

BioGaia®

ANNUAL REPORT 2016

Humans and bacteria	10
New organization equipped for growth	16
BioGaia takes a new approach	22

Laying the foundation
for continued growth



CONTENTS

- 02** Company presentation
- 03** Key events during the year
- 04** **MESSAGE FROM THE MANAGING DIRECTOR**
Sales of over 500 million
- 07** **MESSAGE FROM THE CHAIRMAN**
Successful management succession sets the stage for the future
- 08** **INTERVIEW WITH THE MANAGING DIRECTOR**
Long-term focus
- 09** **BIOGAIA HAS A UNIQUE POSITION IN THE MARKET**
- 10** **BACTERIA WITH HUMAN ORIGINS**
Humans and bacteria
- 12** **WIDE RANGE OF PRODUCTS IN SMART PACKAGES**
A world-leader with unique products
- 14** **FLEXIBLE BUSINESS MODEL WITH THREE GLOBAL NETWORKS**
Business model the key to ongoing expansion
BioGaia's global networks
New organization equipped for growth
Employees
- 18** **SCIENTIFICALLY PROVEN CLAIMS**
Strong network of independent researchers
Interviews with researchers
Clinical studies
- 22** **PARTNERSHIP WITH STRONG LOCAL DISTRIBUTORS**
BioGaia takes a new approach
Sales by geographical market
Japan/Brazil/Canada/Germany
- 28** **COMMITMENT THAT EXTENDS FURTHER**
The fight against antibiotic resistance is our greatest contribution
Taking our sustainability commitment to a new level
- 35** **FINANCIAL REPORT**
Financial information and notes

COMPANY PRESENTATION

► **BUSINESS MISSION** BioGaia conducts research and development to provide consumers with clinically proven, health-promoting, patented and user-friendly probiotic products.

► **POSITIONING** 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.

► **VISION** BioGaia's vision is to be a ground-breaking leader in probiotics.

► **STRATEGY** BioGaia's strategy rests on five cornerstones: Growth, Customer Focus, Operational Excellence, Innovation and Sustainability. It is based on the following:

- 1 Conducting high quality clinical studies.
- 2 Developing innovative new products and packaging solutions.
- 3 Providing our partners with effective support, among other things by participating in international medical conferences, hosting seminars, training sales staff and providing marketing materials based on clinical studies.
- 4 Having dedicated and skilled employees who challenge the existing solutions.

► **FINANCIAL TARGETS** see page 42.

► **BUSINESS RISKS AND UNCERTAINTIES** see page 40.

► **BIOGAIA'S CLASS B SHARE** is listed on the Mid Cap list of Nasdaq Stockholm.

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

ANNUAL GENERAL MEETING 2017

Wednesday, 3 May 2017, 5 p.m. at Lundqvist & Lindqvist, Klara Strand, Klarabergsviadukten 90 in Stockholm

This year, the printed annual report will be distributed only to those who have ordered it. Printed copies can be ordered from BioGaia's head office, +46 8-555 293 00, or via info@biogaia.se. The annual report is also published on biogaiaannualreport.com.

The year-end reports, annual reports and quarterly reports are published in Swedish and English.

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

2016

KEY EVENTS DURING THE YEAR

QUARTER 1

- Distribution of the shares in the subsidiary Infant Bacterial Therapeutics (IBT).
- New meta-analysis confirms effectiveness of BioGaia Protectis on colic.
- Meta-analysis confirms effectiveness of BioGaia Prodentis on periodontal disease.

QUARTER 2

- Agreement for the sale of BioGaia Prodentis in Hong Kong.
- Additional meta-analysis confirms effectiveness of BioGaia Protectis on colic.
- Publication of study showing positive effects of BioGaia Prodentis in treatment of abdominal pain in children.

QUARTER 3

- Publication of study showing that BioGaia Prodentis reduces pregnancy gingivitis.
- Agreement for the sale of drops, tablets and oral rehydration solution in Kenya, Nigeria and Ghana.

QUARTER 4

- Major new agreements for the sale of BioGaia's probiotic products in Japan.
- BioGaia makes further investment in MetaboGen.

KEY EVENTS AFTER THE END OF 2016

- Agreement for the sale of BioGaia's products in Thailand.

Sales
SEK **535** million

Operating profit
SEK **199** million

Growth
11%

Operating margin
37%

Number of employees
109

Number of markets
90



“The results of the studies and our solid financial performance, at the same time as we have built a platform for future growth and signed important distribution agreements, demonstrates the strength of our business model, our employees and our products.

AXEL SJÖBLAD,
MANAGING DIRECTOR, BIOGAIA



MESSAGE FROM THE MANAGING DIRECTOR

Sales of over 500 million

Looking back at my first 12 months as Managing Director of BioGaia AB, I see an exciting and successful 2016. With sales growth of 9 percent after foreign exchange effects, we were able to pass the half billion mark and recorded annual sales of SEK 534.7 million. Since the total market for probiotic supplements is growing by an estimated 7 percent annually, this means that we increased our market share despite the fact that our sales to Brazil, one of our most important markets, were low as a result of the inventory build-up in 2015.

OPERATING PROFIT ALMOST SEK 200 MILLION

Our operating profit, excluding the distributed former subsidiary IBT, reached SEK 199.4 million. This is an increase of 14 percent after foreign exchange effects and equal to an operating margin of 37 percent.

In our most important region, Europe, we grew by 22 percent and I'm particularly satisfied with our performance in major markets like Italy, Germany, Spain and France. In Asia we grew by 19 percent and the highlights were sales in Indonesia and the two exclusive distribution agreements that we signed with Kabaya Ohayo Holdings Inc. through our Japanese subsidiary. The first agreement concerns the exclusive rights to sell probiotic supplements with BioGaia's patented strains of *Lactobacillus reuteri* in drugstores, supermarkets and similar outlets. The other agreement is an exclusive license that gives Ohayo Dairy Products the rights to use strains of *Lactobacillus reuteri* in food products. The two agreements will ensure a stable revenue stream in Japan over the next few years. In January 2017 BioGaia signed an exclusive agreement with Abbott for the rights to sell BioGaia's products in the pediatrics and gastroenterology areas in Thailand. Given our positive experiences of working with Abbott in Latin America, we look forward to successful launches in 2017.

In North America we showed healthy growth in both the USA and Canada, but since we are coming from a low level in relation to the potential, we still have a lot of hard work to do before achieving sales we can be happy with. Sales in Rest of the World were down by 24 percent, which was an effect of the inventory build-up in Brazil during 2015. It is therefore encouraging to see that our Brazilian partner Aché is once again ordering

our products and that development in South Africa was strong. In the third quarter we also signed a sales agreement for drops, digestive health tablets and oral rehydration solution in Kenya, Nigeria and Ghana, which was an important step into West and East Africa.

With regard to our partner Nestlé, our excellent collaboration has continued and they have followed the previous trend of buying fewer cultures for infant formula with a very low margin at the same time that royalties from Growing Up Milk for children over the age of one year are rising, which has strengthened our margins and profitability.

INVESTING FOR GROWTH Our operating expenses rose by 16 percent during the year, an increase attributable to marketing activities, personnel expenses and costs for patents and R&D in line with our research initiatives in existing and new areas. We are investing with the goal of optimizing the conditions for future growth through a stronger local presence, better support to our partners and future product launches.

In November we made our third previously agreed on investment in the research company MetaboGen. We have now invested a total of SEK 12 million and our holding amounts to 36 percent. Our investment is of a long-term nature and is aimed at developing the next generation of probiotic products based on in-depth analysis of the microbiome.

EXPANSION OF EXISTING PORTFOLIO Externally, our main focus has been on expanding our existing product portfolio. In the Pediatric area we have striven to optimally utilize our fantastic partner network and we are proud to have grown by 10 percent (excluding foreign exchange effects). It was especially satisfying that the launch of Easy Dropper (our new drop package with improved dosing) was so well received by our partners, which also contributed to our strong performance in Europe. We also grew by 10 percent in the Adult Health area (excluding foreign exchange effects). Here, sales were driven mainly by Protectis digestive health tablets combined with the rollout of Prodentis oral health lozenges and Gastrus digestive health tablets. However, I would also like to point out that our distribution network in Adult Health is still under development. ▶

“We are investing with the goal of optimizing the conditions for continued growth.

VISION

BioGaia's vision is to be a ground-breaking leader in probiotics.

MISSION

BioGaia conducts research and development to provide consumers with clinically proven, health-promoting, patented and user-friendly probiotic products.

STRATEGIC DRIVERS

Growth

- Strong brand
- Develop digital marketing
- Develop partner network
- Increase the number of product launches
- Reduce "time to market"
- Evaluate potential acquisitions

Customer focus

- Strengthen presence in local markets
- Develop strategic partnerships
- Set up new BioGaia Academy (training for doctors)
- Develop network of opinion-leaders
- Launch new website and partner lounge

Operational Excellence

- Strengthen IT platform
- Enhance internal quality assurance system
- Improve internal and external processes
- Create proactive regulatory strategy

Innovation

- Develop long-term pipeline strategy
- Develop IP platform

Sustainability

- Establish BioGaia as a company dedicated to fighting antibiotic resistance
- Focus on chosen sustainability areas

VALUES

My personal engagement 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

► **NEW ORGANIZATION IN PLACE** Internally, we have worked on developing our organization and our operations. On 1 June we presented a new management team that focused on three specific areas during the summer and autumn; getting the new organization in place, presenting a strategy for the next few years and ensuring that this was done without any negative impact on our day-to-day activities and earnings for the year.

Our future strategic priorities will be governed by cornerstones representing five selected areas: growth, customer focus, operational excellence, innovation and sustainability. In each area, we have defined a number of strategic initiatives that will ensure our ability to meet our goals.

A NEW GRIP ON SUSTAINABILITY When it comes to sustainability, I want to especially underline our commitment to fighting antibiotic resistance. The work being done by Peter Rothschild in this area is continuing with undiminished strength and being increasingly integrated into our day-to-day activities. During the year we also reviewed our entire sustainability platform, which resulted in a better structure, priorities and long-term approach.

STRONG RESEARCH RESULTS Our vision is to be a ground-breaking leader in probiotics. Our mission is to conduct research and development to provide consumers with clinically proven, health-promoting, patented and user-friendly probiotic products. We were therefore delighted to see a number of studies of major importance to BioGaia published during the year. I want to especially point out two meta-analyses that confirmed the effectiveness of BioGaia Protectis on colic, a meta-analysis that confirmed the effectiveness of BioGaia Prodentis on gingivitis, a clinical study on reduced abdominal pain in children and a positive study in an area that is new to BioGaia, pregnancy gingivitis.

The results of the studies and our solid financial performance, at the same time as we have built a platform for future growth and signed important distribution agreements, demonstrates the strength of our business model, our employees and our products, and gives us reason to look at the future with continued confidence.


AXEL SJÖBLAD

MESSAGE FROM THE CHAIRMAN

Successful management succession sets the stage for the future

We are summing up yet another excellent year when Axel Sjöblad and Peter Rothschild found their new roles as Managing Director and Group President. The well established business model, in combination with strong studies and products, vouches for continued success.

BioGaia has closed the books on yet another outstanding year. The company completed a smooth and successful management succession and our new Managing Director Axel Sjöblad got off to a flying start with boundless energy and a priority to quickly get acquainted with our key partners and provide them with effective support in their sales efforts. The transition to a role as Group President of BioGaia for our eminent founder Peter Rothschild has gone well and the company is continuing to benefit greatly from Peter's in-depth product and research expertise in the company's core areas.

BioGaia has continued to drive the business model that has so successfully established the company and its excellent reputation in the financial sphere and among both medical professionals and researchers around the world.

THE MAIN GOALS INCLUDE having a close connection between sales and earnings growth, with a healthy operating margin and a generous dividend strategy for the shareholders. It is notable that the company is free from debt and has a strong cash position that not only provides scope for attractive

dividends but also more than satisfies the need for investments in research and development of our current finished products as well as future potential solutions in the core area and new areas of interest.

THE BUSINESS MODEL ALSO INCLUDES a strategy to mainly use *Lactobacillus reuteri* in our products. Several comparative studies show that strains of *Lactobacillus reuteri* are superior to several other bacteria strains that are often included in the competitors' probiotic products.

We are continuing to develop and prioritize the BioGaia brand and this is also an important part of the strategy for future product launches.

FINALLY, BIOGAIA'S EXISTING products have large potential for ongoing geographical expansion and greater awareness and attention. In view of this and the exciting pipeline, I look forward to many more successful years ahead.

DAVID DANGOOR,
BOARD CHAIRMAN,
BIOGAIA



“BioGaia has a strong cash position that more than satisfies the need for investments in research and development of both current and future products.”

Long-term focus

Peter Rothschild, BioGaia's founder and President for 19 years, has been the company's Group President since March 2016. Here he talks about his new role.

“Now I'm mainly focusing on long-term research and development activities. And I'm very involved in BioGaia's central sustainability initiative contributing to reduction of antibiotic resistance.

PETER ROTHSCHILD
FOUNDER AND
GROUP PRESIDENT



What have you been doing for the past 12 months?
Well, my working hours are now down to full time, but it's a whole different situation to not have operating responsibility. Thanks to our successful recruitment of Axel Sjöblad, who is now Managing Director, I have been able to focus on certain projects and long-term research and development activities. I'm also responsible for the associated company MetaboGen and BioGaia's production company TwoPac. And I'm very involved in BioGaia's central sustainability initiatives aimed at contributing to reduction of antibiotic resistance.

What are your views on MetaboGen and TwoPac?
BioGaia owns 36 percent of MetaboGen and I'm Board Chairman there. It's an enormously interesting company that is active in the microbiome area, where they analyze the entire intestinal microflora of healthy people and compare it to that in individuals with various clinical conditions. The idea is then to be able to correct the microflora as a means for curing or preventing disease. You could say that this is the next generation of probiotics, and we want to play an active role in learning and understanding what is happening in this tremendously hot field of research.

TwoPac is a wholly owned subsidiary of BioGaia and manufactures a large share of BioGaia's volume product, the drops, now also in a new package called "Easy Dropper" that has been very well received by the market. TwoPac has GMP status, meaning that it is approved for manufacturing of medicinal products, and a state-of-the-art facility where we also develop new unique and user-friendly packages. Peter Persson, who is President of TwoPac, and his team are doing a fantastic job and I see TwoPac as a strategic asset and a strong contributor to BioGaia's success. Furthermore, we are currently gathering all laboratory operations at TwoPac's excellent facilities in Eslöv.

Tell us more about your initiatives related to antibiotic resistance.
Jan Annwall and I founded BioGaia 27 years ago with an ambition to replace antibiotics in animal feed, so this has been a central issue for us for many years. Now we are working very actively with politicians and other decision-makers to step up efforts when it comes to preventing infections that would otherwise have required antibiotics, and would therefore increase the risk for antibiotic resistance.

But what are you doing in more concrete terms?
We are taking part in the debate through articles and participation in TV programs and podcasts, and we are in discussions with both county councils and members of the Swedish Parliament. In fact, we have been invited to hold a seminar in Parliament. Parallel to this, we are developing a product line that we believe will help to strengthen the immune defence and thereby prevent infections that would otherwise require treatment with antibiotics.

What is happening in BioGaia's long-term research and development?
It's critical for us to plan far ahead, since it takes several years to develop new products. Here, I try to help prioritize when it comes to research projects and in efforts to find replacements for our existing products. This kind of work demands both experience and a lot of creativity, and I think that we are making real progress and have opportunities to break into new areas while at the same time defending our existing positions. I also try to support BioGaia's business development outside the core area, and we have some exciting projects in the works.

Can you tell us more about these?
No, not yet.

And finally, how does it feel not to be President anymore?
It actually feels good, since we've found such an outstanding successor. I'm confident that the company is being managed in the best possible way. But, of course, things are very different today than when I was in the middle of things. One major advantage now is that I have a little more time to devote to my new sport, horseback riding. ●

BioGaia has a unique position in the market

1

BACTERIA WITH HUMAN ORIGINS

2

WIDE RANGE OF PRODUCTS IN SMART PACKAGES

3

FLEXIBLE BUSINESS MODEL WITH THREE GLOBAL NETWORKS

4

SCIENTIFICALLY BASED CLAIMS

5

PARTNERSHIP WITH STRONG LOCAL DISTRIBUTORS

6

COMMITMENT THAT GOES FURTHER

1

BACTERIA WITH HUMAN ORIGINS

BioGaia's probiotic strain *Lactobacillus reuteri* Protectis was originally isolated from the breast milk of a woman in Peru.



Humans and bacteria

Lactobacillus reuteri a bacteria species that has developed in symbiosis with humans through evolution. Now BioGaia is shedding light on this unique phenomenon.

BioGaia has a new pay-off: "BioGaia – Probiotics grounded in evolution. Driven by science." What is the story behind it and does BioGaia really have grounds for these claims?

Around four billion years ago the earth saw the emergence of its first forms of life – microorganisms. Since then, these single-cell organisms have "populated" our planet. The reason they have been able to survive for such an incredibly long time – despite dramatically varying conditions such as volcanic eruptions and ice ages – is their fantastic ability to adapt. Microorganisms, of which bacteria are just one type, can live and multiply under the most varying conditions, like in hot springs and glaciers.

As humans we have around 100,000 billion microorganisms, mainly bacteria, on the outside and inside of our bodies. In other words, we carry twice as many microorganisms as human cells. Most of the bacteria are found in the digestive tract, the gut, where they perform vital functions such as training our immune system and breaking down the food we eat.

The fact is that no mammals have ever existed in nature without their microbiota. The gut flora is now considered to be an organ in its own right and both the amount of bacteria – they weigh around two kilos – and their diversity are important for our survival.

RESEARCH ON BACTERIA and their importance for our health has literally exploded in recent years and new theories and insights are being published at a furious rate. One of the many research teams that have become interested in the bacteria species *Lactobacillus reuteri* is Jens Walter and his colleagues at Alberta University in Canada.

Their research has shown that *Lactobacillus reuteri* is a species of bacteria that has developed a mutualistic relationship with its specific host over

millions of years. By mapping how different strains of *Lactobacillus reuteri* have adapted, Professor Walter has been able to define host-specific strains of *Lactobacillus reuteri* for different mammals such as humans, pigs, rats and horses.

In other words, throughout evolution certain strains of *Lactobacillus reuteri* have made their home in the specific environment that is found in the human gut. In some of us they still reside there today, while most others have insufficient levels and require supplements of *Lactobacillus reuteri*, the probiotic that is "Grounded in evolution".

MANY PROBIOTIC BACTERIA available on the market today have been isolated from plants or animals. Research has shown that bacteria that belong in the human gut "speak the right language" and thus have greater opportunity to exert their mechanisms. *Lactobacillus reuteri* is one of the few probiotic bacteria on the market that have the human digestive tract as its natural habitat. This is one possible explanation why *Lactobacillus reuteri* has shown positive effects in more than 170 clinical studies covering numerous different indication areas.

The studies, i.e. the results of the research conducted on *Lactobacillus reuteri*, are of central importance to BioGaia since all of the company's marketing is based on these findings. The fact is that research is the foundation for everything BioGaia does and stands for. It is BioGaia's greatest source of pride and decisive for our future. In short, there are also grounds for the second part of the new pay-off "Driven by science".

Why then has *Lactobacillus reuteri* been so loyal to its host for such a long time? The answer is found in our mutual dependency. *Lactobacillus reuteri* wouldn't have remained in our intestinal tract if they didn't benefit from it, but most importantly, we wouldn't have kept them if we didn't need them. The law of evolution. ●

BIOGAIA'S NEW PAY-OFF:

Probiotics
grounded in
evolution
Driven
by science

2

WIDE RANGE OF PRODUCTS IN SMART PACKAGES

An attractive package isn't everything. BioGaia's user-friendly products are adapted to the target group's needs.



A world-leader with unique products

2016 marked the passing of ten years since BioGaia launched its own brand. A great deal has happened since then. At that time, the focus was on Protectis drops for infants with colic. Now BioGaia works with both a wider range of indications and more products – for infants, toddlers, children and adults.

The strategy to focus on finished consumer products sold under our own brand has been further sharpened since the launch in 2006 and the goal is to continuously raise the share of BioGaia-branded products. Today there is a growing interest in probiotics around the world and new products are being launched constantly. The market is increasingly competitive and fragmented and the shelves of both pharmacies and grocery stores are filled with probiotics of various types.

This puts new demands on BioGaia's brand and the way in which it is communicated. As a result, in 2016 a whole new brand platform was developed with the aim of strengthening the BioGaia brand and making it the only brand. Consequently, Protectis, Prodentis and Gastrus are no longer brands, only product names. A new graphic design was also created to clarify the product advantages and high-light BioGaia's clean, fresh and appealing design idiom.

The new package design is now being implemented by partners around the world. The goal is for all partners working with the BioGaia brand to have implemented the new design by the end of 2018.

TODAY BIOGAIAS PRODUCTS are sold in around 90 countries. Pediatrics accounts for over 80 percent of total sales and Adult Health for 15 percent. Other revenue accounts for 5 percent.

BioGaia Protectis drops are still the largest product, with sales in some 70 countries. Other important products in the Pediatrics area are Protectis drops with vitamin D, oral rehydration solution and digestive health tablets. The most common areas of use for children and infants are colic, regurgitation, constipation and diarrhea.

In Adult Health, the digestive health tablets and oral health lozenges are the key products. The primary indications here are general digestive health, constipation and, in the oral health area, gingivitis, periodontal disease and candida.

IN 2016 BIOGAIAS LAUNCHED EASY DROPPER. BioGaia Protectis drops in a new user-friendly package. The tube enables more precise dosing and has the same long and stable shelf life at room temperature as the glass bottle. Several countries, such as Finland, Italy and France, have already introduced Easy Dropper and the feedback from the market is very positive. Additional launches are planned for 2017. ●



Easy Dropper is a new user-friendly package for drops in a tube. Here in the new package design.

BioGaia first in the world to launch probiotics such as...

2000
chewable tablets for digestive health

2001
ingredient in infant formula

2002
straws

2004
drops for digestive health

2005
lozenges and chewing gum for oral health

2009
oral rehydration solution

2011
drops for oral health and drops that can be stored at room temperature

2016
drops in a tube (Easy Dropper)

3

FLEXIBLE BUSINESS MODEL WITH THREE GLOBAL NETWORKS

Under BioGaia's umbrella there are networks with suppliers, partners and researchers.



Business model the key to ongoing expansion

Thanks to a successful business model, BioGaia has been able to grow globally with a lean, efficient and agile organization. The business model will also be a key enabler for BioGaia's ongoing expansion.

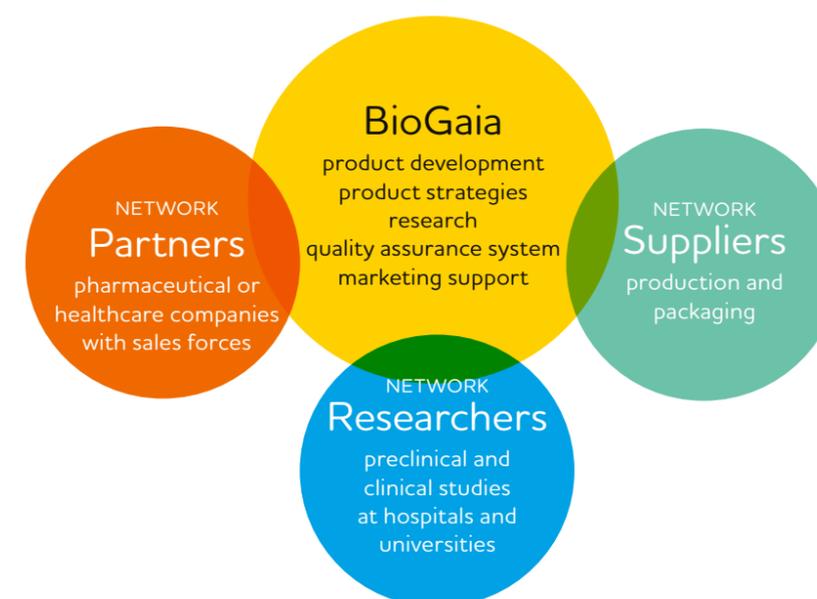
BioGaia's business model is based on three external networks for research, production and distribution.

