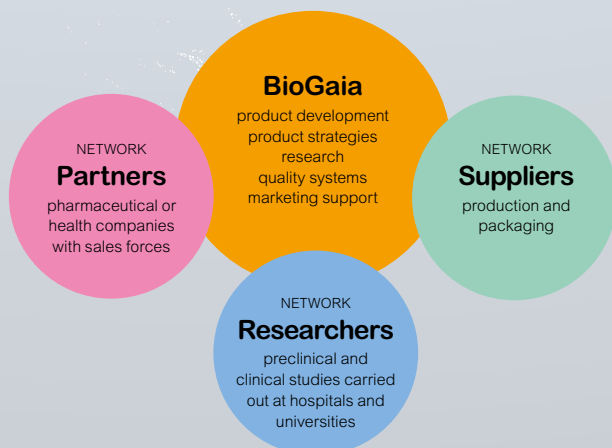
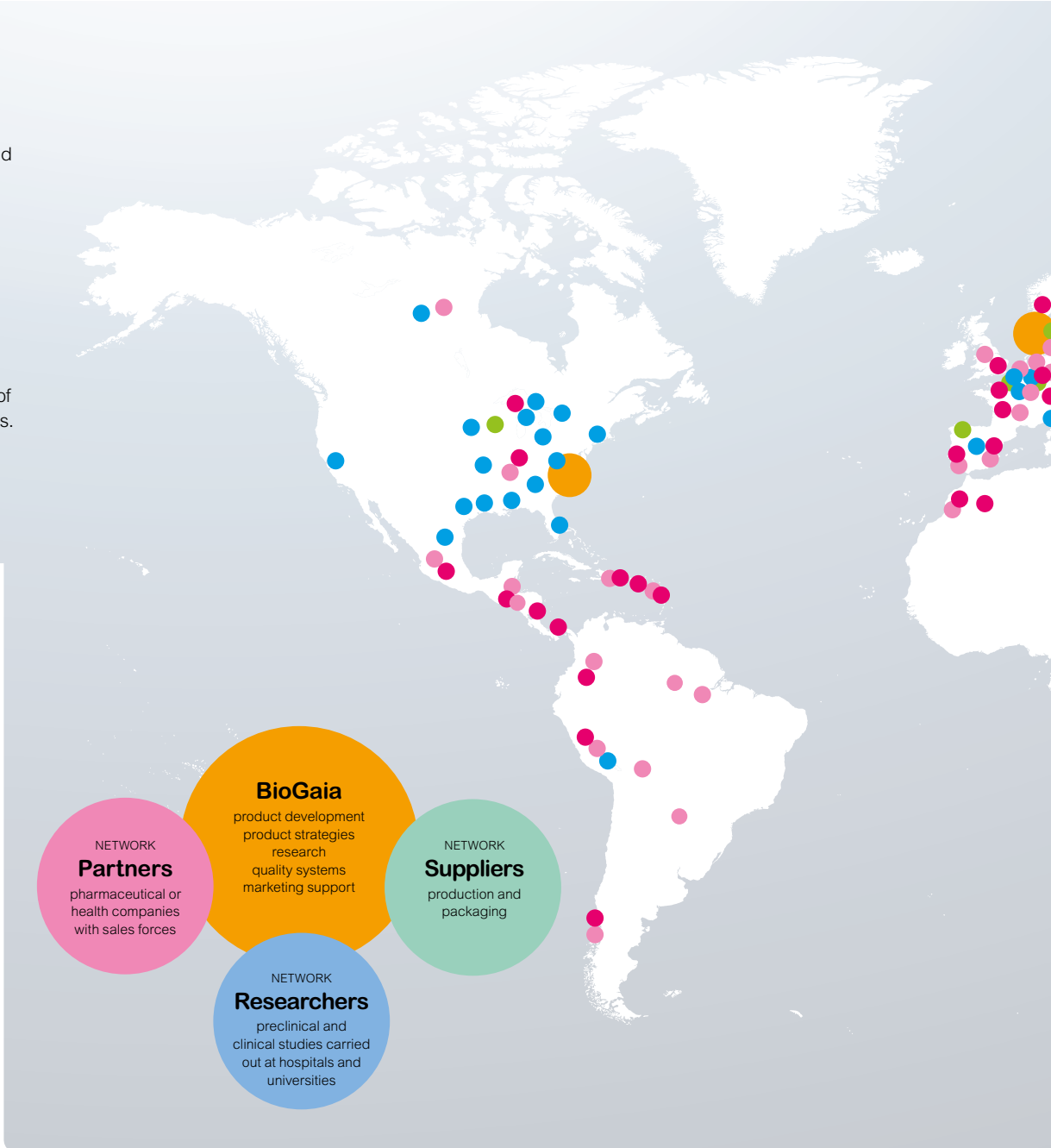
**BioGaia's business model is based on three external networks – research, production and distribution. In the research area there are collaborations with more than 50 research institutions and clinics. The products are manufactured and packaged at six different facilities in Europe and the USA. The distribution network consists of around 60 partners with sales in some 90 countries.**

**IN THE RESEARCH AREA** there are collaborations with more than 50 research institutions and clinics around the world (see page 20). Many of the researchers are among the most prominent in their fields. Some

of these collaborations have been underway since BioGaia was founded, while others are newer.

**THE PRODUCTS ARE MANUFACTURED** and packaged at six different facilities in Europe and the USA. Long-term and close collaborations with the suppliers make it possible to continuously optimise production and logistics. The suppliers – above all the wholly owned subsidiary TwoPac – are also important partners in product development, both in the creation of new products and in further development of existing products.

- = BioGaia's offices: Stockholm (headquarters), Lund, Eslöv, Raleigh/USA, Hiroshima/Japan and Shanghai/China.
- = Universities and hospitals where research is conducted.
- = Manufacturing and packaging units.
- = Partners with sales of component products.
- = Partners with sales of finished products.



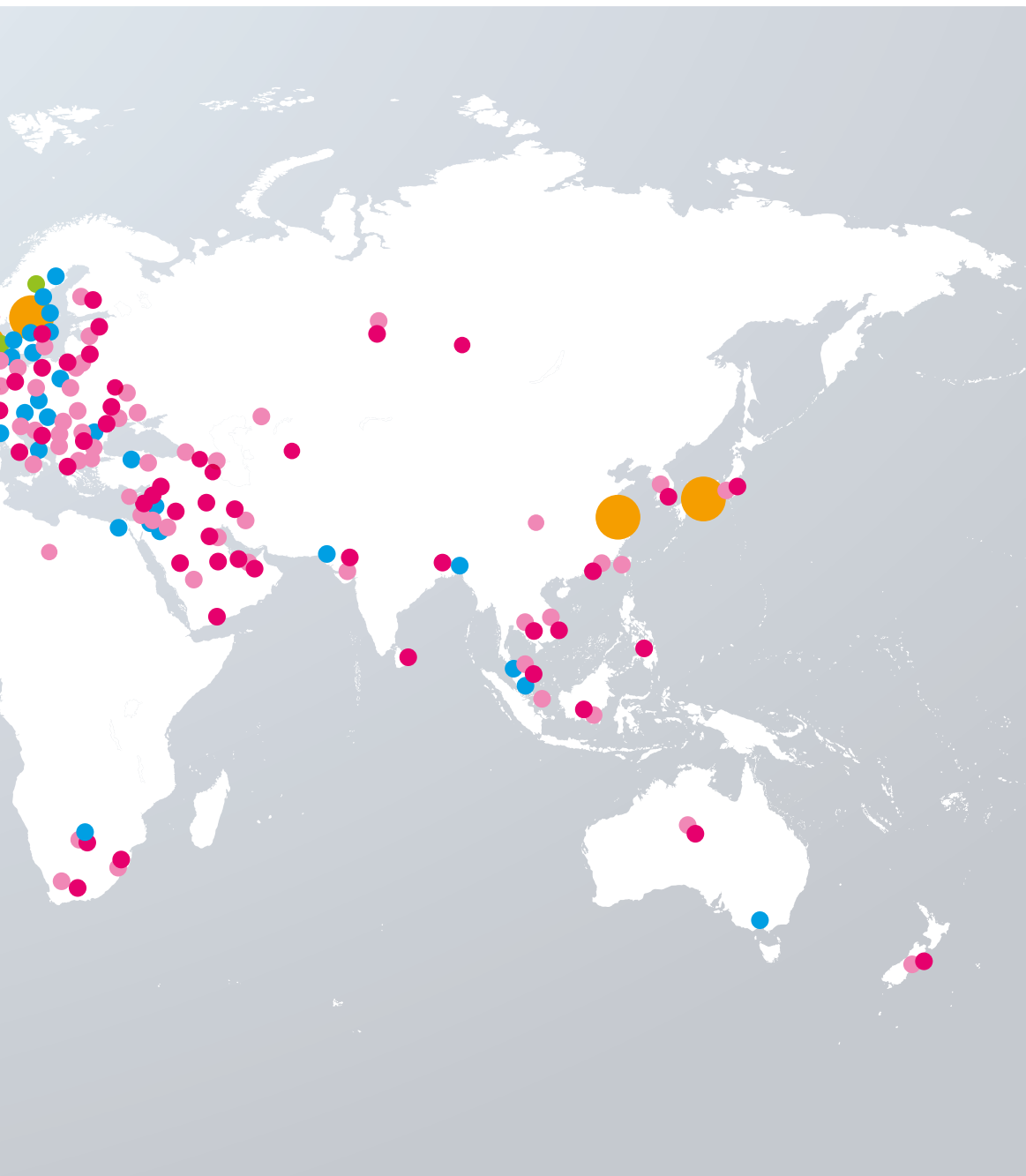


**THE DISTRIBUTION NETWORK** is made up of some 60 partners with sales in around 90 countries. Most of these companies have sales staff that visit doctors and other healthcare professionals. By informing them about the published results of clinical trials, the sales staff creates interest and confidence among doctors who then recommend the products to their patients, who in turn buy the products in pharmacies and similar sales outlets.

In many countries the same partner markets all or large parts of BioGaia's product portfolio, but in a number of markets there are two or more partners.

In the 24 countries where the oral health products are sold, the partner in most cases is a company specialised in oral health products, of which Sunstar is the largest, with sales in four countries.

The distribution collaboration with Nestlé covers some 60 countries and applies to infant formula where *Lactobacillus reuteri* Protectis is included as an ingredient in products that are marketed under Nestlé's own brand. In a few cases, like Gerber in the USA and Nestlé Mexico, Nestlé sells BioGaia's drops. ■



# Successful business model

**Y**et another strong year of profitable growth. Our geographic expansion is continuing and sales are rising in the majority of markets. We have satisfied partners and consumers, because our products deliver the expected benefits and without any side effects. Our brand is continuing to grow in recognition, not least through our consumers and healthcare professionals who are enthusiastically sharing their positive experiences with each other.

**BIOGAIA'S IMPRESSIVE RESULTS** have been achieved thanks to our successful business model. It allows us in a very cost-efficient manner to expand distribution, enter new markets, develop and launch new products, as well as continuously build brand credibility and recognition. The BioGaia brand represents a line of products aimed primarily at specific health conditions and for which our products are recommended by doctors and other healthcare professionals and via medical journals. We are not competing in the market for probiotic supplements in the form of food or beverages, nor in the market for "cocktail products" (containing a large number of probiotic strains), segments that demand large and continuous marketing investments.

**THE BUSINESS MODEL HAS SEVERAL STRENGTHS.** First of all, our marketing is primarily targeted towards doctors and other healthcare experts, who in turn recommend our products to their patients and their parents. We build credibility by solely relying on clinical studies conducted by independent

researchers and these are continuing to confirm the benefits of our products. We have a very strong network that includes some of the world's foremost researchers in the areas we focus on.

Secondly, we distribute our products internationally through partners that are carefully selected, successful distributors with a solid reputation in the medical and healthcare sector. Most new partners use the BioGaia brand, but with a few of our bigger, as well as earlier partners we have co-branding agreements. In a few cases our partners sell the products under their own brands and in such cases BioGaia is shown as the manufacturer of the product.

**FINALLY, WE PRODUCE** our probiotic cultures and a few of our finished products through contract manufacturing by several prominent producers, with rigorous internal quality control by BioGaia. In recent years we have also expanded our development of new products by initiating joint development projects with a few of our most important partners, like Nestlé.

This business model allows BioGaia to remain a highly profitable and steadily growing company with a lean and flexible organisation and with low fixed costs and marketing expenses. It is also a model that continuously enhances the credibility and reputation of our company and our brand.



DAVID DANGOOR,  
BOARD CHAIRMAN, BIOGAIA



*This business model allows BioGaia to remain a highly profitable and steadily growing company. At the same time, the brand is becoming increasingly well established. 🐛*

# Strategy

## Vision

To improve the health of people around the world by offering first class probiotic products.

## Mission

To develop, market and sell well documented probiotic products worldwide in the form of innovative and appealing dietary supplements and food products.

## Financial targets

BioGaia's goal is to create strong value growth and a good return for the shareholders. This will be achieved through a greater emphasis on the BioGaia brand, increased sales to both existing and new customers and a controlled cost level.

### ► DIVIDEND

BioGaia's objective for capital management is to safeguard the Group's ability to continue as a going concern and to provide a good return to the shareholders. The policy is to pay a shareholder dividend equal to 40 per cent of profit after tax.

**THIS YEAR'S OUTCOME** BioGaia's Board of Directors and President propose to the upcoming AGM an ordinary dividend (40 per cent of profit after tax) of SEK 3.46 per share and an extraordinary dividend of SEK 1.54 per share, for a total dividend of 5.00 per share.

### ► THE BIOGAI A BRAND

BioGaia has had its own consumer brand since 2006. One central part of BioGaia's strategy is for sales to take place primarily under this brand. For 2014 BioGaia's goal was for sales under its own brand, including co-branding, to account for 60 per cent of sales of finished consumer products.

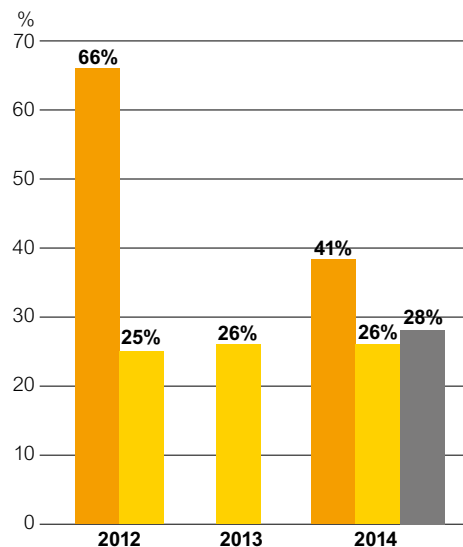
**THIS YEAR'S OUTCOME** This goal was met and sales under the BioGaia brand (including co-branding) during the year accounted for 61 per cent of finished consumer product sales.

### ► OPERATING MARGIN

The target is a sustainable operating margin of at least 30 per cent with continued strong growth and increased investments in research, product development and brand building.

**THIS YEAR'S OUTCOME** BioGaia's operating margin in 2014 was 41 per cent, including license revenue from Nestlé amounted to SEK 95.4 million. Excluding license revenue from Nestlé, the operating margin was 26 per cent.

Operating expenses include costs of SEK 6.7 million for the development of a drug in the subsidiary IBT. Excluding the subsidiary IBT, the operating margin (excluding license revenue from Nestlé) was 28 per cent.



■ = Operating margin including license revenue from Nestlé.

■ = Operating margin excluding license revenue from Nestlé.

■ = Operating margin excluding license revenue from Nestlé and expenses for the development of a drug in the subsidiary IBT.



## BioGaia's value drivers



### ► RESULTS OF HIGH QUALITY CLINICAL TRIALS

BioGaia focuses strongly on research, both preclinical and clinical studies, with the aim of developing scientifically proven health-promoting products. BioGaia's research department collaborates with a network of researchers at hospitals and universities around the world.

In 2014 the results of 17 clinical and 12 preclinical studies were published in medical journals. Most of the studies that are performed are carried out by external independent researchers. Such studies are regarded as more objective and also contribute to keeping research expenses down.



### ► PRODUCTS AND PACKAGING SOLUTIONS THAT MEET CUSTOMER NEEDS

Another key area is to continuously develop new products and packaging solutions that meet customer needs. One vital condition for these activities is that the innovations can be protected. BioGaia therefore has a large number of intellectual property rights

such as patents, trademarks, names of strains and Internet domains.

BioGaia continuously works with business intelligence and to strengthen intellectual property rights by protecting the use of its products.



► **POWERFUL SUPPORT TO PARTNERS**

BioGaia supports its partners, for example through education and information about new results from studies. The company also works internationally with PR and Internet marketing and produces marketing material.

Participation in international medical conferences

is a central component of BioGaia's partner support, but is also an important forum for meeting and getting a direct response from doctors and other healthcare professionals. During the year BioGaia took part in four conferences and at three of them also hosted scientific symposia.



► **DEDICATED AND SKILLED EMPLOYEES WHO CHALLENGE EXISTING SOLUTIONS**

In order to attract and retain skilled and motivated employees, BioGaia strives to create a culture in which all employees are given the opportunity to

develop, influence their own work situation and maintain a good balance between work and leisure in order to avoid stress.

These are the factors that are driving BioGaia forward. In part, a company's success also depends on the ability to manage the risks associated with them.

**Read more about risks on page 41-42.**



The body's microcommunity of bacteria equips us to handle a great deal of wear and tear. But we risk putting our "home defence" out of commission when we eat foods that don't agree with us, are subject to too little sleep and too much stress, travel to places with foreign bacteria, are careless about nutrition and overuse antibiotics.



# Bacteria control our lives

You have around 100,000 billion microbes living in and on your body – bacteria, fungi and viruses. This means that you are made up of ten times as many microbes as human cells. Most of these are bacteria and are found in the digestive tract. There, some 1,200 different types of good and bad bacteria are waging a constant war for dominance, and you affect the outcome through your lifestyle.

**T**here are several models that explain the origins of the universe some 14 billion years ago. There are an equal number of theories about the importance of bacteria for the emergence of life, despite the fact that these building blocks have been studied for over a century. In recent years this field of research has literally exploded with new insights and hypotheses. Professor William Schopf at UCLA has shown that certain geological formations contain fossilised cyanobacteria that are 3.5 billion years old, which would make them the earliest traces of life on Earth. Other findings indicate that bacteria have been found on Earth for more than two billion years.

The consensus is that bacteria play a critical role in the history of mankind. But it has taken time for the scientific world to understand the combined benefits they confer and how vital bacteria are for our entire existence.

**WE ARE BORN AS 100 PER CENT HUMAN AND DIE AS 90 PER CENT MICROBE** We are born virtually sterile and remain so – until saliva from kisses, skin contact and other interactions introduce the first bacteria to our bodies. Today many babies are born at hospitals and delivered via caesarean section, which means that the first bacteria the body comes in contact with are different from before. This fact and what happens during the first two years of life are decisive, because it is during this time that each individual's unique gut flora is developed. The gut flora then remains

more or less intact throughout our lives.

Aside from the way we are born, development of the gut flora is affected by factors like breast-feeding and diet, hygiene and the use of antibiotics and other drugs. For example, we know today that antibiotics disrupt the equilibrium in the gut flora and that this imbalance lasts for a long time.

**THE CRITICAL TASKS OF BACTERIA** The gut flora is now recognised as a one of the body's organs. It weighs around two kilos and both the number of bacteria and their diversity are vital in maintaining the balance in the body and for the bacteria to remain friendly. Among other things, the bacteria in the digestive tract train our immune system, help to break down the food we eat and are our first line of defence from foreign and pathogenic microbes.

Although the gut flora is relatively stable during our lives – just as when it is built up, it can be disrupted by external factors. Our modern lifestyle with a high intake of antibiotics and other drugs, low nutrition food, stress, sleep deficiency and environmental toxins leads to an imbalance in the system. New research indicates that there is a connection between a disrupted gut flora and many common conditions such as diabetes, obesity, cardiovascular disease and asthma.

These research findings shed whole new light on the role and importance of these microbes for our health. Could it be that we are turning our friends, bacteria, into our worst enemies? ■



"Microbes play a critical role in your immunity as well as your ability to combat disease. In short, it is your microbiome that keeps you healthy. And parts of it are disappearing."

DOKTOR  
MARTIN J. BLASER,  
MISSING MICROBES (2014)

## BioGaia *first in the world* to launch probiotics as...





# World-leading with unique products

Today finished consumer products are sold in around 75 countries. Including component products, BioGaia's products are found in some 90 countries. Paediatrics account for over 80 per cent of total sales and Adult Health for the remainder of nearly 20 per cent.<sup>1</sup>

**B**ioGaia's focus is on finished consumer products that are sold under its own brand. In 2014 these sales, including co-branding, accounted for 61 per cent of sales of finished consumer products.<sup>2</sup> But although the strategy is to continuously increase this share, products that are sold under a partner's own brand or are co-branded make up a large and important part of sales.

**PRODUCTS UNDER DIFFERENT BRANDS.** All partners that started selling BioGaia's products prior to 2006, when BioGaia launched its own brand, do so under their own respective brand names. Over the years, a few of them have managed to build up very strong local brands. One such example is Verman in Finland, which has succeeded in making Rela one of the largest and best known brands among over-the-counter (OTC) products in pharmacies. Another example is Reuterina in South Africa, which is sold by the partner Acacia and is the leading probiotic brand in the country.

**BACTERIA CULTURE IN MANY PRODUCTS** Aside from finished consumer products, BioGaia sells so-called component products, bacteria cultures of *Lactobacillus reuteri* Protectis that are used as an ingredient in infant formula, yoghurt and other dairy products. As a component product, the bacteria are packaged as "powder" and are sold in bulk. Nestlé is the largest customer when it comes to component products. Recently, they launched an additional product with

*Lactobacillus reuteri* Protectis, infant formula for children over the age of one year.

**NO SIMPLE SOLUTION FOR PATENTS** BioGaia applies for and holds patents in the countries where it is commercially relevant to do so and where there are functioning patent systems. Applying for patents is a cumbersome process that requires extensive documentation. BioGaia handles the fundamental aspects of the process and uses representatives in the respective country for contacts with the country's patent authorities.

Thanks to BioGaia's forefront position when it comes to new knowledge in the field of probiotics, it has been possible to patent specific new strains and indications/areas of use. New packaging solutions are also protected. ■

<sup>1</sup> Since 2014, sales are divided into the segments Paediatrics and Adult Health. However, the earlier division between finished consumer products and component products has been included in 2014 in order to facilitate comparability between years. Furthermore, sales of finished consumer products under BioGaia's own brand are measured in relation to total sales of these products.

<sup>2</sup> Finished consumer products that are not sold under BioGaia's brand are sold either under the partner's own brand or with a combination of the partner's own and BioGaia's brand, so-called co-branding.

## BIOGAIIA'S INTELLECTUAL PROPERTY RIGHTS

- ▶ Registered trademarks in some 50 countries, in addition to a number of approved trademarks in Europe
- ▶ Around 400 patents in 31 patent families



All products that are sold under the BioGaia brand and are based on the *Lactobacillus reuteri* Protectis strain have been given the product name ProTectis, such as BioGaia ProTectis drops and BioGaia ProTectis tablets. Products based on *Lactobacillus reuteri* ProDentis are called BioGaia ProDentis – lozenges, chewing gum or drops. The newest product contains *Lactobacillus reuteri* Gastrus and is accordingly called BioGaia Gastrus.

## Products for paediatric health

### ► FINISHED CONSUMER PRODUCTS

Probiotic dietary supplements under BioGaia's brand, co-branding or under the partner's own brand. The products are sold in pharmacies and similar sales outlets.

*Indication:* Digestive health for children. For prevention and treatment of colic, regurgitation, constipation and diarrhoea.

*Products:*

- drops for cold storage
- drops that can be stored at room temperature
- drops with Vitamin D for cold storage
- drops with Vitamin D that can be stored at room temperature
- drops with Vitamins D and K for cold storage
- oral rehydration solution
- digestive health tablets
- digestive health tablets with Vitamin D

*Sales:* Products for children account for more than 80 per cent of sales.

*Markets:* The drops are sold in around 70 countries, drops with Vitamin D in 14 countries, digestive health tablets in 50 countries, oral rehydration solution in 15 countries, digestive health tablets with Vitamin D in six countries.

### ► COMPONENT PRODUCTS

Bacteria cultures of *Lactobacillus reuteri* Protectis that are used as an ingredient in infant formula and infant cereal. Component products are always sold under the partner's brand.

#### PAEDIATRIC PRODUCTS UNDER THE BIOGAIA BRAND

- BioGaia ProTectis Baby drops
- BioGaia ProTectis Baby drops with Vitamin D
- BioGaia ProTectis oral rehydration solution
- BioGaia ProTectis tablets
- BioGaia ProTectis with Vitamin D



Prevention and treatment of...



# Products for adult health

## ► FINISHED CONSUMER PRODUCTS

Probiotic dietary supplements under the BioGaia brand, co-branding or under the partner's own brand. The products are sold in pharmacies and similar sales outlets.

### Indication:

- Digestive health and oral health for adults.
- Treatment of constipation and diarrhoea, as well as adjunct treatment of *Helicobacter pylori* infection.
- Prevention and treatment of periodontal disease and gingivitis.

### Products:

- digestive health tablets (two different strains)
- digestive health tablets med vitamin D
- oral rehydration solution
- oral health lozenges
- oral health chewing gum
- oral health drops

**Sales:** Products for adults account for 18 per cent of sales.

**Markets:** Digestive health tablets are sold in around 15 countries and digestive health tablets for use in connection with *Helicobacter pylori* infection in two countries. Oral health lozenges are sold in 24 countries and in a few of these the chewing gum and oral health drops are also sold on a small scale.

## ► COMPONENT PRODUCTS

Bacteria cultures of *Lactobacillus reuteri* Protectis that are used primarily as an ingredient in yoghurt and other dairy products. Component products are always sold under the partner's brand.

### ADULT PRODUCTS UNDER THE BIOGAIA BRAND

- BioGaia ProTectis tablets
- BioGaia ProTectis oral rehydration solution
- BioGaia ProDentis lozenges
- BioGaia ProDentis chewing gum
- BioGaia ProDentis drops
- BioGaia Gastrus tablets



## Prevention and treatment of...



... constipation and diarrhoea

... periodontal disease and gingivitis

... diarrhoea and abdominal pain in connection with use of antibiotics

*Strong network of independent researchers*



BioGaia collaborates with specialists at over 50 research institutions and clinics in a unique global research network. To maintain a position at the leading edge, it is of the utmost importance to work with and inspire the top researchers in the various indication areas. The research department at BioGaia functions as a central hub and engine.

**AUSTRALIA** Royal Children's Hospital & Murdoch Childrens Research Institute.

**BANGLADESH** International Center for Diarrheal Disease Research.

**BELGIUM** Leuven Catholic University.

**BOTSWANA** Princess Marina Hospital.

**BULGARIA** University Hospital St Marina.

**CANADA** The Hospital for Sick Children, McMaster University, University of Alberta.

**CHILE** Pontificia Universidad Católica de Chile.

**CROATIA** Children's Hospital Zagreb, Clinical Hospital Centre Sestre Milosrdnice.

**DENMARK** University of Copenhagen.

**EGYPT** Zagazig University.

**FRANCE** University Hospital Robert Debré, University of Nantes.

**GREECE** Athens Children's Hospital Agia Sofia.

**ISRAEL** Shaare Zedek Medical Center, Soroka University Medical Center, Ben-Gurion University.

**ITALY** University of Bari, Clinica Pediatrica B. Trambusti, University of Bologna, Università Cattolica del Sacro Cuore, Regina Margherita Children's Hospital.

