ANNUAL REPORT

KARO BIO

2013

CONTENTS

This annual report contains statements that are forward looking and actual future results may differ substantially from those anticipated. In addition to the factors discussed, the actual results can be influenced by developments within research programs, the impact of competing research programs, the effects of economic and cyclical conditions, the effectiveness of patent protection and obstacles due to third party patent rights, technological development, exchange rate and interest rate fluctuations, as well as regulatory and political risks.

ANNUAL GENERAL MEETING AND OTHER INFORMATION

ANNUAL GENERAL MEETING

The Annual General Meeting of Karo Bio (publ) will be held on Thursday May 8, 2014 at 4:00 p.m. in in the Lecture Hall, Novum Science Park (4th floor – elevator E), Hälsovägen 7, Huddinge, Sweden. The notice to attend the Annual General Meeting is available through Kari Bio's website at www.karobio.com/general-meeting.

RIGHT TO ATTEND

Entitled to attend the Annual General Meeting are those who are both registered shareholders in the share register held by Euroclear Sweden AB at the record date Friday May 2, 2014 and have notified the company of their intention to attend the general meeting no later than on May 2, 2014 at 4:00 p.m.

Notification to attend the meeting shall be submitted in writing including name, personal identification number or corporate identity number and phone number, to the address Karo Bio AB, att: Susanne Thylin Westlund, Novum, S-141 57 Huddinge, Sweden, by fax to +46 (0) 8 774 82 61, via e-mail to susanne.thylin-westlund@karobio.se.

Shareholders whose shares are registered through a bank or other trustee must, in order to be entitled to participate in the meeting, temporarily register their shares in their own name. Such registration must be completed no later than Friday May 2, 2014, which means that shareholders must notify their trustee well in advance of this date.

OTHER INFORMATION

Upcoming financial reports

Interim report January–March	May 8, 2014
Interim report January–June	July 11, 2014
Interim report January–September	October 29, 2014
2014 Year-end report	February 13, 2015

Other

Extra general meeting	March 17, 2014

Financial reports, press releases, notification to the extra general meeting and other information are available on Karo Bio's website www.karobio.com from time of publication. Karo Bio's financial reports and press releases can be subscribed to and downloaded from the website. Karo Bio employs electronic distribution as the main distribution channel for financial reports. The annual report is mailed to shareholders and other stakeholders who have specifically requested this. Printouts of interim reports are mailed upon request.

For further information, please contact Per Bengtsson, President and CEO, phone +46 (0)8-608 60 20, or Henrik Palm, CFO, phone +46 (0)8-608 60 76, or e-mail: investor@karobio.com.

2013 IN BRIEF

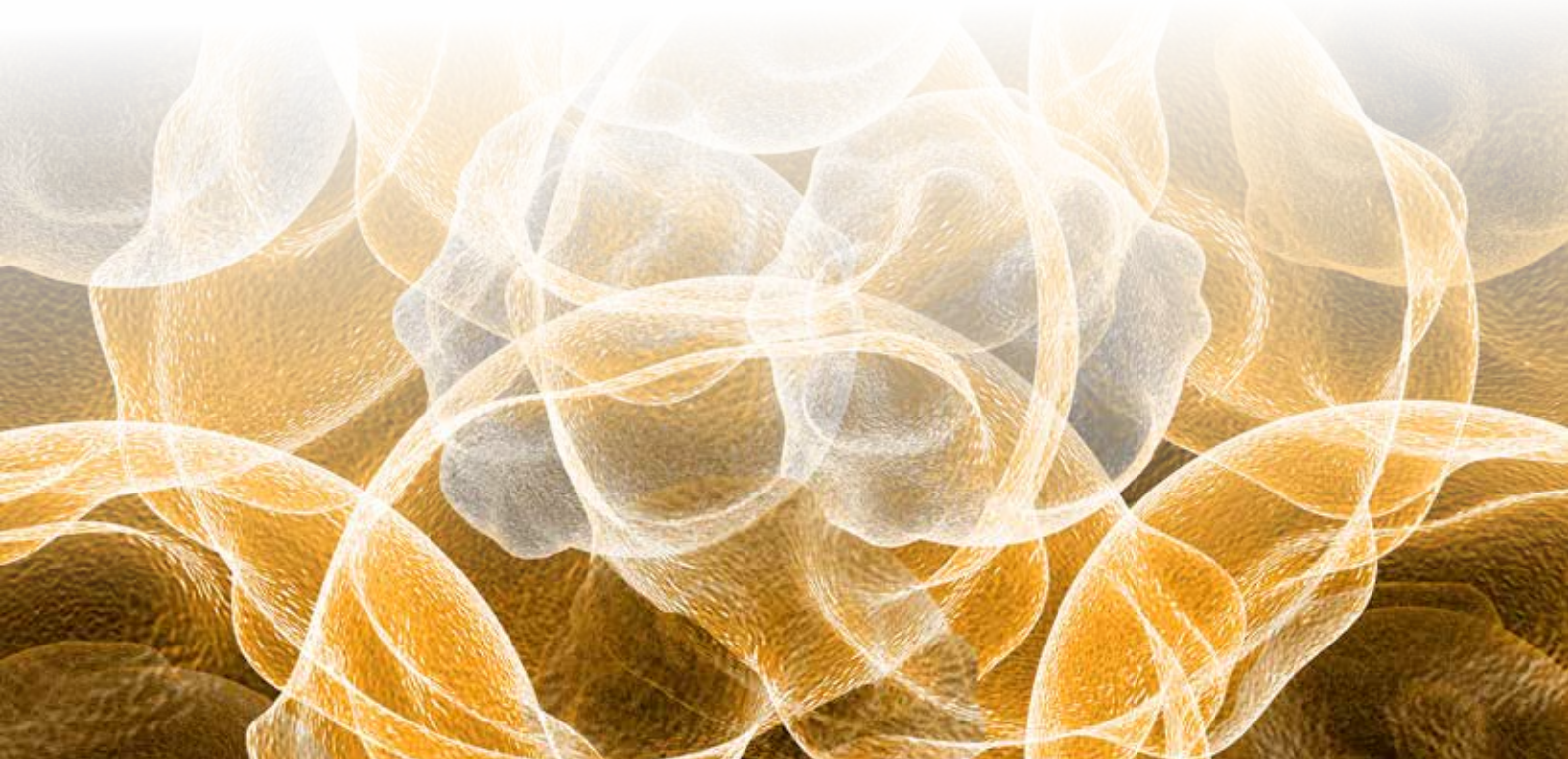
- Pfizer extended the RORgamma research collaboration to 2015
- Karo Bio obtained a milestone payment of USD 2 million in the RORgamma project
- Research collaboration on fibrosis entered into with Dr Jörg Distler and 4D Science GmbH
- Karo Bio was awarded a conditional loan of USD 0.5 million by the US National MS Society
- Net sales increased to 47.0 (33.2) MSEK
- Group net loss improved to -22.1 (-98.3) MSEK

FINANCIAL DATA

MSEK	2013	2012	2011	2010	2009
Net sales	47.0	33.2	–	–	5.9
Operating expenses	–69.3	–132.9	–231.2	–161.8	–163.0
- of which R&D expenses	–52.5	–107.9	–189.3	–129.4	–132.4
Net loss	–22.1	–98.3	–226.6	–163.5	–154.6
Loss per share (SEK)	–0.04	–0.25	–0.58	–0.67	–0.78
Cash flow from operating activities	–33.4	–127.8	–198.3	–158.9	–146.9
Cash, cash equivalents and other short term investments	22.8	54.1	158.5	395.0	237.2

ABOUT KARO BIO

Karo Bio is a research and development company focused on development of innovative drugs for key medical needs. The company's unique knowledge of nuclear receptors as target proteins for pharmaceuticals and the related of mechanisms of action, are utilized to develop novel, more effective and safer pharmaceuticals. Karo Bio is active in preclinical development focused primarily in the fields of neuropsychiatry, inflammation, autoimmune diseases and cancer. The company has a number of strategic agreements and collaborations with international pharmaceutical companies. Karo Bio is based in Huddinge, Sweden, has around 39 employees and is listed on the NASDAQ OMX Stockholm exchange (Reuters: KARO.ST).



VISION, GOAL, BUSINESS MODEL AND STRATEGY

VISION

Karo Bio's vision is to become a pharmaceutical company with sustainable profitability, commercial products and a competitive portfolio that combines partnered projects with proprietary development projects.

FINANCIAL GOAL

- Karo Bio is to achieve a positive cash flow.

The Board believes that Karo Bio has the potential to reach a positive cash flow in the long-term. For this to happen, the company must secure additional revenue, and at the same time continue to work on the cost side of the operations.

BUSINESS MODEL

From knowledge to value for patients and owners

Karo Bio develops pharmaceuticals for markets with large medical needs. Within niche areas, Karo Bio is qualified to process selected compounds throughout the entire development process, but intends to outlicense its projects to an industrial partner at the latest after clinical phase II.

When a compound is out-licensed or a collaboration is entered into, Karo Bio usually obtains an upfront payment followed by research funding for the joint discovery phase, milestone payments when certain predetermined goals are reached and finally royalty payments on sales. When an agreement has been reached, the partnering company is usually responsible for the project's development costs.

In strategic alliances or in development collaborations, the parties cooperate around a specific area and thus share the expenses of the development work and the immaterial rights generated. This kind of collaboration is most common in early phases. Karo Bio is also seeking other types of agreements for early phases, for example for conducting so-called feasibility studies in which the conditions for creating a drug within a specific area are investigated.

Karo Bio is also looking for public and private grants and other soft financing to fund some of its activities. The possibilities for companies to obtain such funding have increased in recent years but vary over time and across different therapy areas. Funders typically grant financing with certain conditions, such as repayment if and when the project generates revenue. In 2013, Karo Bio was awarded 0.5 million dollars from the U.S. National Multiple Sclerosis Society to continue the development of a new treatment of progressive MS. Karo Bio believes that there are good opportunities to obtain grants to fund some of its operations.

STRATEGY

Focus that creates unique opportunities

- World leader in nuclear receptors
- We can provide the most benefit until early clinical phase
- Build knowledge in specific therapeutic areas

Risk management

- Select lower risk projects
- Several early projects increases the possibilities
- Risks are gladly shared with others

Commercial approach

- Different types of contracts and financing, and preferably during early phases
- Lean organization with maintained edge
- Active business intelligence to enhance opportunities

ON THE RIGHT TRACK

For a long time, Karo Bio has focused on high quality in science and research, which has paved the way for our strong brand in the industry. Upon taking over as President in 2011, one of my main goals was to also increase the organization's business awareness. Through a concerted effort, we have now developed a commercial mindset that permeates the entire organization. This means that we have a clear and common picture of what work needs to be done and what priorities are needed if we are to develop the business and achieve commercial success.

The past year has shown that Karo Bio is on the right track. Sales increased by almost 50 per cent to 47 million kronor while costs continued to decrease step by step and amounted to 69 million kronor, nearly half of those in the previous year.

COLLABORATING WITH PARTNERS

In the long term, our overall aim is naturally to achieve a profit, which requires larger revenue. The collaboration with Pfizer on RORgamma generated the majority of our revenue in the form of research funding and a milestone payment. This summer, the research agreement was extended one year further, and the next milestone is within reach during 2014. We are very pleased with how the project is advancing and it is important to me to point out that Karo Bio has had a key role in the success of the project.

We aim to close further license agreements. I have shared that in 2012 already, we were close to reaching an agreement for our ERbeta project in MS, but a change in strategy at our prospective partner thwarted those plans. We decided to take the project a step further and the data we have produced so far confirms the view that the project has good potential to become a novel drug. We are in a strategic position since our project targets progressive MS, an area that garner increasing interest among the leading MS companies. In the fall, this positive view was confirmed when we, after careful examination, was awarded 0.5 million dollar by the U.S. National MS Society for the continued development of our lead drug compound. We have now initiated discussions with a number of companies that are active in the MS field. It is, as always, hard to predict when and how these may be concluded.

ALTERNATIVE SOURCES OF FUNDING

As you all know, we conduct active and successful efforts to find alternative sources of funding. This means above all that we are seeking soft money in the form of public and private funding such as for ERbeta MS. The opportunities for such funding has improved in recent years for players outside the academic world, as more and more funders want to ensure that new technology will also reach patients.

Opportunities for soft money vary between different therapeutic areas and some funding bodies also vary their focus over time. We can therefore expect the element of soft financing to develop unevenly over time. One advantage with soft money is that projects are put under competitive review

at a very early stage, which helps Karo Bio to maintain high commercial quality in the project portfolio.

Soft money is also an option for advancing our third active project, ERbeta cancer, to the next level. There is a relative abundance of this form of financing in the field of cancer, but competition for it is also great. During the year, we had significant success in the project, in the form of experimental data on human tumor tissue studied in animal models. The effects we have seen are powerful and it appears possible to extend the use of a compound to several different tumor diseases.

NAVIGATING THE OUTSIDE WORLD

We have deliberately tried to create a greater understanding of what is happening in the world around us. We are following developments closely in the receptor field through dialogues with research groups around the globe and by studying what other pharmaceutical companies are doing as closely as possible considering business confidentiality. Thereby, we have gained a larger ”catchment” for project ideas that we benchmark against each other and against our own projects in a systematic evaluation process.

This resulted in that we in the fall of 2013 started a research collaboration on fibrosis with Dr. Jörg Distler at 4D Science. The German doctor's research team has discovered that a specific nuclear receptor plays a key role in the pathogenesis of fibrosis. Their findings could pave the way for novel and effective ways to treat patients with these serious and difficult to treat diseases. In the first phase, the collaboration aims to validate the nuclear receptor as a target in fibrosis. If the outcome is positive, we will jointly decide on the next step.

MOVING TOWARDS THE CLINIC

The systematic approach we apply in Karo Bio today provides us with a well thought out consensus on our projects and priorities. Many persons contribute to make our common view as clear as possible and to properly reflect risks and opportunities. This paves the way for decisions that will bring us to scientific, medical and commercial success.

Our new approach gradually increases the value of our portfolio. Currently, we have three strong project areas, all approaching clinical phase at good speed. This provides good scope and risk diversification to our portfolio. In order to advance towards a very powerful commercial position within 18 months, with the ability to have three projects in clinical development, we have decided to turn to the stock market to strengthen our financing.

WELL EQUIPPED FOR THE FUTURE

Karo Bio is in a position where the business is well placed to continue to create value for its shareholders, and also to clearly display it soon. In an environment where large companies are increasingly inclined to turn to innovative small research companies, time is benefitting Karo Bio.

Stockholm in March 2014

CEO Per Bengtsson

OUR ENVIRONMENT

BIG PHARMA EYING COLLABORATIONS

There are rich opportunities for the pharmaceutical industry to market new, effective treatments. However, the industry has struggled in recent years to maintain the pace in launching new products. Many projects have run into problems, often in late stage development. Novel ideas have often emanated from smaller companies. This has caused considerable change within major pharmaceutical companies. Internal research departments have been downsized, in favor of collaborations with smaller companies and academic research groups. Pharmaceutical companies thus achieve flexibility, while they can obtain the specialist skills they desire. The risks for suboptimal choices in their own organization are lowered.

The trend towards collaboration set off several years ago, and this is now reflected by the new drugs that have reached the market. Of the 14 marketing approvals of new products awarded major pharmaceutical companies in the US during 2013, 11 have originated with smaller companies.

The trend towards increasing external research continued in 2013. Burrill & Company estimates the combined potential licensing deal value announced in the industry in 2013 at USD 35.4 billion, a three percent increase over the previous year. As much as 40 percent of these were signed for projects in preclinical phase, where contracts now increasingly are designed with milestones clearly tided to commercial success.

FEWER DRUG APPROVALS IN 2013

In 2013, the USA Food and Drug Administration approved 27 novel pharmaceuticals (NME's), a substantially lower figure than the 39 approvals the previous year, although in line with the five-year average of 28. Just over half of the new products were registered by major pharmaceutical companies, according to Forbes magazine. Ten of these drugs have new mechanisms of action, while six are biological. One third are classified as orphan drugs. Cancer continues to be the most active area, with eight new product approvals, followed by five new anti-infective drugs, four of which are antiviral. Widely acknowledged as one of the most significant approvals, is the Hepatitis C drug Sovaldi by Gilead Sciences, which promises dramatic improvement for the millions of people infected by this virus.

An apparent trend over the past five years is that large pharmaceutical companies' share of drug approvals is declining, with an estimated annual average of 11. And many of these products have their origins with smaller companies. Only eight of the 27 approved new drugs in 2013 were registered by the inventing company. For major pharmaceutical companies, the corresponding figure was three out of 14.

THE LONG ROAD TO PHARMACEUTICAL PRODUCT APPROVAL

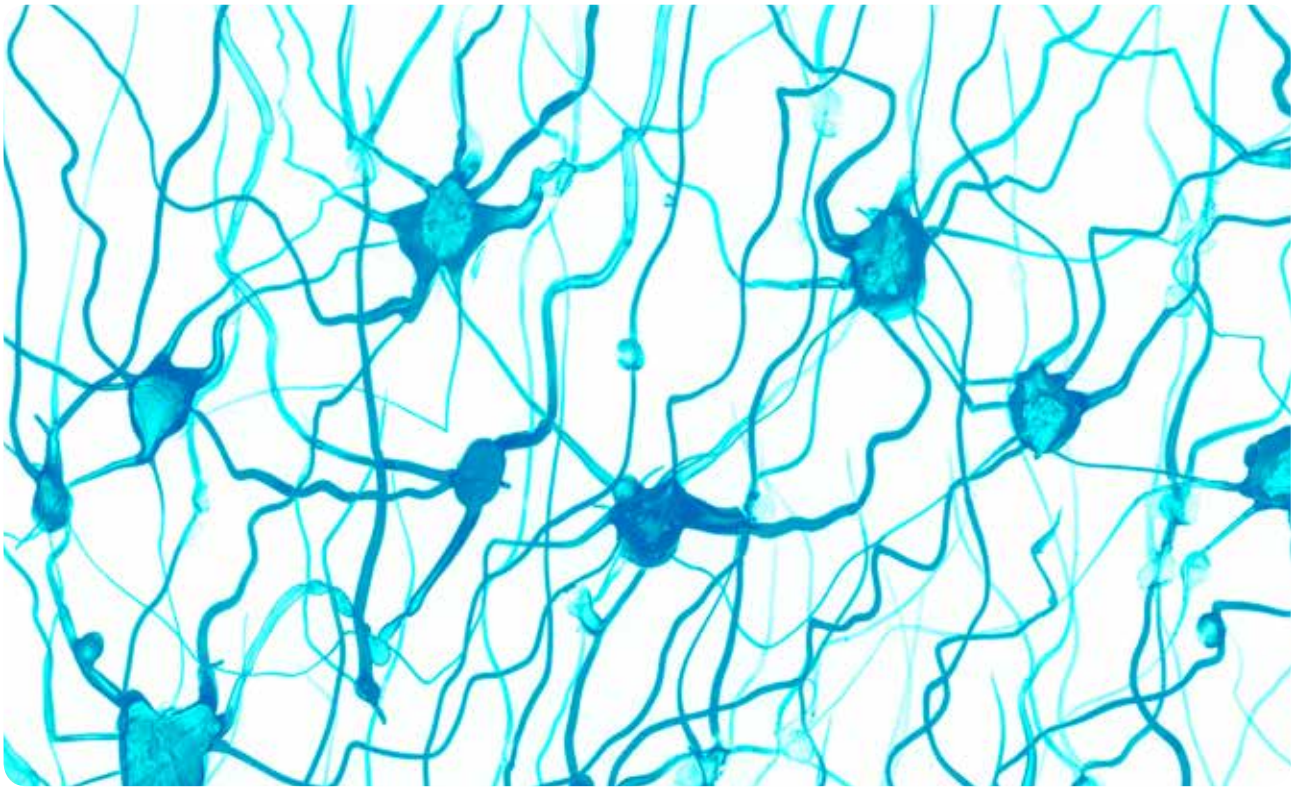
Target protein
Initially, the target protein must be identified and validated, which means that the target protein is confirmed to have a key role in the specific disease to be addressed by treatment.