IN THE RESEARCH AREA BioGaia collaborates with more than 50 research institutions and clinics worldwide. Many of the researchers are among the foremost in their fields. Some of these collaborations have been underway since BioGaia was founded, while others are new.

THE PRODUCTS ARE MANUFACTURED and packaged at six different facilities in Europe and the USA. Through close and long-term collaboration, it is possible to continuously optimize production and

logistics. The suppliers – above all the subsidiary TwoPac – are also important partners for product development, both in creating new products and enhancing existing ones.

THE DISTRIBUTION NETWORK consists of around 60 partners with sales in some 90 countries. Most of these companies have sales representatives who visit doctors and other healthcare professionals. By informing them about the published results of clinical studies, the representatives create interest, knowledge and confidence among doctors who then recommend the products to their patients, who in turn buy the products in pharmacies and similar sales outlets. ●



A map of BioGaia's global networks can be found on the back cover.

New organization equipped for growth

BioGaia has grown steadily over the past years and the plan is to continue on this trajectory. In 2016 a new organization was introduced to both meet the current challenges and seize future opportunities.

The most important task of the HR department is to adapt the company's operations to future needs while at the same time safeguarding BioGaia's status as an attractive employer. These efforts are focused on both attracting new talents and retaining the right expertise.

"At the moment we are in the process of creating a platform for further growth based on the current organization. As part of our sustainability work, we are also adapting our priorities according to the existing legal requirements in areas like equality, diversity and the working environment", says Helen Olsson, Vice President Human Resources at BioGaia.

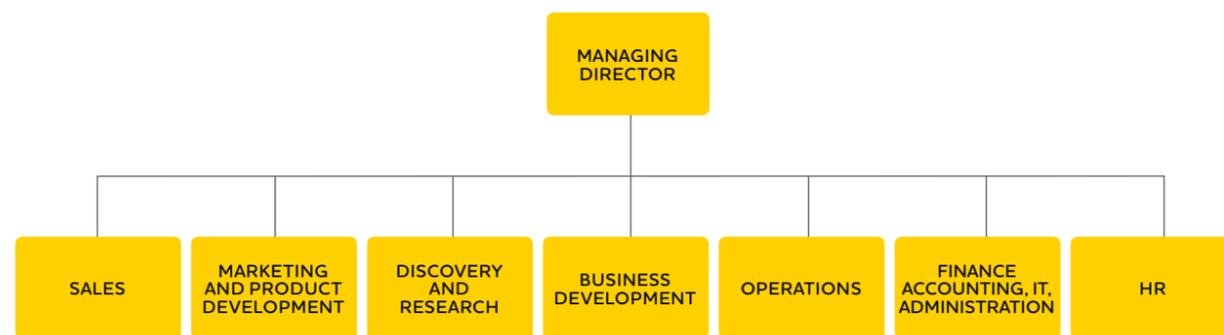
► **NUMBER OF EMPLOYEES** 109 employees, of whom 40 in Stockholm, 31 in Lund, 28 in Eslöv, nine in Japan, one in the USA.

► **AVERAGE TERM OF SERVICE** 7 years (BioGaia AB).

► **AVERAGE AGE** 45 years (BioGaia AB).

► **SICKNESS ABSENCE** 4.25 days.

► **SUBSIDIARIES** TwoPac (TwoPac AB, Two Pac Lab, Two Pac Machine), BioGaia Japan, CapAble, BioGaia Biologics Inc.



"Good relations with our employees is our success factor. Trust in the employees' expertise, personal commitment and willingness to develop are keys to continued success for BioGaia."

HELEN OLSSON,
VICE PRESIDENT
HUMAN RESOURCES



"BioGaia has unique knowledge in the probiotics area that creates opportunities for business development in both our core expertise and new areas. Our digital platform is being significantly upgraded to meet the growing interest in our products from partners, researchers and consumers."

SEBASTIAN SCHRÖDER,
BUSINESS DEVELOPMENT
DIRECTOR & DIGITAL
MARKETING MANAGER



"By understanding the world around us, we can provide our markets with high quality communication, products and knowledge. Through good relations and hard work, we strive to continuously outperform our competitors."

PONTUS KÄLLBOM,
PRODUCT MANAGER



"Enhancing our existing products and developing products for whole new indications in an area is an exciting long-term process that demands structure and patience – but also flexibility!"

FATIMA KACHOUR,
PRODUCT
DEVELOPMENT
MANAGER



4

SCIENTIFICALLY BASED CLAIMS

Many aspects of *Lactobacillus reuteri* and its functions in the body have been mapped out, but there is still a great deal to be explored.

Strong network of independent researchers

BioGaia collaborates with specialists at more than 50 research institutions and clinics that study *Lactobacillus reuteri* at both a preclinical and clinical level.

BioGaia's research network is unique in several respects. Firstly because many of the researchers are global leaders in their fields, and secondly because some of the collaborations have been underway since BioGaia was founded 27 years ago. The company also has a significant breadth that extends across many different indications on both the pediatric and adult side. Furthermore, the aim is not only to establish that *Lactobacillus reuteri* works, but also how and why. For that reason, there is also preclinical research, i.e. research conducted in a laboratory with the help of different models.

The objective is for all research to conform to the highest possible scientific standards. Regular publication of data on *Lactobacillus reuteri* in medical journals is a testimony to strong scientific relevance and high research quality.

ALREADY BEFORE BIOGAIA was founded, intensive research on *Lactobacillus reuteri* was being conducted at places such as the Swedish University of Agricultural Sciences (SLU) in Uppsala. There, Sven Lindgren and Walter Dobrogosz studied how *Lactobacillus reuteri* was able to inhibit pathogenic microorganisms such as *E. coli* and *Salmonella*.

Stefan Roos then moved on to preclinical research by determining how *Lactobacillus reuteri* binds to the intestinal mucous membrane. Stefan defended his thesis on this in 1999 and he still works part time as a researcher at SLU, but for the past three years he has also been employed by BioGaia, where he is responsible for coordinating preclinical research.

“OVER THE YEARS, many aspects of *Lactobacillus reuteri* and its functions in the body have been mapped out, although numerous questions still remain to be answered,” says Stefan. “For instance, we know that *Lactobacillus reuteri* in preclinical models has a beneficial effect on gut motility, reduces perceived pain intensity and can prevent the intestinal mucous membrane from leaking bacteria and toxic substances. These so-called mechanisms of action most likely lie behind the clinical effects shown by *Lactobacillus reuteri*.

“In other words, preclinical research gives us knowledge about how the probiotic bacteria work, which is important for several reasons. First and foremost, this knowledge can generate ideas for how to develop more effective products, but it also adds to the credibility of the products,” says Stefan. ●



“Preclinical research gives us knowledge about how the probiotic bacteria work.

STEFAN ROOS,
ASSOCIATE PROFESSOR
AND SENIOR
MICROBIOLOGIST,
BIOGAIA

14,800

14,800 individuals of all ages have taken part in clinical studies with BioGaia's human strains of *Lactobacillus reuteri*.

173

173 clinical studies have been carried out to date. Results have been published in 146 articles in scientific journals and 12 doctoral theses (March 2017).

18

During the year, 18 clinical studies were published in different indications areas.

PRECLINICAL RESEARCH

Lactobacillus reuteri is polite and friendly, like a good neighbour

Professor James Versalovic at Baylor College of Medicine in Huston, Texas, became interested in *Lactobacillus reuteri* already back in 2000. Here, he talks about his research.

What is it that makes *Lactobacillus reuteri* so interesting?

Lactobacillus reuteri is fascinating because it's a bacterium that occurs naturally in many species of birds and mammals, such as humans. It is an adept colonizer that seems to be friendly to its microbial neighbours. Like a polite and kind friend, *Lactobacillus reuteri* maintains the conversations between host and bacteria without invading the host or dominating other microorganisms. In short, *Lactobacillus reuteri* is a good neighbor, never a bully.

What is the most exciting discovery about *Lactobacillus reuteri* that you and your team have made?

It was the discovery that *Lactobacillus reuteri* generates histamine and that this histamine can suppress intestinal inflammation in mammals.

What are you and your team focusing on at the moment?

We are studying metabolism via probiotic bacteria and, for example, how histamine can modulate the functions of the immune and nervous systems.

What answers do you hope to find in the future?

We hope to be able to select strains of *Lactobacillus reuteri* that suppress chronic gut inflammation. We also want to find out if it is possible to use a combination of dietary ingredients to improve the effectiveness of probiotics, such as *Lactobacillus reuteri*, to promote health. ●



“We hope to be able to select strains of *Lactobacillus reuteri* that suppress chronic gut inflammation.

JAMES VERSALOVIC, PROFESSOR, BAYLOR COLLEGE OF MEDICINE, HUSTON, USA



META-ANALYSIS PUBLISHED

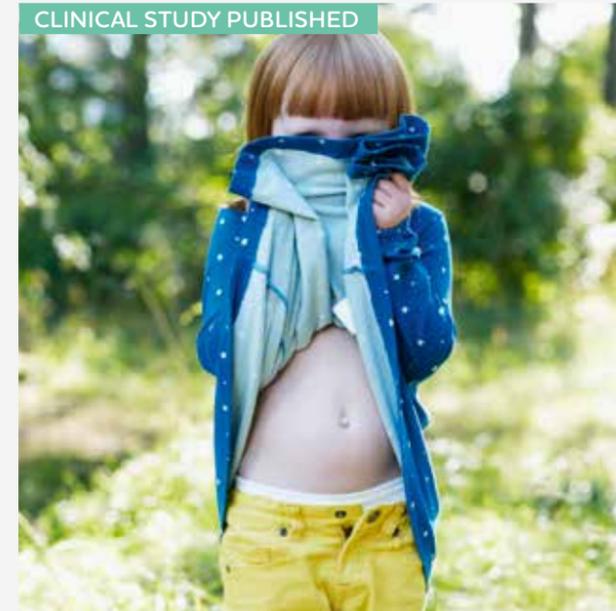
Patients with periodontal disease helped by Prodentis

Olivier Huck at the Department of Periodontology, Dental Faculty, University of Strasbourg in France.

A systematic review of probiotics as an adjunct to standard treatment of periodontal disease has confirmed the effectiveness of *Lactobacillus reuteri* Prodentis. Prodentis proved to be the only probiotic that was effective for patients with chronic periodontitis.

The meta-analysis was the first for probiotics in periodontal treatment. Only four studies, all with *L. reuteri* Prodentis, met the criteria for inclusion in the systematic review. Since no other probiotic products qualified, the analysis concluded that *L. reuteri* Prodentis is the only effective probiotic.

The studies show that Prodentis gives significant pocket depth reductions in moderate and deep dental pockets when used in combination with standard treatment of chronic periodontitis. According to the authors, the results are similar to those noted for other types of adjuncts to treatment of periodontitis, such as systemic antibiotics. ●



CLINICAL STUDY PUBLISHED

BioGaia's probiotic effective in treating abdominal pain in children

Zvi Weizman, Professor at the Pediatric Gastroenterology and Nutrition Unit, Soroka University Medical Center, Faculty of Health Sciences, Ben-Gurion University, Beer-Sheva, Israel.

Tell us about the background for the study.

Stomach pain is common among children and often affects the child's daily life, for example through anxiety and school absenteeism. As a pediatric gastroenterologist I often meet these children and since there hasn't been any effective treatment, I and my research colleagues wanted to test a well documented probiotic.

What did the results show?

The study confirms earlier results with *L. reuteri* Protectis. The number of pain episodes was almost halved among the children supplemented with Protectis. The intensity of the pain was also significantly reduced in the probiotic group compared to placebo, and this effect persisted during the follow-up period.

What conclusions can you draw from the study?

According to the results, physicians facing the common and challenging problem of functional abdominal pain in children can suggest *L. reuteri* Protectis as an easy way to relieve pain intensity and reduce its frequency. Protectis is reliable, effective and has no side effects. ●



CLINICAL STUDY PUBLISHED

Oral health probiotic reduces pregnancy gingivitis

Ulrich Schlegelhauf, Professor at the Department of Periodontology, University Hospital Würzburg in Germany.

Tell us about the background for the study.

Pregnancy causes hormonal changes that increase the risk of developing gingivitis (inflammation of the gums). Statistics show that between 35 percent and 100 percent of all pregnant women experience pregnancy gingivitis. *L. reuteri* has shown good results in a large number of clinical studies and on several different indications, but had not yet been tested on this patient group.

What did the results show?

Both inflammation and plaque were significantly reduced in the pregnant women who were supplemented with *L. reuteri* and the study thus shows that lozenges containing *L. reuteri* can be an effective complement in controlling pregnancy gingivitis.

What conclusions can you draw from the study?

Brushing, flossing and seeing a dentist during pregnancy are important for oral health and may decrease the risk of adverse pregnancy complications. Our study shows that lozenges with *L. reuteri* may be an additional valuable tool in the control of pregnancy gingivitis. ●



5

PARTNERSHIP WITH STRONG LOCAL DISTRIBUTORS

Although most of the partners have pediatricians as their primary target group, BioGaia has products for all ages.

BioGaia takes a new approach

BioGaia's products are available at drug stores and pharmacies around the world. To get closer to the markets, BioGaia will open two new regional offices.

BioGaia's products are sold and marketed by a global network of partners. Over the years the partner network has grown, but so has the need for closer collaboration with the local distributors. The partners require more support and assistance, for example in matters related to sales, marketing and research.

"Here, we have taken a new approach and will open local BioGaia offices in Miami and Singapore", says Urban Strindlöv, Executive Vice President and Sales Director at BioGaia.

The Miami office will open in 2017 and the plan in Singapore is to have an office in place by the beginning of 2018. In Latin America we are already well established, at the same time that the USA is the world's largest market for probiotics. In view of that, the Miami office is strategically located and can serve as a base for both North and South America. In the same manner, Singapore will function as a hub in Asia, which is a market with strong growth and potential for BioGaia.

"Another advantage of these locations is that they are attractive places to work. This is important", says Urban. "We want to attract skilled and talented people who can both convey the BioGaia 'spirit' and work independently in their regions."

Regional offices are a whole new step for BioGaia. The offices will be focused on supporting the local markets with sales, marketing and research. The Americas and Asia are regions where BioGaia has large and important partners and several ongoing research collaborations.

"Being closer to our partners will facilitate relations and make it easier to cooperate," says Urban. "We will be able to reduce long business trips and different time zones."

"Europe is BioGaia's most established market, where we have the greatest geographical penetration, good coverage in many countries and longstanding

partnerships in the majority of markets. Overall, Europe accounts for around 65 percent of BioGaia's sales. Italy, Spain, France, Germany and Turkey are markets where we have a strong position today."

STRATEGICALLY IMPORTANT PARTNERSHIPS IN EUROPE.

Italy is one of the world's largest markets for probiotics and is extremely competitive, with more than 450 different probiotic products. "In 2016 one of BioGaia's distributors was acquired by Recordati, which is also our distributor in Spain and Portugal, a move that has made Recordati an even more strategic partner for us," says Urban. "In Germany, our collaboration with InfectoPharm has been deepened and we are seeing an increased focus on BioGaia by the company. Their positioning toward midwives has proven highly successful." (Read more on page 27).

"We also have a strong position in France but believe there is further growth potential, particularly for our pediatric products. Here we need to support our partner PediAct, which is a relatively small but focused company."

LATIN AMERICA GOING STRONG.

In Latin America BioGaia has continued its excellent partnership with Aché in Brazil (read more on page 26). For many years Abbott/Recalcine has been BioGaia's partner in a number of Latin American countries, such as Chile, Peru and Colombia. In 2016 Abbott also launched BioGaia's products in Mexico, a country with a large population and many children that has the potential to become an important BioGaia market. At the end of 2016 an agreement was signed with Abbott for Thailand, thereby expanding the partnership to outside Latin America. In total, the partnership with Abbott now covers 13 countries.

BUILDING NETWORKS IN THE USA. "In the USA we have launched a long-term initiative ►

“The regional offices will be focused on supporting the local markets with sales, marketing and research.

URBAN STRINDLÖV,
SALES DIRECTOR
BIOGAIA



to build a network of opinion-leaders in the pediatric area," says Urban. "We are doing this in collaboration with one of our partners, Everidis, and is part of the strategy to strengthen our brand. We also have long-term ambitions to get more clinical studies performed in North America. Much of the preclinical work on BioGaia's patented strains of reuteri is already being carried out in the USA."

SEVERAL NEW AGREEMENTS IN ASIA. In December 2016 BioGaia Japan signed major agreements with one of the leading confectionery and dairy companies in Japan, Nippon Kabaya Ohayo Holdings, whose subsidiary Kabaya Foods will market BioGaia's products to consumers at drug stores, supermarkets and similar outlets. Another subsidiary, Ohayo Dairy, will use BioGaia's probiotic strains in beverages and dairy products.

"Expectations for the collaboration with Kabaya Ohayo are high and it will be exciting to follow the developments in Japan," says Urban (read more on page 26).

Indonesia is one of the biggest markets for probiotics in Asia and the focus there is on treatment of diarrhea. Together with the partner Interbat, the use of BioGaia's products is being widened to also include colic and other digestive problems.

China is a complex market in terms of the regulatory environment, with time-consuming regulatory procedures that take several years. While waiting for the desired registration there

are limited opportunities to market the products, which is reflected in sales. There is currently a study underway in China on infants with colic.

"One of many bright spots in Asia is that after several years of registration work, sales have now commenced in the Philippines. Our partner Unilab has a strong position and the successful launch of the tablets will be followed by the drops later this year," says Urban. "Hong Kong, on the other hand, is a market where we have been active for many years and which has the highest per capita sales of tablets in Asia. In 2016 we signed an agreement with a new partner, Biowelltech, for sales of our oral health products."

BioGaia's relationship with Nestlé began in 2008 and today Nestlé is BioGaia's largest partner. The areas of collaboration are mainly related to infant formula and Growing Up Milk for children over the age of one year, where Nestlé uses bacteria culture of *L. reuteri* Protectis in its products. Growing Up Milk was launched in 2014 and now generates substantial revenue for BioGaia. The close collaboration between the companies also includes research and product development.

STRENGTHENING THE BRAND "We have a clear and explicit ambition to strengthen our brand in the countries where the products are sold under the BioGaia brand," says Urban. "At the moment, this work is focused on supporting a few strategic partners, including PediAct in France and Everidis in the USA." ●

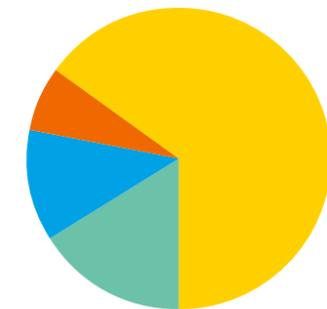
“The marketing is targeted toward doctors and other healthcare professionals, and the most important advantage that is pointed out is the scientific proof of the products' effectiveness.



Europe is still the largest market by a wide margin, accounting for 65 percent of sales. In 2016 sales in this region rose by 22 percent compared to the previous year.

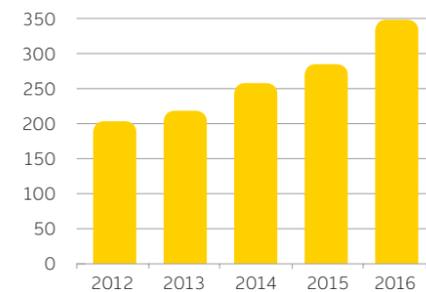
In Rest of the World, on the other hand, sales declined by 24 percent as a result of low sales to Brazil. However, Rest of the World remains BioGaia's second largest market. Sales in Asia increased by 19 percent during the year and in the USA and Canada by 14 percent compared to 2015.

SALES BY GEOGRAPHICAL MARKET

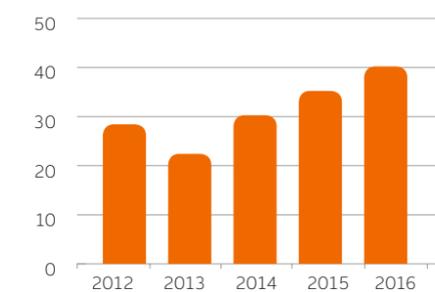


- Europe 65% (59)
- Rest of the World 16% (23)
- Asia 12% (11)
- USA and Canada 7% (7)

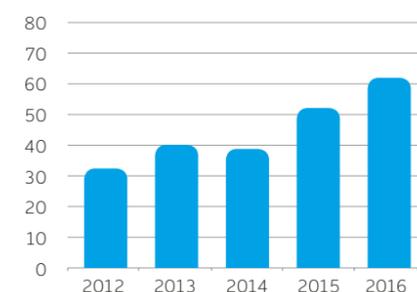
SALES IN EUROPE, SEK M



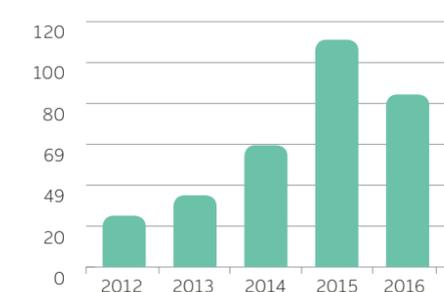
SALES IN THE USA AND CANADA, SEK M



SALES IN ASIA, SEK M



SALES IN REST OF THE WORLD, SEK M



JAPAN

Partners: Subsidiary BioGaia Japan, ADI.G Asano, Nippon Kabaya Ohayo Holdings Inc., Alfresa, Erina

Population: 127 million

Births per year: 1 million

Maturity level: Probiotics in dairy products are very well known, but as dietary supplements they are still relatively unknown.

Products: BioGaia Protectis, BioGaia Prodentis, BioGaia Gastrus

JAPAN IS HOME to Asia's largest probiotics market. The market for dairy products with probiotics is worth around SEK 6.5 billion annually, while that for probiotics as dietary supplements still has a large potential. BioGaia is one of few players here and is benefitting from having scientifically documented products.

Among probiotic dietary supplements for oral health, BioGaia Prodentis is the market-leader. The market for dental implants is vast and since many patients experience problems, such as peri-implantitis, they have recently started to market Prodentis for this indication. Pregnancy gingivitis is another new and interesting indication.

In the pediatrics area, BioGaia Japan is currently building up the colic market in Japan by calling attention to the catastrophic consequences when parents shake screaming infants. This will now be communicated to pediatricians and gynecologists together with the "solution", BioGaia's drops. Here BioGaia Japan are collaborating with two prominent opinion-leaders in the pediatrics field.



“Thanks to our early collaboration with Japanese dentists and researchers, we are the market-leader in oral health. BioGaia Japan is a pioneer, which is an advantage when we launch Prodentis in new markets. There is enormous potential in the pediatrics area and I look forward to building this segment with our Japanese team.

JONAS WEIMER, VICE PRESIDENT SALES APAC



“The past year has seen a powerful focus on Kabaya Ohayo Holding. For BioGaia Japan, this partnership is vital for ensuring long-term profitability. It also gives us the resources to further develop our business in both the oral health and pediatric areas.

KEITARO NOMURA, MANAGING DIRECTOR BIOGAIA JAPAN

BRAZIL

Partner: Aché

Population: 200 million

Births per year: 3 million

Maturity level: Probiotics are relatively well known as an effective treatment for diarrhea, but are unknown in other areas of use.