**MEXICO** National Perinatology Institute.

**PERU** Johns Hopkins Bloomberg School of Public Health and Hygiene Satellite laboratory.

**PAKISTAN** University Medicals College Islamabad.

**POLAND** Children's Memorial Health Institute, Medical University Children's Health Memorial Institute.

**SINGAPORE** Singapore Polytechnic, School of Chemical and Life Sciences.

**SLOVENIA** University Children's Hospital Ljubljana, University Medical Centre Ljubljana.

**SPAIN** University Hospital Ramón y Cajal.

**SWEDEN** Swedish University of Agricultural Sciences, Akademiska Hospital in Uppsala, Uppsala University, Karolinska Institute, Karolinska University Hospital, University of Örebro, Linköping University Hospital, Karolinska University Hospital, Sahlgrenska University Hospital, Lund University.

**THE NETHERLANDS** Wageningen University.

**TURKEY** Yeditepe University Dental School, Eskisehir Osmangazi University Faculty of Medicine.

**USA** Case Western Reserve University, Tulane University, Texas Children's Hospital, University of Texas Medical Center, Baylor College of Medicine, Michigan State University, University of Miami, Emory University, St Luke's Hospital, Stanford University, Wake Forest School of Medicine.

# A focus on research

*Lactobacillus reuteri* is one of the world's most well researched probiotics and the number of scientific publications is growing continuously. At BioGaia, research is critical since scientifically based claims about the products are the company's most important marketing tool.

The majority of clinical studies carried out with BioGaia's products are randomised, double blind and placebo-controlled, and are thus fully comparable to pharmaceutical studies in terms of research quality. Furthermore, all studies must be approved by a local ethics review board before starting. Research on BioGaia's products should generate publication of well founded and scientifically based articles. As a result, BioGaia actively supports publication of the results in well-reputed scientific journals.

**ONE FOURTH OF ALL STUDIES** are initiated by BioGaia itself, to investigate product safety and health benefits in a specific area, and are monitored by BioGaia's research supervisor. However, there is a widespread interest in research on *Lactobacillus reuteri* and another fourth of the studies are initiated and conducted by independent researchers. Aside from requesting the researcher's resumé and study protocol and requiring ethical approval (these criteria apply to all studies), BioGaia has no insight into or influence over these studies.

Around half of all studies are initiated and conducted by one of BioGaia's partners.

**STUDIES 2014.** During the year, 17 clinical studies in different indication areas were published. One of

the perhaps most significant was a study on newborns that was published in a very well-reputed medical journal, *JAMA Pediatrics*, in January. Another important study, on healthy preschool children, was published in *Pediatrics* in March 2014. Read more about it on page 22.

There were already three previous studies showing that *Lactobacillus reuteri* Protectis can reduce the crying time among infants with colic, and during the year another two were published. The first was published in *The British Medical Journal* in April and showed neutral results (although these could be explained by the way in which the study was performed) and the second in *Journal Pediatrics* in October. The latter was the fourth positive study with *Lactobacillus reuteri* Protectis on infants with colic. Read more about the results on page 23.

**IN 2014 FIVE SCIENTIFIC SYSTEMATIC REVIEWS** were also published that evaluated the clinical use of *Lactobacillus reuteri* Protectis from different aspects: safety for children up to two years of age and efficacy in infants and children, as well as specifically the efficacy of use in children with acute diarrhoea.

Twelve articles presented the results of preclinical<sup>1</sup> studies that further illuminate various probiotic attributes of a few of BioGaia's commercial strains. ■

<sup>1</sup> Preclinical studies include *in vitro* studies (laboratory) and animal studies.

## Number of studies and articles

<b>17</b> During the year, 17 clinical studies were published in different indication areas.	<b>11700</b> To date, 137 clinical studies using BioGaia's human strains of <i>Lactobacillus reuteri</i> have been performed on 11,700 individuals of all ages.	<b>108</b> The results have been published in 108 articles in scientific journals and nine doctoral theses (January 2015).
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## Clinical study published in 2014

### Common infections among children can be prevented



**Pedro Gutiérrez-Castrellón, MD, MSc, PhD.** Head of Translational Research Unit on Pediatric Nutrition, Hospital General Dr. Manuel Gea González and Academic Professor of Public Health at Medicine Faculty ULSA, Mexico.

**What motivated you to perform another study to investigate whether probiotics can prevent infection?**

– Several earlier studies with both *Lactobacillus reuteri* Protectis and other probiotic strains have shown that the risk for diarrhoea and other infections can be reduced. But since the studies have been carried out with different strains, I wanted to test the one that has shown positive results on diarrhoea in two independent studies, namely *Lactobacillus reuteri* Protectis. In order to create evidence-based recommendations, several independent studies are necessary.

**And what conclusions can you draw from the results?**

– Our study confirms earlier published data in proving that preventative use of *Lactobacillus reuteri* Protectis in healthy children reduces diarrhoeic episodes. Moreover, the study demonstrated a reduction of respiratory tract infections in supplemented children.

**What implications of the results do you see?**

– The intervention was shown to be cost-effective and therefore, both in terms of reducing disease and from an economic perspective, this trial adds independent support to previous evidence that daily preventative use of *Lactobacillus reuteri* Protectis could be valuable for families and the society. ■

**► STUDY FACTS**

**Background** A study from 2011 showed that *Lactobacillus reuteri* Protectis could prevent diarrhoea and affect height and weight in children in Indonesia (Agustina). In 2005 a study was published in which *Lactobacillus reuteri* Protectis was shown to reduce the risk of fever, respiratory tract infection and need of antibiotics. The children who received Protectis were healthier and had fewer sick days than the children who received placebo (Weizman). A Swedish study performed with employees at TetraPak showed that those who received a daily supplementation of *Lactobacillus reuteri* Protectis had fewer sick days (Tubelius, 2005).

**About the study** The objective of the study was to investigate whether daily administration of the probiotic *Lactobacillus reuteri* Protectis reduces the frequency and duration of diarrhoeal episodes and other health outcomes in healthy preschool children. 336 children aged 6-36 months were enrolled. During the three-month period, half of them were given drops with *Lactobacillus reuteri* Protectis and half were given placebo. After the intervention period the children were followed up for additional three months without supplementation.

**Results** The children receiving *Lactobacillus reuteri* Protectis had fewer days with diarrhoea or respiratory tract infection or fever, and when infected, the episodes were also shorter than in the placebo group. In addition, they used less antibiotics and had fewer days of absence from day care than the children in the placebo group. Furthermore, Protectis was shown to be cost-effective for both families and the community.

**Conclusions** The study confirms that daily supplementations of *Lactobacillus reuteri* Protectis is effective in preventing common infections among children.

*Fewer sick days with Protectis.*



## Clinical study published in 2014

Fourth independent study published

### Protectis helps children with colic



**Gideon Koren, Director and Senior Scientist, The Motherisk Program, The Hospital for Sick Children. Professor of Pediatrics, Pharmacology, Pharmacy and Medical Genetics, the University of Toronto, Canada.**

**Professor Koren, please briefly explain the background for your study and how it has been performed.**

Infantile colic is one of the major concerns of many parents of babies, and for a long time, doctors and parents alike have struggled with a lack of treatment options to ease colic symptoms in early infancy. Therefore, this randomised placebo-controlled trial was conducted to determine whether colicky infants administered the probiotic *Lactobacillus reuteri* DSM 17938 would show significant improvement of colic symptoms compared to infants given placebo. When evaluating probiotics it is critical to use the same scientific rigour used for medicinal drugs and thus the study was conducted accordingly.

#### **What conclusions can be drawn from the results?**

One important strength of our study is that, to date, this is the first North American study, conducted with high scientific rigour, that has investigated the effectiveness of probiotic therapy for the treatment of infantile colic. The results show that *Lactobacillus reuteri* DSM 17938 can help breast-fed infants with colic and thus support the results of previously published studies from other parts of the world. ■

#### ► STUDY FACTS

**Background** Several earlier studies (Savino 2007, 2010, Szajewska 2013) have shown that *Lactobacillus reuteri* Protectis can reduce crying time among infants with colic.


**About the study** The objective of the study was to investigate the effectiveness of *Lactobacillus reuteri* Protectis for the treatment of infantile colic in breastfed infants. 52 infants between the ages of 3 weeks and 6 months were given either 5 drops of *Lactobacillus reuteri* Protectis (n=24) or placebo (n=28) daily for 21 days. All of the included infants were healthy at the start of the study.

**Results** After seven days of treatment crying and fussing was reduced by more than 40 minutes per day in infants given *Lactobacillus reuteri* Protectis, whereas there was practically no reduction in the placebo group. Crying and fussing continued to decrease significantly in the *Lactobacillus reuteri* Protectis group throughout the 21-day long study period. In the placebo group this decrease was significantly smaller.

**Conclusions** The study confirms earlier positive results with *Lactobacillus reuteri* Protectis in infants with colic. With this study, there is now also clinical data for North American children.

*Less crying after just one week.*



A photograph of a busy street in Japan, likely a shopping district. In the foreground, a crowd of people is visible, including an elderly man with glasses and a dark suit jacket. The background is filled with various neon signs and advertisements, including a prominent red sign with Japanese characters. The overall atmosphere is one of a densely populated urban environment.

*Helicobacter pylori* is the primary cause of gastric ulcers and stomach cancer

- China, Korea, Iran, Pakistan, South Africa, Egypt and Morocco are examples of densely populated countries where 70-80 per cent of the population carries *Helicobacter pylori*.
- In Northern Europe, North America and Australia, the prevalence of *Helicobacter pylori* is around 20 per cent.
- Stomach cancer has the fourth highest mortality rate of all cancer types worldwide.



## Time for new alternatives

# Combating the world's most common bacterium

Half of the Earth's population carries a bacterium that is called *Helicobacter pylori* and has a proven connection to stomach cancer. How are researchers tackling this challenge, and how can BioGaia's probiotics contribute?

**T**he story of *Helicobacter pylori* began in 1982 when Robin Warren and Barry J. Marshall made their remarkable discovery from cultures from patients with chronic gastritis. In 2005 these researchers won the Nobel Prize for their discovery of the bacterium that is the primary cause of gastric ulcers and stomach cancer. In fact, the prevalence of *Helicobacter pylori* is so common that it is estimated to be present in 50 per cent of the world's population, and there is a clear link between the infection and people's living standards. The bacterium is much more prevalent in developing countries where people live in crowded and unsanitary conditions and have limited access to clean water.

**THIS AGGRESSIVE BACTERIUM** burrows into the mucous lining of the stomach where it can give rise to ulcers and inflammation, and is an invisible curse for a large part of the world's population. *Helicobacter pylori* infection causes no noticeable symptoms in 70 per cent of those who are affected. In cases where the infection manifests itself, the main symptoms are a burning pain in the mid-upper stomach area, abdominal pain, bloating and nausea.

*Helicobacter pylori* resides in the stomach, where it is well adapted to the acidic pH. In the stomach it

causes a chronic inflammation (gastritis) that significantly increases the risk for peptic ulcers. In a worst case scenario, it can also develop into stomach cancer. The link to *Helicobacter pylori* is so strong that the bacterium has been shown to be the most common risk factor for this type of cancer.

**IF UNTREATED**, *Helicobacter pylori* infection is lifelong. However, one of the major challenges is that many of the antibiotics that are currently part of the standard treatment regimen are no longer effective. This is mainly due to widespread resistance to antibiotics, particularly in developing countries where antibiotics are over-prescribed.

"In view of this, we need new ways to tackle the treatment problem", according to David Y. Graham, Professor in the Department of Medicine-Gastroenterology at Baylor College of Medicine in the USA.

Graham also points out the acute need to evaluate alternative methods to combat *Helicobacter pylori*. One such promising alternative is clinically tested probiotics.

"We already know that certain strains work well as a complement to today's standard therapies with different antibiotics. In the future these probiotics may also be effective without antibiotics in eradicating *Helicobacter pylori*," says David Graham. ■



*Lactobacillus reuteri* Gastrus has been shown to be an effective adjunct to standard treatment of *Helicobacter pylori* infection.

“Resistant bacteria jeopardise the success of *Helicobacter pylori* treatment. But we have gained momentum. In the past year opinion turned, and the WHO and other leading authorities are now in agreement that the bacterium that is the primary cause of peptic ulcers and stomach cancer must be eliminated. The question is how this will be achieved, above all in those parts of the world where the resistance problems are greatest. ”



DAVID Y. GRAHAM, PROFESSOR IN THE DEPARTMENT OF MEDICINE-GASTROENTEROLOGY AT BAYLOR COLLEGE OF MEDICINE IN THE USA.

A woman with long blonde hair, wearing a black wetsuit, is walking on a rocky beach. She is carrying a white surfboard under her arm. The beach is framed by a large, gnarled tree on the left and right. The ocean is visible in the background. The text "A good balance makes life easier" is written in a cursive font over the image.

*A good balance  
makes life easier*



## BioGaia's products

# At pharmacies around the world

The market for probiotic supplements reached approximately SEK 23 billion\* in 2012 and is growing by 8-10 per cent annually.

\* Euromonitor International 2013

Europe is BioGaia's largest market, and accounts for 67 per cent of sales. In 2014 sales in this region rose by 18 per cent to SEK 257.8 million. The increase is mainly attributable to higher sales of drops in several countries in Eastern Europe (Turkey, Poland, Bulgaria, Slovakia and the Czech Republic), but also to royalty revenue from Nestlé.

**ITALY IN THE LEAD** With the two distributors Noos and Italchimichi, Italy remains BioGaia's largest single market. Sales at the beginning of 2014 were down somewhat compared to the previous year, but rose in the second half of the year and reached the same level as in 2013.

Ewopharma is one of BioGaia's oldest and most important customers. The Swiss pharmaceutical company is active in more than 15 countries in Central and Eastern Europe, many of which have small populations and relatively low purchasing power. BioGaia's products, which are sold under the BioGaia brand, are currently found in 13 of these countries, of which Bulgaria, Poland and Slovakia account for the bulk of sales.

Bulgaria and Slovakia were among the first Ewopharma countries to launch BioGaia's products. Despite increasing competition and a tough market climate in the past year, Ewopharma succeeded in defending its leading market positions and even showed double-digit growth in both countries. A few other markets that grew during the year are the Czech Republic, Serbia and Romania.

Ukraine showed growth of a full 60 per cent in 2013, but in 2014 was affected by political unrest in the country and devaluation of the currency, which led to lower consumer sales and therefore also lower purchasing from BioGaia. In total during the year,

consumer sales of Delta Medical's products in Ukraine fell by more than 30 per cent.

After having searched for a suitable partner in the UK for several years, an agreement was signed with Nestlé Nutrition during the year. Via its UK infant nutrition business, Nestlé plans to launch BioGaia's drops in the UK and Ireland during 2015.

**PRODENTIS BACK IN GERMANY** In 2007 Sunstar launched ProDentis in Germany, but due to low sales the product was withdrawn two years later. However, in 2013 they decided to relaunch ProDentis. The venture has proven successful and sales so far have surpassed expectations.

**NORTH AMERICA MOVING FORWARD** In the USA and Canada, sales were up by 35 per cent to SEK 30.3 million. Sales increased in both countries thanks to growth in sales of both drops and digestive health tablets. The USA and Canada accounted for around 8 per cent of BioGaia's sales during 2014.

Gerber's Soothe Colic Drops are available in several of the major national pharmacy chains like Rite Aid, CVS Pharmacies and Walgreens, and a number of local chains. At the beginning of 2015 BioGaia's other partner in the USA, Everidis, launched drops with Vitamin D at Walgreens. In contrast to Soothe Colic Drops, whose obvious target group is infants with colic, this product is targeted toward children with digestive problems and over the age of one year.

Much remains to be done in exploiting the potential BioGaia sees in the US market. One step in building BioGaia's brand here was taken through the launch of ProTectis with Vitamin D at Walgreens – BioGaia now has three products on the shelves of the USA's largest pharmacy chain.

**JAPAN LAUNCHES DROPS** Sales in Asia fell by 3 per cent to SEK 38.8 million. The decrease was mainly due to lower revenue from sales of dairy products in South Korea and Japan. Sales of drops rose somewhat in Asia, while sales of digestive health tablets were largely unchanged. Asia accounted for approximately 10 per cent of BioGaia's sales.

In the autumn the drops were launched in Japan through a digital marketing campaign and in 2015 they will also be launched in several pharmacy chains. During the year BioGaia discontinued sales of yoghurt products in Japan, since the margins were too low.

The largest market for oral health products is Japan. Here, ProDentis is sold primarily on the recommendation of a dentist at a dental clinic. In 2014 sales increased for the fourth consecutive year.

BioGaia's new product Gastrus, for patients with *Helicobacter pylori* (read more on page 25), was launched in two markets during 2014, China and South Korea. In South Korea, Dong Sung has a sales force of 60 people who visit healthcare and medical professionals, and although sales are still modest, the potential in South Korea, China and other Asian countries is deemed substantial.

**FASTEST GROWTH IN REST OF WORLD** Sales in "Rest of world" (outside Europe, Asia, the USA and Canada) rose by 70 per cent to SEK 59.5 million. The increase was mainly attributable to Brazil, where both drops and tablets were launched in the autumn of 2014. Sales in "Rest of world" accounted for 15 per cent of BioGaia's sales.

Brazil was the site of the year's most important launches for BioGaia: the relaunch of tablets and the launch of drops. The new partner Aché is strongly committed to BioGaia's products and carried out two successful launches during the autumn that featured scientific symposia for Brazil's most prominent doctors. Thanks to these activities, Aché's leading position in the industry and the size of the market, sales in Latin America grew by a full 158 per cent in 2014, the highest ever for the region.

Even if Brazil is excluded, Latin America showed strong sales growth of around 30 per cent during the year. Two other Latin American countries that also carried out successful launches during 2014 are Paraguay and El Salvador.

In 2014 Abbott Laboratories acquired BioGaia's second largest partner in the region, CFR Pharmaceuticals (Recalcine). Instead of the anticipated temporary downturn, Abbott is fully focused on BioGaia's portfolio and Chile, Bolivia, Colombia, Peru and Paraguay are all showing continued strong growth. In the spring of 2015 they will also launch in Panama.

Acacia in South Africa is one of BioGaia's oldest partners, and launched the drops back in 2002 under the Reuterina brand. Today Reuterina is the largest probiotic brand in the country, with a market share of nearly 30 per cent (measured in volume). In 2014 consumer sales increased by more than 30 per cent and the products that mainly contributed to this success were drops, tablets in 10-pack and tablets with strawberry flavour for children. ■

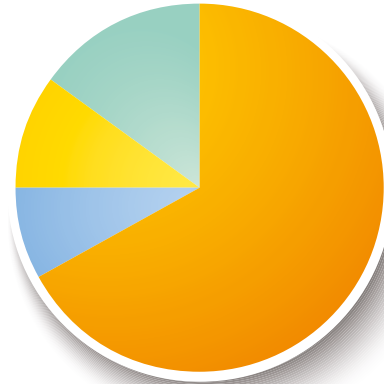


# Geographic markets

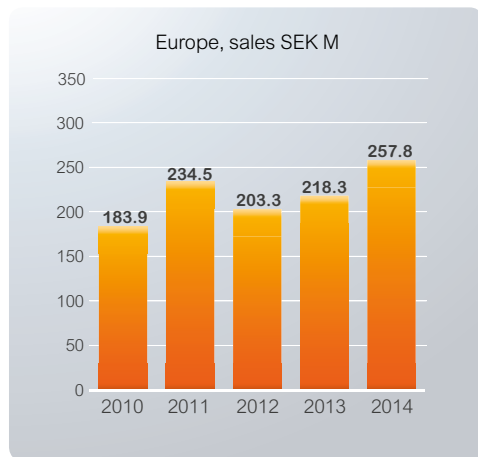
## SALES PER GEOGRAPHIC MARKET.

Sales in "Rest of world" rose by a full 70 per cent, which was mainly attributable to growth in sales of finished consumer products in particularly South Africa and Chile.

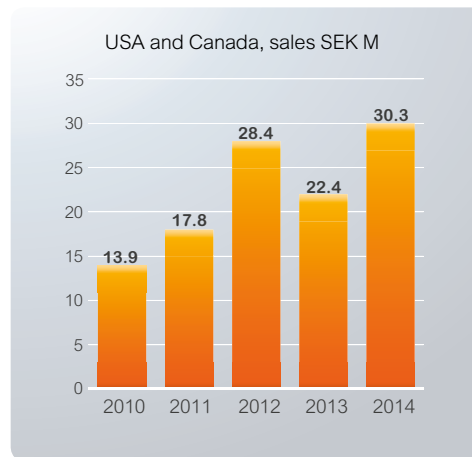
- = Europe 67 per cent (69 per cent)
- = USA and Canada 8 per cent (7 per cent)
- = Rest of world 15 per cent (11 per cent)
- = Asia 10 per cent (12 per cent)



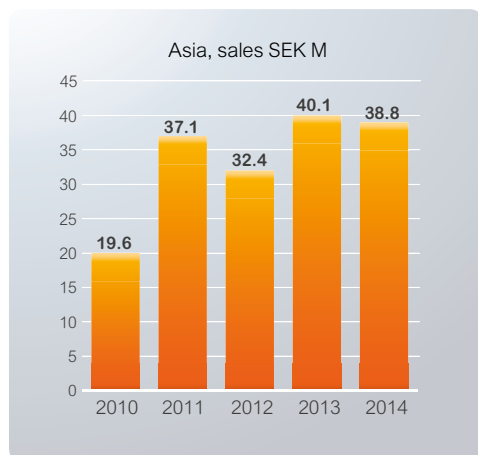
► **EUROPE** is BioGai's largest market and accounts for 67 per cent of total sales. In 2014 sales in this region increased by 18 per cent to SEK 257.8 million.



► **NORTH AMERICA** In the USA and Canada, sales were up by 35 per cent to SEK 30.3 million and accounted for around 8 per cent of total sales in 2014.



► **ASIA** In 2014 sales in Asia declined by 3 per cent to SEK 38.8 million. The region accounted for approximately 10 per cent of total sales.



► **REST OF WORLD** Sales in "Rest of world" rose by 70 per cent to SEK 59.5 million and the region accounted for 15 per cent of total sales.



*The ecological-biological  
approach is at the very core of  
BioGaia's operations.*



# BioGaia takes responsibility

BioGaia has an ethical and environmentally beneficial vision – to improve the health of people around the world by offering first class probiotic products.

**B**ioGaia's health-enhancing products are clinically tested, which means they are tested on humans. Research is conducted in an ethical manner with consumer safety as the top priority. By improving health through the use of probiotics,

which are natural organisms without negative side effects for those who take them, it is hopefully possible to reduce the use of medications and antibiotics. In the long term, this will also have positive effects on the environment. ■

## Ethical and financial responsibility

### VALUES THAT GUIDE BIOGAIA'S EMPLOYEES

- 1 My personal commitment is vital for BioGaia's success.
- 2 We are innovative and action-oriented.
- 3 We are business-minded and deliver on our promises.
- 4 We are honest, respectful and selfless in what we do and say.

### OTHER GUIDELINES AND ETHICAL STANDPOINTS

*BioGaia respects the applicable legislation*

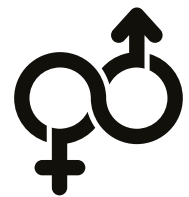
All employees shall naturally comply with the applicable laws and regulations. In addition, they shall adhere to the specific internal rules established by BioGaia. These may go beyond what is required by law.

*BioGaia condemns bribery and corruption*

The employees may never, directly or through intermediaries, offer or accept bribes from a third party, regardless of who that party may be. All employees are also encouraged to report any activity of this type that they suspect, hear of or come across.

*BioGaia's ethical policy for animal studies*

The clinical effects of BioGaia's probiotics are demonstrated on humans in ethically approved clinical trials. In order to develop more effective methods for clinical studies, however, the researchers must understand the modes of action of BioGaia's probiotics. For this purpose it can be necessary to use animal models. In such cases, BioGaia collaborates with well established research institutions and requires these to have independent ethical approval for such experimentation. ■



## BioGaia Sweden's fifth best company in gender equality

In the AllBright Foundation's report on gender equality among the management teams and boards of Swedish listed companies, BioGaia is ranked as number five of the 264 companies (March 2015).

*"For us, equality is a matter of course. We are convinced that a gender-equal company is both more profitable and more fun to work for."*

HELEN OLSSON,  
HUMAN RESOURCES  
DIRECTOR, BIOGAIA

## Social responsibility



### PROMOTES HEALTH AND SUPPORTS ORPHANAGE

BioGaia emphasises the importance of always setting a good example, i.e. by acting ethically in all contexts. Ethical issues can include which ingredients BioGaia's products should contain or whether the company should allow the core component *Lactobacillus reuteri* to be used in products that do not have a clear health profile.

Taking social responsibility is important to BioGaia, and the company works actively in this area. Since 2007 BioGaia supports the Scandinavian Children's Mission in the Philippines, which helps children and their parents by taking care of malnourished children, running a preschool and offering vocation training to parents. In 2014 BioGaia donated SEK 525,000 to the Scandinavian Children's Mission. ■



## Environmental responsibility

### STRIVING FOR ECOLOGY AND BIOLOGY IN BALANCE

The microorganisms used by the company are completely natural and normally present in human beings. The modes of action of these microorganisms are based on biological principles. To stay healthy, the human body must maintain equilibrium between its various systems. An imbalance quickly results in diminished ability of the immune defence to prevent and fight disease. This ecological-biological approach is at the very core of BioGaia's operations.

### BIOGAIA CONTRIBUTES TO A BETTER ENVIRONMENT BY:

- 1 Selecting packages that have the smallest possible environmental impact during their life cycle.
- 2 Ensuring that the packages are not unnecessarily large and bulky.
- 3 Choosing modes of transport with the smallest possible environmental impact for goods and employees.
- 4 Urging the suppliers to always take environmental aspects into account in their decisions.
- 5 Weighing in environmental aspects every time a significant decision is made.

### BIOGAIA'S CLIMATE IMPACT

BioGaia has measured the company's climate impact in 2012 and 2013 and will also do so during 2014. Starting in 2013, the measurement also

includes the subsidiary TwoPac. The greatest climate impact is caused by the company's air travel, followed by product packages. In 2013 BioGaia took part in CDP Nordic Climate Change report for the first time and won a prize for its report as the best newcomer. In 2014 the company will also participate in the CDP report.

BioGaia climate compensates by purchasing certificates from Vi Agroforestry. In 2013 and 2014, a total of 9,286 trees were planted through BioGaia's compensation in Vi Agroforestry's projects in the Kagera region of western Tanzania.

### LIFE CYCLE ANALYSIS OF THE PACKAGES

BioGaia carried out an in-depth analysis of the packages' climate impact in 2013, which was a follow-up of the earlier analysis carried out in 2010. The measurement was performed in collaboration with the Swedish Environmental Research Institute (IVL). The analysis shows for example that the bottles with volumes of less than 60 tablets have the greatest climate impact per dose. BioGaia therefore recommends that the distributors always choose blister packaging for smaller packages. Parallel to this, BioGaia is working to develop the existing packages towards recyclable materials. ■





Time to win

# in the fight against antibiotic resistance

Antibiotic resistance is a global threat to public health. And although scientists have discovered a whole new type of antibiotic for the first time in 30 years, a finished product is a long way into the future. The situation is alarming and new solutions and preventative treatments must be implemented already today.

**M**ankind is waging an uphill battle against bacteria that are developing resistance to antibiotics. What researchers need is time to find new principles for fighting this growing public health problem that is causing higher morbidity and mortality rates and leading to escalating healthcare costs for prolonged hospitalisation and more expensive drugs.

**IN SPITE OF THE GLARING NEED**, few new antibiotics are being developed today. Other types of drugs, such as cancer medicines, are far more profitable for the pharmaceutical companies and the incentives for research on new antibiotics are therefore few.<sup>1</sup> To combat this scenario, a number of national and international collaborative efforts between the industry and government agencies have been initiated.<sup>2,3</sup> The agencies are also taking action by issuing new guidelines to curb overuse of antibiotics. But these measures are not sufficient. According to a recent report from the WHO, antibiotic resistance is a growing public health scourge of such magnitude that it threatens everything our modern medicines have succeeded in achieving.<sup>3</sup>

Alongside these enormous investments, we therefore need to take additional measures. "Furthermore, I believe that these other alternatives can be at least as effective as the billions that are spent on developing new drugs," says *Peter Rothschild*, BioGaia's President and founder.

