LEO FOUNDATION

Annual Report 2018

Supporting advances in dermatology

In the LEO Foundation, we take a long-term view on creating value and impact through active ownership, philanthropic activities and investments.

Contents

About LEO Foundation

The LEO Foundation is one of Denmark's largest commercial foundations. Established in 1984, our main objective is to ensure the long-term independence and success of the global, research-based pharmaceutical company LEO Pharma. The LEO Foundation is the sole shareholder of LEO Pharma and is independent of heirs, outside shareholders and other interests.

The LEO Foundation also provides philanthropic grants to some of the world's leading scientists within skin research, combating the impact of skin diseases. Our mission is to support the best international research in skin diseases and make Denmark a global beacon for skin research.

In addition to the ownership of LEO Pharma, the LEO Foundation owns financial assets of around DKK 18 billion. The main objectives of the investments are to provide the capability to support LEO Pharma's long-term continuance and strategic development as well as providing funds for the Foundation's philanthropic activities.

The LEO Foundation organisation is made up of a small and dedicated team of specialists:
Charlotte Malassé (Communication Specialist), Ida Brams (Chief Grant Officer), Charlotte Thers (Administration), Maximilian Bergenhem (Student Assistant), Morten Stampe Christensen (Chief Investment Officer) and Lars Kruse (Scientific Officer).

About LEO Group

The LEO Group consists of the LEO Foundation, LEO Holding A/S and LEO Pharma A/S, including its Danish and international subsidiaries (collectively LEO Pharma Group).

LEO Group legal structure

LEO Foundation

2018 grants
In 2018, the LEO Foundation gave out grants and awards with a total value of DKK 300 million. The total amount was awarded as one strategic grant, 17 open competition grants, three education & awareness grants and two awards.

LEO Holding A/S

Total assets
The LEO Foundation's assets consist of its ultimate sole ownership of LEO Pharma, with a book value of DKK 9.5 billion and financial assets valued at DKK 17.8 billion.

LEO Pharma Group

About LEO Pharma
LEO Pharma develops, manufactures and markets pharmaceutical drugs for dermatology in more than 130 countries. In 2018, LEO Pharma had revenue of DKK 10,410 million, an EBIT of DKK 1,605 million and employed more than 5,500 people worldwide.

(continued):
Mette Poulsen (Finance Manager), Lars Thørs (Senior Investment Director), Peter Kjeldsen Hansen (Director, Legal and Business Development), Arne Mandøe (LEO Historical Archives & Museum), Jesper Mailind (CEO) and Lars Olsen (Chairman, Board of Trustees).

Management review

Moving forward

2018 marked our first year of full operation following the modernisation of the LEO Foundation's governance model in 2017, and we now operate as an independent organisation exerting engaged and active ownership of LEO Pharma while managing our financial assets and developing our philanthropic activities.

At any given time, one in four people around the world are suffering from a skin disease, many of which cannot be adequately treated. Through our active ownership of LEO Pharma and our support to leading international skin research, we strive to help find solutions that will improve the lives of the millions of people suffering from skin diseases.

2018 marked our first year of full operation following the modernisation of the LEO Foundation's governance model in 2017. We now operate as an independent organisation exerting engaged and active ownership of LEO Pharma while managing our financial assets and developing our philanthropic activities.

Over the course of 2018, we reviewed and further developed our strategies, completed the establishment of our business processes and supporting systems, established an active communication profile and arrived at an organisation with all the competences needed to support our current activities.

The aim of our active ownership of LEO Pharma is for the company to develop as a global leader in dermatology, producing outstanding results. In 2018, LEO Pharma took important steps towards this goal by strengthening its pipeline and market platform through partnerships and acquisitions. In addition, existing development projects progressed as planned. A portfolio of non-strategic products was also divested. Even though LEO Pharma faced increased generic competition and price pressure, the company achieved positive results in line with the expectations for 2018.

Pivotal investments in pipeline and infrastructure will continue in the coming years, with the aim of growing LEO Pharma's global market presence.

In the philanthropic area, our aspirations are to support the best international research in skin diseases and make Denmark a global beacon for skin research. While we continue to support research through our open competition grants and LEO Foundation Awards, a significant element of our grant strategy is an increased focus on strategic grants that provide significant long-term funding to activities that promote scientific excellence. The result of this strategy is a step change in our grant level, which will increase towards an annual average of DKK 200 million over the coming years. Towards the end of 2018, we announced a strategic 10-year grant to the LEO Foundation Skin Immunology Research Center at the University of Copenhagen, Denmark. The grant will enable the establishment of a world-class Research Center in the Maersk Tower at the university's Faculty of Health and Medical Sciences. 2018 thus saw substantial growth in the grant level compared with previous years.

The main objectives of our investment activities are to ensure the continued financial capability to support LEO Pharma's long-term continuance and strategic development as well as providing funds for the LEO Foundation's philanthropic activities. In line with these objectives, we focus on generating the best possible returns while retaining a sensible, well-balanced risk profile. The financial markets were characterised by significant volatility in 2018, which resulted in a negative return on our financial assets at year-end.

Over the past two years, we have built a new organisation and developed the strategies that enable us to take the LEO Foundation to the next level. More than ever before, the Foundation stands ready to fulfill its obligations to ensure the long-term independence and success of LEO Pharma and support scientific research.

2018 milestones

- The LEO Foundation's strategies for active ownership, philanthropy and investments were reviewed and further developed.
- The LEO Foundation completed building processes and business systems, and established an active communication profile.
- The LEO Foundation expanded its organisation with expertise in the communications area and with further competences in the investment area.
- The LEO Foundation Awards were presented to two leading young researchers at the IID congress in Orlando, US.
- The LEO Foundation announced its largest commitment ever – a 10-year grant to the LEO Foundation Skin Immunology Research Center at the University of Copenhagen.

Our vision is for LEO Pharma to develop as a global leader in dermatology, delivering outstanding results.

Jesper Mailind, CEO

Lars Olsen, Chairman of the Board of Trustees

LEO Pharma

A strong position in medical dermatology

With the clear goal to be the leading company in medical dermatology in 2025, LEO Pharma made significant R&D investments and acquired a large portfolio of established products in 2018. The financial results were in line with the expectations for the year.

Laying the groundwork for future growth
LEO Pharma has set itself the goal to be the leading company in medical dermatology in 2025. The company's 2025 strategy is based on strengthening its portfolio of established products while also bringing new and innovative treatments to the market. The strategy will require substantial investments over the coming years, not least in R&D and product launches. The LEO Foundation's main objective is to ensure the long-term success of LEO Pharma, and the Foundation thus fully supports the strategy, which will lay the groundwork for the company's future growth and profitability.

Good results in line with expectations
Following a record year in 2017, LEO Pharma's 2018 results were in line with expectations. LEO Pharma made significant R&D investments and acquired a large portfolio of established products. To help fund the investments in the innovative portfolio, LEO Pharma continues to implement cost savings to improve the EBITDA margin.

Focusing the business
In 2018, LEO Pharma made a significant shift in its topical derma product portfolio to increase profitability. This was achieved through the divestment of the company's non-strategic portfolio to Swedish company Karo Pharma AB in April 2018, leading to a significantly reduced number of stock-keeping units, simplified manufacturing and improved gross profit margins. In addition, LEO Pharma acquired Bayer's prescription dermatology unit to gain scale in specific markets in Europe, Asia and Latin America, and add sales to the existing organisation with only a marginal increase in costs. The acquisition was closed in the US in September 2018, with expected closing in all other countries in July 2019, subject to the fulfilment of customary closing conditions.

Revenue
Revenue for 2018 decreased slightly to DKK 10,410 million (2017: DKK 10,481 million). Adjusting for the divestment and acquisition, the decrease in organic sales was DKK 187 million. 2018 revenue was impacted by constraints in supply, resulting in delays in the delivery of orders, affecting a range of products.

Revenue by region
Region Europe+ grew by DKK 186 million, or 5% in local currencies, to DKK 4,302 million. Sales were impacted by DKK 397 million due to the divestment to Karo Pharma AB.

Region US declined by DKK 220 million, or 17% in local currencies, to DKK 1,077 million, mainly because the US portfolio operates in a market influenced by strong generic competition, resulting in net pricing pressures. These pressures were partly offset by strong performances from LEO Pharma's key marketed products Enstilar® and Picato®.

The US-based part of the prescription dermatology unit acquired from Bayer was integrated on 4 September 2018. The Bayer portfolio is particularly strong in the rosacea indication area, where total net sales in 2018 were DKK 112 million.

Region International increased by DKK 127 million, or 5% in local currencies, to DKK 2,785 million. The divestment to Karo Pharma AB impacted sales by DKK 74 million.

Operating profit
Operating profit EBIT) increased to DKK 1,605 million (2017: DKK 852 million), mainly driven by the divestment of LEO Pharma's non-strategic derma portfolio to Karo Pharma AB. The divestment resulted in a net gain of DKK 1,566 million, recognised as other operating income.

Sales and distribution costs decreased by DKK 145 million to DKK 3,946 million in 2018 (2017: DKK 4,091 million).

Research and development costs increased by DKK 312 million to DKK 1,914 million (2017: DKK 1,602 million). The increase was mainly due to increased investments in the innovative portfolio.

A strong and expanding pipeline
Increasing investments in R&D to 18% of revenue in 2018 fuelled the progression of the clinical pipeline. In 2018, LEO Pharma initiated the third phase 3 clinical study for tralokinumab, an investigational monoclonal antibody for the treatment of moderate-to-severe atopic dermatitis, and entered phase 2b for delgocitinib for atopic dermatitis and hand eczema. Together with further early-stage projects, including oral treatments, LEO Pharma now has one of the world's strongest pipelines in eczema.

In November, LEO Pharma entered the rare disease arena by concluding a partnership with PellePharm with the aim of developing a treatment for Gorlin syndrome, a rare but severe skin disease for which there are currently no approved therapies.

2019 outlook
For 2019, LEO Pharma expects sales growth primarily from the acquisition of Bayer's prescription dermatology unit, which will have full-year impact in the US and six months' impact in the rest of the world. LEO Pharma anticipates total annual revenue in the range of DKK 10.8-11.0 billion.

LEO Pharma will continue to focus on profitability improvements in its established portfolio and, at the same time, significantly increase spending on research and development activities. Combined with modest growth in sales, LEO Pharma expects this to lead to an operating loss of up to DKK 750 million in 2019.

Elements of uncertainty
Financial expectations are subject to uncertainties and assumptions. This may cause actual results to differ from expectations. The factors that may affect future results include delayed or unsuccessful development projects, market-driven price reductions for products, exposure to product liability and other lawsuits, and changes in reimbursement rules and legislation.

For further information about the LEO Pharma Group, please refer to LEO Pharma's Annual Report.

Investment report

A year of transition and diversification

The main objectives of our investments are to ensure the continued financial capability to support LEO Pharma's long-term continuance and strategic development as well as provide funds for the LEO Foundation's philanthropic activities. In line with these objectives, we strive to generate the best possible returns while retaining a sensible, well-balanced risk profile.

Towards the end of 2017, accumulated reserves of DKK 17.2 billion were transferred from LEO Pharma to the holding company, LEO Holding A/S, which is 100% owned by the LEO Foundation. The transferred financial portfolio had a very low risk – and exposure to only a few asset classes. During H1 2018, the financial portfolio transitioned to a new strategic asset allocation, reflecting the LEO Foundation's long-term investment horizon. This implied higher risk but with due respect for the Foundation's obligations towards LEO Pharma, which is moving into a period of substantial investments in pipeline and infrastructure.

Within equities, Danish equities and emerging market equities were added to the financial portfolio and, within credit, lower-rated credit such as emerging market debt, was added as well. Allocation to alternatives was increased substantially, with commitments to private debt and private equity and investments in three fixed-income hedge funds. Both active and passive mandates were used in the portfolio construction.

A challenging year

2018 was a challenging year on the financial markets – and most asset classes ended the year with negative returns. The markets were hit in three ways. Firstly, central banks continued to move towards tighter monetary policy. With the US Federal Reserve hiking rates four times and the European Central Bank discontinuing its quantitative easing at the end of December 2018 – and almost preannouncing rate hikes in H2 2019. Secondly, global growth levelled off and is expected to fall back to trend level in the coming years – and talk of a coming recession is high on investors' radar. Thirdly, political issues had a big impact, with US President Donald Trump's trade war(s), the Italian budget situation and country-specific issues in emerging markets (China, South Africa, Turkey and Brazil) providing substantial uncertainty and thereby making investors more cautious.

LEO Holding's financial portfolio generated a negative return of DKK 519 million. This corresponds to a return of -3.1%. The return was impacted by the substantial change in portfolio allocation during H1 2018, when – among other things – equities increased from 19% to 40% of the portfolio.

The portfolio saw negative contributions from all of the portfolio's main asset classes – equities, credit, government and mortgage bonds, and alternatives.

Equities contributed DKK -438 million to the portfolio return – and had an asset class return of -7.8%. This was caused by a negative return from developed market equities, but emerging market equities and Danish equities also detracted heavily from the return.

The return from credit was DKK -46 million, corresponding to an asset class return of -1.0%. European corporate bonds had a return of -0.9% (partly impacted by positive active manager performance), while emerging market debt hard and local currency index exposure had returns of -2.1% and -1.7% respectively.

The government and mortgage bond portfolio managed to return 0.7%. This was due to slightly falling yields – and positive manager performance. The passive mortgage portfolio detracted from the return at the beginning of the year, before it was substantially reduced.

Exposure to alternatives was fairly small – and was primarily built up during H2 2018, hence, the effect on the return was limited. Listed real estate was the main reason for the return, with a contribution of DKK -23 million.

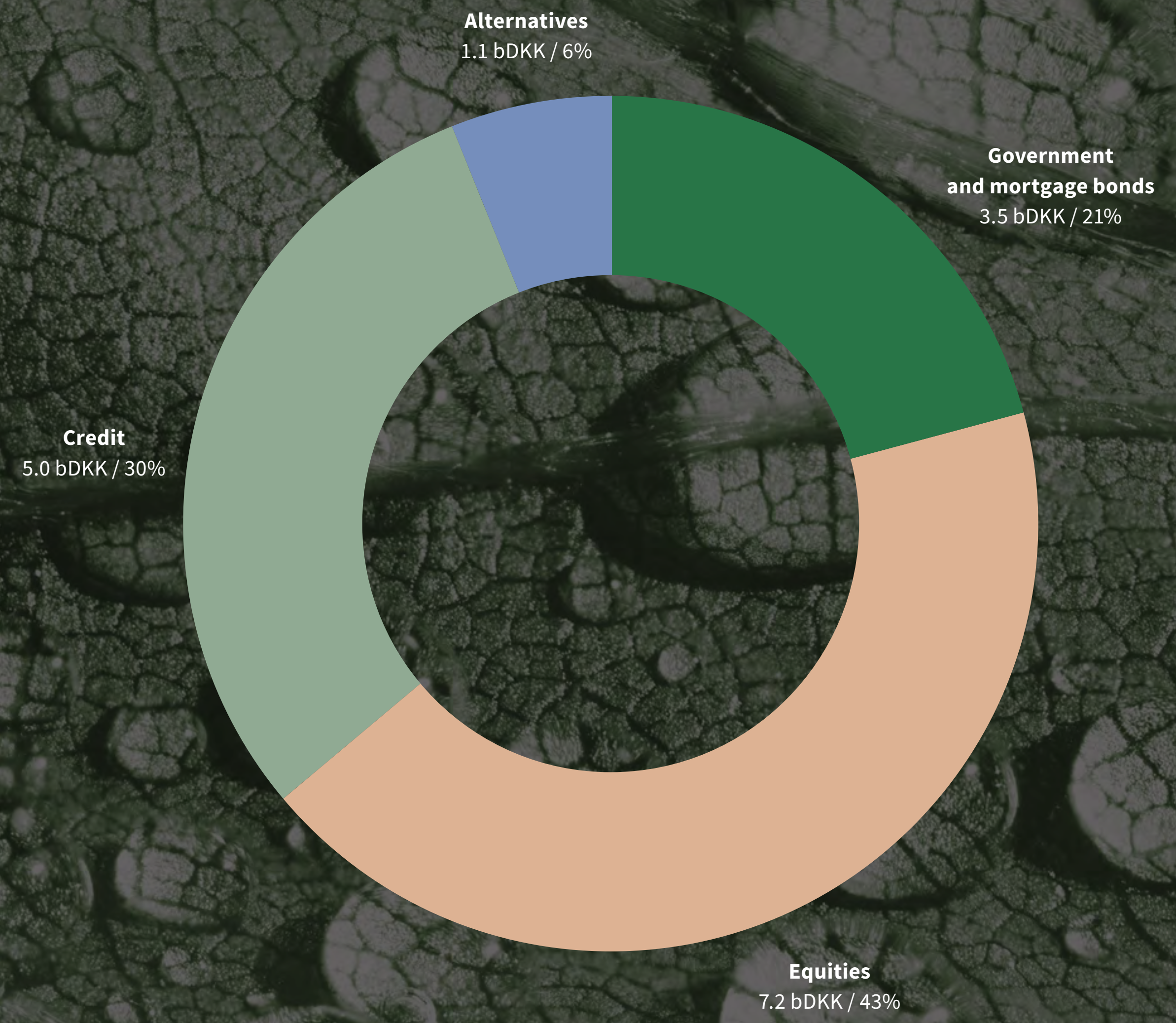
Investment strategy going forward

The return from the financial portfolio is expected to be low – but positive – in 2019, due to the very low yields in the fixed-income markets. Further refinements of the portfolio are expected, with increasing exposure to alternatives substituting low-yielding fixed-income exposure. The risk in the portfolio is expected to be kept at the same level as at the end of 2018 – although with a few more equities and somewhat lower credit exposure. This relatively low risk profile, combined with high liquidity, is expected to be upheld over the coming years while LEO Pharma goes through its current phase of substantial investments in future growth. LEO Pharma will finance part of these investments with external loan capital, and the LEO Foundation expects to participate in this financing.