Products: Colikids, ProVance

BRAZIL IS LATIN AMERICA'S largest probiotics market, worth close to SEK 900 million, and there are around 30 different products (dietary supplements and pharmaceuticals), all with a primary focus on diarrhoea. Eleven new products were launched in 2016 and the market is showing double-digit growth.

The use of probiotics for other digestive problems, such as infantile colic, constipation and stomach pain, has been relatively unknown until now. Since the launch of BioGaia's products just over two years ago, Aché is working to expand the market with these "new" indications. Both Colikids and ProVance are among the three most widely prescribed products in their respective areas of use.

The regulatory situation in Brazil has led to delays of the launches of several BioGaia products, but plans to expand the collaboration are well established by both parties.



“Working with Aché is not only tremendously rewarding but also a learning experience. Their professionalism, combined with enthusiasm and passion, makes it impossible not to want to work closely with them and share in their fantastic successes.

CRISTIÁN CONTRERAS, VICE PRESIDENT SALES AMERICAS



“With *Lactobacillus reuteri* Protectis, Aché has had the advantage of introducing the concept of probiotics, with various strains and their different attributes, to doctors in Brazil. BioGaia is also an excellent partner that gives us full support. It's inspiring to see how our team works with such a focus on achieving success.

STEPHANI SAVERIO, HEAD OF INNOVATION & BUSINESS DEVELOPMENT, ACHÉ

CANADA

Partner: Ferring

Invånare: 35,4 million

Partner: Ferring

Population: 35.4 million

Births per year: 393,000

Maturity level: Probiotics are very well known, particularly for treating antibiotic-related problems, IBS and infantile colic.

Products: BioGaia Probiotic Drops, BioGaia ProTectis Digestive Health

THE CANADIAN MARKET for probiotics is worth more than SEK 1.3 billion and is growing by 8 percent annually. The most important areas of use are general digestive health, but diarrhea, IBS and the side effects of antibiotics are other common indications.

All "natural health" products must have their health claims approved by Health Canada, which benefits BioGaia/Ferring and also vouches for continued growth. In 2016, a full 18 health claims were approved – far more than for the competitors – thanks to the large number of high quality clinical studies with *L. reuteri* Protectis.

Ferring's marketing is mainly targeted to pediatricians, but they also have web-based consumer marketing. The company aims to become stronger in Pediatrics but also to advance its position in Adult Health. All of BioGaia's products are carried by the major drug store chains and there is a high level of knowledge about BioGaia among healthcare professionals.



“The future looks very bright for BioGaia in Canada. Together with Ferring we are accelerating the pace and moving full steam ahead.

JOAKIM ANNWALL, REGIONAL SALES DIRECTOR USA AND CANADA



“The BioGaia portfolio will expand beyond the segment for infant colic, to toddlers, children and teens. We look forward to improving life for Canadians and making this journey with our colleagues at BioGaia.

MIKE SECKLER, GENERAL MANAGER AND PRESIDENT, FERRING CANADA

GERMANY

Partner: InfectoPharm

Population: 80 million

Births per year: 680,000

Maturity level: Significant market that is still growing

Products: BiGaia Tropfen, BiGaia Vitamin D3, BiGaia Kautabletten (launched in 2017)

GERMANY IS A "prescription market" when it comes to children. The majority of products are classified as pharmaceuticals, are prescribed by doctors and are subsidized by healthcare insurance. The colic market is dominated by several different drugs containing simethicone and a few products with cumin.

InfectoPharm, with its subsidiary Pädia, is Germany's leading pharmaceutical company in the pediatric area. They have a large portfolio with successful products in nearly all pediatric indications. The business model is based on direct contact with doctors through a large number of local seminars. Twice a year, they also host symposia that gather more than 3,000 participants. They have no sales force but work with direct marketing.

The subsidiary Pädia took over marketing of BioGaia products at the end of 2015. Pädia is also an umbrella brand for InfectoPharm's OTC drugs and products.

Despite tough competition, BiGaia Tropfen has secured a position as one of the leading colic products on the market. In 2017, BiGaia tablets will be launched.



“It's a pleasure to work with InfectoPharm and see how our sales are growing continuously throughout Germany, a country that is at the core of the European economy and an extremely important market for us.

KARIN KNIBERG, REGIONAL SALES DIRECTOR NORTH AND EASTERN EUROPE



“We are proud to be part of the BioGaia family and look forward to expanding our portfolio and continuing to build the probiotics market with the help of BioGaia's innovations.

DR. MARKUS RUDOLPH, MANAGING DIRECTOR, INFECTOPHARM & PÄDIA

6

COMMITMENT THAT EXTENDS FURTHER

BioGaia is stepping up its efforts in the fight against one of the greatest global threats to public health.



The fight against antibiotic resistance is our greatest contribution

BioGaia's efforts to combat antibiotic resistance are the company's primary focus in the sustainability area. Peter Rothschild explains how BioGaia aims to contribute on several fronts.

Antibiotic resistance is a hot topic. Everywhere, we can read about the catastrophic consequences that can become a reality if antibiotics stop functioning as the effective treatment they have been for close to a century. Antibiotics are a basic fundament of modern health-care, and when they no longer work we will be thrown back to 1927, the year before penicillin was discovered. A minor wound can then become a serious infection that is impossible to cure, and major surgery may have to be cancelled. The list of potential consequences is endless.

Already today, some 25,000 Europeans are dying every year as a result of antibiotic resistance. This is a figure that is as alarming as it is shocking, but also one that will unfortunately increase dramatically unless more is done to stop it.

Sweden is a frontrunner in this area and one of the few countries in the world where the problem of resistant bacteria is still comparatively minor. We were early to take action on both the human and animal side. We have since long had an effective system for spreading information and our already relatively low use of antibiotics has continued to decline. And yet, this is not enough. Alongside the hunt for new antibiotics, we must work on several fronts simultaneously – just as the bacteria are doing.

Without a doubt, the work being carried out by Strama (the Swedish strategic program against antibiotic resistance), the Swedish Public Health Agency and ReAct is incredibly important, but more needs to be done. I'm convinced that we also need to devote ourselves to more preventive measures. These can include utilizing the available technologies, for example to reduce the risk for infection in ►

“Our greatest contribution to sustainable development is our work to combat antibiotic resistance.”

PETER ROTHSCHILD,
GROUP PRESIDENT
BIOGAIA



“We need to stop using antibiotics where they are not needed”

By preventing infections, we can reduce the need for antibiotics.

- Strengthen our immune system with the help of minerals, vitamins, probiotics, sleep, exercise and reduced stress.
- Targeted initiatives to train healthcare professionals.
- Use the available techniques to reduce the risk for infections in connection with surgery and hospital visits.



☛ Much of what we take for granted in modern healthcare requires antibiotics.

connection with surgical procedures or rapid diagnostics to identify which antibiotic will work best on a patient's infection. They can also involve strengthening our immune system by increasing our intake of minerals, vitamins and probiotics. This has been shown in several studies with both *Lactobacillus reuteri* and other substances, such as vitamin D. It has also been demonstrated that there is a clear connection between a strengthened immune defence, fewer infections and lower use of antibiotics.

By adding this to the arsenal of measures we already know can prevent infections, we can reduce the need for antibiotic treatment. And by doing so we can avoid allowing bacteria to develop a resistance so that antibiotics become ineffective. Antibiotics can then be saved for the situations where they are truly needed. To achieve this we need targeted educational programmes for doctors, nurses and other healthcare professionals about scientifically proven methods to boost the immune defence. The healthcare sector also needs to become more active in informing the public

about how to strengthen their ability to fend off infections.

BioGaia is actively participating in the debate through articles and participation in TV programs and podcasts. We are also talking to politicians at the county and parliamentary level and other decision-makers to raise the stakes when it comes to preventing infections that would otherwise have required antibiotics. On 5 April we will hold a seminar in the Swedish Parliament to highlight this issue. We also have a newsletter and a Twitter account that spread knowledge about new findings.

Antibiotic resistance affects every one of us. At BioGaia, we are stepping up our efforts to combat one of the greatest global threats to public health. ●

Curious about following our work on antibiotic resistance?

Follow us on Twitter, @ResResistance, and subscribe to our newsletter, news@biogaia.se.

ANTIBIOTICS IN BRIEF

In 1928 the Scottish scientist Alexander Fleming discovered that a fungus growing in his laboratory had destroyed some of the bacteria he was studying. He named the substance it released penicillin, but didn't fully understand its effect. In 1945, other scientists found a cost-effective method for producing large quantities of penicillin and industrialized production was started. Several other effective antibiotics were soon discovered.

HOW RESISTANCE IS DEVELOPED

Antibiotics are drugs that are used to kill bacteria that cause infections. But every time an antibiotic is used, some of the bacteria will survive. Over time, these "survivors" multiply and form a new strain that is resistant to the antibiotic.

The problem is the same for every type of antibiotic that has been developed – the more it is used, the faster the emergence of new bacteria that are resistant to it.

To make matters worse, the number of new antibiotics in the development pipeline has fallen sharply. And at the same time, several so-called superbugs are thriving and spreading around the world.

WHAT IS ANTIBIOTIC RESISTANCE?

Antibiotic resistance is the ability of pathogenic bacteria to resist the effects of antibiotics. The pathogenic bacteria have then become

resistant to the drug that is intended to kill them.

A human cannot be antibiotic-resistant but a human can carry antibiotic-resistant bacteria. Resistant bacteria can be spread between humans, animals and in the environment.

COMMON CAUSES OF ANTIBIOTIC RESISTANCE

- Overuse of antibiotics
- Failure by patients to complete a course of antibiotics
- Overuse of antibiotics in animal agriculture
- Poor infection control in hospitals and clinics
- Inadequate sanitary conditions

"LAST LINE OF DEFENCE" NOW BREACHED?

Colistin was developed in the 1950s and belongs to a class called polymyxins. The reason doctors avoid using this antibiotic on humans is that it can be toxic to the kidneys. As a result, resistance to colistin has developed more slowly than to other antibiotics.

However, colistin is used extensively in agriculture to promote growth and to prevent disease among the animals. In China alone, 12,000 tonnes of colistin are used annually in agriculture.

Taking our sustainability commitment to a new level

A materiality analysis has laid the foundation for BioGaia's ongoing sustainability work. We have a clear strategy and have set the goals and priorities for 2017. Our sustainability initiatives have been given structure and a long-term approach.

In 2016 BioGaia reviewed its sustainability work. In connection with this, a materiality analysis was carried out to define the future strategic focus and to ensure compliance with the new legislation on non-financial reporting and board diversity. "One of the main goals of the project was to better integrate sustainability work into our core activities," says Eva Nelson, Communications and Sustainability Manager at BioGaia. "Another was to improve our communication about what we are already doing."

KEY STAKEHOLDER OPINIONS IMPORTANT
The first part of the project consisted of a market analysis to identify the global megatrends that are

shaping the world and how these could affect BioGaia (read more on page 34). This also included a review of international initiatives and policies and benchmarking against competitors in the industry.

Surveys and interviews were carried out with a number of key internal and external stakeholders who had the opportunity to give their views on BioGaia's challenges and opportunities from a sustainability perspective. To increase the understanding of what external stakeholders consider to be BioGaia's most important focus areas, they were asked to take a stand on a number of specific aspects and evaluate the importance of corporate social responsibility for BioGaia's future.

KEY ISSUES FOR THE STAKEHOLDERS

As part of the materiality analysis, in-depth interviews were conducted with a number of stakeholder groups such as investors, shareholders, board members and suppliers.



"It's crucial that sustainability efforts are genuine and well anchored in every part of the company, that they are seen as part of BioGaia's strategic business framework."
BRIT STAKSTON, BOARD MEMBER OF BIOGAIA



"Gender equality, both within the Board and in the company as a whole, is fundamental for BioGaia. Today this factor is extremely important in making a company attractive."
SEBASTIAN JAHRESKOG, SHAREHOLDER IN BIOGAIA



"BioGaia has a good understanding of and requires a sustainable production of the company's products."
CARLOS GARCIA, MANUFACTURING MANAGING DIRECTOR, FARMASIERRA



"Ethical aspects are particularly important given the large number of unscrupulous players in the industry."
LOUISE UNGERT, HEAD OF CONSUMER AND ENVIRONMENT, STOCKHOLM CONSUMER COOPERATIVE SOCIETY

SELECTED STAKEHOLDER GROUPS:

Shareholders, investors, suppliers, board members, distribution partners (customers), special interest groups and academia (researchers).

The final part of the project was an internal workshop with BioGaia's management. The members of the management team discussed the same issues as the external stakeholders and then ranked the various aspects.

"When the results of the external and internal analyses were combined, it became clear that everyone was essentially in agreement. Both internal and external stakeholders ranked sustainability work as highly important and there was also far-reaching consensus about which issues were the most central for BioGaia," says Eva. "Some of the issues that most people agreed on as being the most significant for BioGaia to handle and communicate were the safety and quality of the products, that purchasing is carried out in a responsible manner, that the company has a sustainable supply chain, and how BioGaia contributes to global health."

THE NEXT STEP. The most important aspects have been categorized in four strategic focus areas:

- products and production
- supply chain
- attractive employer
- contribution to global health.

For issues such as conducting ethical and responsible marketing, having policies for bribery and compliance with laws, BioGaia has been found to already have established internal rules and policies, and these have therefore ended up outside the focus areas.

In order to set realistic goals for 2017, BioGaia's management further prioritized the most material aspects in each of the strategic focus areas.

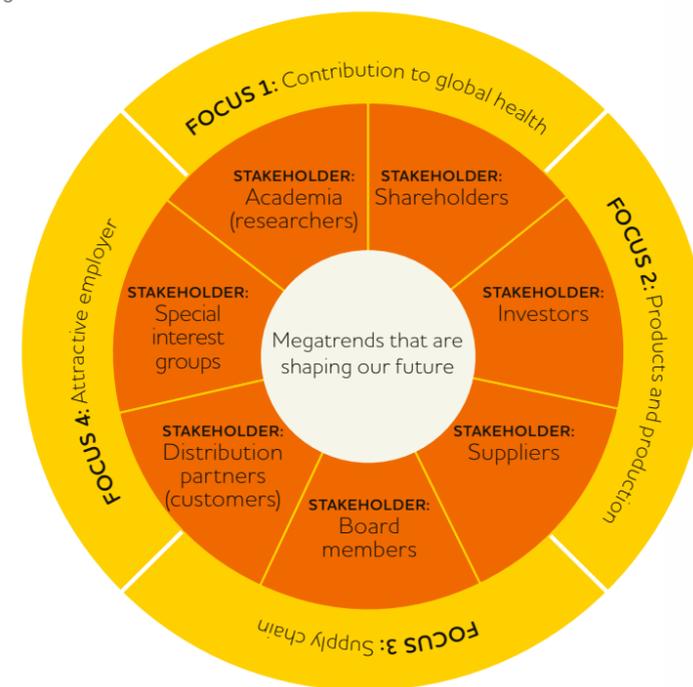
"For the aspects that were given highest priority, we will now break these down into greater detail, set goals for them and work with them during the year," says Eva. "Other issues in the strategic areas will be prioritized in the next few years, but there is no detailed plan for these at present."

SUSTAINABILITY PART OF CORE OPERATIONS

"The materiality analysis has helped us define the most significant aspects for being a sustainable company. Fortunately, it turned out that virtually all these issues were found within our core operations, which was one of our ambitions when we started the project. Now we know that we focus on and communicate issues that are important to both us and our stakeholders. These efforts must naturally be upheld and continuously evaluated, but now we have a platform to work from, which is a big step forward," says Eva. ●

"Our sustainability work is long-term in nature and focused on four strategic areas."

EVA NELSON,
COMMUNICATIONS
MANAGER, BIOGAIA



In 2016 BioGaia mapped the megatrends that affect the company, ranked the stakeholders' key issues and prioritized which of these issues to focus on moving forward.



Megatrends that are shaping our future

1 DEMOGRAPHIC AND SOCIAL CHANGES

A full 99 percent of growth in the global population over the next four years will be concentrated in regions that are classified as less developed, such as Africa, Asia (excluding Japan), Latin America and the Caribbean. Birth rates vary between Europe's low 1.6 children per woman to 4.6 in Africa.

Around the world there is a growing health awareness and industries like ecological food and dietary supplements are expected to continued expanding rapidly. Consumers are also increasingly seeking information about preventive healthcare, on the Internet and through other channels.

2 SHIFT IN PURCHASING POWER

The focus for global growth has shifted. For example, China overtook the USA as the world's largest economy in terms of purchasing power parity (PPP) already in 2014. Several of the other so-called E7 countries, which aside from China include India, Brazil, Russia, Mexico, Indonesia and Turkey, will also climb up the value chain.

Today the E7 countries are graduating three times as many academics as in G7. Eventually, more and more of the major multinational corporations will be led by people from emerging markets, which will among other things affect the corporate culture.

3 CLIMATE CHANGE AND DEPLETION OF RESOURCES

Today's economic development means that we are consuming resources beyond the planet's capacity to cope. The consequences of this include climate change and depletion of resources.

Between 2030 and 2050, climate change is expected to cause an estimated additional 250,000 deaths per year as a result of malnutrition, malaria, diarrhea and heat stress.

Decision-makers will most likely continue to be driven by short-term goals, and companies will therefore play a leading role in managing the sustainability challenges. At the same time, organizations must become more flexible in order to handle the changes arising from unpredictable climate and environmental policy.

Stakeholders will increasingly judge companies from a sustainability perspective. For example, consumers want to know about product origins and whether they have been produced in an ethical and sustainable manner. The ability to build and manufactured trust among different stakeholder groups will be decisive for a company's success.

4 TECHNOLOGICAL BREAKTHROUGHS

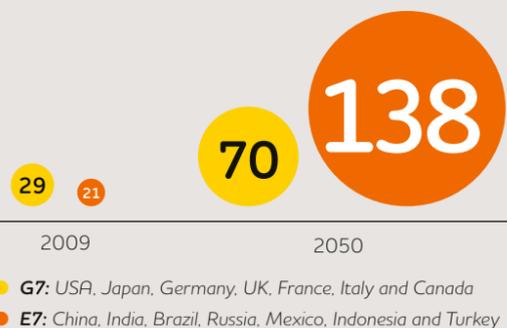
Technological innovation is at the heart of the changes that are taking place in many sectors. Above all in emerging markets, new technology is giving rise to major changes.

The Internet, mobile phones, computer analysis and cloud-based services make it possible for companies to get closer to their customers and take on a more "advisory" role.

In the healthcare sector there is already a wide range of digital tools for selection, development and testing of new products. Another trend is "big data", which can be used for example to gather and cross-check health information from different registers to better understand illnesses, develop new methods and more efficiently allocate resources at the right time and to the right patient.

Apps and "wearables" enable patients to keep track of their health wherever and whenever, which is among other things freeing up hospital beds. By the same token, healthcare professionals can be available to patients regardless of where they are.

GDP GROWTH IN G7 COMPARED TO THE E7 ECONOMIES BETWEEN 2009 AND 2050 (IN USD TRILLIONS)



By 2050, a dramatic shift in purchasing power is expected to take place from the G7 to the E7 economies.

Financial Information and Notes 2016



Table of contents

37 Administration report

- BioGaia
- Key events of 2016
- Key events after the end of the financial year
- Financial performance in 2016
- Research and development activities
- Environmental information
- Business risks and uncertainties
- Financial risk management
- Employees
- Future outlook
- The Board of Directors' proposal to the AGM regarding remuneration and other terms of employment for senior executives
- Most recently adopted guidelines regarding remuneration and other terms of employment for senior executives
- Corporate governance
- Proposed appropriation of profits

43 Five-year summary

44 Group

- Statement of comprehensive income
- Cash flow statement
- Statement of financial position
- Statement of changes in equity

46 Parent Company

- Income statement
- Cash flow statement
- Balance sheet
- Statement of changes in equity

48 Notes to the financial statements and accounting policies

60 Signatures of the Board of Directors

61 Auditor's report

63 Corporate governance report

66 The BioGaia share

68 Executive Management and Board of Directors

70 Definitions and Glossary



Administration report

Figures in brackets refer to the previous year

The Board of Directors and the Managing Director of BioGaia AB (publ), corporate identification number 556380-8723, hereby submit their annual report and consolidated accounts for the financial year 2016.

The financial statements were approved for publication by the Board of the Parent Company on 27 February 2017.

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 Stockholm.

BioGaia has 109 employees, of whom 40 are based in Stockholm, 31 in Lund, 28 in Eslöv, one in Raleigh, USA, and nine in Hiroshima, Japan.

Business model BioGaia's revenue comes mainly from the sale of probiotic 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 (such as infant formula), royalty income for the use of *Lactobacillus reuteri* in a licensee's products and to a certain extent also sales of delivery solutions such as straws and caps.

The products are sold through distributors, of which several are 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 that add reuteri culture to their products 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 2016

New agreements

- **Agreement for the sale of BioGaia Prodentis in Hong Kong** In April BioGaia signed an exclusive agreement with BioWellTech Co Ltd, giving the company the rights to sell BioGaia Prodentis in Hong Kong. The launch took place in the fourth quarter of 2016.
- **Agreement for the sale of drops, tablets and oral rehydration solution in Kenya, Nigeria and Ghana** In September BioGaia signed an exclusive distribution agreement with Phillips Pharma Group for the rights to sell BioGaia Protectis drops, tablets and oral rehydration solution in Kenya, Nigeria and Ghana. The products will be sold under the BioGaia brand and the launch will take place at the beginning of 2017.
- **Major distribution and license agreements with partner in Japan** Through its Japanese subsidiary, BioGaia has signed two new exclusive distributor agreements for Japan with Nippon Kabaya Ohayo Holdings Inc., one for sales of finished probiotic supplements with *Lactobacillus reuteri* and one for the use of *Lactobacillus reuteri* as an ingredient in food. Launches are planned for 2017.

The first agreement concerns the exclusive rights to sell probiotic supplements with BioGaia's patented strains of *Lactobacillus reuteri* in drugstores, supermarkets and similar outlets. Depending on the product category, products will be sold under the Kabaya, Ohayo and/or BioGaia brands and the main target segment is

adults. The second agreement is an exclusive license, giving Ohayo Dairy Products the rights to use strains of *Lactobacillus reuteri* in food, such as beverages and dairy products.

The agreements are long-term and include exclusivity fees and minimum royalties over the terms of the contracts, which will have a substantial impact on BioGaia's Japanese business. Due to confidentiality, the amounts of the fees and the royalties cannot be disclosed.

Clinical studies

- **Two meta-analyses confirm effect of BioGaia Protectis on colic** The first analysis evaluated 17 studies on different treatments for colic, of which *L. reuteri* Protectis was the only probiotic. Only one other product was deemed effective. Simethicone, a drug that is often prescribed for colic, was shown to have no effect.

The systematic review and meta-analysis was published online by researchers Tracy Harb and colleagues at University of Queensland, Australia, in Journal of Pediatric Gastroenterology and Nutrition on 14 December 2015.

At the beginning of May, yet another systematic review further strengthened the proof of Protectis' effect on infantile colic.

This new, eighth review included four studies on *L. reuteri* Protectis. The analysis combined raw data from these trials (Individual Participant Data Meta-Analysis, IPDMA), a method that yields more reliable estimates based on published data only. The analysis was undertaken according to the methods recommended by Cochrane.

The systematic review and meta-analysis was presented at the PAS (Pediatric Academic Societies) meeting in Baltimore, USA, on 1 May 2016.

- **Meta-analysis confirms effectiveness of BioGaia Prodentis on periodontitis** In a systematic review of probiotics as an adjunct to standard treatment of periodontitis, *Lactobacillus reuteri* Prodentis was shown to be the only probiotic effective for patients with chronic periodontitis.