**IN THE RESEARCH WORLD THERE ARE** many who support the same reform agenda as Peter Rothschild and feel that we need to completely revise our approach to how antibiotics are used. The American professor *David Y. Graham* from the Department of Medicine-Gastroenterology at Baylor College of Medicine is one example. Graham stresses that we must explore the alternatives – while waiting for new ways to use antibiotics. Among other things,

he believes that clinically tested probiotics can contribute to reducing the risk for antibiotic resistance and perhaps also the need for antibiotics at all. Another researcher whose voice is being heard in this debate is the American professor *Martin J. Blaser*. He claims that today's large-scale misuse



DAVID Y GRAHAM



MARTIN J BLASER

of antibiotics is quite simply depleting and destroying the good bacteria inside us, and that this is a strongly contributing factor to the galloping increase in modern plagues such as asthma, allergies, diabetes, obesity and inflammatory intestinal disorders.<sup>4</sup>

## FROM HEALTHCARE TO PREVENTATIVE CARE

According to the Swedish National Board of Health and Welfare's guidelines for 2011, preventative care accounted for only 1 per cent of total healthcare and medical spending in Sweden.<sup>5</sup> The remaining 99 per cent was devoted to alleviating symptoms or, in the best case, curing infections that had already occurred. Peter Rothschild's opinion is that this distribution should be completely different, since it is better from both a human and an economic perspective to prevent diseases than to treat them. Healthy people are less susceptible to infections, need fewer antibiotics and therefore cause less antibiotic resistance. In addition to a reallocation of economic resources, we must above all realign our focus from relieving symptoms to promoting preventative healthcare. To achieve this, we need



PETER ROTHSCHILD,  
BIOGAIJA'S PRESIDENT  
AND FOUNDER

Antibiotics disrupt the gut flora by killing both "bad" and "good" bacteria.

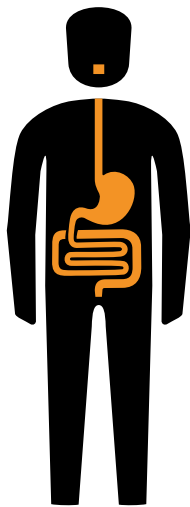


incentives to change our habits, what we eat, how much we exercise – basically, our entire lifestyle, according to Peter.

**SO WHAT CAN *Lactobacillus reuteri* do to fight the problem of antibiotic resistance?** A great deal, believes Peter Rothschild. *Lactobacillus reuteri* affects the immune system and if it is possible to prevent infections, one logical consequence should be a decreased need for antibiotics. This is something we have shown in several studies – children who were given supplements of *Lactobacillus reuteri* were healthier and used less antibiotics.<sup>6-8</sup>

Another area of use for *Lactobacillus reuteri* is in reducing the side effects of antibiotic treatment.<sup>9-13</sup> In this way, *Lactobacillus reuteri* can make it easier for patients to complete treatment, which can contribute to lowering the risk for antibiotic resistance.

*Lactobacillus reuteri* can thus create benefits in several ways – by preventing infection, by reducing the side effects of antibiotics and by thereby affecting antibiotic resistance. “The threat of antibiotic resistance is like a ticking bomb and it is high time to better exploit the potential offered by well documented probiotic bacteria,” concludes Peter Rothschild. ■



*Lactobacillus reuteri* survives the harshly acidic environment in the stomach and colonises the entire gastrointestinal tract.

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# Financial information and Notes 2014



**BioGaia®**

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# Administration report

Figures in brackets refer to the previous year.

The Board of Directors and the President of BioGaia AB (publ.), corporate identification number 556380-8723, hereby submit their annual report and consolidated accounts for the financial year 2014.

The financial statements were approved for publication by the Board of the Parent Company on 20 February 2015.

## BioGaia

**The company** BioGaia is a health company that develops, markets and sells probiotic products with documented health benefits. The products are primarily based on different strains of the lactic acid bacterium *Lactobacillus reuteri* in combination with unique packaging solutions that make it possible to create probiotic products with a long shelf life.

The class B share of the Parent Company BioGaia AB is quoted on the Mid Cap list of NASDAQ OMX Nordic Exchange Stockholm.

BioGaia has 95 employees, of whom 34 are based in Stockholm, 28 in Lund, 22 in Eslöv, three in Raleigh, USA, six in Hiroshima, Japan, and two in Shanghai, China.

**Business model** BioGaia's revenue comes mainly from the sale of drops, digestive health tablets, oral rehydration solution (ORS) and oral health products to distributors, but also of revenue from the sale of bacteria cultures to be used in a licensee's products (for example infant formula and dairy products), royalty income for the use of *Lactobacillus reuteri* in a licensee's product and sales of packaging solutions such as straws and caps.

The products are sold through nutrition and pharmaceutical companies in 90 countries.

BioGaia holds patents for the use of *Lactobacillus reuteri* and certain packaging solutions in all major markets.

**The BioGaia brand** At the beginning of 2006 BioGaia launched its own consumer brand and today there are a number of distribution partners that sell finished products under the BioGaia brand in a large number of markets. One central part of BioGaia's strategy is to increase the share of sales consisting of BioGaia-branded products.

Some of BioGaia's distributors sell finished consumer products under their own brand names. For these products, the BioGaia brand is shown on the consumer package since BioGaia is both the manufacturer and licensor.

BioGaia's licensees add reuteri culture to their products and sell these under their own brand names. On these products, the BioGaia brand is most often shown on the consumer package as the licensor/patent holder.

## Key events in 2014

### New agreements

- **New major agreement with Nestlé including payment of contingent consideration** In February 2012 BioGaia sold the rights for the use of *Lactobacillus reuteri* Protectis in infant formula to Nestlé for the remainder of the patent lifetime. BioGaia received EUR 40 million up front and a commitment for a further EUR 10.8 million during the period from 2014 to 2017 upon the achievement of certain milestones. The first milestone payment of EUR 3.6 million was received and recognised in February 2014.

Nestlé and BioGaia have further broadened and strengthened the cooperation and in March entered into a supplementary agreement to the original one. The agreement will provide BioGaia with royalties of around SEK 92 million over a three-year period, starting in the second quarter of 2014, for which BioGaia will carry out specific clinical studies in the paediatric area. In addition, BioGaia will develop new products for Nestlé in whole new areas.

Furthermore, the agreement means that BioGaia immediately received the remaining milestone payments of EUR 7.2 million from the 2012 agreement. Consequently, the entire contingent consideration of EUR 10.8 million (SEK 95.4 million) was recognised and paid in the first quarter of 2014.

- **Agreement for the sale of drops in India** In June BioGaia signed a non-exclusive agreement with Pharma Base SA for the rights to sell BioGaia's ProTectis Baby drops in India. Pharma Base will cooperate with a local distributor for marketing and sales of the drops, which will be sold under BioGaia's own brand. Registration of the product started in 2014 and the launch is planned for 2015.
- **Agreement for the sale of drops in the UK** In June BioGaia signed an agreement with Nestlé Nutrition UK that gives its subsidiary SMA exclusive rights to sell BioGaia's ProTectis Baby drops in the United Kingdom and Ireland. The drops will be sold under the BioGaia brand with elements of SMA's brand, which is very well known in the UK. The launch is planned to take place in 2015.

### Clinical studies

- **Publication of study showing that colic can be prevented** A study on 468 healthy newborns, which was published in January 2014, shows that infants given the probiotic *Lactobacillus reuteri* Protectis cried less than half as long as infants given a placebo. The infants given Protectis also had significantly fewer daily regurgitations and were less constipated compared to the infants in the placebo group.

The study was published in the highly regarded medical journal JAMA on 13 January 2014.

- **No significant differences in BioGaia's diabetes study** In May 2012 BioGaia initiated a double-blind, placebo-controlled study to investigate the effects of *Lactobacillus reuteri* Protectis on blood glucose in type 2 diabetics. Despite positive results from an earlier pilot study, no significant differences between the groups were seen in this study.
- **Publication of study showing that it is possible to prevent common infections in children** Healthy children attending daycare centres have a significantly lower risk of getting diarrhoea or respiratory tract infections when given a daily supplement of *Lactobacillus reuteri* Protectis, as shown by a study on 336 children that was conducted in Mexico. The study confirms previously published data and proves that preventative treatment with *Lactobacillus reuteri* Protectis in healthy children reduces episodes of diarrhoea. Furthermore, the study demonstrated a reduction in respiratory tract infections among the children given supplements of Protectis. Moreover, the children receiving Protectis had fewer days with fever, used less antibiotics and had fewer days of absence from daycare.

The study was published in the medical journal Pediatrics on 17 March 2014.

- **Publication of additional study showing that infants with colic cry less with BioGaia's drops** A study carried out in Canada on 52 infants with colic shows that babies given *Lactobacillus reuteri* Protectis cry and fuss less compared to babies given placebo. After seven days of treatment, crying and fussing was reduced by more than 40 minutes per day in infants given *Lactobacillus reuteri* Protectis, whereas there was practically no reduction in the placebo group. Crying and fussing continued to decrease significantly in the *Lactobacillus reuteri* Protectis group throughout the 21-day long study period. This was a significant difference compared to the placebo group. The study was published in Journal of Pediatrics on 24 October 2014.
- **Publication of study showing that BioGaia Protectis tablets are effective in constipated adults** A study of 40 adults with constipation shows that the patients given *Lactobacillus reuteri* Protectis were significantly less constipated after four weeks compared to the patients given placebo. The study was published in J Gastrointest Liver Dis on 9 December 2014.

### Other key events during the year

- **BioGaia invests in MetaboGen AB** BioGaia decided to invest SEK 12 million in MetaboGen AB, based in Gothenburg, Sweden, provided that MetaboGen fulfils certain milestones/commitments. The investment will be made over a two-year period and will then give BioGaia 35% of the share

capital in the company. BioGaia's President, Peter Rothschild, is now Chairman of MetaboGen. The investment of SEK 4.0 million was made in the fourth quarter of 2014 and corresponds to 15% of the share capital.

MetaboGen is a research company that was founded in 2011 in Gothenburg by Professor Fredrik Bäckhed at the University of Gothenburg and Professor Jens B. Nielsen at Chalmers University of Technology, together with GU Holding, which commercialises research results and develops companies linked to the University of Gothenburg. MetaboGen conducts research in metagenomics, the research-intensive and rapidly expanding field devoted to sequencing of all genes in the microbial communities, for example in the human gut, to find previously unknown members of and patterns in the microbial diversity related to health and disease. The aim is to develop new treatments and products for different metabolic and other microbial-associated diseases by influencing large parts of the microflora.

- **Decision to extend the existing production plant at the subsidiary TwoPac in Eslöv** In 2012 a new production plant was completed in Eslöv and was mainly financed by loans from BioGaia AB.

In June 2014 BioGaia made a decision for the subsidiary TwoPac to extend the existing production plant in Eslöv. BioGaia will invest around SEK 16 million in the new facility over the three-year period.

## Key events after the end of the year

- **Agreement for the sale of drops in Vietnam** In January 2015 BioGaia signed an exclusive agreement with VietPhap International Co Ltd for the rights to sell BioGaia ProTectis drops in Vietnam. The launch is planned to take place during 2015.

- **Nestlé launches new product with BioGaia's probiotic** Since the end of 2014 Nestlé has initiated the launch of powder formula with *Lactobacillus reuteri* Protectis for children above the age of one year. The products will mainly be sold in emerging markets.

For several years, BioGaia and Nestlé have had a fruitful cooperation to develop products with probiotics. As previously announced, the parties have entered into an agreement on 30 May 2013 that gives Nestlé the exclusive rights to use BioGaia's patented probiotic strain *Lactobacillus reuteri* Protectis in an additional range of products. The agreement covers infant formula products for children over the age of one year.

## Financial performance in 2014

**Sales** Consolidated net sales amounted to SEK 481.8 million (315.9), which is an increase of SEK 165.9 million (53%). Net sales include license revenue from Nestlé of SEK 95.4 million.

- **License and royalty revenue from Nestlé** In March 2014 BioGaia and Nestlé signed a supplementary agreement to the original one, which meant among other things that BioGaia received the remaining EUR 10.8 million (SEK 95.4 million) – for more information see above.

Nestlé and BioGaia have further broadened and strengthened their cooperation and entered into a supplementary agreement to the original one. The agreement will provide BioGaia with royalties of around SEK 92 million over a three-year period starting in the second quarter of 2014. The royalty revenue in 2014 amounted to SEK 22.9 million.

## Launches in 2014

DISTRIBUTOR/LICENSEE	PRODUCT	COUNTRY	BRAND
Aché	Drops and digestive health tablets	Brazil	BioGaia co-branding
Agefinsa	Drops and digestive health tablets	El Salvador	BioGaia
BG Distribution	Drops with Vitamin D and digestive health tablets with Vitamin D	Hungary	BioGaia
CFR Pharmaceutical/Recalcine	Drops and digestive health tablets	Paraguay	BioGaia
Cube Pharmaceutical	Oral rehydration product with orange flavour and drops with Vitamin D	Greece	BioGaia
Delta	Drops with Vitamin D	Ukraine	BioGaia
Dong Sung	Drops and Gastrus digestive health tablets	South Korea	BioGaia
Ewopharma	Drops with Vitamin D	Croatia and Slovenia	BioGaia
Ewopharma	Tablets with Vitamin D	Latvia and Lithuania	BioGaia
Exeer	Drops and oral rehydration product	Libya	BioGaia
George Petrou Ltd	Oral health tablets	Cyprus	BioGaia
Infectopharm	Drops with Vitamin D	Germany	BioGaia co-branding
KeYuan	Drops and Gastrus digestive health tablets	China	BioGaia
NeoCare	Oral rehydration product	Belgium	BioGaia co-branding
Nestlé	Infant formula with <i>Lactobacillus reuteri</i> Protectis	Ukraine, Russia, the CIS countries and Switzerland	Partner brand
Noos	Drops with Vitamins D and K	Italy	Partner brand
PediAct	Oral rehydration product	France	BioGaia
Plac Control	Oral health tablets	Greece	BioGaia
Semper	Drops and digestive health tablets with strawberry flavour	Norway	Partner brand



- **Net sales excluding license revenue** Excluding license revenue from Nestlé, net sales amounted to SEK 386.4 million, an increase of 22% compared to the previous year. Most of the company's sales are denominated in foreign currency, primarily EUR but also USD and JPY. With unchanged exchange rates compared to the same period of last year, net sales (excluding license revenue) would have been SEK 14.1 million lower. Excluding foreign exchange effects, net sales (excluding license revenue) thus rose by 18%. Exchange rate fluctuations affect both revenue and expenses. Operating profit would also have been SEK 9.2 million lower in the event of unchanged exchange rates, which means an increase (excluding license revenue from Nestlé) of 13% excluding foreign exchange effects compared to the previous year.

**Sales by segment** Since the autumn of 2013 the company is divided into three business units, Paediatrics, Adult Health and New Business. Support functions have been retained at the central level, but the business units are responsible for product development and sales to their respective target groups. This results in a better focus and more effective decision-making. Starting in the first quarter of 2014, the company reports sales and gross profit for these business units. To facilitate comparison, sales and gross profit for the earlier segments, finished consumer products and component products, have been reported during 2014.

- **Paediatric business unit** Sales in BioGaia's core unit, Paediatrics, amounted to SEK 409.1 million (238.6), an increase of SEK 170.5 million (71%). Excluding license revenue from Nestlé, sales of paediatric products reached SEK 313.7 million (238.6), representing growth of 31% (excluding foreign exchange effects, 27%).

The increase is mainly attributable to sales of drops, which rose in all markets, primarily in Europe and "Rest of world", but also in North America and somewhat in Asia. In Europe, sales of drops increased in a number of countries in Eastern Europe (Turkey, Poland, Bulgaria, Slovakia and the Czech Republic), as well as Germany and Finland, while sales decreased mainly in Ukraine, but also slightly in Sweden. The decrease in Ukraine is due to the current instability in the country.

In "Rest of world", sales of drops increased primarily in Brazil, where they were launched in October. Sales were also up in Mexico and Colombia, but declined in South Africa. In North America, sales grew in both Canada and the USA.

Sales of digestive health tablets related to the Paediatrics business unit were also up. Sales increased primarily in "Rest of world", as well as North America, but declined in Europe and were largely unchanged in Asia. The increase in "Rest of world" is mainly attributable to Brazil, where the tablets were launched in September. In North America, sales increased in both the USA and Canada. The decrease in Europe is mainly attributable to Ukraine.

Sales of cultures for infant formula declined slightly compared to the previous year. The agreement regarding infant formula now in force with Nestlé gives them the right to manufacture *Lactobacillus reuteri* for use in infant nutrition, which would result in lower sales of cultures. BioGaia currently has no information about when, and in such case, to what extent Nestlé will exercise this right. This would have a negative impact on sales, but would not affect profit to a large extent since Nestlé buys cultures for infant formula at a significantly lower price following the sale of the rights for use in infant formula (see above).

Revenue under the agreement with Nestlé from 2013 regarding powder formula with *Lactobacillus reuteri* (for more information see below under "Key events after the end of the year") rose somewhat compared to the previous year.

Royalty revenue of SEK 22.9 million (0.0) from the new collaboration agreement with Nestlé was included in sales for the Paediatrics business unit (for more information – see above).

Activities in the Paediatrics business unit during the year were focused on participation in a number of influential conferences, among other things in the USA. These conferences are of vital importance, since they provide opportunity for direct contact with medical professionals from around the world to whom BioGaia promotes the BioGaia brand. Often, the company hosts satellite symposia at which researchers selected by BioGaia present BioGaia's clinical studies to between 100 and 300 doctors. The company is also preparing for the launch of new packaging solutions in 2015.

- **Adult Health business area** Net sales in the Adult Health business unit amounted to SEK 69.4 million (75.6), down by SEK 6.2 million (-8%) (excluding foreign exchange effects, -12%).

The decrease is due to lower sales of digestive health tablets, above all in Finland, where BioGaia's partner has been exposed to aggressive price competition. Sales of digestive health tablets also decreased in Italy.

Sales of oral health tablets grew compared to the previous year. The increase was attributable to both Asia and Europe. In Asia, sales were up in Japan. The increase in Europe was attributable to several countries, primarily in Eastern Europe.

Sales of yoghurt products in Japan decreased. The company discontinued sales of yogurt products in Japan during September, since the margin has not met expectations and because BioGaia's partner has not invested in consumer marketing to the extent required to reach the volumes necessary to achieve profitability.

Activities in the business unit during the year were focused on clarifying the positioning of the new product Gastrus (digestive health product for adults) and on reducing the costs for this product and the ORS product. Furthermore, the company is continuing its efforts to clarify the positioning of other products while at the same time studying the conditions for the launch of additional products. In the Adult Health unit, a great deal of fundamental positioning work towards the target groups remains to be done. In certain areas a repositioning is sufficient, but in others it is necessary to carry out complementary clinical studies in order to boost sales.

- **Finished consumer products** Sales of finished consumer products rose over the previous year by SEK 47.5 million (19%) (excluding foreign exchange effects, 14%) to SEK 303.7 million.

Sales of finished consumer products increased in all regions during the period.

- **Component products** Sales of component products grew by SEK 117.5 million to SEK 176.1 million (201%) compared to the previous year. These sales include license revenue from Nestlé of SEK 95.4 million (see above for more information). Excluding license revenue from Nestlé, sales of component products amounted to SEK 80.7 million (58.6), an increase of 38% (excluding foreign exchange effects, 34%).

Sales were up in Europe but declined in Asia. The decrease in Asia is mainly attributable to sales of cultures to a dairy in South Korea.

Sales of cultures for infant formula decreased somewhat, while revenue from the new product for Nestlé (see above) increased.

Sales of component products include royalties of SEK 22.9 million (0.0) from the new collaboration agreement with Nestlé (see above).

**Sales by geographical market** Sales in Europe grew by SEK 39.5 million (18%)<sup>1)</sup> to SEK 257.81 million.

Sales in the USA and Canada increased by SEK 7.9 million (35%) to SEK 30.3 million.

In Asia, sales declined by SEK 1.3 million (-3%) to SEK 38.8 million. Sales in "Rest of world" were up by SEK 24.4 million (70%) to SEK 59.5 million.

**The BioGaia brand** Of total finished consumer products, 61% (55%) were sold under the BioGaia brand, including co-branding. The target for 2014 was a minimum of 60%.

**Gross profit** Gross profit was SEK 255.1<sup>1)</sup> million (214.2), which is an increase of SEK 40.9 million (19%) compared to the previous year. The total gross margin declined from 68% to 66%<sup>1)</sup>.

Gross margin for the Paediatrics business unit decreased from 70% to 66%<sup>1)</sup>. The margin has fallen during the year as a result of a lower margin on sales of cultures for infant formula, but also due to costs (of around SEK 11.0 million for the full year 2014) attributable to stability problems. To a certain extent, this has been compensated by royalties from Nestlé with a margin of 100% at the gross profit level. The stability problem is now under control and no additional costs are expected to arise.

Gross margin for the Adult Health business unit rose from 62% to 64%. The variation is due to a somewhat changed product mix to products with better margins.

**Operating expenses** Total operating expenses rose by 20% to SEK 161.3 million. Excluding the subsidiary IBT, operating expenses were up by 15%.

Selling expenses grew by SEK 10.4 million (13%) and amounted to SEK 89.8 million (79.4), which is equal to 23% (25) of net sales<sup>1)</sup>. It was primarily expenses for samples and conferences that increased compared to the previous year. In addition, marketing expenses were up in Japan, partly in connection with the launch of drops during the third quarter.

Administrative expenses amounted to SEK 17.7 million (14.4), which is equal to 5% (5) of net sales<sup>1)</sup>. The increase of SEK 3.3 million (23%) is mainly due to higher personnel expenses and increased administrative expenses in the subsidiary TwoPac (see below).

R&D expenses are reported at SEK 53.9 million (40.6), which is equal to 14% (13) of net sales<sup>1)</sup>. The increase of SEK 13.3 million (33%) is mainly attributable to costs for the subsidiary IBT of SEK 6.6 million (0) (see below). In addition, development costs rose sharply, mainly due to development projects together with Nestlé resulting from the new collaboration agreement (see above). Furthermore, both patent expenses and personnel expenses were higher during the year. Excluding the costs for IBT, R&D expenses were up by 17%

Other operating income/expenses refer to foreign exchange gains/losses on operating receivables and liabilities.

**Operating profit** Operating profit was SEK 196.9 million (81.7), an increase of SEK 115.2 million (141%). Excluding license revenue from Nestlé, operating profit was SEK 101.5 million (81.7), an increase of SEK 24%. Excluding the subsidiary IBT, operating profit rose by 32%. Operating margin was 26%<sup>1)</sup> (excluding the subsidiary IBT, 28%).

**Financial items and profit before tax** Profit before tax was SEK 192.5 million (83.8), an increase of SEK 108.7 million (130%) compared to the previous year. Net financial items include a foreign exchange loss of SEK -6.6 million (-2.9) on forward exchange contracts in EUR. At 31 December 2014 the company had outstanding forward exchange contracts for EUR 13.3 million at an average exchange rate of SEK 9.07. Forward exchange contracts amounting to EUR 8.7 million will mature for payment in 2015 and the remaining EUR 4.6 million in 2016. The actual exchange gain/loss depends on the exchange rate on the maturity date of the contracts. If the EUR rate on the maturity date is lower/higher than that at 31 December 2014 (9.48), an exchange gain/loss will be recognised in the future.

**Profit after tax** Profit after tax was SEK 148.0 million (64.2), an increase of SEK 83.8 million (130%). Excluding license revenue from Nestlé, profit after tax was SEK 73.6 million (64.2), which is SEK 9.4 million (15%) better than in the previous year.

The tax rate for the Group was 24% (23). The Group pays tax on profits in the Swedish companies. The loss in Japan is not deductible against the Swedish profits. Loss carryforwards in the Japanese subsidiary at 31 December 2014 amounted to SEK 35.2 million. The deferred tax asset for these has not been recognised, since a sustainable profit level has not yet been shown in the Japanese subsidiary.

The company has an ongoing tax matter related to a write-down of receivables from the Japanese subsidiary. In the event of a negative outcome, this could result in additional tax expenses of SEK 3.1 million. If the outcome is positive, there is opportunity to receive an additional tax income of SEK 3.8 million for previous years.

**Earnings per share** Earnings per share were SEK 8.53 (3.57). Excluding license revenue from Nestlé, earnings per share amounted to SEK 4.23.

**Cash flow** The Group's cash and cash equivalents at 31 December 2014 totalled SEK 210.7 million (234.3). Cash flow for the year amounted to SEK -25.0 million (-140.8). Cash flow for the year included license revenue from Nestlé of SEK 95.4 million (0), dividends of SEK 120.9 million (172.7) and tax payments of SEK 66.8 million (10.8).

**Equity** Consolidated equity at 31 December 2014 amounted to SEK 344.6 (316.9). The Group's equity/assets ratio was 83% (83).

In June 2012 BioGaia carried out the warrant programme that was resolved on by the Annual General Meeting the same year. A total of 87,000 warrants were subscribed for, of which the management subscribed for 41,000. The warrants were issued at a market price of SEK 14.27 each following valuation according to the Black & Scholes formula, which provided

the Parent Company with proceeds of SEK 1.3 million. Each warrant entitles the holder to subscribe for one class B share for SEK 241.90 on 1 June 2015. Volatility was estimated at 40%. If all of the subscription warrants are exercised, the company's equity will be increased by SEK 21.0 million. This represents a dilutive effect of approximately 0.5% on the share capital and 0.4% on the total number of votes upon the full exercise of warrants.

In order to achieve a high level of participation, the 2012 AGM decided to pay a subsidy of SEK 10 per warrant (after 1 June 2015) to the employees who have subscribed for subscription warrants but have not exercised the right to buy shares. A provision of SEK 1.1 million for this obligation was made in 2014 since at the current share price there is a risk that the subsidy must be paid.

**Dividend** The Board of Directors of BioGaia AB proposes to the upcoming AGM an ordinary dividend of SEK 3.46 per share and an extraordinary dividend of SEK 1.54 per share, for a total dividend of SEK 5.00 per share. For more information, see below under "Proposed appropriation of profits".

**Investments in property, plant and equipment** Investments in property, plant and equipment amounted to SEK 18.4 million (16.6), of which SEK 17.3 million (14.7) refers to TwoPac AB.

Investments in capitalised development expenses amounted to SEK 6.1 million (0) and refer to the development of a product for the NEC project in the subsidiary IBT AB.

Investments in financial assets refer to the investment in MetaboGen AB (see above).

**Subsidiary in Japan** Net sales in the wholly owned subsidiary in Japan reached SEK 17.1 million (15.2). Operating profit in the Japanese subsidiary amounted to SEK -6.1 million (-7.7). The growth in sales is primarily attributable to dental products. In 2015 BioGaia Japan will work with the launch of drops and will continue the successful focus on oral health products through BioGaia's distributor, which markets the products at dental clinics.

**Subsidiary TwoPac AB** Net sales in the wholly owned subsidiary TwoPac amounted to SEK 44.7 million (37.5). Operating profit was SEK 7.7 million (9.9). Profit after tax was SEK 5.5 million (7.3). The drop in profit is mainly explained by higher personnel expenses as a result of more stringent quality requirements and higher costs for development of new products. The increased quality requirements are internally driven to a certain extent, but are also motivated by BioGaia's desire to have the facility approved for pharmaceutical production by the Swedish Medical Products Agency. Furthermore, additional resources have been devoted to qualification and validation of new machinery.

In June BioGaia made a decision for the subsidiary TwoPac to extend its existing production plant in Eslöv. BioGaia will invest around SEK 16 million in the new facility over a three-year period.

TwoPac manufactures and develops products only for BioGaia.

**Subsidiary CapAble AB** CapAble, which is owned 90.1% by BioGaia AB and 9.9% by the company's president, was started in November 2008 to manufacture and sell the patented LifeTop Cap. Net sales in CapAble totalled SEK 0.5 million (0.5) during the period. Operating profit amounted to SEK -2.9 million (-2.6). The company experienced quality problems during the year, which meant that sales did not gain momentum as expected. The company's assessment is that the problems have now been solved and that sales will increase during 2015.