Active leads
In the next phase, molecules which influence the target protein are identified.

Model compounds
Next, classes of molecules that could be developed into drugs are identified.

Optimization phase
Molecules' characteristics are optimized to become safe and effective.

Candidate drug
One compound is selected for further development.



The picture shows a healthy network of nerve fibers between neurons. The larger protrusions are called axons and the smaller dendrites. In MS and many other diseases of the brain, the function of this network is impaired.

Preclinical development
The chosen candidate drug is tested to ensure that it is safe for entry into human trials.

Phase I
The first clinical study is performed on healthy persons, to document the drug's safety, followed by patient studies to define safe and effective dosage.

Phase II
The candidate drug is administered to patients to establish safe and effective dosage.

Phase III
The candidate drug is tried on a larger patient group to ensure safety and to ascertain effectiveness during extended treatment.

Registration and product launch

PROJECT PORTFOLIO

ERBETA SELECTIVE COMPOUNDS – A PLATFORM WITH MANY OPPORTUNITIES

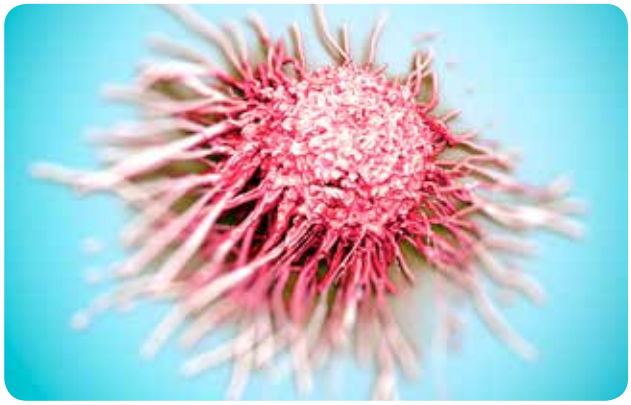
The estrogen receptor (ER) is activated by estrogen and regulates a number of functions in the body. Estrogen has several positive effects but its medical use has been limited by the associated increased risk for uterine and breast cancer as well as thrombosis. These risks are mainly linked to the estrogen receptor's ERalpha subtype, while ERbeta, which Karo Bio was involved in discovering in the 1990's, seems to account for many of the positive effects of estrogen without the side effects. Understanding of the ERbeta receptor's role has increased with intense research in the field. Today, the image is clearer that there are several clinical development opportunities for compounds that act through the ERbeta receptor.

Karo Bio's efforts in the field have resulted in a world-leading position and a platform with many promising ERbeta selective compounds. These have slightly different properties and may thus be suitable for different indications.

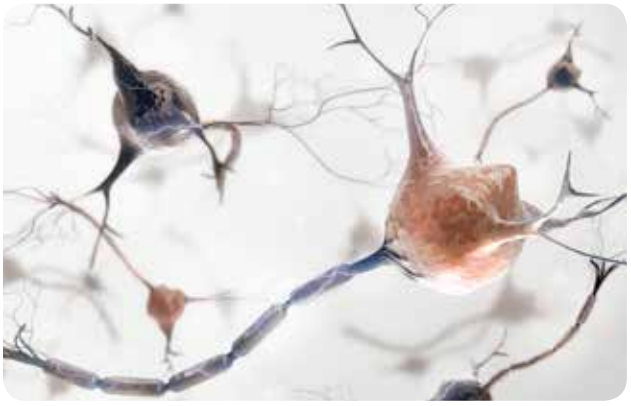
A collaboration with Merck (known as MSD outside the US and Canada) regarding an ER compound was discontinued in 2010 when in Phase II. As there have not been any safety related issues reported around the compound, Karo Bio is exploring the possibility to regain the rights to the compound for use in other areas.

ERbeta cancer

Karo Bio has collated preclinical data that suggest that ERbeta has a very interesting potential in the field of cancer. The first drug candidate within the program, KB9520, has shown good efficacy in preclinical models for several different forms of cancer. These effects can be assumed to have a general effect in several different forms of cancer tumors, provided they express ERbeta. Karo Bio is seeking funding to continue the development of ERbeta in the field of cancer.



The image shows a cancer cell. Karo Bio examines the effect of ERbeta on cancer tumors.



The image shows neurons with protrusions, called axons and dendrites. Axons are the longer protrusions that are protected by sheaths, called myelin. Nerve signals jump between the sheaths. In MS, myelin is damaged which cause nerve signals to weaken.

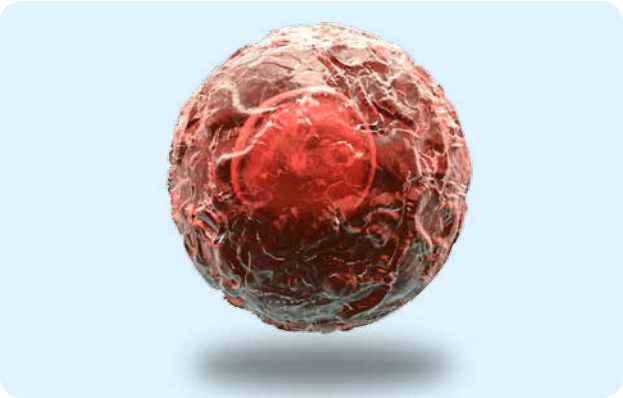
ERbeta MS

Since 2011, Karo Bio has a development project for ERbeta focused on the autoimmune disease multiple sclerosis (MS). In preclinical models, ERbeta agonists have demonstrated protective and reparative effects on the myelin sheaths that surround nerve cells, which are very promising since damaged myelin is involved in the symptoms and disability in MS. If treatment with ERbeta agonists proves capable of repairing damaged myelin also in patients this will represent a significant breakthrough in the treatment of patients with progressive MS, since current therapies only aim at reducing inflammation at early stages of the disease.

To further investigate ERbeta agonists' therapeutic effect, Karo Bio performed additional studies in disease models in animals in the beginning of 2013. The new results indicate that ERbeta has positive effects by protecting and repairing nerve tissue. Karo Bio continues the preclinical development of the project and in September 2013 the U.S. National MS Society awarded the project MUSD 0.5 in funding with conditional repayment.

RORGAMMA – A NEW OPPORTUNITY TO TREAT AUTOIMMUNE DISEASES

Recent research reveals that the nuclear receptor RORgamma may play a critical role in the development of autoimmune disease, such as rheumatoid arthritis and psoriasis. In 2010, Karo Bio initiated a research program to develop and evaluate compounds that inhibit RORgamma activity, which



The image shows a Th17 cell, a T helper cell that produces interleukin 17 (IL-17), and which is overly active in autoimmune disease. By dampening this activity through RORgamma, Karo Bio hopes to develop novel drugs for autoimmune diseases.

may prove to be a novel concept for a potential new treatment alternative for autoimmune diseases. RORgamma has been shown to control the maturation of, and activity in, a certain type of immune cell, believed to drive inflammatory and debilitating processes in such diseases.

In December 2011, Karo Bio entered into a research collaboration with Pfizer for RORgamma to discover and develop new compounds for the treatment of autoimmune diseases. Pfizer has exclusive rights to products developed as a result of the collaboration, while Karo Bio has the right to royalties on sales.

Initially, Pfizer assumed responsibility to fully fund research for two years. In June 2013, Pfizer decided to extend the research funding agreement one year further until 2015. In September 2013, Karo Bio achieved a project milestone, triggering a compensation of MUSD 2. In 2013, Karo Bio recognized revenue from the project of in total MUSD 7, equivalent to MSEK 44. The project is advancing.

RESEARCH

Karo Bio also conducts research at earlier stages around certain receptors to determine whether drugs can be designed that qualify for individual projects. Ideas are gathered from academic research and other pharmaceutical research, usually around certain signaling pathways. By testing if these pathways can be influenced via nuclear receptors or in a similar manner, Karo Bio can use its expertise to create value. This is very early research where some ideas can be dismissed relatively quickly; while others can be evaluated over a longer or shorter period of time to when successful qualify as a development project. Work is underway on a small number of nuclear receptors.

In 2013, Karo Bio entered into collaboration with Dr. Jörg Distler and his company 4D Science GmbH surrounding fibrosis. Dr. Distler's research team has discovered that a specific nuclear receptor plays a key role in the pathogenesis of fibrotic diseases, which may have implications for the treatment of patients with this type of intractable diseases. The partnership initially focused on generating additional data to validate the nuclear receptor as a target in fibrosis and to demonstrate that it is possible to address it with a drug.

NUCLEAR RECEPTORS – REGULATE KEY FUNCTIONS

The human body's 48 nuclear receptors regulate many important functions and effect common diseases such as inflammation, diabetes, dyslipidemia and osteoporosis, and certain forms of cancer. Some of these receptors have been well documented while others are relatively unexplored. Today, around one in ten drugs act via nuclear receptors. Karo Bio, whose research and development work focuses on nuclear receptors, is one of the pioneers in the field.

Nuclear receptors are naturally activated through the hormonal system. Hormones are produced in an organ and are transported via the blood to one or more target organs where they exert their effect. In the target organ the hormone binds to a protein called a receptor. There are receptors on both the surface of the cell as well as inside the cell. Receptors inside the cell are known as nuclear receptors.

Nuclear receptors control which genes that the cells express at a certain time which in turn determines which proteins a cell contains. One ligand-receptor complex can have different effects on different tissues. The hormone cortisol, which is secreted by the adrenal glands, can for example regulate the gene expression in the inflamed tissue, so that anti-inflammatory proteins are stimulated and inflammation-inducing proteins are inhibited. Cortisol affects the liver by increasing glucose production and thereby elevated blood sugar levels. Some nuclear receptors are activated or inhibited by hormones, while others are controlled by vitamins, fatty acids or bile acids. For some receptors, the natural neurotransmitter, called the ligand is unknown. The natural ligands bind to certain pockets in the nuclear receptors.

By designing drugs that only have anti-inflammatory effect and simultaneously do not lead to side effects such as elevated blood sugar levels, various diseases can be treated.

THE SHARE AND OWNERS

LISTING
Karo Bio's share is listed on NASDAQ OMX Stockholm since 1998.

SHARE DEVELOPMENT AND TRADING
In 2013, the Karo Bio share more than doubled in value, from 0.36 SEK to 0.73 SEK. During the same period OMX Stockholm Pharmaceuticals & Biotechnology increased by 34 per cent. In total, turnover amounted to 1,703 million shares, implying that total share capital traded 3.9 times.

SHAREHOLDERS
The number of shareholders was 11,145 at the beginning of the year and 11,799 at the end of 2013. A list of the larger shareholders can be found on the opposite page. At year-end, the ten largest shareholder held 29 (33) per cent of total number of shares. Foreign owners held 14 (25) per cent of the share capital. Shareholders with 1,000 shares or less accounted for 0.2 (0.4) per cent of shares.

RIGHTS ISSUE
In the beginning of 2013, Karo Bio completed a rights issue in which a total of 108,883,397 new shares were issued and net proceeds amounted to 32.6 MSEK.

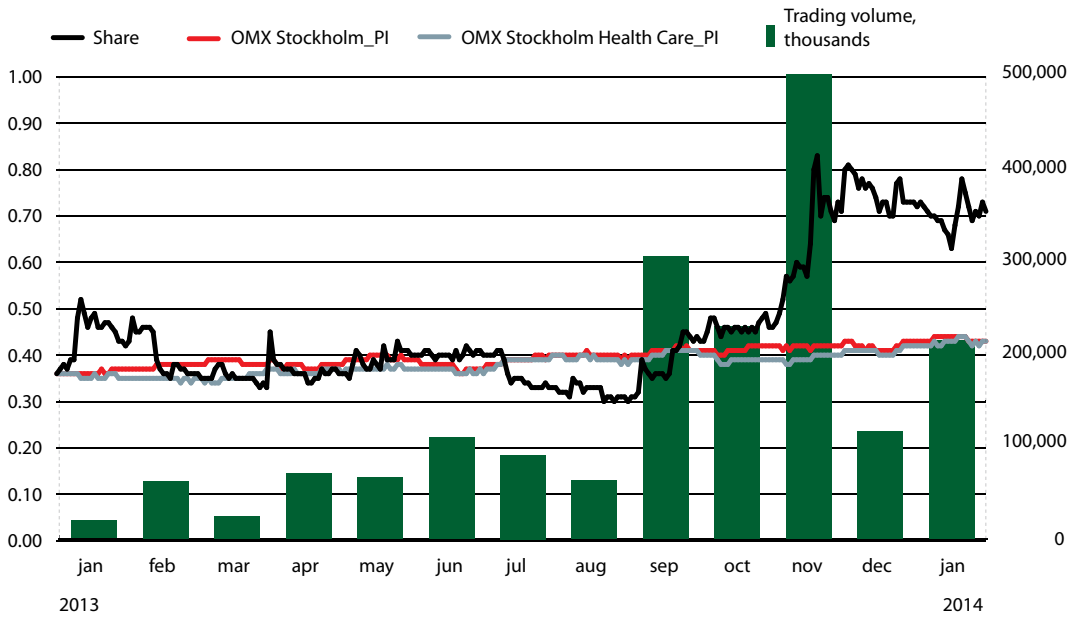
In conjunction with the year-end report 2013, the Board proposed a rights issue to existing shareholders with net proceed of approx. 70 MSEK. The Board also suggested a share issue to Mr. Anders Lönner of approx. 7 MSEK.

SHARES AND SHARE CAPITAL
At December 31, 2013, Karo Bio's share capital amounted to 9,918,838, an increase with 2,177,559 from the previous year. The number of shares increased during 2013 to 495,947,369 from 387,063,972. The share has a par value of SEK 0.02. The average number of shares in 2013 was 494,178,448.

DIVIDEND POLICY
The Board does not intend to propose any dividends until the company generates healthy profits and cash flows. Karo Bio has not paid dividends since it was founded in 1987.

COMMUNICATION WITH FINANCIAL MARKETS
Karo Bio strives for an open dialogue with current and potential shareholders and to provide the outside world a good insight into and understanding of the business. In each interim report, we describe the current status of all pipeline projects and operations in general. In 2013, Karo Bio also arranged open conference calls in connection with all interim reports. Recorded versions of those calls are available on the website. Karo Bio also participated in several different types of meetings in financial markets. During the year, the CEO started a blog on the website where he comments events inside and outside the company. At a ceremony in March 2013, Karo Bio was awarded Financial Hearings presentation award 2012 in the category of Micro Cap.

SHARE PRICE DEVELOPMENT



PRINCIPAL SHAREHOLDERS AT JANUARY 31, 2014

Owner	Number of shares	Holding in % of capital and votes
Försäkringsaktiebolaget Avanza Pension	46,001,602	9.3
JP Morgan Bank	22,067,911	4.4
Nomic AB	19,333,333	3.9
Nordnet Pensionsförsäkring AB	14,044,634	2.8
Robur Försäkring	10,289,452	2.1
JPMP I Visby AB	6,297,844	1.3
Goldman Sachs International Ltd, W8IMY	5,904,401	1.2
Lönn, Mikael	5,275,000	1.1
LGT Bank LTD	5,024,831	1.0
Grolander, Daniel	4,400,000	0.9
Total 10 largest shareholders	**138,639,008**	**28.0**
Total other shareholders	357,308,361	72.0
Total per January 31, 2014	**495,947,369**	**100.0**

OWNERSHIP STRUCTURE AT JANUARY 31, 2014

Holding, number of shares	Number of shareholders	Holding as a % of share-holders	Number of shares	Holding as a % of share capital
1 – 500	1,956	16.3	396,393	0.1
501 – 1,000	1,077	9.0	891,567	0.2
1,001 – 2,000	1,290	10.7	2,052,028	0.4
2,001 – 5,000	2,089	17.4	7,498,858	1.5
5,001 – 10,000	1,637	13.6	13,129,591	2.6
10,001 – 20,000	1,385	11.5	21,380,611	4.3
20,001 – 50,000	1,295	10.8	43,475,037	8.8
50,001 – 100,000	640	5.3	49,861,094	10.1
100,001 – 500,000	548	4.6	113,291,374	22.8
500,001 – 1,000,000	57	0.5	40,110,882	8.1
1,000,001 – 5,000,000	38	0.3	69,620,926	14.0
5,000,001 –	9	0.1	134,239,008	27.1
Total 2014-01-31	**12,021**	**100.0**	**495,947,369**	**100.0**

SHARE CAPITAL DEVELOPMENT

Year	Transaction	Increase in no. of shares	Accumulated no. of shares	Total share capital (SEK)	Issue amount (SEK)[1]
	Capital structure January 1, 1998	-	3,943,586	39,435,860	-
1998	Stock split 2:1	3,943,586	7,887,172	39,435,860	-
1998	New issue - IPO	1,050,000	8,937,172	44,685,860	96,600,000
1998	New issue - IPO[2]	240,000	9,177,172	45,885,860	22,080,000
2000	New issue in kind[3]	2,206,198	11,383,370	56,916,850	699,759,830[3]
2000	New issue – private placement	600,000	11,983,370	59,916,850	196,868,448
2000	Exercise of stock options	15,731	11,999,101	59,995,505	78,655
2001	Exercise of stock options	26,970	12,026,071	60,130,355	134,850
2002	Exercise of stock options	26,586	12,052,657	60,263,285	132,930
2003	Rights issue	4,821,850	16,874,507	84,372,535	118,578,253
2003	Exercise of stock options	3,547	16,878,054	84,390,270	17,735
2004	Exercise of stock options	12,011	16,890,065	84,450,325	60,055
2004	Rights issue	11,260,043	28,150,108	140,750,540	90,737,898
2004	Rights issue	2,815,010	30,965,118	154,825,590	22,684,468
2005	Reduction of share capital	-	30,965,118	61,930,236	-
2005	Rights issue	46,447,677	77,412,795	154,825,590	263,413,134
2006	Reduction of share capital	-	77,412,795	38,706,398	-
2007	Rights issue	38,706,397	116,119,192	58,059,596	387,160,784
2009	Rights issue	38,706,397	154,825,589	77,412,794	150,241,238
2010	Rights issue[4]	232,238,383	387,063,972	193,531,986	290,926,058
2012	Reduction of share capital	-	387,063,972	7,741,279	-
2012	Rights issue[5]	108,883,397	495,947,369	9,918,838	28,249,177

1) Amount generated by issue after transaction costs.

2) Result of over-allotment option.

3) A non-cash issue.

4) The shares issued were registered in part in December 2010 and in part in January 2011. For further details, please refer to note 18 in the annual report.

5) All shares were registered with the Companies Registration Office in January 2013. For further details, please refer to note 18 in the annual report.