Investment portfolio

Assets	Market value (DKK million) 31/12 2017	Market value (DKK million) 31/12 2018	Return (%) 2017	Return (%) 2018
Government and mortgage bonds	9,121	3,521	2.9%	0.7%
Equities	3,278	7,210	12.1%	-7.8%
Credit	4,441	4,968	3.4%	-1.0%
Alternatives	327	1,057	10.4%	-3.2%
Total	**17,167**	**16,756**	**4.7%**	**-3.1%**

Investment portfolio value on 31/12 2018: DKK 16.8 billion



Grants and awards

A step change in grant level

Through philanthropic activities, the LEO Foundation aims to support the best international research in skin diseases and make Denmark a global beacon for skin research. In 2018, the LEO Foundation supported dermatological research through grants and awards of DKK 300 million, a significant increase on previous years.

The LEO Foundation provides four types of grants and awards
During 2018, the Foundation developed a new grant strategy and started implementing it. The strategy makes use of four types of grants and awards:

- Strategic grants, which are large, long-term commitments given to support excellent dermatology research within specific areas.
- Open competition grants, which are given to support the best dermatology research projects worldwide.
- Education and awareness grants, which are given to support activities that strengthen the pipeline of future researchers within the fields of medicine, chemistry and pharmacy, and raise awareness about skin, skin diseases and the LEO Foundation.
- LEO Foundation Awards, which are given annually to outstanding young scientists from around the world whose work represents an extraordinary contribution to dermatology research.

The LEO Foundation Board of Trustees approves all grants and awards, and the Foundation has no intellectual property rights to results from our philanthropic activities. However, the Foundation requests that the results are published.

Two large long-term commitments at the University of Copenhagen
In November 2018, the University of Copenhagen announced the establishment of the LEO Foundation Skin Immunology Research Center (SIC), made possible by a strategic grant of up to DKK 400 million over 10 years from the LEO Foundation. This grant represents the LEO Foundation's largest commitment ever and is composed of a base grant of DKK 250 million and expected add-on grants of up to a total of DKK 150 million.[1]

In June 2017, the University of Copenhagen inaugurated the LEO Foundation Center for Cutaneous Drug Delivery (LFCCDD), made possible by a strategic grant of DKK 40 million over 10 years from the LEO Foundation.

In 2018, the LFCCDD continued to build its organisation with new PhD students and postdocs, who will substantially increase the Center's research capabilities, especially within advanced model systems and bacterial experiments. Through additional open competition grants from the LEO Foundation, the LFCCDD has expanded, with new experimental facilities and instruments. Although still in its initial phase, the Center has already made good scientific progress, with 18 scientific publications and presentations at scientific meetings.

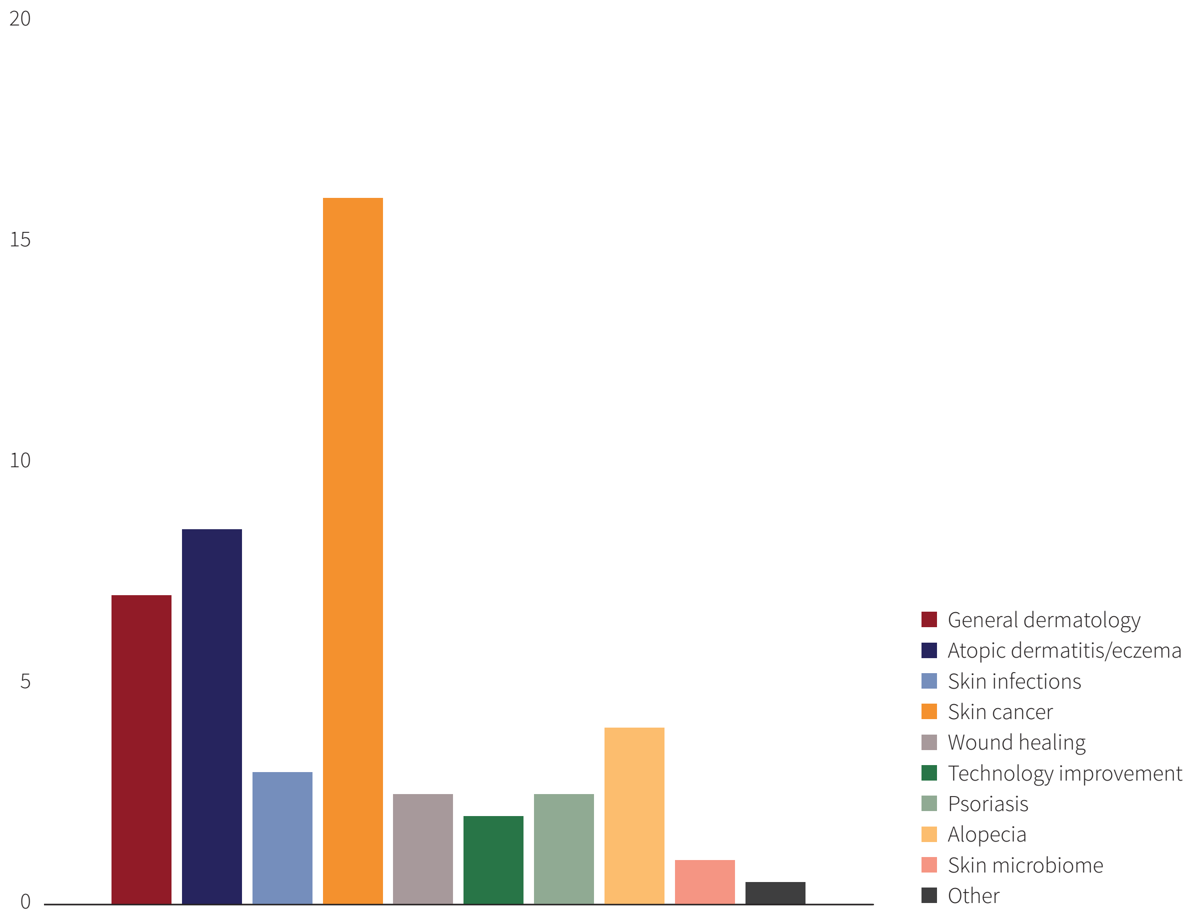
1. Please see feature article on the new Skin Immunology Research Center on page 18.

Grants and awards

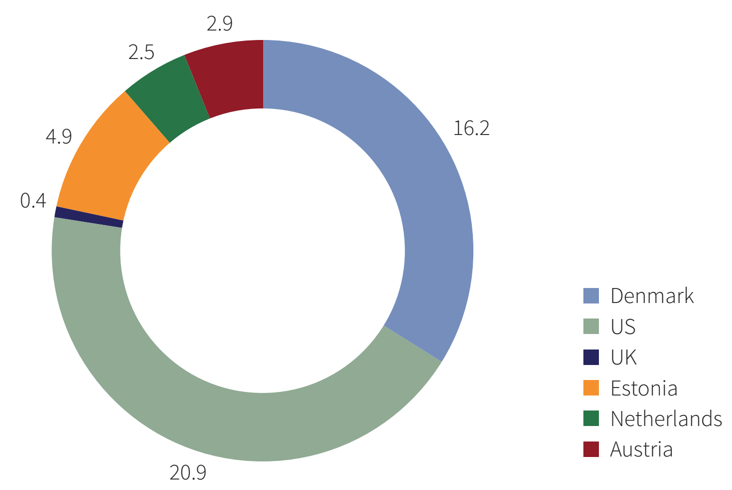
Supporting advances in dermatology

17 grants awarded in open competition
In 2018, 91 applications were evaluated in open competition, and the LEO Foundation Board of Trustees approved 17 grants totalling DKK 47.8 million (ranging from DKK 0.1 to 5.8 million). Researchers from the US and Denmark received 77% of the grant amount, and 66% of the grant amount was given to support research within skin cancer, atopic dermatitis/eczema and general dermatology.

Grant amount (DKK million)/area



Grant amount (DKK million)/country



Studying human cancer in an experimental animal model
One of the researchers who received funding in 2018 was Professor Rudolf Jaenisch, Professor of Biology at Massachusetts Institute of Technology (MIT) and a founding member of Whitehead Institute for Biomedical Research, both in the US. Professor Jaenisch received DKK 2.4 million for his project “In vivo model of human melanoma using a novel crest chimera system”.

Professor Jaenisch is a pioneer of transgenic science, and together with colleague Beatrice Mintz at the Fox Chase Cancer Center in Philadelphia, US, he introduced the first transgenic mice to the world in 1974. A transgenic animal contains one or more genes that have been added from another animal.

Today, mouse models are used in melanoma research to represent human skin cancer disease. These models present two major challenges: 1) the human tumour cells, which are transplanted into the test mice, represent the end stage of the disease and 2) the immune system of the test mice is usually suppressed. Thus, current research models fail to show the development of the disease as well as fail to display the ongoing interaction between melanoma cells and the immune system as the disease progresses.

To address the challenges with the current research models, the team led by Professor Jaenisch has set out to create a new experimental animal model that will reflect a more realistic set-up and make it possible to study initiation, progression and manifestation of human cancers such as melanoma. More specifically, the team plans to add a special type of human cell with cancer mutations to early mouse embryos, and these cells will eventually become an integral part of the skin. This approach will generate a humanised mouse model with an intact immune system, enabling the researchers to gain a detailed understanding of how, over time, the cancer interacts with and ultimately evades the immune responses.

Given a positive outcome, this innovative project could help to improve the effectiveness of current immunotherapies, test novel immunotherapies and identify novel targets in melanoma treatment.

Details about all LEO Foundation grants awarded in open competition can be found on www.leo-foundation.org.

Awarding the extraordinary

Focus on quality, evaluation and results
In 2018, the LEO Foundation continued its efforts to strengthen the scientific evaluation process for all applications. This means that new Scientific Evaluation Committee (SEC) members have been recruited to reflect a wider range of competences and a broader international perspective.

It also means that all applications received in open competition are now evaluated by an independent international Scientific Evaluation Committee, utilising a scoring system adopted from the National Institutes of Health (NIH), US. Following the SEC evaluations, the LEO Foundation Grant Committee prioritises the applications and makes recommendations to the LEO Foundation Board of Trustees.

In order to further strengthen its processes, the Foundation has decided to purchase and implement a suite of electronic grant management systems and tools.

The LEO Foundation is ready for the future and to pursue an impact for all those living with skin diseases and for society.

LEO Foundation Awards in 2018
LEO Foundation Awards are presented annually to outstanding young scientists whose work represents an extraordinary contribution to medical research and whose results advance our understanding of skin diseases and have the potential to pave the way for new and improved treatments for patients.

In 2018, the LEO Foundation engaged in a collaboration with the SID (American Society for Investigative Dermatology), the ESDR (European Society for Dermatological Research) and the JSID (Japanese Society for Investigative Dermatology) to identify global candidates for the LEO Foundation Awards. As a result, the LEO Foundation was able to present its Gold and Silver Awards at the three societies' joint meeting, the IID 2018, which was held in May in Orlando, Florida, US.

Dr Hayato Takahashi, Keio University, Tokyo, Japan, received the LEO Foundation Gold Award of DKK 1 million for his research on T-cell biology with a specific focus on desmoglein-3-specific T-cells, which are involved in the autoimmune blistering disease pemphigus vulgaris.

Pemphigus vulgaris is a rare and serious (potentially life-threatening) chronic condition that causes painful blisters to develop on the skin and lining of the mouth, nose, throat and genitals. The blisters are fragile and can easily burst open, leaving areas of raw unhealed skin that are very painful and can put the patient at risk of infections. There is currently no cure for pemphigus vulgaris. Dr Takahashi's long-term goal is to obtain knowledge that can ultimately lead to effective treatments for autoimmune bullous diseases.

Dr Tiffany Scharschmidt, UCSF, San Francisco, California, US, received the LEO Foundation Silver Award of DKK 500,000 for her research on filaggrin deficiency, the adaptive immune system and the interplay with the skin microbiome. Inflammatory skin disorders are among the most challenging for dermatologists to treat, on account of their persistent nature and the side-effect profiles of current therapies. It is now recognised that skin bacteria have the potential to contribute to inflammation and, in some cases, play a major role in the pathogenesis of many of these disorders. Dr Scharschmidt's long-term goal is to enable the development of new therapies with enhanced efficacy and fewer side effects. This will require a deeper understanding of the cellular and molecular mechanisms underlying the adaptive immune response to skin bacteria, which is needed to better define their role in skin inflammation.

Watch Dr Hayato Takahashi and Dr Tiffany Scharschmidt on www.leo-foundation.org

LEO Foundation Skin Immunology Research Center

New Center for skin research

The LEO Foundation is supporting the establishment of a new Center for skin research at the University of Copenhagen, Denmark, through a grant of up to DKK 400 million. This grant represents the LEO Foundation's largest commitment ever and is composed of a base grant of DKK 250 million and expected add-on grants of up to a total of DKK 150 million, which will be applied for separately.

The LEO Foundation supports the best international research in skin and skin diseases, and the new Center will provide unique opportunities to better understand the skin and its diseases.

The skin is our largest organ, and skin biology and skin diseases comprise a very large field of research, with more than 3,000 skin diseases known today. The skin acts as our shield and ensures our survival by protecting us against the bacteria, viruses and chemical substances that constantly attack our bodies. In other words, our skin can be perceived as an extension of the immune system, and at least 50% of skin diseases can be classified as having an immunological component.

At any point in time, one in every four people will be suffering from a skin disease, which is often visible, stigmatising and, in some cases, completely debilitating. Despite the high prevalence of skin diseases, research in this field remains underprioritised – and much more research on skin and skin diseases is required to provide better diagnoses, treatments and, perhaps even cures.

The aim is for the LEO Foundation Skin Immunology Research Center (or SIC) to be recognised for:

- Practising scientific excellence in skin and skin disease research with an interdisciplinary approach and strong clinical outreach.
- Developing and integrating new technologies, methods and data/omics approaches for skin diseases.
- Creating new stratification paradigms for diagnosis, treatment and prevention in the context of precision medicine.

The Skin Immunology Research Center will be led by Professor Niels Ødum and headquartered on the 12th floor of the new Maersk Tower at the University of Copenhagen. SIC researchers will contribute with basic, translational and clinical research expertise, thus collaboration will be a key driver. They will work closely with leading international researchers at universities and hospitals to provide valuable, effective knowledge-sharing across this major field of research. Having such a Center in one of the world's leading research regions makes it possible to routinely involve specialists within many different areas and create truly innovative breakthroughs.

SIC will also provide the best possible framework for education, training and talent development for students, and will help form future generations of specialists within dermatology. Consequently, the Center will strengthen the pipeline of future expert researchers in skin and skin diseases.

More than 3,000 skin diseases exist, for example:

- Psoriasis
- Vitiligo
- Rosacea
- Epidermolysis bullosa
- Atopic dermatitis
- Actinic keratosis
- Acne vulgaris
- Contact allergy

At least 50% can be classified as having an immunological component.

The Center will focus on inflammatory skin diseases, for example:

- Psoriasis
- Atopic dermatitis
- Contact allergy
- T-cell lymphoma as a model

Skin diseases and comorbidities without (as far as we know) an immunological component as well as cosmetic/aesthetic skin conditions will be outside of the Center's scope.

Key research themes for the Center:

- Skin disease mechanisms
- Patient stratification and precision medicine
- Novel ways to attack and cure skin diseases

Skin Immunology Research Center (SIC)
The LEO Foundation is supporting the establishment of a new Center for skin research at the University of Copenhagen. The new Center will provide unique opportunities to better understand the skin and its diseases.