**Subsidiary IBT AB** In November 2013, the Board of BioGaia made a decision to invest in the first phase of a long-term project aimed at developing a drug with rigorous hygiene, analysis and documentation requirements, to treat the highly fatal disease Necrotising Enterocolitis (NEC), which affects premature infants. BioGaia will invest up to SEK 42 million in the project over a two-year period. The project will be driven by BioGaia's subsidiary Infant Bacterial Therapeutics (IBT), of which 9% is owned by the company's President, Staffan Strömberg, and its Research Director, Eamonn Connolly, and 0.9% by Board member Anders Eklblom, (former Global Head of R&D Science & Technology Integration at AstraZeneca AB and President of AstraZeneca AB). The remaining 90.1% is owned by BioGaia. It is the company's assessment that approximately SEK 26 million of the SEK 42 million will be capitalisable in IBT as development expenses, which will result in a cost burden of around SEK 16 million over a two-year period.

<sup>1)</sup> Excluding license revenue from Nestlé of SEK 95.4 million. Including license revenue from Nestlé, operating margin amounted to 41%, total net sales to SEK 481.8 million, net sales of component products to SEK 176.1 million, net sales in the Paediatrics business unit to SEK 409.1 million, net sales in Europe to SEK 353.2 million, gross profit to SEK 350.4 million, operating profit to SEK 196.8 million, profit before tax to SEK 192.5 million and profit after tax to SEK 148.0 million. Operating margin amounted to 41%. Earnings per share amounted to SEK 8.53.



Operating profit in IBT during the period amounted to SEK -6.7 million. The company has made investments in capitalised development expenses of SEK 6.1 (0) million. The company does not yet have any revenue but it is BioGaia's assessment that the product will generate sufficient future economic benefits and that there is therefore no indication of impairment.

**Parent Company** Net sales in the Parent Company reached SEK 464.2 million (304.6) and profit before tax was SEK 192.6 million (76.9). Cash flow in the Parent Company totalled SEK -27.6 million (-143.2).

## Research and development activities

BioGaia has an extensive research network and collaborates with numerous universities and hospitals around the world, such as the Swedish University of Agricultural Sciences in Uppsala, Sweden, the Karolinska Institute in Stockholm, Sweden, Sahlgrenska University Hospital in Gothenburg, Sweden, Texas Children's Hospital in the USA, and the University Hospitals of Bari and Turin in Italy.

BioGaia's strains of *Lactobacillus reuteri* are some of the world's most well researched probiotics, especially in young children. To date, 137 clinical studies using BioGaia's human strains of *Lactobacillus reuteri* have been performed on around 11,700 individuals of all ages. The results have been published in 108 articles in scientific journals.

Studies have been performed on:

- Infantile colic and digestive health in children
- Antibiotic-associated diarrhoea (AAD)
- Acute diarrhoea
- Gingivitis (inflammation of the gums)
- Periodontal disease (tooth loss)
- General health
- *Helicobacter pylori* (the gastric ulcer bacterium)
- Necrotising enterocolitis (NEC)

R&D expenses are reported at SEK 53.9 million (40.6), which is equal to 14% (13) of net sales. The increase of SEK 13.3 million (33%) is mainly attributable to costs in the subsidiary IBT of SEK 6.6 million (0) (see below). Furthermore, costs for development projects increased substantially as a result of the new cooperation agreement with Nestlé (see above). In addition, patent costs and personnel expenses were up during the period. Excluding costs related to IBT, R&D expenses rose by 17%.

**Reporting of clinical studies** Publication of clinical trial results is a key success factor for BioGaia. The International Committee of Medical Journal Editors has initiated a policy requiring clinical investigators to deposit information about trial design into an accepted clinical trials registry before the onset of patient enrolment, and this has now become a prerequisite for publication of trial outcomes in major medical journals. ClinicalTrials.gov is a registry of clinical trials provided by the U.S. National Institutes of Health and BioGaia encourages all clinicians working with BioGaia products to register their trials on this site. Many of the trials are registered at an early stage, which means that some of the registered trials will not be performed as planned. Consequently, BioGaia takes no responsibility for ensuring that the registered trials reach completion or are successfully reported in the register or the scientific literature. When clinical trial results of significance for the company's operations do become available, BioGaia will report these through press releases.

## Environmental information

BioGaia has a fundamentally ethical vision, namely to improve the health of people around the world by offering first class probiotic products. By offering alternatives that make it possible to improve health through the use of natural organisms, without side effects, the company's hope is to reduce the use of medications and antibiotics. In a longer perspective, this will also have positive effects on the environment.

BioGaia has measured the company's climate impact in 2012 and 2013. Starting in 2013, the subsidiary TwoPac AB is also included. The greatest climate impact is caused by the company's air travel, followed by product packages. In 2013 BioGaia took part in CDP Nordic Climate Change report for the first time and won a prize for its report as the best newcomer. In 2014 the company will also participate in the CDP report.

BioGaia climate compensates by purchasing certificates from Vi Agroforestry. In 2013 and 2014, a total of 9,286 trees were planted through BioGaia's compensation in Vi Agroforestry's projects in the Kagera region of western Tanzania.

### Goals for environmental work in 2015

1. Report on BioGaia's climate impact in 2014
2. Communicate BioGaia's environmental responsibility to employees and distributors.
3. Climate compensate via Vi Agroforestry for emissions during 2014.
4. Take part in CDP Nordic Climate Change Report together with 260 Nordic companies.

BioGaia conducts no operations that require permits.

## Business risks and uncertainties

BioGaia's operations are associated with both risks and opportunities of various types. Certain risks are of a general nature, while others are more specific to the company. The following section is not a complete risk analysis, but an indication of the factors of significance for future development.

**The Japanese venture** The wholly owned Japanese subsidiary has operated at a loss since the start in 2006. The business model previously used was found to be unsuccessful and in 2010 a decision was made to change the business model in Japan to that which is used in the other markets. On the balance sheet date, assets in the Japanese subsidiary were reported at SEK 6.3 million. BioGaia's assessment is that there is no indication of impairment of these assets. In the Parent Company, current receivables from the Japanese subsidiary have been written off. The loan to the Japanese subsidiary and participations in the company have been written down to zero.

Net sales in the wholly owned Japanese subsidiary amounted to SEK 17.1 million (15.2) and operating profit was SEK -6.1 million (-7.7). The increase in sales is mainly attributable to dental products. In 2015 BioGaia Japan will work on the launch of drops and will continue to support the successful focus on oral health products through BioGaia's distributor, which markets the products at dental clinics.

**CapAble AB** CapAble, which is 90.1% owned by BioGaia AB, was started in November 2008 to manufacture and sell the patented LifeTop Cap. The shares in the subsidiary CapAble are reported at a total of SEK 6.9 million in the Parent Company. CapAble has operated at a loss since the start in 2008. BioGaia made total conditional shareholder contributions of SEK 6 million to CapAble in 2009 and 2010. BioGaia AB has made total group contributions of SEK 12.7 million during the period from 2010 to 2014. Profit before tax for 2014 Profit before tax for -2.9 million (-2.6). On the balance sheet date, the assets in CapAble were reported at SEK 3.6 million. BioGaia's assessment is that CapAble will show profitability in coming years, for which reason there was no indication of impairment on the balance sheet date.

**Development of drug against NEC** Infant Bacteria Therapeutics AB (IBT), which is 90.1% owned by BioGaia, was established in November 2013. At that time, the Board of BioGaia made a decision to invest in the first phase of a long-term project aimed at developing a drug with rigorous hygiene, analysis and documentation requirements, to treat the highly fatal disease Necrotising Enterocolitis (NEC), which affects premature infants. BioGaia will invest up to SEK 42 million in the project over a two-year period. BioGaia AB has made conditional shareholder contributions of SEK 11.0 million and group contributions of SEK 7.0 million to IBT. On the balance sheet date, assets in IBT were reported at SEK 7.6 million in the Group. BioGaia's assessment is that IBT will show profitability in coming years, for which reason there was no indication of impairment on the balance sheet date.

The project offers major opportunities, but is also associated with substantial risks. If the drug development is not realised, it is BioGaia's intention to market the formulation under another product category.

**BioGaia's partners** BioGaia does not sell directly to end-users but instead sells its products to companies (partners) which then sell the products to third parties (end-users). The normal agreement has term of 3-5 years.

BioGaia is dependent on these partners to invest the resources necessary for marketing and sales. In order to influence this to a greater extent on its own, BioGaia launched its own brand in 2006. Today a number

of BioGaia's partners sell products wholly or partly under the BioGaia brand and BioGaia-branded products are currently sold in more than 50 countries. BioGaia also provides its partners with strong support in the form of education, information about new clinical studies and speakers at symposia, as well as marketing and PR support. There is a risk that BioGaia's partners will not perform according to the company's wishes. However, BioGaia has formulated its agreements so that it is possible to terminate the agreement if a distributor does not meet certain minimum targets.

**Research and development** BioGaia invests considerable sums in research, clinical studies and product development with the aim of developing products with proven health benefits. Even after thorough pilot studies, there is always a risk that a project will be wholly or partly unsuccessful.

**Intellectual property** BioGaia's business activities are based on a large number of intellectual property rights, such as patents, trademarks, names of strains and Internet domains. The company works continuously to strengthen its intellectual property rights by protecting the use of the company's products. The various patents have different terms but those covering the most used strains in BioGaia's products apply until 2027.

There is always a risk for infringement of intellectual property. These rights are enforced on an ongoing basis, but there are no guarantees that future infringements will not cause the company damage. BioGaia continuously monitors the market.

**Regulatory situation** BioGaia's products are currently sold in some 90 countries around the world. Due to their differing regulatory systems, the length of time between contract and product launch varies between countries. In most countries the products are registered as dietary supplements but in certain markets, like Turkey, Canada, Hong Kong and Peru, they are registered as a category of pharmaceuticals.

There is always a risk that the rules will be changed in the different markets with a resulting negative impact on sales, at least for a limited period of time.

In the EU, the use of nutrition and health claims is regulated by the European Food Safety Authority (EFSA). The EFSA rules, which went into effect in December 2012, apply to food products that are marketed to consumers with various claims about preventative health effects, for example that a lower intake of cholesterol reduces the risk for cardiovascular disease or a food product's ability to improve the immune defence. In order to make a health claim for a product and in marketing, EFSA approval is required.

In the case of BioGaia's products, the distributors show the clinical studies to healthcare professionals (doctors, midwives, etc.) who then recommend the products to patients because the patient in question is in more or less urgent need of the product's probiotic effects. As a result, the EFSA rules are not applicable to the majority of BioGaia's products. Furthermore, because the products are primarily recommended by healthcare professionals, such as doctors and nurses, in most countries there is no need to make general health claims in the marketing materials as would be the case if the company was marketing a yoghurt or beverage directly to consumers.

If it becomes necessary to use another type of marketing for future products, BioGaia will apply for approval of its health claims from the EFSA. Together with partners BioGaia is assessing the opportunities to register its products under the existing regulations as Food for Special Medical Purposes, natural remedies or other registration categories depending on the type of product and the country involved.

**Employees** BioGaia's operations are wholly dependent on the employees' expertise, and they therefore make up the company's most valuable resource. In order to attract and retain skilled and motivated employees, BioGaia strives to create a culture in which all employees are given the opportunity to develop, influence their own work situation and maintain a good balance between work and leisure in order to avoid stress.

**Product liability insurance** BioGaia's partners require the company to have product liability insurance as protection against liability claims for third party damage. BioGaia has product liability insurance that provides coverage up to SEK 60 million per claim up to a maximum of SEK 120 million per year. The insurance is valid worldwide. BioGaia's assessment is that these insurance amounts are relevant and adequate for the company's operations.

## Financial risk management

The overall objective of the Group's finance function is to secure cost-effective financing for the Group's operations and group companies and to provide secure cash management with a market-based return on investment. The overall objective of financial risk management is to minimise the risk for negative effects on the Group's earnings. Consequently, the Group's financial investments must have a low risk profile.

Below is a description of the Group's assessed risk exposure and the related risk management.

**Currency risk** BioGaia has revenue primarily in EUR, but also in SEK, USD and JPY, and expenses primarily in SEK, EUR, JPY and USD.

The breakdown of net sales in 2014 (excluding license revenue from Nestlé) was approximately:

EUR 55%  
SEK 25%  
USD 15%  
JPY 5%

In 2014 the company had a cash flow surplus of approximately EUR 25.9 million (17.2) (2014 including the payment of EUR 10.8 million from Nestlé), a cash flow deficit of JPY -76.8 million (-138.7) and a cash flow surplus of USD 3.5 million (2.2).

Growth in sales has also led to increased currency risks, for which reason the company has taken currency hedges in EUR. The company's Board of Directors has issued a policy to hedge approximately 50-60% of projected cash flow 12 months forward and approximately 10-40% of projected cash flow 13-24 months forward in order to spread the risk for exchange rate fluctuations. At 31 December 2014 the company had outstanding forward exchange contracts for EUR 13.3 million at an average exchange rate of SEK 9.07. Forward exchange contracts amounting to EUR 8.7 million will mature for payment in 2015 and the remaining EUR 4.6 million in 2016. The actual exchange gain/loss depends on the exchange rate on the maturity date of the contracts. If the EUR rate on the maturity date is lower/higher than that at 31 December 2014 (9.48), an exchange gain/loss will be recognised in the future. For more information see Notes 9, 21 and 24.

The average exchange rate for EUR/SEK in 2014 was 9.10. If the EUR/SEK rate had been SEK 0.10 higher, BioGaia's net sales would have been approximately SEK 2.4 million higher and operating profit would have been around SEK 1.4 million higher (excluding license revenue from Nestlé).

The average exchange rate for USD/SEK in 2014 was 6.86. If the USD/SEK rate had been SEK 0.10 higher, BioGaia's net sales would have been approximately SEK 1.0 million higher and operating profit would have been around SEK 0.7 million higher.

A stronger SEK rate, primarily against the EUR, will decrease the value of BioGaia's sales and profit, but through profitable forward exchange transactions and by trying to reallocate a portion of expenses to EUR, the company is trying to minimise the impact on profit. The company is also trying to reallocate a portion of revenue from EUR to other currencies.

**Interest rate risk** The Group has no loans and therefore no interest rate risks. Excess liquidity is invested mainly in bank accounts – see liquidity risk below.

**Credit risks** BioGaia's credit risks are attached to trade receivables and, for the Parent Company, also loans to subsidiaries. When signing agreements with new customers, BioGaia always carries out an assessment of the customer's financial position. The company has routines for collection of past due accounts receivable and additional evaluation of the customers' financial position is carried out when needed in order to minimise risks.

The loan from the Parent Company to the subsidiary CapAble AB has been used to purchase equipment for manufacturing of LifeTop Cap. The company's assessment is that credit risk on the loan is low.

The loan from the Parent Company to the subsidiary TwoPac AB has been used mainly to build a new production facility in Eslöv, Sweden, that was completed and taken into operation during 2012. In 2013 and 2014 additional loans were paid to TwoPac for construction of new facility and new production machinery. The company's assessment is that credit risk on the loan is low.

**Liquidity risk** The company's excess liquidity may be invested only in bank accounts, commercial paper or other fixed income securities with very limited risk. This means that no investments may be made in shares, equity funds, options, etc.

**Cash flow risk** Cash flow for the period amounted to SEK -25.0 million (-140.8). Cash flow included license revenue from Nestlé of SEK 95.4 million (0), dividends of SEK 120.9 million (172.7) and tax payments of SEK 66.8 million (10.8). Because cash and cash equivalents at 31 December 2014 amounted to SEK 210.7 million (234.3), no infusion of capital is necessary during the nearest 12-month period.

**Price risk** BioGaia buys most of its goods on the international market and has several alternative suppliers, which reduces the company's price risk. BioGaia's price to distributors is largely the same for all, but can vary with respect to the order volume. Certain markets are subject to aggressive price competition towards consumers. However, BioGaia's strategy is not to compete in terms of price but to instead convince doctors of the effectiveness and safety of the products by showing the results of clinical studies.

## Employees

The number of employees in the Group at 31 December 2014 was 95 (85), consisting of 54 women and 41 men. The management team includes five men and seven women. In 2014, 17 new employees were hired and seven left the company.

**BioGaia's incentive scheme for the employees** In June 2012 BioGaia carried out the warrant programme that was decided by the Annual General Meeting the same year. A total of 87,000 warrants have been subscribed for, of which the management subscribed for 41,000. The warrants were issued at a market price of SEK 14.27 each following valuation according to the Black & Scholes formula, which provided the Parent Company with proceeds of SEK 1.3 million. Each warrant entitles the holder to subscribe for one class B share for SEK 241.90 on 1 June 2015. Volatility was estimated at 40%.

If all of the subscription warrants are exercised, the company's equity will be increased by SEK 21.0 million. This represents a dilutive effect of approximately 0.5% on the share capital and 0.4% on the total number of votes upon the full exercise of warrants.

In order to achieve a high level of participation, the 2012 AGM decided to pay a subsidy of SEK 10 per warrant (after 1 June 2015) to the employees who have subscribed for subscription warrants but have not exercised the right to buy shares. A provision of SEK 1.1 million for this obligation was made in 2014 since at the current share price there is a risk that the subsidy must be paid.

BioGaia has no incentive schemes currently in force for the employees and in 2014 has only paid fixed salary to the employees.

## Future outlook

BioGaia's goal is to create strong value growth and a good return for the shareholders. This will be achieved through a greater emphasis on the BioGaia brand, increased sales to both existing and new customers and a controlled cost level.

The financial target is a sustainable operating margin (operating profit in relation to sales) of at least 30% with continued strong growth and increased investments in research, product development and brand building.

BioGaia's dividend policy is to pay a shareholder dividend equal to 40% of profit after tax.

In view of the Company's strong portfolio consisting of an increased number of innovative products the majority under the company's own brand, clinical trials and a growing distribution network covering a large share of the key markets, BioGaia's future outlook is bright.

## The Board of Directors' proposal to the AGM regarding remuneration and other terms of employment for senior executives

The Board of Directors proposes that the AGM approve the following guidelines for remuneration and other terms of employment for senior executives in the Group. These principles apply to employment contracts entered into after the decision of the AGM and in the event that changes are made in the existing terms after this time. It is of fundamental importance for the Board that the principles for remuneration and other terms of employment for senior executives in the Group create long-term motivation and enable the company to retain competent employees who work to attain maximum shareholder and customer value. In order to achieve this, it is vital to uphold fair and internally

balanced terms that are market-based and competitive with respect to the structure, scope and level of remuneration. The total remuneration package for the affected individuals should contain a well-balanced mix of fixed salary, variable remuneration, long-term incentive schemes, pension benefits, other benefits and terms of notice/termination benefits.

- **Fixed salary** Fixed salary shall be differentiated on the basis of the individual's role and responsibilities, as well as the individual's competence and experience in the relevant position.
- **Variable remuneration** The amount of variable remuneration shall not exceed 25% of total remuneration.
- **Long-term incentive schemes** Every year, the Board of Directors shall evaluate whether a long-term share-based or share price-based incentive scheme should be proposed to the AGM. Other types of long-term incentive schemes can be decided on by the Board. Any remuneration in the form of long-term incentive schemes shall be consistent with generally accepted practices in the respective market.
- **Pensions** Senior executives who are entitled to pension benefits shall have pension agreements of the defined contribution type. The mandatory age of retirement for senior executives who are Swedish citizens is 65 years, and for others according to the pension rules in their respective countries. The amount of benefit payable depends on the amount payable under the pension agreements in force.
- **Other benefits** Other benefits shall be of limited value in relation to the other remuneration and shall be consistent with general norms in the respective geographical market.
- **Terms of notice and termination benefits** The President and the company have a mutual notice period of 18 months. The company's Vice Presidents have a corresponding notice period of six months. For other senior executives, the notice period is three months.

The Board of Directors proposes that the Board be authorised to deviate from the above proposed guidelines in individual cases when there is special reason to do so.

For more information about remuneration to senior executives, see Note 4.

## Most recently adopted guidelines regarding remuneration and other terms of employment of senior executives

The most recently adopted guidelines correspond to those that are proposed to the AGM (see above).

## Corporate governance

BioGaia has issued a separate corporate governance report. See page 64-65.

## Proposed appropriation of profits

The following funds in the Parent Company are at the disposal of the Annual General Meeting (SEK):

Retained profit	182,186,541
Profit for the year	149,589,779
Together amounting to:	<b>331,776,320</b>

The Board of Directors proposes that the profits be disposed of as follows:

To be paid as a dividend to the shareholders	86,354,810
To be carried forward to new account:	245,421,510
Total:	<b>331,776,320</b>

\*) The proposed dividend consists of an ordinary dividend of SEK 3.46 per share and, in view of the company's good liquidity and strong balance sheet, an extraordinary dividend of SEK 1.54 per share, amounting to a total dividend of SEK 5.00 per share.

# Group

## Statement of comprehensive income

SEK 000s	Note	2014	2013
Net sales	2, 3	481,802	315,875
Cost of goods sold	2	-131,338	-101,711
<b>Gross profit</b>	<b>2</b>	<b>350,464</b>	<b>214,164</b>
Selling expenses	4	-89,759	-79,396
Administrative expenses	4, 5	-17,666	-14,356
Research and development expenses	4, 12	-53,867	-40,555
Other operating income	6	7,711	1,796
<b>Operating profit</b>	<b>7</b>	<b>196,883</b>	<b>81,653</b>
Financial income	8	2,382	5,081
Financial expenses	9	-6,740	-2,974
<b>Net financial items</b>		<b>-4,358</b>	<b>2,107</b>
<b>Profit before tax</b>		<b>192,525</b>	<b>83,760</b>
Tax	10	-44,536	-19,572
<b>PROFIT FOR THE YEAR</b>		<b>147,989</b>	<b>64,188</b>
<i>Other comprehensive income:</i>			
Gain/losses arising on translation of the financial statements of foreign operations:		642	-1,419
<b>Comprehensive income for the year</b>		<b>148,631</b>	<b>62,769</b>
<i>Profit for the year attributable to:</i>			
Owners of the Parent Company		147,406	61,722
Non-controlling interests	11	583	2,466
		147,989	64,188
<i>Comprehensive income for the period attributable to:</i>			
Owners of the Parent Company		148,048	60,303
Non-controlling interests	11	583	2,466
		148,631	62,769
<b>Earnings per share</b>			
Basic earnings per share, SEK		8,53	3,57
Diluted earnings per share, SEK		8,53	3,56
Number of shares, thousands		17,271	17,271
Average number of shares, thousands		17,271	17,271
Number of outstanding warrants, thousands		87	87
Number of outstanding warrants with a dilutive effect, thousands		-	87
Average number of shares after dilution, thousands		17,271	17,358

## Cash flow statements

SEK 000s	Note	2014	2013
<b>Operating activities</b>			
Operating profit		196,883	81,653
<i>Adjustments for non-cash items:</i>			
Depreciation/amortisation		5,652	5,541
Capital gains/losses on the sale of shares		-4	-
Capital gains/losses on the sale of non-current assets		307	-86
Other non-cash items		-1,156	-222
		201,682	86,886
Realised forward exchange contracts		-1,186	193
Interest received		2,362	5,080
Interest paid		-148	-84
Taxes paid		-66,829	-10,799
<b>Cash flow from operating activities before changes in working capital</b>		<b>135 881</b>	<b>81,276</b>
<i>Cash flow from changes in working capital:</i>			
Inventories		-6,412	7,288
Current receivables		-19,048	-7,123
Trade payables		-1,000	3,192
Current interest-free operating liabilities		14,962	-6,192
<b>Cash flow from operating activities</b>		<b>124,383</b>	<b>78,441</b>
<i>Investing activities:</i>			
Acquisition of intangible assets	12	-6,075	-
Purchase of property, plant and equipment	13	-18,406	-16,634
Sale of property, plant and equipment		-	6
Purchase of financial assets	14	-4,000	- <sup>1)</sup>
<b>Cash flow from investing activities</b>		<b>-28,481</b>	<b>-16,628</b>
<i>Financing activities:</i>			
Purchase of financial assets	14	-	-30,000 <sup>1)</sup>
Sale of financial assets		5	90 <sup>1)</sup>
Dividend	14	-120,897	-172,710
<b>Cash flow from financing activities</b>		<b>-120,892</b>	<b>-202,620</b>
<b>CASH FLOW FOR THE YEAR</b>		<b>-24,990</b>	<b>-140,807</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>			
		234,271	374,974
Exchange difference in cash and cash equivalents		1,385	104
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>		<b>210,666</b>	<b>234,271</b>

<sup>1)</sup> In 2013 figures a reclassification of SEK 29,910 thousand has been made between cash flow from investing activities and cashflow from financing activities.

## Statement of financial position

SEK 000s	Note	31Dec, 2014	31Dec, 2013
<b>ASSETS</b>			
<i>Non-current assets:</i>			
Intangible assets	12	6,075	–
Property, plant and equipment	13	72,752	60,286
Other financial assets	14	4,000	–
Deposits		20	17
<b>Total non-current assets</b>		<b>82,847</b>	60,303
<i>Current assets:</i>			
Inventories	16	21,148	14,585
Trade receivables	17, 21	75,911	65,065
Other receivables	19	6,726	4,089
Deferred expenses and accrued income	20	18,297	5,025
Short-term investments	21	13	80
Cash and cash equivalents	21	210,666	234,271
<b>Total current assets</b>		<b>332,761</b>	323,116
<b>TOTAL ASSETS</b>		<b>415,608</b>	383,419

## Statement of changes in equity

SEK 000s	Share capital	Other contributed capital	Translation reserve	Retain profit incl. profit for the year	Equity attributable to owners of the Parent Company	Non-controlling interests	Total equity
<b>Opening balance, 1 Jan 2013</b>	17,271	6,053	586	429,393	453,303	3,491	456,794
Dividend				–172,710	–172,710		–172,710
Purchase of 50% of TwoPac AB <sup>1)</sup>				–23,553	–23,553	–6,447	–30,000
Disposal of 9% of IBT AB <sup>1)</sup>					–	4	4
<b>Total transactions with owners</b>				–196,263	–196,263	–6,443	–202,706
<b>Profit for 2013</b>				61,722	61,722	2,466	64,188
<i>Other comprehensive income</i>							
Gain/losses arising on translation of the financial statements of foreign operations			–1,419		–1,419		–1,419
<b>Comprehensive income for the year</b>			1 419	61 722	60 302	2 466	62 769
<b>Closing balance, 31 December 2013</b>	17,271	6,053	–835	294,852	317,341	–484	316,857
Dividend				–120,897	–120,897		–120,897
Disposal of 0.9% of IBT AB						0	0
<b>Total transactions with owners</b>				–120,897	–120,897	0	–120,897
<b>Profit for 2014</b>				147,406	147,406	583	147,989
Gain/losses arising on translation of the financial statements of foreign operations			642		642		642
<b>Comprehensive income for the year</b>			642	147,406	148,048	583	148,631
<b>Closing balance, 31 Dec 2014</b>	17,271	6,053	–193	321,361	344,492	99	344,591

<sup>1)</sup> In the previous year's annual report these transactions were not reported as transaction with owners but other transactions. A correction has been made in this year's annual report.