The meta-analysis is the first for probiotics in periodontal treatment. Only four studies, all with *Lactobacillus reuteri* Prodentis, were eligible for inclusion in the systematic review. As no other probiotic product qualified, the analysis concludes that *Lactobacillus reuteri* Prodentis was the only probiotic that gives significant additional pocket reductions in moderate and deep dental pockets when used in combination with standard treatment of chronic periodontitis. In the trials, *Lactobacillus reuteri* Prodentis consistently showed a statistically significant improvement versus standard treatment only.

The meta-analysis was published online by researchers Olivier Huck and colleagues at the Department of Periodontology, Dental Faculty, University of Strasbourg, France, in Journal of Periodontology on 11 March 2016.

- **Publication of study showing that BioGaia Protectis is effective in treating abdominal pain in children** A randomized, double-blind, placebo-controlled study in 93 children diagnosed with functional abdominal pain showed that *L. reuteri* Protectis reduced both frequency and severity of pain compared to placebo. After four weeks of intervention the number of pain episodes were almost halved among the children supplemented with one chewable tablet per day of *L. reuteri* Protectis compared to the placebo group. The severity of pain was also significantly reduced in the probiotic group compared to placebo and this effect persisted during the follow-up period. The study was published online in Journal of Pediatrics on 4 May 2016.

- **Publication of study showing that BioGaia Prodentis reduces pregnancy gingivitis** A double-blind, randomized, placebo-controlled study in 45 women with pregnancy gingivitis showed that supplementation of *L. reuteri* Prodentis significantly reduced inflammation and plaque compared to placebo.

The women with pregnancy gingivitis were enrolled at the beginning of their third trimester. Participants were randomly provided with a supply of lozenges to be consumed twice daily until birth (approximately three months), each containing either Prodentis or a placebo. At the end of the intervention period both gingival index and plaque index of the probiotics group were significantly lower than in the placebo group. The study was published in Journal of Clinical Periodontology on 27 July 2016.



Other key events during the year

- **Distribution of the shares in IBT** An extraordinary general meeting on 18 March 2016 resolved to distribute the shares in the subsidiary Infant Bacterial Therapeutics (IBT) to BioGaia's shareholders. At the end of March, IBT commenced trading on First North. As of 22 March 2016, IBT is no longer part of the BioGaia Group. The operations in IBT are reported as "Discontinued operations" in the income statement. The company applies IFRIC 17, which means that the distribution of the subsidiary IBT is recognized at the fair value of the assets distributed. The difference between the previously reported value and the fair value (based on the average traded price for the first day of trading on 29 March 2016) has been recognized in the income statement and amounted to a profit of SEK 73.1 million. IBT's prospectus for the upcoming rights issue was published on 27 April. To ensure the rights issue, BioGaia guaranteed the issue up to an amount of SEK 38 million. The rights issue was fully subscribed without any need to utilize BioGaia's guarantee. BioGaia received interest income of SEK 1.4 million for the guarantee.
- **Additional investment in MetaboGen** In December 2014 BioGaia reported its decision to invest SEK 12 million in MetaboGen AB in Gothenburg, Sweden. The investment was to be made over a two-year period. The first investment of SEK 4 million took place in December 2014, the second in December 2015 and, as MetaboGen had reached the agreed milestones, the third investment of SEK 4 million was made at the end of November. BioGaia's holding in MetaboGen thereafter amounts to 36%, a stake the company has no plans to change at present.

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. MetaboGen conducts research on metagenomics, the research-intensive and fast developing field concerned with sequencing of all genes in the microbial communities of for example the human gut, to find previously unknown members and patterns of 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 microbiota. Peter Rothschild is Board Chairman and Sara Malcus is President of MetaboGen AB.

At the beginning of December, MetaboGen announced that it had started a study on intrahepatic cholestasis of pregnancy together with Ferring. The study commenced in December and is expected to continue for 18 months.

BioGaia's investment in MetaboGen is long term and aimed at developing the next generation of probiotic products, based on in-depth analyses of the microbiome. The research field is expanding rapidly and a number of large pharmaceutical companies have invested in microbiome companies.

KEY EVENTS AFTER THE END OF THE YEAR

- **BioGaia's probiotic launched in Thailand** In January BioGaia signed an exclusive agreement with Abbott for the rights to sell BioGaia's products in the area of pediatrics and gastroenterology in Thailand. The products will be marketed with a combination of BioGaia's and Abbott's brands. The launch is planned for 2017.

FINANCIAL PERFORMANCE IN 2016

Sales Consolidated net sales amounted to SEK 534.7 million (483.2), which is an increase of SEK 51.5 million (11%) compared to the same period of last year.

Most of the company's sales are denominated in foreign currency, primarily EUR but also USD, CHF and JPY. With unchanged exchange rates compared to the same period of last year, net sales would have been SEK 7.5 million lower. Changes in foreign exchange rates affect both income and expenses. With unchanged exchange rates, operating profit for 2016 would have been SEK 2.6 million lower. Expenses arise mainly in SEK but also in JPY, EUR and USD.

Sales by segment

- **Business unit Pediatrics** Net sales in BioGaia's core area Pediatrics amounted to SEK 433.0 million (389.6), an increase of SEK 43.4 million (11%) (excluding foreign exchange effects, 10%).

Sales of drops were up compared to last year. Sales of drops rose steeply in Europe, somewhat less in the USA and Canada and modestly in Asia, but declined in Rest of the World (mainly in Brazil).

Sales of digestive health tablets were largely unchanged compared to last year. Tablet sales rose in the USA, Canada and Asia, were unchanged in Europe and fell sharply in Rest of the World (mainly in Brazil).

Sales of cultures for infant formula were lower than in the previous year.

Royalty revenue from Nestlé for the use of *Lactobacillus reuteri* Protectis in Growing Up Milk for children older than one year increased dramatically compared to last year.

Royalty revenue from the collaboration agreement with Nestlé (for more information, see below under other sales) in Business Unit Pediatrics amounted to SEK 9.4 million (5.3).

- **Business Unit Adult Health** Net sales in Business Unit Adult Health amounted to SEK 85.3 million (74.7), an increase of SEK 10.6 million (14%) (excluding foreign exchange effects, 10%). The increase was driven mainly by higher sales of Protectis digestive health tablets but also high sales of Prodentis oral health lozenges and the rollout of Gastrus digestive health tablets.

Sales of Protectis digestive health tablets rose in Asia and Rest of the World (South Africa) compared to last year but were unchanged in Europe. In the USA and Canada and South and Latin America regions, no digestive health tablets are sold in the Adult Health segment.

Sales of oral health products were up in all markets except the USA and Canada. Since 2015, Gastrus is sold in Japan and South Korea. In 2016 Gastrus was launched in Italy, Spain, Singapore and the USA, and sales are rising steadily from a low level.

- **Other sales** Other sales amounted to SEK 16.4 million (19.0), a decrease of SEK 2.6 million (14%). No foreign exchange effects arose during the period.

Other sales include royalty revenue of SEK 14.1 (million 12.1) from the collaboration agreement that was signed with Nestlé in March 2014. The royalty revenue amounts to a total of SEK 92.0 million for the period 2014-2017 and is distributed between the segments Pediatrics and Other sales. Under the agreement, BioGaia has undertaken to carry out clinical studies on children and develop new products in new areas. BioGaia will recognize the royalty revenue in pace with completion of the projects. As of 31 December 2016, BioGaia had recognized revenue of SEK 63.9 million of a total of SEK 92 million, of which SEK 38.7 million in Other sales and SEK 25.2 million in the segment Pediatrics.

Sales by geographical market

- Sales in Europe were up by SEK 63.5 million (22%) to SEK 348.2 million.
- Sales in the USA and Canada rose by SEK 5.0 million (14%) to SEK 40.2 million.
- Sales in Asia grew by SEK 9.9 million (19%) to SEK 62.0 million.
- Sales in Rest of the World were down by SEK 26.9 million (24%) to SEK 84.3 million. This is almost exclusively due to lower sales to Brazil resulting from the inventory build-up there in the previous year.

The BioGaia brand Of total finished consumer products, (drops, digestive health tablets, oral health lozenges, oral rehydration solution, etc.), 59% (60%) were sold under the BioGaia brand, including co-branding, during the 2016.

Gross profit Gross profit amounted to SEK 387.8 million (336.6), which is an increase of SEK 51.2 million (15%) compared to last year. The total gross margin rose from 70% to 73%.

Gross margin for Business Unit Pediatrics increased from 68% to 74%. This is due to higher royalty revenue for the use of cultures in Growing Up Milk for children over the age of one year (with a 100% margin) and lower sales of cultures for infant formula with a very low margin.

Gross margin for Business Unit Adult Health fell from 70% to 62%. This is explained by the fact that the company recognized an obsolescence charge for bacteria cultures in inventory that had become too old, costs for Gastrus increased during the launch period and the margin on both digestive health tablets and oral health lozenges has shrunk somewhat due to higher costs for bacteria cultures.

Operating expenses Total operating expenses excluding discontinued operations (IBT) rose by 16% to SEK 192.8 million (165.5).

Selling expenses, excluding IBT, increased compared to the previous year by SEK 14.4 million (15%) and amounted to SEK 108.1 million (93.7), which is equal to 20% (20%) of net sales. The increase is attributable to higher costs for marketing activities such as market samples and congress costs as well as higher personnel costs.

Administrative expenses amounted to SEK 20.9 million (18.5), which is equal to 4% (4%) of net sales. The increase of SEK 2.4 million (13%) is mainly explained by higher personnel costs.

R&D expenses excluding IBT are reported at SEK 63.8 million (53.3), which is equal to 12% (13%) of net sales. The increase of SEK 10.5 million (20%) is mainly attributable to higher personnel costs and increased costs for research projects and clinical studies, but also to higher patent costs. Furthermore, a provision of SEK 3.9 million was reversed in the fourth quarter of last year, which reduced the comparative figure.

Other operating income/expenses refer to foreign exchange gains/losses on operating receivables and liabilities. These amounted to SEK 5.6 million (1.8).

Share in profit of associates In December BioGaia invested further in MetaboGen AB (see above). Following the investment, BioGaia's holding amounts to 36%. MetaboGen is reported as an associate to BioGaia. The share of profit in MetaboGen is reported according to the equity method and amounted to SEK -1.1 million (-0.1).

Operating profit Operating profit excluding IBT was SEK 199.4 million (172.8), an increase of SEK 26.6 million (15%), and operating margin excluding IBT was 37% (36%). Including IBT, operating profit was SEK 194.3 million (152.2).

Financial items and profit before tax Profit before tax excluding IBT was SEK 196.1 million (178.0), an increase of SEK 18.1 million (10%). Net financial items include a foreign exchange loss of SEK 4.7 million on forward exchange contracts in EUR and USD. The figures for the previous year include a corresponding foreign exchange gain of SEK 5.1 million.

At 31 December 2016 the company had outstanding forward exchange contracts for EUR 11.1 million at an average exchange rate of SEK 9.45 and USD 2.2 million at an average exchange rate of SEK 8.76. The actual exchange gain/loss depends on the exchange rate on the maturity date of the contracts.

Profit after tax Profit after tax from continuing operations was SEK 159.3 million (137.4), an increase of SEK 21.9 million (16%).

The tax rate for the Group was 19% (23%). At 31 December 2015 the subsidiary BioGaia Japan had an accumulated loss carryforward of approximately SEK 35.2 million. Owing to the new distribution and license agreement (see above), a large share of the loss carryforward will be utilized in the Japanese company. In the Group, exclusivity fees will be recognized successively over the term of the agreement. BioGaia's assessment is that it will be possible to utilize the entire loss carryforward and a deferred tax asset of SEK 10.4 million has therefore been recognized.

Earnings per share Earnings per share from continuing operations amounted to SEK 9.19 (7.94). Earnings per share including discontinued operations amounted to SEK 13.13 (7.01). No dilutive effects arose during the period.

Cash flow Cash flow for the year was SEK 14.0 million (15.1). BioGaia's former subsidiary IBT was distributed to BioGaia's shareholders on 22 March 2016. At that time, IBT's cash and cash equivalents amounted to SEK 37.6 million, compared to SEK 44.4 million at year-end 2015. Excluding IBT, cash flow for the period was SEK 58.4 million (56.1). Cash flow includes dividends of SEK 86.7 million (86.3). Cash and cash equivalents at 31 December 2016 amounted to SEK 243.1 million (226.9).

Equity Consolidated equity at 31 December 2016 amounted to SEK 404.7 million (395.8). The Group's equity/assets ratio was 84% (84%).

LAUNCHES IN 2016

DISTRIBUTOR/LICENSEE	COUNTRY	PRODUCT	BRAND
Abbott/Recalcine	Chile	Prodentis oral health lozenges	BioGaia
Alimentary Health	Ireland	LifeTop Straw (CapAble AB)	Partner brand
Axero	Sri Lanka	Drops and digestive health tablets	BioGaia
Baltic Business Partners	Lithuania	Prodentis oral health lozenges	BioGaia
Biovagen	Vietnam	Tablets	BioGaia
BioWellTech	Hong Kong	Prodentis oral health lozenges	BioGaia
Casern/Recordati	Spain	Gastrus digestive health tablets, Easy Dropper ¹⁾	BioGaia
Dong Sung	South Korea	Protectis digestive health tablets with strawberry flavour and Easy Dropper ¹⁾	BioGaia co-brand
Everidis	USA	Gastrus digestive health tablets and Easy Dropper ¹⁾	BioGaia
Ewopharma	Czech Republic, Slovenia and Croatia	Easy Dropper ¹⁾	BioGaia
Interbat	Indonesia	Protectis digestive health tablets with strawberry flavour	BioGaia co-brand
Italchimichi	Italy	Easy Dropper ¹⁾ with vitamins D and K	Partner brand
J Health	Hong Kong	Drops with vitamin D	BioGaia co-brand
NeoCare	Belgium	Easy Dropper ¹⁾	BioGaia
Nestlé	Mexico	Growing Up milk with <i>Lactobacillus reuteri</i> Protectis	Partner brand
Noos	Italy	Easy Dropper ¹⁾ with vitamins D and K	Partner brand
Noos	Italy	Gastrus digestive health tablets	BioGaia
Pediact	France	Easy Dropper ¹⁾	BioGaia
Pharmaforte	Singapore	Gastrus digestive health tablets	BioGaia
Unilab	Philippines	Protectis digestive health tablets with strawberry flavour	BioGaia Co-branding
Verman	Finland	Easy Dropper ¹⁾	Partner brand

¹⁾New, user-friendly package for drops.



Investments in property, plant and equipment Investments in property, plant and equipment amounted to SEK 5.6 million (17.8), of which the majority refers to the subsidiary TwoPac.

Investments in capitalized development expenditure amounted to SEK 0.0 million (10.1). Investments during 2015 referred to development of a product for the NEC project in the former subsidiary IBT, which was distributed to the shareholders in March 2016.

Subsidiary in Japan Net sales in the wholly owned subsidiary in Japan reached SEK 24.4 million (21.1). Operating profit/loss in the Japanese subsidiary was SEK -2.0 million (-2.8).

In December 2016 BioGaia signed a major distribution and sales agreement with a partner in Japan – see above under “Key events of 2016”.

Subsidiary TwoPac AB TwoPac AB is a wholly owned subsidiary of BioGaia that manufactures and develops products, such as drops, exclusively for BioGaia.

Net sales in TwoPac totalled SEK 71.1 million (52.6). Operating profit was SEK 17.9 million (9.9). Profit after tax was SEK 13.6 million (7.2).

Subsidiary CapAble AB CapAble, which is owned 90.1% by BioGaia and 9.9% by CapAble’s President, was started in November 2008 to manufacture and sell the patented LifeTop Cap. Net sales in CapAble amounted to SEK 0.0 million (1.6). Operating loss was SEK -3.6 million (-3.5). During the year, both the tool designs for the cap and the machine that fills the blister and assembles them together were re-engineered and improved. As a result, there has been no production during the year. The rebuild will be completed in the first quarter of 2017 and deliveries can resume in the second quarter.

Parent Company Net sales in the Parent Company amounted to SEK 518.3 million (470.6) and profit before tax was SEK 180.1 million (165.6). The Parent Company’s profit includes a write-down of the loan to the subsidiary in Japan by SEK 7.2 million. No new loans have been paid, and the write-down refers to currency adjustment of the existing loan. Cash flow in the Parent Company totalled SEK 40.9 million (-29.9).

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, 173 clinical studies using BioGaia’s human strains of *Lactobacillus reuteri* have been performed on around 14,800 individuals. The results have been published in 146 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)
- Necrotizing enterocolitis (NEC)

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 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 and environmentally friendly mission, namely to conduct research and development aimed at offering clinically proven, health-enhancing and user-friendly 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 -2015. 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 2013-2016 BioGaia took part in the CDP Nordic Climate Change report, an initiative to provide investors and the market worldwide with information about the climate impacts of the largest corporations and how efforts to reduce negative impact are integrated in their business strategies. In 2013-2015 BioGaia climate compensated through contributions totalling approximately SEK 290,000 to Vi Agroforestry projects in the Kagera region of western Tanzania.

In 2016 BioGaia climate compensated through contributions totalling approximately SEK 150,000 to two projects, one in Malawi and one in Kenya, via Zero Mission.

Goals for environmental work in 2017

1. Further develop efforts to reduce the use of antibiotics and antibiotic resistance.
2. Communicate BioGaia’s sustainability responsibility to employees and distributors.
3. Climate compensate in selected projects for emissions during 2016.

BioGaia conducts no operations that are subject to permit or notification requirements.

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.

GROUP

Associated company MetaboGen AB Since 1 December 2016, BioGaia owns 36% of MetaboGen AB (for more information, see above). The remaining shares are held by the researchers who founded the company and GU Holding. So far, MetaboGen has shown a loss. On the balance sheet date, assets in MetaboGen were reported at SEK 10.7 million. BioGaia’s assessment is that MetaboGen will show profitability in the future, for which reason there was no indication of impairment on the balance sheet date.

BioGaia’s partners BioGaia does not sell directly to end-users but instead sells its products to companies (partners) which then sell the products further. The agreements normally have a term of 3-7 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 sales 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 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 and 2028.

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, 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, 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. As 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.

PARENT COMPANY

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. The shares in the subsidiary CapAble amount to a total of SEK 6.9 million in the Parent Company. CapAble has operated at a loss since the start in 2008.

Profit/loss before tax and group contributions for 2016 was SEK -3.6 million (-3.5). BioGaia made total conditional shareholder contributions to the subsidiary CapAble of SEK 6.0 million in 2009 and 2010. BioGaia AB made total group contributions of SEK 18.7 million during the period 2010-2016.

On the balance sheet date, assets in CapAble were reported at SEK 6.9 million in the Parent Company. BioGaia’s assessment is that CapAble will show profitability in the future, for which reason there was no indication of impairment on the balance sheet date.

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 minimize 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. For more information, see Note 29.

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

In 2016 the company had a cash flow surplus of approximately EUR 23.8 million (14.5), a cash flow surplus/deficit of JPY 29.4 million (-62.0) and a cash flow surplus of USD 11.1 million (12.8).

Growth in sales has also led to increased currency risks, for which reason the company has taken currency hedges in EUR, and since 2015 also in USD. For more information, see Notes 10, 11, 23 and 29.

Interest rate and liquidity risk The Group has no external loans.

For cash and cash equivalents, the company has a liquidity policy in which the basic principles are that investment risks should always be minimized and investments should be made primarily in Swedish kronor. To minimize currency risk, other currencies may also be considered. 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.

Credit risks BioGaia’s credit risks are tied to trade receivables. 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 minimize risks.

Cash flow risk Cash flow including IBT amounted to SEK 14.0 million (15.1). Cash flow included dividends of SEK 86.7 million (86.4) and tax payments of SEK 43.4 million (50.1). BioGaia’s former subsidiary IBT was distributed to BioGaia’s shareholders in March 2016. Excluding IBT, cash flow was SEK 58.4 million (56.1). Because cash and cash equivalent at 31 December 2016 amounted to SEK 243.1 million (226.9), no infusion of capital is necessary during the coming 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 2016 (excluding discontinued operations in IBT) was 109 (101), consisting of 61 women and 48 men. The management team includes three men and five women. In 2016, 21 new employees were hired and 13 left the company. See Note 4 for additional information about employees and personnel expenses.

BioGaia’s incentive scheme for the employees BioGaia currently has no incentive scheme in place for the employees and during 2016 and 2015 paid only basic salary to the employees.

The warrant programme that was resolved on by the Annual General Meeting 2012 expired on 1 June 2015. A total of 65,500 warrants were redeemed and the share capital now amounts to SEK 17,336,462. The subscription price for the share was SEK 241.90 and the company was thus provided with proceeds of SEK 15.8 million in 2015.



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.

In view of the Company's strong portfolio consisting of an increased number of innovative products that are sold under the BioGaia brand to a growing extent, successful clinical trials and an expanding distribution network that covers a large share of the key markets, BioGaia's future outlook is bright.

Financial target and dividend policy The long-term financial target is a sustainable operating margin (operating profit in relation to sales) of at least 34% (previously 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.

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 date.

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 basic salary, variable remuneration, long-term incentive schemes, pension benefits, other benefits and terms of notice/termination benefits.

- **Basic salary** Basic 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 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 other remuneration and shall be consistent with general norms in the respective geographical market.
- **Terms of notice and termination benefits** In the event that employment is terminated by the company, the term of notice for senior executives may not exceed 18 months. In the event that employment is terminated by the employee, the term of notice may not be shorter than three months.

The Board of Directors proposes that the Board be authorized 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 FOR 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 pages 63-65.

PROPOSED APPROPRIATION OF PROFITS

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

Retained earnings	223,491,724
Profit for the year	136,953,063
Together amounting to	360,444,787

The Board of Directors proposes that the profits be appropriated as follows

To be paid as a dividend to the shareholders	130,023,465 ^{*)}
To be carried forward to new account	230,421,322
Total	360,444,787

^{*)} The proposed dividend consists of an ordinary dividend of SEK 3.16 (3.03) per share and an extraordinary dividend of SEK 4.34 (1.97) per share, amounting to a total dividend of SEK 7.50 (5.00) per share.