FIVE-YEAR OVERVIEW

	GROUP				
(Amounts in MSEK unless otherwise stated)	2009	2010	2011	2012	2013
Income statement					
Net sales	5.9	–	–	33.2	47.0
Administrative expenses	–30.9	–32.8	–40.8	–25.1	–20.4
R&D expenses	–132.4	–129.4	–189.3	–107.9	–52.5
Other operating income and expenses	0.3	0.4	–1.0	0.0	3.6
Operating profit	–157.1	–161.8	–231.1	–99.8	–22.3
Financial net	2.6	–1.7	4.5	1.5	0.2
Results after financial items	–154.5	–163.5	–226.6	–98.3	–22.1
Balance sheet					
Licenses and similar assets	0.5	–	–	–	–
Equipment	5.8	4.6	5.6	3.7	4.5
Total non-current assets	6.3	4.6	5.6	3.7	4.5
Other non-current assets	10.2	9.9	7.4	19.9	13.0
Cash and cash equivalents	237.2	395.0	158.5	54.1	22.8
Total current assets	247.4	404.9	165.9	74.0	35.8
Total assets	253.7	409.5	171.5	77.7	40.3
Equity	215.2	342.5	115.9	45.9	23.8
Long-term liabilities	1.2	0.5	–	–	–
Short-term liabilities	37.3	66.5	55.6	31.8	16.5
Total equity and liabilities	253.7	409.5	171.5	77.7	40.3
Cash flow					
Cash flow from operating activities	–146.9	–158.9	–198.3	–127.8	–33.4
Net investments in non-current assets	–1.2	–2.0	–4.3	–0.2	–2.2
Net investments in other short-term placements	–19.9	82.3	–45.2	88.4	26.1
Cash flow from investing activities	–21.1	80.3	–49.5	88.2	23.9
Cash flow from financing activities	150.2	324.9	–33.9	23.9	4.3
Cash flow for the year	–17.8	246.3	–281.7	–15.7	–5.2
Operating cash flow	–148.1	–160.9	–202.6	–128.0	–35.6
Key figures					
Equity	215.2	342.5	115.9	45.9	23.8
Return on equity, %	–71.1	–58.6	–98.9	–121.5	–63.4
Return on capital employed, %	–72.3	–58.0	–100.8	–123.3	–64.0
Operating margin, %	n.m	n.m	n.m	n.m	n.m
Profit margin, %	n.m	n.m	n.m	n.m	n.m
Equity ratio, %	84.8	83.6	67.6	59.1	59.2
Interest-bearing assets (net)	237.2	395.0	158.5	54.1	22.8
Net investments in equipment	1.2	2.0	4.3	0.2	2.2
Average number of employees	67	68	68	51	40
– of whom work in R&D	60	60	60	43	35

	GROUP				
(SEK, unless otherwise stated)	2009	2010	2011	2012	2013
Data per share (SEK) [1) 2)]					
Earnings per share					
– Average number of shares	–0.78	–0.67	–0.58	–0.25	–0.04
– Number of shares at year end	–0.64	–0.42	–0.58	–0.25	–0.04
Operating cash flow per share					
– Average number of shares	–0.74	–0.66	–0.52	–0.33	–0.07
– Number of shares at year end	–0.62	–0.41	–0.52	–0.33	–0.07
Equity per share, year end	0.90	0.88	0.30	0.12	0.05
Share price at year end [3)]	4.55	1.95	1.47	0.35	0.73
Share price/equity per share at year end, % [3)]	507	222	494	297	1521
Number of shares (millions) [1) 2)]					
Average number of shares	198.9	244.1	389.8	389.8	494.2
Average number of shares including warrants	199.7	244.8	390.1	389.8	494.2
Number of shares at year end	239.9	389.8	389.8	389.8	495.9
Number of shares at year end including warrants	240.7	390.5	389.8	389.8	495.9

1) The outstanding cash warrants have no dilution effect as their conversion to shares would lead to an improvement in earnings and cash flow per share for the years included.
2) The number of shares for periods prior to rights issues have been adjusted for the bonus element in accordance with IAS 33, Earnings per share.
3) Share price data has been adjusted to reflect new share issues.

Definitions

AVERAGE NUMBER OF SHARES
Weighted-average number of shares outstanding during the year.

AVERAGE NUMBER OF SHARES, INCLUDING WARRANTS
Weighted-average number of shares, including warrants, outstanding during the year.

CASH AND CASH EQUIVALENTS
Cash and bank balances, and short-term investments with maturities of less than 90 days.

EARNINGS/LOSS PER SHARE
Earnings/loss in relation to the number of shares.

EQUITY PER SHARE
Shareholders' equity in relation to outstanding shares at year-end.

EQUITY RATIO
Equity as a percentage of total assets.

INTEREST BEARING ASSETS (NET)
Cash, bank balances and short-term investments.

NET CAPITAL INVESTMENTS
Capital investments in equipment net of disposals.

NUMBER OF SHARES AT YEAR-END
Number of shares outstanding at the end of the year.

NUMBER OF SHARES AT YEAR-END, INCLUDING WARRANTS
Number of shares, including warrants, outstanding at the end of the year.

OPERATING CASH FLOW
Cash flow from operating activities and cash flow from investments in machines, equipment and licenses.

OPERATING CASH FLOW PER SHARE
Cash flow from operating activities and cash flow from investments in equipment and licenses per share.

OPERATING MARGIN
Operating loss as a percentage of net sales.

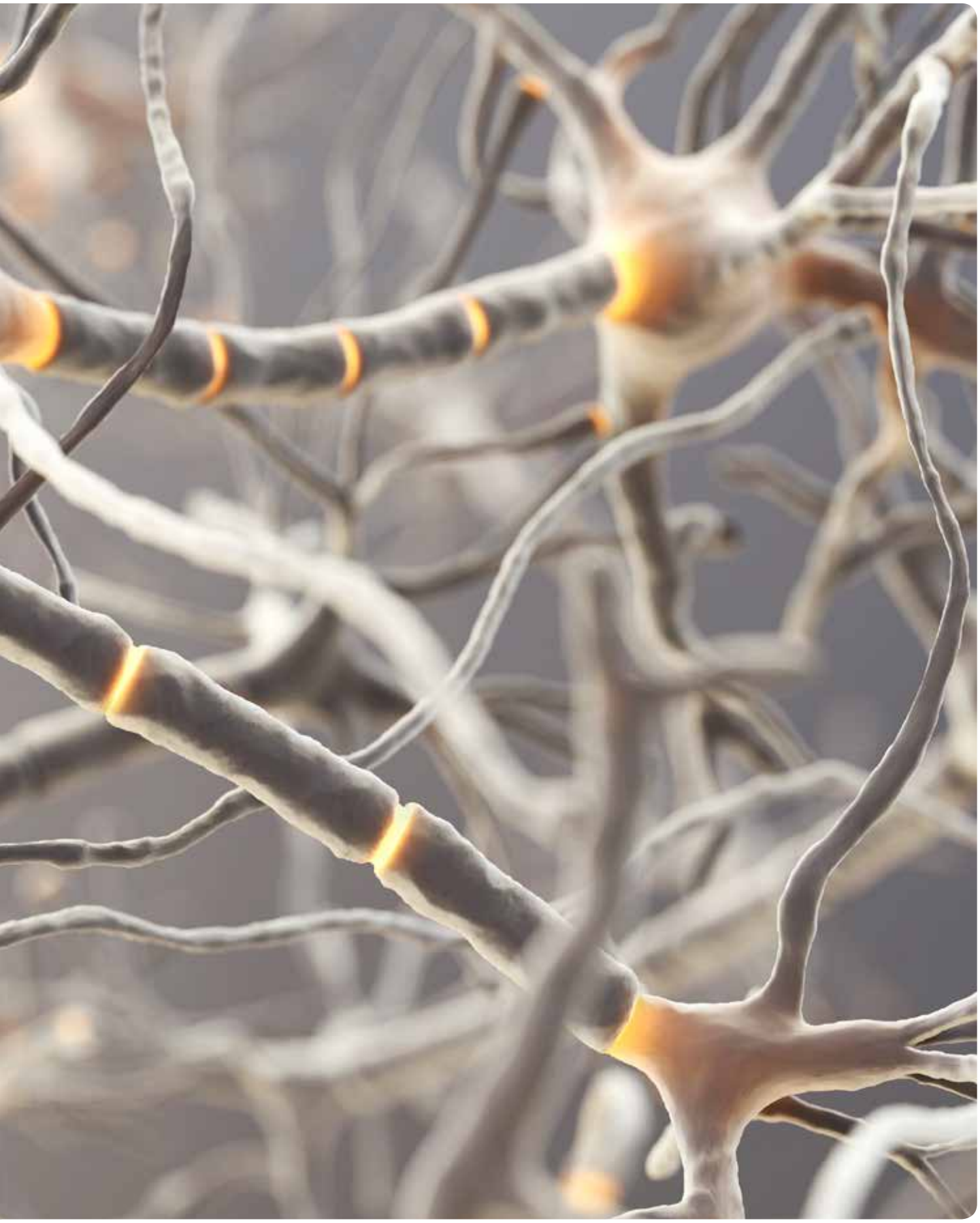
PROFIT MARGIN
Results for the year as a percentage of net sales.

RETURN ON CAPITAL EMPLOYED
Operating loss and financial income as a percentage of the average total assets less non-interest bearing liabilities.

RETURN ON EQUITY
Results after financial items as a percentage of average equity.

SHARE PRICE/EQUITY PER SHARE
Share price as a percentage of shareholders' equity per share at year-end.

FINANCIAL REPORTS



ADMINISTRATION REPORT

The Board of Directors and the President of Karo Bio AB (publ), registration number 556309-3359 and domiciled in Huddinge, Sweden, hereby presents its annual report regarding the operations of the Group and the Parent Company for the fiscal year beginning January 1 and ending December 31, 2013.

OPERATIONS

Karo Bio is an innovative research and development company which since the early 1990s has specialized in nuclear receptors as target proteins for the development of new drugs.

Nuclear receptors can be seen as on and off switches by which the body's own production of proteins can be regulated with great precision. By targeting these nuclear receptors, the body's own control systems can be tuned to treat several illnesses and diseases. Based on this knowledge, Karo Bio runs preclinical drug development projects within the areas of neuropsychiatry, inflammatory conditions, autoimmune diseases, and cancer.

Important processes within the company include research, drug discovery and preclinical development. Besides these processes, the company's expertise also covers clinical development, medical and regulatory issues. Karo Bio has the capacity to process selected compounds for niche indications through the entire development chain, while compounds addressing large patient groups require development collaborations or out-licensing at some stage of the process.

Karo Bio currently runs two proprietary preclinical projects in-house, one project in collaboration with Pfizer, and additional preclinical research activities. Karo Bio was founded in 1987 and has been listed on NASDAQ OMX Stockholm since 1998.

RESEARCH AND DEVELOPMENT – CURRENT STATUS AND SIGNIFICANT EVENTS 2013

Significant events during 2013 and current status for each of Karo Bio's projects are described briefly below.

ERbeta selective compounds – a platform with many opportunities

The estrogen receptor (ER) is activated by the estrogen hormone and regulates a number of functions in the body. Estrogen has a number of positive effects, but its medical use has been limited by an increased risk of developing breast and uterus cancer as well as thrombosis. These risks are primarily linked to the receptor subtype ERalfa, while the ERbeta receptor that Karo Bio was instrumental in discovering in the 1990s, appears to mediate many of the positive effects of estrogen without the side effects. From the intense research within this area, there is an increasing understanding of the role of the ERbeta receptor. Today, there is a clearer view that there are several clinical development opportunities for substances that act through the ER beta receptor.

Karo Bio's work in the ERbeta-field has resulted in a world-leading platform with several promising ERbeta-selective compounds. These substances have slightly varying properties and may thus be suitable for different indications.

A collaboration with Merck & Co., Inc. regarding an ERbeta substance was terminated in 2010, as the project had entered phase II development. As there have not been any safety related issues reported for the compound, Karo Bio is exploring the possibility to regain the rights to the compound for application in other areas.

ERbeta cancer

The preclinical data collated by Karo Bio indicate that ERbeta has an interesting potential in the area of cancer. In several preclinical models, the first drug candidate within the program, KB9520, has shown good efficacy for various forms of cancer. These effects can be assumed to have a general effect in several different types of cancer tumors, provided that they express ERbeta. Karo Bio is actively working to secure financing for continued development of ERbeta in the field of cancer.

ERbeta MS

Since 2011, Karo Bio is running a development project for ERbeta focused on the autoimmune disease multiple sclerosis (MS). In preclinical models, ERbeta agonists have demonstrated protective and reparative effects on the myelin sheaths that surround nerve cells. This is a significant finding, as myelin damage is involved in the symptoms of and disabilities in MS. If treatment with ERbeta agonists proves capable of repairing damaged myelin also in patients, this will represent a significant breakthrough in the treatment of patients with progressive MS, as current therapies only aim at reducing inflammation during the early stages of the disease.

To study the therapeutic effect of ERbeta agonists in more closely, in early 2013, Karo Bio conducted additional studies in disease models in animals. The new findings indicate that ERbeta has positive effects by protecting and repairing nerve tissue. Karo Bio continues the preclinical development of the project and in September 2013 the U.S. National MS Society awarded the project MUSD 0.5 in funding with conditional repayment.

RORgamma – a new opportunity to treat auto-immune disease

Recent research reveals that the nuclear receptor RORgamma may play a critical role in the development of auto-immune diseases, such as rheumatoid arthritis and psoriasis. In 2010, Karo Bio initiated a research program to develop and evaluate compounds that inhibit RORgamma activity. These compounds have potential as an innovative treatment for auto-immune diseases, since RORgamma has been shown to control the maturation of, and activity in, a certain type of immune cell, believed to drive inflammatory and debilitating processes in such diseases.

In December 2011, Karo Bio entered a research collaboration and licensing agreement with Pfizer for RORgamma to discover and develop new compounds for the treatment of auto-immune diseases. Pfizer will have exclusive rights to products developed as a result of the collaboration, while Karo Bio is entitled to royalties on sales.

Pfizer initially agreed to fully cover the research costs for two years. In June 2013, Pfizer opted to extend the research financing agreement for another year, up to and including 2015. In September 2013, Karo Bio achieved a project milestone, triggering a compensation of MUSD 2. In 2013, Karo Bio recognized revenue from the project of in total MUSD 7, equivalent to MSEK 44. The research collaboration is advancing.

Research

Karo Bio also conducts research at earlier stages around certain receptors to determine whether drugs can be designed that qualify for individual projects. Ideas are gathered from academic research and other pharmaceutical research, usually around certain signaling pathways. By testing if these pathways can be influenced via nuclear receptors or in a similar manner, Karo Bio can use its expertise to create value. This is very early research, where some ideas can be dismissed relatively quickly, while others can be evaluated over a longer or shorter period of time to when successful, qualify as a development project. Work is underway on a small number of nuclear receptors.

In 2013, Karo Bio entered into collaboration with Dr. Jörg Distler and his company 4D Science GmbH surrounding fibrosis. Dr. Distler's research team has discovered that a specific nuclear receptor plays a key role in the pathogenesis of fibrotic diseases, which may have implications for the treatment of patients with this type of intractable diseases. The partnership is initially focused on generating additional data to validate the nuclear receptor as a target in fibrosis and to demonstrate that it is possible to address it pharmacologically.

TR / eprotirome – dyslipidemia (No longer active)

Eprotirome is a liver-selective thyroid hormone receptor (TR), which was developed for the treatment of dyslipidemia. The pharmaceutical project was canceled in February 2012 when an animal study demonstrated adverse effects during long-term exposure. The total cost of the eprotirome Phase III program, which was scheduled to run until 2014, was estimated at about MSEK 300. The total cost of the program amounted to approximately MSEK 140, of which exit costs accounted for about MSEK 33.

KEY EVENTS AFTER THE END OF FISCAL YEAR 2013

February 13, the Board convened an Extraordinary General Meeting on March 17, 2014 to decide on a proposed share issue to existing shareholders in order to provide the company with net proceeds of approximately MSEK 70. Of the total issue, 85 per cent is underwritten. To enable the share issue, the Board proposes that the Articles of Association be amended so that the number of shares should be at least 250 million and at most 1,000 million.

The Board of Directors also proposes a share issue of a maximum 15 million shares to Anders Lönner, corresponding to approximately MSEK 7. This share issue is proposed at the same subscription price as the rights issue to existing shareholders. The proposed share issue to Anders Lönner represents 2.2 per cent of share capital after both issues, which implies that Anders Lönner would become one of Karo Bio's five largest owners.

The Nomination Committee also intends to propose Anders Lönner as new Chairman of Karo Bio. Göran Wessman will be proposed to remain on the Board as a Director. Until 2013, Anders Lönner was CEO of Meda. Prior to that, in 1997, he was CEO of Karo Bio and before that, he held senior positions with Astra.

The nomination committee also proposes Thomas Hedner as a new Board member, and that all other members are reelected.

Mark Farmery assumed the position as Group Head of Business Development on February 10. Mark Farmery has joined the management team, replacing Lars Öhman, who remains in a new consulting role. Maria Öhlander, Director of Clinical Development, is leaving Karo Bio on her own request on April 24, 2014 to take up a position as Research Director for a development-oriented nutrition company.

ORGANIZATION

In addition to the parent company Karo Bio AB, the Group consists of the wholly owned subsidiary Karo Bio Research AB, Karo Bio Discovery AB, and Kommanditbolaget Odenplan Fastigheter, none of which currently is conducting any business. The head office is located in Huddinge, outside of Stockholm, Sweden, also the site of the company's operations.

The management team consists of five people: the President and CEO, the Chief Financial Officer, the Director of Preclinical Development, the Director of Clinical Development, and the Vice President Business Development.

At the end of the year, Karo Bio had 39 (43) permanent employees, of whom 34 (37) were engaged in research and development, 1 (3) in business development and patents, and 4 (5) had administrative duties.

RESULTS AND FINANCIAL POSITION

Results

Group consolidated net sales amounted to MSEK 47.0 (33.2). Sales were mainly attributable to the RORgamma collaboration with Pfizer.

Operating expenses decreased to MSEK 69.3 (132.9), of which MSEK 33.0 is directly attributable to the divestment of the eprotirome program in 2012, while the remainder has resulted from savings. This year's expenditure on research and development amounted to MSEK 52.5 (107.9). Administrative expenses decreased to MSEK 20.4 (25.1).

Operating loss improved to MSEK -22.3 (-99.7). In the fourth quarter, Kommanditbolaget Odenplan Fastigheter was acquired. The purpose of the acquisition was to finance operations, by the means of balancing part of the Group accumulated debt deductions with untaxed profits of the acquired company. Due to the acquisition, net income for the year improved by MSEK 3.6. Financial items amounted to MSEK 0.2 (1.5). Net loss for the year improved to MSEK -22.1 (-98.3).

Investments

Investments amounted to MSEK 2.2 (0.6) and relate primarily to laboratory and IT equipment and laboratory reconfigurations.

Cash flow and financial position

Cash flow from operating activities amounted to MSEK -33.4 (-127.8). The rights issue of MSEK 32.7, which was conducted in the fourth quarter of 2012, brought in MSEK 28.3 to the company after transaction costs, of which MSEK 23.9 was booked in 2012 and MSEK 4.5 in 2013.

Cash and cash equivalents amounted to MSEK 22.8 (28.0) at year end. Including the short-term investments with a maturity exceeding 90 days, the company's financial assets amounted to MSEK 22.8 (54.1). Very early in 2014, the Group received cash payments of about MSEK 5, including a quarterly payment from the Pfizer collaboration.

Equity and share data

The registered share capital was MSEK 9.9 per December 31, 2013. The total number of shares was 495,947,369.

Total shareholders' equity amounted to MSEK 23.7 (45.9) after accounting for 2013 net income. Earnings per share, based on a weighted average of shares outstanding, amounted to SEK -0.04 (-0.25). The Group's equity at year end was 59.2 (59.1) per cent and equity per share, based on the fully diluted number of shares at year end, was SEK 0.05 (0.12).