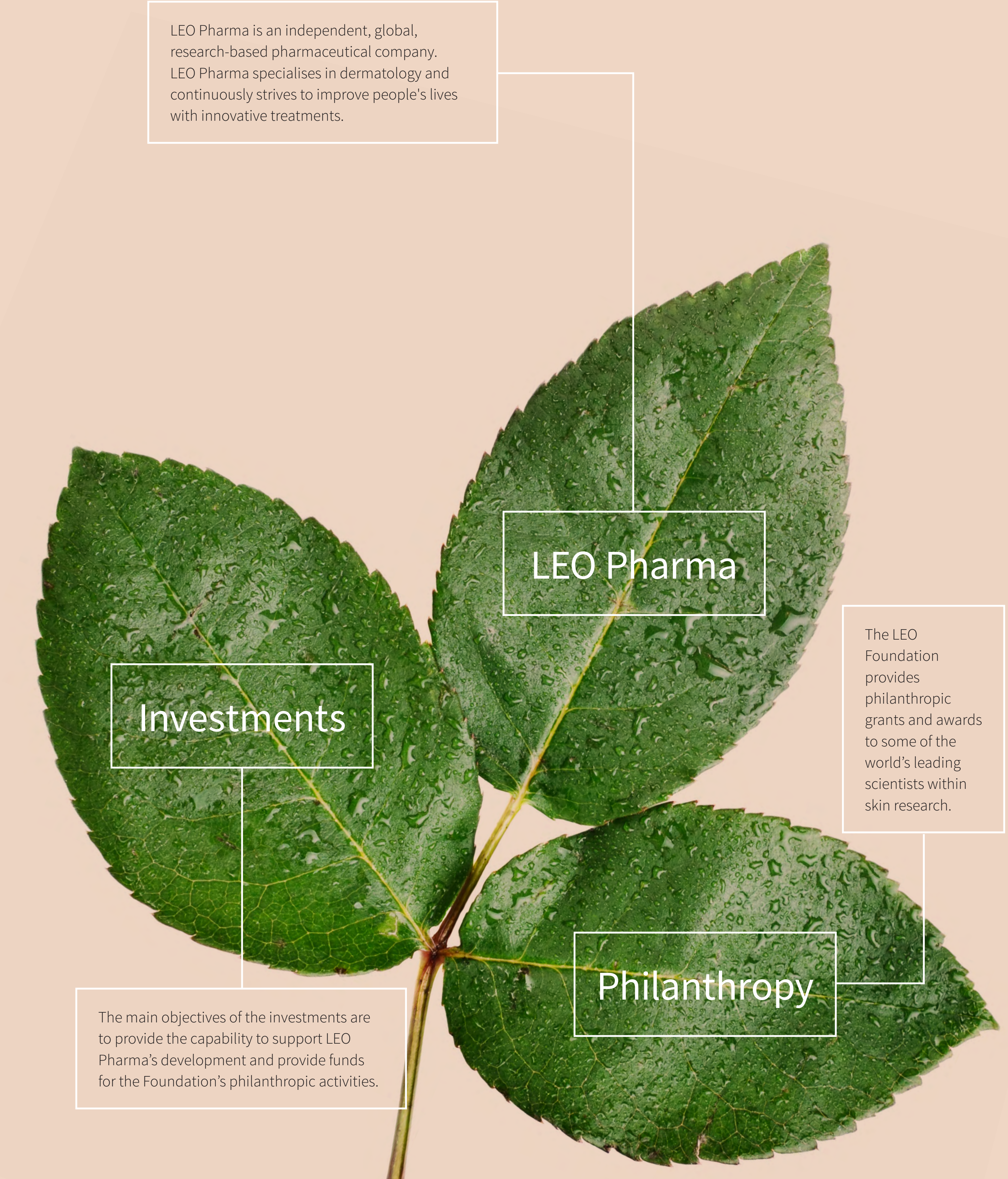
Photo: Nikolaj Rentzmann

Grants and awards 2018

Grantee	Host organisation	Country	Title	Amount, DKK	Area/Type of grant
University of Copenhagen	University of Copenhagen	Denmark	LEO Foundation Skin Immunology Research Center	250,000,000	Strategic grant
Gregor Borut Ernst Jemec and Ole B. V. Pedersen	Zealand University Hospital	Denmark	GWA studies on common dermatological diseases	5,770,000	General dermatology
Simon Danby	University of Sheffield	UK	Implementation of novel 3-bounce 2-pass ATR FTIR spectroscopy into the skin testing for atopic dermatitis (STAR) study	390,506	Atopic dermatitis/ eczema
Andrew G. Myers	Harvard University, Cambridge, Massachusetts	USA	Fully synthetic lincosamides to combat multidrug-resistant skin infections	3,108,110	Skin infections
Rudolf Jaenisch	Whitehead Institute for Biomedical Research, Cambridge, Massachusetts	USA	In vivo model of human melanoma using a novel neural crest chimera system	2,476,836	Skin cancer
Sunny Wong	University of Michigan, Ann Arbor	USA	Investigating the tumor suppressive functions of Notch signaling during skin cancer initiation and progression	2,486,354	Skin cancer
Mariena van der Plas	University of Copenhagen	Denmark	Development of biomarkers and models for wound infection	2,745,375	Wound healing
Kathryn Browning	University of Copenhagen	Denmark	Neutron reflectivity of healthy and atopic dermatitis lesional skin lipid models	2,234,415	Atopic dermatitis/ eczema
Kai Kisand	University of Tartu	Estonia	Impaired thymic negative selection as a source of melanoma-reactive TCR specificities	4,908,566	Skin cancer
Jan J. Enghild	Aarhus University	Denmark	Investigating the role of human periostin in healthy skin and severe eczema	3,045,231	Atopic dermatitis/ eczema
Alex Rojas Bie Thomsen	University of Columbia, New York	USA	Endosomal chemokine receptor signaling as basis for metastasis in malignant melanoma	3,600,308	Skin cancer

The LEO Foundation publishes all grants and the beneficiaries. The above-mentioned grants and awards were adopted during 2018. For more information about the beneficiaries, projects or LEO Foundation grant policy, please visit www.leo-foundation.org.

Grantee	Host organisation	Country	Title	Amount, DKK	Area/Type of grant
Merete Hædersdal	Bispebjerg Hospital, Copenhagen	Denmark	Local targeted immunotherapy for treatment of squamous cell carcinomas	2,358,825	Skin cancer
David M. Sabatini	Whitehead Institute for Biomedical Research, Cambridge, Massachusetts	USA	Probing the function of melanosomal transporters in pigmentation using metabolic profiling	1,278,270	General dermatology
Samir Mitragotri	Harvard John A. Paulson School of Engineering and Applied Sciences, Cambridge, Massachusetts	USA	Nucleic acid ionic liquids (NAILs) for topical skin applications	2,000,043	Technology development
Patrick Zeeuwen	Radboud University Medical Center, Nijmegen	Netherlands	Psoriasis: a microbiome-driven disease?	2,545,944	Psoriasis
Julia Oh	Jackson Laboratory, Farmington, Connecticut	USA	Compartmentalized and systemic interactions of the skin microbiome in cancer immunotherapy response	2,107,529	Skin microbiome
Patrick M. Brunner	Medical University of Vienna	Austria	Characterizing the disease memory in atopic dermatitis	2,920,541	Atopic dermatitis/ eczema
George Cotsarelis	Perelman School of Medicine, University of Pennsylvania, Philadelphia	USA	Developing a cell-based therapy for alopecia	3,793,808	Alopecia
Valentina Greco	Yale University, New Haven, Connecticut	USA	The 2019 Gordon Research Conference on epithelial differentia-tion and keratinization	146,536	Education & awareness
Matthias Mann and Beatice Dyring-Andersen	University of Copenhagen	Denmark	The proteomic skin atlas	100,000	Education & awareness
Svante Lindeburg	Golden Days, Copenhagen	Denmark	Bloom festival 2019	500,000	Education & awareness
Hayato Takahashi	Keio University, Tokyo	Japan	LEO Foundation Gold Award 2018	1,000,000	Awards
Tiffany Scharschmidt	UCSF, San Francisco	USA	LEO Foundation Silver Award 2018	500,000	Awards



Governance

As the ultimate sole owner of LEO Pharma and as one of Denmark's largest commercial foundations with increasing philanthropic activities in the form of grants and awards, the LEO Foundation has considerable societal influence in Denmark and beyond. Thus, we have an important obligation to operate transparently and with integrity, and we fully support and comply with all the recommendations of the Danish Committee on Foundation Governance. For further information, please visit www.leo-foundation.org/governancerecommendations

The LEO Foundation Board of Trustees consists of 11 members. Seven members are appointed in accordance with the Foundation's charter, while four members are elected by LEO Pharma employees in accordance with applicable laws. The composition of the Board reflects the qualifications and skills necessary for the LEO Foundation to fulfil the objectives specified in the Foundation's charter.

The members of the Board of Trustees of the LEO Foundation also make up the Board of Directors of LEO Holding A/S. Both boards meet at least four times a year and, in addition, hold an annual seminar to discuss and review strategies. Two permanent Board committees have been set up: a Grant Committee (as part of LEO Foundation) and an Investment Committee (as part of LEO Holding A/S). Both meet at regular intervals. In addition, ad hoc committees are established when deemed relevant, to handle specific matters.

Statutory Report on Gender Diversity
The Board strives to ensure that, by 2020, at least 40% of charter-appointed members are women and, similarly, that at least 40% of its charter-appointed members are men. No changes were made to the composition of the Board in 2018, thus the gender diversity remained unchanged. At the end of 2018, 30% of the charter-appointed members were women.

Given the very limited number of employees in the LEO Foundation, no policy has been established for gender diversity at management levels below the Board.

In 2018, LEO Pharma set the goal to have at least three female members on its Board of Directors (in addition to the employee-elected members) by the end of 2021. On average, both genders are equally represented (by at least 40%) at management levels below the Board of Directors of LEO Pharma A/S.

For more information on LEO Pharma's governance, please refer to LEO Pharma's Annual Report.

Active ownership of LEO Pharma
The LEO Foundation's main objective is to ensure the long-term independence and success of the global, research-based pharmaceutical company LEO Pharma. We exert our ownership actively by electing highly qualified professionals to the LEO Pharma Board of Directors and by:

- Issuing a mandate to LEO Pharma's Board of Directors specifying the fundamental values and scope of the company
- Approving the long-term performance targets and capital structure of the company
- Endorsing the strategy proposed by LEO Pharma's Board of Directors

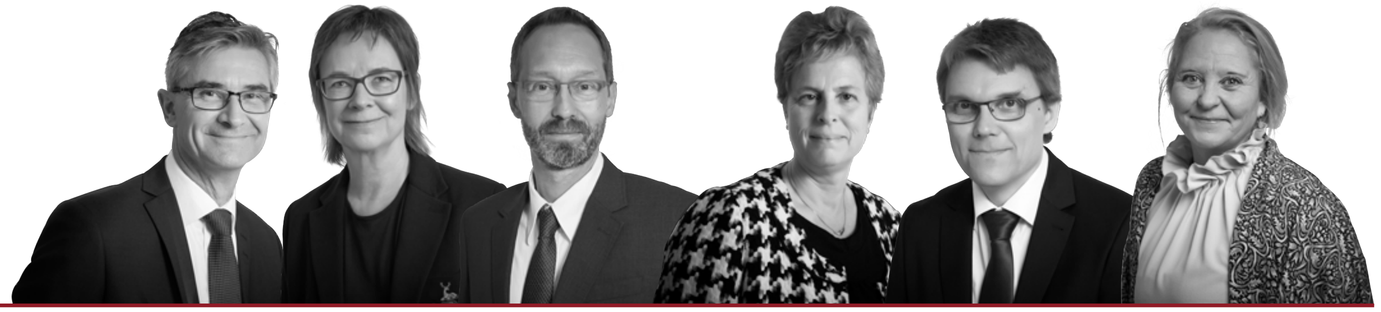
LEO Pharma issues a quarterly report on the progress and performance of the business, followed by status meetings. In addition, an annual Capital Market Day is held, during which the strategic progress is reviewed and discussed. The LEO Foundation holds two ordinary seats on the company's Board of Directors.

Grant Committee
The Grant Committee supervises all grant and award activities and advises the Board on relevant matters, including grant strategies and policies. The Grant Committee also ensures that all grant and award applications undergo relevant assessment to ensure alignment with the Foundation's objectives for its philanthropic activities. This includes evaluation of applications by a Scientific Evaluation Committee with external members who, among other things, assess the scientific topic being researched, the qualifications of the applicant and the academic standard of the host institution. All grants and awards are decided by the Board of Trustees.

Investment Committee
The Investment Committee advises the Board on matters relating to investments and asset management. It prepares and recommends investment strategies and policies to the Board, and ensures their implementation in cooperation with the Executive Management. The Committee also monitors and reviews relevant internal controls, risk management and governance models.

Board of Trustees

In accordance with the governance recommendations issued by the Danish Committee on Foundation Governance, the LEO Foundation discloses the following information about the Board of Trustees:



	Lars Olsen *Chairman*	**Jens Bo Olesen** *Vice Chairman*	**Ingelise Saunders** *Board member*	**John Mehlbye** *Board member*	**Eivind Kolding** *Board member*
Born / Gender	1965 / M	1951 / M	1949 / F	1950 / M	1959 / M
Joined the Board of Trustees	2015	2007	2016	2008	2017
Re-elected	Yes	Yes	Yes	Yes	No
Term expires	2019	2019	2019	2019	2019
Member's special skills	Pharma, general management, R&D, sales and marketing	Pharma, general management, sales and marketing	Pharma, general management, biotech, sales and marketing, business development, drug development	Pharma, general management, product supply	General management, finance, law
Other management positions	LEO Holding A/S, Chairman LEO Foundation, Grant Committee member	LEO Holding A/S, Board member LEO Foundation, Grant Committee member	LEO Holding A/S, Board member Acesion Pharma ApS, Chairman MinervaX Aps, Chairman	LEO Holding A/S, Board member LEO Holding A/S, Investment Committee member Østagergaard, Board member	LEO Holding A/S, Board member LEO Holding A/S, Investment Committee member Danish Ship Finance, Chairman CASA Group, Chairman NNIT, Board member Axcelfuture, Advisory Board member Kunstforeningen Gl Strand, Chairman BiQ ApS, Board member Altor Fund Manager AB, Board member
Appointed by the authorities	No	No	No	No	No
Member considered independent?	No	No	Yes	No	Yes

	Peter Schwarz *Board member*	**Cristina Patricia Lage** *Board member*	**Lars Kjøller** *Employee-elected Board member*	**Jannie Kogsbøll** *Employee-elected Board member*	**Allan Carsten Dahl** *Employee-elected Board member*	**Lotte Hjortshøj** *Employee-elected Board member*
Born / Gender	1959 / M	1954 / F	1967 / M	1962 / F	1967 / M	1971 / F
Joined the Board of Trustees	2017	2016	2017	1998	2015	2018
Re-elected	No	Yes	Yes	Yes	Yes	No
Term expires	2019	2019	2022	2022	2022	2022
Member's special skills	Endocrinology, medicine and clinical biochemistry	General and change management, investment and asset management, financial risk management	R&D information search and analysis, scientific competitive intelligence	Production, processes	Organic process R&D, CMC development	People, project management, administration
Other management positions	LEO Holding A/S, Board member LEO Foundation, Grant Committee, Chairman	LEO Holding A/S, Board member LEO Pharma A/S, Board member LEO Holding A/S, Investment Committee, Chairman Arbejdsmarkedets Erhvervssikring, Chairman Det Obelske Familiefond, Board member C.L. Davids Fond, Board member	LEO Holding A/S, employee-elected Board member	LEO Holding A/S, employee-elected Board member LEO Pharma A/S, employee-elected Board member	LEO Holding A/S, employee-elected Board member	LEO Holding A/S, employee-elected Board member
Appointed by the authorities	No	No	No	No	No	No
Member considered independent?	Yes	Yes	No	No	No	No

Corporate social responsibility

The LEO Foundation plays an active role in society through our substantial philanthropic grants to science and research, both in Denmark and abroad. We aim to support world-leading research within dermatology which, in time, may lead to better diagnoses, treatments and even cures for the millions of people living with skin diseases. For further details about our grants and beneficiaries, please refer to Grants and awards above. For more information about our overall business model, please refer to About LEO Foundation above.

We are committed to acting ethically and responsibly throughout our organisation. A key initiative in 2018 was the adoption of an environmental, social and governance (ESG) policy for our investment activities. The policy is based on adherence to the Ten Principles of the UN Global Compact, which form the basis for ethical, human and corporate behaviour supporting long-term sustainability and success. By basing our policy on these principles, we aim to address the CSR risks we face as a large financial investor. As our investments are managed through the use of external investment managers, we work actively with these managers to ensure compliance with the policy. Our investment team reviews the investment managers as an integrated part of the investment process, and managers are required to report yearly on ESG factors and matters including, where relevant, exited investments, engagement with companies, and corrective actions carried out by the managers. With the adoption of the ESG policy, we have strengthened our framework for responsible conduct in relation to our investments.

The vast majority of the LEO Group's business activities are conducted by LEO Pharma, and CSR is embedded in the company's business and in the behaviour of its employees. LEO Pharma has a business-driven CSR approach and acknowledges its economic, social and environmental responsibility in compliance with the principles of the UN Global Compact. LEO Pharma's 2018-2020 CSR commitment defines nine focus areas where the company takes concrete action to contribute to the UN Sustainable Development Goals. The commitment is built on three pillars: empowering patients, sustainable operations and business integrity. A key objective is to expand dermatological treatments in order to address unmet medical needs. As part of this objective, LEO Pharma built a special unit in 2018 to prepare for new projects within rare dermatological diseases. As a global pharmaceutical company, LEO Pharma performs many functions that impact society. To address and mitigate the risk of negative impacts, the company has developed policies and processes covering the different CSR focus areas.

For more information about LEO Pharma's CSR initiatives and policies, please refer to LEO Pharma's Annual Report.

Given the type of business conducted by the LEO Foundation with just 10 employees, our direct impact on climate and the environment is limited. At LEO Group level, the main impact stems from LEO Pharma's six production facilities. Protecting and preserving the environment is an integral part of LEO Pharma's daily business, and the company actively works to minimise its impact. In 2018, the company achieved its goal of obtaining ISO 14001 certifications in accordance with the new ISO standard for five of its manufacturing sites. With regard to energy efficiency, LEO Pharma set itself a goal to save an amount of energy corresponding to 10% of its energy consumption in 2013 through energy savings. This is equivalent to reducing the company's energy consumption by 12,900 MWh.

The LEO Foundation supports and respects the protection of internationally adopted human and labour rights. At the LEO Foundation, we require our grantees and everybody working on the projects we support to be employed under conditions that comply with applicable laws. The LEO Code of Conduct, which applies to all employees of the LEO Group, prohibits any discrimination on the basis of privacy, race, colour, sex, language, religion, political or other opinion, caste, national or social background, property, citizenship, ethnicity, birth, union affiliation, sexual orientation, health status, family responsibilities, age, disability or any other distinguishing characteristics. At LEO Group level, a key focus area is supplier assessment and management, ensuring that suppliers respect and protect human rights when supplying their goods and services. The vast majority of the LEO Group's supplier relationships tie into LEO Pharma, which systematically screens all new suppliers based on parameters aligned with the Ten Principles of the UN Global Compact. Through a risk-based approach, the company prioritises suppliers for further assessment. In 2018, new ranking criteria were implemented to strengthen the due diligence process, and in 2019, the company plans to reinforce supplier engagement and develop a site visit programme to increase awareness about responsible business practices among its priority suppliers.

Throughout the LEO Group, we are committed to upholding high business standards and promoting good business conduct in our interactions with customers, grantees, healthcare professionals, public officials and other business partners. Our commitment to work against corruption is set out in our anti-corruption and bribery policy, which is part of the LEO Code of Conduct. The policy is supported by the LEO whistleblower hotline, which employees and external stakeholders can use to report serious concerns in a secure and confidential way. In 2018, LEO Pharma focused on strengthening its anti-corruption compliance programme to improve the prevention and early detection of corruption.