Five-year summary

Key ratios	2016	2015	2014	2014 ¹⁾	2013	2012	2012 ¹⁾
Net sales, SEK M	534.7	483.2	481.8	386.4	315.9	645.2	289.2
Net sales, Pediatrics, SEK M	433.0	389.6	409.1	313.7	238.6	N/A	N/A
Net sales, Adult Health, SEK M	85.3	74.7	69.4	69.4	75.6	N/A	N/A
Net sales, other SEK M	16.4	19.0	15.7	15.7	1.7	N/A	N/A
Operating profit, SEK M ²⁾	199.4	172.8	203.6	108.2	81.9	428.1	72.1
Profit before tax, SEK M ²⁾	196.1	178.0	199.3	103.9	84.0	442.2	86.2
Profit after tax, SEK M ²⁾	159.3	137.4	152.7	78.3	64.4	329.9	63.7
Net earnings including discontinued operations	227.3	121.3	148.0	73.6	64.2	329.9	63.7
Profit after tax attributable to owners of the Parent Company, SEK M ²⁾	159.3	137.4	153.3	78.9	61.9	327.0	60.8
Growth net sales %	11	25	53	22	9	105	-8
Operating margin, % ²⁾	37	36	42	28	26	66	25
Profit margin, % ²⁾	37	37	42	27	27	69	30
Current ratio, times	5.2	4.7	4.7	4.8	4.9	13.2	5.1
Equity/assets ratio, %	85	84	83	84	83	88	82
Capital employed, SEK M	415.5	396.2	344.8	270.4	316.9	481.5	195.7
Return on capital employed, % ²⁾	49	48	61	37	22	124	40
Return on equity, %	56	33	45	25	16	96	29
Average number of employees ²⁾	108	98	87	87	79	70	70
Data per share							
Number of shares at 31 Dec, thousands ³⁾	17,336	17,336	17,271	17,271	17,271	17,271	17,271
Average number of shares, thousands	17,336	17,309	17,271	17,271	17,271	17,271	17,271
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	17,336	17,336	17,271	17,271	17,358	17,271	17,271
The results per share, continuing operations, SEK ²⁾	9.19	7.94	8.87	4.57	3.73	18.93	3.52
Earnings per share before dilution, SEK ⁴⁾	13.13	7.01	8.53	4.23	3.57	18.93	3.52
Earnings per share after dilution ⁴⁾	13.13	7.01	8.53	4.23	3.56	18.93	3.52
Equity per share, SEK	23.95	22.87	19.95	15.64	18.37	26.25	10.83
Equity per share after dilution, SEK	23.95	22.87	19.95	15.64	18.28	26.25	10.83
Cash flow from operating activities per share, SEK	8.53	6.78	7.20	N/A	4.54	19.43	N/A
Cash flow from operating activities per share after dilution, SEK	8.53	6.78	7.20	N/A	4.52	19.43	N/A
Share price on the balance sheet date, SEK	300.00	281.50	179.50	179.50	253.50	175.00	175.00
Dividend per share, SEK	7.50⁵⁾	5.00	5.00	5.00	7.00	10.00	10.00

¹⁾ Key ratio excluding license revenue from Nestlé of SEK 95.4 million in 2014 and SEK 356.0 million in 2012.

²⁾ Excluding discontinued operations (distribution of IBT)

³⁾ The share capital consists of 740,668 class A shares and 16,595,794 class B shares. The quota value is SEK 1 per share.

⁴⁾ Key figures defined according to IFRS.

⁵⁾ Dividend proposed but not yet approved.

For definitions of key ratios, see page 70.





Group

STATEMENT OF COMPREHENSIVE INCOME

SEK 000s	Not	2016	2015
Net sales	2, 3	534,696	483,241
Cost of goods sold	2	-146,889	-146,657
Gross profit	2	387,807	336,584
Selling expenses	4, 5	-108,108	-93,735
Administrative expenses	4, 6	-20,893	-18,475
Research and development expenses	4, 5, 14	-63,795	-53,283
Share of profit of associates	7	-1,184	-65
Other operating income	8	5,610	1,773
Operating profit	9	199,437	172,799
Financial income	10	1,429	5,438
Financial expenses	11	-4,807	-260
Net financial items		-3,378	5,178
Profit before tax		196,059	177,977
Tax	12	-36,710	-40,594
PROFIT FOR THE YEAR FROM CONTINUING OPERATIONS		159,349	137,383
Discontinued operations (distribution of IBT)			
RESULT FROM DISCONTINUED OPERATIONS		67,935	-16,092
PROFIT FOR THE YEAR		227,284	121,291
<i>Items that may be reclassified subsequently to profit or loss:</i>			
Gain/losses arising on translation of the financial statements of foreign operations:		889	462
Comprehensive income for the year		228,173	121,753
<i>Profit from continuing operations attributable to:</i>			
Owners of the Parent Company		159,349	137,497
Non-controlling interests	13	-	-114
		159,349	137,383
<i>Profit for the year attributable to:</i>			
Owners of the Parent Company		227,568	121,408
Non-controlling interests		-284	-117
		227,284	121,292
<i>Comprehensive income for the period attributable to:</i>			
Owners of the Parent Company		228,457	121,870
Non-controlling interests		-284	-117
		228,173	121,753
Earnings per share			
Basic earnings per share in continuing operations, SEK		9.19	7.94
Earnings per share after dilution, continuing operations, SEK		9.19	7.94
Earnings per share including discontinued operations, SEK		13.13	7.01
Earnings per share after dilution, including discontinued operations, SEK		13.13	7.01
Number of shares, thousands		17,336	17,336
Average number of shares, thousands		17,336	17,309

CASH FLOW STATEMENT

SEK 000s	Not	2016	2015
Operating activities			
Operating profit		194,275	152,184
<i>Adjustments for non-cash items:</i>			
Depreciation/amortization		7,074	6,548
Capital gains/losses on the sale of non-current assets		58	-
Share in profit of associates		1,184	65
Other non-cash items		-3,127	-878
		199,464	157,919
Realized forward exchange contracts		-2,081	2,203
Interest received		1,429	331
Interest paid		-124	-268
Taxes paid		-43,381	-50,124
Cash flow from operating activities before changes in working capital		155,307	110,061
<i>Cash flow from changes in working capital:</i>			
Inventories		4,534	-22,438
Current receivables		-13,797	17,855
Trade payables		-7,217	6,595
Current interest-free operating liabilities		9,102	5,428
Cash flow from operating activities		147,929	117,501
<i>Investing activities:</i>			
Acquisition of intangible assets	14	-	-10,150
Purchase of property, plant and equipment	15	-5,611	-17,780
Purchase of financial assets	16	-4,000	-4,000
Cash flow from investing activities		-9,611	-31,930
<i>Financing activities:</i>			
Dividend		-124,311	-86,355
New issue of warrants		-	15,844
Cash flow from financing activities		-124,311	-70,511
CASH FLOW FOR THE YEAR		14,007	15,060
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR			
		226,882	210,666
<i>Exchange difference in cash and cash equivalents</i>			
		2,180	1,156
CASH AND CASH EQUIVALENTS AT END OF YEAR		243,069	226,882

STATEMENT OF FINANCIAL POSITION

SEK 000s	Note	31 Dec 2016	31 Dec 2015
ASSETS			
<i>Non-current assets:</i>			
Intangible assets	14	-	16,225
Property, plant and equipment	15	82,430	83,934
Investments in associates	16, 30	10,752	7,936
Deferred tax assets	12	10,433	-
Deposits		23	22
Total non-current assets		103,638	108,117
<i>Current assets:</i>			
Inventories	18	40,479	43,546
Trade receivables	19, 23	75,668	65,937
Current tax assets	21	-	7,129
Other receivables	21	6,352	7,600
Deferred expenses and accrued income	22	19,759	13,954
Short-term investments	23	13	13
Cash and cash equivalents	23	243,069	226,882
Total current assets		385,340	365,061
TOTAL ASSETS		488,978	473,178

STATEMENT OF FINANCIAL POSITION

SEK 000s	Note	31 Dec 2016	31 Dec 2015
EQUITY AND LIABILITIES			
<i>Equity</i>			
Share capital	24	17,336	17,336
Other contributed capital		21,831	21,831
Reserves		1,159	270
Retained earnings		147,304	235,006
Profit for the year attributable to owners of the Parent Company		227,568	121,408
Total equity attributable to owners of the Parent Company		415,198	395,851
Non-controlling interests	13, 16	-18	-18
Total non-controlling interests		-18	-18
Total equity		415,180	395,833
<i>Non-current liabilities:</i>			
Deferred tax liability	12	332	351
Total non-current liabilities		332	351
<i>Current liabilities:</i>			
Prepayments from customers	23	21,799	16,762
Trade payables	23	16,951	23,638
Current tax liabilities	26	94	-
Other liabilities	26	9,241	4,754
Accrued expenses and deferred income	27	25,381	31,840
Total current liabilities		73,466	76,994
Total liabilities		73,798	77,345
TOTAL EQUITY AND LIABILITIES		488,978	473,178

STATEMENT OF CHANGES IN EQUITY

SEK 000s	Share capital	Statutory reserve	Other contributed capital	Foreign currency translation reserve	Retained earnings	Profit for the year	Equity attributable to owners of the parent company	Non-controlling interests	Total equity
Opening balance, 1 January 2015	17,271	1,735	4,318	-193	173,956	147,405	344,492	99	344,591
Dividend					-86,355		-86,355		-86,355
New issue warrants programme	65		15,778				15,843		15,843
Total transactions with owners	65	-	15,778	-	-86,355	-	-70,512	-	-70,512
<i>Carried forward</i>					147,405	-147,405	-		-
Profit for 2015						121,408	121,408	-117	121,291
<i>Other comprehensive income</i>									
Translation differences on translation of foreign operations				462			462		462
Comprehensive income for the year	-	-	-	462	-	121,408	121,870	-117	121,753
Closing balance, 31 December 2015	17,336	1,735	20,096	270	235,006	121,408	395,851	-18	395,833
Dividend					-86,682		-86,682		-86,682
Distribution of shares in IBT					-122,428		-122,428	284	-122,144
Total transactions with owners	-	-	-	-	-209,110	-	-209,110	284	-208,826
<i>Carried forward</i>					121,408	-121,408	-		-
Profit for 2016						227,568	227,568	-284	227,284
<i>Other comprehensive income</i>									
Translation differences on translation of foreign operations				889			889		889
Comprehensive income for the year	-	-	-	889	-	227,568	228,457	-284	228,173
Closing balance, 31 December 2016	17,336	1,735	20,096	1,159	147,304	227,568	415,198	-18	415,180



Parent Company

INCOME STATEMENT

SEK 000s	Note	2016	2015
Net sales	2, 3	518,307	470,612
Cost of goods sold	2	-164,201	-157,364
Gross profit	2	354,106	313,248
Selling expenses	4	-90,308	-78,480
Administrative expenses	4, 6	-19,119	-16,360
Research and development expenses	4, 14	-64,203	-54,072
Other operating income	8	6,002	1,789
Operating profit	9	186,478	166,125
<i>Result from financial investments</i>			
Impairment loss on shares in group companies	16	-3,578	-22,974
Anticipated dividends from subsidiaries	5	-	20,600
Impairment loss on non-current receivables from group companies	17	-	-4,052
Interest income and similar profit/loss items	10	2,007	6,121
Interest expense and similar profit/loss items	11	-4,798	-193
Net financial items		-6,369	-498
Profit before tax		180,109	165,627
Tax	12	-43,156	-34,847
PROFIT FOR THE YEAR		136,953	130,780

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 STATEMENT

SEK 000s	Note	2016	2015
Operating activities			
Operating profit		186,478	166,125
<i>Adjustments for non-cash items:</i>			
Depreciation/amortization		449	560
Other non-cash items		-1,944	-947
		184,983	165,738
Realized forward exchange contracts		-2,082	2,203
Interest received		2,008	1,014
Interest paid		-113	-193
Taxes		-40,637	-47,296
Cash flow from operating activities before changes in working capital		144,159	121,466
<i>Cash flow from changes in working capital:</i>			
Inventories		5,698	-19,064
Current receivables		-23,567	15,956
Trade payables		-8,013	10,661
Current interest-free operating liabilities		13,549	-1,633
Cash flow from operating activities		131,826	127,386
<i>Investing activities:</i>			
Purchase of property, plant and equipment	15	-283	-60
Purchase of financial assets	16	-4,000	-67,800
Payment of loan to subsidiary	17	-	-18,873
Cash flow from investing activities		-4,283	-86,733
<i>Financing activities:</i>			
Dividend		-86,682	-86,355
New issue of warrants		-	15,844
Cash flow from financing activities		-86,682	-70,511
CASH FLOW FOR THE YEAR		40,861	-29,858
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		173,077	201,988
Exchange difference in cash and cash equivalents		1,942	947
CASH AND CASH EQUIVALENTS AT END OF YEAR		215,880	173,077

BALANCE SHEET

SEK 000s	Note	31 Dec 2016	31 Dec 2015
ASSETS			
Non-current assets			
Property, plant and equipment	15		
Production equipment		245	494
Office equipment and computers		449	366
Total property, plant and equipment		694	860
<i>Financial assets</i>			
Investments in group companies	16	51,133	132,938
Investments in associates	16	12,000	8,000
Receivables from group companies	17	55,835	55,835
Total financial assets		118,968	196,773
Total non-current assets		119,662	197,633
Current assets			
Inventories	18	28,438	34,137
<i>Current receivables</i>			
Trade receivables	19	69,387	60,550
Receivables from group companies	20	8,956	1,029
Current tax assets	21	1,371	5,363
Other receivables	21	6,025	7,003
Deferred expenses and accrued income	22	17,764	11,205
Total current receivables		103,503	85,149
Short-term investments	23	13	13
Cash and cash equivalents		215,880	173,077
Total current assets		347,834	292,377
TOTAL ASSETS		467,496	490,010

BALANCE SHEET

SEK 000s	Note	31 Dec 2016	31 Dec 2015
EQUITY AND LIABILITIES			
Equity			
<i>Restricted equity</i>			
Share capital		17,336	17,336
Other restricted equity	24	1,253	1,253
		18,589	18,589
<i>Non-restricted equity</i>			
Retained earnings		223,492	261,200
Profit for the year	25	136,953	130,780
		360,445	391,980
Total equity		379,034	410,569
Liabilities			
<i>Current liabilities</i>			
Prepayments from customers		28,793	16,762
Trade payables		12,175	20,188
Liabilities to group companies	20	20,813	18,300
Other liabilities	26	3,145	1,153
Accrued expenses and deferred income	27	23,536	23,038
Total current liabilities		88,462	79,441
Total liabilities		88,462	79,441
TOTAL EQUITY AND LIABILITIES		467,496	490,010

STATEMENT OF CHANGES IN EQUITY

	Share capital	Other restricted equity	Retained earnings	Profit for the year	Total equity
Opening balance, 1 January 2015	17,271	1,253	182,186	149,590	350,300
Carried forward			149,590	-149,590	0
Dividend			-86,355		-86,355
Profit for 2015				130,780	130,780
New issue warrants programme	65		15,779		15,844
Closing balance, 31 December 2015	17,336	1,253	261,200	130,780	410,569
Carried forward			130,780	-130,780	0
Dividend			-86,682		-86,682
Distribution of shares in IBT			-81,806		-81,806
Profit for 2016				136,953	136,953
Closing balance, 31 December 2016	17,336	1,253	223,492	136,953	379,034



Notes to the financial statements and accounting policies

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

TABLE OF CONTENTS

	Sidan
Note 1	48
Note 2	51
Note 3	51
Note 4	51
Note 5	52
Note 6	53
Note 7	53
Note 8	53
Note 9	53
Note 10	53
Note 11	53
Note 12	53
Note 13	54
Note 14	54
Note 15	55
Note 16	56
Note 17	56
Note 18	56
Note 19	56
Note 20	57
Note 21	57
Note 22	58
Note 23	58
Note 24	58
Note 25	59
Note 26	59
Note 27	59
Note 28	59
Note 29	59
Note 30	60

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 Annual Accounts Act and 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 Annual Accounts Act limits the applicability of IFRS in the Parent Company.

New and revised IFRS standards and new interpretations effective for 2016

The new and revised standards and new interpretations have not had any material impact on the consolidated financial statements for 2016.

New and revised IFRS standards and new interpretations not yet effective The new and revised standards and new interpretations that have been issued, but are mandatorily effective for accounting periods beginning on or after 1 January 2017, have not yet been adopted by the Group. Below is a description of those that are assessed to have an impact on the consolidated financial statements in the period when they are applied for the first time.

Standards	Effective for accounting periods beginning:
IFRS 9 Financial Instruments	on or after 1 January 2018
IFRS 15 Revenue from Contracts with Customers	on or after 1 January 2018
IFRS 16 Leases	on or after 1 January 2019

● **IFRS 9 Financial Instruments** was issued on 24 July 2014 and will replace IAS 39 Financial Instruments: Recognition and Measurement. The standard has been issued in phases, of which the version issued in July 2014 supersedes all earlier versions.

IFRS 9 contains new principles for classification and measurement of financial assets and liabilities. The decisive factors for determining which measurement category a financial asset is attributed to are the entity's objective for holding asset (i.e. the entity's "business model"), and the financial asset's contractual cash flows.

The new standard also contains new rules for impairment testing of financial assets, replacing the earlier "incurred loss method" with a new "expected loss method".

The new rules for hedge accounting are intended to enable entities to better reflect risk management activities in the financial statements. The standard permits greater scope to hedge risk components of non-financial items and allows more types of instruments to be part of a hedging relationship. Furthermore, the quantitative test for hedge effectiveness is no longer required. IFRS 9 is mandatorily effective for accounting periods beginning on or after 1 January 2018 and was endorsed by the EU in December 2016. Management's assessment is that the application of IFRS 9 may affect the amounts recognized in the financial statements for the Group's financial assets and liabilities. Management has not yet made a detailed analysis of the impact of the application of IFRS 9 and is therefore not yet able to quantify the effects.

● **IFRS 15 Revenue from Contracts with Customers** was issued on 28 May 2014 and will replace IAS 18 Revenue and IAS 11 Construction Contracts. IFRS 15 establishes a model for accounting for almost all revenue that arises through contracts with customers, with the exception of leases, financial instruments and insurance agreements. The core principle of IFRS 15 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Revenue is recognized when control of the goods or services is transferred to the customer. IFRS 15 provides significantly more guidance for specific areas and the disclosure requirements are extensive. IFRS 15 is mandatorily effective for accounting periods beginning on or after 1 January 2018, with earlier application permitted. The standard was endorsed by the EU in September 2016. Management has not yet made a

detailed analysis of the impact of the application of IFRS 15 but does not expect it to have any material impact on revenue recognition.

● **IFRS 16 Leases** Leases was issued on 13 January 2016 and will replace IAS 17 Leases. IFRS 16 introduces a "right of use model" that requires lessees to recognize assets and liabilities for all leases, for which reason leases are no longer classified as operating or finance leases. The exceptions are leases that have a term of 12 months or less and leases where the underlying asset has a low value. In the income statement, the entity shall recognize depreciation on the asset and interest expenses on the liability. The standard contains more extensive disclosure requirements compared to the current standard. For the lessor, IFRS 16 entails no real changes compared to IAS 17. IFRS 16 is mandatorily effective for accounting periods beginning on or after 1 January 2019, with earlier adoption permitted on the condition that IFRS 15 is also applied. The standard was endorsed by the EU in December 2016. Management has not yet made a detailed analysis of the impact of the application of IFRS 9 and is therefore not yet able to quantify the effects.

Management's assessment is that the other new and revised standards and new interpretations that are not yet effective will not have any material impact on the consolidated financial statements when they are applied for the first time.

Basis of preparation The consolidated financial statements have been prepared on the historical cost basis unless otherwise specified.

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 30.

Basis of consolidation The consolidated financial statements consolidate the operations of the Parent Company and the subsidiaries for the period ended 31 December 2016. 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 intragroup transactions and balances are eliminated in full on consolidation, including unrealized gains or losses arising from inter-company transactions. In cases where unrealized losses on intragroup 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 recognized from the date on which the acquisition or sale went into force, according to what is applicable.

Non-controlling interests, which are recognized 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 recognized in the cash flow statement in "Cash flow from financing operations" and in 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 recognized 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 recognized in operating profit, while foreign exchange gains/losses on financial receivables and liabilities are recognized 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 and USD. 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 computed quarterly. Exchange differences arising on translation of foreign operations are recognized 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 information The Executive Management has analyzed the Group's internal reporting and determined that the Group's operations are monitored and evaluated based on the following segments:

● **Business Unit Pediatrics** (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).

● **Business Unit Adult Health** (digestive health tablets, oral health lozenges, cultures as an ingredient in a licensee's dairy products).

● **Other** (royalties in respect of development projects, animal health products, etc).

Sales and gross profit are reported for the above segments and are monitored regularly by the Managing Director (who is regarded as the chief operating decision maker) together with the management. There is no monitoring of the company's total assets and liabilities against the segments' assets.

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 from 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 recognized 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.

Royalty revenue based on the licensee's reporting of units produced or on the sales value of products containing BioGaia's probiotic is recognized quarterly. The presentation of and time for the licensee's reporting is regulated by agreement. 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 recognized 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 recognized in pace with completion of the projects.

Interest income is recognized profit or loss for the period in which it arises.



Leasing 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 recognized 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 legislation, and other employees in accordance with the respective country's legislation. 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 taxable profit for the period. Taxable profit differs from recognized profit in the consolidated income statement in that it has been adjusted for non-taxable income and non-deductible expenses and for items of income and expense that are taxable or deductible in other periods.

Deferred tax refers to the tax computed partly on the basis of temporary differences and partly on tax losses. At every closing date, an assessment is made to determine whether to recognize deferred tax assets not previously recognized in the balance sheet. Such tax assets are recognized to the extent that it is probable that there will sufficient taxable profits against which to utilize these in the future.

Research and development expenses Expenditure on research activities is recognized as an expense in the period in which it is incurred. An internally-generated intangible asset arising from development is recognized if, and only if, all of the following have been demonstrated:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale;
- the company's intention to complete the intangible asset and use or sell it;
- the ability to use or sell the intangible asset;
- how the intangible asset will generate probably future economic benefits;
- the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset, and
- the ability to measure reliably the expenditure attributable to the intangible asset during its development

Other expenditure on development activities is recognized as an expense in the period in which it is incurred. An individual assessment of all ongoing research and development projects is made quarterly to determine which costs are capitalizable. The carrying amount of capitalized expenditure includes all directly attributable costs such as materials, purchased services and employment costs.

BioGaia typically has research activities in the form of clinical studies underway parallel to product development. Much of BioGaia's product development consists of stability tests to ensure that the products remain stable throughout their shelf lives. While the clinical studies and stability tests are in progress, it is often not possible to be certain that the project will be successful and that the product can be sold. This means that projects often do not meet the requirements for capitalization. Other aspects of product development include finding new delivery systems and developing existing products.

Amortization of capitalized development costs is started when the asset can be used and the products begins generating revenue, and is carried out on a straight-line basis over the expected useful life of the asset.

Intangible assets and property, plant and equipment Intangible assets and property, plant and equipment are recognized at cost less accumulated amortization/depreciation and impairment.

Intangible assets are amortized on a straight-line basis over their expected useful lives. The following depreciation schedules are applied for property, plant and equipment:

Tangible fixed assets	
Production equipment	5–10 years
Equipment and computers	3–5 years
Buildings	20–60 years

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

Depreciation of buildings is started when construction is completed. For electrical and internal construction work, etc., the depreciation period is 20–30 years, and for framework and foundation the depreciation period is 60 years.

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

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

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

The financial assets recognized in balance sheet include cash and cash equivalents, 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 in the Group refer to shares in a company where the holding is below 20% and the Group does not have control.

When the holding exceeds 20% (and controlling interests do not exist), the shares in the company will instead be recognized as interests in associates.

A financial asset or liability is recognized in the balance sheet when the company initially becomes party to the contractual provisions of the instrument. Financial liabilities are recognized 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 amortized cost less provision for impairment. Impairment losses on trade receivables are recognized in profit or loss. Trade payables are recognized when an invoice has been received.

The purchase or sale of other financial assets is recognized on the trade date, which is the date on which the company commits to purchase or sell the asset.

A financial asset is derecognized from the balance sheet when the company's rights under the agreement are realized, expire or the company has relinquished control of the asset. The same applies to a part of a financial asset. A financial liability is derecognized 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, it is 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 observable in the market.

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.

Revisions in RFR 2 have not had any material impact on the financial statements of the Parent Company for 2016.

● **Presentation** The income statement and balance sheet of the Parent Company are presented in accordance with the schedules in the Swedish Annual Accounts Act.

● **Income taxes** In the Parent Company, untaxed reserves are recognized including the deferred tax liability. In the consolidated financial statements, however, untaxed reserves are divided between the deferred tax liability and equity.

● **Subsidiaries** In the Parent Company, shareholdings in subsidiaries are accounted for on a historical cost basis. The carrying amount is tested regularly against the subsidiaries' consolidated equity.