PARENT COMPANY

The parent company's reported revenues amounted to MSEK 47.0 (33.2) and income after financial items to MSEK -22.1 (-98.6). Investments in fixed assets amounted to MSEK 2.2 (0.6). Cash and other short-term investments at year end amounted to MSEK 22.6 (54.0).

GUIDELINES FOR RENUMERATION TO SENIOR EXECUTIVES

The Board of Karo Bio proposes that the Annual General Meeting on May 8, 2014 resolves the following guidelines for determining salaries and other remuneration to senior executives of Karo Bio, to be applied until the AGM is held in 2015.

The proposed guidelines are largely the same as those approved by the 2013 AGM, except for the earlier provision that the recipient should invest a certain part of variable renumeration in Karo Bio stock.

General Information

Karo Bio will apply remuneration levels and terms of employment that are necessary to recruit and retain a competent management with the capacity to achieve established business goals. As a result, competitiveness shall be the overriding principle in relation to the salary and other remuneration of executive management.

Fixed salary

A fixed salary will be paid for work performed in a satisfactory manner.

Variable remuneration

In addition to fixed salary, variable remuneration may be offered to reward clearly goal-related achievements by simple and transparent mechanisms. The executive management's remuneration under incentive programs will be based on the extent to which business goals are achieved.

Karo Bio's commitments under incentive programs shall be limited in relation to the fixed annual salary and shall not exceed 40 per cent of the fixed annual salary, before taking into account social security charges, for each executive during the relevant period. The remuneration under incentive programs shall include pension and vacation benefits according to vacation legislation, and is thus not pensionable. The total maximum variable remuneration at 40 per cent of current fixed annual salary levels in 2013, including social security charges, would amount to MSEK 1.8.

Pension benefits

The terms of the executive management's pension benefits shall be competitive taking into account what is generally applicable to equivalent executives on the market and shall be based on defined contribution pension schemes or accede to the Swedish ITP plan. The pension benefits shall be based on a retirement age of 65 years.

Non-monetary benefits

The executive management's non-monetary benefits (such as car and health care benefits) should facilitate the performance of their work and be equivalent to what is considered reasonable in relation to market practice and the benefit for the company.

Dismissal and severance pay

Dismissal and severance pay shall not exceed 12 monthly salaries in total for each executive.

The executives to whom the remuneration guidelines apply

The above guidelines shall apply to the president of Karo Bio AB and executives that report directly to the president as well as presidents of Karo Bio's subsidiaries.

Information on remuneration previously resolved upon that has not fallen due

At present, there is no remuneration that has not fallen due that deviates from guidelines decided at previous AGMs.

Consultancy fee paid to board members

Going market rates may be paid to board members for consultancy work carried out for the company beyond the framework of their commitment to the Board.

Deviation from the guidelines under special circumstances

The Board may deviate from the guidelines in certain cases if there are special reasons for doing so.

INFORMATION REGARDING THE KARO BIO SHARE

At December 31, 2013, there were a total of 495,947,369 outstanding shares with a deviate value of SEK 0.02. The shares carry one vote each and are entitled to equal part of the company's distributable earnings. There are no limitations to the transferability of the Karo Bio shares due to legal constraints or by regulations in the company by-laws. To the best of Karo Bio's knowledge, no agreements have been made between any shareholders, which could limit the transferability of the shares. There is no shareholder that alone controls 10 per cent or more of the total number of shares of Karo Bio.

In the event of a substantial change in the ownership structure of Karo Bio (a "change of control"), Pfizer may terminate the research collaboration agreement entered into in December 2011.

AUTHORIZATION TO ISSUE NEW SHARES

The general meeting in 2013 gave the Board of Directors authorization, valid until the 2014 AGM, to decide on issuing new shares within the framework of the ECF agreement that gave the company the right, but not an obligation, to issue shares to Azimuth Opportunity Ltd. The agreement expired in October 2013 without having been exercised.

CONTINUED OPERATIONS

Without additional funding or revenues, present cash and financial investments are estimated to be sufficient to finance the current scope of operations until late in the second quarter 2014. Under the same conditions, equity may fall below 50 percent of the registered share capital at the beginning of the second quarter 2014.

The company believes that there are opportunities for additional revenue during the following quarters. As value creation from the operations would benefit from additional financing, the Board has decided to convene an Extraordinary General Meeting to decide on a share issue to existing shareholders, and a directed share issue.

When fully underwritten, these share issues are expected to contribute net proceeds of about MSEK 77. Following the share issues, Karo Bio's cash and cash equivalents are estimated to be sufficient for 12 months of further operations, even if no new collaboration contracts are signed or other financing is obtained.

CORPORATE GOVERNANCE REPORT

Karo Bio's corporate governance report is available at the company website www.karobio.com and is also included in this Annual Report.

Systems for internal control and risk management

The Group's systems for internal control and risk management regarding the consolidated financial reports are described in the section internal control and risk management regarding financial reporting in Karo Bio's corporate governance report.

FUTURE DEVELOPMENT

The Board and company management will strive to eventually reach a point where the Group's revenues significantly better match its costs. Revenues in such a situation could be in the form of payments from partnerships, public and private grants and compensation for certain activities. The operations are considered to be attractive enough for this to be achievable, although it may take years to get there. Before Karo Bio reaches this point, additional capital needs may arise.

Karo Bio is focusing its operations on the projects and activities that are expected to generate the best business opportunities and create the greatest value in the short term, thereby creating the best conditions for its development in the long run.

In the long term, the intention is that its activities should generate significant revenues from sales of pharmaceutical products in the market, where Karo Bio receives royalties on partners' product sales.

RISK FACTORS

There is no guarantee that Karo Bio's research and development will result in commercial success. There can be no guarantee that Karo Bio will develop products that can be patented, that granted patents can be retained, that future inventions will lead to patents, or that granted patents will be sufficient to protect Karo Bio's rights.

There is no guarantee that Karo Bio obtains approvals on its clinical trials applications or that the clinical trials conducted by Karo Bio, whether independently or in collaboration with its partners, can demonstrate sufficient safety and efficacy to obtain the necessary approvals from regulatory authorities, neither that they will result in marketable products. It cannot be excluded that the approval process at regulatory level will involve requirements for extended documentation and thereby increasing costs and introducing delays in the projects, or even discontinuation of projects. Increased total development costs and development time of a project could result in an increased project risk and reduce the product's potential to successfully reach the commercial stage or reduce the time from product launch to patent expiry.

There may be a need for the company to turn to the capital market for additional funding in the future. Both the size and the timing of the company's potential future capital requirements are dependent on a number of factors, including opportunities to enter into collaboration or licensing agreements and the progress made in research and development projects undertaken. There is a risk that the required funding of the operations will not be available when needed or at a reasonable cost.

PROPOSED APPROPRIATION OF LOSS

The Board of Directors proposes that the available non-restricted equity of SEK 13,928,475 is carried forward.

The company's results for the financial year and the financial position per December 31, 2013, are presented in the attached financial statements and accompanying notes which are integral parts of this Annual Report.

Consolidated income statements and income statements for the Parent Company

		GROUP			PARENT COMPANY	
KSEK	Note	2013	2012	2011	2013	2012
Net sales	1	47,029	33,173	-	47,029	33,173
Operating expenses	2–5					
Administrative expenses		–20,434	–25,116	–40,797	–20,434	–25,116
Research and development expenses		–52,529	–107,857	–189,321	–52,547	–108,207
Other operating income and expenses	6	3,676	51	–1,041	117	51
		–69,287	**–132,922**	**–231,159**	**–72,864**	**–133,272**
Operating profit/loss		**–22,258**	**–99,749**	**–231,159**	**–25,835**	**–100,099**
Income from financial investments						
Income from participations in Group companies		-	-	-	4,839	-
Write-downs on shares in Group companies	14	-	-	-	–1,280	-
Interest income and other similar income	7	198	1,510	5,921	195	1,510
Interest expenses and other similar expenses	8	–18	–15	–1,388	–3	–3
		180	**1,495**	**4,533**	**3,751**	**1,507**
Profit/loss after financial items		**–22,078**	**–98,254**	**–226,626**	**–22,084**	**–98,592**
Tax	9	-	-	-	-	-
PROFIT/LOSS FOR THE YEAR	10	**–22,078**	**–98,254**	**–226,626**	**–22,084**	**–98,592**
Earnings per share (SEK)	11					
– based on weighted-average number of shares outstanding		–0.04	–0.25	–0.58		
– based on weighted-average number of shares fully diluted [1]		–0.04	–0.25	–0.58		

[1] The final day of redemption for the warrants issued in the latest program was in April 2011. No dilutive effect from warrants outstanding is therefore taken into account.

Consolidated statements of comprehensive income and comprehensive income for the Parent Company

		GROUP			PARENT COMPANY	
KSEK	Note	2013	2012	2011	2013	2012
Profit/loss for the period		–22,078	–98,254	–226,626	–22,084	–98,592
Other comprehensive income for the year, net of tax		-	-	-	-	-
TOTAL COMPREHENSIVE PROFIT/LOSS FOR THE PERIOD		**–22,078**	**–98,254**	**–226,626**	**–22,084**	**–98,592**
Total comprehensive profit/loss attributable to:						
Shareholders of the parent company		–22,078	–98,254	–226,626	–22,084	–98,592

Consolidated statement of financial position and balance sheets for the Parent Company

ASSETS (KSEK)		GROUP			PARENT COMPANY	
At December 31	Note	2013	2012	2011	2013	2012
NON-CURRENT ASSETS						
Intangible assets						
Licenses and similar rights	12	-	-	-	-	-
Tangible assets						
Equipment	13, 20	4,500	3,771	5,558	4,316	3,509
Financial assets						
Participations in Group companies	14	-	-	-	150	150
Total non-current assets		**4,500**	**3,771**	**5,558**	**4,466**	**3,659**
CURRENT ASSETS						
Current receivables						
Accounts receivable		6,463	6,371	-	6,463	6,371
Derivative instruments	28	144	-	-	144	-
Other receivables		2,609	2,621	2,945	2,478	2,621
Prepaid expenses and accrued income	15	3,776	10,901	4,464	3,776	10,901
		12,992	**19,893**	**7,409**	**12,861**	**19,893**
Financial assets at fair value through profit or loss	16, 28	-	26,049	114,780	-	26,049
Cash and cash equivalents	17	22,799	28,024	43,753	22,619	27,964
Total current assets		**35,791**	**73,966**	**165,942**	**35,480**	**73,906**
TOTAL ASSETS		**40,291**	**77,737**	**171,500**	**39,946**	**77,565**

Consolidated statement of financial position and balance sheets for the Parent Company

SHAREHOLDER'S EQUITY AND LIABILITIES (KSEK)		GROUP			PARENT COMPANY	
At December 31	Note	2013	2012	2011	2013	2012
SHAREHOLDER'S EQUITY	18					
Share capital		9,919	7,741	193,532	9,919	7,741
Other contributed capital		1,006,818	1,008,996	980,747	-	-
Rights issue of new shares – on-going		-	-	-	-	2,178
Share premium reserve, restricted		-	-	-	-	-
Total non-restricted equity (Parent Company)		-	-	-	*9,919*	*9,919*
Share premium reserve, non-restricted		-	-	-	26,071	-
Accumulated loss (incl. Group profit/loss for the year)		–992,898	–970,820	–1,058,357	9,942	108,534
On-going new rights issue		-	-	-	-	26,071
Profit/loss for the year (Parent Company)		-	-	-	–22,084	–98,592
Total non-restricted equity (Parent Company)		-	-	-	*13,929*	*36,013*
Total shareholder's equity		**23,839**	**45,917**	**115,922**	**23,848**	**45,932**
LIABILITIES						
Non-current liabilities						
Other non-current liabilities	19, 20	-	-	-	-	-
Total non-current liabilities		**-**	**-**	**-**	**-**	**-**
Current liabilities						
Accounts payable – trade		3,657	5,812	9,952	3,657	5,812
Payables to Group companies		-	-	-	90	90
Other current liabilities	20	7,206	7,739	3,159	6,762	7,462
Accrued expenses and deferred income	21	5,589	18,269	42,467	5,589	18,269
Total current liabilities		**16,452**	**31,820**	**55,578**	**16,098**	**31,633**
TOTAL SHAREHOLDER'S EQUITY AND LIABILITIES		**40,291**	**77,737**	**171,500**	**39,946**	**77,565**
Pledged assets		-	-	-	-	-
Contingent liabilities	22	-	-	-	-	-

Consolidated statement of cash flows and cash flow statement for the Parent Company

		GROUP			PARENT COMPANY	
KSEK	Note	2013	2012	2011	2013	2012
Operating activities						
Operating loss before financial items		–22,258	–99,749	–231,159	–25,835	–100,099
Items note effecting cash flow						
Depreciation and amortization	5	1,434	1,748	2,409	1,353	1,515
Other		-	-	19	-	-
		–20,824	**–98,001**	**–228,731**	**–24,482**	**–98,584**
Financial income received	23	151	1,921	5,938	147	1,921
Dividends received		-	-	-	4,839	-
Financial items paid	23	–18	–14	–1,388	–3	–3
Cash flow from operating activities before changes in working capital		**–20,691**	**–96,094**	**–224,181**	**–19,499**	**–96,666**
Changes in working capital						
Changes in current operating receivables		–763	–4,819	4,552	–632	–4,819
Changes in accounts payable		79	–6,373	-1,685	79	–6,373
Changes in other current operating liabilities		–12,014	–20,514	23,031	–12,261	–20,514
Cash flow from operating activities		**–33,389**	**–127,800**	**–198,283**	**–32,313**	**–128,372**
Investing activities						
Investments in equipment		–2,245	–184	–4,262	–2,161	388
Investments in subsidiaries	14	-	-	-	–1,280	-
Other short-term investments		–25,904	–130,777	–553,362	–25,904	–130,827
Sale and redemption of other short-term investments		52,000	219,096	508,114	52,000	219,096
Cash flow from investing activities		**23,851**	**88,135**	**–49,510**	**22,655**	**88,657**
Financing activities						
Proceeds from rights issues		-	32,665	-	-	32,665
Portion of proceeds from rights issue received in 2013		7,665	–7,665	-	7,665	–7,665
Transaction costs for new rights issue [1]		–3,352	–1,064	–33,940	–3,352	–1,064
Cash flow from financing activities		**4,313**	**23,936**	**–33,940**	**4,313**	**23,936**
CASH FLOW FOR THE YEAR		**–5,225**	**–15,729**	**–281,733**	**–5,345**	**–15,779**
Cash and cash equivalents at the beginning of the year	17	28,024	43,753	325,486	27,964	43,743
Cash and cash equivalents at the end of the year	17	22,799	28,024	43,753	22,619	27,964

[1] At year-end paid out part of totally 4,416 KSEK regarding the rights issue 2012.

Consolidated statement of changes in equity

GROUP

KSEK	Share capital	Restricted reserves	Accumulated loss	Total
Balance at January 1, 2011	**191,593**	**982,686**	**–831,731**	**342,548**
Profit/loss for the year	-	-	–226,626	–226,626
Transactions with shareholders				
Issuance of new shares (net after deduction of transaction-related costs)	1,939	–1,939	-	0
Total transactions with shareholders	**1,939**	**–1,939**	**0**	**0**
Balance at January 1, 2012	**193,532**	**980,747**	**–1,058,357**	**115,922**
Profit/loss for the year	-	-	–98,254	–98,254
Transactions with shareholders				
Reduction of share capital	–185,791	-	185,791	0
Issuance of new shares (net after deduction of transaction-related costs) [1]	-	28,249	-	28,249
Total transactions with shareholders	**–185,791**	**28,249**	**185,791**	**28,249**
Balance at January 1, 2013	**7,741**	**1,008,996**	**–970,820**	**45,917**
Profit/loss for the year	-	-	–22,078	–22,078
Transactions with shareholders				
Issuance of new shares (net after deduction of transaction related costs) [1]	2,178	–2,178	-	0
Total transactions with shareholders	**2,178**	**–2,178**	**0**	**0**
BALANCE AT DECEMBER 31, 2013	**9,919**	**1,006,818**	**–992,898**	**23,839**

[1] All shares are registered with the Companies Registration Office in January 2013

The Parent Company's statement of changes in equity

PARENT COMPANY

KSEK	Share capital	On-going rights issue	Restricted reserve	Non-restricted reserve	On-going rights issue	Accumulated loss	Loss for the year	Total
Amount at January 1, 2012	**193,532**	**0**	**138,015**	**11,340**	**0**	**0**	**–226,612**	**116,275**
Total profit/loss	-	-	-	-	-	-	–98,592	–98,592
Transactions with shareholders								
Reduction of share capital	–185,791	-	-	-	-	185,791	-	0
Issuance of new shares (net after deduction of transaction-related costs)	-	2,178	-	-	26,071	-	-	28,249
Treatment of loss	-	-	–138,015	–11,340	-	–77,257	226,612	0
AMOUNT AT DECEMBER 31, 2012	**7,741**	**2,178**	**0**	**0**	**26,071**	**108,534**	**–98,592**	**45,932**
Total profit/loss	-	-	-	-	-	-	–22,084	–22,084
Transactions with shareholders								
Issuance of new shares (net after deduction of transaction-related costs)	2,178	–2,178	-	26,071	–26,071	-	-	0
Treatment of loss	-	-	-	-	-	–98,592	98,592	0
AMOUNT AT DECEMBER 31, 2013	**9,919**	**0**	**0**	**26,071**	**0**	**9,942**	**–22,084**	**23,848**

See note 18 for further information.

Accounting and valuation principles

THE GROUP

Statement of compliance

The consolidated financial statements of Karo Bio have been prepared in accordance with the Swedish Annual Accounts Act, RFR 1 *Supplementary Accounting Regulations for Groups*, *International Financial Reporting Standards* (IFRS) and statements concerning interpretation published by IFRIC as adopted by the European Union. The statements have been prepared on a historical cost basis, except for financial assets available for sale and financial assets and liabilities at fair value through profit and loss.

CHANGES IN ACCOUNTING PRINCIPLES AND INFORMATION

New accounting standards applied to the Group

None of the IFRS or IFRIC interpretations, mandatory for the first time in the financial year beginning January 1, 2013 have had a significant impact on the Group.

New standards, amendments and interpretations to existing standards which are not yet effective and not prematurely adopted

A number of new standards, amendments and interpretations to existing standards will become effective for annual periods beginning after January 1, 2013 and have not been applied in preparing the consolidated financial statements. None of these is expected to have a material impact on the consolidated financial statements.

Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis, except for certain financial instruments that are measured at fair value. Amounts are expressed in KSEK (thousands of Swedish kronor) unless otherwise indicated. MSEK is an abbreviation for millions of Swedish kronor. Amounts or figures in parentheses indicate comparative figures for 2012 and 2011, respectively.

Critical accounting estimates and judgments

The preparation of financial statements 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 principles. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements, relate to the valuation of tax losses carried forward and decisions regarding expensing or capitalizing development costs. For further information, see accounting and valuation principles below and notes 9 and 27.

Basis of consolidation

The consolidated financial statements comprise the financial statements of Karo Bio AB and its subsidiaries at December 31 each year. The financial statements of subsidiaries are prepared for the same reporting year as the Parent Company, using consistent accounting policies. All intra-group transactions, income and expenses, profits and losses and balance sheet items resulting from intra-group transactions are eliminated in full in the consolidated financial statements.