Risk management

Risk management is a key part of the LEO Foundation's work. The main objective of these efforts is to remain able to fulfil the charter-defined obligations of ensuring the continuance of LEO Pharma and supporting research within medicine, chemistry and pharmacy. In order to do so, the LEO Foundation must ensure that sufficient capital is always available to withstand a severe crisis, including a convergence of several high-impact risk events.

Updating the LEO Foundation's risk management and reporting system was a focus area in 2018. As part of this work, updated risk models were applied to simulate the effect of a number of potential high-impact risks to ensure that the Foundation always has sufficient capital available to withstand such crises.

The LEO Foundation's main risks relate to value generation and operational risks at LEO Pharma as well as the management of the financial assets. In addition, a number of other risks of a more generic nature were identified, including risks related to the Foundation's philanthropic activities as well as political and reputational risks. These are, as far as possible, mitigated through the implementation of policies and procedures.

LEO Pharma

Business and financial risks associated with operations are managed by LEO Pharma, which has defined risk management policies and procedures. LEO Pharma works continuously to map and mitigate its risks in order to ensure a reasonable risk profile. The LEO Foundation is kept updated about relevant risks through regular reporting from LEO Pharma's Management and via the Foundation's two seats on LEO Pharma's Board of Directors. For more information about risks at LEO Pharma, please refer to LEO Pharma's Annual Report.

Financial portfolio risks

The financial portfolio is managed according to the investment policy, which is reviewed and approved annually by the Board. The investment policy states the strategic asset allocation and the boundaries for each asset class within which tactical asset allocation positions can be taken. Furthermore, the investment policy sets limits on counterparty risk, overall interest rate risk and liquidity of the financial portfolio. Currency risk is hedged for all fixed-income exposure, while equity investments have full currency exposure but with the option to hedge this. All asset classes, external managers and external investment funds are approved by the Board's Investment Committee prior to any investments. Compliance with the investment policy is verified by the finance department, and investment results are documented in reports to the Investment Committee and the CEO.

Each week, a portfolio performance report is prepared by the Chief Investment Officer and distributed to the CEO and the Chairman of the LEO Holding Investment Committee, followed by a meeting between the CEO and the investment team. A monthly report is issued to the Investment Committee. At all regular Board meetings, an investment update is presented to the full Board by the Chief Investment Officer.

In relation to ESG, the investment team reviews the external investment managers as an integrated part of the investment process. In 2018, a new ESG policy was approved by the LEO Holding Board of Directors. This policy requires all managers to report yearly on ESG factors and matters, including, where relevant, exited investments, engagement with companies and ESG Committee issues.

Financial highlights

(DKK million)	2018	2017	2016	2015	2014
Income statement					
Revenue	10,410	10,481	9,863	8,457	7,973
Operating profit	1,577	835	329	759	758
Financial items	(674)	941	789	179	1,290
Profit before tax	892	1,773	1,115	925	2,048
Net profit for the year	708	1,383	723	713	1,544
Balance sheet					
Investments in property, plant and equipment	480	385	302	261	121
Non-current assets	10,234	8,216	19,471	14,895	17,357
Current assets	22,715	23,608	17,500	17,333	14,284
Total assets	**32,949**	**31,824**	**36,971**	**32,228**	**31,641**
Equity	**26,921**	**26,519**	**25,094**	**24,804**	**24,622**
Ratios					
Return on equity	3%	7%	4%	4%	9%
Solvency ratio	82%	83%	68%	77%	78%

The figures for 2018, 2017 and 2016 as well as the balance sheet items and ratios for 2015 have been prepared in accordance with IFRS. All other figures have been prepared in accordance with the Danish Financial Statements Act.

Consolidated Financial Statements – LEO Group

Financial Statements

Notes

Income statement

1 JANUARY – 31 DECEMBER

(DKK million)	Note	2018	2017
Revenue	2	10,410	10,481
Cost of sales	3, 10, 13	(3,040)	(2,938)
Gross profit		**7,370**	**7,543**
Sales and distribution costs	3, 9, 10	(3,946)	(3,378)
Research and development costs	3, 9, 10	(1,914)	(1,602)
Administrative costs	3, 6, 9, 10	(1,330)	(1,841)
Other operating income		1,612	145
Other operating expenses		(215)	(32)
Operating profit		**1,577**	**835**
Share of profit/(loss) on investment in associates		(11)	(3)
Financial income	7	27	1,094
Financial expenses	7	(701)	(153)
Profit before tax		**892**	**1,773**
Tax on profit for the year	8	(184)	(390)
Net profit for the year		**708**	**1,383**

Statement of comprehensive income

1 JANUARY – 31 DECEMBER

(DKK million)	Note	2018	2017
Net profit for the year		708	1,383
Other comprehensive income			
Actuarial gains/(losses)	16	59	131
Tax	8	(6)	(48)
Items that will not be reclassified subsequently to the income statement		**53**	**83**
Exchange rate adjustments on investments in foreign subsidiaries		(40)	(64)
Cash flow hedges (exchange rate), deferred gains/(losses) incurred during the period		(27)	-
Cash flow hedges (intrest rate), deferred gains/(losses) incurred during the period		2	5
Other adjustments		-	17
Tax	8	5	(1)
Items that may be reclassified subsequently to the income statement		**(60)**	**(43)**
Other comprehensive income		**(7)**	**40**
Comprehensive income for the year		**701**	**1,423**

Balance sheet at 31 December

ASSETS

(DKK million)	Note	2018	2017
Intellectual property rights		3,514	3,992
Development projects		2,099	1,159
Software		654	497
Intangible assets	9	**6,267**	**5,648**
Land and buildings		707	691
Leasehold improvements		38	39
Plant and machinery		496	434
Other fixtures and fittings, tools and equipment		126	96
Assets under construction		799	551
Property, plant and equipment	10	**2,166**	**1,811**
Investment in associates		35	3
Other financial securities	11	1,076	27
Deferred tax assets	12	673	667
Other receivables	11	17	60
Financial assets		**1,801**	**757**
Total non-current assets		**10,234**	**8,216**
Inventories	13	1,729	1,719
Trade receivables	14	3,229	2,644
Tax receivables		689	656
Other receivables		499	381
Prepayments		208	162
Other securities	11	16,010	17,618
Cash and bank balances	11	351	428
Total current assets		**22,715**	**23,608**
TOTAL ASSETS		**32,949**	**31,824**

Balance sheet at 31 December

EQUITY AND LIABILITIES

(DKK million)	Note	2018	2017
Foundation capital	15	98	98
Foreign currency translation reserve		(212)	(172)
Hedging reserve		(23)	(3)
Reserve for future grants		104	83
Retained earnings		26,954	26,513
Equity		**26,921**	**26,519**
Deferred tax liabilities	12	4	20
Retirement benefit obligations	16	243	355
Provisions	17	234	170
Credit institutions	11	536	1,006
Contract liabilities	2	-	14
Other long-term liabilities		3	22
Total non-current liabilities		**1,020**	**1,587**
Provisions	17	842	673
Credit institutions	11	914	482
Trade payables		2,455	1,733
Tax payables		59	70
Contract liabilities	2	15	30
Other payables		723	730
Total current liabilities		**5,008**	**3,718**
TOTAL EQUITY AND LIABILITIES		**32,949**	**31,824**

Statement of changes in equity

(DKK million)	Foundation capital	Foreign currency translation reserve	Hedging reserve	Reserve for future grants	Retained earnings	Total
2018						
Equity at 1 January 2018	98	(172)	(3)	83	26,513	26,519
Net profit for the year	-	-	-	100	608	708
Other comprehensive income for the year	-	(40)	(20)	-	53	(7)
Total other comprehensive income for the year	-	(40)	(20)	100	661	701
	-	-	-	-	-	-
Additions	-	-	-	220	(220)	-
Grants for the year	-	-	-	(299)	-	(299)
Equity at 31 December 2018	**98**	**(212)**	**(23)**	**104**	**26,954**	**26,921**
2017						
Equity at 1 January 2017	52	(108)	(8)	47	25,111	25,094
Net profit for the year	-	-	-	80	1,303	1,383
Other comprehensive income for the year	-	(64)	5	-	99	40
Total other comprehensive income for the year	-	(64)	5	80	1,402	1,423
Additions	46	-	-		-	46
Grants for the year	-	-	-	(44)	-	(44)
Equity at 31 December 2017	**98**	**(172)**	**(3)**	**83**	**26,513**	**26,519**

Cash flow statement

1 JANUARY – 31 DECEMBER

(DKK million)	Note	2018	2017
Operating profit		**1,577**	**835**
Adjustment for non-cash operating items			
Amortisation, depreciation and impairment losses	9, 10	760	1,143
Change in retirement benefit obligations	16	(112)	(420)
Change in provisions	17	203	(21)
Reversal of gain on divestments of assets		(1,593)	-
Other adjustments	18	(66)	50
Change in working capital			
Change in inventories and receivables		(643)	(340)
Change in trade payables and other payables		110	(537)
Corporation tax paid		(240)	(161)
Interest paid		(143)	(32)
Interest received		43	256
Cash flows from operating activities		**(104)**	**773**
Investments in intangible assets	9	(878)	(479)
Investments in property, plant and equipment	10	(478)	(385)
Investments in acquisitions		(436)	-
Proceeds from sale of intangible assets and property, plant and equipment		1,858	45
Investments in other securities		(160)	-
Proceeds from sale of other securities		206	5,698
Cash flows from investing activities		**112**	**4,879**
Repayment of bank debt		(474)	(5,325)
Overdraft		443	-
Grants paid out during the year		(49)	(32)
Cash flows from financing activities		**(80)**	**(5,357)**
Change in cash and cash equivalents		**(72)**	**295**
Cash and cash equivalents at 1 January		428	150
Unrealised exchange gains/(losses) on cash and cash equivalents		(5)	(17)
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	11	**351**	**428**

The figures in the cash flow statement cannot be directly derived from the figures in the balance sheet.

Notes LEO Group

NOTE 1 BASIS OF REPORTING

Basis of preparation
The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the EU, and the additional requirements of the Danish Financial Statements Act.

The Consolidated Financial Statements are presented in Danish kroner (DKK), which is also the functional currency of the Parent Company.

The accounting policies applied to the Consolidated Financial Statements in general are described below, while the remaining accounting policies are described in the notes to which they relate.

Applying materiality
In the preparation of the Consolidated Financial Statements, the LEO Group aims to focus on information which is considered to be material and relevant to the users of the Consolidated Financial Statements.

The Consolidated Financial Statements are a result of aggregating large numbers of transactions into classes of similar items according to their nature or function in the Consolidated Financial Statements. If a line item is not individually material, it is aggregated with other items of a similar nature in the Consolidated Financial Statements or in the notes.

The provisions in IFRS contain extensive disclosure requirements. The specific disclosures required by IFRS are provided in the Consolidated Financial Statements unless the information is considered immaterial to the users of the Consolidated Financial Statements.

Key accounting estimates and judgements
Executive Management has made certain estimates regarding valuation and judgements that affect the accounting policies and the reported amounts in the Consolidated Financial Statements. Estimates are based on historical experience and assumptions reasonable under the circumstances. They are based on whatever information is currently available. Therefore the actual amounts may differ from the estimated amounts.

Below are listed the key accounting estimates and judgements relevant to the specific notes:

- Note 5 Acquisition and divestments: Assessment of type of acquisition, control and purchase price allocation
- Note 8 Intangible assets: Estimated useful lives, impairment test and judgement on acquisition of intangible assets
- Note 10 Financial instruments: Judgement on measurement of fair value, classifications and assessment of credit risk
- Note 11 Deferred tax: Estimates of deferred tax assets
- Note 12 Inventories: Estimates of valuation of inventories
- Note 16 Provisions: Estimates of provision for legal disputes and sales deductions

In 2018, the useful lives of intangible assets have been re-assessed. Based on the review, the useful lives of some intellectual property rights have been increased to reflect the pattern of future economic benefits from the assets. The change is accounted for in accordance with IAS 8 as a change in accounting estimates.

The impact on the Consolidated Financial Statements in 2018 is a decrease in amortisation of DKK 239 million in the income statement and a corresponding increase in carrying amount of intangible assets in the balance sheet.

NOTE 1 BASIS OF REPORTING (CONTINUED)

General accounting policies

Consolidation

The Consolidated Financial Statements comprise the LEO Foundation and entities in which the LEO Foundation directly holds more than 50% of the votes or otherwise exercises control (its subsidiaries).

The Consolidated Financial Statements are prepared by combining the Financial Statements of the Parent Company and all subsidiaries with subsequent elimination of intercompany transactions, intercompany shareholdings and balances, as well as unrealised profits from intercompany transactions. The Financial Statements of all companies have been prepared according to the same accounting policies as applied by the LEO Group.

The proportionate share of the results of associates is recognized in the income statement after tax. Unrealised gains and losses on transactions with associates are eliminated in proportion to the Group's share of the enterprise.

Foreign currency translation

On initial recognition, transactions in foreign currencies are translated at the exchange rates at the transaction dates. Exchange rate differences arising between the rates on the transaction and payment dates are recognised in Financial income and Financial expenses in the income statement.

Receivables, payables and other monetary items in foreign currencies are translated at the exchange rates at the balance sheet date. Any differences between the exchange rates at the balance sheet date and the rate at the time when the receivable or the payable arises, or on recognition in the most recent Financial Statements, are recognised in Financial income and Financial expenses in the income statement.

On consolidation of foreign subsidiaries having a functional currency other than DKK, income statements are translated into DKK at the average exchange rates for the period, and balance sheet items are translated at the exchange rates at the balance sheet date. The effects of the translation of the opening equity of foreign subsidiaries at the exchange rates at the balance sheet date and the translation of the statement of comprehensive income from average exchange rates to the exchange rates at the balance sheet date are recognised in Other comprehensive income.

Cash flow statement

The cash flow statement is prepared according to the indirect method based on operating profit. The statement shows cash flows from operating, investing and financing activities, as well as cash and cash equivalents at the start and end of the year. Cash flows from operating activities are calculated as the Group's operating profit, adjusted for non-cash operating items such as depreciation, amortisation and impairment losses, as well as changes in working capital. Working capital comprises inventories, trade receivables and trade payables, etc.

Cash flows from investing activities comprise payments from acquisitions and disposals of intangible assets and property, plant and equipment, as well as fixed asset investments.

Cash flows from financing activities comprise payments from the raising and repayment of short-term and long-term debt, and payments to and from shareholders. Cash and cash equivalents comprise solely cash at bank and in hand.

Grants

Grants paid out: Grants that have been adopted and paid out in accordance with the purpose of the Foundation at the balance sheet date are deducted from equity.

Grants not yet paid out: Grants that have been adopted in accordance with the purpose of the Foundation at the balance sheet date and announced to the recipients, but not yet been paid out at the balance sheet date, are deducted from equity and recognised as debt.

Grant limit : At the meeting of the Board of Trustees at which the Annual Report is adopted, the Board of Trustees lays down a grant limit in respect of the amount expected to be granted. This amount is transferred from retained earnings to the grant limit. Concurrently with being announced to the recipients, the grant amounts are paid out, transferred to debt or, in rare cases, transferred to provisions relating to grants.

Definition of key figures

$$\text{Return on equity}^{1} = \frac{\text{Profit before tax}}{\text{Average equity}} \times 100$$

$$\text{Solvency ratio}^{1} = \frac{\text{Equity}}{\text{Assets}} \times 100$$

1. Definitions according to the Danish Society of Financial Analysts' Recommendations & Financial Ratios.

NOTE 1 BASIS OF REPORTING (CONTINUED)

Implementation of new standards and interpretations

While the LEO Group in 2017 applied IFRS 9, Financial instruments, and IFRS 15, Revenue from contracts with customers, in advance of their effective dates, other new and amended standards and interpretations that are effective as at 1 January 2018 have been implemented in the current year. Their adoption has not had any material impact on the disclosures or on the amounts reported in the Consolidated Financial Statements.

The following new or changed accounting standards and interpretations have been implemented:

- *IFRIC 22 Foreign Currency Transactions and Advance Consideration*

- *Annual Improvement Cycle – 2014-2016*

New and revised IFRSs issued but not yet effective that are relevant to LEO Group

The LEO Group has not applied the following standards that have been issued but are not yet effective:

IFRS 16 Leases (effective for annual periods beginning on or after 1 January 2019)

- The LEO Group will adopt IFRS 16 from the effective date. We are still analysing the effect, but preliminary conclusions are that the change in lease accounting will have limited impact on both the balance sheet and the income statement. We expect to implement the standard based on the simplified transition method, where comparative figures will not be restated. The balance sheet is expected to increase by the value of the right-of-use assets, at an estimated amount of DKK 300 million in 2019. In the income statement, the lease costs will be split between depreciation of the right-of-use assets and interest on the lease liabilities recognised in financial expenses.

IFRIC 23 Uncertainty over Income Tax Treatments (effective for annual periods beginning on or after 1 January 2019)

- The interpretation addresses the accounting for income taxes when tax treatments involve uncertainty affecting the application of IAS 12 and does not apply to taxes and levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The LEO Group will apply the interpretation from its effective date and perform the necessary procedures to ensure implementation in a timely manner.

Other new and revised IFRSs issued but not yet effective are listed below. LEO Group does not expect that the adoption of these standards will have a material impact on the Group Financial Statements in future periods.

- *Amendments to IFRS 9 (Prepayment Features with negative compensation)*

- *Amendments to IAS 28 (Long-term interests in associates and Joint Ventures)*

- *Annual Improvements to IFRS Standards 2015-2017 Cycle (Amendments to IFRS 3 Business Combinations, IFRS 11 Joint Arrangements, IAS 12 Income Taxes, and IAS 23 Borrowing Costs)*

- *Amendments to IAS 19 Employee Benefits (Plan Amendment, Curtailment or Settlement).*

NOTE 2 REVENUE

Accounting policies

Revenue from the sale of goods for resale and finished goods is recognised in the income statement when control has been transferred – generally this is when delivery and transfer of risk have taken place. For sales delivered on a consignment basis, control is transferred when the products are sold to the end-customer.