## Statement of financial position

SEK 000s	Note	31Dec, 2014	31Dec, 2013
<b>EQUITY AND LIABILITIES</b>			
<i>Equity</i>			
Share capital		17,271	17,271
Other contributed capital		6,053	6,053
Reserves		–193	–835
Retained profit		173,955	233,130
Profit for the year attributable to owners of the Parent Company		147,406	61,722
<b>Total equity attributable to owners of the Parent Company</b>		<b>344,492</b>	317,341
Non-controlling interests	11, 14	99	–484
<b>Total non-controlling interests</b>		<b>99</b>	–484
<b>Total equity</b>		<b>344,591</b>	316,857
<i>Non-current liabilities:</i>			
Deferred tax liability	10	192	85
<b>Total non-current liabilities</b>		<b>192</b>	85
<i>Current liabilities:</i>			
Other provisions	23	3,900	–
Prepayments from customers	21	6,804	508
Trade payables	21	16,952	17,808
Current tax liability		5,827	29,340
Other liabilities	24	8,991	3,934
Accrued expenses and deferred income	25	28,351	14,887
<b>Total current liabilities</b>		<b>70,825</b>	66,477
<b>Total liabilities</b>		<b>71,017</b>	66,562
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>415,608</b>	383,419
<b>Pledged assets and contingent liabilities in the Group</b>			
	26		

# Parent Company

## Income statements

SEK 000s	Note	2014	2013
Net sales	2, 3	464,206	304,624
Cost of goods sold	2	-139,971	-108,840
<b>Gross profit</b>	2	<b>324,235</b>	195,784
Selling expenses	4	-68,720	-59,662
Administrative expenses	4, 5	-15,075	-13,302
Research and development expenses	4, 12	-46,346	-40,461
Other operating income	6	7,851	1,796
<b>Operating profit</b>	7	<b>201,945</b>	84,155
<i>Result from financial investments</i>			
Impairment loss on shares in group companies	14	-2,874	-2,589
Impairment loss on receivable from group company	15	-2,835	-8,960
Interest income and similar profit/loss items	8	3,096	7,279
Interest expense and similar profit/loss items	9	-6,707	-2,965
<b>Net financial items</b>		<b>-9,320</b>	-7,235
<b>Profit before appropriations and taxes</b>		<b>192,625</b>	76,920
Change in tax allocation reserve	9	-	109,341
<b>Profit before tax</b>		<b>192,624</b>	186,261
Tax	10	-43,035	-41,604
<b>PROFIT FOR THE YEAR</b>		<b>149,590</b>	144,657

The Parent Company has no transactions in other comprehensive income, which means that comprehensive income for the year corresponds to profit for the year above. As a result, the Parent Company presents no separate statement of comprehensive income.

## Cash flow statements

SEK 000s	Note	2014	2013
<b>Operating activities</b>			
Operating profit		201,945	84,155
<i>Adjustments for non-cash items:</i>			
Depreciation/amortisation		867	1,157
Capital gains/losses on the sale of shares		-4	-
Capital gains/losses on the sale of non-current assets		-	-86
Other non-cash items		-1,156	-224
		201,652	85,002
Realised forward exchange contracts		-1,186	193
Interest received		3,077	5,686
Interest paid		-116	-83
Taxes		-64,828	-9,816
<b>Cash flow from operating activities before changes in working capital</b>		<b>138,599</b>	80,982
<i>Cash flow from changes in working capital:</i>			
Inventories		-5,368	8,990
Current receivables		-30,097	-4,793
Trade payables		-4,015	2,218
Current interest-free operating liabilities		22,653	-13,633
<b>Cash flow from operating activities</b>		<b>121,772</b>	73,764
<i>Investing activities:</i>			
Purchase of property, plant and equipment	13	-169	-895
Sale of property, plant and equipment		-	6
Purchase of financial assets	14	-14,000	-31,000
Sale of financial assets		5	90
Payment of loan to subsidiary	15	-14,335	-12,419
<b>Cash flow from investing activities</b>		<b>-28,499</b>	-44,218
<i>Financing activities:</i>			
Dividend		-120,897	-172,710
<b>Cash flow from financing activities</b>		<b>-120,897</b>	-172,710
<b>CASH FLOW FOR THE YEAR</b>		<b>-27,624</b>	-143,164
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>		<b>228,456</b>	371,448
Exchange difference in cash and cash equivalents		1,156	172
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>		<b>201,988</b>	228,456

## Balance sheets

SEK 000s	Note	31 Dec, 2014	31 Dec, 2013
<b>ASSETS</b>			
<b>Non-current assets</b>			
<i>Intangible assets</i>			
Capital development expenditure		–	–
<b>Total intangible assets</b>		–	–
<i>Property, plant and equipment</i>			
Production equipment		743	1,048
Office equipment and computers		617	1,010
<b>Total property, plant and equipment</b>		1,360	2,058
<i>Financial assets</i>			
Participations in group companies	14	69,129	52,394
Shares in other companies	14	4,000	–
Receivables from group companies	15, 28	41,013	29,513
<b>Total financial assets</b>		114,142	81,907
<b>Total non-current assets</b>		115,502	83,965
<b>Current assets</b>			
Inventories	16	15,072	9,704
<i>Current receivables</i>			
Trade receivables	17	74,166	59,437
Receivables from group companies	18	–	271
Other receivables	19	4,796	2,742
Deferred expenses and accrued income	20	17,037	4,360
<b>Total current receivables</b>		95,999	66,810
Short-term investments	21	13	80
Cash and cash equivalents		201,988	228,456
<b>Total current assets</b>		313,072	305,050
<b>TOTAL ASSETS</b>		428,574	389,015

## Balance sheets

SEK 000s	Note	31 Dec, 2014	31 Dec, 2013
<b>EQUITY AND LIABILITIES</b>			
<b>Equity</b>			
<i>Restricted equity</i>			
Share capital	22	17,271	17,271
Other restricted equity		1,253	1,253
		18,524	18,524
<i>Non-restricted equity</i>			
Retained profit		182 186	158,426
Profit for the year		149 590	144,657
		331 776	303,083
<b>Total equity</b>		350,300	321,607
<b>Liabilities</b>			
<i>Current liabilities</i>			
Other provisions	23	3,900	–
Prepayments from customers		6,804	508
Trade payables		9,527	13,542
Liabilities to group companies	18	21,487	10,734
Current tax liability		5,827	26,138
Other liabilities	24	7,240	3,946
Accrued expenses and deferred income	25	23,489	12,540
<b>Total current liabilities</b>		78,274	67,408
<b>Total liabilities</b>		78,274	67,408
<b>TOTAL EQUITY AND LIABILITIES</b>		428,574	389,015
<b>Pledged assets and contingent liabilities for the Parent Company</b>			
Floating charges	26	2,000	2,000
Contingent liabilities		None	None

## Statement of changes in equity

	Share capital	Other restricted equity	Retained profit incl. profit for the year	Total equity
<b>Opening balance, 1 Jan 2013</b>	17,271	1,253	331,136	349,660
Dividend			–172,710	–172,710
Profit for 2013			144,657	144,657
<b>Closing balance, 31 Dec 2013</b>	17,271	1,253	303,083	321,607
Dividend			–120,897	–120,197
Profit for 2014			149,590	149,590
<b>Closing balance, 31 Dec 2014</b>	17,271	1,253	331,776	350,300

# Notes to the financial statements and accounts

All figures in SEK 000s unless otherwise specified. Figures in brackets refer to the preceding year.

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## Note 1 Accounting policies

**Compliance with norms and laws** The consolidated financial statements have been prepared in compliance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) and interpretations from the International Financial Reporting Interpretations Committee (IFRIC) that have been approved by the European Commission for application in the EU.

The Parent Company applies the Swedish Financial Reporting Board's recommendation RFR 2, Accounting for Legal Entities, i.e. the same accounting policies as the Group except in cases where the Parent Company's compliance with the Swedish Companies Act limits the applicability of IFRS in the Parent Company.

### New and updated standards that are effective for financial periods starting on or after 1 January 2014

- **IFRS 10 Consolidated Financial Statements** IFRS 10 replaces IAS 27 Consolidated and Separate Financial Statements regarding the rules for consolidated financial statements (IAS 27) and SIC 12 regarding when a special purpose entity should be consolidated. IFRS 10 changes the definition of control and provides extensive new guidance on how it is to be applied. The new requirements have the potential to affect which of the Group's investments are to be regarded as subsidiaries and can therefore change the scope of consolidation. The requirements for treatment of consolidation, accounting for changes in non-controlling interests and accounting for loss of control of a subsidiary are the same as earlier. Management has re-evaluated its definition of control in accordance with IFRS 10 and has come to the conclusion that it will not change the classification (as subsidiary, etc.) for any of the Group's holdings during the current or comparison periods covered by these financial statements.
- **IFRS 11 Joint Arrangements** Management has determined that the standard will not affect the Group's financial statements.
- **IFRS 12 Disclosure of Interests in Other Entities** IFRS 12 integrates supplementary disclosures for different types of investments, including unconsolidated structured entities. The standard introduces new requirements for supplementary disclosures about the risks that a company is exposed to through its involvement in structured entities. Notes 14 and 18 illustrate the application of IFRS 12 during the current year.
- **Concurrent amendments to IAS 27 Separate Financial Statements (IAS 27) and IAS 28 Investments in Associates and Joint Ventures (IAS 28)** IAS 27 now contains only rules for separate financial statements. IAS 28 has been extended to include investments in joint ventures. IAS 28's equity method remains unchanged. Management has determined that the standard will not affect the Group's financial statements.
- **Amendments to IAS 32 Financial Instruments: Presentation** Management has determined that the standard will not affect the Group's financial statements.
- **Amendments to IAS 36 Impairment of Assets** These amendments require an entity to provide disclosures about the recoverable amount of an asset (or cash-generating unit) for which the entity has recognised or reversed an impairment loss during the reporting period.

They also require several new disclosures when the recoverable value of the impaired assets is based on fair value less costs of disposal, including:

- additional information about measurement at fair value including the applicable level in the fair value hierarchy
- description of the valuation techniques and key assumptions used
- the discount rate that has been used if fair value less costs of disposal is determined using a present value technique

The amendments have been applied retrospectively in accordance with their transitional provisions.



# nting policies

- *IFRIC 21 Levies (17 June 2014)* IFRIC 21 identifies the obligating event for the recognition of a liability as the activity that triggers the payment of the levy in accordance with the relevant legislation. If this event takes place on a certain date, the entire obligation must be recognised on that date in the reporting period.

The same recognition principles are applied in interim financial reports.

IFRIC 21 does not have any material impact on the financial statements but affects the distribution of costs for certain property taxes between the interim periods. The Group's earlier praxis was to spread the costs for the annual property tax evenly over the year, which resulted in the Group recognising a prepayment on the date of the interim report. The application of IFRIC 21 requires the Group to recognise all obligations as an expense at the beginning of the reporting period, which is the date specified in the relevant legislation.

IFRIC 21 has been applied retrospectively in accordance with its transitional provisions and has not had any impact on the Group's financial statements for the periods presented.

#### Standards, amendments and interpretations of existing standards that are not yet effective and are not subject to early adoption by the Group

- *IFRS 9 Financial Instruments* (this standard is applied for financial periods beginning on or after 1 January 2018)
- *IFRS 15 'Revenue from Contracts with Customers'* (this standard is applied for financial periods beginning on or after 1 January 2017)

The Group's Board of Directors and President have not yet evaluated the effects of IFRS 9 and IFRS 15 on these consolidated financial statements.

- *Amendments to Defined Benefit Plans: Employee Contributions (IAS 19 Amendments)*
- *Amendments to IFRS 11 Joint Arrangements.*

**Basis of presentation** The financial statements have been prepared in accordance with the cost method of accounting unless otherwise stated.

Non-current assets, non-current liabilities and provisions essentially consist of amounts that are expected to be recovered or settled more than 12 months after the closing date. Current assets and current liabilities essentially consist of amounts that are expected to be recovered or settled within 12 months from the closing date.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 28.

**Scope of consolidation** The consolidated financial statements include the operations of the Parent Company and the subsidiaries up to and including 31 December 2014. The Parent Company controls the subsidiaries, and has the ability to affect returns from its involvement with the subsidiaries through its power over the subsidiaries. All subsidiaries have their balance sheet date on 31 December.

All inter-company transactions and balances are eliminated on consolidation, including unrealised gains or losses arising from inter-company transactions. In cases where unrealised losses on inter-company sales of assets are reversed on consolidation, the underlying asset is tested for impairment also from a group perspective. When necessary, amounts reported in the financial statements of subsidiaries have been adjusted to ensure conformity with the accounting policies of the Group.

Profit/loss and other comprehensive income for subsidiaries that are acquired or sold during the year are recognised from the date on which the acquisition or sale went into force, according to what is applicable.

Non-controlling interests, who are recognised as component of equity,

represent the share of the subsidiary's profit or loss and net assets that is not held by the Group. The Group attributes comprehensive income for the subsidiaries to owners of the Parent Company and non-controlling interest based on their respective holdings. Transactions involving the acquisition and disposal of shares in companies where there are non-controlling interests are recognised in the cash flow statement in "Cash flow from financing operations" and the statement of changes in equity as transactions with owners.

#### Foreign currency translation

- *Functional currency* The functional currency is the currency of the primary economic environments in which the Group's companies operate.
- *Transactions* Foreign currency transactions are translated to the functional currency at the rate of exchange ruling on the transaction date. Monetary assets and liabilities in foreign currency are translated to the functional currency at the closing day rate. Exchange differences arising on translation are recognised in profit or loss. Non-monetary assets and liabilities carried at cost are translated at the rate of exchange ruling on the transaction date. Non-monetary assets and liabilities measured at fair value are translated to the functional currency using the rates of exchange ruling on the date when the fair value was determined. Foreign exchange gains/losses on operating receivables and liabilities are recognised in operating profit, while foreign exchange gains/losses on financial receivables and liabilities are recognised in net financial items.
- *Derivatives* Growth in sales has also led to increased currency risks, for which reason the company has taken currency hedges in EUR. The company's Board of Directors has issued a policy to hedge approximately 50-60% of projected cash flow 12 months forward and approximately 10-40% of projected cash flow 13-24 months forward in order to spread the risk for exchange rate fluctuations. The forward contracts are reported at fair value through profit or loss. A financial asset or liability is taken up in the balance sheet when the company becomes party to the contractual terms of the instrument.
- *Financial statements of foreign operations* Assets and liabilities in foreign operations are translated from the foreign operation's functional currency to the Group's presentation currency, SEK, at the closing day rate of exchange. Income and expenses in foreign operations are translated to SEK at an average rate that is a reasonable approximation of actual rates on the respective transaction dates. An average rate is calculated quarterly. Exchange differences arising on translation of foreign operations are recognised in other comprehensive income.
- *Net investments in foreign operations* Receivables from a foreign operation for which settlement is neither planned nor likely occur in the foreseeable future are, in substance, part of the company's net investment in that foreign operation. Exchange differences arising on translation of long-term loans in foreign currency that form part of the net investment in a foreign operation are deferred to a translation reserve in other comprehensive income.

**Segment reporting** Since the autumn of 2013 the company is divided into three business units, Paediatrics, Adult Health and New Business. Support functions have been retained at the central level, but the business units are responsible for product development and sales to their respective target groups.

The Executive Management has analysed the Group's internal reporting and determined that since the autumn of 2013, the Group's operations are monitored and evaluated based on the following segments:

- *Paediatrics business unit* (drops, digestive health tablets, oral rehydration solution (ORS) and cultures as an ingredient in a licensee's product (i.e. infant formula) and royalties from paediatric health products).
- *Adult Health business unit* (digestive health tablets, oral health tablets, cultures as an ingredient in a licensee's dairy products).
- *New Business business unit* (recognised in the item "other" since it accounts for less than 1% of net sales)
- *Other* (animal health products, etc.)

Sales and gross profit are reported for the above segments. Previously, operations were reported according to the segments below. To facilitate comparison, sales and gross profit have also been reported for these segments during 2014.

- **Finished consumer products:** Sales of digestive health tablets, drops, oral rehydration solution (ORS) and oral health products, etc.
- **Component products:** Sales of cultures as an ingredient in licensee products such as infant formula and dairy products, royalties for the use of *Lactobacillus reuteri* and sales of LifeTop Straw and LifeTop Cap
- **Other products:** Animal health, etc.

**Revenue recognition** BioGaia's revenue comes mainly from the sale of drops, digestive health tablets, oral rehydration solution (ORS) and oral health products to distributors, but also of revenue from the sale of bacteria cultures to be used in a licensee's products (for example infant formula and dairy products), royalty income for the use of *Lactobacillus reuteri* in a licensee's product and sales of packaging systems such as straws and caps.

Revenue from the sale of goods is recognised when the amount can be measured reliably, it is probable that the economic benefits will flow to the company and the criteria have been met for delivery in accordance with the agreed sale and shipping conditions.

Royalties are measured as a percentage of the licensee's reported sales value for consumer products containing BioGaia's probiotics, and are recognised monthly or quarterly. Minimum royalties are specified in the terms of the agreements. License revenue received in connection with the signing of agreements is accrued in cases where it intended to cover costs until the time of launch. In other cases, the revenue is recognised immediately. Royalties from the sale of licences (rights), such as the 2012 agreement with Nestlé which gives them the right to use the probiotic *Lactobacillus reuteri* Protectis in infant formula during the remaining term of the patent, are recognised as income directly in cases where there are no remaining conditions to be met and the right is transferred to the customer in connection with signing of the agreement. Royalty revenue attributable to development projects is recognised on a straight-line basis over the term of the agreement.

Interest income is recognised in the income statement for the period in which it arises.

**Leases** Leased assets are classified as operating leases, since all the risks and rewards incident to ownership have not been substantially transferred to BioGaia. As a result, the lease payments are recognised on a straight-line basis over the term of the lease.

**Pensions** All employees in Sweden are subject to mandatory retirement in accordance with Swedish law, currently at the age of 65 years. The company has no pension commitments other than payment of annual pension insurance premiums. The pension insurance premiums are of the defined contribution type and are expensed as incurred.

**Income taxes** Current tax refers to the tax computed on the year's taxable profit. Deferred tax refers to the tax calculated partly on the basis of temporary differences and partly on taxable deficits. At every closing date, an assessment is made to determine whether to recognise deferred tax assets not previously recognised in the balance sheet. Such tax assets are recognised to the extent that it is deemed likely that sufficient taxable profits will be available in the future.

**Research and development expenses** Costs related to research undertaken with the prospect of gaining new scientific or technical knowledge in the Group's operations are expensed as incurred.

Costs for development, where knowledge and understanding gained from research and practical experience are directed towards producing new products, processes or systems, are recognised as intangible assets in the balance sheet when they meet the criteria for capitalisation according to IAS 38, i.e. only when the technical and commercial feasibility of the product or process has been established, the Group has adequate resources to complete development and the Group intends and is able to complete the intangible asset and either use it or sell it. It should also be probable that the future economic benefits attributable to the asset will flow to the company and the cost of the asset can be reliably measured. The reported value includes all directly attributable costs, such as those for materials, purchased services and compensation to employees engaged in R&D activities. Other development

costs are expensed as incurred. Individual assessment is made of all ongoing research and development projects to determine which costs for the respective project are capitalisable and to look for any indications of impairment.

The company has a number of projects that meet the criteria for capitalisation and were thus recognised in the balance sheet in previous years. These had been amortised in full at 31 December 2012. Investments in capitalised development costs in 2014 amounted to SEK 6,1 million (0) and refer to development of a product for the NEC project in the subsidiary IBT AB. The project is expected to be completed within 3-5 years. Other development costs are not regarded as meeting the criteria for capitalisation and have therefore been expensed in full. Costs for development projects that are carried out in collaboration with Nestlé are recognised on a straight-line basis.

**Intangible assets and property, plant and equipment** Intangible assets and property, plant and equipment are recognised at cost less accumulated amortisation/depreciation and impairment.

The following amortisation schedules are applied:

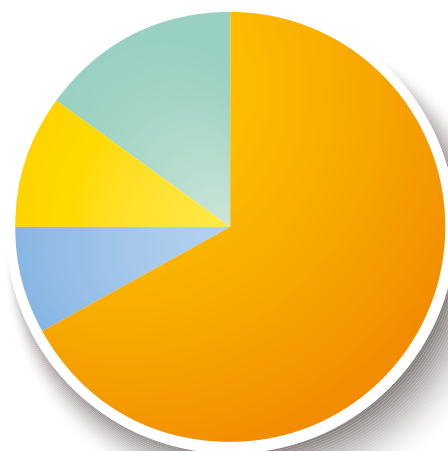
	Group	Parent Company
<b>Intangible assets</b>		
Capitalised development expenditure	5–10 yrs	5–10 yrs
Licenses	5 yrs	5 yrs
Trademarks	5 yrs	5 yrs
<b>Property, plant and equipment</b>		
Production equipment	5–10 yrs	5 yrs
Equipment and computers	3–5 yrs	3–5 yrs
Buildings	20-60 yrs	–

Amortisation of intangible assets is started when a project has been completed and the product begins generating revenue.

The amortisation period has varied between 5-10 years depending on the estimated useful life of the project. In the future, the amortisation period may be changed depending on the nature of the product.

The carrying amounts of the Group's assets are reviewed at each balance sheet date to look for any indication that an asset may be impaired. Incomplete projects are tested for impairment annually. The cash-generating unit is the applicable segment. If impairment is indicated, the recoverable

### Sales by geographical market 2014



- = Europe 67% (69%)
- = Rest of world 15% (11%)
- = USA and Canada 8% (7%)
- = Asia 10% (12%)

amount of the asset is calculated. If this is lower than the carrying amount, the value is written down to recoverable amount.

Depreciation of a building is started when construction is completed. The depreciation period is 20-30 years for electricity and internal construction work, etc., and 60 years for the framework and foundation.

**Inventories** Inventories are stated at the lower of cost and net realisable value, including provisions for obsolescence. Cost is measured according to weighted average prices.

**Cash and cash equivalents** Cash and cash equivalents comprise cash in hand and at bank.

**Financial assets and liabilities** Financial instruments in the Group are measured and recognised in accordance with the rules in IAS 39.

The financial assets recognised in balance sheet include cash and cash equivalents, short-term investments, and loans and receivables. Financial liabilities and equity include trade payables and prepayments from customers.

Financial assets and liabilities are initially measured at cost, corresponding to fair value including transaction costs for all financial assets and liabilities not measured at fair value through profit or loss. Subsequent measurement depends on how the instruments have been classified according to the following.

Financial assets refer to shares in a company in which the holding is below 20%. The Group has decided to invest further in the company, but since certain obligations and milestones must be met in order for additional investments to be made, the holding is recognised as a financial asset. When the holding exceeds 20%, the company will be recognised in shares in associates.

A financial asset or liability is recognised in the balance sheet when the company initially becomes party to the contractual provisions of the instrument. Financial liabilities are recognised when the counterparty has performed and there is contractual obligation to pay, even if no invoice has been received. Trade receivables are initially measured at cost and subsequently at amortised cost less provision for impairment. Impairment losses on trade receivables are recognised in profit or loss. Trade payables are recognised when an invoice has been received.

The purchase or sale of a financial asset is recognised on the trade date, which is the date on which the company commits to purchase or sell the asset.

A financial asset is derecognised from the balance sheet when the company's rights under the agreement are realised, expire or the company has relinquished control of the asset. The same applies to a part of a financial asset. A financial liability is derecognised from the balance sheet when the obligation specified in the agreement is discharged or otherwise extinguished. The same applies to a part of a financial liability.

The company classifies its financial assets and liabilities in the following categories; financial assets and liabilities at fair value through profit or loss, loans and receivables, held-to-maturity investments and other financial liabilities.

In accordance with IFRS 7 Financial Instruments, is it specified in connection with the note, regarding the balance sheet item for all financial instruments measured at fair value, which of the following levels of measurement has been used:

- **Level 1**, fair value is determined based on quoted prices in an active market for the instrument
- **Level 2**, fair value is determined based on a valuation technique using observable market data, either direct (such as prices) or indirect (derived from prices), and which are not included in level 1
- **Level 3**, fair value is determined with the help of valuation techniques, using significant inputs that are not based on observable in the market data.

**Accounting policies of the Parent Company** The differences between the accounting policies applied by the Group and the Parent Company are described below. The following accounting policies for the Parent Company have been applied consistently for all periods presented in the Parent Company financial statements.

- **Subsidiaries** In the Parent Company, shareholdings in subsidiaries are accounted for in accordance with the cost method of accounting.
- **Income taxes** In the Parent Company, untaxed reserves are recognised including the deferred tax liability. In the consolidated financial statements, however, untaxed reserves are divided between deferred tax liability and equity.

## Note 2 Segment reporting

As of 2014 the Group's operations are monitored and evaluated based on the business units Paediatrics, Adult Health, and New Business. The Paediatrics segment includes sales of drops, oral rehydration solution (ORS), digestive health tablets and cultures as an ingredient in a licensee's product (such as infant formula), as well as royalties pertaining to Paediatrics products. The Adult Health segment mainly includes sales of digestive health tablets, oral health products and cultures as an ingredient in a licensee's dairy product. Other consists of the New Business business unit and a few minor products, such as Animal Health products. Together these account for less than 1% of sales and are therefore not reported separately.

The management monitors net sales and gross profit. Other expenses are not broken down at the segment level, but only at the group level.

### INCOME BY SEGMENT - BUSINESS UNIT:

	Group		Parent Company	
	2014	2013	2014	2013
Paediatrics	313,716	238,586	313,716	238,586
License revenue (Paediatrics) <sup>1)</sup>	95,397	–	95,397	–
Adult Health	69,446	75,616	52,314	64,870
Other	3,243	1,673	2,779	1,168
	481,802	315,875	464,206	304,624

### GROSS PROFIT BY SEGMENT - BUSINESS UNIT:

	Group		Parent Company	
	2014	2013	2014	2013
Paediatrics	208,445	166,161	196,497	154,902
License revenue (Paediatrics) <sup>1)</sup>	95,397	–	95,397	–
Adult Health	44,229	47,023	30,001	40,003
Other	2,393	980	2,340	879
	350,464	214,164	324,235	195,784

<sup>1)</sup> The license revenue refers to revenue from Nestlé. The license revenue is included in paediatrics but is reported on a separate line in order to achieve better comparability between years.

Before 2014 the revenue reporting was based on products instead of business units. The segments were Finished consumer products and Component products.

To facilitate comparison, sales and gross profit for the earlier segments, Finished consumer products and Component products, are reported below.

### REVENUE BY SEGMENT:

	Group		Parent Company	
	2014	2013	2014	2013
Finished consumer products	303,603	256,164	286,471	245,418
Component products	80,724	58,592	80,260	58,087
License revenue (component products) <sup>1)</sup>	95,397	–	95,397	–
Other products	2,078	1,119	2,078	1,119
	481,802	315,875	464,206	304,624

## GROSS PROFIT BY SEGMENT:

	Group		Parent Company	
	2014	2013	2014	2013
Finished consumer products	207,512	180,088	181,336	161,809
Component products	45,477	33,384	45,424	33,283
License revenue (component products) <sup>1)</sup>	95,397	–	95,397	–
Other products	2,078	692	2,078	692
	<b>350,464</b>	214,164	<b>324,235</b>	195,784

<sup>1)</sup> The license revenue refers to revenue from Nestlé. The license revenue is included in component products but is reported on a separate line in order to achieve better comparability between years.

In 2014, SEK 137.3 million (106.7), or 35.5% (33.8%) of revenue, was related to three customers. The largest customer was related to the segment Paediatrics and the other two to both Paediatrics and Adult Health. Including license revenue from Nestlé, SEK 232.7 million or 48.3% of revenue was related to three customers. In 2014 one customer accounted for more than 10% of revenue. In 2013 two customers each accounted for 10% of revenue.

## NET SALES BY GEOGRAPHICAL MARKET:

	Group		Parent Company	
	2014	2013	2014	2013
Europe	257,808	218,301	257,808	218,301
License revenue (Europe) <sup>1)</sup>	95,397	–	95,397	–
USA and Canada	30,273	22,412	29,809	21,907
Asia	38,778	40,100	21,646	29,354
Rest of world	59,546	35,062	59,546	35,062
	<b>418,802</b>	315,875	<b>464,206</b>	304,624

<sup>1)</sup> The license revenue refers to revenue from Nestlé. The license revenue is included in Europe but is reported on a separate line in order to achieve better comparability between years.

More than 90% of the Group's total assets, amounting to SEK 415,608 thousand (383,419), are located in Europe.

Of the Group's capital expenditure on property, plant and equipment and intangible assets, totalling SEK 18,406 thousand (16,634), more than 90% pertained to Europe.