A subsidiary is a company over which the Parent Company has a controlling influence, generally as a consequence of a holding of shares that, directly or indirectly, provides the Parent Company with the control over more than 50 per cent of votes. A subsidiary is included in the consolidated financial statements as of the date of the acquisition, being the day on which the Parent Company obtains controlling influence, until that date where the controlling influence ceases.

Business combinations and goodwill

Business combinations are accounted for using the acquisition accounting method. The acquisition is considered to be a transaction by which the Group indirectly acquires the assets of the subsidiary and assumes its liabilities and other obligations. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair value at the acquisition date. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. Goodwill is reported as an asset in the balance sheet. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the income statement.

The shareholders' equity in the subsidiary is entirely eliminated upon acquisition. The Group's equity comprises the equity in the Parent Company and the equity in the subsidiaries earned after the acquisition.

Goodwill is reviewed for impairment annually, or more frequently if events or changes in circumstances indicate that the carrying value may not be recoverable. Where the recoverable amount is less than the carrying value, an impairment loss is reported. The recoverable amount is defined as the higher of an asset's fair value less costs of disposal and its value in use.

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Foreign currency translation

The consolidated financial statements are presented in Swedish Kronor (SEK), which is the functional currency of the company's operations. Transactions in foreign currencies are initially recorded at the functional currency rate ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange ruling on the balance sheet date. Any differences in the rate of exchange arising from the translation are recognized in the income statement. Non-monetary assets and liabilities that are valued at cost are recognized at historical rates of exchange, i.e. at the rates of exchange on the respective transaction dates. Items measured at fair value are translated at the rate of exchange on the valuation date.

Revenue recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured.

Revenue from strategic research collaborations

Karo Bio may receive four types of revenues from its strategic collaborative research projects: upfront payments, research funding, milestone payments and royalties. The specific recognition criteria for the different types of revenue described below must be met before revenue is recognized.

Compensation received for research collaborations, and for commitments in the agreement that Karo Bio has not yet completed, are amortized over the term of the contract during which Karo Bio fulfills its commitments.

Research funding is received periodically, often quarterly in advance, as a fixed amount for a defined number of Karo Bio scientists working in the project during the period. Research funding received is allocated over the contractual period to which it refers.

Milestone payments are triggered when a certain result has been achieved or a certain event has occurred, e.g. when compounds enter or pass a major step in the development process, as defined in the research collaboration agreement. These steps are usually linked to significant decision points in the partner's drug development process. A milestone payment is accounted for when all requirements specified in the research collaboration agreement for earning the milestone are met.

Royalty payments are based on the sale of finished partnered pharmaceutical products in the market. Royalty payments are accounted for when they are reported by the partner.

Other revenue

Revenue from out-licensing agreements other than research and development collaborations can be either in the form of upfront payments which are recognized as revenue when the conditions for receiving them are fulfilled, or as license maintenance fees which are allocated over the duration of a specified license period. Karo Bio may also receive compensation for services provided, which is recognized as revenue when contractual terms are met.

Government grants and other public funding are recognized as other operating income in the income statement over the period necessary to match the grant to the cost that it is intended to compensate.

Interest income is recognized on a time proportion basis using the effective interest method. Interest income is recognized as a financial item and not included in operating profit and loss.

Taxes

Income tax

Income tax comprises current and deferred taxes. Income tax is recognized in the income statement in respect of items recognized in the income statement, and recognized directly in equity when the tax is related to items recognized directly in equity.

Deferred tax is calculated as the difference between, on the one hand, the tax base of assets and liabilities and, on the other hand, their carrying amounts in the financial statements (temporary differences). Deferred tax is calculated based on the tax rates estimated to apply to settlement of the tax. As required by IAS 12 Income Taxes, deferred tax liabilities are recognized for all taxable temporary differences using the liability method.

Deferred tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which unused tax losses and deductible temporary differences can be balanced. As Karo Bio historically has reported losses, deferred tax assets are recognized only when there is convincing evidence that sufficient taxable profits will be available.

Value added tax (VAT)

Revenues, expenses and assets are recognized net of VAT. The net amount of VAT recoverable from, or payable to, the Tax Agency is included as part of receivables or payables in the balance sheet.

Intangible assets

Acquired intangible assets are recognized as assets in the balance sheet. Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of the acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. Internally generated intangible assets are not capitalized and expenditure for these is charged against profits in the year in which the expenditure is incurred, with the exception of capitalized development costs (see below).

The useful lives of all intangible assets of the Group have been assessed to be finite. Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and amortization method for

an intangible asset is reviewed at least at each financial year-end. Changes in the expected useful lives or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. The amortization expense is recognized in the income statement in the expense category consistent with the function of the intangible asset.

Research and development costs
Costs regarding development activities shall, as stipulated by IAS 38 Intangible Assets, be capitalized and reported in the balance sheet if certain criteria are met, while research costs are expensed as incurred. An intangible asset arising from development expenditure is recognized only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale; its intention to complete and its ability to use or sell the asset; how the asset will generate future economic benefits; the availability of resources to complete; and the ability to reliably measure the expenditure during the development. To date the Group has expensed all development costs as incurred since the recognition criteria for capitalization have not been met.

Property, plant and equipment
Property, plant and equipment are stated at historical cost less accumulated depreciation and any accumulated impairment losses. Historical cost includes, in addition to the purchase price, expenses directly related to bringing the asset into use. The difference between cost and estimated residual value is depreciated on a straight-line basis over the useful life of the assets.

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may no longer be recoverable. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each financial year-end.

Depreciation and amortization of non-current assets
Property, plant and equipment and intangible non-current assets are depreciated and amortized, using a straight-line depreciation and amortization method, over their estimated useful life based on the asset's cost as per the following schedule.

Year	
Licenses	3–10
Laboratory equipment	4–7
Leasehold improvements, IT equipment and other equipment	4

Impairment of non-current assets
At each reporting date the Group assesses whether there is an indication that an asset may be impaired. If any such indication exists, the Karo Bio Group makes an estimate of the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. Impairment losses of continuing operations are recognized in the income statement in the expense categories consistent with the function of the impaired asset.

Investments and other financial assets
Financial investments in the scope of IAS 39 *Financial Instruments:* Recognition and Measurement are classified as either financial assets at fair value through profit and loss, loans and receivables, held to maturity investments, or financial assets available for sale. When financial assets are recognized initially, they are measured at fair value plus directly attributable transaction costs, except for financial assets at fair value through profit and loss for which attributable transaction costs are included in the income statement. The classification of a financial asset is determined at initial recognition.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortized cost using the effective interest method. Gains and losses are recognized in income when the loans and receivables are derecognized or impaired.

Currency forward contracts
Karo Bio may hedge known future cash flows in foreign currencies from large currency rate fluctuations as provided in the company's financial policy. In this respect, a certain level of assurance must exist in order to consider possible transactions and related cash flows. Currency hedging is accomplished through currency forward contracts. In accordance with IAS 39, all derivatives are to be measured at fair value defined as market value by Karo Bio. The derivatives which can be used by the company do not qualify for hedge accounting in accordance with IAS 39. The classification of these instruments provides for them to be reported in the balance sheet at fair value with changes in fair value included in other operating income and expenses in the income statement.

Short-term investments

Short-term investments consist of investments in money market instruments, highly liquid bonds with maturities of less than five years and investments in highly liquid fixed income mutual funds. Short-term investments are classified as financial assets at fair value through profit or loss (financial assets held for trading purposes). This entails that the assets are stated at fair value in the balance sheet, defined as market value.

Changes in fair value are included in financial items in the income statement. Acquisitions and dispositions of short-term investments are reported as of the transaction day, the day when Karo Bio is committed to buy or sell the asset.

Fair value estimation of financial instruments measured in the balance sheet at fair value

When the group value on financial instruments at fair value, fair value is determined using a valuation hierarchy. The different levels are defined as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included in level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from process).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

According to Karo Bio's financial policy, funds shall be invested in financial instruments classified as level 1. The fair value of such financial instruments, traded in active markets, is based on quoted market prices on the balance sheet date. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. For further information, see note 28.

Trade and other receivables

Trade receivables, which generally have 30 day terms, are recognized and carried at original invoice amount less an allowance for any uncollectible amounts. Write-downs are made when there is objective evidence that Karo Bio will not be able to collect the debts.

Cash and cash equivalents

Cash and cash equivalents in the balance sheet comprise cash at banks and in hand and short-term deposits with an original maturity not exceeding 90 days. Other short-term investments are reported as financial assets at fair value through profit and loss. See notes 16 and 28 for further information on the classification of Karo Bio's short-term investments.

For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above. The cash flow statements for each year show direct cash flows from investment and financing activities. The operational cash flow is based on the indirect method.

Provisions

Provisions are recognized when the Group has a legal or constructive obligation as a consequence of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and that a reliable estimate can be made of the amount of the obligation. The expenses relating to any provision is presented in the income statement net of any reimbursement.

Pensions and other post-employment benefits

Employees in Sweden are entitled to retirement and family pension benefits in accordance with the nationwide ITP Plan. Commitments for these pensions are secured through an insurance arrangement with Alecta Pension Insurance (Alecta). In accordance with an announcement (UFR 3) from the Swedish Financial Reporting Council, this arrangement is considered a defined benefit multi-employer plan. Karo Bio has not had access to such information to facilitate reporting of the plan as a defined benefit plan. Consequently, the ITP plan that is secured through an insurance arrangement with Alecta is reported, in accordance with IAS 19 Employee Benefits, as a defined contribution plan. Under a defined contribution plan, fixed payments are made to an unaffiliated entity and thereafter no legal or constructive obligation exists to pay further contributions. Premiums for pension insurance written with Alecta are expensed in the year they relate to.

Termination benefits are payable when employment is terminated before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. Karo Bio recognizes termination benefits when it is demonstrably committed to either terminating the employment with current employees according to a detailed formal plan without possibilities of withdrawal; or providing termination benefits as a result of an offer made to encourage voluntary redundancy.

Lease agreements

Karo Bio has entered into lease agreements with third parties in the ordinary course of business. These contracts are for office and laboratory space, laboratory equipment, automobiles and other equipment. Leasing contracts are classified as either financial or operating, depending on the terms of the lease.

A financial lease transfers substantially all the risks and benefits incidental to ownership of the leased asset to Karo Bio. All other lease contracts are considered operating leases.

Financial leases are capitalized at the inception of the lease at fair value of the leased property or, if lower, at the present value of the minimum lease payments. Thus, the equipment under lease is recorded as an asset and the net present value of future minimum lease payments is recorded as a liability. Lease payments are apportioned between finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term, if there is no reasonable certainty that the Karo Bio Group will obtain ownership by the end of the lease term. Property, plant and equipment are depreciated as described under the heading Depreciation and amortization of non-current assets.

Operating lease payments are recognized in the income statement over the lease term in the period they relate to.

Stock option program

Karo Bio currently has no share-based incentive programs.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker is the function responsible for allocating resources and assessing performance of the operating segments. In Karo Bio, this function has been identified as the Group's executive management team. Karo Bio's operations entail only one segment; research and development of drugs, and the consolidated income statement, balance sheet, cash flow statement and the associated notes regard this single segment.

THE PARENT COMPANY

The annual report of the Parent Company is prepared in accordance with the Swedish Annual Accounts Act and in compliance with the Swedish Financial Accounting Standards Council's Recommendation RFR 2 and statements from the Financial Accounting Standards Council. The Parent Company's accounting and valuation principles are the same as the Group's with the exception for leasing. In the Parent Company, all leasing contracts are reported as operating leases.

Notes

NOTE 1 NET SALES

Net sales for 2013 and 2012 consisted of research payments for collaboration projects. For 2011, no net sales were reported.

NOTE 2 PERSONNEL AND REMUNERATION TO MEMBERS OF THE BOARD AND EXECUTIVE MANAGEMENT

All of the Group's employees are employed by the Parent Company. Consequently, the information provided below is the same for the Parent Company and the Group.

AVERAGE NUMBER OF EMPLOYEES	2013		2012		2011	
	Number of employees	Men	Number of employees	Men	Number of employees	Men
Huddinge, Sweden	40	22	51	28	68	34
Total	**40**	**22**	**51**	**28**	**68**	**34**

WAGES, SALARIES, OTHER REMUNERATION AND SOCIAL SECURITY EXPENSES	2013		2012		2011	
	Wages, Salaries, other remuneration	Social security expenses (of which pension costs)	Wages, Salaries, other remuneration	Social security expenses (of which pension costs)	Wages, Salaries, other remuneration	Social security expenses (of which pension costs)
Board and President	2,976	1,477	3,190	1,450	8,601	3,589
		(424)		(507)		(811)
Other employees	23,996	11,529	35,313	18,006	45,921	23,709
		(3,090)		(5,036)		(7,364)
Total	**26,972**	**13,006**	**38,503**	**19,456**	**54,522**	**27,298**
		(3,514)		**(5,543)**		**(8,175)**

Of wages, Salaries, other remuneration, KSEK 1,993 (2,205 and 4,345 respectively) refers to the President.

REMUNERATION TO BOARD MEMBERS

The Board consists of five Board members elected by the annual general meeting and two Board members with one deputy appointed by employee organizations.

The Chairman of the Board receives annual remuneration of KSEK 420. Each Board member who is not paid as an employee or consultant by the company receives KSEK 150 based on the decision at the 2013 annual general meeting. In 2013, a total of KSEK 1,200 (956 and 1,017, respectively) was paid in Board members' fees. Board members are reimbursed for direct expenses such as travel costs. All committee work is done by the full Board, and thus no specific committee fees are paid.

No other compensation has been expensed or paid to board members or companies owned by them in 2013. Total expensed compensation for 2013 for each member of the Board is specified in the table on the next page.

REMUNERATION TO EXECUTIVE MANAGEMENT

The Board of Directors has decided that the full Board should carry out the tasks that are to be performed by the compensation committee and thus deal with all matters regarding executive management compensation and benefits.

The guidelines for remuneration of the executive management adopted by the AGM 2013, as well as the Board's proposal for guidelines to be adopted by the AGM 2014, are included in the Administration Report. Below is a description of the application of the guidelines in 2013.

Members of executive management are paid a fixed monthly salary, and some executives have received other benefits in 2013, such as health care insurance. In 2013 no member of executive management has participated in any bonus program. Executive management is entitled to pension benefits in accordance with the nationwide ITP Plan as are all other Swedish employees, unless otherwise stated. Pension benefits are based on a retirement age of 65 and paid as long as the retiree lives. Paid salary including bonus qualifies for pension benefits. The ITP Plan provides for no pension benefits for annual salaries currently exceeding KSEK 1,698.

Executive management has also been eligible to participate in companywide share-based incentive programs. At December 31, 2013, the President and CEO Per Bengtsson held no employee stock options in Karo Bio. Other members of executive management held employee stock options representing in total 0 shares (0 and 0, respectively). No allocation was made in 2013. See Note 27 Stock Option Programs for further information.

At year-end 2013, the executive management consisted of, in addition to the CEO, four (four) persons, whereof two (two) women. The management consists of Maria Sjöberg, Chief Scientific Officer responsible for Preclinical Research and Development, Henrik Palm, Chief Financial Officer and responsible for Human Resources, Maria Öhlander, Head of Clinical Development and Regulatory Affairs, and Lars Öhman, Head of Business Development.

AGREEMENTS REGARDING SEVERANCE PAY

The President has a notice period of six months and is entitled to six months' salary as severance pay if employment is terminated by the company. Other members of executive management have a notice period of six months and are not entitled to severance pay.

TRANSACTIONS WITH RELATED PARTIES

Karo Bio has not granted any loans, guarantees, or surety to or for the benefit of any of its Board members, executive management or auditors. Apart from the exceptions stated below and under the heading Remuneration to Board members, none of the company's Board members or executive management has directly or indirectly participated in any business transactions with the company during the current or previous fiscal year. None of the company's auditors have participated in any such transactions.

Professor Jan-Åke Gustafsson, who was a deputy Board member of Karo Bio until and including the 2007 annual general meeting, has previously been active at the department of Biosciences and Nutrition at Karolinska Institutet, with which Karo Bio had a research collaboration. Prof. Gustafsson also provides scientific consulting services for the company. Prof. Gustafsson has received no Board fee, but for his consultancy services Karo Bio has paid a total of KSEK 0 (208 and 500, respectively). The agreement for consulting services from Prof. Gustafsson was discontinued in 2012.

REMUNERATION AND OTHER BENEFITS DURING THE YEAR TO THE BOARD OF DIRECTORS AND EXECUTIVE MANAGEMENT KSEK	Board remuneration/ Base salary	Variable salary	Other benefits	Share-based remuneration	Other remuneration	Pension expense	Total
Board of Directors							
Göran Wessman	420	-	-	-	-	-	420
Per Bengtsson (member since AGM 2013)	-	-	-	-	-	-	-
Christer Fåhraeus	150	-	-	-	-	-	150
Anders Waas	150	-	-	-	-	-	150
Per-Anders Johansson	150	-	-	-	-	-	150
Sibylle Lenz (member since AGM 2013)	112	-	-	-	-	-	112
Executive management							
Per Bengtsson, President	1,993	-	9	-	-	424	2,426
Other members of Executive management (4 persons) [1]	4,634	-	4	-	-	643	5,281
Total	**7,609**	**-**	**13**	**-**	**-**	**1,067**	**8,689**

1) The amount includes consultant compensation to Lars Öhman, VP of Business Development.

Comments to the table:

- Other benefits refer mainly to company car benefits and health care insurance.
- Pension expense refers to the expense that affected earnings as recognized in accordance with IAS 19 for the year. See Accounting and valuation principles and note 3 for further disclosures concerning the terms and conditions of pension benefits.

NOTE 3 PENSION COSTS

Commitments for retirement and family pension under the ITP plan are secured through an insurance arrangement with Alecta Pension Insurance (Alecta). Premiums regarding pension insurance with Alecta total KSEK 949 (1,590 and 2,734, respectively) for the year and premiums to other pension institutions under the ITP plan total KSEK 2,564 (3,953 and 5,441, respectively).

Alecta's surplus may be allocated to the insurance holders and the insured. At year-end, Alecta's surplus in the form of total consolidation level amounted to 148 per cent (129 and 113, respectively). The total consolidation level is defined as the market value of Alecta's assets as a percentage of the actuarial commitments determined as per Alecta's assumptions, which are different from IAS 19 Employee benefits. Please refer to Accounting and valuation principles for additional information on pensions.

NOTE 4 OPERATING EXPENSES BY TYPE

Operating expenses are distributed on expense type as follows.

	Group			Parent company	
	2013	2012	2011	2013	2012
Depreciation	–1,434	–1,748	–2,409	–1,353	–1,515
Personnel costs	–39,869	–58,033	–82,873	–39,869	–58,033
Facilities costs	–7,873	–9,661	–10,288	–7,873	–9,661
External costs	–23,787	–63,530	–134,548	–23,886	–64,114
Other operating income and expenses	3,676	51	–1,041	117	51
	–69,287	**–132,921**	**–231,159**	**–72,864**	**–133,272**

NOTE 5 DEPRECIATION AND AMORTIZATION

Depreciation and amortization costs are allocated to the company's functions and types of assets as follows.