Revenue is measured at the amount of consideration which the Group expects to be entitled to in exchange for transferring the goods. Revenue is recognised exclusive of VAT and net of sales deductions, including product returns as well as discounts and rebates.

Revenue includes licence income and sales-based royalties from outlicensed products as well as milestone payments and other revenues in connection with partnerships. These revenues, except for royalties, are recognised when the performance obligation is satisfied, when transferred to the customer. For sales-based royalties, revenue is recognised when the subsequent sale occurs. Please refer to note 16 Provisions regarding the accounting policies for sales deductions and returns.

(DKK million)	2018	2017
Revenue by region		
Europe+	6,530	6,379
International	2,795	2,745
US	1,085	1,357
Total	**10,410**	**10,481**
Revenue by therapeutic area		
Psoriasis	3,837	3,587
Actinic keratosis	374	369
Eczema/skin infections	2.598	3,015
Thrombosis	2,396	2,488
Other	1,205	1,022
Total	**10,410**	**10,481**
Revenue by category		
Products	10,164	10,083
Sales-based royalties	225	377
Other	21	21
Total	**10,410**	**10,481**
Timing of revenue recognition		
Goods transferred at a point in time	10,380	10,449
Services transferred over time	30	32
Total	**10,410**	**10,481**

NOTE 2 REVENUE (CONTINUED)

Contract balances

Generally, billing occurs subsequent to revenue recognition, resulting in trade receivables. Payment terms are typically 30-60 days. However, the Group sometimes receives upfront payments related to various sales and distribution rights where the upfront payments are recognised over time, resulting in contract liabilities. Contract liabilities are recognised as Revenue in line with fulfillment of the contract obligation.

(DKK million)	2018	2017	2016
Contract liabilities (non-current)	-	14	45
Contract liabilities (current)	15	30	30
Total contract liabilities	**15**	**44**	75
Revenue recognised in the period from			
Amounts included in contract liabilities at the beginning of the period	30	32	26

Unsatisfied performance obligations

The Group's unsatisfied performance obligations relate to the contract liabilities that have not yet been recognised as Revenue, as well as contracts where the Group has an obligation to deliver goods that has not yet been satisfied.

The transaction price not yet recognised as Revenue is:

(DKK million)	2019	2020	Total
Remaining performance obligations expected to be recognised as of 31 December 2018	111	-	**111**

The Group applies the practical expedient in section C5(c) of IFRS 15 and does not disclose the amount of the transaction price allocated to the remaining performance obligations or when the Group expects to recognise that amount as revenue for the year ended 31 December 2018.

NOTE 3 STAFF EXPENSES

(DKK million)	2018	2017
Wages and salaries	3,086	2,734
Pensions – defined benefit plans	6	7
Pensions – defined contribution plans	256	211
Social security expenses	292	271
Other employee expenses	213	219
Total staff expenses for the year	**3,853**	**3,442**
Capitalised staff expenses	(137)	(63)
Total staff expenses in the income statement	**3,716**	**3,379**
Staff expenses included in		
Cost of sales	656	603
Sales and distribution costs	1,701	1,625
Research and development costs	709	658
Administrative costs	650	493
Total	**3,716**	**3,379**
Remuneration to the Executive Board	3	3
Average number of full-time employees	5,534	5,253

Remuneration to the Board of Trustees

In accordance with the governance recommendations issued by the Danish Committee on Foundation Governance, the LEO Foundation discloses the following information about the Board of Trustees (with the exception of employee-elected members):

(DKK thousand)	Lars Olsen	Jens Bo Olesen	Ingelise Saunders	John Mehlbye	Cristina Lage	Peter Schwarz	Eivind D Kolding	Employee-elected	Total
Remuneration period	Full year	Full year	Full year	Full year	Full year	Full year	Full year		
LEO Foundation, Board	450	300	150	150	150	150	150	575	2,075
LEO Foundation, Committees	-	-	-	-	-	100	-	-	100
LEO Holding A/S	450	300	150	150	150	150	150	575	2,075
LEO Holding A/S, Committees	-	-	-	50	100	-	50	-	200
LEO Pharma A/S	-	-	58	-	350	-	-	408	816
LEO Pharma A/S, Committees	-	-	8	-	50	-	-	-	58

The Chairman and Vice Chairman do not receive separate remuneration for committee work.

NOTE 4 OTHER OPERATING INCOME AND EXPENSES

Accounting policies
Other operating income and other operating expenses comprises items of a secondary nature to the LEO Group's primary activities.

Other operating income and expenses
The increase in other operating income for 2018 compared with 2017 is mainly gain from the divestment of products to Karo Pharma AB of DKK 1,566 million. The increase in other operating expenses relates mainly to cash proceeds of DKK 151 million, also related to the divestment.

NOTE 5 ACQUISITION AND DIVESTMENT OF ASSETS AND ACTIVITIES

Accounting policies
Acquisition of activities are recognized using the acquisition method whereby assets and liabilities as well as contingent liabilities are measured at fair value on the date of acquisition.

The fair value of intellectual property rights is determined using an income approach where they are valued at present value based on the expected cash flows. Other assets and liabilities are valued using the most relevant approach for the individual item.

Key accounting estimates and judgements

Assessment of type of transaction and control
LEO Group carry out specific assessments of each transaction to determine how the acquisition must be accounted for. This includes an assessment of the assets and activities acquired, termination of acquisition date and LEO Group's ability to exercise influence in the acquired enterprise.

Purchase price allocations
When applying the acquisition method for business combinations, by nature this involves judgement in assessing the fair value of identifiable assets and liabilities.

The assessment of fair value of intellectual property rights is based on a number of estimates regarding WACC and expected cash flows which have a large impact on the fair value.

On 27 July 2018, the LEO Pharma Group entered into two separate agreements to purchase Bayer's global prescription dermatology portfolio. The first agreement relating to the US business was recognised in the consolidated financial statements at the closing date, 4 September 2018.

The second agreement regarding the rest of the world will be recognised on the date when the LEO Pharma Group obtains control, which is expected to be 1 July 2019.

From the acquisition date to 31 December 2018, the US business contributed revenue of DKK 128 million. If the acquisition had taken place on 1 January 2018, the impact on the Group's revenue would have been DKK 423 million.

US acquisition in 2018
A cash consideration of DKK 436 million was paid in 2018. Intellectual property rights were valued at DKK 332 million and inventory at DKK 104 million. No goodwill was recognised as part of the transaction. Transaction costs of DKK 27 million were recognised in Administrative costs.

Rest of the world 2019
LEO Pharma Group is expected to acquire the global product rights and take over sales and marketing organisations in the rest of the world in 2019. The acquisition further comprises a factory in Segrate, Italy, and 100% of the shares in the German companies Intendis GmbH, Intraserv GmbH and Intraserv KG. The initial accounting for the purchase price allocation for the rest of the world agreement will commence in 2019.

There were no acquisitions in 2017.

Divestment
LEO Pharma A/S divested a portfolio of 10 products to Kara Pharma AB in 2018. The divestment was effective from 4 April 2018. The divestment resulted in an accounting gain of DKK 1,566 million recognised under Other operating income.

There were no divestments in 2017.

NOTE 6 AUDIT FEES

(DKK million)	2018	2017
Deloitte Statsautoriseret Revisionspartnerselskab		
Statutory audit	7	6
Tax advisory services	2	-
Other services	6	3
Total	**15**	**9**

NOTE 7 FINANCIAL INCOME AND EXPENSES

Accounting policies
Financial income and expenses comprise interest, realised and unrealised exchange rate adjustments and market value adjustments of financial assets.

Market value adjustments of currency derivatives that have not been classified as effective cash flow hedges are presented as Financial income and expenses.

NOTE 7 FINANCIAL INCOME AND EXPENSES (CONTINUED)

(DKK million)	2018	2017
Interest income on bonds (amortised cost)	8	188
Interest income on bonds (fair value)	-	28
Capital gains, financial assets	3	582
Gain arising on reclassification of financial assets from amortised cost at fair value through profit and loss	-	252
Other interest income	3	-
Other financial income	13	44
Financial income	**27**	**1,094**
Interest expenses, banks	(19)	-
Capital losses, financial assets	(522)	-
Loss arising from financial assets measured at amortised cost	-	(10)
Loss arising on financial assets designated at fair value through profit and loss	(2)	-
Exchange rate losses	(74)	(43)
Write-down of financial assets	(67)	(48)
Other financial expenses	(17)	(52)
Financial expenses	**(701)**	**(153)**

NOTE 8 TAX ON PROFIT FOR THE YEAR

Accounting policies
Tax for the year, which consists of the year's current tax, the change in deferred tax and adjustment in respect of previous years, is recognised in the income statement at the amount that can be attributed to the net profit or loss for the year and in other comprehensive income at the amount that can be attributed to items in other comprehensive income. The effect of foreign currency exchange differences on deferred tax is recognised in the balance sheet as part of the movement in deferred tax.

Current tax for the year is calculated based on the income tax rates and rules applicable at the balance sheet date.

(DKK million)	2018	2017
Current tax	219	75
Prior-year adjustments, current tax	(14)	(19)
Prior-year adjustments, deferred tax	30	17
Change in deferred tax for the year	(50)	366
Total tax for the year	**185**	**439**
Tax for the year is included in		
Tax on profit/(loss) for the year	184	390
Tax on other comprehensive income	1	49
Total tax for the year	**185**	**439**

For a specification of tax on other comprehensive income, please refer to the statement of comprehensive income.

NOTE 8 TAX ON PROFIT FOR THE YEAR (CONTINUED)

Explanation of the Group's effective tax rate relative to the Danish corporate income tax rate

(DKK million)		%
2018		
Profit/(loss) before tax	**892**	
Calculated tax, 22%	196	22,0%
Tax effect of		
Differences in the income tax rates of foreign subsidiaries from the Danish corporate income tax rate	(151)	-17.0%
Non-deductible expenses/non-taxable income and other permanent differences	2	0.2%
Tax credits	(1)	-0.1%
Change in deferred tax as a result of changed income tax rate	(24)	-2.7%
Change in valuation of net tax assets	146	16.4%
Prior-year tax adjustments, etc., total effect on operations	16	1.8%
Effective tax/tax rate for the year	**184**	**20.6%**

Explanation of the Group's effective tax rate relative to the Danish corporate income tax rate

(DKK million)		%
2017		
Profit/(loss) before tax	**1,773**	
Calculated tax, 22%	390	22.0%
Tax effect of		
Differences in the income tax rates of foreign subsidiaries from the Danish corporate income tax rate	(86)	-4.8%
Non-deductible expenses/non-taxable income and other permanent differences	18	1,0%
Tax credits	(3)	-0.2%
Change in deferred tax as a result of changed income tax rate	56	3.2%
Change in valuation of net tax assets	16	0.9%
Prior-year tax adjustments, etc., total effect on operations	(1)	-0.1%
Effective tax/tax rate for the year	**390**	**22.0%**

NOTE 9 INTANGIBLE ASSETS

Accounting policies

Intellectual property rights are measured at cost less accumulated amortisation and impairment losses. Amortisation is provided on a straight-line basis over the expected useful lives of the assets. For the relevant assets, the amortisation profile is adjusted to reflect the economic benefit relating to the underlying asset. Amortisation of intellectual property rights is mainly recognised in Sales and distribution costs.

Costs relating to the maintenance of patents, etc. are expensed in the income statement as incurred.

Development projects are recognised as Intangible assets if the recognition criteria are met. Development costs are capitalised only if the following can be demonstrated: technical feasibility of and intention to complete the asset, ability to use or sell the asset, expectation of generating future economic benefits and ability to measure the expenditure reliably.

The costs of development projects include direct salaries, materials and other direct costs attributable to the development project. Other development costs are recognised in the income statement as incurred. Projects are assessed on an ongoing basis taking into account development progress, expected approvals and commercial utilisation. Development projects are not amortised, as the assets are not available for use.

Research costs are recognised in the income statement as incurred.

Internally developed computer software and other IT projects for internal use are recognised as Intangible assets if the recognition criteria are met. Amortisation is provided on a straight-line basis over the expected useful lives. Amortisation and impairment are recognised in the income statement as Administrative costs.

Useful lives are determined at the acquisition date and reassessed annually. The expected useful lives are as follows:

Intellectual property rights and trademarks:	3-15 years
Software:	3-10 years

Impairment

At the end of each reporting period, the carrying amounts of the intangible assets are reviewed to determine whether there is any indication that they have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss.

Intangible assets not yet available for use are tested for impairment at least annually, and whenever there is an indication that the asset may be impaired.

The recoverable amount is the higher of fair value less costs of disposal and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

Key accounting estimates and judgements

To determine the value in use, the expected cash flow approach is applied. The expected future cash flows are based on the budget and target plans for the next five years for marketable products and up to 15 years for licences where products have not yet been launched. Useful life is estimated individually in each case. In addition, the budgets and target plans are based on Executive Management's expectations of current market conditions and future growth.
The key factors used in calculating the value are revenue, EBIT, working capital and discount rate.

LEO Pharma Group has identified capitalised software relating to the ERP system (GLOBE) as corporate assets. During the year, Executive Management considers the recoverability of the assets and assesses indications of impairment.

Useful lives are initially assessed when the assets are acquired. Executive Management assesses intangible assets for changes in useful lives and impairment on an annual basis. This assessment may involve judgement and inherent uncertainties, as there is often no active market for the intangible assets.

Impairment testing

Irrespective of whether there is an indication of impairment, intangible assets not yet available for use are tested for impairment annually. Intangible assets in use with definite useful lives are tested for impairment if there is any indication of impairment.

Indications of impairment are the following:

- Changes in patent and licence rights
- Changes to future cash inflows in the Group
- R&D results
- Technological changes
- Development of competing products

NOTE 9 INTANGIBLE ASSETS (CONTINUED)

(DKK million)	Intellectual property rights	Trademarks	Development projects	Software	Total intangible assets
2018					
Cost at 1 January 2018	10,292	30	2,924	617	13,863
Exchange rate adjustment	24	-	(64)	-	(40)
Additions during the year	331	-	1,058	127	1,516
Disposals during the year	(542)	(30)	(1)	-	(573)
Transfers	-	-	(114)	114	-
Cost at 31 December 2018	**10,105**	**0**	**3,803**	**858**	**14,766**
Amortisation and impairment losses at 1 January 2018	(6,300)	(30)	(1,765)	(120)	(8,215)
Exchange rate adjustment	(24)	-	64	-	40
Amortisation for the year	(462)	-	-	(76)	(538)
Disposals during the year	195	30	1	-	226
Impairment losses for the year	-	-	(4)	(8)	(12)
Amortisation and impairment losses at 31 December 2018	**(6,591)**	**0**	**(1,704)**	**(204)**	**(8,499)**
CARRYING AMOUNT AT 31 DECEMBER 2018	**3,514**	**0**	**2,099**	**654**	**6,267**
2017					
Cost at 1 January 2017	10,150	30	2,846	475	13,501
Exchange rate adjustment					
Additions during the year	125	-	297	57	479
Disposals during the year	(117)	-	-	-	(117)
Transfers	134	-	(219)	85	-
Cost at 31 December 2017	**10,292**	**30**	**2,924**	**617**	**13,863**
Amortisation and impairment losses at 1 January 2017	(5,623)	(30)	(1,765)	(86)	(7,504)
Exchange rate adjustment					
Amortisation for the year	(758)	-	-	(34)	(792)
Disposals during the year	81	-	-	-	81
Impairment losses for the year					
Amortisation and impairment losses at 31 December 2017	**(6,300)**	**(30)**	**(1,765)**	**(120)**	**(8,215)**
CARRYING AMOUNT AT 31 DECEMBER 2017	**3,992**	**0**	**1,159**	**497**	**5,648**

NOTE 9 INTANGIBLE ASSETS (CONTINUED)

In 2018, Research and development costs recognised in the income statement amounted to DKK 1,914 million (2017: DKK 1,602 million). Research and development costs primarily comprise internal and external costs related to studies, employee costs, materials, depreciation and other directly attributable costs.

The value of intellectual property rights acquired from Astellas amounted to DKK 5,013 million when purchased in 2016. The carrying amount at 31 December 2018 was DKK 2,963 million (2017: DKK 3,760 million). The remaining amortisation period is eight years.

Other individually significant intellectual property rights comprises Tralukinumab (carrying amount of DKK 771 milion) and Kyntheum® (carrying amount of DKK 225 million).

(DKK million)	2018	2017
Amortisation and impairment losses are specified as follows:		
Cost of sales		
Sales and distribution costs	446	714
Research and development costs	4	-
Administrative costs	100	78
Total	**550**	**792**

NOTE 10 PROPERTY, PLANT AND EQUIPMENT

Accounting policies
Property, plant and equipment are measured at cost less accumulated depreciation and impairment. Cost comprises the acquisition price and other directly attributable costs until the date the asset is available for use. For self-constructed assets, cost comprises direct costs of materials, sub-suppliers and salaries, etc. The total cost of an asset is broken down into components that are depreciated separately if the expected useful lives of the individual components are not the same.

Depreciation is provided on a straight-line basis from the time of acquisition, or when the asset is available for use, over the expected useful life. A reassessment is made once a year to ascertain that the deprecia-tion basis reflects the expected useful life and future residual values of the assets. Land is not depreciated.

The expected useful lives are as follows:

Buildings:	10-50 years
Leasehold improvements:	Up to 10 years
Plant and machinery:	5-10 years
Other fixtures and fittings, tools and equipment:	3-10 years

Impairment testing
The carrying amount of property, plant and equipment is reviewed to determine whether there is any indication of impairment loss. If the recoverable amount of an asset is estimated to be lower than the carrying amount, an impairment loss is recognised.

For 2018, the impairment test resulted in an impairment loss of DKK 0 million (2017: DKK 147 million).