NOTE 2 SEGMENT REPORTING

BioGaia's operating segments consist of Pediatrics and Adult Health. The Pediatrics segment includes sales of drops, oral rehydration solution (ORS), digestive health tablets and also cultures as an ingredient in a licensee's product (such as infant formula), as well as royalties pertaining to Paediatric products.

The Adult Health segment mainly includes digestive health tablets, oral health products and also sales of cultures as an ingredient in a licensee's dairy product. Other consists of a number of smaller segments (such as royalties from the collaboration with Nestlé) and a few minor products, such as Animal Health products. Together these account for less than 10% of sales and are therefore not reported separately.

NET SALES BY SEGMENT:

Business unit	Group	
	2016	2015
Pediatrics	433,028	389,561
Adult Health	85,274	74,667
Other	16,394	19,013
	534,696	483,241

GROSS PROFIT BY SEGMENT:

Business unit	Group	
	2016	2015
Pediatrics	318,811	266,391
Adult Health	52,917	51,907
Other	16,079	18,286
	387,807	336,584

The discontinued operations had no revenue and no gross profit, only operating expenses, see Note 5, and do not affect the above figures.

In 2016, SEK 184.6 million (177.2), or 34.5% (36.7%) of revenue in the Group, was attributable to three customers. The largest of these three customers belongs to the Pediatrics segment, while the two others belong to both the Pediatrics and Adult Health segments. In 2016 there was one customer that accounted for more than 10% of sales. In 2015 there were two customers who each accounted for more than 10% of sales.

NET SALES BY GEOGRAPHICAL MARKET:

	Group		Parent Company	
	2016	2015	2016	2015
Europe	348,175	284,729	348,175	284,729
USA and Canada	40,222	35,231	40,184	33,589
Asia	61,963	52,130	45,612	41,143
Rest of World	84,336	111,151	84,336	111,151
	534,696	483,241	518,307	470,612

More than 90% of the Group's total assets, amounting to SEK 488,978 thousand (473,478), are located in Europe.

Of the Group's capital expenditure on property, plant and equipment and intangible assets, totalling SEK 5,610 thousand (27,930), more than 90% pertained to Europe.

Sales in Sweden amounted to SEK 14.3 million (13.0), or 2.7% (2.7%) of total sales in the Group, excluding the license revenue.

The Group's non-current assets amount to SEK 103.6 million, of which SEK 103.2 million is located in Sweden and SEK 0.4 million in other countries (the USA and Japan).

NOTE 3 REVENUE

	Group		Parent Company	
	2016	2015	2016	2015
Product revenue	457,789	442,565	441,400	429,936
Royalties	76,907	40,676	76,907	40,676
	534,696	483,241	518,307	470,612

NOTE 4 EMPLOYEES AND PERSONNEL EXPENSES, REMUNERATION TO SENIOR EXECUTIVES

AVERAGE NUMBER OF EMPLOYEES BY COUNTRY:

	2016		2015	
	Of whom, men		Of whom, men	
<i>Parent Company:</i>				
Sweden	68	24	61	21
<i>Subsidiaries:</i>				
Sweden	32	16	28	15
Japan	6	4	6	4
USA	2	1	3	1
Total subsidiaries	40	21	37	20
Total Group	108	45	98	41

The number of employees in the Group at 31 December, 2016 was 109 (101).

SALARIES AND OTHER REMUNERATION DIVIDED BY COUNTRY AND BETWEEN THE BOARD/MANAGING DIRECTOR AND OTHER EMPLOYEES:

	2016		2015	
	Board and Managing Director	Other employees	Board and Managing Director	Other employees
<i>Parent Company:</i>				
Sweden	3,156	3,641	44,844	36,326
<i>Subsidiaries:</i>				
Sweden	1,770	1,720	7,419	6,607
Japan	2,102	2,213	2,730	2,808
USA	–	–	3,356	2,630
Total subsidiaries	3,872	3,933	13,505	12,045
Total Group	7,028	7,574	58,349	48,371

TOTAL SALARIES AND SOCIAL SECURITY EXPENSES:

	Group		Parent Company	
	2016	2015	2016	2015
Salaries and other remuneration	65,376	55,945	48,000	39,967
Pension expenses for the Board and Managing Director	979	1,267	440	734
Pension expenses for other employees	6,215	5,213	5,486	4,679
Other social security expenses	18,668	15,896	14,939	12,468
	91,238	78,321	68,865	57,848



Cont'd, Note 4

Pensions and health insurance: All employees in Sweden are subject to mandatory retirement in accordance with Swedish law. 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	4.5%	30%	0%

All employees are covered by health insurance, with benefits. 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.

BioGaia's incentive scheme for the employees BioGaia currently has no incentive scheme in place for the employees.

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.

Remuneration to the Managing Director, Group President and other senior executives employed by the company consists of basic salary and other benefits. Other senior executives consist of the 7 persons who together with the Managing Director make up the Executive Management.

In the event of termination by the company, the Managing Director is entitled to full salary during an 12 month period of notice and the Group President and Vice Presidents are entitled to full salary during an 18 month period of notice. In the event of termination by the company, other senior executives have a statutory notice period of at least 3 months in accordance with the Swedish Employment Protection Act. For the Group President, Peter Rothschild the company made an extra pension provision of SEK 700,000 in 2015 and of SEK 500,000 in 2016. In other respects, the Managing Director and Group President have the same benefits as other employees.

Otherwise, no agreements for termination benefits exist for the Managing Director, Group President or other senior executives.

REMUNERATION AND OTHER BENEFITS DURING THE YEAR:

	Director's fees	Basic salary	Other benefits	Pension insurance incl. health insurance	Other remuneration	Total
Board Chairman:						
David Dangoor:	300					300
Board members:						
Jan Annwall	150				225	375
Ewa Björling	150					150
Stefan Elving	150					150
Inger Holmström	150					150
Anthon Jahreskog	150					150
Brit Stakston	150					150
Paula Zeilon	150					150
Managing Director: Axel Sjöblad	1,806	178		440		2,424
Group President/former Managing Director Peter Rothschild	2,415			500		2,915
Other senior executives (7 persons):	7,998			1,995		9,993
	1,350	12,219	178	2,935	225	16,907

Comment on the table above:

Other benefits consist of housing benefits. Other remuneration refers to Board member Jan Annwall, who works as a consultant to BioGaia to a limited extent.

GENDER DISTRIBUTION:

	2016 Women	2015 Women	2016 Men	2015 Men
Board members	4	4	4	4
Management including Managing Director and Group President	5	7	4	5

NOTE 5 DISCONTINUED OPERATIONS (DISTRIBUTION)

BioGaia's former subsidiary IBT was distributed to BioGaia's shareholders on 22 March 2016. Below is a presentation of the profit/loss, assets, liabilities and cash flows from the discontinued operations.

RESULTS FROM DISCONTINUED OPERATIONS

	2016	2015
Net sales	-	-
Selling expenses	-	-2,600
Research and development expenses	-5,101	-17,974
Other operating income/expenses	-61	-41
Operating result	-5,162	-20,615
Financial expenses	-2	-9
The difference between the fair value of the IBT's shares and the book value	73,099	-
Profit/loss for the period	67,935	-20,624

ASSETS ATTRIBUTABLE TO DISCONTINUED OPERATIONS

	31 Dec 2016	31 Dec 2015
Intangible assets	-	16,225
Current assets excl. cash and cash equivalents	-	1,488
Cash and cash equivalents	-	44,411
Total assets	-	62,124
Trade payables	-	518
Accrued expenses	-	7,079
Other current liabilities	-	138
Total liabilities	-	7,735

CASH FLOW FROM DISCONTINUED OPERATIONS

	2016	2015
Operating activities	-6,781	-30,895
Investing activities	-	-10,150
Total cash flow	-6,781	-41,045

NOTE 6 AUDITOR'S FEES

	Group		Parent Company	
	2016	2015	2016	2015
<i>Grant Thornton Sweden AB:</i>				
Audit assignments	-	167	-	108
Audit services in addition to audit	-	58	-	39
Audit advice	-	38	-	33
Tax advice	-	16	-	-
Other services	-	-	-	-
<i>Deloitte AB</i>				
Audit assignments	500	440	500	365
Audit services in addition to audit	20	95	20	95
Tax advice	40	10	40	10
Other services	-	-	-	-
<i>Cherry, Bekaert & Holland, LLP:</i>				
Audit assignments	57	70	-	-
Other services	276	201	-	-

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. Since the 2015 Annual General Meeting, Deloitte is the appointed auditor for the Group.

NOTE 7 SHARE OF PROFIT OF ASSOCIATES

	Group	
	2016	2015
Share of profit of MetaboGen AB	-1,184	-65
	-1,184	-65

NOTE 8 OTHER OPERATING INCOME

	Group		Parent Company	
	2016	2015	2016	2015
Exchange gains on operating receivables and liabilities, net	5,610	1,773	6,002	1,789
	5,610	1,773	6,002	1,789

NOTE 9 OPERATING EXPENSES ALLOCATED BY TYPE OF COST

	Group		Parent Company	
	2016	2015	2016	2015
Cost of sales	146,889	146,657	164,201	157,364
Personnel expenses	93,671	88,314	70,776	60,827
Depreciation/amortization	7,074	6,548	449	560
Other operating expenses	92,051	70,631	102,405	87,525
	339,685	312,150	337,831	306,276

Operating expenses include lease payments of SEK 177 thousand (177). The total amount of minimum future lease payments falls due as follows:

- Within one year: SEK 66 thousand
- Within two to five years: SEK 84 thousand
- After five years: -

The Group's future payment commitments for rents amount to SEK 22.6 million, of which SEK 17.6 million refers to the Parent Company. The Group's rents fall due for payment in an amount of SEK 5.8 million within one year and SEK 16.8 million within two to five years.

NOTE 10 FINANCIAL INCOME

	Group		Parent Company	
	2016	2015	2016	2015
Exchange gains, forward exchange contracts	-	5,107	-	5,107
Interest income	1,429	331	2,007	1,014
	1,429	5,438	2,007	6,121

NOTE 11 FINANCIAL EXPENSES

	Group		Parent Company	
	2016	2015	2016	2015
Exchange losses, forward exchange contracts	4,685	-	4,685	-
Other financial expenses	122	260	113	193
	4,807	260	4,798	193

At 31 December 2016 the Parent Company and the Group had outstanding foreign exchange contracts for EUR 11.1 million (11.8) at an average exchange rate of SEK 9.45 and USD 2.2 million (1.0) at an average exchange rate of SEK 8.76. The unrealized foreign exchange gain/loss is reported in financial income/expense.

NOTE 12 TAX ON PROFIT FOR THE YEAR

	Group		Parent Company	
	2016	2015	2016	2015
Current tax	-47,124	-40,435	-43,156	-34,847
Deferred tax	10,414	-159	-	-
	-36,710	-40,594	-43,156	-34,847



Cont'd, Note 12

DEFERRED TAX IN UNTAXED RESERVES:

	Group		Parent Company	
	2016	2015	2016	2015
Deferred tax attributable to untaxed reserves	332	351	-	-
	332	351	-	-

CHANGES IN DEFERRED TAX LIABILITY:

	Group	
	2016	2015
Opening balance deferred taxes	351	192
Reversal of deferred tax	-19	-
Provision for deferred tax	-	159
Closing deferred tax	332	351

The deferred tax liability is attributable to the subsidiary TwoPac AB.

CHANGE IN DEFERRED TAX ASSETS:

	Group	
	2016	2015
Opening balance, deferred tax	-	-
Provisions for deferred tax	10,433	-
Closing balance, deferred tax	10,433	-

The deferred tax asset is attributable to the Japanese subsidiary.

RECONCILIATION OF NOMINAL TAX AND ACTUAL TAX EXPENSES:

	Group		Parent Company	
	2016	2015	2016	2015
Reported profit before tax	196,059	177,977	180,109	165,627
Tax rate	22.0%	22.0%	22.0%	22.0%
Anticipated tax expense	-43,133	-39,154	-39,624	-36,438
Tax effect of other non-deductible and non-taxable items	-2,103	-767	-1,890	3,127
Tax effect of loss carryforwards	10,182	863	-	-
Tax effect attributable to previous years	-1,643	-1,536	-1,642	-1,536
Other tax adjustment	-13	-	-	-
Actual tax expense	-36,710	-40,594	-43,156	-34,847

The tax rate for the Group was 19% (23%) of profit for the year after financial items. At 31 December 2016 the subsidiary BioGaia Japan had a cumulative tax loss carryforward of approximately SEK 35.2 million. As a result of the new distribution and licensing agreement that was signed in December 2016 (for more information, see the administration report), it will be possible to utilize a large share of the loss carryforward in the Japanese company. Because the Group recognizes exclusivity fees successively over the term of the agreement, a deferred asset is recognized on the temporary difference. Cumulative loss carryforwards amount to approximately SEK 34.9 million and expire in 2022.

The company has had a tax matter pertaining to the 2014 financial year concerning an openly reported marketing contribution to the Japanese subsidiary. The Administrative Courts have not yet announced their ruling. However, the company has not been given a reprieve to pay the tax liability, for which reason tax expenses of SEK 1.6 million attributable to earlier financial years have been charged to profit for 2016.

NOTE 13 NON-CONTROLLING INTERESTS (CONTINUING OPERATIONS)

	2016	2015
At beginning of year	-18	99
Profit for the year attributable to non-controlling interests (continuing operations)	-	-114
Dividend IBT's shares	-	-3
At end of year	-18	-18

The non-controlling interests refer to a 9.9% stake in the subsidiary CapAble AB that is held by its President Staffan Pålsson.

NOTE 14 INTANGIBLE ASSETS

GROUP:

	Capitalized development expenditure	Licenses and brands	Total intangible assets
<i>Accumulated cost:</i>			
Opening balance, 1 January 2015	32,950	2,528	35,478
Additions	10,150	-	10,150
Closing balance, 31 December 2015	43,100	2,528	45,628
Opening balance, 1 January 2016	43,100	2,528	45,628
Distribution of IBT's shares	-43,100	-	-43,100
Closing balance, 31 December 2016	-	2,528	2,528

Accumulated amortization

Opening balance, 1 January 2015	26,875	2,528	29,403
The year's amortization	-	-	-
Closing balance, 31 December 2015	26,875	2,528	29,403
Opening balance, 1 January 2016	26,875	2,528	29,403
Distribution of IBT's shares	-26,875	-	-26,875
Closing balance, 31 December 2016	-	2,528	2,528

Carrying amounts:

At 1 January 2015	6,075	-	6,075
At 31 December 2015	16,225	-	16,225
At 31 December 2016	-	-	-

Capitalized expenses include internally generated and externally acquired assets. Investments in capitalized development expenditures are related to development of a product for the NEC project in the former subsidiary IBT AB.

Since the company distributed the shares in IBT to BioGaia's shareholders in March 2016 and IBT is thus no longer part of the Group, the value of the capitalized expenses in BioGaia was zero at 31 December 2016.

No other development expenses in the subsidiaries or the Parent Company meet the criteria for capitalization in the balance sheet.

Cont'd, Note 14

TOTAL RESEARCH AND DEVELOPMENT EXPENDITURE:

	Group		Parent Company	
	2016	2015	2016	2015
Total R&D expenditure excl. amortization	63,526	52,745	64,049	53,890
The year's capitalization of development expenses	-	-	-	-
Uncapitalized R&D expenses	63,526	52,745	64,049	53,890
Amortization component of R&D expenses *)	269	538	155	182
R&D expenses with an effect on profit/loss	63,795	53,283	64,204	54,072

*) This amount refers only to the portion of depreciation on property, plant and equipment attributable to the research and development function in the income statement classified by function.

NOTE 15 PROPERTY, PLANT AND EQUIPMENT

GROUP:

	Land and buildings	Production equipment	Work in progress	Office equipment and computers	Total property, plant and equipment
	<i>Accumulated cost:</i>				
Opening balance, 1 January 2015	49,898	26,450	14,780	16,055	107,183
Adjustment opening balance	-	775	-	-	775
Additions	12,577	3,413	2,243	321	18,555
Sales and disposals	-	-	-	-910	-910
Reclassifications	-	6,499	-6,499	-	-
Exchange differences	-	-	-	128	128
Closing balance, 31 December 2015	62,475	35,587	10,524	15,594	124,181
Opening balance, 1 January 2016	62,475	35,587	10,524	15,594	124,181
Additions	3,437	1,120	-	1,056	5,613
Sales and disposals	-	-310	-	-1,119	-1,429
Exchange differences	-	-	-	99	99
Closing balance, 31 December 2016	65,912	36,397	10,524	15,630	128,464
<i>Accumulated depreciation</i>					
Opening balance, 1 January 2015	2,528	17,319	-	14,584	34,431
Adjustment opening balance	-	-775	-	-	-775
Depreciation	1,798	3,656	-	910	6,363
Impairment losses	-	959	-	-	959
Sales and disposals	-	-	-	-839	-839
Exchange differences	-	-	-	106	106
Closing balance, 31 December 2015	4,326	21,159	-	14,761	40,245
Opening balance, 1 January 2016	4,326	21,159	-	14,761	40,245
Depreciation	1,856	4,519	-	700	7,075
Sales and disposals	-	-310	-	-1,062	-1,372
Exchange differences	-	-	-	85	85
Closing balance, 31 December 2016	6,182	25,368	-	14,484	46,033

Cont'd, Note 15

Carrying amounts:

At 1 January 2015	47,370	9,131	14,780	1,471	72,752
At 31 December 2015	58,150	14,429	10,524	833	83,936
At 31 December 2016	59,731	11,030	10,524	1,146	82,431

PARENT COMPANY:

	Production equipment	Office equipment and computers	Total property, plant and equipment
<i>Accumulated cost:</i>			
Opening balance, 1 January 2015	3,559	11,413	14,972
Additions	-	60	60
Closing balance, 31 December 2015	3,559	11,473	15,032
Opening balance, 1 January 2016	3,559	11,473	15,032
Additions	-	283	283
Closing balance, 31 December 2016	3,559	11,756	15,315

Accumulated depreciation:

Opening balance, 1 January 2015	2,817	10,796	13,613
Depreciation	249	310	559
Closing balance, 31 December 2015	3,066	11,106	14,172
Opening balance, 1 January 2016	3,066	11,106	14,172
Depreciation	249	201	450
Closing balance, 31 December 2016	3,315	11,307	14,622

Carrying amounts:

At 1 January 2015	742	617	1,359
At 31 December 2015	493	367	860
At 31 December 2016	244	449	693

Depreciation on property, plant and equipment is recognized on the following lines in the income statement:

	Group		Parent Company	
	2016	2015	2016	2015
Cost of sales	5,141	4,240	-	-
Selling expenses	1,225	1,265	243	305
Administrative expenses	446	505	54	73
Research and development expenses	263	538	153	182
	7,075	6,547	450	560



NOTE 16 FINANCIAL ASSETS

PARENT COMPANY

Participations in group companies	2016	2015
At beginning of year	132,938	69,130
Group contribution paid to CapAble AB	3,578	2,374
Group contribution paid to TriPac AB	1	8
Dividend shares in IBT	-81,806	-
Group contribution paid to IBT AB	-	20,601
Impairment loss on shares in IBT AB	-	-20,601
Impairment loss on shares in CapAble AB	-3,578	-2,374
New share issue in IBT AB	-	52,800
Shareholder contribution paid to IBT AB	-	11,000
Carrying amount at end of year	51,133	132,938

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	3,590
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
			51,133

The assets and liabilities of the American subsidiary BioGaia Biologics Inc. have been translated at the closing day rate of exchange, SEK 9.10 (8.42). All items in the income statement have been translated at the average exchange rate during the year, SEK 8.56 (8.42). The assets and liabilities of the Japanese subsidiary BioGaia Japan Inc. have been translated at an exchange rate of SEK 0.078 (0.070). All items in the income statement have been translated at an exchange rate of SEK 0.079 (0.070). The resulting translation differences have been recognized in consolidated comprehensive income.

CapAble AB was formed in 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 -18 thousand.

TwoPac AB was formed in 2002 and is 100% owned by BioGaia since 1 July 2013.

Of total purchases made by the Parent Company, 23.5% (19.5) was attributable to group companies. Of total sales made by the Parent Company, 1.2% (2.2) was attributable to group companies.

INVESTMENTS IN ASSOCIATES

	Group		Parent Company	
	2016	2015	2016	2015
At beginning of year	7,936	0	8,000	0
Reclassification of MetaboGen AB to associate	-	8,000	-	8,000
Acquisition of shares in MetaboGen AB	4,000	-	4,000	-
Share of profit for the year	-1,184	-64	-	-
Carrying amount at end of year	10,752	7,936	12,000	8,000

SPECIFICATION OF THE PARENT COMPANY'S EQUITY HOLDINGS IN ASSOCIATES

Associated company/Corp. ID no./Domicile	No. of shares	Holding, %	Carrying amount
MetaboGen AB/556872-7142/Göteborg	315	36	12,000

NOTE 17 NON-CURRENT RECEIVABLES FROM SUBSIDIARIES

NON-CURRENT RECEIVABLES FROM SUBSIDIARIES:

	Parent Company	
	2016	2015
At beginning of year	55,835	41,013
Payment of loan to BioGaia Japan Inc.	-	4,052
Payment of loan to TwoPac AB	-	15,844
Repayment of debt from CapAble	-	-1,022
Exchange difference related to loan to BioGaia Japan Inc.	7,208	4,181
Provisions for net receivable ¹⁾	-7,208	-8,233
	55,835	55,835

¹⁾ Due to uncertainty as to whether the receivable from the subsidiary in Japan will be repaid within the foreseeable future, a provision has been made for the net amount.

NON-CURRENT RECEIVABLES FROM GROUP COMPANIES AT 31 DECEMBER 2016:

	Parent Company	
	2016	2015
TwoPac AB	55,835	55,835
Closing balance at end of year	55,835	55,835

NOTE 18 INVENTORIES

	Group		Parent Company	
	2016	2015	2016	2015
Raw materials and consumables	8,891	6,396	-	-
Finished goods and goods for resale	31,588	37,150	28,438	34,137
	40,479	43,546	28,438	34,137

The Group's provisions for obsolescence amounted to SEK 5,471 thousand (3,362) at 31 December 2016. Expenses related to impairment losses on inventory and scrapping amount to SEK 2,872 thousand (3,690) at 31 December 2016.

NOTE 19 TRADE RECEIVABLES

Provisions for bad debt losses amounted to SEK 1,899 thousand (1,899) at 31 December 2016.

At 31 December 2016, trade receivables of SEK 38,598 thousand (13,435) were overdue without any assessed grounds for impairment. Of the overdue receivables, SEK 36,374 had been recovered as of the closing date.

AGE ANALYSIS:

	Group		Parent Company	
	2016	2015	2016	2015
Less than 3 months	33,962	12,414	33,948	12,414
3-6 months	767	1,021	767	1,021
More than 6 months	3,869	-	3,869	-
	38,598	13,435	38,584	13,435

Cont'd. Note 19

THE CARRYING AMOUNTS, BY CURRENCY, ARE AS FOLLOWS:

	Group		Parent Company	
	2016	2015	2016	2015
SEK	9,318	14,169	9,318	14,169
EUR	24,381	28,864	24,381	28,363
USD	35,702	17,981	35,688	17,981
GBP	-	7	-	7
DKK	-	30	-	30
JPY	6,268	4,886	-	-
	75,668	65,937	69,387	60,550

NOTE 20 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, Group President of BioGaia AB, and Jan Annwall, a member of the Board of the Parent Company. The only transactions that took place during 2016 was a dividend of SEK 5.00 per share and remuneration and director's fees - for further information see note 4.

Parent Company The Parent Company owns 100% of TwoPac AB, BioGaia Biologics Inc., USA, BioGaia Japan Inc. and Tripac AB.