		Group			Parent company	
	Note	2013	2012	2011	2013	2012
Function						
Administrative costs		233	333	389	233	333
Research and development costs		1,201	1,415	2,020	1,120	1,182
		1,434	**1,748**	**2,409**	**1,353**	**1,515**
Type of asset						
Licenses	12	-	-	-	-	-
Equipment	13	1,434	1,748	2,409	1,353	1,515
		1,434	**1,748**	**2,409**	**1,353**	**1,515**

NOTE 6 OTHER OPERATING INCOME AND EXPENSES

	Group			Parent company	
	2013	2012	2011	2013	2012
Exchange gains and losses, net	117	–288	–1,041	117	–288
Income from acquisition of KB Odenplan Fastigheter [1)]	3,559	-	-	-	-
Other	-	339	-	-	339
[1)] Net after transaction costs, see the Administration Report, page 19.	**3,676**	**51**	**–1,041**	**117**	**51**

NOTE 7 INTEREST INCOME AND OTHER SIMILAR INCOME

	Group			Parent company	
	2013	2012	2011	2013	2012
Interest income, capital gains/losses and dividends from short-term investments	333	1,818	5,322	330	1,818
Fair value gains and losses	–135	–308	599	–135	–308
	198	**1,510**	**5,921**	**195**	**1,510**

NOTE 8 INTEREST EXPENSE AND OTHER SIMILAR EXPENSES

Interest expense and other similar expenses amounted to KSEK 18 (15 and 1,388, respectively) for the Group. Of the amount, KSEK 1,370 was a cost for the adjustment for the Equity Credit Facility (EFC) agreement that the company entered into in 2010. Of the amount for 2011, KSEK 2,440 was an upfront payment of 1% of the ECF agreement that the Company entered into in 2010. Since the utilization of the ECF is conditional upon future resolutions of general meetings, this upfront payment is accounted for as a financial expense in the income statement. The remaining part of KSEK 18 (15 and 18, respectively) consists of interest charges on banking accounts and financial leasing (see also note 20). For the Parent Company, the entire amount of KSEK 3 (3) refers to interest charges on accounts payable.

NOTE 9 TAXES

Since Karo Bio is reporting losses for income taxation it is currently not paying any income taxes. Karo Bio has not recognized any deferred tax assets in relation to the unutilized tax losses carried forward as there is no convincing evidence, according to the definition in IAS 12, that sufficient future taxable profits will be available.

At year-end, the Parent Company's unutilized tax losses carried forward amounted to MSEK 2,143 (2,238 and 2,136, respectively). During the year, the Parent Company's unutilized tax losses were impacted by the acquisition of Odenplan KB as well as by the net loss. There is no statutory time limit for Swedish companies to utilize tax losses
.

RECONCILIATION BETWEEN ACTUAL AND NOMINAL TAX	Group			Parent company	
	2013	2012	2011	2013	2012
Reported loss before tax	–22,078	–98,254	–226,626	–22,084	–98,592
Tax at nominal tax rate 22.0 % (26.3% and 26.3% respectively)	4,857	25,841	59,603	4,859	25,930
Tax effect from deductible items not recorded as expenses	–	1,161	–	–	1,161
Tax effect from non-deductible items not recorded as revenue	–26,620	–	–	–26,620	–
Tax effect from other non-deductible items	758	–27	–65	758	–27
Tax effect of losses for which no deferred tax assets are recognized	–	–26,975	–59,538	–	–27,064
Tax effect of previously unrecognized loss carryforwards	21,005	–	–	21,003	–
Tax on reported loss	**0**	**0**	**0**	**0**	**0**

NOTE 10 LOSS FOR THE YEAR

The entire loss is related to the Parent Company's shareholders, no minority interests exist.

NOTE 11 LOSS PER SHARE

Loss per share is calculated as the loss for the year in relation to the weighted average number of shares outstanding during the year. Warrants are non-dilutive as exercise of warrants would decrease the loss per share reported for 2011–2013. Per share data is calculated based on the following number of shares.

NUMBER OF SHARES OUTSTANDING			
(000)	2013	2012	2011
Weighted-average during the year	494,178	389,812	389,812
At year-end	495,947	389,812	389,812

The number of shares for periods prior to rights issues has been adjusted for the bonus element in accordance with IAS 33 Earnings per share.

NOTE 12 LICENSES AND SIMILAR RIGHTS

Licenses and similar rights consist of exclusive rights to technologies licensed from Duke University, Durham, North Carolina in 2001 and licenses from University of California, San Francisco for scientific rights that were acquired in 1996. In 2007, a follow-up investment of KSEK 3,460 was made in the license from Duke University, in accordance with the terms of the license agreement.

	Group			Parent company	
	2013	2012	2011	2013	2012
Opening balance acquisition cost	33,779	33,779	33,779	74,719	74,719
Acquisitions	-	-	-	-	-
Closing balance acquisition cost	**33,779**	**33,779**	**33,779**	**74,719**	**74,719**
Opening balance amortization	–33,779	–33,779	–33,779	–74,719	–74,719
Depreciation for the year	-	-	-	-	-
Closing balance accumulated amortization	**–33,779**	**–33,779**	**–33,779**	**–74,719**	**–74,719**
Net book value	**0**	**0**	**0**	**0**	**0**

NOTE 13 EQUIPMENT

	Group			Parent company	
	2013	2012	2011	2013	2012
Opening balance acquisition cost	75,408	78,506	76,846	66,919	70,366
Acquisitions	2,164	637	3,402	2,161	288
Sales and discards	–3,865	–3,735	–1,742	–3,865	–3,735
Closing balance acquisition cost	**73,707**	**75,408**	**78,506**	**65,215**	**66,919**
Opening balance depreciation	–71,637	–72,948	–72,261	–63,410	–64,954
Sales and discards	3,864	3,059	1,722	3,864	3,059
Depreciation for the year	–1,434	–1,748	–2,409	–1,353	–1,515
Closing balance accumulated depreciation	**–69,207**	**–71,637**	**–72,948**	**–60,899**	**–63,410**
Net book value	**4,500**	**3,771**	**5,558**	**4,316**	**3,509**

Laboratory equipment with a carrying value of KSEK 184 (262 and 146, respectively) in the Group is financed through capital leases.

NOTE 14 PARTICIPATIONS IN GROUP COMPANIES

	Parent company	
	2013	2012
Opening balance acquisition cost	4,400	4,350
Acquisitions	1,280	50
Closing balance acquisition cost	**5,680**	**4,400**
Opening balance depreciation	–4,250	–4,250
Depreciation for the year	–1,280	–
Closing balance accumulated depreciation	**–5,530**	**–4,250**
Net book value	**150**	**150**

Name	Domicile	Reg.no.	Holding	No. of shares	Book value
Karo Bio Research AB	Huddinge, Sweden	556588-3641	100%	1,000	100
Karo Bio Discovery AB	Huddinge, Sweden	556880-1541	100%	50,000	50
Kommanditbolaget Odenplan Fastigheter	Stockholm, Sweden	915200-2044	100%	1	0

NOTE 15 PREPAID EXPENSES AND ACCRUED INCOME

	Group			Parent company	
Amount at December 31	2013	2012	2011	2013	2012
Prepaid rent	1,182	1,746	2,109	1,182	1,746
Prepaid insurance	389	389	506	389	389
Prepaid licenses and other IT-related expenses	1,762	639	666	1,762	639
Other	443	8,127	1,183	443	8,127
	3,776	**10,901**	**4,464**	**3,776**	**10,901**

NOTE 16 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

Financial assets at fair value through profit or loss consist of investments in liquid bonds with maturities of more than 90 days but less than five years at the time of acquisition.

NOTE 17 CASH AND CASH EQUIVALENTS

	Group			Parent company	
Amount at December 31	2013	2012	2011	2013	2012
Short-term investments with maturities of less than 90 days	-	-	9,931	-	-
Cash and bank balances	22,799	28,024	33,822	22,619	27,964
Cash and cash equivalents	**22,799**	**28,024**	**43,753**	**22,619**	**27,964**

NOTE 18 SHAREHOLDER'S EQUITY

Share capital consists of 495,947,369 shares (387,063,972 and 387,063,972, respectively) with a par value of SEK 0.02 (0.02 and 0.50, respectively). On April 27, 2012, the General Meeting voted to lower shareholder's equity to MSEK 7.7. In December 2012 a share issue with preferential rights to existing shareholders was carried out, resulting in 108,883,397 new shares for a total of 495,947,369 shares and an increase in share capital of KSEK 2,178 (whereof KSEK 2,178 was registered in January 2013) to KSEK 9,919 (whereof KSEK 7,741 was registered at the end of 2012 and KSEK 2,178 was registered in January 2013). In total, the rights issue generated KSEK 28,249 in net proceeds after transactions costs of KSEK 4,416.

In 2010 a rights issue with preferential rights to existing shareholders was carried out, resulting in 232,238,383 new shares and an increase in share capital of KSEK 116,120 (whereof KSEK 114,181 regarding shares registered 2010 and KSEK 1,939 regarding shares registered in January 2011) to KSEK 193,532 (whereof KSEK 191,593 was registered at the end of 2010 and KSEK 1,939 was registered in January 2011). In total, the rights issue generated KSEK 290,926 net of transaction costs amounting to KSEK 34,208.

At year-end, there were no outstanding warrants. No warrants were exercised during 2011, 2012 or 2013.

In accordance with the Board's policy for dividend, the Board of Directors will propose to the annual general meeting to be held on May 8, 2014, that no dividend shall be paid for the financial year 2013.

NOTE 19 NON-CURRENT LIABILITIES

The balance sheet item non-current liabilities comprises future lease payments on leased equipment only. None of the non-current liabilities falls due more than five years after the balance sheet date. See note 20.

NOTE 20 CAPITAL LEASES

The present value of future minimum lease payments is reported as a liability in the balance sheet. Such payments fall due as outlined below.

	Group		
Amount at December 31	2013	2012	2011
Within one year	195	277	229
Later than one, but within five years	-	-	-
Later than five years	-	-	-
	195	**277**	**229**

Variable fees, which mean the difference between the interest when entering into the agreement and paid interest, are included in operating expenses during the year and amount to KSEK 8 (8 and 48, respectively). Capital lease contracts entered into in the year amounted to KSEK 2 (350 and –, respectively). The capital lease contracts pertain to laboratory equipment with a carrying value of KSEK 184 (262 and 146, respectively).

The interest rate in lease contracts is variable and linked to the Swedish general interest rate. Karo Bio has the right to extend the leasing period or acquire, direct or indirectly via another entity, the equipment at a predetermined price upon expiration of the contract.

NOTE 21 ACCRUED EXPENSES AND DEFERRED INCOME

	Group			Parent company	
Amount at December 31	2013	2012	2011	2013	2012
Accrued employee related expenses	4,093	3,487	14,499	4,093	3,487
Deferred income	330	10,389	20,778	330	10,389
Accrued research and development expenses	633	2,884	6,707	633	2,884
Other	533	1,509	483	533	1,509
	5,589	**18,269**	**42,467**	**5,589**	**18,269**

NOTE 22 CONTINGENT LIABILITIES

In 2013, Karo Bio was awarded a research grant of MSEK 0.5 from the National MS Society with conditional repayment.

Karo Bio's collaboration agreements with former partners Abbot Laboratories and Bristol-Myers Squibb remain in effect. The agreements have varying terms in the event that one of the parties wishes to conclude its active participation.

Certain situations stipulate mutual rights of participation in the other party's future revenue from the collaboration that has concluded or a compound that has been surrendered. Regarding the agreement with Bristol-Myers Squibb and the compound KB2115 (eprotirome), Karo Bio is obligated to pass on part of its future revenue from the compound to Bristol-Myers Squibb, both in the form of one-time payments from a licensing partner and in the form of royalty payments on future product sales.

Pursuant to agreements with a handful of external partners, they are entitled to royalty and/or milestone payments attributable to Karo Bio's future revenues. One agreement gives the counterparty the right to receive a milestone payment and royalty payments attributable to Karo Bio's future US-related revenues from the thyroid receptor area. These payments constitute, in full, a limited share of Karo Bio's future revenue in this area. Another agreement gives the counterparty the right to royalty payments of 5 per cent attributable to Karo Bio's future revenue from certain indications within the GR area.

Karo Bio has also entered into an agreement with staff to waive salary under 2013 in exchange for certain compensation in the event that the Company have reported net profits by the end of 2017.

NOTE 23 ADDITIONAL INFORMATION ON CASH FLOW STATEMENTS

	Group			Parent company	
	2013	2012	2011	2013	2012
Interest received	446	3,040	6,410	443	3,040
Interest paid	–3	–3	–1,374	–3	–3
Income taxes paid	–	–	–	–	–

NOTE 24 OPERATING LEASES

Leasing costs for the year amounted to KSEK 5,538 (6,535 and 6,827, respectively) for the Group and KSEK 5,628 (6,842) for the Parent Company. Future minimum lease payments on non-cancelable lease contracts fall due as follows. Most contracts state lease payments that are either linked to inflation or based on flexible interest rates. The leasing agreements relate to laboratory and office space and laboratory equipment.

	Group			Parent company	
Amount at December 31	2013	2012	2011	2013	2012
Within one year	4,062	5,832	6,654	4,142	5,948
Later than one, but within five years	8,120	16,038	4,991	8,120	16,038
Later than five years	-	-	-	-	-
	12,182	**21,870**	**11,645**	**12,262**	**21,986**

NOTE 25 INTER-COMPANY PURCHASES AND SALES

Karo Bio AB did not purchase any services from subsidiaries in 2013, 2012 or 2011.

NOTE 26 REMUNERATION TO AUDITORS

GROUP AND PARENT COMPANY (KSEK)	2013	2012
PwC		
-Auditing commission	485	485
-Auditing in addition to the audit commission	131	138
-Tax guidance	35	43
-Other assignments	-	148
Total	**651**	**814**

NOTE 27 STOCK OPTION PROGRAMS

WARRANT INCENTIVE PROGRAM 2010

The annual general meeting 2010 approved a warrant incentive program for executive management. The Board has since decided not to pursue the program, and consequently no allocation of warrants under the program has been made. The program originally comprised warrants representing 5,000,000 shares, which, following adjustment for effects of the rights issue in 2010 in accordance with the terms and conditions for this program corresponds to 7,100,000 shares. The warrants are issued to the wholly owned subsidiary Karo Bio Research AB.

PROGRAM 2003

On May 31, 2011, all outstanding warrants were cancelled regarding a previous employee stock option program, Program 2003, representing 732,640 shares at year-end 2010.

ALLOCATION OF STOCK OPTIONS (CORRESPONDING NUMBER OF SHARES)	2013	2012	2011
Outstanding at January 1	0	0	138,427
Allocated	-	-	-
Effect from issuance of shares	-	-	-
Exercised	-	-	-
Forfeited	-	-	–138,427
Outstanding at December 31	**0**	**0**	**0**
Whereof vested	0	0	0

WEIGHTED AVERAGE EXERCISE PRICE FOR STOCK OPTIONS SEK	2013	2012	2011
Outstanding at the beginning of the year	0	0	13
Effect from issuance of shares	-	-	-
Forfeited in the period	0	0	13
Exercised in the period	-	-	-
Outstanding at the end of the period	0	0	0
Exercisable at the end of the period	0	0	0

The weighted average remaining period for stock options outstanding at year-end was 0 (0 and 0 respectively) with exercise prices ranging from SEK 11.00 to 14.40.

NOTE 28 FINANCIAL INSTRUMENTS PER CATEGORY

31 December 2013	Liabilities and accounts receivable	Financial assets at fair value through profit or loss	Financial assets that may be sold	Total
Assets on the balance sheet				
Financial assets at fair value through profit or loss	–	–	–	0
Derivative instruments	–	144	–	144
Accounts receivable and other receivables	6,463	–	–	6,463
Cash and cash equivalents	22,799	–	–	22,799
Total	**29,262**	**144**	**0**	**29,406**

	Liabilities at fair value through profit or loss	Other financial liabilities	Total
Liabilities on the balance sheet			
Liabilities regarding financial leasing	–	196	196
Accounts payble and other liabilities excluding non-financial debt	–	8,954	8,954
Total		**9,150**	**9,150**

31 December 2012	Liabilities and accounts receivable	Financial assets at fair value through profit or loss	Financial assets that may be sold	Total
Assets on the balance sheet				
Financial assets at fair value through profit or loss	–	26,049	–	26,049
Accounts receivable and other receivables	6,371	–	–	6,371
Cash and cash equivalents	28,024	–	–	28,024
Total	**34,395**	**26,049**	**0**	**60,444**

	Liabilities at fair value through profit or loss	Other financial liabilities	Total
Liabilities on the balance sheet			
Liabilities regarding financial leasing	–	277	277
Accounts payble and other liabilities excluding non-financial debt	–	11,284	11,284
Total	**0**	**11,561**	**11,561**

Karo Bio, like any other business enterprise, is exposed to various risks that change over time. The relevant risks for Karo Bio can be broken down into commercial risks and financial risks. Karo Bio's financial policy determines allocation of responsibility for the finance operations, which financial risks the company is willing to assume and guidelines for how such risks are to be reduced and managed. Financial risk management is centralized and is the responsibility of the Chief Financial Officer. The policy, which is reviewed and approved annually by the Karo Bio Board of Directors, is developed to control and manage the following risks:

- Foreign currency risk
- Funding risk
- Liquidity risk
- Interest rate risk
- Credit risk in investments

FOREIGN CURRENCY RISKS

Changes in foreign currency rates have an impact on Karo Bio's earnings and equity in different ways:

- Earnings are affected when revenues and expenses are denominated in different currencies – transaction risk
- Earnings are affected when assets and liabilities are denominated in different currencies – translation risk
- Earnings are affected when the income statements of foreign subsidiaries are converted into Swedish kronor – translation risk
- Shareholder's equity is affected when the balance sheets of foreign subsidiaries are converted into Swedish kronor – translation risk

Operational currency risks

Karo Bio operates in an international industry. Most of the company's revenues have been denominated in US dollars and approximately 84 (65 and 58, respectively) per cent of expenses are incurred in SEK. The remainder of Karo Bio's expenses is mainly denominated in euros, British pounds (GBP) and US dollars (USD). This leads to an exposure to currency fluctuations, a combination of translation and transaction risks. Karo Bio's reporting currency is SEK.

The table on the next page indicates the effect on Karo Bio's revenues and operating result, if the Swedish krona is strengthened by 10 per cent. Both translation and transaction risks have been considered. The total effect on the operating result would be MSEK -3.4 (1.4 and 9.5, respectively).

At year-end 2013, the total nominal value of existing currency forward contracts was MSEK 5.5, with an average time to maturity of 0 months. At year-end, the unrealized gain on these contracts amounted to MSEK 0.1. There were no active currency forward contracts at year-end 2012 or 2011, and the operating losses for these years have not been affected by any matured currency forward contracts.

Financial risks

Currency risks in financial flows related to liabilities and investments is reduced by making investments in SEK, unless an investment using a foreign currency would serve as a hedge of an existing exposure.

FUNDING RISK

The risk that the company will not have access to necessary financing at all times is defined as funding risk. From time to time, the company has raised additional funds in the capital market to secure sufficient funds for the operations and stability of the company. The aim is to always have sufficient capital for at least 12 months of operations. A recurring review of funding needs is carried out in combination with an assessment of capital market developments to evaluate financing strategies. For further information, see under the headline Continued operations in the Administration Report.

The equity credit facility entered into in connection with the new share issue in 2010 was adjusted during the third quarter of 2011 so that it could be utilized at the then current share price, which is not possible at the prevailing share price. The mandate to utilize the credit facility will be annually submitted to the Annual General Meeting. The option to utilize the equity credit facility expired in the fourth quarter.

LIQUIDITY RISK

Liquidity risk refers to the risk that the company will not have sufficient monetary assets readily available to pay current foreseen or unforeseen expenditures. The risk is associated with the supply and maturity of short-term investments and the risk that there is no market for a specific instrument that the company intends to sell. Liquidity risk is managed by structuring the maturities of investments based on cash flow forecasts and also by limiting investments in bonds with low liquidity on the second-hand market. Weighted remaining duration of short-term investments was 0 months (3 and 5 respectively) at year-end.