Sales in Sweden amounted to SEK 12.4 million (14.6), or 3.2% (4.6%) of total sales in the Group, excluding the license revenue.

The Group's non-current assets amount to SEK 82.8 million, of which SEK 82.5 million is located in Sweden and SEK 0.3 million in other countries (the USA and Japan).

## Note 3 Revenue

	Group		Parent Company	
	2014	2013	2014	2013
Product revenue	353,640	311,966	336,044	300,715
Royalties	32,765	3,909	32,765	3,909
License revenue	95,397	–	95,397	–
	<b>481,802</b>	315,875	<b>464,206</b>	304,624

## Note 4 Employees and personnel expenses, remuneration to senior executives

## AVERAGE NUMBER OF EMPLOYEES BY COUNTRY:

	2014	of whom, men	2013	of whom, men
<i>Parent Company:</i>				
Sweden	55	20	53	19
<i>Subsidiaries:</i>				
Sweden	27	16	21	14
Japan	6	5	6	5
USA	2	0	2	0
Total subsidiaries	35	21	29	19
<b>Total Group</b>	<b>90</b>	<b>41</b>	82	38

The number of employees in the Group at 31 December, 2014 was 95 (85).

## Salaries and other remuneration divided by country and between the Board/President and other employees:

	2014 Board and President	2013 Board and President	2014 Other employees	2014 Other employees
<i>Parent Company:</i>				
Sweden	3,601	3,364	32,175	30,978
<i>Subsidiaries:</i>				
Sweden	2,870	1,962	9,606	6,406
Japan	2,067	1,980	2,695	2,402
USA	–	–	1,550	1,048
Total subsidiaries	4,937	3,942	13,851	9,856
<b>Total Group</b>	<b>8,538</b>	7,306	<b>46,026</b>	40,834

## TOTAL SALARIES AND SOCIAL SECURITY EXPENSES:

	Group		Parent Company	
	2014	2013	2014	2013
Salaries and other remuneration	54,564	48,141	35,776	34,342
Pension expenses for the Board and President	1,843	1,501	1,162	1,155
Pension expenses for other employees	5,312	4,536	4,436	4,109
Other social security expenses	15,965	14,341	11,792	11,556
	<b>77,684</b>	68,519	<b>53,166</b>	51,162

**Pensions and health insurance:** All employees in Sweden are subject to mandatory retirement in accordance with Swedish law, currently at the age of 65 years. The company has no pension commitments other than payment of annual pension insurance premiums. For all employees over the age of 25 years, the following pension insurance premiums are paid in relation to salary:

Pensionable salary within the range:	0–7.5 base amounts	>7.5–30 base amounts	>30 base amounts
Premium	6%	25%	0%

All employees aside from the President (for the President, see below) are covered by health insurance, with benefits, in addition to compensation from the Swedish Social Insurance Agency. This health insurance is activated after 90 days of sick leave. Together with the employer's health insurance and

compensation from the Social Insurance Agency, the employee receives total benefits equal to approximately 65-87% of salary after a qualifying period of 3 months (depending on the level of salary).

The company also pays sick pay during the qualifying period (see above), i.e. from day 15 to day 90, when the health insurance is activated. Compensation from the Swedish Social Insurance Agency from day 15 corresponds to just under 80% of salary and is payable in a maximum amount corresponding to an annual salary of 7.5 price base amounts. During this period, the company pays compensation for loss of income so that the employee, regardless of salary level, receives a total of 80% of salary together with compensation from the Swedish Social Insurance Agency.

**Remuneration to senior executives:** Remuneration to the Chairman and members of the Board is paid according to the decision of the Annual General Meeting. The Board has appointed a remuneration committee consisting of Board Chairman David Dangoor and Board member Stefan Elving. The remuneration committee handles matters related to remuneration and other terms of employment of senior executives. The principles for remuneration to senior executives are approved by the Annual General Meeting. The task of the remuneration committee is to prepare recommendations in accordance with these principles.

Board member Jan Annwall was Vice President until 1 April 2010 and has thereafter worked for BioGaia to a limited extent in the capacity of consultant.

Remuneration to the President and other senior executives employed by the company consists of basic salary and other benefits. Other senior executives consist of the 11 persons who together with the President make up the Executive Management.

In the event of termination by the company, the President is entitled to full salary during an 18-month period of notice. For Vice Presidents, the corresponding period is 6 months. Other senior executives have a statutory notice period of at least 3 months in the event of termination by the company. For the President the company made an extra pension provision of SEK 750 thousand during 2013 and 2014. For 2014 the cost has been accounted for but not paid. For the President the company pays the cost of health insurance that provides sickness benefits equal to 75% of salary after a qualifying period of 3 months. In other respects, the President has the same benefits as other employees. Otherwise, no agreements for termination benefits exist for the President or other senior executives.

#### REMUNERATION AND OTHER BENEFITS DURING THE YEAR:

	Director's fees	Basic salary	Pension insurance including health insurance	Other remuneration*)	Total
<b>Board Chairman:</b>					
David Dangoor:	300				300
<b>Board members:</b>					
Jan Annwall	150			225	375
Stefan Elving	150				150
Inger Holmström	150				150
Jan Litborn	150				150
Brit Stakston	150				150
Jörgen Thorball	150				150
Paula Zeilon	150				150
<b>President:</b>					
Peter Rothschild		2,251	1,162		3,413
<b>Other senior executives (11 persons):</b>					
		9,061	1,865	10,532	21,458
	<b>1,350</b>	<b>11,312</b>	<b>3,027</b>	<b>10,757</b>	<b>26,446</b>

\*) Bo Möllstam is Technical Director and a member of BioGaia's Executive Management. He is not employed by the company but is contracted as a consultant and invoices his fees through a company. Bo Möllstam is a partner in Synergon AB, which invoiced an amount of SEK 9.7 million to BioGaia AB during the year. Of this total, SEK 5.5 million refers to forwarded patent expenses and the remainder consists of consulting fees.

Helen Olsson is HR Director and a member of the Executive Management. She is not employed by the company but is contracted as a consultant and invoices her fees through a company. Helen Olsson is a partner in Spirean AB, which invoiced an amount of SEK 0.8 million to BioGaia AB during the year.

**BioGaia's incentive scheme for the employees:** BioGaia's incentive scheme In June 2012 BioGaia carried out the warrant programme that was decided by the Annual General Meeting on 8 May 2012. A total of 87,000 warrants were subscribed for, of which the management subscribed for 41,000. The warrants were issued at a market price of SEK 14.27 each following valuation according to the Black & Scholes formula, which provided the Parent Company with proceeds of SEK 1.3 million. Each warrant entitles the holder to subscribe for one class B share for SEK 241.90 on 1 June 2015. Volatility was estimated at 40%.

If all of the subscription warrants are exercised, the company's equity will be increased by SEK 21.0 million. This represents a dilutive effect of approximately 0.5% on the share capital and 0.4% on the total number of votes upon the full exercise of warrants.

In order to achieve a high level of participation, the AGM decided to pay a subsidy of SEK 10 per warrant (after 1 June 2015) to the employees who have subscribed for subscription warrants but have not exercised the right to buy shares. A provision of SEK 1.1 Million for this obligation has been made since at the current share price there is a risk that the subsidy must be paid.

#### GENDER DISTRIBUTION:

	2014 Women	2013 Women	2014 Men	2013 Men
Board members	3	2	5	5
Management including President	7	5	5	4

#### Note 5 Audit fees

	Group		Parent Company	
	2014	2013	2014	2013
<b>Grant Thornton Sweden AB:</b>				
Audit assignments	484	473	325	325
Audit services in addition to audit	137	181	120	120
Audit advice	125	104	101	59
Tax advice	16	101	9	93
Other assignments	-	4	-	-
<b>Cherry, Bekaert &amp; Holland, L.L.P.:</b>				
Audit assignments	48	59	-	-
Other assignments	144	124	-	-
<b>Grant Thornton Taiyo LLC:</b>				
Audit assignments	20	20	-	-
Other assignments	-	-	-	-

Audit assignments refer to the auditors' work on the statutory audit, other auditing activities and different types of quality assurance services. Other services are such that are not included in the audit assignment, auditing activities or tax advice.

#### Note 6 Other operating income

	Group		Parent Company	
	2014	2013	2014	2013
Exchange gains on operating receivables and liabilities, net	7,711	1,796	7,851	1,796
	<b>7,711</b>	1,796	<b>7,851</b>	1,796

## Note 7 Operating expenses allocated by type of cost

	Group		Parent Company	
	2014	2013	2014	2013
Cost of goods sold	131,338	101,711	139,971	108,840
Personnel expenses	78,773	68,961	54,016	51,515
Depreciation/amortisation	5,652	5,541	867	1,157
Other operating expenses	76,908	59,804	75,259	60,753
	<b>292,631</b>	236,017	<b>270,113</b>	222,265

Operating expenses include lease payments of SEK 167 thousand (192). Total minimum future lease payments fall due as follows:

- Within one year: 48
- Within two to five years: 145

The Group's future payment commitments for rents amount to SEK 8.2 million, of which SEK 6.7 million refers to the Parent Company. The Group's rents fall due for payment in an amount of SEK 4.3 million within one year and SEK 1.3 million within two to five years.

## Note 8 Financial income

	Group		Parent Company	
	2014	2013	2014	2013
Interest income	2,382	5,081	3,096	7,280
	<b>2,382</b>	5,081	<b>3,096</b>	7,280

## Note 9 Financial expenses

	Group		Parent Company	
	2014	2013	2014	2013
Exchange loss on forward exchange contracts	6,592	2,882	6,592	2,882
Other financial expenses	148	93	116	83
	<b>6,740</b>	2,975	<b>6,708</b>	2,965

The Parent Company and the Group have entered into forward exchange contracts in EUR for a total of EUR 13.3 million (13.7) at an average exchange rate of SEK 9.07 of which EUR 8.7 million will mature in 2014 and EUR 4.6 million in 2016. The unrealised foreign exchange loss is reported as a financial income/expense.

## Note 10 Tax on profit for the year

	Group		Parent Company	
	2014	2013	2014	2013
Current tax	-44,643	-44,195	-43,035	-41,605
Deferred tax	107	24,623	-	-
	<b>-44,536</b>	-19,572	<b>-43,035</b>	-41,605

## DEFERRED TAX EXPENSE/TAX INCOME:

	Group	
	2014	2013
Deferred tax income attributable to loss carryforwards capitalised during the year	192	85
	<b>192</b>	85

## DEFERRED TAX LIABILITIES:

	2014	2013
	Opening balance deferred tax liabilities	85
Reversal of deferred tax	-	-
Provision for deferred tax	107	-
<b>Closing balance deferred tax liabilities</b>	<b>192</b>	85

## RECONCILIATION OF NOMINAL TAX AND ACTUAL TAX EXPENSES:

	Group		Parent Company	
	2014	2013	2014	2013
Reported profit before tax	192,525	83,760	192,625	186,261
Domestic tax	22.0%	22.0%	22.0%	22.0%
Nominal tax rate	-42,355	-18,427	-42,378	-40,977
Tax effect of non-capitalised loss carryforwards	3,167	-2,381	-	-
Tax effect of other non-deductible and non-taxable items	-5,554	783	-859	-1,079
Other tax adjustment	206	453	202	451
<b>Actual tax</b>	<b>-44,536</b>	-19,572	<b>-43,035</b>	-41,605

The Group's loss carryforwards amounted to a total of SEK 35.2 million (50.0) at 31 December 2013. Loss carryforwards of SEK 0 thousand (0) are attributable to the Swedish companies. No deferred tax has been recognised on loss carryforwards amounting to SEK 35.2 million (50.0). These carryforwards are attributable to the Japanese subsidiary and will expire as follows: SEK 0.4 million will expire in the financial year 2017, SEK 8.3 million in 2018, SEK 10.2 million in 2019, SEK 3.8 million in 2020, SEK 4.6 million in 2021, SEK 7.9 million in 2022.

The company has an ongoing tax matter related to a write-down of receivables from the Japanese subsidiary. In the event of a negative outcome, this could result in additional tax expenses of SEK 3.1 million. If the outcome is positive, there is opportunity to receive an additional tax income of SEK 3.8 million for previous years.

## Note 11 Non-controlling interests

	2014	2013
At beginning of year	-484	3,492
Acquisition of 50% of TwoPac	-	-6,447
Sale of 9% of IBT	-	5
Profit for the year attributable to non-controlling interests	583	2,466
<b>At end of year</b>	<b>99</b>	-484

The non-controlling interests refer to a 9.9% stake in the subsidiary CapAble AB that is held by its Managing Director Staffan Pålsson and a 9.9% stake in the subsidiary IBT that is held by the company's Managing Director Staffan Strömberg (4.5), its Research Director Eamonn Connolly (4.5%) and board member Anders Ekblom (0.9%).

## Note 12 Intangible assets

### GROUP:

	Capitalised development expenditure	Licenses and brands	Total intangible assets
<i>Accumulated cost:</i>			
Opening balance, 1 Jan 2013	26,875	2,528	29,403
Purchases	–	–	–
<b>Closing balance, 31 Dec 2013</b>	<b>26,875</b>	<b>2,528</b>	<b>29,403</b>

Opening balance, 1 January 2014	26,875	2,528	29,403
Purchases	6,075	–	6,075
<b>Closing balance, 31 Dec 2014</b>	<b>32,950</b>	<b>2,528</b>	<b>35,478</b>

### *Accumulated amortisation:*

Opening balance, 1 Jan 2013	26,875	2,528	29,403
The year's amortisation	–	–	–
<b>Closing balance, 31 Dec 2013</b>	<b>26,875</b>	<b>2,528</b>	<b>29,403</b>

Opening balance, 1 Jan 2014	26,875	2,528	29,403
The year's amortisation	–	–	–
<b>Closing balance, 31 Dec 2014</b>	<b>26,875</b>	<b>2,528</b>	<b>29,403</b>

### *Carrying amounts:*

At 1 Jan 2013	–	–	–
At 31 Dec 2013	–	–	–
<b>At 31 Dec 2014</b>	<b>6,075</b>	<b>–</b>	<b>6,075</b>

### PARENT COMPANY:

	Capitalised development expenditure	Licenses and brands	Total intangible assets
<i>Accumulated cost:</i>			
Opening balance, 1 Jan 2013	26,875	2,528	29,403
Purchases	–	–	–
<b>Closing balance, 31 Dec 2013</b>	<b>26,875</b>	<b>2,528</b>	<b>29,403</b>

Opening balance, 1 Jan 2014	26,875	2,528	29,403
Purchases	–	–	–
<b>Closing balance, 31 Dec 2014</b>	<b>26,875</b>	<b>2,528</b>	<b>29,403</b>

### *Accumulated amortisation:*

Opening balance, 1 Jan 2013	26,875	2,528	29,403
The year's amortisation	–	–	–
<b>Closing balance, 31 Dec 2013</b>	<b>26,875</b>	<b>2,528</b>	<b>29,403</b>

Opening balance, 1 Jan 2014	26,875	2,528	29,403
The year's amortisation	–	–	–
<b>Closing balance, 31 Dec 2014</b>	<b>26,875</b>	<b>2,528</b>	<b>29,403</b>

### *Carrying amounts:*

At 1 Jan 2013	–	–	–
At 31 Dec 2013	–	–	–
<b>At 31 Dec 2014</b>	<b>–</b>	<b>–</b>	<b>–</b>

Capitalised expenses include internally generated and externally acquired assets. No amortisation on intangible assets has been made during the year. Investments in capitalised development expenditures are related to development of a product for the NEC project in the subsidiary IBT AB:

### TOTAL RESEARCH AND DEVELOPMENT EXPENDITURE:

	Group		Parent Company	
	2014	2013	2014	2013
Total R&D expenditure	<b>52,842</b>	40,260	<b>46,108</b>	40,169
The year's capitalisation of development expenses	<b>6,075</b>	–	–	–
Uncapitalised R&D expenditure	<b>53,593</b>	40,260	<b>46,108</b>	40,169
Amortisation/depreciation recognised in R&D expenses*)	<b>274</b>	294	<b>238</b>	292
<b>R&amp;D expenses with an effect on income</b>	<b>53,867</b>	40,554	<b>46,346</b>	40,461

\*) This amount relates only to that portion of depreciation on property, plant and equipment to the function Research and Development according to the income statement classified by function. No amortisation on capitalised development expenditures has been recognised during the year.

## Note 13 Property, plant and equipment

### GROUP:

	Land and buildings	Production equipment	Work in progress	Office equipment and computers	Total property, plant and equipment
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### *Accumulated cost:*

Opening balance, 1 Jan 2013	34,986	19,805	4,144	14,172	73,107
Purchases	4,842	3,515	7,314	1,014	16,685
Sales and disposals	–	–	–	–63	–63
Translation difference	–	–	–	–149	–149
<b>Closing balance, 31 Dec 2013</b>	<b>39,828</b>	<b>23,320</b>	<b>11,458</b>	<b>14,974</b>	<b>89,580</b>

Opening balance, 1 January 2014	39,828	23,320	11,458	14,974	89,580
Purchases	10,070	1,708	5,750	883	18,411
Sales and disposals	–	–1,006	–	–12	–1,018
Reclassifications	–	2,428	–2,428	–	–
Translation difference	–	–	–	210	210
<b>Closing balance, 31 Dec 2014</b>	<b>49,898</b>	<b>26,450</b>	<b>14,780</b>	<b>16,055</b>	<b>107,183</b>

	Land and buildings	Production equipment	Work in progress	Office equipment and computers	Total property, plant and equipment
<i>Accumulated depreciation:</i>					
Opening balance, 1 Jan 2013	165	11,789	–	11,959	23,913
Depreciation	1,078	3,090	–	1,403	5,571
Sales and disposals	–	–	–	–58	–58
Translation difference	–	–	–	–132	–132
<b>Closing balance, 31 Dec 2013</b>	<b>1,243</b>	<b>14,879</b>	<b>–</b>	<b>13,172</b>	<b>29,294</b>
Opening balance, 1 January 2014	1,243	14,879	–	13,172	29,294
Depreciation	1,285	3,139	–	1,233	5,657
Write downs	–	307	–	–	307
Sales and disposals	–	–1,006	–	–12	–1,018
Translation difference	–	–	–	191	191
<b>Closing balance, 31 Dec 2014</b>	<b>2,528</b>	<b>17,319</b>	<b>–</b>	<b>14,584</b>	<b>34,431</b>

*Carrying amounts*

At 1 Jan 2013	34,821	8,016	4,144	2,213	49,194
At 31 Dec 2013	38,585	8,441	11,458	1,802	60,286
<b>At 31 Dec 2014</b>	<b>47,370</b>	<b>9,131</b>	<b>14,780</b>	<b>1,471</b>	<b>72,752</b>

**PARENT COMPANY:**

	Production equipment	Office equipment and computers	Total tangibles property, plant and equipment
<i>Accumulated cost:</i>			
Opening balance, 1 Jan 2013	3,019	10,910	13,929
Purchases	540	407	947
Sales and disposals	–	–63	–63
<b>Closing balance, 31 Dec 2013</b>	<b>3,559</b>	<b>11,254</b>	<b>14,813</b>
Opening balance, 1 Jan 2014	3,559	11,254	14,813
Purchases	–	169	169
Sales and disposals	–	–12	–12
<b>Closing balance, 31 Dec 2014</b>	<b>3,559</b>	<b>11,411</b>	<b>14,970</b>

*Accumulated depreciation:*

Opening balance, 1 Jan 2013	2,261	9,393	11,654
Depreciation	249	908	1,157
Sales and disposals	–	–56	–56
<b>Closing balance, 31 Dec 2013</b>	<b>2,510</b>	<b>10,245</b>	<b>12,755</b>
Opening balance, 1 Jan 2014	2,510	10,245	12,755
Depreciation	306	562	868
Sales and disposals	–	–12	–12
<b>Closing balance, 31 Dec 2014</b>	<b>2,816</b>	<b>10,795</b>	<b>13,611</b>

*Carrying amounts*

At 1 Jan 2013	758	1,517	2,275
At 31 Dec 2013	1,049	1,009	2,058
<b>At 31 Dec 2014</b>	<b>743</b>	<b>616</b>	<b>1,359</b>

Depreciation is recognised on the following lines in the income statement:

	Group		Parent Company	
	2014	2013	2014	2013
Cost of goods sold	3,294	3,006	–	–
Selling expenses	1,565	1,869	498	696
Administrative expenses	519	372	131	169
Research and development expenses	274	294	238	292
	<b>5,652</b>	5,541	<b>868</b>	1,157

**Note 14 Financial assets****PARENT COMPANY**

Participations in group companies	2014	2013
At beginning of year	52,394	21,160
Group contribution to CapAble AB	2,874	2,590
Group contribution to TriPac AB	5	9
Group contribution to IBT AB	6,730	229
Impairment loss on shares in CapAble AB	–2,874	–2,590
Acquisition of shares in TwoPac AB (50%)	–	30,000
Conditional shareholder contribution to IBT AB	10,000	1,000
Sale of shares in IBT AB	–	–4
<b>Book value at end of year</b>	<b>69,129</b>	52,394

**SPECIFICATION OF THE PARENT COMPANY'S EQUITY HOLDINGS IN GROUP COMPANIES:**

Subsidiary/corp. reg.no./ Domicile	No. of shares	Holding, %	Book value
BioGaia Biologics Inc. /-/Raleigh, NC, USA	100,000	100	0
TriPac AB /556153-2200/Stockholm	10,000	100	3,582
CapAble AB /556768-3601/Stockholm	9,010	90.1	6,901
BioGaia Japan Inc. /-/Hiroshima, Japan	180	100	0
TwoPac AB /556591-9767/Eslöv	10,000	100	40,641
Infant Bacterial Therapeutics AB (IBT) /556873-8586/Stockholm	45,500	90.1	18,005
			<b>69,129</b>

The assets and liabilities of the American subsidiary BioGaia Biologics Inc. have been translated at the closing day rate of exchange, SEK 7.80 (6.48). All items in the income statement have been translated at the average exchange rate during the year, SEK 6.86 (6.51). The assets and liabilities of the Japanese subsidiary BioGaia Japan Inc. have been translated at an exchange rate of SEK 0.065 (0.062). All items in the income statement have been translated at an exchange rate of SEK 0.065 (0.066). The resulting translation differences have been recognised in consolidated comprehensive income.

CapAble AB was formed in the autumn of 2008. BioGaia owns 90.1% of the company. CapAble's President, Staffan Pålsson, owns 9.9% of the



company. The non-controlling interests' share in equity of CapAble amounts to SEK 97 thousand.

TwoPac was formed in 2002 and is 100% owned by BioGaia AB since 1 July 2013, following the acquisition of the remaining 50% that was previously owned by TwoPac's management. The purchase consideration for the acquisition amounted to SEK 30 million and has affected cash flow in the Group and the Parent Company. See also Note 19.

Infant Bacterial Therapeutics (IBT) AB (formerly Infant Baby AB) was formed in 2011 and changed name to Infant Bacterial Therapeutics AB in 2013. BioGaia owns 90.1% of the company. IBT's President, Staffan Strömberg, IBT's Research Director, Eamonn Connolly and the board member Anders Ekblom together own 9.9% of the company. The non-controlling interests' share of equity in IBT amounts to SEK 3 thousand.

Of total purchases made by the Parent Company, 17.8% (18.0) was attributable to group companies. Of total sales made by the Parent Company, 0% (1.5) was attributable to group companies.

#### SHARES IN OTHER COMPANIES:

	Group		Parent Company	
	2014	2013	2014	2013
Purchase in MetaboGen AB	4,000	–	4,000	–
Carrying amount at end of year	4,000	–	4,000	–

### Note 15 Non-current receivables from subsidiaries and associated company

#### NON-CURRENT RECEIVABLES FROM SUBSIDIARIES:

	Parent Company	
	2014	2013
At beginning of year	29,513	24,513
Payment of loan to BioGaia Japan Inc.	2,835	7,419
Payment of loan to TwoPac AB	11,500	5,000
Net accounting of liability to Biogaia Japan Inc.	–	–4,434
Exchange rate difference related to loan to Biogaia Japan Inc.	–6,075	–
Sale of products to BioGaia Japan Inc.	–	4,410
Interest income from BioGaia Japan Inc.	–	1,565
Provisions for receivables <sup>1)</sup>	3,240	–8,960
	41,013	29,513

<sup>1)</sup> Because it is uncertain whether the receivable from the subsidiary in Japan will be repaid within the foreseeable future, a provision has been made for this amount.

#### NON-CURRENT RECEIVABLES FROM SUBSIDIARIES AT DECEMBER 31:

	Parent Company	
	2014	2013
CapAble AB	1,022	1,022
TwoPac AB	39,991	28,491
Closing balance at end of year	41,013	29,513

### Note 16 Inventories

	Group		Parent Company	
	2014	2013	2014	2013
Raw materials and consumables	4,310	2,251	–	–
Finished goods and goods for resale	16,838	12,334	15,072	9,704
	21,148	14,585	15,072	9,704

The Group's provisions for obsolescence amount to SEK 1,698 thousand (1,483) at 31 December 2014. Expenses related to write-downs of inventory and scrapping amount to SEK 3,624 thousand (2,424). In 2014 BioGaia had additional costs arising from stability problem in bacteria cultures of SEK 11.0 million which are included in the "Cost of goods sold".

### Note 17 Trade receivables

The Group has recorded a loss of SEK 268 thousand (0) on the write-down of trade receivables in 2014.

Provisions for bad debt losses amounted to SEK 487 thousand (399) at 31 December 2014.

At 31 December 2014, trade receivables of SEK 17,816 thousand (7,714) were overdue without any assessed grounds for impairment.

Of the overdue receivables, SEK 15,641 thousand had been recovered as of the closing date.

#### AN AGE ANALYSIS OF OVERDUE TRADE RECEIVABLES IS SHOWN BELOW:

	Group		Parent Company	
	2014	2013	2014	2013
Less than 3 months	17,356	7,714	17,356	7,714
3-6 months	460	–	460	–
	17,816	7,714	17,816	7,714

#### THE REPORTED AMOUNTS FOR THE GROUP'S TRADE RECEIVABLES BY CURRENCY ARE:

	Group		Parent Company	
	2014	2013	2014	2013
SEK	17,327	11,107	17,327	11,108
EUR	36,345	36,664	36,345	36,664
USD	18,692	7,825	18,509	7,384
CHF	–	4,180	–	4,180
GBP	–	101	–	101
NOK	76	–	76	–
DKK	1,909	–	1,909	–
JPY	1,562	5,188	–	–
	75,911	65,065	74,166	59,437

## Note 18 Related party transactions

**Group** Annwall & Rothschild Investment AB holds 740,668 class A shares and 759,332 class B shares, corresponding to 8.7% of the share capital and 34.1% of the votes. Annwall & Rothschild Investment AB is owned by Peter Rothschild, President of BioGaia AB, and Jan Annwall, a member of the Board of the Parent Company. The transaction that took place during 2014 is a dividend of SEK 7.00 per share.

Bo Möllstam is Technical Director and a member of BioGaia's Executive Management. He is not employed by the company but is contracted as a consultant and invoices his fees through a company. Bo Möllstam is a partner in Synergon AB, which invoiced an amount of SEK 9.7 million to BioGaia AB during the year. Of this total, SEK 5.5 million refers to forwarded patent expenses and the remainder consists of consulting fees.

Helen Olsson is HR Director and a member of the Executive Management. She is not employed by the company but is contracted as a consultant and invoices her fees through a company. Helen Olsson is a partner in Spirean AB, which invoiced an amount of SEK 0.8 million to BioGaia AB during the year.

**Parent Company** The Parent Company owns 100% of TwoPac AB, since 1 July 2013. BioGaia has previously owned 50% of TwoPac AB and the remaining shares have been held by TwoPac's management. BioGaia acquired the remaining 50% of TwoPac AB on 1 July 2013 for SEK 30 million. A controlling influence was acquired already on 1 January 2011, although no shares were purchased at the time since the assessment was that BioGaia had a controlling influence as of that date. As a result, only cash and cash equivalents and total equity were affected by the acquisition of the remaining 50% as of 1 July 2013. The Parent Company owns 100% of the shares in BioGaia Biologics Inc, USA, BioGaia Japan Inc. and Tripac AB. The Parent Company owns 90.1% of the shares in CapAble AB. The Parent Company owns 90.1% of the shares in Infant Bacterial Therapeutics (IBT) AB.

### THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH TWOPAC AB:

	Parent Company	
	2014	2013
Interest income	696	610
Loan paid	-11,500	-5,000
Purchase of goods	-44,689	-37,487

Goods are purchased at cost plus profit margin.

### THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH BIOGAIA JAPAN INC.:

	Parent Company	
	2014	2013
Interest income	-	1,565
Loan paid <sup>1)</sup>	-2,835	-7,419
Sale of goods <sup>2)</sup>	-	4,410

<sup>1)</sup> Due to uncertainty as to whether the receivable from BioGaia Japan will be recovered within the foreseeable future, a provision has been made for this amount.

<sup>2)</sup> BioGaia has delivered products during 2014 but not invoiced this amount as it refers to a marketing contribution during the start-up phase.

### THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH BIOGAIA BIOLOGICS INC.:

	Parent Company	
	2014	2013
Purchase of services	-3,259	-2,371

### THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH CAPABLE AB:

	Parent Company	
	2014	2013
Interest income	25	30
Sales of services	163	117
Group contribution paid	-2,874	-2,590

### THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH TRIPAC AB:

	Parent Company	
	2014	2013
Group contribution paid	-5	-9

### THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH IBT AB:

	Parent Company	
	2014	2013
Group contribution paid	-6,730	-229
Conditional shareholder contribution	-10,000	-1,000
Purchase of services	-480	-

### THE CLOSING BALANCE WAS AS FOLLOWS:

	Parent Company	
	31 Dec 2014	31 Dec 2014
<b>Non-current receivables, related parties</b>		
Non-current receivables, TwoPac AB	39,991	28,491
Non-current receivables, CapAble AB	1,022	1,022
	41,013	29,513
<b>Current liabilities, related parties</b>		
Current liabilities, BioGaia Biologics Inc.	-930	-643
Current liabilities, CapAble AB	-4,793	-5,206
Current liabilities, Tripac AB	-4,662	-4,657
Current liabilities, IBT AB	-6,956	-229
Current liabilities, TwoPac AB	-4,146	-
	-21,487	-10,735
<b>Current receivables, related parties</b>		
Current receivables, TwoPac AB	-	271
	-	271

For further information, see also Note 4, Employees and personnel expenses.

## Note 19 Other receivables

	Group		Parent Company	
	2014	2013	2014	2013
VAT refund	4,322	2,945	4,030	2,122
Tax asset	490	281	320	236
Other receivables	1,912	863	446	384
	6,724	4,089	4,796	2,742

## Note 20 Deferred expenses and accrued income

	Group		Parent Company	
	2014	2013	2014	2013
Accrued income	15,955	2,895	15,955	2,624
Prepaid rents	1,117	1,079	879	841
Other deferred expenses	1,225	1,051	203	895
	18,297	5,025	17,037	4,360

## Note 21 Financial assets and liabilities

The Group classifies its financial assets and liabilities in the following categories; financial assets at fair value through profit or loss, held-to-maturity investments, loans and receivables and other financial liabilities.

### Financial assets measured at fair value through profit or loss

The Group's assets at fair value through profit or loss consist of cash and cash equivalents and short-term investments. The financial assets are recognised in the balance sheet and are valued at the closing day rate of exchange.

	Fair value		Carrying amount	
	2014	2013	2014	2013
Cash and cash equivalents in SEK	194,618	219,888	194,618	219,888
Cash and cash equivalents in EUR	927	6,706	927	6,706
Cash and cash equivalents in USD	13,083	5,985	13,083	5,985
Cash and cash equivalents in JPY	1,985	556	1,985	556
Cash and cash equivalents in DKK	53	1,136	53	1,136
Short-term investments	13	9	13	80
Total assets	210,680	234,280	210,680	234,351

Short-term investments refer to listed securities. The shares are recognised at historical cost less accumulated impairment. The intention is to sell the shares when an appropriate occasion arises. Fair value corresponds to the quoted market price on the balance sheet date.

The company has taken forward currency hedges in EUR. The forward currency hedges have been recognised at their fair value at 31 December 2014. This value is included in other liabilities – see Note 24.

**Held-to-maturity investments** The Group has no held-to-maturity investments.

**Loans and receivables** The Group's trade receivables amount to SEK 75,911 thousand (65,065). Fair value corresponds to the carrying amount.

**Other financial liabilities** The Group's other financial liabilities consist of trade payables and prepayments from customers. Financial liabilities are valued at the closing day rate of exchange.

	Fair value		Carrying amount	
	31 Dec 2014	31 Dec 2013	31 Dec 2014	31 Dec 2013
Trade payables	16,952	17,808	16,952	17,808
Prepayments from customers	6,804	508	6,804	508
Total other financial liabilities	23,757	18,316	23,757	18,316

## Note 22 Equity

The objective of the Group's capital management is to safeguard the Group's ability to continue as a going concern and to provide a good return to the shareholders.

The share capital in BioGaia AB consists of 740,668 class A shares, carrying 10 votes each, and 16,530,294 class B shares, carrying one vote each. The class A and B shares grant equal entitlement to the company's assets and profits. Both the A shares and B shares have a quota value of SEK 1 each. All shares are fully paid-up and no shares are reserved for transfer. No shares are held in treasury by the company itself or by its subsidiaries.

Other contributed capital consists of payments made by the shareholders in excess of the quota value.

The translation reserve arises in translation of the net assets of foreign operations according to the acquisition method.

Retained profit consists of other equity. The Parent Company's dividend for 2013 as decided by the 2014 AGM was SEK 120.9 million, equal to SEK 7.00 per share. For 2014 the Board and President propose that the company pay an ordinary dividend of SEK 3.46 per share and an extraordinary dividend of SEK 1.54 per share, amounting to a total dividend of SEK 5.00 per share. This is equal to total dividends of SEK 86.4 million.

Non-controlling interests account for 9.9% of equity in the subsidiary CapAble and 9.9% of equity in the subsidiary Infant Bacterial Therapeutics (IBT) AB.

Equity in the BioGaia Group consists of the sum of equity attributable to owners of the Parent Company and equity attributable to non-controlling interests. At 31 December 2014, total consolidated equity amounted to SEK 344.6 million (316.9) and equity attributable to owners of the Parent Company amounted to SEK 344.5 million (317.3).

**BioGaia's dividend policy** is to pay a shareholder dividend equal to 40% of profit after tax.

### KEY RATIOS

	2014	2013
Number of shares at 31 Dec., thousands	17,271	17,271
Average number of shares, thousands	17,271	17,271
Number of outstanding warrants, thousands	87	87
Number of outstanding warrants with a dilutive effect, thousands	–	87
Number of outstanding shares including outstanding warrants with a dilutive effect, thousands	17,271	17,358
Earnings per share, SEK	8.53	3.57
Earnings per share after dilution, SEK	8.53	3.56
Equity per share, SEK	19.95	18.37
Equity per share after dilution, SEK	19.95	18.28
Return on equity, %	45	16
Share price on closing day, SEK	179.50	253.50
Dividend per share, SEK	5.00 <sup>1)</sup>	7.00

<sup>1)</sup> Dividend proposed but not yet approved. The Board and President propose that the company pay an ordinary dividend of SEK 3.46 per share and an extraordinary dividend of SEK 1.54 per share, equal to a total dividend of SEK 5.00 per share.

## Note 23 Other provisions

	Group		Parent Company	
	2014	2013	2014	2013
Carrying amount as of January 1	–	–	–	–
The years provision	3,900	–	3,900	–
Carrying amount December 31	3,900	–	3,900	–

These provisions relate to BioGaia's estimated cost for development projects to which it is committed in accordance with the collaboration agreement with Nestlé (for more information – see the administration report). These provisions are expected to be settled in the next 12 months.

## Note 24 Other liabilities

	Group		Parent Company	
	2014	2013	2014	2013
Employee withholding tax	1,278	1,272	941	1,062
Other current liabilities	7,713	2,662	6,299	2,884
	8,991	3,934	7,240	3,946

Other current liabilities above include forward exchange contracts with a fair value of SEK 6.3 million (2.7). All forward exchange contracts are attributable to level 2 in the fair value hierarchy.

## Note 25 Accrued expenses and deferred income

	Group		Parent Company	
	2014	2013	2014	2013
Accrued holiday pay	6,210	5,986	4,745	4,615
Accrued social security expenses	1,308	1,218	796	900
Other accrued expenses	20,831	7,682	17,948	7,025
	28,350	14,886	23,490	12,540

## Note 26 Pledged assets and contingent liabilities

### PLEDGED ASSETS

	Group		Parent Company	
	2014	2013	2014	2013
Floating charges	2,000	2,000	2,000	2,000
Contingent liabilities	None	None	None	None

The floating charges relate to credit for credit cards.

## Note 27 Policy for financial risk management

The overall objective of the Group's finance function is to secure cost-effective financing for the Group's operations and group companies and to provide secure cash management with a market-based return on investment. The overall objective of financial risk management is to minimise the risk for negative effects on the Group's earnings. Consequently, the Group's financial investments must have a low risk profile. Below is a description of the Group's assessed risk exposure and the related risk management.

**Currency risk** BioGaia has revenue primarily in EUR, but also in SEK, USD and JPY, and expenses primarily in SEK, EUR, JPY and USD. The breakdown of net sales in 2014 (excluding license revenue from Nestlé) was approximately:

EUR 55%  
SEK 25%  
USD 15%  
JPY 5%

In 2014 the company had a cash flow surplus of approximately EUR 25.9 million (17.2) (2014 including the payment of EUR 10.8 million from Nestlé), a cash flow deficit of JPY -76.8 million (-138.7) and a cash flow surplus of USD 3.5 million (2.2).

Growth in sales has also led to increased currency risks, for which reason the company has taken currency hedges in EUR. The company's Board of Directors has issued a policy to hedge approximately 50-60% of projected cash flow 12 months forward and approximately 10-40% of projected cash flow 13-24 months forward in order to spread the risk for exchange rate fluctuations. At 31 December 2014 the company had outstanding forward exchange contracts for EUR 13.3 million at an average exchange rate of SEK 9.07. Forward exchange contracts amounting to EUR 8.7 million will mature for payment in 2015 and the remaining EUR 4.6 million in 2016. The actual exchange gain/loss depends on the exchange rate on the maturity date of the contracts. If the EUR rate on the maturity date is lower/higher than that at 31 December 2014 (9.48), an exchange gain/loss will be recognised in the future. For more information see Notes 9, 21 and 24.

The average exchange rate for EUR/SEK in 2014 was 9.10. If the EUR/SEK rate had been SEK 0.10 higher, BioGaia's net sales would have been approximately SEK 2.4 million higher and operating profit would have been around SEK 1.4 million higher (excluding license revenue from Nestlé).

The average exchange rate for USD/SEK in 2014 was 6.86. If the USD/SEK rate had been SEK 0.10 higher, BioGaia's net sales would have been approximately SEK 1.0 million higher and operating profit would have been around SEK 0.7 million higher.

A stronger SEK rate, primarily against the EUR, will decrease the value of BioGaia's sales and profit, but through profitable forward exchange transactions and by trying to reallocate a portion of expenses to EUR, the company is trying to minimise the impact on profit. The company is also trying to reallocate a portion of revenue from EUR to other currencies.

**Interest rate risk** The Group has no loans and therefore no interest rate risks. Excess liquidity is invested mainly in bank accounts – see liquidity risk below.

**Credit risks** BioGaia's credit risks are attached to trade receivables and, for the Parent Company, also loans to subsidiaries. When signing agreements with new customers, BioGaia always carries out an assessment of the customer's financial position. The company has routines for collection of past due accounts receivable and additional evaluation of the customers' financial position is carried out when needed in order to minimise risks.

The loan from the Parent Company to the subsidiary CapAble AB has been used to purchase equipment for manufacturing of LifeTop Cap. The company's assessment is that credit risk on the loan is low.

The loan from the Parent Company to the subsidiary TwoPac AB has been used mainly to build a new production facility in Eslöv, Sweden, that was completed and taken into operation during 2012. In 2013 an additional loan has been paid to TwoPac for construction of new production machinery. The company's assessment is that credit risk on the loan is low.

**Liquidity risk** The company's excess liquidity may be invested only in bank accounts, commercial paper or other fixed income securities with very limited risk. This means that no investments may be made in shares, equity funds, options, etc.

**Cash flow risk** In 2014 BioGaia had a positive cash flow from operating activities before changes in working capital of SEK 135.9 million (81.3). After changes in working capital, cash flow was SEK 124.4 million (78.4). Total cash flow for the year was SEK -25.0 million (-140.8). The cash flow includes payment of SEK 95.4 million in licence revenue from Nestlé, dividend of SEK 120.9 million (172.7) and tax payments of SEK 66.8 million (10.8).

Because cash and cash equivalents at 31 December 2014 amounted to SEK 210.7 million (234.3), no infusion of capital is necessary during the next 12 months.

**Price risk** BioGaia buys most of its goods on the international market and has several alternative suppliers, which reduces the company's price risk. BioGaia's price to distributors is largely the same for all, but can vary with respect to the order volume. Certain markets are subject to aggressive price competition towards consumers. However, BioGaia's strategy is not to compete in terms of price but to instead convince doctors of the effectiveness and safety of the products by showing the results of clinical studies.

## Note 28 Critical accounting estimates and assumptions

Certain sources of uncertainty in accounting estimates and assumptions are described below.

**BioGaia's Japanese venture** The Japanese subsidiary has operated at a loss since the start in 2006. The previously chosen business model was found to be unsuccessful and in 2010 BioGaia decided to change the business model in Japan to that which is used in the other markets. On the balance sheet date, assets in the Japanese subsidiary were reported at SEK 6.3 million. BioGaia's assessment is that there was no indication of impairment of these assets on the balance sheet date. In the Parent Company all current receivables from BioGaia Japan Inc. have been written off. The loan to the Japanese subsidiary and shares in the company have been written down to zero.

**Shares in group companies** CapAble, which is 90.1% owned by BioGaia AB, was started in November 2008 to manufacture and sell the patented LifeTop Cap. The shares in the subsidiary CapAble are reported at a total of SEK 6.9 million in the Parent Company. CapAble has operated at a loss since the start in 2008. Loss before tax for 2014 was SEK -2.9 (million (-2.6)). BioGaia made total conditional shareholder contributions of SEK 6 million to CapAble in 2009 and 2010. BioGaia AB made total group contributions of SEK 12.7 million during the period 2010-2014. On the balance sheet date, assets in CapAble were reported at SEK 3.6 million. BioGaia's assessment is that CapAble will show profitability in the coming years, for which reason there was no indication of impairment on the balance sheet date.

**Development of pharmaceutical against NEC** Infant Bacteria Therapeutics AB (IBT), which is 90.1% owned by BioGaia, was established in November 2013. At that time, the Board of BioGaia made a decision to invest in phase one of a long-term project aimed at developing a drug with rigorous hygiene, analysis and documentation requirements, to treat the highly fatal disease Necrotising Enterocolitis (NEC), which affects premature infants. BioGaia will invest up to SEK 42 million in the project over a two-year period. BioGaia AB has made conditional shareholder contributions of SEK 11.0 million to IBT and group contribution of SEK 7.0 million. On the balance sheet date, assets in IBT were reported at SEK 7.6 million in the Group. BioGaia's assessment is that IBT will show profitability in coming years, for which reason there was no indication of impairment on the balance sheet date.

The project offers major opportunities, but is also associated with substantial risks. The drug development is not realised, it is BioGaia's intention to market the formulation under another product category.

**Ongoing tax matter** The company has an ongoing tax matter related to a write-down of receivables from the Japanese subsidiary. In the event of a negative outcome, this could result in additional tax expenses of SEK 3.1 million. If the outcome is positive, there is opportunity to receive an additional tax income of SEK 3.8 million for previous years.

**Expenses for stability problem** During 2014 BioGaia experienced problems with the stability of the bacteria cultures from one of its suppliers. On delivery the cultures met specifications, but in the finished product the shelf life was shorter than normal. The problem was detected through BioGaia's own quality control system. BioGaia has recalled a number of products from its partners, which cost the company a total of around SEK 11 million in 2014 including accrued expenses of SEK 9.0 million as of year-end. The problem is now under control and no further expenses are expected. BioGaia has a comprehensive action plan, which includes both short-term measures and an ambitious development project to build further knowledge in the fermentation area.

The Board of Directors and the President hereby give their assurance that the consolidated financial statements and annual report have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and generally accepted auditing practices, and give a true and fair view of the financial position and results of operations of the Group and the Parent Company. The administration report for the Group and the Parent Company gives a true and fair view of the business activities, financial position and results of operations of the Group and the Parent Company, and describes the significant risks and uncertainties to which the Parent Company and the Group companies are exposed.

### Stockholm, 20 February 2015

David Dangoor  
*Chairman*

Peter Rothschild  
*President*

Inger Holmström  
*Member of the Board*

Jan Litborn  
*Member of the Board*

Brit Stakston  
*Member of the Board*

Jörgen Thorball  
*Member of the Board*

Paula Zeilon  
*Member of the Board*

### My audit report was submitted on 20 February 2015

Grant Thornton Sweden AB

Lena Möllerström Nording  
*Authorised Public Accountant*

# Five-year summary

Key ratios	2014	2014 <sup>1)</sup>	2013	2012	2012 <sup>1)</sup>	2011	2010
Net sales, SEK M	481.8	386.4	315.9	645.2	289.2	315.0	236.0
Net sales, Paediatrics, SEK M	409.1	313.7	238.6	N/A	N/A	N/A	N/A
Net sales, Adult Health, SEK M	69.4	69.4	75.6	N/A	N/A	N/A	N/A
Net sales, finished consumer products, SEK M	303.6	303.6	256.2	237.6	237.6	215.4	165.6
Net sales, component products, SEK M	176.1	80.7	58.6	406.6	50.6	97.7	68.6
Operating profit, SEK M	196.9	101.5	81.7	428.1	72.1	103.2	56.3
Profit before tax, SEK M	192.5	97.1	83.8	442.2	86.2	108.9	69.7
Profit after tax, SEK M	148.0	73.6	64.2	329.9	63.7	79.5	47.2
Profit after tax attributable to owners of the Parent Company, SEK M	147.4	73.0	61.7	327.0	60.8	76.4	47.3
Growth, %	53	22	9	105	-8	33	16
Operating margin, %	41	26	26	66	25	33	24
Profit margin, %	40	25	27	69	30	35	30
Current ratio, times	4.7	4.8	4.9	13.2	5.1	5.2	5.1
Equity/assets ratio, %	83	84	83	88	82	82	82
Capital employed, SEK M	344.8	270.4	316.9	481.5	195.7	230.5	187.3
Return on capital employed, %	60	35	22	124	40	52	40
Return on equity, %	45	25	16	96	29	37	27
Average number of employees	90	90	82	70	70	61	45
<b>Data per share</b>							
Number of shares at 31 Dec., thousands <sup>2)</sup>	17,271	17,271	17,271	17,271	17,271	17,271	17,271
Average number of shares, thousands	17,271	17,271	17,271	17,271	17,271	17,271	17,230
Number of outstanding warrants, thousands	87	87	87	87	87	-	-
Number of outstanding warrants with a dilutive effect, thousands	-	-	87	-	-	-	-
Number of outstanding shares including outstanding warrants with a dilutive effect, thousands	17,271	17,271	17,358	17,271	17,271	17,271	17,271
Basic earnings per share, SEK	8.53	4.23	3.57	18.93	3.52	4.42	2.74
Diluted earnings per share, SEK	8.53	4.23	3.56	18.93	3.52	4.42	2.74
Equity per share, SEK	19.95	15.64	18.37	26.25	10.83	13.30	10.84
Equity per share after dilution, SEK	19.95	15.64	18.28	26.25	10.83	13.30	10.84
Cash flow from operating activities per share, SEK	7.2	N/A	4.54	19.43	N/A	4.21	3.99
Cash flow from operating activities per share after dilution, SEK	7.2	N/A	4.52	19.43	N/A	4.21	3.99
Share price on the balance sheet date, SEK	179.50	179.5	253.50	175.00	175.00	163.00	96.00
Dividend per share, SEK	5.00 <sup>3)</sup>	5.00 <sup>3)</sup>	7.00	10.00	10.00	6.00	2.00

<sup>1)</sup> Key ratio excluding license revenue from Nestlé of SEK 95.4 million in 2014 and SEK 356.0 million in 2012. For more information, see administration report.

<sup>2)</sup> The share capital consists of 740,668 class A shares and 16,530,294 class B shares. The quota value is SEK 1 per share.

<sup>3)</sup> Dividend proposed but not yet approved.

For definitions of key ratios, see page 70.

# Audit report

To the general meeting of the shareholders in BioGaia AB (publ), corporate identity number 556380-8723

## Report on the annual accounts and consolidated accounts

We have audited the annual accounts and consolidated accounts of BioGaia AB for the year 2014.

The annual accounts and consolidated accounts of the company are included in the printed version of this document on pages 36-62.

### RESPONSIBILITIES OF THE BOARD OF DIRECTORS AND THE PRESIDENT FOR THE ANNUAL ACCOUNTS AND CONSOLIDATED ACCOUNTS

The Board of Directors and the President are responsible for the preparation and fair presentation of these annual accounts in accordance with the Annual Accounts Act and of the consolidated accounts in accordance with International Financial Reporting Standards, as adopted by the EU, and the Annual Accounts Act, and for such internal control as the Board of Directors and the President determine is necessary to enable the preparation of annual accounts and consolidated accounts that are free from material misstatement, whether due to fraud or error.

### AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these annual accounts and consolidated accounts based on our audit. We conducted our audit in accordance with International Standards on Auditing and generally accepted auditing standards in Sweden. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the annual accounts and consolidated accounts are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the annual accounts and consolidated accounts. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the annual accounts and consolidated accounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation and fair presentation of the annual accounts and consolidated accounts in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Board of Directors and the President, as well as evaluating the overall presentation of the annual accounts and consolidated accounts.

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

### OPINIONS

In our opinion, the annual accounts have been prepared in accordance with the Annual Accounts Act and present fairly, in all material respects, the financial position of the Parent Company as of 31 December 2013 and of its financial performance and its cash flows for the year then ended in accordance with the Annual Accounts Act. The consolidated accounts have been prepared in accordance with the Annual Accounts Act and present fairly, in all material respects, the financial position of the Group as of 31 December 2014 and of their financial performance and cash flows for the year in accordance with International Financial Reporting Standards, as adopted by the EU, and the Annual Accounts Act. The statutory administration report is consistent with the other parts of the annual accounts and consolidated accounts.

We therefore recommend that the annual meeting of shareholders adopt the income statement and balance sheet for the Parent Company and the statement of consolidated income and financial position for the Group.

## Report on other legal and regulatory requirements

In addition to our audit of the annual accounts and consolidated accounts, we have examined the proposed appropriations of the company's profit or loss and the administration of the Board of Directors and the President of BioGaia AB for the year 2014.

### RESPONSIBILITIES OF THE BOARD OF DIRECTORS AND THE PRESIDENT

The Board of Directors is responsible for the proposal for appropriations of the company's profit or loss, and the Board of Directors and the President are responsible for administration under the Companies Act.

### AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion with reasonable assurance on the proposed appropriations of the company's profit or loss and on the administration based on our audit. We conducted the audit in accordance with generally accepted auditing standards in Sweden.

As a basis for our opinion on the Board of Directors' proposed appropriations of the company's profit or loss, we examined the Board of Directors' reasoned statement and a selection of supporting evidence in order to be able to assess whether the proposal is in accordance with the Companies Act.

As a basis for our opinion concerning discharge from liability, in addition to our audit of the annual accounts and consolidated accounts, we examined significant decisions, actions taken and circumstances of the company in order to determine whether any member of the Board of Directors or the President is liable to the company. We also examined whether any member of the Board of Directors or the President has, in any other way, acted in contravention of the Companies Act, the Annual Accounts Act or the Articles of Association.

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

### OPINIONS

We recommend to the annual meeting of shareholders that the profit be appropriated in accordance with the proposal in the statutory administration report and that the members of the Board of Directors and the President be discharged from liability for the financial year.

Stockholm, 20 February 2015

Grant Thornton Sweden AB

Lena Möllerström Nording  
*Authorised Public Accountant*

# Corporate governance report 2014

**Corporate governance in BioGaia** BioGaia is a Swedish public limited company whose class B shares are listed on the Mid Cap list of the NASDAQ OMX Nordic Exchange Stockholm. The company's corporate governance is exercised through the General Meeting of Shareholders, the Board of Directors, the President and the Executive Management in accordance with the Swedish Companies Act, the Articles of Association and the Swedish Code of Corporate Governance

**Articles of Association** According to BioGaia's Articles of Association, the company, directly or through subsidiaries or other forms of co-ownership or partnership, shall engage in the development, production, marketing and sale of health-enhancing products in the form of pharmaceuticals, natural health products, dietary supplements, additives for food products and animal feed, suitable delivery systems for these products and other activities compatible therewith. The company is domiciled in Stockholm, Sweden. The Articles of Association can be viewed on BioGaia's website under the heading "Investors/Corporate Governance".

**General Meeting of Shareholders** The General Meeting of Shareholders is the company's highest decision-making body. The Annual General Meeting (AGM) elects the members of the Board of Directors. In addition, the responsibilities of the AGM include adoption of the company's income statements and balance sheets, approval of the appropriation of disposable profits and discharge from liability for the members of the Board and the President. The AGM also elects the company's auditors.

One shareholder, Annwall & Rothschild Investment AB, holds 8.7% of the share capital and 34.1% of the votes in the company. Other individual shareholders hold less than 10% of the share capital and votes each.

**2014 AGM** BioGaia's AGM was held on 6 May 2014 and was attended by shareholders representing 55.5% of the total number of votes in the company. The AGM was also attended by the company's President, the Board members elected by the previous AGM and all of the Board members elected by the year's AGM, as well as the company's elected auditor.

**2015 AGM** The 2015 AGM will be held at 4:00 p.m. on Thursday, 7 May, at Lundqvist & Lindqvist Klara Strand, Klarabergsviadukten 90, in Stockholm.

**Notice of the AGM** Notice of the AGM is given through an announcement in the Official Gazette (Post- och Inrikes Tidningar) and on the company's website. An announcement that notice has been given shall be published in Svenska Dagbladet no earlier than six weeks and no later than four weeks prior to the AGM.

**Nominating Committee** The task of the Nominating Committee is to prepare recommendations regarding election and remuneration for decision by the AGM.

The 2014 AGM resolved that the Nominating Committee would be appointed according to the following: "The Board Chairman shall convene the three largest shareholders in the company in terms of voting power, each of which has the right to appoint a member to the Nominating Committee together with the Board Chairman. In determining the composition of the Nominating Committee, the largest shareholders in terms of voting power shall be based on the ownership conditions at 30 June 2014. The Nominating Committee shall be chaired by the member representing the largest shareholder at that time. If any of the three largest shareholders should waive their right to appoint a member to the Nominating Committee, the next largest shareholder in order of voting power shall be given the opportunity to appoint a member. The names of the three shareholder representatives shall be made public as soon as they have been appointed, but no later than six months before the 2015 AGM. The term of office shall extend until a new Nominating Committee has been appointed.

In the event that the shareholder represented by a member is no longer one of the three largest shareholders in terms of voting power, and if the Nominating Committee deems it appropriate, the member can resign and a representative for the next largest shareholder in order of voting power can be given the opportunity to replace this member. The same applies of a member of the Nominating Committee leaves the Committee for some other reason." In accordance with the AGM's resolution, the Nominating Committee was appointed and consists of the Chairman of BioGaia AB, David Dangoor, together with Per-Erik Andersson, representing Annwall & Rothschild Investment AB, the company's largest shareholder, Allan Ladow, representing Sebastian Jahreskog, who via direct and indirect ownership is the second largest shareholder, and Jannis Kitsakis, representing Fjärde AP-Fonden, the company's third largest shareholder. All four members of the Nominating Committee are independent in relation to the company and its management.