The Parent Company owns 90.1% of the shares in CapAble AB. BioGaia's former subsidiary IBT was distributed to BioGaia's shareholders on 22 March 2016, see note 5.

THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH TWOPAC AB (INCLUDING TWOPAC'S WHOLLY OWNED SUBSIDIARIES):

	Parent Company	
	2016	2015
Interest income	584	683
Loan paid	-	-15,844
Purchase of services	-2,300	-1,601
Purchase of goods	-68,031	-50,561

Goods are purchased on a cost plus basis.

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

	Parent Company	
	2016	2015
Interest income	1,195	942
Purchase of services	-807	-
Loan paid ¹⁾	-	-4,052
Sale of goods ²⁾	8,283	11,455
Marketing contribution paid	-6,672	-10,727

¹⁾ Due to uncertainty as to whether the loan to BioGaia Japan will be recovered within the foreseeable future, a provision has been made for the net amount.

²⁾ BioGaia has delivered products but only invoiced a small amount in 2015 and 2016, since the bulk refers to marketing contributions during the start-up phase.

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

	Parent Company	
	2016	2015
Purchase of services	-6,901	-5,476

THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH CAPABLE AB:

	Parent Company	
	2016	2015
Repayment of Loan	-	1,022
Sale of Services	128	148
Group contribution paid	-3,577	-2,374

THE FOLLOWING TRANSACTIONS HAVE TAKEN PLACE WITH TRIPAC AB:

	Parent Company	
	2016	2015
Group contribution paid	-1	-8

THE CLOSING BALANCE AT THE END OF THE PERIOD WAS AS FOLLOWS:

	Parent Company	
	31 Dec. 2016	31 Dec. 2015
Non-current receivables from subsidiaries		
Non-current receivables, TwoPac AB	55,835	55,835
	55,835	55,835
Current liabilities from subsidiaries		
Current liabilities, BioGaia Biologics Inc	-2,678	-1,627
Current liabilities, CapAble AB	-5,295	-3,700
Current liabilities, Tripac AB	-4,671	-4,670
Current liabilities, TwoPac AB	-8,169	-8,303
	-20,813	-18,300
Current receivables from subsidiaries		
Current receivables, IBT AB	-	180
Current receivables, BioGaia Japan Inc.	8,956	849
	8,956	1,029

See also Note 4 for other related party transactions.

NOTE 21 OTHER RECEIVABLES

	Group		Parent Company	
	2016	2015	2016	2015
VAT refund	5,511	4,948	5,364	4,402
Current tax asset	-	7,129	1,371	5,363
Other receivables	840	2,652	661	2,601
	6,351	14,729	7,396	12,366

Other receivables above include forward exchange contracts with a fair value of SEK 2.0 million in 2016. All forward exchange contracts are attributable to level 2 of the fair value hierarchy.



NOTE 22 DEFERRED EXPENSES AND ACCRUED INCOME

	Group		Parent Company	
	2016	2015	2016	2015
Accrued income	16,538	9,022	16,538	9,022
Prepaid rents	1,314	1,141	1,190	879
Other deferred expenses	1,907	3,791	36	1,304
	19,759	13,954	17,764	11,205

NOTE 23 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 financial assets at fair value through profit or loss consist of cash and cash equivalents and short-term investments. The financial assets are recognized in the balance sheet and are valued at the closing day rate of exchange.

	Fair value		Carrying amount	
	31 Dec, 2016	31 Dec, 2015	31 Dec, 2016	31 Dec, 2015
Assets				
Cash and cash equivalents in SEK	160,939	172,449	160,939	172,449
Cash and cash equivalents in EUR	72,481	23,322	72,481	23,322
Cash and cash equivalents in USD	4,157	27,446	4,157	27,446
Cash and cash equivalents in JPY	4,264	1,783	4,264	1,783
Cash and cash equivalents in DKK	475	1,882	475	1,882
Cash and cash equivalents in CHF	753	–	753	–
Total assets	243,069	226,882	243,069	226,882

Short-term investments refer to listed securities. The shares are recognized at historical cost less accumulated impairment. The fair value refers to the bid price on the balance sheet date. The intention is to sell the shares when an appropriate occasion arises.

The company has taken forward currency hedges in EUR and USD. The forward currency hedges have been recognized at their fair value at 31 December 2016. This value is included in other liabilities – see Note 26. In BioGaia's measurement of fair value, the fair values of financial assets and financial liabilities are determined according to level 2.

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

Loans and receivables The Group's trade receivables amount to SEK 75,668 thousand (65,937). 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, 2016	31 Dec, 2015	31 Dec, 2016	31 Dec, 2015
Trade payables	16,951	23,638	16,951	23,638
Prepayments from customers	21,798	16,762	21,798	16,762
Total other financial liabilities	38,749	40,400	38,749	40,400

NOTE 24 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 16,595,794 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 foreign currency translation reserve arises in translation of the net assets of foreign operations according to the acquisition method.

Retained earnings consist of other equity. The Parent Company's dividend for 2015, as resolved on by the 2016 AGM, was SEK 86.7 million, equal to SEK 5.00 per share. For 2016 the Board of Directors proposes that the company pay a dividend according to policy of SEK 3.16 per share and an extraordinary dividend of SEK 4.34 per share, amounting to a total dividend of SEK 7.50 per share. This is equal to a total dividend of SEK 130.0 million.

Non-controlling interests account for 9.9% of equity in the subsidiary CapAble. 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 2016, total consolidated equity amounted to SEK 415.2 million (395.8) and equity attributable to owners of the Parent Company amounted to SEK 415.2 million (395.9).

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

KEY RATIOS

	2016	2015
Number of shares at 31 Dec., thousands	17,336	17,336
Average number of shares, thousands	17,336	17,309
Average number of shares after dilution, thousands	17,336	17,309
Earnings per share, continuing operations, SEK	9.19	7.94
Earnings per share, SEK	13.13	7.01
Earnings per share after dilution, SEK	13.13	7.01
Equity per share, SEK	23.95	22.87
Equity per share after dilution, SEK	23.95	22.87
Return on equity, %	56	33
Share price on closing day, SEK	300.00	281.50
Dividend per share, SEK	7.50 ¹⁾	5.00

¹⁾ Dividend proposed but not yet approved. The Board and President propose that the company pay an ordinary dividend of SEK 3.16 per share and an extraordinary dividend of SEK 4.34 per share, equal to a total dividend of SEK 7.50 per share.

NOTE 25 PROPOSED APPROPRIATION OF PROFITS

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

Retained earnings	223,491,724
Profit for the year	136,953,063
Together amounting to	360,444,787

The Board of Directors proposes that the profits be appropriated as follows

To be paid as a dividend to the shareholders	130,023,465
To be carried forward to new account	230,421,322
Total	360,444,787

NOTE 26 OTHER LIABILITIES

	Group		Parent Company	
	2016	2015	2016	2015
Employee withholding tax	1,681	1,572	1,410	1,153
Current tax liabilities	94	–	–	–
Other current liabilities	7,560	3,182	1,736	–
	9,335	4,754	3,146	1,153

Other current liabilities above include forward exchange contracts with a fair value of SEK 1.7 million in 2016. All forward exchange contracts are attributable to level 2 of the fair value hierarchy.

NOTE 27 ACCRUED EXPENSES AND DEFERRED INCOME

	Group		Parent Company	
	2016	2015	2016	2015
Accrued holiday pay	7,598	6,829	6,269	4,916
Accrued social security expenses	1,484	1,580	1,115	957
Other accrued expenses	16,299	23,431	16,152	17,165
	25,381	31,840	23,536	23,038

NOTE 28 PLEDGED ASSETS AND CONTINGENT LIABILITIES

	Group		Parent Company	
	2016	2015	2016	2015
Pledged assets				
Floating charges	2,000	2,000	2,000	2,000
Assets pledged for construction of a facility for the subsidiary TwoPac AB	253	690	–	–
	2,253	2,690	2,000	2,000
Contingent liabilities	None	None	None	None

The floating charges relate to credit for credit cards.

NOTE 29 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 minimize 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 conducts operations in various geographical markets and has revenue and expenses in different currencies. This affects both transaction exposure (cash flow) and translation exposure (the balance sheet).

Transaction exposure

The breakdown of net sales in 2016 was approximately:	The breakdown of expenses in 2016 was approximately:
EUR 50%	SEK 55%
USD 21%	EUR 27%
SEK 15%	JPY 9%
Other currencies 14%	USD 8%
	Other currencies 1%

In 2016 the company had a cash flow surplus of approximately EUR 23.8 million (14.5), a cash flow surplus/deficit of JPY 29.4 million (-62.0) and a cash flow surplus of USD 11.1 million (12.8).

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 2016 the company had outstanding forward exchange contracts for EUR 11.1 million at an average exchange rate of SEK 9.45 and USD 2.2 million USD at an average exchange rate of SEK 8.76. Forward exchange contracts amounting to EUR 3.3 million will mature for payment in 2018 and contracts amounting to EUR 7.8 million and USD 2.2 million will mature in 2017. The actual exchange gain/loss depends on the exchange rate on the maturity date of the contracts. For more information, see Notes 10, 11, 23 and 26.

The average exchange rate for EUR/SEK in 2016 was SEK 9.47. If the EUR/SEK rate had been SEK 0.10 higher/lower, BioGaia's net sales would have been approximately SEK 2.8 million higher/lower and operating profit would have been approximately SEK 1.8 million higher/lower.

The average exchange rate for USD/SEK in 2016 was SEK 8.56. If the USD/SEK rate had been SEK 0.10 higher/lower, BioGaia's sales would have been approximately SEK 1.3 million higher/lower and operating profit would have been approximately SEK 1.0 million higher/lower. A stronger SEK rate, primarily against the EUR and USD, decreases BioGaia's sales and profit, but through forward exchange transactions and by working to reallocate a portion of expenses to EUR, the company is working to minimize the impact on profit. BioGaia is also trying to reallocate a portion of revenue from EUR to other currencies.

Translation exposure Translation exposure is the risk that the value of the Group's net investments in foreign currencies will be negatively affected by changes in foreign exchange rates.

The Group has two foreign subsidiaries, one in the USA and one in Japan. The assets and liabilities of the American subsidiary, BioGaia Biologics Inc., have been translated at the closing day rate of SEK 9.10 (8.42). Items in the income statement have been translated at an average rate of SEK 8.56 (8.42). The assets and liabilities of the Japanese subsidiary, BioGaia Japan Inc., have been translated at a rate of SEK 0.078 (0.070). The translation difference amounted to SEK 0.2 million (0.1) for the American subsidiary and SEK 0.7 million (0.3) for the Japanese subsidiary.

Interest rate and liquidity risk The Group has no external loans. Excess liquidity is invested mainly in bank accounts. For cash and cash equivalents, the company has a liquidity policy in which the basic principles are that investment risks should always be minimized and investments should be made primarily in Swedish kronor. To minimize currency risk, other currencies may also be considered. 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.



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 trade receivables and additional evaluation of the customers' financial position is carried out when needed in order to minimize risks.

Cash flow risk Cash flow for the period amounted to SEK 14.0 million (15.1). Cash flow included, dividends of SEK 86.7 million (86.4) and tax payments of SEK 43.4 million (50.1).

BioGaia's former subsidiary IBT was distributed to the shareholders in March 2016. Excluding IBT, cashflow was SEK 58.4 million (56.1).

Age analysis of the Group's liabilities:

	Due in less than:					Total
	Interest rate	1-3 months	3-12 months	1-5 years		
31 December 2015						
Non-current liabilities	-			351		351
Current liabilities	-	28,099	544	48,351		76,994
		28,099	544	48,351	351	77,345
31 December 2016						
Non-current liabilities	-			332		332
Current liabilities	-	20,113	6,822	46,531		73,466
		20,113	6,822	46,531	332	73,798

Because cash and cash equivalents at 31 December 2016 amounted to SEK 243.1 million (226.9), no infusion of capital is necessary during the coming 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.

NOTE 30 CRITICAL ACCOUNTING ESTIMATES AND ASSUMPTIONS

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

Associated company MetaboGen AB Since 1 December 2016, BioGaia owns 36% of MetaboGen AB (for more information, see Administration report). The remaining shares are held by the researchers who founded the company and GU Holding. So far, MetaboGen has shown a loss. On the balance sheet date, assets in MetaboGen were reported at SEK 10.8 million in the Group. BioGaia's assessment is that MetaboGen will show profitability in the future, for which reason there was no indication of impairment on the balance sheet date.

The Board of Directors and the Managing Director 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, 27 February 2017

David Dangoor
Chairman

Axel Sjöblad
Managing Director

Jan Annwall
Member of the Board

Ewa Björling
Member of the Board

Stefan Elving
Member of the Board

Inger Holmström
Member of the Board

Anthon Jahreskog
Member of the Board

Brit Stakston
Member of the Board

Paula Zeilon
Member of the Board

My audit report was submitted on 10 March 2017

Deloitte AB

Birgitta Löf
Authorized Public Accountant

Auditor's report

To the annual meeting of the shareholders of BioGaia AB (publ)
Corporate identity number 556380-8723

REPORT ON THE ANNUAL ACCOUNTS AND CONSOLIDATED ACCOUNTS

OPINIONS

We have audited the annual accounts and consolidated accounts of BioGaia AB (publ) for the financial year from 1 January 2016 to 31 December 2016. The annual accounts and consolidated accounts of the company are included on pages 37-60 in this document.

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 parent company as of 31 December 2016 and its financial performance and cash flow 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 2016 and their financial performance and cash flow for the year then ended in accordance with International Financial Reporting Standards (IFRS), as adopted by the EU, and the Annual Accounts Act.

We therefore recommend that the general meeting of shareholders adopts the statement of comprehensive income and statement of financial position for the parent company and the group.

BASIS FOR OPINIONS

We conducted our audit in accordance with International Standards on Auditing (ISA) and generally accepted auditing standards in Sweden. Our responsibilities under those standards are further described in the Auditor's Responsibilities section. We are independent of the parent company and the group in accordance with professional ethics for accountants in Sweden and have otherwise fulfilled our ethical responsibilities in accordance with these requirements.

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

KEY AUDIT MATTERS

Key audit matters of the audit are those matters that, in our professional judgment, were of most significance in our audit of the annual accounts and consolidated accounts of the current period. These matters were addressed in the context of our audit of, and in forming our opinion thereon, the annual accounts and consolidated accounts as a whole, but we do not provide a separate opinion on these matters.

DISTRIBUTION OF THE SUBSIDIARY INFANT BACTERIAL THERAPEUTICS AB (IBT)

At the extraordinary general meeting in March 2016 the subsidiary IBT was distributed to the shareholders. IBT's carrying value in the parent company and in the Group amounted to SEK 81.8 million and SEK 49.0 million.

The Group applies IFRIC17 which means that the dividend should be recognized at the fair value of the assets distributed. The accounting is based on estimates that may have a significant impact on the Group's earnings and financial position.

For further information, please refer to the section "Other key events during the year" on page 38 and Note 5 to the financial statements.

Our audit included the following procedures but were not limited to these:

- We have examined BioGaia's dividend proposal and reasoned statement and evaluated these based on the rules of the Companies
- We have examined the calculation of the result of the dividend
- We have examined the relevant notes to the financial statements.

OTHER INFORMATION THAN THE ANNUAL ACCOUNTS AND CONSOLIDATED ACCOUNTS

This document also contains other information than the annual accounts and consolidated accounts and is found on pages 1-36 and 66-72. The Board of Directors and the Managing Director are responsible for this other information. Our opinion on the annual accounts and consolidated accounts does not cover this other information and we do not express any form of assurance conclusion regarding this other information.

In connection with our audit of the annual accounts and consolidated accounts, our responsibility is to read the information identified above and consider whether the information is materially inconsistent with the annual accounts and consolidated accounts. In this procedure we also take into account our knowledge otherwise obtained in the audit and assess whether the information otherwise appears to be materially misstated.

If we, based on the work performed concerning this information, conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

RESPONSIBILITIES OF THE BOARD OF DIRECTORS AND THE MANAGING DIRECTOR

The Board of Directors and the Managing Director are responsible for the preparation of the annual accounts and consolidated accounts and that they give a fair presentation in accordance with the Annual Accounts Act and, concerning the consolidated accounts, in accordance with IFRS as adopted by the EU. The Board of Directors and the Managing Director are also responsible for such internal control as they determine is necessary to enable the preparation of annual accounts and consolidated accounts that are free from material misstatement, whether due to fraud or error.

In preparing the annual accounts and consolidated accounts, the Board of Directors and the Managing Director are responsible for the assessment of the company's and the group's ability to continue as a going concern. They disclose, as applicable, matters related to going concern and using the going concern basis of accounting. The going concern basis of accounting is however not applied if the Board of Directors and the Managing Director intends to liquidate the company, to cease operations, or has no realistic alternative but to do so.

AUDITOR'S RESPONSIBILITY

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

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the annual accounts and consolidated accounts, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of the company's internal control relevant to our audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control.





- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Directors and the Managing Director.
- Conclude on the appropriateness of the Board of Directors' and the Managing Director's use of the going concern basis of accounting in preparing the annual accounts and consolidated accounts. We also draw a conclusion, based on the audit evidence obtained, as to whether any material uncertainty exists related to events or conditions that may cast significant doubt on the company's and the group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the annual accounts and consolidated accounts or, if such disclosures are inadequate, to modify our opinion about the annual accounts and consolidated accounts. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause a company and a group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the annual accounts and consolidated accounts, including the disclosures, and whether the annual accounts and consolidated accounts represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient and appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated accounts. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our opinions.

We must inform the Board of Directors of, among other matters, the planned scope and timing of the audit. We must also inform of significant audit findings during our audit, including any significant deficiencies in internal control that we identified.

We must also provide the Board of Directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Board of Directors, we determine those matters that were of most significance in the audit of the annual accounts and consolidated accounts, including the most important assessed risks for material misstatement, and are therefore the key audit matters. We describe these matters in the auditor's report unless law or regulation precludes disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

OPINIONS

In addition to our audit of the annual accounts and consolidated accounts, we have also audited the administration of the Board of Directors and the Managing Director of BioGaia AB (publ) for the financial year from 1 January 2016 to 31 December 2016 and the proposed appropriations of the company's profit or loss.

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

BASIS FOR OPINIONS

We conducted the audit in accordance with generally accepted auditing standards in Sweden. Our responsibilities under those standards are further described in the Auditor's Responsibilities section. We are independent of the parent company and the group in accordance with professional ethics for accountants in Sweden and have otherwise fulfilled our ethical responsibilities in accordance with these requirements.

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

RESPONSIBILITIES OF THE BOARD OF DIRECTORS AND THE MANAGING DIRECTOR

The Board of Directors is responsible for the proposal for appropriations of the company's profit or loss. At the proposal of a dividend, this includes an assessment of whether the dividend is justifiable considering the requirements which the company's and the group's type of operations, size and risks place on the size of the parent company's and the group's equity, consolidation requirements, liquidity and position in general.

The Board of Directors is responsible for the company's organization and the administration of the company's affairs. This includes among other things continuous assessment of the company's and the group's financial situation and ensuring that the company's organization is designed so that the accounting, management of assets and the company's financial affairs otherwise are controlled in a reassuring manner. The Managing Director shall manage the ongoing administration according to the Board of Directors' guidelines and instructions and among other matters take measures that are necessary to fulfill the company's accounting in accordance with law and handle the management of assets in a reassuring manner.

AUDITOR'S RESPONSIBILITY

Our objective concerning the audit of the administration, and thereby our opinion about discharge from liability, is to obtain audit evidence to assess with a reasonable degree of assurance whether any member of the Board of Directors or the Managing Director in any material respect:

- has undertaken any action or been guilty of any omission which can give rise to liability to the company, or
- Accounts Act or the Articles of Association.

Our objective concerning the audit of the proposed appropriations of the company's profit or loss, and thereby our opinion about this, is to assess with reasonable degree of assurance whether the proposal is in accordance with the Companies Act.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with generally accepted auditing standards in Sweden will always detect actions or omissions that can give rise to liability to the company, or that the proposed appropriations of the company's profit or loss are not in accordance with the Companies Act.

As part of an audit in accordance with generally accepted auditing standards in Sweden, we exercise professional judgment and maintain professional scepticism throughout the audit. The examination of the administration and the proposed appropriations of the company's profit or loss is based primarily on the audit of the accounts. Additional audit procedures performed are based on our professional judgment with starting point in risk and materiality. This means that we focus the examination on such actions, areas and relationships that are material for the operations and where deviations and violations would have particular importance for the company's situation. We examine and test decisions undertaken, support for decisions, actions taken and other circumstances that are relevant to our opinion concerning discharge from liability. 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.

Stockholm, 10 March 2017
Deloitte AB

Birgitta Löf
Authorized public accountant

Corporate governance report BioGaia AB 2016

Compliance with the Swedish Code of Corporate Governance The purpose of the Code is to strengthen confidence in Swedish listed companies by promoting positive development of the companies' corporate governance. The Code is based on the "comply or explain" principle, which means that a company may deviate from the Code but that any such deviations must be explained.

BioGaia has not deviated from any of the rules set out in the Code.

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

The share capital consists of 740,668 class A shares carrying 10 votes each and 16,595,794 class B shares carrying one vote each.

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 8.6% of the share capital and 34.0% of the votes in the company. Other individual shareholders hold less than 10% of the share capital and votes each.

2016 AGM BioGaia's AGM was held on 10 May 2016 and was attended by shareholders representing 59.1% of the total number of votes in the company. The AGM was also attended by the company's Managing Director, the Board members elected by the previous AGM except for Stefan Elving, and all of the Board members elected by the year's AGM except for Stefan Elving, as well as the company's elected auditor.

The AGM resolved on the following proposals, among others:

- Adoption of the annual report
- Discharge from liability for the Board of Directors and the Managing Director
- A dividend of SEK 5.00 per share
- Re-election of sitting Board members Jan Annwall, Ewa Björling, David Dangoor, Stefan Elving, Inger Holmström, Anthon Jahreskog, Brit Stakston and Paula Zeilon
- Re-election of David Dangoor as Board Chairman
- Re-election of the registered auditing firm Deloitte AB
- Board fees of SEK 300,000 to the Board Chairman and SEK 150,000 to each of the other Board members not employed by the company
- Payment of auditor's fees according to approved account
- Principles for remuneration and other terms of employment for senior executives in accordance with the Board's proposal
- Appointment of the Nominating Committee in accordance with the Nominating Committee's proposal

Extraordinary General Meeting on 18 March 2016 An Extraordinary General Meeting was held on Friday, 18 March 2016, at Lundqvist & Lindqvist Klara Strand, Klarabergsviadukten 90, in Stockholm.

The Extraordinary General Meeting of BioGaia AB (publ) on 18 March 2016 resolved on:

- the approval of BioGaia's transfers of 2,250 shares in BioGaia's subsidiary Infant Bacterial Therapeutics AB ("IBT") to each of Eamonn Connolly and Staffan Strömberg; and

- the distribution of all BioGaia's shares, namely 74,066 shares of series A and 1,659,579 shares of series B, in IBT, to BioGaia's shareholders, whereby one (1) series A share in BioGaia shall entitle to one (1) series A share fraction in IBT and one (1) series B share in BioGaia shall entitle to one (1) series B share fraction in IBT. Ten series A share fractions shall entitle to one (1) share of series A in IBT and ten series B share fractions shall entitle to one (1) share of series B in IBT. In the event that a shareholder's holding in BioGaia is not evenly divisible by ten, any excess share fractions that have not entitled to shares in IBT will be sold, free of brokerage fees, on the respective shareholder's behalf.

2017 AGM The 2017 AGM will be held at 5:00 p.m. on 3 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 is published in Svenska Dagbladet.