INTEREST RATE RISK

Interest rate risk is the risk that a change in interest rates will cause a negative impact on the value of interest-bearing assets. In accordance with policy, investments are made with variable terms and maturities. The immediate impact on short-term investments if the interest rate would decrease by one percentage is 0 per cent (0.22 and 0.23, respectively) or MSEK 0 (0.1 and 0.3, respectively).

CREDIT RISK IN INVESTMENTS

Credit risk refers to the risk that Karo Bio will not receive payment for an investment. The credit risk is divided into an issuer's risk and a counterpart's risk. Issuer's risk is the risk that the securities, which Karo Bio owns, will lose their value because the issuer cannot meet its commitments in the form of interest payments and payments on the due date. Counterpart's risk is the risk that the party that from which Karo Bio buys investments from or sells investments to cannot provide securities or fails to make payments as agreed.

The policy manages credit risk by regulating which parties Karo Bio can do business with and what credit ratings are required for investments. There is no material concentration of credit risks.

FAIR VALUE OF ASSETS AND LIABILITIES

Short-term investments comprise investments in money market instruments, highly liquid bonds with maturities of less than five years and investments in highly liquid fixed income mutual funds. These assets are classified as financial assets at fair value through profit and loss. This entails that the assets are stated at fair value in the balance sheet, defined as market value. Changes in fair value are included in financial items in the income statement.

Karo Bio's financial instruments are traded in active markets with readily and regularly available quoted market prices which represent actual and regularly occurring market transactions on an arm's length basis. Thus, these are classified as level 1 according to IFRS 7. The fair value of Karo Bio's financial assets measured at fair value through profit and loss, defined as the quoted price in the market, amounts to MSEK 0 (26 and 115, respectively). For other assets and liabilities, book value corresponds to market value.

CURRENCY EFFECT (MSEK)
Effect on consolidated revenues and operating result before hedging transactions, when SEK is strengthened by 10 per cent.

Currency	Revenues	Operating profit/loss
USD	–4.5	–4.1
Euro	-	0.5
GBP	-	0.2
Other	-	-
Total	**–4.5**	**–3.4**

NOTE 29 SEGMENT INFORMATION

Based on the information that is processed by the Group's management team and used to make strategic decisions, Karo Bio's operations consists of a single operating segment, namely research and development for drug discovery. When evaluating the business and in strategic discussions and decisions, no breakdowns are made of the business in additional operating segments. Development of Karo Bio's drug projects is an integrated process coordinated by project managers who report to the executive management.

Different parts of the organization are involved in this process to varying degrees at different stages of the development chain. Project managers establish project budgets, including direct project costs, internal resources and timelines for the various activities. The executive management team evaluates projects budgets and conducts regular monitoring of project costs and timelines. The following table shows how the revenue and assets are distributed by geographic area.

	Group		
KSEK	2013	2012	2011
Revenues			
Sweden	960	236	-
Rest of Europe	-	-	-
USA	46,069	32,937	-
	47,029	**33,173**	**-**
Non-current assets			
Sweden	4,500	3,771	5,558
Rest of Europe	-	-	-
USA	-	-	-
	4,500	**3,771**	**5,558**

NOTE 30 TRANSACTIONS WITH RELATED PARTIES

Karo Bio has no transactions with related parties as defined in IAS 24 *Related Party Disclosures* to disclose other than those named in note 2 regarding remuneration to members of the Board and executive management.

NOTE 31 SIGNIFICANT EVENTS AFTER THE END OF THE FISCAL YEAR

New share issue proposed by the Board

The Board of Directors has proposed a share issue to existing shareholders, with net proceeds of approximately MSEK 70. Of the total issue, about 85 per cent is underwritten. To enable the share issue, the Board proposes that the Articles of Association be amended so that the number of shares should be at least 250 million and at most 1,000 million.

The Board of Directors also proposes a directed share issue of a maximum 15 million shares to Anders Lönner, corresponding to approximately MSEK 7. This share issue is proposed at the same subscription price as the rights issue to existing shareholders. The directed share issue to Anders Lönner represents 2.2 per cent of share capital after both issues, which implies that Anders Lönner would become one of Karo Bio's five largest shareholders.

To decide on these proposals, the Board has convened an Extraordinary General Meeting held on March 17, 2014 at 16.00 CET, at Restaurang Tango, Novum Research Park (5th floor), Hälsovägen 7, Huddinge, Sweden.

Anders Lönner nominated as Chairman

The Nomination Committee also intends to propose Anders Lönner as new Chairman of Karo Bio. Göran Wessman will be proposed to remain on the Board as a Director.

Until 2013, Anders Lönner was CEO of Meda. Prior to that, in 1997, he was CEO of Karo Bio and before that, he held senior positions with Astra.

The nomination committee also proposes Thomas Hedner as a new Board member, and that all other members are reelected.

New Head of Business Development

Mark Farmery assumed the position as Group Head of Business Development on February 10. Mark Farmery, who has BSc in Protein chemistry and a PhD in Microbiology, has joined Karo Bio from AstraZeneca, where he was active in Business Development. Lars Öhman remains in a new consulting role.

Other organizational changes

Maria Öhlander, Director of Clinical Development, is leaving Karo Bio at her own request on April 24, 2014 to take up a position as Research Director for a development-oriented nutrition company.

Other

In January 2014, Karo Bio reached a first milestone in the MS project's collaboration with MS Society, resulting in approximately half of the granted 0.5 MUSD was paid out.

The Board of Directors and the President declare that the consolidated financial statements have been prepared in accordance with IFRS as adopted by the EU and give a true and fair view of the Group's financial position and results of operations. The financial statements of the Parent Company have been prepared in accordance with generally accepted accounting principles in Sweden and give a true and fair view of the Parent Company's financial position and results of operations.

The statutory Administration Report for the Group and the Parent Company provides a fair review of the development of the Group's and the Parent Company's operations, financial position and results of operations and describes material risks and uncertainties facing the parent company and the companies included in the Group.

The income statements and balance sheets will be presented for the annual general meeting on May 8, 2014 for adoption.

HUDDINGE, MARCH 13, 2014

Per Bengtsson
President and CEO

Göran Wessman
Chairman

Christer Fåhraeus
Board member

Per-Anders Johansson
Board member

Sibylle Lenz
Board member

Anders Waas
Board member

Bo Carlsson
Board member
Employee representative

Johnny Sandberg
Board member
Employee representative

OUR AUDIT REPORT WAS ISSUED MARCH 14, 2014

PricewaterhouseCoopers AB

Håkan Malmström
Authorized Public Accountant

Auditor's report

To the annual meeting of the shareholders of Karo Bio AB (publ), corporate identity number 556309-3359

REPORT ON THE ANNUAL ACCOUNTS AND CONSOLIDATED ACCOUNTS

We have audited the annual accounts and consolidated accounts of Karo Bio AB (publ) for the year 2013. The annual accounts and consolidated accounts of the company are included in the printed version of this document on pages 18–42.

Responsibilities of the Board of Directors and the Managing Director for the annual accounts and consolidated accounts

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

Auditor's responsibility

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

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

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

Opinions

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

We therefore recommend that the annual meeting of shareholders adopt the income statement and balance sheet for the parent company and the income statement and financial position of the group.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

In addition to our audit of the annual accounts and consolidated accounts, we have also audited the proposed appropriations of the company's profit or loss and the administration of the Board of Directors and the Managing Director of ABC AB for the year 2013.

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, and the Board of Directors and the Managing Director are responsible for administration under the Companies Act.

Auditor's responsibility

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

As a basis for our opinion on the Board of Directors' proposed appropriations of the company's profit or loss, we examined whether the proposal is in accordance with the Companies Act.

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

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

Opinions

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

Stockholm March 12, 2014
PricewaterhouseCoopers AB

Håkan Malmström
Authorized Public Accountant

Corporate governance report

INTRODUCTION

The Board of Directors of Karo Bio hereby submits the corporate governance report for 2013, compliant with the Annual Reports Act (ÅRL 6 kap 6 §) and the Swedish Code of Corporate Governance (" the Code") (available at www.corporategovernanceboard.se). Karo Bio has applied the Code since July 1, 2008.

The corporate governance report has been reviewed by the company's auditor, in accordance with the Annual Reports Act. It does not constitute a section of the formal annual report documentation.

The Group consists of the Parent Company, Karo Bio AB, and the subsidiaries, Karo Bio Research AB, Karo Bio Discovery AB and Kommanditbolaget Odenplan Fastigheter. The subsidiaries conduct no operations.

SHAREHOLDERS

Karo Bio AB's shares have been listed on the NASDAQ OMX Stockholm exchange since 1998. As per December 31, 2013, the number of shareholders amounted to 11,799 (11,145). According to the shareholder list provided by Euroclear Sweden AB as per December 31, 2013, Försäkringsaktiebolaget Avanza Pension had accumulated shareholdings of 9.6 (7.0) per cent, JP Morgan 4.5 (12.2) per cent and Nomic AB 3.9 (0.5) per cent, respectively. The ten largest shareholders owned 29 (33) per cent of the total number of shares. The proportion of foreign shareholders amounted to 14 (25) per cent. A proportion of 0.2 (0.4) per cent of shareholders held 1,000 shares or fewer.

There are no limitations that apply to the transferability of Karo Bio shares due to either legal restrictions or the Articles of Association. To the best of Karo Bio's knowledge, no agreements exist between any shareholders which could possibly limit the transferability of shares. No single shareholder controls more than 10 per cent of the total number of shares in Karo Bio.

No breaches of the listing agreement or good practice on the stock market according to resolutions from the Exchange's disciplinary committee or the Swedish Securities Council disciplinary committee occurred during the financial year.

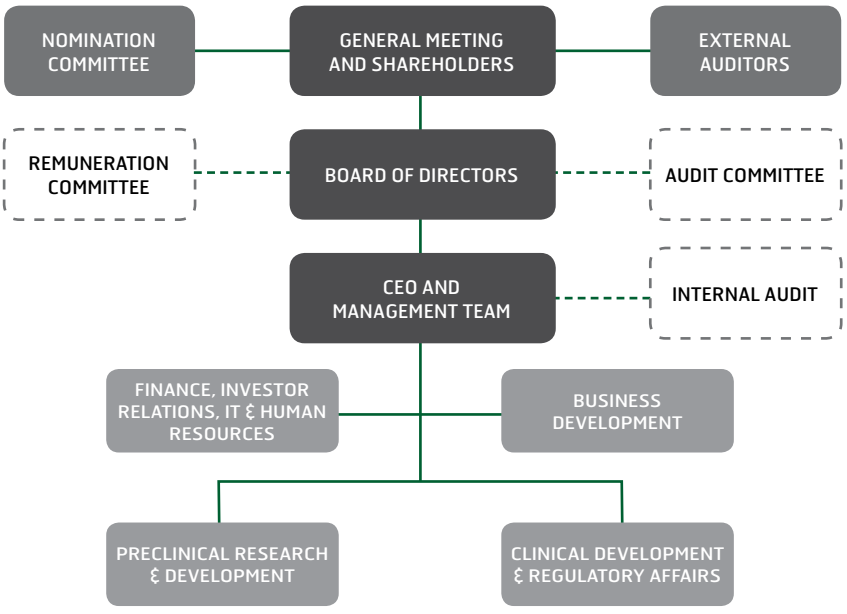
INFORMATION REGARDING OUTSTANDING SHARES IN KARO BIO

At December 31, 2013, the company had a total of 495,947,369 shares with a par value of SEK 0.02. Each share carries entitlement to one vote and carries the same right to share in the company's assets and profits.

The 2013 Annual General Meeting authorized the Board until the next AGM, to issue new shares under an agreement for an Equity Credit Facility (ECF), which gave the company a right, but not an obligation, to issue shares to Azimuth Opportunity Ltd. The agreement assumed that the stock price was higher than it was in 2013. The ability to use the credit facility expired in the fourth quarter.

KARO BIO'S CORPORATE GOVERNANCE MODEL

The chart below illustrates Karo Bio's corporate governance model and the manner in which the central bodies interact.



Important external and internal rules, regulations and policies affecting corporate governance:

Important internal rules, regulations and policies:

- Articles of Association
- The Board of Directors' work procedure
- Instructions for the President including instructions regarding financial reporting
- Instructions to the respective Board committees
- Information policy
- Insider policy
- Financial policy
- Risk management policy
- Financial manual
- Code of Conduct and provisions regarding business ethics

Important external rules and regulations:

- Swedish Companies Act
- Swedish Book-keeping Act
- Swedish Annual Accounts Act
- NASDAQ OMX Stockholm's Rule Book for Issuers
- Swedish Code of Corporate Governance

GENERAL MEETING OF THE SHAREHOLDERS

The highest decision-making body is the general meeting of shareholders, where the shareholders exercise their influence in the company. Shareholders wishing to participate in the general meeting of shareholders, either in person or via a representative, must have their names entered in the shareholders' register maintained by Euroclear Sweden AB no later than five weekdays before the general meeting and must report their intention to attend to the company in accordance with the notice.

Notice of a general meeting of shareholders is given via notices in the press and via the company website (www.karobio.com). The annual general meeting shall be held within six months from the end of the financial year. At the annual general meeting, the shareholders vote on proposed resolutions regarding such matters as the election of the members of the Board of Directors and, where appropriate, the auditors, the manner of appointment of the Nomination Committee and discharge from responsibility for the members of the Board of Directors and President for the last year.

Resolutions are also adopted regarding the preparation of the financial statements, the allocation of profit or treatment of loss, the fees for the Board of Directors and auditors and guidelines for remuneration to the President and other members of executive management.

2013 ANNUAL GENERAL MEETING

The Board gave the Annual General Meeting an account of their work during the year and on corporate governance issues in general. The President informed the AGM about the group's development and position and commented on the results for 2012.

The AGM approved the financial statements for 2012, decided on the handling of the Company loss and discharged the members of the Board from liability. The AGM decided that no dividend would be paid.

The Nomination Committee's Chairman informed on the work during the year and reported the reasons for the suggested proposals. In accordance with the proposal, Göran Wessman was elected as Chairman and Christer Fåhraeus, Per-Anders Johansson, Sibylle Lenz (new election) and Anders Waas were elected as Board Members. The AGM resolved on the election of auditor and remuneration to the Board and auditor in accordance with the Nomination Committee's proposal.

The minutes of the Meeting held on May 7, 2013 is available at Karo Bio's website (www.karobio.com).

NOMINATION COMMITTEE

The AGM 2013 resolved on the principles to be applied for the Nomination Committee. The Chairman of the Board shall ensure that, by the end of the third quarter each year, the company's five largest shareholders or shareholder groups in votes are offered to appoint one representative to the Nomination Committee. Where one or more shareholders decline to appoint a member of the Nomination Committee, the next shareholder in turn based on ownership will be contacted with a mandate to appoint a member to the committee.

The Chairman is the convener of the Nomination Committee. If a member leaves the Nomination Committee before the work is completed, the Nomination Committee shall, if it deems it necessary, invite the same shareholder or, if it is no longer one of the major shareholders, the next shareholders in terms of size to appoint a replacement. A change of this kind shall be announced on the company's website.

The Nomination Committee shall prepare proposals for resolution as regards to the election of the chairman for the meeting, the number of board members and deputies, fees for to Board of Directors and auditor, the election of Board Chairman and other Board Members to the Board of Directors and auditors.

The term of office for the Nomination Committee runs until the new committee is appointed. The Nomination Committee shall not receive remuneration but to the extent it considers necessary, have the right to contract other resources such as external consultants as part of their assignment at the company's expense, and to a reasonable extent. The AGM 2013 decided that the principles adopted for the Nomination Committee should apply until changed.

The Nomination Committee ahead of the AGM 2014 consists of Lars Magnusson, Per-Anders Johansson, Jan Lundström and Göran Wessman.

EXTERNAL AUDITORS

According to the Articles of Association, Karo Bio shall engage a registered public accounting firm as external auditor. At the 2013 AGM, the registered public accounting firm Pricewaterhouse-Coopers AB was re-elected as auditor until the AGM 2014. Since the 2008 annual general meeting, auditor in charge has been Authorized Public Accountant Håkan Malmström, who is also auditor in charge of the companies NCC AB, Nordstjernan AB, Axel Johnson AB and Saab AB.

The auditors review the accounting records and administration of the Parent Company and the Group on behalf of the annual general meeting. The external audit of the accounting records of the Parent Company and the Group and the administration of the Board of Directors and the President is performed according to generally accepted auditing standards in Sweden. The Company's auditor in charge participates in some of the Board's Audit Committee meetings. The auditor participates in at least one Board meeting per year to review the year's audit and to have a discussion with the Members of the Board without the presence of the President.

The company has entrusted the auditor to review one of the interim reports for 2013 in accordance with the Code's statues. Information regarding the auditors' fee is included in Note 26 in the 2013 annual report.

THE BOARD OF DIRECTORS

The Board of Directors has the overall task of administering the company's affairs on behalf of the shareholders in the best possible manner. The Board shall continuously assess the Group's operations, development and financial situation, as well as assessing its operative management. Among its other work, the Board

Board of Directors


GÖRAN WESSMAN


CHRISTER FÅHRAEUS


PER-ANDERS JOHANSSON


SIBYLLE LENZ


ANDERS WAAS

BOARD MEMBERS

GÖRAN WESSMAN (1948)
Elected in 2011, Chairman since 2011.

Education: Biomedicine and Chemistry at Uppsala and Gothenburg Universities.

Primary experience: Leading positions in Nobel Pharma, business development consultant. Founder of Protem Wessman Boule Diagnostics and Carmel Pharma. Former CEO of the Holding company at the Gothenburg University, A+ Science Holding and as Chairman of the Board of SCRI and Isconova.

Other assignments: CEO and board member of Mintage Scientific, Chairman of I-Tech, Vicore Pharma and Protem Wessman.

Number of shares in Karo Bio: 3,999,999

CHRISTER FÅHRAEUS (1965)

Elected in 2011

Education: M.Sc. Bioengineering (UCSD), B.Sc. Mathematics, Ph.D. (hc) Lund University. Three years of medical studies and four years of Ph.D. studies in Neurophysiology.

Primary experience: Innovator and entrepreneur. CEO and Board member in several development and listed companies within medtech, IT and pharmaceuticals. Founder of Anoto Group AB, Precise Biometrics AB, CellaVision AB, Respiratorius AB and Agellis Group AB.

Other assignments: CEO of EQL Pharma AB. Chairman of Agellis Group AB, Respiratorius AB and Flatfrog Laboratories AB. Board member of EQL Pharma AB, Lund University's development company (LUAB), Fårö Capital AB and CellaVision AB.

Number of shares in Karo Bio: 0

PER-ANDERS JOHANSSON (1954)

Elected in 2012

Education:

Primary experience: Founder of the engineering company CIMON, CFO and Vice President of Ellos, Nordico and Karlshamns Group.

Other assignments: CEI and chairman of CIMON AB. Chairman of Sparbanken Karlshamn.

Number of shares in Karo Bio: 19,333,333

SIBYLLE LENZ (1961)

Elected in 2013

Education: PhD in Medicinal Chemistry from the Faculty of Pharmacy at Copenhagen University.

Primary experience: Vice President, Corporate Business Development at Dako A/S, senior positions within both research & development and commercial areas in H. Lundbeck A/S.

Other assignments: CEO Alligator Bioscience AB.