NOTE 10 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

(DKK million)	Land and buildings	Leasehold improve-ments	Plant and machinery	Other fixtures and fittings, tools and equipment	Fixed assets under construction	Total property, plant and equipment
2018						
Cost at 1 January 2018	2,085	148	2,248	452	673	5,606
Exchange rate adjustment	3	(1)	1	-	2	5
Additions during the year	-	6	3	47	424	480
Disposals during the year	(25)	(73)	(89)	(16)	(34)	(237)
Transfers	70	-	178	18	(266)	-
Cost at 31 December 2018	**2,133**	**80**	**2,341**	**501**	**799**	**5,854**
Depreciation and impairment losses at 1 January 2018	(1,394)	(109)	(1,814)	(356)	(122)	(3,795)
Adjustment to opening	-	-	-	-	122	122
Exchange rate adjustment	(2)	2	(1)	-	-	(1)
Disposals during the year	22	73	90	12	-	197
Impairment for the year	-	-	-	-	-	-
Depreciation for the year	(52)	(8)	(120)	(31)	-	(211)
Depreciation and impairment losses at 31 December 2018	**(1,426)**	**(42)**	**(1,845)**	**(375)**	**0**	**(3,688)**
CARRYING AMOUNT AT 31 DECEMBER 2018	**707**	**38**	**496**	**126**	**799**	**2,166**
2017						
Cost at 1 January 2017	2,198	158	2,446	465	406	5,673
Exchange rate adjustment	1	(9)	(2)	(4)	-	(14)
Additions during the year	-	8	3	34	340	385
Disposals during the year	(121)	(9)	(261)	(47)	-	(438)
Transfers	7	-	62	4	(73)	-
Cost at 31 December 2017	**2,085**	**148**	**2,248**	**452**	**673**	**5,606**
Depreciation and impairment losses at 1 January 2017	(1,438)	(88)	(1,954)	(382)	-	(3,862)
Exchange rate adjustment	(1)	4	2	2	-	7
Disposals during the year	121	9	244	47	-	421
Impairment for the year	-	(20)	(5)	-	(122)	(147)
Depreciation for the year	(76)	(14)	(101)	(23)	-	(214)
Depreciation and impairment losses at 31 December 2017	**(1,394)**	**(109)**	**(1,814)**	**(356)**	**(122)**	**(3,795)**
CARRYING AMOUNT AT 31 DECEMBER 2017	**691**	**39**	**434**	**96**	**551**	**1,811**

NOTE 10 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

(DKK million)	2018	2017
Depreciation and impairment losses are specified as follows:		
Cost of sales	176	326
Sales and distribution costs	13	15
Research and development costs	10	10
Administrative costs	12	10
Total	**211**	**361**

NOTE 11 FINANCIAL INSTRUMENTS

Accounting policies

Financial instruments

Financial assets and financial liabilities are recognised when the Group becomes a party to the contractual provisions of the instrument. Financial assets, except for trade receivables, and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of the financial assets and financial liabilities are added to or deducted from the fair value of the financial assets or financial liabilities, as appropiate, on initial recognition.

Financial assets

All recognised financial assets are required to be measured subsequently at amortised cost or fair value on the basis of the business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. Other financial securities presented under non-current assets consist of equity investments and bond.

Investments in bonds that are held within a business model the objective of which is to collect the contractual cash flows are subsequently measured at amortised cost. Investments that are held within a business model the objective of which is both to collect the contractual cash flows and to sell are subsequently measured at fair value through Other comprehensive income.

All other investments, including equity investments, are subsequently measured at fair value through profit and loss.

Other securities, which comprise listed bonds, shares, credit and listed and unlisted alternatives, are classified as current assets and measured at fair value through profit and loss. Securities that are subsequently measured at amortised cost or at fair value through Other comprehensive income are subject to impairment.

Financial liabilities

All financial liabilities are subsequently measured at amortised cost using the effective interest method.

Derivative financial instruments

Derivative financial instruments are used to manage the exposure to interest rate and foreign exchange rate risk. None of the derivative financial instruments are held for trading. On initiation of the contract, the Group designates each derivative financial contract as either a hedge of the fair value of a recognised asset or liability (fair value hedge) or as a hedge of a future transaction (cash flow hedge). All contracts are initially recognised at fair value and subsequently remeasured at fair value at the end of the reporting period. The resulting gain or loss is recognised in profit and loss immediately, unless the derivative is designated and effective as a hedging instrument, in which case the timing of recognition in profit and loss depends on the nature of the hedge relationship.

Hedge accounting

The Group designates certain derivatives held as hedging instruments in respect of foreign currency risk as either fair value hedges or cash flow hedges, and certain derivatives held as hedging instruments in respect of interest rate risk as cash flow hedges.

The fair value adjustment on qualifying hedging instruments is recognised in the income statement under Financial income or Financial expenses along with any value adjustment of the hedged asset or liability that is attributable to the hedged risk.

Value adjustments of the effective part of cash flow hedges are recognised in equity through Other comprehensive income. The cumulative value adjustment of these contracts is transferred from Other comprehensive income to the income statement under Financial income or Financial expenses when the hedged transaction is recognised in the Income statement.

Discontinuance of cash flow hedging

When a hedging instrument expires or is sold but the hedge still meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

transaction is ultimately recognised in the income statement. If a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement under Financial income or Financial expenses.

Fair value determination

The fair value of derivative financial instruments is measured on the basis of quoted market prices of financial instruments traded in active markets. If an active market exists, the fair value is based on the most recently observed market price at the end of the reporting period.

If a financial instrument is quoted in a market that is not active, the Group bases its valuation on the most recent transaction price. Adjustment is made for subsequent changes in market conditions, for instance by including transactions in similar financial instruments assumed to be motivated by normal business considerations.

If an active market does not exist, the fair value of standard and simple financial instruments, such as foreign exchange forward contracts or interest rate swaps, is measured according to generally accepted valuation techniques. Market-based parameters are used to measure the fair value.

Key accounting estimates and judgements

The application of IFRS 9 and IFRS 13 requires significant judgements, including:

- Judgement on measurement of fair value
- Classification of financial assets and assessment of business model within which the assets are held
- Assessment of credit risks on financial assets and impairment within IFRS 9

Financial portfolio risks

Financial portfolio risks are managed according to the LEO Holding Investment policy, which is approved by LEO Holding's Board of Directors. The Investment policy states the strategic asset allocation and the boundaries for each asset class within which tactical asset allocation positions can be taken. Furthermore, the policy defines the limits on counterparty risk, overall duration risk and liquidity of the financial portfolio. Currency risk is hedged for all fixed-income exposure, while equity investments generally have full currency exposure.

Operational financial risks

Operational financial risks are managed by LEO Pharma Group, which has centralised risk management. The overall objectives and policies for the company's financial risk management are outlined in an internal Treasury policy. The new Treasury policy approved in February 2018 incorporates cash flow hedges of highly probable forecast sales and purchase transactions as a new area.

The Treasury policy consists of the Foreign Exchange policy, the Investment policy and the policy regarding Credit Risk on Financial Counterparties, and includes a description of permitted use of financial instruments. LEO Pharma hedges only commercial exposures and consequently does not enter into derivative transactions for trading or speculative purposes. LEO Pharma uses a fully integrated Treasury Management System to manage all financial positions.

Credit risk

LEO Pharma's products are sold primarily to pharmacies, wholesalers and hospitals. Historically, realised losses sustained on debtors have been insignificant, which was also the case in both 2018 and 2017. However, LEO Pharma has a number of ongoing legal actions nearing completion against customers in receivership and other financial difficulties.

LEO Pharma has no significant concentration of credit risk related to trade receivables, as the exposure is spread over a large number of counterparties and customers. As such, LEO Pharma has no significant reliance on any specific customer, but continues to monitor the credit exposure on all customers, both new and existing. Thus, the risk of significant loss is minimised and at an acceptable level.

To manage credit risk on financial counterparties, LEO Pharma enters into derivative financial instruments and money market deposits only with financial counterparties having a satisfactory long-term credit rating assigned by at least one of the three international credit-rating agencies: Standard and Poor's, Moody's and Fitch. If a counterparty has a rating below Investment Grade, LEO Pharma minimises the risk by keeping the lowest possible bank balance or by spreading the risk between several banks. At year-end, the bank balances held with counterparties below Investment Grade are low, and the credit risk is considered low. Furthermore, the credit risk on bond investments is limited, as investments are made in highly liquid bonds with solid credit ratings such as Investment Grade.

Foreign exchange risk

As a global company, LEO Pharma undertakes transactions denominated in foreign currencies and therefore foreign exchange risk has a significant impact on the income statement, balance sheet and cash flow statement. The overall objective of foreign exchange risk management is to reduce the short-term negative impact of exchange rate fluctuations on earnings and cash flow.

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

LEO Pharma hedges existing assets and liabilities in key currencies as well as future expected cash flows 12 months forward. The majority of LEO Pharma's sales are in EUR, USD, GBP, CAD, JPY, RUB, SAR and CNY, but the EUR exchange risk is considered low, as we believe that Denmark will maintain its fixed-exchange-rate policy.

Monetary assets and monetary liabilities for the major currencies at 31 December
LEO Pharma is mainly exposed to USD, GBP, CAD, JPY, RUB, SAR and CNY, either through direct sales to third parties or indirect sales through a subsidiary. The carrying amount of the foreign currency-denominated monetary assets and liabilities in LEO Pharma can be seen in the table below.

(DKK million)	Monetary assets		Monetary liabilities	
	2018	**2017**	**2018**	**2017**
USD	1,239	1,251	483	1,000
GBP	254	280	471	350
CAD	78	183	31	10
JPY	309	112	44	46
RUB	129	111	23	0
SAR	168	97	19	0
CNY	134	77	42	38
AUD	36	43	208	241

Monetary assets and monetary liabilities include trade receivables, other receivables, securities, cash, trade payables and other payables.

Foreign currency sensitivity analysis
The sensitivity analysis below shows the estimated impact on operating profit of a 5% change in DKK versus the key currencies. The analysis shows the impact of foreign currency exchange differences on the Group's monetary assets and liabilities and foreign exchange forwards. A similar negative change in exchange rates would have a similar opposite effect on operating profit.

Estimated impact on profit/(loss) for the year and equity of a 5% increase in year-end exchange rates for the major currencies

(DKK million)	CAD	CNY	GBP	JPY	USD	RUB	SAR
2018							
Profit/(loss) for the year/Equity	(2)	3	(3)	(14)	10	(3)	1
Other equity [1]	(18)	-	(13)	-	(12)	(5)	(5)
2017							
Profit/(loss) for the year/Equity	-	2	(4)	1	(2)	1	

1. This is mainly as a result of the changes in fair value of derivative instruments designated as cash flow hedges.

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

Forward exchange rate contracts
It is the policy of LEO Pharma to enter into either forward exchange contracts or currency options to hedge minimum 80% of the forecasted sales and purchase transactions for the coming 12 months and to hedge recognised assets and liabilities. In the case of hedges of highly probable forecast sales and purchases, as the critical terms of the foreign exchange forward contracts and their corresponding hedged items are the same, LEO Pharma performs a qualitative assessment of effectiveness, and it is expected that the value of the forward contracts and the corresponding hedged items will systematically change in opposite directions in response to movements in the underlying exchange rates. Executive Management has chosen to classify the result of cash flow hedging activities as part of financial items.

Currently, net investments in foreign subsidiaries are not hedged.

LEO Pharma has entered into foreign xchange forward contracts to hedge the exchange rate risk arising from the expected future sales transactions that will take place during the next 12 months, at which time the amount deferred in equity will be reclassified as a gain or loss under financial items. During 2018, no purchase transactions where hedged. The following table shows the outstanding forward contracts classified as cash flow hedges at the end of the reporting period. Foreign currency forward contract assets and liabilities are presented in the line Derivative financial instruments (either as asset or liabilities) within the statement of financial position (see the table Categories of financial assets and financial liabilities).

Financial derivatives – Cash flow hedges

Forward exchange contracts maturing within 12 months	Average hedge rate	Notional value foreign currency	Contract value	Carrying amount of the hedging instruments assets/ (liabilities)	Change in fair value recognised in Other Comprehensive Income
			2018		
Sold CAD	4.75	74	352	4 / (3)	1
Sold GBP	8.31	31	258	1 / (1)	-
Sold USD	6.16	38	234	(11)	(11)
Sold SAR	1.62	64	104	(7)	(7)
Sold RUB	0.093	1,060	99	3	3
Sold PLN	1.71	51	87	(1)	(1)
Sold THB	0.19	278	53	(3)	(3)
Sold other currencies	N/A	N/A	521	4 / (14)	(9)
Total				**12 / (40)**	**(27)**

The financial contracts are expected to impact the income statement in the next 12 months when the cash flow hedges mature and the fair value will be transferred to either Financial income or Financial expenses.

At the end of December 2018, LEO Pharma has classified the following contracts as fair value hedges. The result of the fair value hedging activities is presented as part of financial items.

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

Financial derivatives – Fair value hedges

Forward exchange contracts (against DKK) (DKK million)	Contract value	Fair value at year-end	Maturity end date	Contract value	Fair value at year-end	Maturity end date
	2018			2017		
Sold CAD	63	1	29/03/2019	178	(1)	12/03/2018
Sold CNY[1]	25	-	10/01/2019	-	-	N/A
Sold GBP	34	-	04/01/2019	-	-	N/A
Sold JPY	263	(6)	29/03/2019	43	-	28/03/2018
Sold SAR	140	-	28/03/2019	98	-	11/06/2018
Sold RUB	108	2	22/03/2019	100	-	21/03/2018
Sold USD	465	-	15/02/2019	299	5	31/07/2018
Bought AUD	174	(6)	15/03/2019	41	-	29/01/2018
Bought EUR[2]	1,533	1	22/02/2019	1,845	1	28/06/2018
Sold other currencies	426	(3)	08/08/2019	461	(1)	15/06/2018
Total	**3,231**	**(11)**		**3,065**	**4**	

1. Chinese yuan traded offshore (CNH) is used as a proxy when hedging the Group's CNY currency exposure.
2. Even though the exchange rate risk of EUR is considered low, EUR is still hedged.

The fair value loss on the forward exchange contracts of DKK 11 million at the end of 2018 is recognised in the income statement in Financial expenses (2017: gain of DKK 4 million recognised in Financial income).

Interest rate risk

Long-term funding at floating interest rates is mitigated by entering interest rate swaps as hedge instruments where, the Group pays fixed and receives floating rates.

Hedging of interest rate risk is approved by the Executive Management, and hedge effectiveness is assessed on a regular basis. No ineffectiveness has been observed so far.

The current hedging instruments are shown in the next table.

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

Classification of and maturity dates for financial assets and financial liabilities

Outstanding contracts, receive floating/pay fixed (DKK million)	Notional principal value	Change in fair value recognised in Other comprehensive income	Fair value assets (liabilities)	Average fixed interest rate	Maturity end date
2018					
DKK	100	1	-	0.386%	29/03/2019
DKK	370	1	(1)	0.445%	30/12/2019
Total		**2**	**(1)**		
2017					
DKK	100	-	-	0.325%	28/03/2018
DKK	400	2	(1)	0.386%	29/03/2019
DKK	370	3	(2)	0.445%	30/12/2019
Total		**5**	**(3)**		

At 31 December 2018, the fair value of DKK 1 million has been recognised in Other payables. At 31 December 2017, the fair value of DKK 3 million was recognised in Other payables.

Liquidity risk

The Group manages liquidity risk by maintaining adequate reserves, banking facilities and reserve borrowing facilities, by continuously monitoring forecast and actual cash flows, and by matching the maturity profiles of financial assets and liabilities. The table below outlines the current cash resources and undrawn credit facilities that the Group has at its disposal.

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

Maturity of contractual cash flows

(DKK million)	Contractual amount	Less than 1 year	1-3 years	3-5 years	5+ years
2018					
Non-financial derivatives					
Floating-interest rate bank debt	471	471	-	-	-
Fixed-interest rate bank debt	543	4	539	-	-
Trade and other payables	3,180	3,180	-	-	-
Financial derivatives					
Interest rate swaps used as hedging instruments	1	1	-	-	-
Forwards used as hedging instruments	60	60		-	-
Total contractual cash flow	**4,255**	**3,716**	**539**	**-**	**-**
2017					
Non-financial derivatives					
Floating-interest rate bank debt	872	401	471	-	-
Fixed-interest rate bank debt	629	87	486	56	-
Trade and other payables	2,463	2,463	-	-	-
Financial derivatives					
Interest rate swaps used as hedging instruments	3	2	1	-	-
Forwards used as hedging instruments	5	5	-	-	-
Total contractual cash flow	**3,972**	**2,958**	**958**	**56**	**-**

Cash resources
Cash and cash equivalents and securities consist of cash at bank and in hand offset by any drawn overdraft facilities plus marketable securities, both current and non-current financial assets.

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

Cash resources

(DKK million)	2018	2017
Cash and cash equivalents	351	428
Secured overdraft facilities, banks – amount unused	532	791
Cash resources, banks	**883**	**1,219**
Marketable securities	15,699	17,618
Securities at 31 December	**15,699**	**17,618**
Cash resources, banks and securities	**16,582**	**18,837**

In addition to the cash resources, at the end of 2018, LEO Group had pledged bonds with a carrying amount of DKK 310 million as security for pension liabilities in Ireland, and the UK.