The Nominating Committee shall prepare recommendations for the following matters to be put before the 2015 AGM for resolution:

- appointment of the Chairman of the AGM
- election of the Board of Directors
- election of the Board Chairman
- fees for members of the Board
- election of auditors
- fees for the auditors
- appointment of the Nominating Committee ahead of the 2016 AGM.

All shareholders have the opportunity to contact the Nominating Committee with recommendations for Board candidates for further evaluation within the framework of the Committee's work. No suggestions or proposals have been submitted to the Nominating Committee as of today's date.

The Nominating Committee presents a written motivation to the AGM for election of Board members.

**Board of Directors** According to BioGaia's Articles of Association, the Board shall consist of at least five and at most eight members with no more than three deputies. The Board is elected yearly by the AGM to serve for the period until the end of the following AGM. In 2014 the Board consisted of eight members elected by the AGM, with no deputies. One Board member, Jan Annwall, has been a member of the Board since 1990 and is a major shareholder in the company. Jan Annwall was previously employed by the company as CFO and Executive Vice President, but retired on 1 April 2010. However, Jan Annwall works to a limited extent as a consultant to the company. The seven remaining members are independent in relation to both the company and its management. A presentation of the Board is provided on page 68.

BioGaia's legal counsel has been appointed to serve as Secretary at Board meetings. The President is not a member of the Board but is co-opted to attend all Board meetings. Other executives in the company take part in Board meetings in order to present reports. The Board has adopted rules of procedure that include instructions for the separation of duties between the Board and the President and the structure of Board activities during the year. Furthermore, the Board has adopted instructions for the President, authorisation instructions including instructions for liquidity management and a policy for foreign exchange management. The rules of procedure, President's instructions and authorisation instructions are reviewed at least once a year.

The Board decides on matters related to the Group's overall strategy, organisation and management. The Board approves both interim reports and the annual report before these are published. The Board held seven minuted meetings and one strategy seminar in 2014. During the year, Paula Zeilon, Inger Holmström, Thomas Flinck and Brit Stakston were each absent from one meeting.

At the meetings the Board has among other things discussed business plans, investments, strategic matters, financial reports, major agreements, budgetary matters and accounting matters. At the strategy seminar, the Board dealt mainly with issues concerning R&D, product development, patent strategy, regulatory and quality issues and related matters.

The Board of Directors continuously evaluates its own performance through both open discussions and a written self-assessment. The results of the written assessment are submitted to the Nominating Committee.

**Board fees** The 2014 AGM resolved that Board fees would be paid in an amount of SEK 300,000 to the Board Chairman and SEK 150,000 to each of the other Board members not employed by the company

**Board Chairman** The Chairman supervises the work of the Board and is responsible for ensuring that the Board carries out its duties in accordance with the Swedish Companies Act and the rules of procedure. Through ongoing contact with the President, the Chairman continuously monitors the company's development and ensures that the Board is provided with the information necessary to carry out its duties. David Dangoor has been Board Chairman since the 2007 AGM.

**President** The President is responsible for overseeing the company's business development and for supervising and coordinating its day-to-day operations. The Board has established instructions for the President that among other things regulate his management and development of the company and the provision of reports and decision data to the Board. The President prepares the requisite information and decision data such as reports on the company's finances, the order situation, significant business matters and strategic issues prior to Board meetings, as well as presenting reports and motivating proposals



for decision. Furthermore, the President continuously informs the Board Chairman about the company's financial and business situation. Every year the Board carries out an evaluation of the President's performance in which no member of the Executive Management is present.

**Executive Management** BioGaia's Group Executive Management consists of the twelve individuals who are presented on page 68. The Group's Executive Management is headed by the President and is responsible for planning, supervising and monitoring the company's day-to-day operations. Minuted meetings are normally held once a month. The responsibilities and powers of the President are regulated by the Swedish Companies Act and by the instructions that are adopted by the Board. The responsibilities and powers of the Executive Management are defined in the established job descriptions and authorisation instructions.

**Remuneration Committee** The Board has appointed a Remuneration Committee consisting of Board Chairman David Dangoor and Board member Stefan Elving. The task of the Remuneration Committee is to prepare recommendations for the remuneration and other terms of employment of the President and other senior executives who together make up the Executive Management. The principles for remuneration to senior executives are resolved on by the AGM. The Remuneration Committee prepares its recommendations based on these principles.

**Auditors** BioGaia's independent auditors are normally appointed by the AGM to serve for a period of four years. The 2010 AGM elected Grant Thornton Sweden AB as the company's auditor until the end of the 2014 AGM. The 2014 AGM resolved to re-elect the certified auditing firm of Grant Thornton Sweden AB for the period until the end of the AGM that will be held in 2015. The auditing firm has appointed Lena Möllerström Nording as Auditor in Charge. By decision of the AGM, auditing fees are paid according to approved account.

The auditors examine the administration of the company by the Board of Directors and the President and the quality of the company's financial reporting. At the request of the Board, the auditors also review 6 month report and the year-end report.

The auditors report the results of their review to the shareholders through an audit report, which is presented to the AGM. In addition, the auditors submit written and oral reports to the Executive Management and the Board. The auditors take part in the Board meeting preceding publication of the year-end report to present the results of their audit of the annual accounts and observations from ongoing examination of the company's internal control during the financial year.

The auditors also submit an auditor's statement on the corporate governance report and a report on the examination of remuneration to senior executives.

In addition, Grant Thornton has provided certain tax-related advice and performed other audit-related services. Information about remuneration to the auditors can be found in Note 4 of the annual report.

Due to the fact that independent Board members have accounting expertise and in view of the Board's ongoing examination of the financial reporting and the company's limited size and transaction volume, the Board has decided not to set up any audit committee. Furthermore, the entire Board of Directors meets with the auditors at least once a year without the presence of the President or other members of the Executive Management.

#### **The Board's report on internal control over financial reporting for the 2014 financial year**

**Introduction** As stated in the Swedish Companies Act, the Swedish Annual Accounts Act and the Swedish Code of Corporate Governance, the Board of Directors is responsible for establishing and maintaining adequate internal control. This description has been prepared in accordance with these rules and provisions and is thereby limited to internal control over financial reporting.

**Financial reporting** The Board is responsible for ensuring that the company's organisation is suitably structured so that the financial accounts, cash management and other financial conditions can be controlled satisfactorily.

Every year, the Board of Directors adopts rules of procedure for the Board's activities and instructions regulating the division of responsibilities between the Board and the President. The rules of procedure state which matters require approval or authorisation from the Board. At Board meetings, the President reports on matters requiring treatment by the Board.

The President ensures that the Board is provided with the objective, detailed and relevant information needed for the Board to make well founded decisions and that the Board is continuously informed about the company's business development and financial position.

Aside from the rules of procedure between the Board and the President, BioGaia's control structure is based on the company's organisation and its operation in which roles and responsibilities are defined. There is a high level of employee awareness about the importance of maintaining good control over financial reporting. The company's financial development is assessed and monitored monthly. Financial reports and summaries are prepared by the Group's finance department and are presented to the Board quarterly and to the Executive Management monthly.

**BioGaia's values** BioGaia also has a set of shared values and the company's employees are well aware of these (see below).

BioGaia's vision is to improve the health of people around the world by offering first class probiotic products.

#### **BioGaia's values:**

- My personal commitment is vital for BioGaia's success.
- We are innovative and action-oriented.
- We are business-minded and deliver on our promises.
- We are honest, respectful and selfless in what we do and say.

**Risk assessment** The company works continuously with risk assessment and risk management to ensure that the risks to which the company is exposed are handled within the limits ultimately established by the Board. The Executive Management continuously analyses the company's business processes with regard to efficiency and risks.

This work includes the identification of significant risks for misstatements and deficiencies in the financial reporting. To limit these risks, suitable processes and controls are built into the company's operations. The most critical business processes and the absolutely largest values, in terms of both assets and business/product development, are found in the Parent Company. In addition, the bulk of sales take place in the Parent Company. Processes that are deemed to be of special importance to BioGaia are sales including quality assurance, R&D and manufacturing.

**Control activities** The risks identified in the financial reporting are managed through a number of control activities in the company's processes. Processes and controls are reviewed and updated regularly in order to detect, prevent and correct any errors or deficiencies. The control structure also includes the division of powers and responsibilities and the Executive Management's monthly review of the company's financial information.

**Information and communication** BioGaia has information and communication paths that are designed to promote the completeness and accuracy of the financial reporting. Authorisation instructions and policies are distributed to all employees and can be viewed on the company's intranet. Once or twice a year, all of BioGaia's employees meet to increase their knowledge about the company's processes and goals and to exchange information and experiences. In 2014 the company's employees met for two days in May.

**Monitoring** The Executive Management performs a yearly evaluation of the effectiveness of internal control. Every year, the company's elected auditing firm, Grant Thornton Sweden AB, also audits of a selection of BioGaia's routines and internal controls. The Board then evaluates this information and ensures that measures are taken in respect of the identified deficiencies and resulting recommendations.

The company has no special internal audit function. In light of the company's size and the volume of transactions, together with the expertise in this area possessed by the Board of Directors and the Board's meeting with the independent auditor, the Board has determined that there is no reason to set up a formal internal audit function.

#### **Stockholm, 20 February 2015**

Board of Directors of BioGaia AB

#### **Auditors' statement on the corporate governance report**

*To the general meeting of the shareholders in BioGaia AB (publ.), corporate identity number 556380-8723*

The Board of Directors is responsible for the corporate governance report for the year 2014 (on pages 64-65) and for ensuring that it has been prepared in accordance with the Annual Accounts Act.

We have read the corporate governance report and based on this reading and our knowledge of the company and the Group we believe we have sufficient grounds for our statement. This means that our statutory review of the corporate governance report has a different focus and scope compared to the focus and scope of an audit according to the International Standards on Auditing and generally accepted accounting principles in Sweden.

In our opinion, a corporate governance report has been prepared and its statutory information is consistent with the annual report and the consolidated accounts.

#### **Stockholm, 20 February 2015**

Grant Thornton Sweden AB

Lena Möllerström Nording  
*Authorised Public Accountant*

# The BioGaia share

Figures in brackets refer to the preceding year

**Trading volume** BioGaia AB's class B share has been quoted on the OMX Nordic Exchange Stockholm since May 1998. On 1 January 2012 the share was moved from the Small Cap list to the Mid Cap list.

In 2014 BioGaia shares were traded for a total of around SEK 1,172 million (906), corresponding to approximately 6.0 million shares (4.2).

The number of shareholders at 31 December 2014 was 7,136 (7,448).

The total registered share capital of BioGaia AB consists of 740,668 class A shares and 16,530,294 class B shares.

**Share price development** In 2014 the share price decreased from SEK 253.50 to SEK 179.50. The highest closing price during the year was SEK 253.00 and the lowest was SEK 151. Market capitalisation at 31 December 2014 was approximately SEK 3,100 million (4,378).

**Dividend policy** BioGaia's policy is to pay a shareholder dividend equal to 40% of profit after tax.

**Incentive scheme** In June 2012 BioGaia carried out the warrant programme that was decided by the Annual General Meeting on 8 May 2012. A total of 87,000 warrants were subscribed for, of which the management subscribed for 41,000. The warrants were issued at a market price of SEK 14.27 each following valuation according to the Black & Scholes formula, which provided the Parent Company with proceeds of SEK 1.3 million. Each warrant entitles

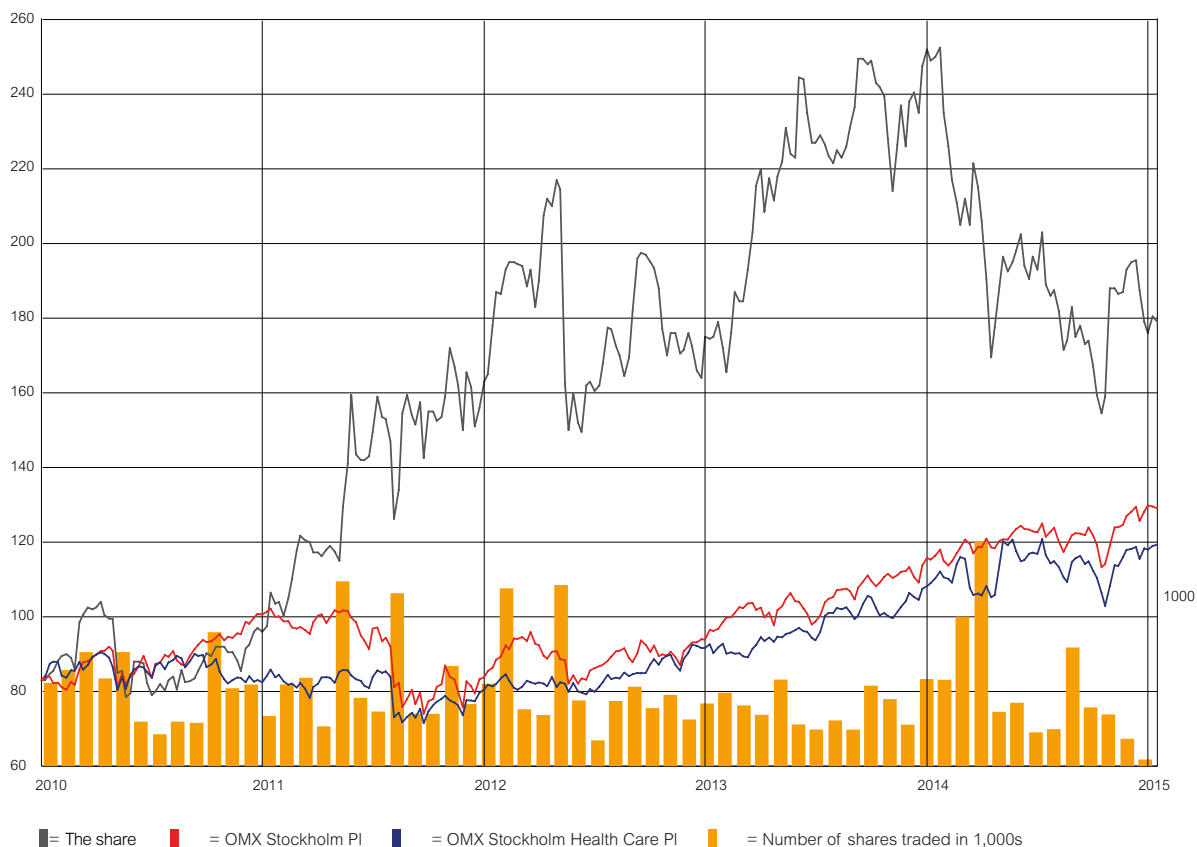
the holder to subscribe for one class B share for SEK 241.90 on 1 June 2015. Volatility was estimated at 40%.

If all of the subscription warrants are exercised, the company's equity will be increased by SEK 21.0 million. This represents a dilutive effect of approximately 0.5% on the share capital and 0.4% on the total number of votes upon the full exercise of warrants.

## Distribution of ownership

Number of shares	Total number of shareholders	
	31 Dec 2014	31 Dec 2013
1-500	5,832	6,080
501-1,000	641	687
1,001-5,000	475	480
5,001-10,000	65	66
10,001-15,000	21	24
15,001-20,000	16	19
20,001-	86	92
<b>Total number of shareholders:</b>	<b>7,136</b>	<b>7,448</b>

## The BioGaia share



## Largest shareholders in BioGaia at 31 December 2014 (source: Euroclear Sweden AB)

	A shares, 000's	B shares, 000's	Share capital, SEK 000's	No. of votes, 000's	Holding, %	Votes, %
Annwall & Rothschild Inv. AB	741	759	1,500	8,166	8.7	34.1
Sebastian Jahreskog		1,263	1,263	1,263	7.3	5.3
Fjärde AP-fonden		693	693	693	4.0	2.9
JPM Chase NA		689	689	689	4.0	2.9
David Dangoor (incl. company)		569	569	569	3.3	2.4
Nordea Investment Funds		550	550	550	3.2	2.3
Handelsbanken Fonder AB		534	534	534	3.1	2.2
Banque Pictet & CIE, W8IMY		509	509	509	3.0	2.1
Six Sis AG W8IMY		426	426	426	2.5	1.8
State Street Bank & Trust com., Boston		415	415	415	2.4	1.7
AMF-Försäkring och fonder		388	388	388	2.2	1.6
Swedbank Robur fonder		386	386	386	2.2	1.6
Caroline Hamilton		303	303	303	1.8	1.3
Banque Carnegie Luxembourg SA		279	279	279	1.6	1.2
JP Morgan Chase N.A		273	273	273	1.6	1.1
Hanvad Invest Aktiebolag		268	268	268	1.6	1.1
Livförsäkringsaktiebolaget Skandia		247	247	247	1.4	1.0
Försäkringsaktiebolaget Avanza Pension		241	241	241	1.4	1.0
Sten Irwe		224	224	224	1.3	0.9
Skandinaviska Enskilda Banken S.A		203	203	203	1.2	0.8
SEB London Client's acc		201	201	201	1.2	0.8
CF Ruffer Investment Funds		200	200	200	1.2	0.8
SSB Client Omnibus Account Abu, Dhabi		193	193	193	1.1	0.8
Nordnet Pensionsförsäkring AB		185	185	185	1.1	0.8
UBS AG Client Account		143	143	143	0.8	0.6
Other		6,389	6,389	6,389	36.8	26.9
<b>Total</b>	<b>741</b>	<b>16,530</b>	<b>17,271</b>	<b>23,937</b>	<b>100.0</b>	<b>100.0</b>

## Changes in share capital since the company's formation

Year	Transaction	Increase in no. of shares	Increase in share capital, SEK	Total share capital, SEK	Total no. of A shares	Total no. of B shares	Quota value, SEK	Issue proceeds, SEK
1990	Company founded			150,000		30,000	5.00	–
1991	New share issue	12,857	64,285	214,285		42,857	5.00	4,500,000
1993	New share issue	12,554	62,770	277,055		55,411	5.00	4,394,341
1995	New share issue	2,303	11,515	288,570		57,714	5.00	806,009
1996	Bonus issue/Split	60,541,986	5,771,400	6,059,970	4,740,278	55,859,422	0.10	–
1996	New share issue	18 200,000	1,820,000	7,897,970	4,740,278	74,059,422	0.10	15,320,000
1997	New share issue Banco Fonder	2,608 696	260,870	8,140,840	4,740,278	76,668,118	0.10	5,760,000
1997	New share issue BioGaia Fermentation	4,400,000	440,000	8,580,840	4,740,278	81,068,118	0.10	7,469,000
1997	New share issue	21,452,099	2,145,210	10,726,050	5,925,347	101,335,148	0.10	38,597,265*
1998	New share issue	5	1		5,925,350	101,335,150	0.10	20
1998	Reverse split				592,535	10,133,515	1.00	–
1998	New share issue (IPO on SSE)	2,681,512	2,681,512	13,407,562	740,668	12,666,894	1.00	57,934,131*
2000	New share issue November	3,275,000	3,275,000	16,682,562	740,668	15,941,894	1.00	73,031,886*
2000	New share issue December	425,000	425,000	17,107,562	740,668	16,366,894	1.00	11,505,294*
2004	New share issue Industrifonden	100,000	100,000	17,207,562	740,668	16,466,894	1.00	100,000
2010	New share issue warrant programme	63 ,400	63,400	17,270,962	740,668	16,530,294	1.00	4,862,780

\* Excluding underwriting costs

## Executive Management



**PETER ROTHSCHILD**  
Born in 1950. M.B.A. President, founder and principal shareholder. Board assignments in Looft Industries AB. Holds 370,334 class A shares and 379 666 class B-shares via Annwall & Rothschild Investment AB, and 10,000 warrants.

**MARGARETA HAGMAN**  
Born in 1966. M.B.A. Executive Vice President Accounting, Finance and Investor Relations. Employed by the company since 1996, in current position since 2010. Holds 9,000 class B shares and 3,000 warrants.

**URBAN STRINDLÖV**  
Born in 1964. Mechanical Engineer. Executive Vice President and Sales Director. Employed by the company since 2004, in current position since 2010. Holds 10,000 warrants.

**EAMONN CONNOLLY**  
Born in 1957. Ph.D. Senior Vice President Research BioGaia and IBT. Employed by the company since 2000, in current position since 2002 (IBT 2013). Holds 0 shares.

**ANN WENNERSTRÖM**  
Born in 1961. Registered nurse, education in marketing, PR and Public Affairs. Marketing Director. Employed by the company since 2012. Holds 6,000 warrants

**KATAYOUN WELIN-BERGER.** Born in 1968. Ph.D. in Pharmacology. Head of the Department for Strategic Purchasing and Quality. Employed by the company since 2014. Holds 0 shares.

## Board of Directors

**DAVID DANGOOR**  
Born in 1949. Chairman of the Board. Elected to the Board in 2003. M.B.A. Marketing and PR consultant. President of Innovative Partners LLC. Former Vice President and Marketing Director at Philip Morris USA and Philip Morris International. Other board

assignments: Lifetime Brands, Inc., New York, City Ballet Inc., BAM, Brooklyn, School of Creative Leadership, Berlin University and the Swedish-American Chamber of Commerce (SACC NY, chairman 1997–2001). Holds 518,918 class B shares and 50,000 class B shares via private company.

**INGER HOLMSTRÖM**  
Born in 1948. Elected to the Board in 2007. M.A. in language and linguistics and a degree in journalism. President of Priority Group. Former Corporate Communications Director at Coop Norden, Posten and Vattenfall. Holds 500 class B shares.

**STEFAN ELVING**  
Born in 1941. Elected to the Board in 2001. Former Marketing Director and Executive Vice President of Icahandlarnas AB. Other board assignments: Arcus AS. Holds 0 shares.

**BRIT STAKSTON**  
Born in 1961. Elected to the Board in 2014. PR Consultant, media strategist and owner of PR Agency Stakston AB. Holds 0 shares.





**JESSICA EIDEMO**

Born in 1974. M.Sc. Biology, education in business economics and marketing. Head of Business Unit Pediatrics. Employed by the company since 2012, in current position since 2014. Holds 6,000 warrants.

**BO MÖLLSTAM**

Born in 1952. M.B.A. Director of Intellectual Property. Employed by the company since 1990, on a consulting basis since 2003. Holds 51,000 class B shares.

**NIGEL TITFORD**

Born in 1973. M.Sc. Business Administration and Business Law. Head of Business Unit Adult Health. Employed by the company since 1999, in current position since 2014. Holds 792 class B shares.

**KRISTINA SILVERIO**

Born in 1964. M.Sc.Eng. Vice President Production and Supply. Employed by the company since 2003, in current position since 2005. Holds 0 shares.

**ULRIKA KÖHLER**

Born in 1966. B.Sc. Biology with extended studies in microbiology. Head of Business Unit New Business. Employed by the company since 2013. Holds 0 shares.

**HELEN OLSSON**

Born in 1965 responsible for Human Resources. Employed by the Company as a consultant since 2013, in current position since 2015. Holds 0 shares.

**JÖRGEN THORBALL**

Born in 1962. Elected to the Board in 2008. Physician. Managing Partner XOventure GmbH, President of Ophiuchus AG. Former international senior positions at Novozymes,

BioGaia, Aventis and Pharmacia, among others. Other board assignments: ViroGates A/S, YourGlobalEye Aps, 1cryobio AG Anova Pharmaceuticals, AG. Holds 0 shares.

**PAULA ZEILON**

Born in 1962. Elected to the Board in 2003. M.Sc. Eng. Partner in Conlega affärskonsultbolag. President of Life Science Foresight Institute. Former Marketing Director at Amersham Biosciences AB. Holds 1,000 class B shares.

**JAN LITBORN**

Born in 1951, Elected to the Board in 2014. Partner at the law firm Glimstedt and specialised in business law. Other board assignments: Anders Hedin Invest AB, Visio Property Ltd,

Svensk Fastighetsfinansiering AB, Lord Asset Management LTD and Consensus Asset Management AB with several medium-sized companies. Holds 0 shares.

**JAN ANNWALL**

Born in 1950. Elected to the Board in 1990. M.B.A. Former Executive Vice President and CFO of BioGaia AB. Founder and principal shareholder in BioGaia AB. Holds 370,334 class A shares and 379,666 class B shares via Annwall & Rothschild Investment.



# Definitions and glossary

## Definitions

### Basic earnings per share

Profit after tax attributable to owners of the Parent Company divided by the number of shares.

### Cash flow from operating activities per share

Cash flow from operating activities divided by the number of shares.

### Cash flow from operating activities per share after dilution

Cash flow from operating activities divided by the number of shares plus the number of outstanding warrants with a dilutive effect.

### Capital employed

Balance sheet total less interest-free liabilities.

### Current ratio

Total current assets divided by current liabilities.

### Diluted earnings per share

Profit after tax attributable to owners of the Parent Company divided by the number of shares plus the number of outstanding warrants with a dilutive effect

### Diluted equity per share

Shareholders' equity attributable to the owners of the Parent Company divided by the number of shares plus the number of outstanding warrants with a dilutive effect.

### Equity/assets ratio

Shareholders' equity attributable to the owners of the Parent Company divided by total assets.

### Equity per share

Shareholders' equity attributable to the owners of the Parent Company divided by the number of shares.

### Growth

Sales for the current year less sales for the previous year divided by sales for the previous year.

### Operating margin

Operating profit in relation to net sales.

### Profit margin

Profit before tax in relation to net sales.

### Return on capital employed

Profit before financial items plus financial income, divided by average capital employed.

### Return on equity

Profit after tax equity attributable to the owners of the Parent Company divided by average shareholders' equity attributable to the owners of the Parent Company.

## Glossary

### Antibiotics

Compounds that kill or inhibit the growth of microorganisms.

### *Helicobacter pylori*

Very commonly occurring bacteria in many parts of the world. Resides in the stomach and may lead to peptic ulcers and gastric cancer.

### Clinical research

Research conducted in humans.

### Lactobacillus

Lactic acid bacteria. A collective name for a group of microorganisms that occur naturally in various foods such as yogurt, olives and pickled vegetables. In the past, we ingested a lot of lactic acid bacteria, but today our diet lack these beneficial bacteria. Some lactic acid bacteria are also present in the human commensal flora.

Lactic acid bacteria have different properties and may thus give different health effects when consuming them. There are a large number of lactic acid bacteria, for example *Lactobacillus reuteri* and *Lactobacillus acidophilus*.

### *Lactobacillus reuteri* (L. reuteri)

Species within the genus *Lactobacillus*. The vast majority of BioGaia's patented probiotics are different strains of *Lactobacillus reuteri*, for example, *Lactobacillus reuteri* Protectis.

### *Lactobacillus reuteri* Gastrus

Combination of two strains of *Lactobacillus reuteri*, used in BioGaia's digestive health product for use in connection with *Helicobacter pylori* infection.

### *Lactobacillus reuteri* Prodentis

Combination of two strains of *Lactobacillus reuteri*, used in BioGaia's oral health products.

### *Lactobacillus reuteri* Protectis

Strain of *Lactobacillus reuteri*, used in BioGaia's digestive health products for children and adults.

### Partner

The companies distributing and selling BioGaia's products.

### Probiotics

Live microorganisms that, when administered in adequate amounts, confer a health benefit on the host.

### Resistant bacteria

Bacteria that have become resistant to one or several antibiotics.



Projektledning: Eva Nelson, kommunikationschef BioGaia. Chatarina Andersson, marknadsassistent, BioGaia (sifferdelen). Anna Jonason, AD/kommunikationstrateg, Krut.

Foto: Magnus Ragnvid, Apelöga, Johnér bildbyrå, Getty Images, Shutterstock. Tryck: Modintryck 2015.

This is a translation of the Swedish version of the interim report. When in doubt, the Swedish wording shall prevail.



## Experts on bacteria

BioGaia, established 25 years ago, is a Swedish innovative health care company and a world leader in probiotics. The products are mainly based on different strains of *Lactobacillus reuteri* and are sold through local distribution partners in some 90 countries.