Number of shares in Karo Bio: 0

ANDERS WAAS (1957)

Elected in 2011

Education: Dentist

Primary experience: CEO in pharmaceutical, medical device and biotech industry as well as senior positions within product development, business development and commercialization at Astra/Astra Zeneca, Ciba Geigy, WL GORE & Associates, CV Therapeutics, and Actogenicss.

Other assignments: MIVAC Development AB, Anders Waas AB and the Law Agency Louise Katsler Waas AB.

Number of shares in Karo Bio: 0

BOARD MEMBERS – EMPLOYEE REPRESENTATIVES

BO CARLSSON (1958)

Employee representative since 1997

Education: Specialist teacher exam, Uppsala University.

Primary experience: Employed by Karo Bio since 1997, Project Manager.

Number of shares in Karo Bio: 27,544

JOHNNY SANDBERG (1967)

Employee representative since 2006

Education: Biomedical analyst, Vårdhögskolan.

Primary experience: Employed by Karo Bio since 1994, Senior Research Investigator.

Number of shares in Karo Bio: 35,000

EVA KOCH (1966)

Employee representative (Deputy) since 2010

Education: Ph.D. in organic chemistry.

Primary experience: Employed by Karo Bio since 1999, Senior Research Scientist.

Number of shares in Karo Bio: 8,666

Executive Managers and Auditors


PER BENGTSSON


MARK FARMERY


HENRIK PALM


MARIA SJÖBERG


MARIA ÖHLANDER


LARS ÖHMAN

PER BENGTSSON (1954)

President and CEO. Employed 2011.

Education: M.D. Ph.D. (Cell Biology).

Primary experience: CEO of Probi AB (publ), R&D Manager Pharmacia/Pharmacia Upjohn Plasma Products, Medical Manager and Therapeutic Manager at Ferring and Development Manager at Bionor Immuno A/S.

Other assignments: Board member for Pharmavizer AB.

Number of shares in Karo Bio: 333,333

MARK FARMERY (1969)

Head of Business Development from February 2014. Employed 2014.

Education: PhD in Biochemistry at the University of Leeds.

Primary experience: Business development in AstraZeneca and research positions at the universities of Gothenburg, Leeds and Manchester.

Number of shares in Karo Bio: 0

HENRIK PALM (1958)

Chief Financial Officer. Employed 2011.

Education: Bachelor of Business Administration, University of Gothenburg.

Previous experience: Business controller within the Ericsson group (1982-2000), CFO Elektronik Gruppen BK AB (publ) (2000-2009) and CFO Feelgood Svenska AB (publ) (2009-2010).

Other assignments: Chairman Dispio AB.

Number of shares in Karo Bio: 100,000

MARIA SJÖBERG (1964)

Vice President, Chief Scientific Officer, Preclinical R&D. Employed 2011.

Education: Ph.D., Associate Professor

Previous experience: R&D/Production Director SentoClone AB, Senior Scientist Astra Zeneca Biotech, Section Head/ Project Leader Karo Bio AB, Group Leader Karolinska Institutet.

Number of shares in Karo Bio: 45,000

MARIA ÖHLANDER (1968)

Vice President Clinical Development. Employed since 2007.

Education: M Sc in Biology.

Primary experience: Clinical Research Manager Pharmacia & Upjohn, Clinical Project Manager and Study Delivery Director AstraZeneca, Director Clinical Operations and Principal Project Manager Karo Bio AB.

Number of shares in Karo Bio: 13,554

LARS ÖHMAN (1957)

Vice President Business Development until February 2014. Employed 1989, active as a consultant since 2012.

Education: MBA Stockholm School of Economics. Chemical Engineering, Royal Institute of Technology.

Previous experience: Project leader and manager within Karo Bio's research- and development organization.

Number of shares in Karo Bio: 38,213

AUDITORS

Auditors are elected by the Annual General Meeting for a term of one year. The auditors review the company's accounting and management on behalf of the AGM.

PricewaterhouseCoopers AB were elected auditors at the AGM in June 2013 for the period until the end of the AGM in 2014. Auditor-in-charge is since April 2008 authorized public accountant Håkan Malmström.

RTHE REPORT PERIOD CONCERNS JANUARY 1 – DECEMBER 31, 2013			ATTENDENCE RATE [1]		INDEPENDENT	
BOARD MEMBER	Elected	Total annual fee, KSEK	Ordinary Board Meetings	Extraordinary Board meetings	In relation to the Company and executive management	In relation to the Company's major shareholders
Elected by the general meeting						
Göran Wessman (Chairman)	2011	420	10 (10)	2 (2)	Yes	Yes
Per Bengtsson [2) 4)]	2011	0	3 (3)	0 (0)	No	Yes
Christer Fåhraeus	2011	150	9 (10)	2 (2)	Yes	Yes
Per-Anders johansson	2012	150	10 (10)	2 (2)	Yes	Yes
Anders Waas	2012	150	10 (10)	2 (2)	Yes	Yes
Sibylle Lenz [3)]	2013	112	6 (7)	2 (2)	Yes	Yes
Employee representatives						
Bo Carlsson [2)]	1997	0	10 (10)	2(2)	No	Yes
Johnny Sandberg [2)]	2006	0	9 (10)	2 (2)	No	Yes
Eva Koch, suppleant [2)]	2010	0	9 (10)	2 (2)	No	Yes

1) The figures in parentheses indicate the number of meetings held during each member's mandate period
2) Employed by Karo Bio AB
3) Elected at the annual general meeting 2013
4) Left assignment at the annual general meeting 2013

determines issues concerning the Group's strategic direction and organization, business plans, financial plans and budget, and also makes decisions regarding important agreements, major investments and commitments, in addition to financial, information and insider and risk management policies.

The Board of Directors works according to a work procedure which is determined annually and which regulates the frequency and agenda of Board meetings, the distribution of material for meetings and matters to be presented to the Board as information or for resolution. The working procedure further regulates the manner in which the tasks of the Board are divided between the members of the Board and any Board committees. The Board has also approved instructions for the President, which regulate the division of duties between the Board of Directors, the Chairman of the Board, and the President, as well as defining the authorities of the President.

The Chairman of the Board plans the Board meetings together with the President. In advance of each Board meeting, the Directors receive a written agenda and adequate supporting documents. At each regular Board meeting, a review of operations is conducted, which includes developments and progress within research and development, business development, the Group's operating results and financial position, financial reporting and forecasts.

The Chairman leads the work of the Board of Directors, represents the company in ownership issues, and is responsible for the assessment of the Board of Directors' work. In addition, the Chairman is responsible for on-going interaction with management and for monitoring that the Board fulfills its duties. According to the Articles of Association, the Board shall consist of a minimum of five and a maximum of nine members, elected by the general meeting of shareholders, with no deputy members. The Board is competent to make decisions when more than half of the total numbers of Directors are present.

THE WORK OF THE BOARD OF DIRECTORS IN 2013

In 2013, ten regular meetings and two extra board meetings have been held. At all of these meetings, the Board of Directors has been competent to make decisions. Secretary to the Board in 2012 was solicitor Madeleine Rydberger. Resolutions are taken by the Board after an open discussion, led by the Chairman.

Major matters dealt with in 2013 have included the extension of the agreement with Pfizer regarding RORgamma, collaboration with 4D Science and Dr Jörg Distler, research operations, business development and financing. The Board continuously evaluates the company's performance and development.

Board Committees

The Board has, based on its size and composition, resolved that the respective tasks of the Compensation Committee and the Audit Committee are best conducted by the Board in its entirety, and that no preparatory committees should be appointed, which is a deviation from the Code rule that the Board should form a remuneration committee. The Board in its entirety thus attends to the matters designated for preparatory Compensation and Audit Committees according to the Companies Act and the Code.

Compensation Committee

The Compensation Committee's responsibilities are discharged by the full Board. The work is governed by instructions determined annually by the Board of Directors, and included in the work procedures for the Board. These include submitting proposals for guidelines for remuneration to senior executives, proposals to the Board on the wages of the Managing Directors and other terms of employment, set wages and employment terms for other members of the executive management and developed proposals for incentive programs and other forms of bonuses or similar compensation to employees.

At the AGM, the Board proposes guidelines for determining salaries and other compensation for the CEO and other senior executives, for approval by the shareholders. At the 2013 AGM it was decided that the remuneration of CEO and other senior executives in addition to fixed salary can be rewarded variable remuneration up to a maximum of 40 per cent of the fixed remuneration to reward the achievement of set goals within simple and transparent structures. The total remuneration shall be market sound and competitive.

For further description of the employment terms for the Board and senior executives, see the administration report and note 2 in the financial statements for 2013.

Audit Committee

The Board as a whole fulfills the tasks of the Audit Committee. The tasks follows from instructions set annually by the Board and contained in the Board's rules. These include supporting the Board in efforts to monitor and ensure the quality of financial reporting and the effectiveness of the Company's internal control and risk management. The Board meets the Company's auditors, evaluating audit work, the auditors' independence and approved the supplementary services company may procure from external auditors.

PRESIDENT AND EXECUTIVE MANAGEMENT TEAM

The Board of Directors appoints the President to lead the company. The President is responsible for the current administration of the company in accordance with the directions and guidelines issued by the Board of Directors.

The executive management team consists of four individuals in addition to the President; the Chief Financial Officer, the Vice President Business Development and the Heads of preclinical and clinical development. The executive management team holds monthly meetings to discuss the Group's result of operations and financial position, the status of research and development projects, strategic issues and the monitoring of budget and forecasts.

The President leads the work of the executive management team, which together makes decisions for later implementation in the organization, based on the strategy and corporate goals determined by the Board of Directors. Each member of the executive management team ensures that decisions are implemented in his or her respective area of responsibility and follows up this implementation.

The executive management is responsible for formulating proposals regarding the Group's overall strategies and for implementing these, as well as dealing with matters such as acquisitions and divestments.

INTERNAL CONTROL AND RISK MANAGEMENT REGARDING FINANCIAL REPORTING

Introduction

The Board of Directors and the President are responsible for internal control, as stipulated in the Swedish Companies Act. The responsibility of the Board is also stipulated in the Code.

The Annual Reports Act includes requirements regarding the provision of information to external parties about the company's system for internal control and risk management regarding the financial reporting.

Karo Bio's processes for internal control regarding the financial reporting are designed to provide, with reasonable security, quality and correctness in the reporting. The process is designed to ensure that the reporting is prepared in accordance with applicable laws and regulations as well as requirements for listed companies in Sweden. One premise to achieving this is that there is a satisfactory control environment, reliable risk assessments are conducted, the existence of established control structures and control activities and that information, communication, as well as follow-up, all function in a satisfactory manner.

Internal audit

The Board of Directors has assessed the need for an internal audit function, and has concluded that no such function can be justified in Karo Bio at present, with consideration of the scope of operations and the fact that the Board of Directors' follow-up of internal control is deemed to be sufficient to ensure the effectiveness of internal control. The Board of Directors will reassess the need for an internal audit function when any changes arise that may cause reassessment, although at least once per year.

The Control Environment

The internal control is based on Karo Bio's control environment, which includes the values and the ethics which the Board, the Audit Committee, the President, executive management and other employees communicate and on which they base their actions.

The control environment is also defined by the company's organizational structure, leadership, decision-making process, authorities, responsibilities and employees' competence.

Risk Assessment

At least once a year, a review is undertaken to identify and evaluate Karo Bio's risk profile. This work also involves the assessment of the preventive measures which are to be undertaken to reduce and prevent risks in the Group. This work includes ensuring that the Group is sufficiently insured and also includes the preparation of decision-making documentation as regards to any possible changes in policies, guidelines and insurance coverage.

Karo Bio's system for identifying, reporting and addressing risks is an integrated part of the on-going reporting to the management team and the Board of Directors and forms a key foundation for the assessment of risks in terms of errors in the financial reporting. As part of the process, items in the income statement and balance sheet where the risk of significant error is greater are identified. For Karo Bio, accrued project costs within the company's clinical projects comprise, at various points in time, significant amounts, the size of which is based to a large extent, on management's assessments of the degree of completion. Cash, cash equivalents and other short term investments account for a substantial part of Karo Bio's total assets and are thus a potential source of risk in the financial reporting. Furthermore, the fact that Karo Bio's administration is handled by a small number of individuals has been noted as a risk, as the dependence on a few key individuals is significant and the possibilities of separation between duties and responsibilities are limited. Special importance has, therefore, been placed on designing controls to prevent and identify weaknesses in these areas.

Control Structure

A clear specification of roles and responsibilities is stipulated in the Board's work procedures and in the instructions for the President and the Board Committees, respectively. The Board of Directors has the overall responsibility for internal control.

The President is responsible for the system of procedures, processes and controls which have been developed for the ongoing operations. These include guidelines and role descriptions for the various officers of Karo Bio and for the regular reporting to the Board. Policies, processes, procedures, instructions and standard formats for the financial reporting and the on-going work with the financial administration and financial issues are documented in Karo Bio's Finance manual.

Procedures and activities have been designed to handle and address significant risks which are related to the financial reporting and which are identified in the risk analysis. In addition to the Finance manual, the most significant, overall group-wise governance documents are the finance policy, information policy, insider policy, and the risk management policy.

Control Activities

The major goal of the control activities is to prevent and, at an early stage, identify errors in the financial reporting so that these can be addressed and corrected. There are control activities both at the overall and more detailed levels and these are both manual and automated in nature.

Authorization in the IT system is limited according to the established authorizations and specified responsibilities.

The finance function compiles monthly financial reports in which results and cash flows for the former period are reported and in which budget deviations are analyzed and commented. Follow-up is conducted via regular meetings which review and analyze these reports, together with the line managers and project managers. In this manner, significant fluctuations and deviations are followed which minimizes the risk of error in the financial reporting.

The closing of the books and annual financial statement work involves processes which add further risks for errors in the financial reporting. This work is of a less repetitive nature and includes a number of instances characterized by assessment. Important control activities includes securing that there is a well-functioning reporting structure in which the line managers and project managers report according to standardized reporting formats, and that important income statement and balance sheet items are specified and commented.

Information and Communication

The company's information-oriented operations are regulated by an information policy. For external communication, there are guidelines which aim to ensure that live up to the high standards for correct information to the market. Karo Bio's communication shall be correct, transparent, timely and on a fair and equal basis with all interested parties.

All communication shall be conducted in accordance with NASDAQ OMX Stockholm's Rule Book for Issuers. The financial information shall provide a comprehensive and clear view of the company, its operations, strategy and financial development. The Board of Directors adopts the annual reports, financial statements and interim reports. All reports are published on the website (www.karobio.com) after having been published in accordance with stock exchange regulations. The annual report is distributed via the company website, and is made available in print to parties on request.

For internal communication purposes, Karo Bio has established an intranet, where internal information items, policies and guidelines are available for all employees. In addition company-wide information meetings are held.

Follow-up

The Board's review of internal control regarding financial reporting is conducted by, among other things, reviewing the work and reports of the Chief Financial Officer and the external auditors. This work includes ensuring that measures have been taken regarding any deficiencies and also includes presenting proposals for measures which have been produced in the context of the external audit. The review is conducted with a focus on the manner in which Karo Bio complies with its framework and on the basis of the existence of efficient and goal-oriented processes for risk management, operational management and internal control.

The external auditors review, on an annual basis, selected parts of the internal control within the framework of the statutory audit. The auditor's report the outcome of the review to the Board of Directors and the executive management. Significant observations are reported, as applicable, directly to the Board of Directors. In 2012, as part of the audit of accounts, the external auditors have reviewed the internal control of select key processes and have reported on these to the Audit Committee, the Board of Directors and the executive management.

AUDITOR'S OPINION ON THE CORPORATE GOVERNANCE STATEMENT

To the annual meeting of the shareholders in Karo Bio AB (publ), corporate identity number 556309-3359

It is the board of directors who is responsible for the corporate governance statement for the year 2013 on pages 42-48 and that it has been prepared in accordance with the Annual Accounts Act.

As a basis for our statement that the corporate governance report has been prepared and is consistent with the annual report and group financial reporting, we have read the corporate governance report and reviewed its statutory content based on our knowledge of the company.

In our opinion, the corporate governance statement has been prepared and its statutory content is consistent with the Annual Accounts Act and the consolidated account reports.

Stockholm on 14 March 2014
PricewaterhouseCoopers AB

Håkan Malmström
Certified Public Accountant

Glossary

AGONIST A compound that has an activating effect.

ANTAGONIST A compound that has inhibiting/blocking effect, i.e. has a reverse effect compared to the agonist.

AXON is a projection from one nerve cell leading electrical impulses to other nerve cells or effector (muscle, glands). Axon ends with a synapse where a neurotransmitter substance is released as a result of the impulse.

CD Candidate Drug. A compound, which has desired effects in relevant animal models and which therefore is further developed towards clinical development.

CLINICAL STUDY Testing and evaluation of pharmaceuticals in humans

CNS Central nervous system.

EMA (European Medicines Agency), European drug agency.

ER The receptor for estrogen hormone.

ER-BETA A form of the estrogen receptor, the discovery of which can lead to new treatment principles in women's health care, depression, certain forms of cancer with several disease areas.

ESTROGEN Female sex hormone.

FDA (Food and Drug Administration), the U.S. drug authority.

GLUCOCORTICOID The hormone that is the natural ligand to the glucocorticoid receptor and is produced in the adrenal cortex, and thus also referred to as adrenocortical hormone. The hormone regulates the body's use of carbohydrates, fat and protein and is a normal response to stress. Compounds that activate the receptor are called glucocorticoids.

GR The receptor for glucocorticoid.

HORMONE Compound secreted from an endocrine gland that is transmitted by the blood to the tissue on which it has a specific effect.

IND (Investigational New Drug) Registration of a substance before the start of clinical trials.

INDICATION In medical terminology a term for a disease or patient category.

LIGAND A substance, such a hormone, that binds with a receptor protein

LIVER SELECTIVE A compound that preferentially acts in the liver

MYELIN Surrounds the outgrowth from nerve cells called axons through which the contact between nerve cells takes place. Myelin has an insulating capability meaning that nerve impulses can propagate faster.

NUCLEAR RECEPTORS Receptors inside a cell that bind to ligands (often hormones) and regulate gene expression.

PHARMACOKINETICS Studies of process time for the uptake, distribution and elimination of a drug in the body.

PHASE I A first clinical study phase where the compound is given as a single dose to healthy volunteers with the primary objective to study safety and pharmacokinetics on a candidate drug.

PHASE IIa First clinical studies in chosen patient category for which the drug is evaluated.

PHASE IIb Extended trials on patients where the primary objective is to find a dose to secure effect and safety before Phase III studies.

PHASE III Clinical studies conducted with a large patient population for which the drug is developed. The primary objective is to assure safety and confirm effect in a large database of a selected patient category under long time treatment. The aim with this part of clinical development is to assure that the launched product is safe for the chosen patient category in clinical practice.

PRECLINICAL DEVELOPMENT Development until permission is granted to test a compound on human beings.

PROOF-OF-CONCEPT Proof for intended effect of a drug in patients.

PROOF-OF-PRINCIPLE Proof that a treatment principle has the intended effect on patients.

RECEPTOR A protein on the cell surface or inside the cell (nuclear receptor) that recognizes and binds to ligands such as steroid hormones. Receptors start or stop biological processes when they bind to ligands.

RORGAMMA Research shows that the nuclear receptor RORgamma may have an important role in the development of autoimmune diseases.

THERAPY Disease treatment method.

TISSUE A collection of cells specialized to perform a particular function. The cells may be of the same type or of different types. Aggregates of tissue constitute organs.

TR A nuclear receptor that is activated by thyroid hormone.

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