Categories of financial assets and financial liabilities

(DKK million)	Carrying amount		Fair value	
	2018	2017	2018	2017
Financial assets				
Amortised cost				
Cash and bank balances	351	428	351	428
Trade and other receivables	3,728	3,025	3,728	3,025
Other financial assets	1,093	87	1,093	87
Total	**5,172**	**3,540**	**5,172**	**3,540**
Fair value through profit and loss (FVTPL)				
Financial assets mandatorily measured at FVTPL	16,010	17,618		
Derivative instruments in designated hedge relationships	10	9		
Total	**16,020**	**17,627**		
Fair value through Other comprehensive income				
Derivative instruments in designated hedge relationships	12			
Total	**12**			

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

Categories of financial assets and financial liabilities

(DKK million)	Carrying amount		Fair value	
	2018	**2017**	**2018**	**2017**
Financial liabilities				
Amortised cost				
Trade and other payables	3,180	2,463	3,180	2,463
Bank loans (both current and non-current)	1,450	1,488	1,458	1,503
Total	**4,630**	**3,951**	**4,638**	**3,966**
Fair value through profit and loss (FVTPL)				
Derivative instruments in designated fair value hedge relationships	22	5		
Total	**22**	**5**		
Fair value through other comprehensive income				
Derivative instruments in designated hedge accounting relationships	39	3		
Total	**39**	**3**		

Fair value measurements
The fair value of derivative financial instruments is measured on the basis of quoted market prices of financial instruments traded in active markets (Level 1). If an active market exists, the fair value is based on the most recently observed market price at the end of the reporting period. If a financial instrument is quoted in a market that is not active, LEO Group bases its valuation on the most recent transaction price. Adjustment is made for subsequent changes in market conditions, for instance by including transactions in similar financial instruments assumed to be motivated by normal business considerations.

If an active market does not exist, the fair value of standard and simple financial instruments, such as foreign exchange forward contracts, interest rate swaps, currency swaps and unlisted bonds and shares, is measured according to generally accepted valuation techniques (Level 2). Market-based parameters are used to measure the fair value.

NOTE 11 FINANCIAL INSTRUMENTS (CONTINUED)

Financial assets and financial liabilities where disclosure at fair value is required

(DKK million)	Fair value hierarchy at 31 December 2018			
	Level 1	Level 2	Level 3	Total
Financial assets				
Measured at fair value				
Government and mortgage bonds	3,831	-	-	3,831
Equities	7,210	-	-	7,210
Credit	4,968	-	-	4,968
Alternatives	826	231	-	1,057
Other financial assets	-	32	-	32
Derivative instruments	-	22	-	22
Total	**16,835**	**285**	**-**	**17,120**
Financial liabilities				
Amortised cost, disclosure of fair value				
Bank loans	-	1,014	-	1,014
Measured at fair value				-
Derivative instruments	-	61	-	61
Total	**-**	**1,075**	**-**	**1,075**

	Fair value hierarchy at 31 December 2017			
	Level 1	Level 2	Level 3	Total
Financial assets				
Measured at fair value				
Government and mortgage bonds	9,572	-	-	9,572
Equities	3,278	-	-	3,278
Credit	4,441	-	-	4,441
Alternatives	327	-	-	327
Other financial assets	-	87	-	87
Derivative instruments	-	9	-	9
Total	**17,618**	**96**	**-**	**17,714**
Financial liabilities				
Amortised cost, disclosure of fair value				
Bank loans	-	1,503	-	1,503
Measured at fair value				
Derivative instruments	-	8	-	8
Total	**-**	**1,511**	**-**	**1,511**

NOTE 12 DEFERRED TAX

Accounting policies
Deferred tax is recognised on all temporary differences between the carrying amounts of assets and liabilities and their tax bases, except for temporary differences arising on initial recognition of a transaction that is not a business combination and where the temporary difference ascertained at the time of initial recognition affects neither the financial result nor the taxable income.

Deferred tax is measured on the basis of the income tax rates and tax rules in force in the respective countries on the balance sheet date. Change in deferred tax as a result of changed income tax rates or tax rules is recognised in the income statement. Deferred tax assets, including the tax value of tax loss carryforwards, are recognised in the balance sheet at the value at which the assets are expected to be realised.

Key accounting estimates and judgements
Executive Management's estimate of future income based on budgets, forecasts, business plans and initiatives scheduled for the coming years supports the utilisation of the deferred tax assets within the foreseeable future.

The Group operates in a multinational tax environment. Complying with tax rules can be complex, as the interpretation of legislation and case law may not always be clear or may change over time. Transfer pricing disputes with the tax authorities may occur. Executive Management exercises judgement to assess the possible effect of exposures and the possible outcome of disputes or interpretational uncertainties.

NOTE 12 DEFERRED TAX (CONTINUED)

(DKK million)	Balance at 1 January	Reclassification	Effect of foreign currency exchange differences	Adjustment of deferred tax at beginning of year	Movements during the year	Balance at 31 December
2018						
Intangible assets	176	-	1	(1)	125	51
Property, plant and equipment	18	-	1	4	22	45
Inventories	543	-	-	-	27	570
Provisions	(203)	-	2	(12)	302	89
Other items	105	-	(2)	(21)	(25)	57
Tax loss carryforwards, etc.	8	-	-	-	(5)	3
Valuation allowance	-	-	-	-	(146)	(146)
Deferred tax assets/ (liabilities)	**647**	**-**	**2**	**(30)**	**50**	**669**
Deferred tax assets	667	-	2	(30)	34	673
Deferred tax liabilities	(20)	-	-	-	16	(4)
Deferred tax assets/ (liabilities)	**647**	**-**	**2**	**(30)**	**50**	**669**
2017						
Intangible assets	29	-	-	(1)	148	176
Property, plant and equipment	(2)	-	-	(1)	21	18
Inventories	599	-	(1)	-	(55)	543
Provisions	98	-	-	-	(301)	(203)
Other items	314	-	(6)	(15)	(188)	105
Tax loss carryforwards, etc.	-	-	(1)	-	9	8
Deferred tax assets/ (liabilities)	**1,038**	**-**	**(8)**	**(17)**	**(366)**	**647**
Deferred tax assets	1,038	-	(8)	(17)	(346)	667
Deferred tax liabilities	-	-	-	-	(20)	(20)
Deferred tax assets/ (liabilities)	**1,038**	**-**	**(8)**	**(17)**	**(366)**	**647**

NOTE 13 INVENTORIES

Accounting policies
Inventories are measured at the lower of standard cost under the FIFO method and net realisable value.

Finished goods and work in progress comprise the cost of raw materials, consumables, direct labour and indirect production costs. Indirect production costs comprise indirect consumables and labour as well as maintenance and depreciation of the machinery, factory buildings and equipment used in the manufacturing process, and costs of factory administration and management. If the expected sales price is lower than the carrying amount, a write -down is recognised.

The net realisable value of inventories is calculated as sales price less costs of completion and expenses incurred to effect the sale, and is determined allowing for marketability, obsolescence and development in expected sales price.

Obsolete goods, including slow-moving goods, are written down.

Key accounting estimates and judgements
Executive Management performs a yearly assessment of whether the standard cost of inventories is at approximately the same level as the actual costs. The standard cost is adjusted if there are significant deviations.

Indirect production costs are calculated on the basis of relevant assumptions as to capacity utilisation, production time and other relevant factors, and allocated based on the normal production capacity.

(DKK million)	2018	2017
Raw materials and consumables	169	166
Work in progress	864	932
Finished goods and goods for resale	696	621
Total	**1,729**	**1,719**
Write-down for the year	72	76
Cost of goods sold included in Cost of sales	2,466	2,295

NOTE 14 TRADE RECEIVABLES

Accounting policies
Trade receivables are recognised initially at their transaction price and subsequently measured at amortised cost, which usually corresponds to the nominal value less lifetime expected credit losses. The expected credit losses on trade receivables are estimated using a provision matrix with reference to past default experience of the debtor and an analysis of the debtor's current financial position, adjusted for general economic conditions in the market in which the debtor operates. The Group recognises a loss allowance for expected credit losses and writes off trade receivables if there is information indicating that the debtor is in severe financial difficulty and there is no realistic prospect of recovery. The amount of write-downs is recognised in the Income statement under Sales and distribution costs. Subsequent recoveries of amounts previously written down are credited against Sales and distribution costs.

(DKK million)	2018	2017	2016
Trade receivables	3,273	2,716	2,600
Write-downs	(44)	(72)	(85)
Total	**3,229**	**2,644**	**2,515**

Write-downs have decreased by DKK 28 million compared to 2017. The decrease is related to (1) a total realised loss of DKK 16 million for customers in El Salvador, Uruguay and Peru on conclusions of legal proceedings, and (2) an increased focus on dunning processes and customer collections equal to DKK 12 million.

Previous bad debt provisions have been reversed, with customers in Chile, Mexico, Panama and Greece representing the largest share.

The following table details the risk profile of trade receivables based on the Group's provision matrix. The Group's historical credit losses do not show different patterns for different customer segments.

(DKK million)	Not past due	Overdue by 3 months	Overdue by 3-6 months	Overdue by 6-12 months	Overdue by more than 12 months	Total
31 December 2018						
Expected credit loss rate	0%	0%	0%	36%	66%	
Trade receivables	2,899	204	89	30	51	3,273
Lifetime expected credit losses	0	0	0	11	33	44
31 December 2017						
Expected credit loss rate	0%	2%	4%	75%	61%	
Trade receivables	2,257	269	90	8	92	2,716
Lifetime expected credit losses	1	5	4	6	56	72

NOTE 15 FOUNDATION CAPITAL

The nominal value of the Foundation capital amounts to DKK 98 million (2017: DKK 98 million).

In December 2017, the LEO Pharma Research Foundation was consolidated with the LEO Foundation with financial effect from 1 January 2017.

As a result of the consolidation, the LEO Foundation's registered capital increased by DKK 46 million.

NOTE 16 RETIREMENT BENEFIT OBLIGATIONS

Accounting policies

Defined contribution plans

Payments to defined contribution plans are recognised in the income statement in the period to which they relate, and any amounts payable are recognised in Other payables in the balance sheet.

Defined benefit plans

Where defined benefit plans are concerned, an annual actuarial calculation is made of the present value of future payments under the scheme. The present value is calculated based on assumptions relating to future developments in salary, interest rates, inflation, mortality and other factors. Present value is calculated only for the benefits to which the employees have earned a right through their employment with the Group. Plan assets are recognised to the extent the Group is able to obtain future economic benefits in the form of reimbursement from the pension scheme or reduction of future payments.

Pension costs for the year are recognised in the income statement based on actuarial estimates and financial expectations at the beginning of the year.

Any differences between expected developments in plan assets and defined benefit obligations on the one hand and the realised values calculated at the beginning of the year on the other are considered actuarial gains or losses. Actuarial gains and losses are recognised in Other comprehensive income. Past service costs are recognised in the income statement as incurred.

Defined contribution plans

The Group operates a number of defined contribution plans throughout the world. These plans are externally funded in entities that are legally separate from the Group.

Defined benefit plans

In a few countries, the Group operates defined benefit plans. The most significant of these are in Ireland, the UK and France. The defined benefit plans expose the Group to actuarial risks, such as longevity, interest rate, salary, market and currency risks.

The plans in Ireland and the UK are funded and constituted under a trust whose assets are legally separated from those of the Group. Under the scheme-funding regime introduced by the UK Pensions Act 2004, the trustees are required to carry out regular scheme-funding valuations for the plans and establish a schedule of contributions and a recovery plan when there is a shortfall in the plan. The plans entitle the employees to an annual pension on retirement, based on length of service and salary level up to retirement.

The plan in France is funded and covered by an insurance contract whose assets are legally separated from those of the Group. The plan is defined by the collective agreement of "Pharmacie; Industrie" and covers all employees, who are entitled to a lump-sum payment on retirement, based on length of service and salary level up to retirement.

Enhanced transfer value in Ireland

In 2017, employees in Ireland were offered an enhanced transfer value (ETV), which was exercised and carried out during the year. The ETV resulted in a net settlement gain of DKK 98 million, recognised under Other operating income..

NOTE 16 RETIREMENT BENEFIT OBLIGATIONS (CONTINUED)

(DKK million)	2018	2017
Present value of defined benefit plans		
Present value of defined benefit plans at 1 January	1,773	2,374
Effect of exchange rate adjustment	-	(24)
Current service costs	6	7
(Gains)/losses on settlements	-	(111)
Interest costs	39	50
Actuarial (gains)/losses from changes in demographic assumptions	(4)	(1)
Actuarial (gains)/losses from changes in financial assumptions	(126)	(38)
Experience adjustments	(12)	(30)
Settlement payments from plan assets	-	(251)
Settlement payments from employer	-	(117)
Benefits paid to employees	(51)	(70)
Past service costs	3	-
Other	-	(16)
Present value of defined benefit plans at 31 December	**1,628**	**1,773**
Fair value of plan assets		
Fair value of plan assets at 1 January	1,418	1,594
Effect of exchange rate adjustment	-	(19)
Return on plan assets	(82)	62
Interest income	33	35
Benefits paid to employees	(51)	(70)
Settlement payments from plan assets	-	(251)
Employer contributions	67	67
Fair value of plan assets at 31 December	**1,385**	**1,418**
Net retirement benefit obligations at 31 December	**243**	**355**

Sensitivity analysis

The discount rate is the most significant assumption used in the calculation of the obligation for defined benefit plans. The sensitivity analysis indicates what the development in the obligation would be as a result of a change in the individual assumptions. However, the assumptions will most likely be correlated and consequently result in a different obligation.

A 0.25% decrease in the discount rate would result in an increase in the obligation of approximately DKK 3 million in France and DKK 43 million in Ireland and vice versa. A 0.1% decrease in the discount rate would result in an increase of approximately DKK 12 million in the UK and vice versa.

(DKK million)	2018	2017
Specification of amount recognised in the statement of comprehensive income		
Actuarial (gains)/losses	(60)	(131)
Total	**(60)**	**(131)**

NOTE 17 PROVISIONS

Accounting policies
Provisions are recognised when, as a result of events before or at the balance sheet date, the Group has a legal or a constructive obligation, it is probable that there may be an outflow of economic resources to settle the obligation and the obligation can be measured reliably. Provisions are measured as the best estimate of the costs required to settle the liabilities at the balance sheet date.

Provisions for sales deductions and returns are recognised at the time the related revenues are recognised. Unsettled deductions and returns are recognised as Provisions when the timing or amount is uncertain. Where absolute amounts are known, the deductions are recognised as Other liabilities.

Staff-related provisions include employee benefits such as long-term incentive programmes and long-service awards as well as provisions for restructuring. Provisions for restructuring are made only for liabilities set out in a specific restructuring plan, either by starting to implement the plan or announcing its main components.

Other provisions consist of different types of other provisions, including provisions for legal disputes and other restructuring provisions.

Key accounting estimates and judgements
Provisions for legal disputes
Provisions for legal disputes consist of various types of provisions linked to ongoing legal disputes. Executive Management makes judgements about provisions and contingencies, including the probability of pending and potential future litigation outcomes, which, by their very nature, are dependent on inherently uncertain future events. When determining likely outcomes of litigations, etc., Executive Management considers the input of external counsels on each case, as well as known outcomes in case law.

Although Executive Management believes that the total provisions for legal proceedings are adequate based on currently available information, there can be no assurance that there will not be any changes in facts or matters, or that any future lawsuits, claims, proceedings or investigations will not be material.

Provisions for sales deductions
Sales discounts and rebates are predominantly issued in the US in connection with the US Federal and State Government Healthcare programmes, primarily commercial rebates, Copay schemes, Medicare and Medicaid.

Executive Management's estimate of sales discounts and rebates is based on a calculation which includes a combination of historical utilisation data and expectations in relation to the development in sales and utilisation. Specific circumstances regarding the different programmes are also considered. The obligations for discounts and rebates are incurred at the time the sale is recorded. However, the actual discount or rebate related to a specific sale may be invoiced six to nine months later.

The Group considers the provisions established for sales discounts and rebates to be reasonable and appropriate based on currently available information. However, the actual amount of discounts and rebates may differ from the amounts estimated by Executive Management as more detailed information becomes available.

NOTE 17 PROVISIONS (CONTINUED)

(DKK million)	Sales deductions	Product returns	Staff-related provisions	Other provisions	Total
2018					
Provisions at 1 January 2018	452	162	152	77	843
Exchange rate adjustment	17	5	(5)	3	20
Additional provisions	1,547	126	130	66	1,869
Used during the year	(1,315)	(73)	(110)	(26)	(1,524)
Reversed during the year	(92)	(12)	(7)	(21)	(132)
Provisions at 31 December 2018	**609**	**208**	**160**	**99**	**1,076**
Provisions are recognised in the balance sheet as					
Non-current liabilities	-	112	40	82	234
Current liabilities	609	96	120	17	842
Provisions at 31 December 2018	**609**	**208**	**160**	**99**	**1,076**
2017					
Provisions at 1 January 2017	460	208	237	49	954
Exchange rate adjustment	(48)	(21)	(5)	(1)	(75)
Additional provisions	1,123	88	60	34	1,305
Used during the year	(929)	(109)	(116)	(5)	(1,159)
Reversed during the year	(154)	(4)	(24)	-	(182)
Provisions at 31 December 2017	**452**	**162**	**152**	**77**	**843**
Provisions are recognised in the balance sheet as					
Non-current liabilities	-	121	36	13	170
Current liabilities	452	41	116	64	673
Provisions at 31 December 2017	**452**	**162**	**152**	**77**	**843**

NOTE 18 OTHER ADJUSTMENTS

(DKK million)	2018	2017
Inventory write-down	(43)	(20)
Provision for bad debt	(27)	(14)
Other	4	84
Total	**(66)**	**50**

NOTE 19 CONTRACTUAL OBLIGATIONS

Operating lease obligation
The Group has operating lease obligations of DKK 441 million (2017: DKK 328 million). The obligations are primarily related to company cars and office premises.

(DKK million)	2018	2017
Minimum operating lease payments are as follows:		
Within one year	140	110
Between one and five years	260	170
After five years	41	48
Total	**441**	**328**
Rental and lease expenses recognised in the income statement	150	148

NOTE 20 CONTINGENCIES

Guarantees and commitments
The total guarantee commitment for the LEO Group amounts to DKK 7,041 million at 31 December 2018 (2017: DKK 1,959 million).