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

The 2016 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 2016. 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 its 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 2017 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. In the event that an appointed member of the Nominating Committee resigns from the Nominating Committee for some other reason, the shareholder who has appointed the member in question has the right to appoint a new representative, the Nominating Committee, if it deems so appropriate in respect of the remaining mandate period, shall ask the next largest shareholder in terms of voting power if it wishes to appoint a representative to the Nominating Committee."

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, Sebastian Jahreskog, who through direct and indirect ownership is the company's second largest shareholder, and Jannis Kitsakis, representing the company's third largest shareholder, Fjärde AP-Fonden. 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 2017 AGM for resolution:

- appointment of the Chairman of the AGM
- election of the Board of Directors
- election of the Board Chairman
- election of auditors
- fees for members of the Board
- fees for the auditors
- appointment of the Nominating Committee ahead of the 2018 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. In its motivation, the Nominating Committee gives consideration to diversity and breadth of experience on the Board and strives for an even gender distribution.

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 2016 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 68-69.

BioGaia's legal counsel has been appointed to serve as Secretary at Board meetings. The Managing Director and the Group President are not members of the Board but are 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 President and the structure of Board activities during the year. In addition to the responsibilities that are generally applicable pursuant to Swedish Companies Act, the Articles of Association and the Swedish Code of Corporate Governance, the following are regulated by the Board's rules of procedure:

- At least 5 Board meetings during the year, in addition to the statutory meeting.
- Establishment of the overall objectives for the company's operations and decision on the company's strategy.
- Approval of budgets and similar long-term plans, including the investment budget.
- Matters related to investments and similar in amounts of more than SEK 2 million.
- Decision on the purchase and sale of real estate, shares or the acquisition of another company's operations in amounts of more than SEK 2 million.
- Decision on the formation and capitalization of subsidiaries in amounts of more than SEK 2 million.
- Adoption of the annual report, administration report and interim reports.
- Raising of loans
- Signing of agreements with a term of more than five years.
- Launching of large-scale lawsuits and settlement of disputes of material significance.
- Other matters of material financial or other significance.

Furthermore, the Board has adopted instructions for the President, authorization instructions including instructions for liquidity management and a policy for foreign exchange management. The rules of procedure, President's instructions and authorization instructions are reviewed at least once a year.

Board attendance during 2016 ¹⁾

Members elected by the AGM	Elected in	Born in	Board meetings Attendance/total no. of Board meetings	Remuneration Committee Attendance/total no. of committee meetings
Board Chairman David Dangoor ²⁾	2003	1949	9/9	2/2
Board member Jan Annwall	1990	1950	9/9	
Board member Ewa Björling ²⁾	2015	1961	9/9	
Board member Stefan Elving ²⁾	2001	1941	7/9	2/2
Board member Inger Holmström ²⁾	2007	1948	8/9	
Board member Anthon Jahreskog ²⁾	2015	1980	9/9	
Board member Brit Stakston ²⁾	2014	1961	9/9	
Board member Paula Zeilon ²⁾	2003	1962	9/9	

¹⁾ All members of the Board who have been prevented from participating in a Board meeting have been given the opportunity to present their views to the Chairman prior to the meeting.

²⁾ Independent in relation to the major shareholders, the company and the company's management.

At the Board meetings, the following are dealt with as needed:

- Business plans
- Business performance monitoring
- Investments
- Strategic matters
- Financial reports
- Major agreements
- Budgetary matters
- Accounting 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 2016 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 Managing Director, 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.

Managing Director The Managing Director 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 Managing Director that among other things regulate his management and development of the company and the provision of reports and decision data to the Board. The Managing Director 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 Managing Director continuously informs the Board Chairman about the company's financial and business situation. Every year the Board carries out an evaluation of the Managing Director's performance in which no member of the Executive Management is present. In October 2015 BioGaia's Board of Directors decided to appoint Axel Sjöblad as the new Managing Director of BioGaia AB. Peter Rothschild was then appointed as Group President.

Executive Management BioGaia's Group Executive Management consists of the eight individuals who are presented on page 68-69.

The Group's Executive Management is headed by the Managing Director 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 Managing Director 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 one year. The 2016 AGM resolved on re-election of the registered auditing firm Deloitte AB to serve for the period until the end of the AGM to be held in 2017. The auditing firm appointed Birgitta Lööf 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 Managing Director and the quality of the company's financial reporting. At the request of the Board, the auditors also review the semi-annual 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.

Deloitte has provided certain tax-related advice and performed other audit-related services. Information about remuneration to the auditors can be found in Note 6 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 Managing Director or other members of the Executive Management.

The Board's report on internal control over financial reporting for the financial year 2016

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.

Internal control over 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 Managing Director. The rules of procedure state which matters require approval or authorisation from the Board. At Board meetings, the Managing Director reports on matters requiring treatment by the Board.

The Managing Director 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 Managing Director, BioGaia's control structure is based on the company's organisation and way of conducting operations, where roles and responsibilities are defined. The employees are continuously informed about the importance of good internal control of the 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.

The company's values BioGaia also has a set of shared values and the company's employees are well aware of these (see below). This is ensured through interviews in connection with new hires and through regular workshops with each department.

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 identifying significant risks for misstatements and deficiencies in the financial reporting and ensuring that there are suitable processes and controls in the company's operations to limit these risks. 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.

Monitoring The Executive Management performs a yearly evaluation of the effectiveness of internal control. Every year, the company's elected auditing firm, Deloitte 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, 27 February 2017

David Dangoor
Chairman

Axel Sjöblad
Managing Director

Jan Annwall
Member of the board

Ewa Björling
Member of the board

Stefan Elving
Member of the board

Inger Holmström
Member of the board

Anthon Jahreskog
Member of the board

Brit Stakston
Member of the board

Paula Zeilon
Member of the board

Auditors' report on the corporate governance statement

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

Engagement and responsibility

It is the board of directors who is responsible for the corporate governance statement for the financial year from 1 January 2016 to 31 December 2016 on pages 63-65 and that it has been prepared in accordance with the Annual Accounts Act.

The scope of the audit

Our examination has been conducted in accordance with FAR's auditing standard RevU 16 The auditor's examination of the corporate governance statement. This means that our examination of the corporate governance statement is different and substantially less in scope than an audit conducted in accordance with International Standards on Auditing and generally accepted auditing standards in Sweden. We believe that the examination has provided us with sufficient basis for our opinions.

Opinions

A corporate governance statement has been prepared. Disclosures in accordance with chapter 6 section 6 the second paragraph points 2-6 the Annual Accounts Act and chapter 7 section 31 the second paragraph the same law are consistent with the annual accounts and the consolidated accounts and are in accordance with the Annual Accounts Act.

Stockholm, 10 March 2017

Deloitte AB

Birgitta Lööf
Authorized 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 2016 BioGaia shares were traded for a total of around SEK 1.081 billion (1.335), corresponding to approximately 4.4 million shares (5.3).

The number of shareholders at 31 December 2016 was 7,740 (7,272).

The total registered share capital of BioGaia AB consists of 740,668 class A shares and 16,595,794 class B shares.

Share price development In 2016 the share price increased from SEK 281.50 to SEK 300.00. The highest closing price during the year was SEK 303.00 and the lowest was SEK 197.00. Market capitalization at 31 December 2016 was approximately SEK 5.200 billion (4.880).

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

Incentive scheme The company has no ongoing share-based incentive schemes. The warrant programme for the employees that was resolved on by the Annual General Meeting on 8 May 2012 expired on 1 June 2015. A total of 65,500 warrants were redeemed and the share capital now amounts to SEK 17,336,462. The subscription price for the share was SEK 241.90 and the company was thus provided with proceeds of SEK 15.8 million in 2015.

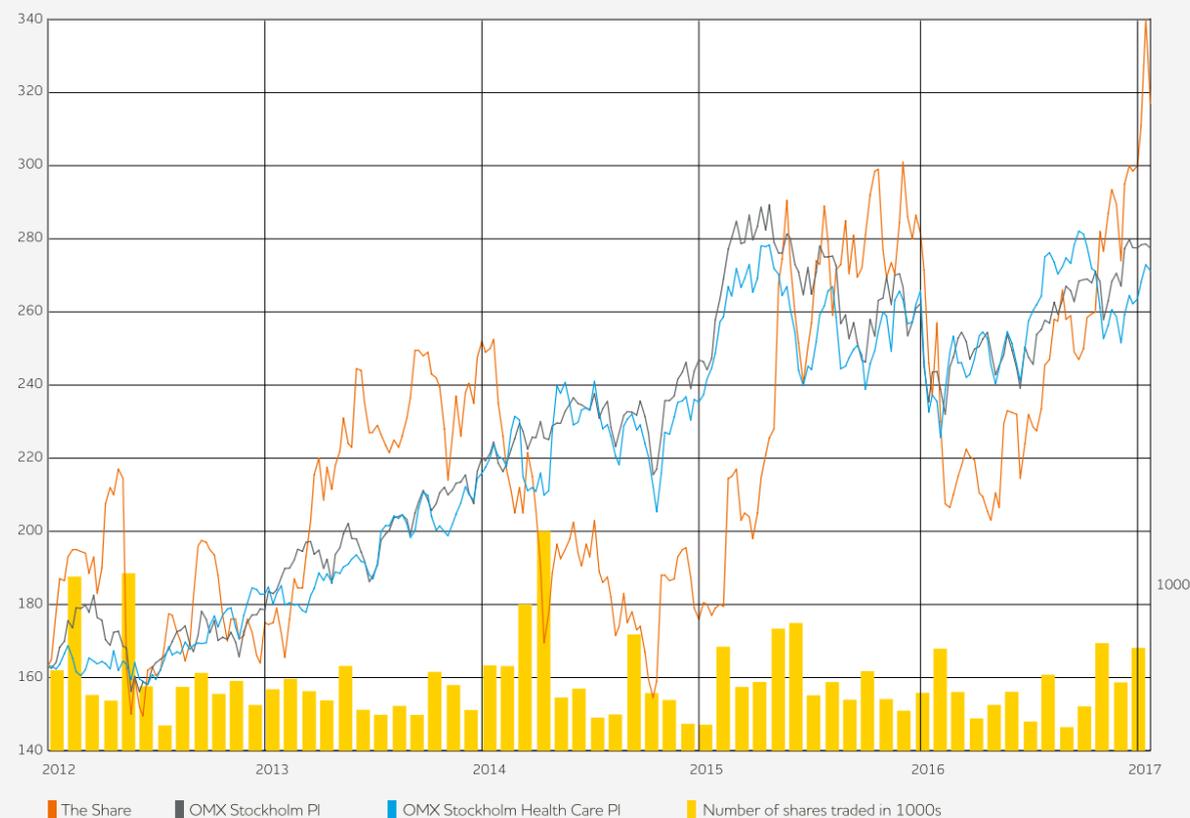
Distribution of ownership

Number of shares	Total number of shareholders	
	31 December 2016	31 December 2015
1–500	6,511	6,039
501–1,000	572	580
1,001–5,000	445	447
5,001–10,000	66	73
10,001–15,000	29	15
15,001–20,000	19	14
20,001–	98	104
Total number of shareholders:	7,740	7,272

LARGEST SHAREHOLDERS IN BIOGAIA AT 31 DECEMBER 2016 (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	8.6	34.0
Banque Ohman SA		1,454	1,454	1,454	8.4	6.1
Swedbank Robur fonder		1,033	1,033	1,033	6.0	4.3
Fjärde AP-fonden		1,018	1,018	1,018	5.9	4.2
David Dangoor (incl. company)		569	569	569	3.3	2.4
Mingdale Company		462	462	462	2.7	1.9
CBNY Norges Bank		451	451	451	2.6	1.9
Livförsäkringsaktiebolaget Skandia		438	438	438	2.5	1.8
SSB and Trust company, Boston		356	356	356	2.1	1.5
State Street Bank & Trust com, Boston		337	337	337	1.9	1.4
Caroline Hamilton		303	303	303	1.7	1.3
Nordea Investment Funds		279	279	279	1.6	1.2
Hanvad Invest Aktiebolag		263	263	263	1.5	1.1
JP Morgan Chase NA		245	245	245	1.4	1.0
AMF-Försäkring och fonder		244	244	244	1.4	1.0
Sten Irwe		224	224	224	1.3	0.9
Ruffer Inv		200	200	200	1.2	0.8
SSB Client Omnibus Account Abu, Dhabi		193	193	193	1.1	0.8
Skandia fonder		188	188	188	1.1	0.8
RBC Investor Services Bank		186	186	186	1.1	0.8
Nordnet Pensionsförsäkring AB		184	184	184	1.1	0.8
DnB Carlson fonder		182	182	182	1.0	0.8
SEB Investment Management		163	163	163	0.9	0.7
Tredje AP-fonden		142	142	142	0.8	0.6
Försäkringsaktiebolaget Avanza Pension		134	134	134	0.8	0.6
Other shareholders		6,589	6,589	6,589	38.0	27.5
Total	741	16,596	17,336	24,002	100.0	100.0

THE BIOGAIA SHARE



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
2015	New share issue warrant programme	65,500	65,500	17,336,462	740,668	16,595,794	1.00	15,844,450

* Excluding underwriting costs



Executive Management



AXEL SJÖBLAD Born 1967. MBA, EMBA, Stockholm School of Economics. Managing Director. Employed by the company since 2016. Board assignments in the subsidiary TwoPac AB and in Vigmed AB. Holds 0 shares.



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. Board assignments in the subsidiary TwoPac AB and in Infant Bacterial Therapeutics (IBT) AB. Holds 7,000 class B shares.

Group President



PETER ROTHSCHILD Born in 1950. M.B.A. Group President, founder and principal shareholder of BioGaia. Working Chairman of the subsidiaries TwoPac AB and CapAble AB as well as of the associated company MetaboGen AB. Also Chairman of the Board of Infant Bacterial Therapeutics AB (IBT) and with board assignments in Looft Industries AB and Stiftelsen Allbright. Holds 370,334 class A shares and 379,666 class B shares via Anwall & Rothschild Investment AB.

Board of Directors



DAVID DANGOOR Born in 1949. Board Chairman. Elected to the board 2003. MBA, Marketing and PR Consultant President of Innovative Partners LLC. Former Vice President and Marketing Director Philip Morris USA och Philip Morris International. Other board assignments: The Feinstein Institute for Medical Research, Manhasset, New York, New York City Ballet Inc., School of Creative Leadership, Berlin University and Swedish-American Chamber of commerce (Chairman 1997-2001) among others. Holds 518,918 class B shares directly and 50,000 class B shares via private company.



EWA BJÖRLING Born in 1961. Elected to the Board in 2015. Doctor of Dentistry, Doctor of Medicine and Associated Professor at the Karolinska Institute. Former member of the Swedish Riksdag and Minister for Trade in the Swedish Government from 2007 to 2014. Minister for Nordic Cooperation from 2010 to 2014. Other board assignments: SCA, Mobilis AB, KAK, Rehman & Partners Global Assessment advisory board. Holds 0 shares



URBAN STRINDLÖV Born in 1964. Mechanical Engineering. Executive Vice President and Sales Director. Employed by the company since 2004, in current position since 2010. Holds 0 shares.



NIGEL TITFORD Born in 1973. MSc Business Administration and Business Law. Vice President Business Development. Employed by the company since 1999. Holds 540 class B shares.



INGER HOLMSTRÖM Born in 1948. Elected to the Board in 2007. MA in Language and Linguistics and a degree in journalism. Senior Partner, Priority. Former Corporate Communications Director at Coop Norden, Posten and Vattenfall. Other board assignments: Järna akademi. Holds 500 class B shares.



ANTHON JAHRESKOG Born in 1980. Elected to the Board in 2015. MSc Financial Management. Former Chief Operating Officer Fund Linked Products at Credit Suisse Investment Bank, London. Holds 0 shares.



KRISTINA MAGNUSSON BORG Born in 1961. MSc Nutrition/Biochemistry, Ph. Lic. Clinical Physiology, MBA. Vice President Discovery and Research. Employed by the company since 2015. Holds 1,500 class B shares.



ULRIKA KÖHLER Born in 1966. BSc Biology with extended studies in microbiology. Vice President Marketing and Product Development. Employed by the company since 2013. Holds 0 shares.



PAULA ZEILON Born in 1962. Elected to the Board in 2003. MSc Engineering. Partner in Conlega affärs-konsultbolag. Former President of Life Science Foresight Institute and former Marketing Director at Amersham Biosciences AB. Other board assignments: Nanologica AB. Holds 1,000 class B shares.



STEFAN ELVING Born in 1941. Elected to the Board in 2001. Former Marketing Director and Executive Vice President of Icahandlarnas AB. Holds 0 shares.



HELEN OLSSON Born in 1965. Studies in Human Resources Management. Vice President Human Resources. Employed by the company on a consulting basis since 2013, in current position since 2015. Holds 0 shares.



KATAYOUN WELIN-BERGER Born in 1968. PhD Pharmacology. Vice President Operations. Employed by the company since 2014. Holds 600 class B shares.



JAN ANWALL 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. Other board assignments in Infant Bacterial Therapeutics (IBT) AB. Holds 370,334 class A shares and 379,666 class B shares via Anwall & Rothschild Investment AB.



BRIT STAKSTON Born in 1961. Elected to the Board in 2014. Media Strategist and Communication Consultant. Owner of Stakston AB and founder of the reportage site Blankspot. Member of Presstödsnämnden. Holds 0 shares.





Definitions and Glossary

DEFINITIONS

The company presents certain financial ratios in the interim report that are not defined according to IFRS. The company is of the opinion that these performance measures provide valuable supplementary information to investors and the company's management since they enable evaluation and benchmarking of the company's performance. Since not all companies calculate financial ratios in the same manner, these are not always comparable to the performance measures used by other companies. Consequently, these financial ratios should not be seen as a replacement for performance measures that are defined according to IFRS. The following key ratios are not defined according to IFRS unless otherwise stated.

Average number of shares weighted average number of shares during a certain period.

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.

Earnings per share in continuing operations Profit from continuing operations attributable to owners of the Parent Company divided by the average number of shares.

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.

Net financial items The result from financial income and financial expenses.

Operating margin Operating profit in relation to net sales.

Operating profit Sales less cost of goods sold, selling expenses, administrative expenses, R & D expenses and other operating expenses plus other operating income.

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.

RECONCILIATION AGAINST IFRS

Return on capital employed	2016	2015
Operating profit	199,437	172,799
Financial income	1,429	5,437
Profit before financial items + financial income	200,866	178,236
Total assets	488,978	473,178
Interest-free liabilities	-73,466	-76,994
Capital employed	415,512	396,184
Average capital employed	405,848	370,492
Return on capital employed	49%	48%

	Pediatrics		Adult Health		Other		Total	
	2016	%	2016	%	2016	%	2016	%
Change in sales by segment								
Organic growth	39064	10%	7506	10%	-2619	-14%	43951	9%
Foreign exchange effects	4403	1%	3101	4%	-		7504	2%
Reported change	43467	11%	10607	14%	-2619	-14%	51455	11%

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 great deal of lactic acid bacteria, but today our diet lacks these beneficial bacteria. Some lactic acid bacteria are also present in the human commensal flora.

Lactic acid bacteria have different properties and may thus provide different health effects when consumed. 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 consist of 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.

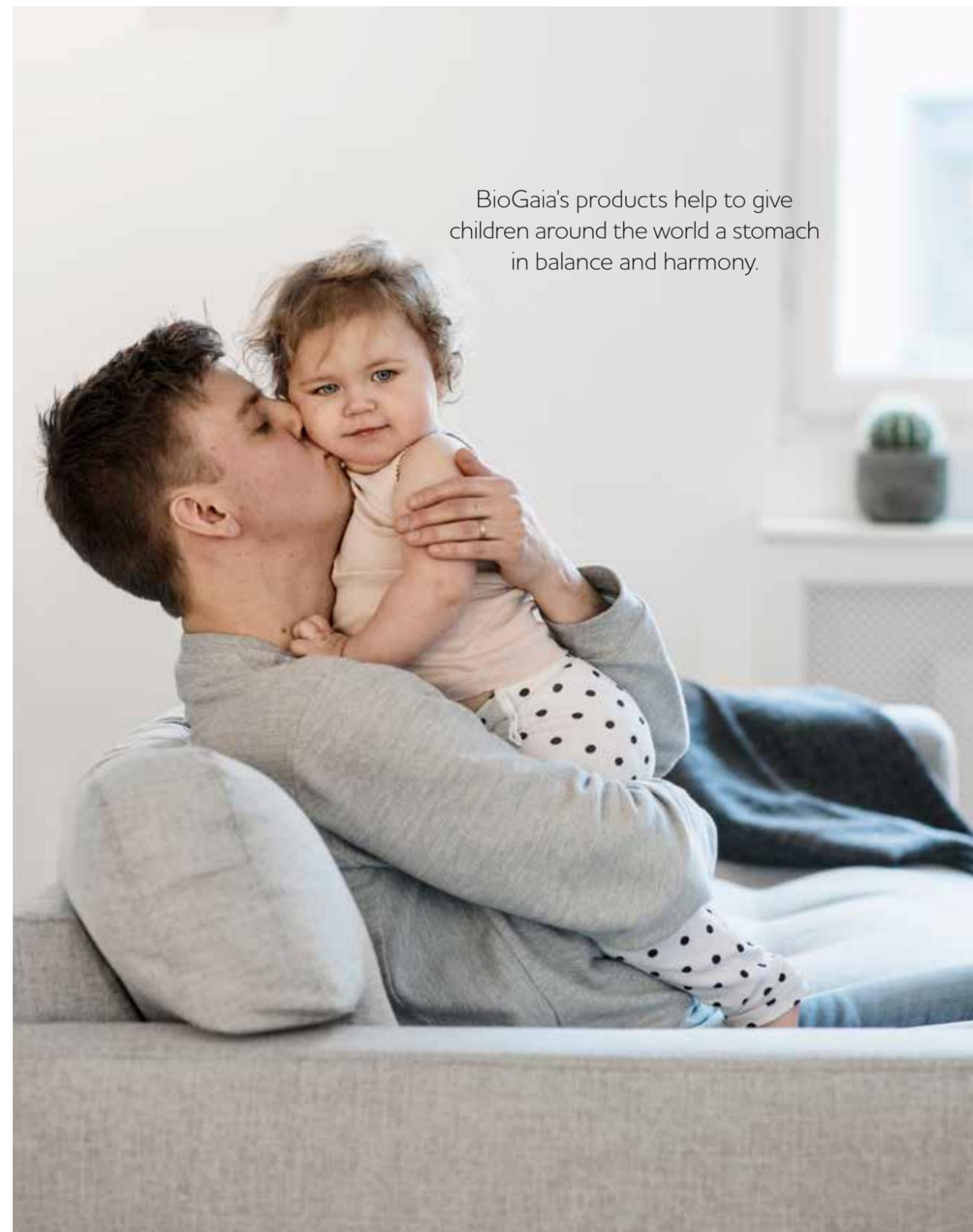
Lactobacillus reuteri Prodentis Combination of two strains of *Lactobacillus reuteri*, used in BioGaia's oral health products.

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.



BioGaia's products help to give children around the world a stomach in balance and harmony.

Project Management: Eva Nelson, Communications Manager, BioGaia, Chatarina Andersson, Marketing Assistant, BioGaia (financial section) Anna Jonason, AD/Communication Strategist, Krut. Photographs: Helén Karlsson, Johnér bildbyrå, Getty Images, Shutterstock. Printing: Ineko 2016



Experts at bacteria

BioGaia is an innovative Swedish healthcare company and has been a world-leader in dietary supplements with probiotics for more than 25 years. The products are based mainly on different strains of *Lactobacillus reuteri* and are sold by local distribution partners in around 90 countries.

BioGaia®