At 31 December 2018, the guarantee commitment comprise mainly guarantees relating to acquisitions of DKK 5,004 million, to loans DKK 1,412 million (2017: DKK1,488 million) and to pension commitments of DKK 559 million (2017: DKK 309 million).

Pending lawsuits
At the end of 2018, there were pending patent lawsuits filed by and against the Group concerning rights related to products in the Group's psoriasis portfolio in both the US and Europe. The Group does not expect the pending cases to have any significant effect on the Group's financial position.

Tax
As a global business, the Group will from time to time have tax audits and tax discussions with tax authorities in various countries regarding transfer pricing issues. Executive Management is of the opinion that current tax audits and tax discussions will have no significant impact on the the Group's financial position.

(DKK million)	2018	2017
Contracted but not provided for in the financial statements:		
Intangible assets	6,283	1,432
Property, plant and equipment	456	-
Other current assets	373	-
Total	**7,112**	**1,432**

The commitments related to intangible assets comprise both intellectual property rights from acquisitions and milestone payments relating to development of new products. DKK 4,297 million of the total commitment comprises fixed contractual obligations. The remaining commitments relate to agreements, which include certain milestone payments that the Group is committed to paying upon achievement. The amounts are not risk-adjusted or discounted. In addition to the above, there are certain commercial milestone payments that depend on future sales.

The Group has commitments related to financial investments of DKK 596 million.

NOTE 21 RELATED PARTIES

The LEO Group's related parties comprise:
- The associates, Skinvision B.V. and PellePharm Inc.
- Members of the LEO Foundation's Board of Trustees and Executive Board as well as close relatives of these persons.
- Companies in which the Board of Trustees and Executive Board have a controlling influence.

Transactions and balances with associates in 2018 were as follows:
- Loan and interest have been converted to investment in the company, in total DKK 9.7 million (2017: DKK 9.3 million)
- Capital transactions from LEO Pharma A/S amounts to total DKK 144 million (2017: DKK 0 million).

There have been no transactions with the Board of Trustees or Executive Board besides remuneration. For information on remuneration, please refer to note 3.

Transactions and balances with LEO Pharma A/S in 2018 were as follows:
- Loan of DKK 1,000 million (2017: DKK 1,000 million)
- Dividend payment from LEO Pharma A/S of DKK 150 million (2017: DKK 1,000 million)
- Receivables of DKK 0.2 million (2017: receivables of DKK 150 million) and payables of DKK 0.2 million (2017: payables of DKK 2 million)
- Interest income of DKK 24 million (2017: DKK 2 million).

Transactions and balances with LEO Holding A/S in 2018 were as follows:
- Loan of DKK 130 million (2017: DKK 0 million)
- Receivables of DKK 0.8 million (2017: DKK 0 million)

NOTE 22 EVENTS AFTER THE BALANCE SHEET DATE

No events have occurred in the period from the balance sheet date until the presentation of the Financial Statements that materially affect the assessment of the Annual Report.

NOTE 23 COMPANIES IN THE LEO GROUP

(DKK million)	Country	Share of ownership, %	Activities
Parent Company			
The LEO Foundation	Denmark		Other
Subsidiaries			
SARL LEO Pharma	Algeria	100	Sales services
LEO Pharma Southport Pty Ltd	Australia	100	Production
LEO Pharma Pty Ltd	Australia	100	Sales and distribution
LEO Pharma GmbH	Austria	100	Sales and distribution
LEO Pharma NV	Belgium	100	Sales and distribution
LEO Pharma LTDA.	Brazil	100	Sales and distribution
LEO Pharma Inc.	Canada	100	Sales and distribution
LEO Pharma Consultancy Company Ltd.	China	100	Sales services
LEO Pharma Trading Company Ltd.	China	100	Sales and distribution
LEO Pharma s.r.o.	Czech Republic	100	Sales services
LEO Holding A/S	Denmark	100	Other
LEO Pharma A/S	Denmark	100	Sales and distribution, Production
Løvens Kemiske Fabriks Handelsaktieselskab	Denmark	100	Other
LEO Pharma OY	Finland	100	Sales and distribution
Laboratoires LEO S.A.	France	100	Sales and distribution, Production
LEO Pharma GmbH	Germany	100	Sales and distribution
LEO Pharmaceutical Hellas S.A.	Greece	100	Sales and distribution
LEO Laboratories Ltd.	Ireland	100	Sales and distribution, Production
Wexport Ltd.	Ireland	100	Production
LEO Pharma Holding Ltd.	Ireland	100	Other
LEO Pharma S.p.A.	Italy	100	Sales and distribution
LEO Pharma K.K.	Japan	100	Sales and distribution
LEO Pharmaceuticals, S. de R.L. de C.V.	Mexico	100	Sales services

NOTE 23 COMPANIES IN THE LEO GROUP (CONTINUED)

(DKK million)	Country	Share of ownership, %	Activities
LEO Pharma LLC	Morocco	100	Sales services
LEO Pharma BV	Netherlands	100	Sales and distribution
LEO Pharma Ltd.	New Zealand	100	Sales and distribution
LEO Pharma AS	Norway	100	Sales and distribution
LEO Pharma Sp. z o.o.	Poland	100	Sales services
LEO Farmacêuticos Lda.	Portugal	100	Sales and distribution
LEO Pharmaceutical Products LLC	Russia	100	Sales and distribution
LEO Pharma Asia PTE Ltd.	Singapore	100	Sales services
LEO Pharma Ltd	South Korea	100	Sales and distribution
Laboratorios LEO Pharma S.A.	Spain	100	Sales and distribution
LEO Pharma AB	Sweden	100	Sales and distribution
LEO Pharmaceutical Products Sarath Ltd.	Switzerland	100	Sales and distribution
LEO Pharma SARL	Tunisia	100	Sales services
LEO Pharma İlaç Ticaret Anonim Şirketi	Turkey	100	Sales and distribution
LEO Laboratories Ltd.	United Kingdom	100	Sales and distribution
LEO Pharma Inc.	USA	100	Sales and distribution
LEO Spiny Merger Sub Inc.	USA	100	Other
LEO US Holding Inc.	USA	100	Other
Associate			
PellePharm Inc.	USA	16.75	
SkinVision B.V.	Netherlands	26.32	

Sales and distribution
Production
Sales services
Other

Financial Statements – LEO Foundation

Financial Statements

Notes

Income statement

(DKK million)	Note	2018	2017
Administrative costs	1, 2	(16)	(17)
Operating profit		**(16)**	**(17)**
Income from investments in subsidiaries	7	667	1,383
Financial income	3	24	4
Profit before tax		**675**	**1,370**
Tax on profit for the year	4	3	13
Net profit for the year	5	**678**	**1,383**

Balance sheet at 31 December

ASSETS

(DKK million)	Note	2018	2017
Intangible and tangible fixed assets	6	1	-
Investments in subsidiaries	7	26,132	25,467
Receivables from LEO Pharma A/S		1,000	1,002
Total financial fixed assets		**27,132**	**26,469**
Total fixed assets		**27,133**	**26,469**
Receivables from subsidiaries		131	148
Other receivables		1	2
Total receivables		**132**	**150**
Cash at bank and in hand		**44**	**67**
Total current assets		**176**	**217**
TOTAL ASSETS		**27,309**	**26,686**

EQUITY AND LIABILITIES

(DKK million)	Note	2018	2017
Foundation capital	8	98	98
Net revaluation, subsidiaries		26,032	25,367
Reserve for future grants		104	83
Retained earnings		681	990
Total equity		**26,915**	**26,538**
Deferred tax liabilities	9	3	6
Total provisions		**3**	**6**
Grants payable	10	306	77
Total non-current liabilities		**306**	**77**
Grants payable	10	80	59
Other payables		5	6
Total current liabilities		**85**	**65**
TOTAL EQUITY AND LIABILITIES		**27,309**	**26,686**

Statement of changes in equity

(DKK million)	Foundation capital	Net revaluations, subsidiaries	Reserve for future grants	Retained earnings	Total
2018					
Equity at 1 January 2018	98	25,367	83	990	26,538
Profit/(loss) in the LEO Foundation	-	667	100	(89)	678
Additions	-	-	220	(220)	-
Other adjustments in subsidiaries	-	(2)	-	-	(2)
Grants for the year	-	-	(299)	-	(299)
Equity at 31 December 2018	**98**	**26,032**	**104**	**681**	**26,915**
2017					
Equity at 1 January 2017	52	24,625	47	389	25,113
Profit/(loss) in the LEO Foundation	-	233	80	1,070	1,383
Additions	46	-	-	-	46
Other adjustments in subsidiaries	-	509	-	(469)	40
Grants for the year	-		(44)	-	(44)
Equity at 31 December 2017	**98**	**25,367**	**83**	**990**	**26,538**

Notes LEO Foundation

NOTE 1 AUDIT FEES

(DKK thousand)	2018	2017
Fees to auditors appointed at the Board meeting		
Statutory audit	110	110
Other services	4	307
Total	**114**	**417**

NOTE 2 STAFF EXPENSES

(DKK million)	2018	2017
Wages and salaries	9	8
Total	**9**	**8**
Included in		
Administrative costs	9	8
Total	**9**	**8**
Remuneration to the Board of Trustees from other Group companies	3	1

Remuneration to the Board of Trustees amounted to DKK 2.2 million (2017: DKK 4.1 million) and the fee to the administrator, LEO Pharma A/S, amounted to DKK 0.2 million (2017: DKK 2.1 million).

Average number of full-time employees	6	2

For a specification of the remuneration to the Board of Trustees and Executive Board, refer to note 3 to the Consolidated Financial Statements.

NOTE 3 FINANCIAL INCOME

(DKK million)	2018	2017
Interest income from subsidiaries	24	2
Other financial income	-	2
Total	**24**	**4**

NOTE 4 TAX ON PROFIT FOR THE YEAR

(DKK million)	2018	2017
Change in deferred tax	3	13
Total	**3**	**13**

NOTE 5 PROPOSED DISTRIBUTION OF NET PROFIT FOR THE YEAR

(DKK million)	2018	2017
Net revaluation for the year	667	233
Proposed grant limit for the following year	100	80
Retained earnings	(89)	1,070
Total	**678**	**1,383**

NOTE 6 FIXED ASSETS

(DKK thousand)	Leasehold improve-ments	Other fix-tures and fittings, tools and equipment	Total tangible assets	Software	Total intangible assets	Total fixed assets
Cost at 1 January 2018	-	-	-	-	-	-
Additions during the year	83	1,266	1,349	247	247	1,596
Cost at 31 December 2018	**83**	**1,266**	**1,349**	**247**	**247**	**1,596**
Depreciation and amortisation at 1 January 2018	-	-	-	-	-	-
Depreciation and amortisation for the year	(16)	(232)	(248)	(54)	(54)	(302)
Depreciation and amortisation at 31 December 2018	**(16)**	**(232)**	**(248)**	**(54)**	**(54)**	**(302)**
Carrying amount at 31 december 2018	**67**	**1,034**	**1,101**	**193**	**193**	**1,294**

NOTE 7 INVESTMENTS IN SUBSIDIARIES

(DKK million)	2018	2017
Cost at 1 January	100	569
Divestments	-	(569)
Additions	-	100
Cost at 31 December	**100**	**100**
Value adjustment at 1 January	25,367	24,625
Share of profit/(loss) for the year	667	1,383
Dividend	-	(1,150)
Exchange rate adjustment	(41)	(64)
Adjustment of financial instruments	(25)	5
Tax on changes in equity	5	(49)
Other movements	59	617
Value adjustment at 31 December	**26,032**	**25,367**
Carrying amount at 31 December	**26,132**	**25,467**

For a list of all subsidiaries in the LEO Group, please refer to note 23 to the Consolidated Financial Statements.

NOTE 8 FOUNDATION CAPITAL

The nominal value of the Foundation capital is DKK 98 million (2017: DKK 98 million).

In December 2017, the LEO Pharma Research Foundation was consolidated with the LEO Foundation with financial effect from 1 January 2017. As a result of the consolidation, the LEO Foundation's registered capital increased by DKK 46 million.

NOTE 9 DEFERRED TAX

(DKK million)	2018	2017
Deferred tax assets/(liabilities) at 1 January	6	19
Deferred tax on profit/(loss) for the year	(3)	(13)
Deferred tax assets/(liabilities) at 31 December	**3**	**6**

NOTE 10 GRANTS PAYABLE

(DKK million)	2018	2017
Grants payable fall due		
Within one year	80	59
Between one and five years	169	65
After more than five years	137	12
Grants payable	**386**	**136**

NOTE 11 CONTINGENCIES

The LEO Foundation has lease obligations of DKK 6 million (2017: DKK 7 million).

The LEO Foundation has no guarantee commitments or pledges.

NOTE 12 RELATED PARTIES

The LEO Foundation's related parties with significant influence comprise the LEO Foundation's Board of Trustees and Executive Board, LEO Holding A/S, and LEO Pharma A/S and its subsidiaries.

For information regarding remuneration to the Board of Trustees and administrative costs, please refer to note 2.

The LEO Foundation has provided a loan to LEO Pharma A/S of DKK 1,000 million (2017: DKK 1,000 million). The loan is granted on an arm's length basis at an interest rate of 2.45% and will be repaid in 2027.

Balances with LEO Pharma A/S comprise receivables of DKK 0 million (2017: receivables of DKK 148 million), and with LEO Holding A/S a receivable of DKK 131 million. The LEO Foundation has no other transactions with related parties.

NOTE 13 EVENTS AFTER THE BALANCE SHEET DATE

No events have occurred in the period from the balance sheet date until the presentation of the Financial Statements that materially affect the assessment of the Annual Report.

NOTE 14 ACCOUNTING POLICIES

Accounting policies
The Financial Statements of the Parent Company, the LEO Foundation, for 2018 have been prepared in accordance with the provisions of the Danish Financial Statements Act applying to large enterprises of reporting class C.

The accounting policies are unchanged from the previous year.

The Parent Company's accounting policies for recognition and measurement are consistent with the policies of the Consolidated Financial Statements with the exceptions stated below.

Cash flow statement
In accordance with the exemption clause in section 86(4) of the Danish Financial Statements Act, no separate cash flow statement has been prepared for the Parent Company.

Investments in subsidiaries
Investments in subsidiaries are measured under the equity method. This means that the subsidiaries are measured in the balance sheet at the proportionate share of their net asset value, with deduction or addition of unrealised intercompany profits or losses, and with addition of any remaining value of positive differences (goodwill) and deduction of any remaining value of negative differences (negative goodwill). The Parent Company's share of the subsidiaries' profit for the year is recognised in the income statement less unrealised intercompany profits.

The total net revaluation of investments in affiliates is transferred upon distribution of profit to Reserve for net revaluation under the equity method under equity. The reserve is reduced by dividends distributed to the Parent Company and adjusted for other equity movements in subsidiaries.

Management Statement

The Executive Board and the Board of Trustees have today considered and adopted the Annual Report of the LEO Foundation for the financial year 1 January – 31 December 2018.

The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards as endorsed by the EU, and the Financial Statements of the Parent Company and the Management Review have been prepared in accordance with the Danish Financial Statements Act.

In our opinion, the Consolidated Financial Statements and the Financial Statements of the Parent Company give a true and fair view of the financial position as at 31 December 2018 of the Group and the Parent Company, and the results of the Group and the Parent Company's operations and consolidated cash flows for 2018.

In our opinion, the Management Review gives a true and fair view of the matters addressed in the Review. We recommend that the Annual Report be adopted at the Board meeting.

Copenhagen, 27 February 2019

EXECUTIVE BOARD:

Jesper Mailind
CEO

BOARD OF TRUSTEES:

Lars Olsen
Chairman

Jens Bo Olesen
Vice Chairman

Ingelise Saunders

Lars Kjøller

Jannie Kogsbøll

John Carsten Mehlbye

Eivind Drachmann Kolding

Peter Schwarz

Allan Carsten Dahl

Cristina Patricia Lage

Lotte Hjortshøj Larsen

Independent auditor's report

TO THE BOARD OF TRUSTEES OF LEO FONDET

Opinion
We have audited the Consolidated Financial Statements and the Parent Financial Statements for LEO Fondet for the financial year 01.01.2018 - 1.12.2018, which comprise the income statement, balance sheet, statement of changes in equity and notes, including a summary of significant accounting policies, for the Group as well as the Parent, and the statement of comprehensive income and the cash flow statement of the Group. The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards as adopted by the EU and additional requirements of the Danish Financial Statements Act, and the Parent Financial Statements have been prepared in accordance with the Danish Financial Statements Act.

In our opinion, the Consolidated Financial Statements give a true and fair view of the Group's financial position at 31.12.2018, and of the results of its operations and cash flows for the financial year 01.01.2018 - 31.12.2018 in accordance with International Financial Reporting Standards as adopted by the EU and additional requirements under the Danish Financial Statements Act.

Further, in our opinion, the Parent Financial Statements give a true and fair view of the Parent's financial position at 31.12.2018, and of the results of its operations for the financial year 01.01.2018 - 31.12.2018 in accordance with the Danish Financial Statements Act.

Basis for opinion
We conducted our audit in accordance with International Standards on Auditing (ISAs) and the additional requirements applicable in Denmark. Our responsibilities under those standards and requirements are further described in the Auditor's responsibilities for the audit of the Consolidated Financial Statements and the Parent Financial Statements section of this auditor's report. We are independent of the Group in accordance with the International Ethics Standards Board of Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the additional requirements applicable in Denmark, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Statement on the Management Review
Management is responsible for the Management Review.

Our opinion on the Consolidated Financial Statements and the Parent Financial Statements does not cover the Management Review, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the Consolidated Financial Statements and the Parent Financial Statements, our responsibility is to read the Management Review and, in doing so, consider whether the Management Review is materially inconsistent with the Consolidated Financial Statements and the Parent Financial Statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

Moreover, it is our responsibility to consider whether the Management Review provides the information required under the Danish Financial Statements Act.

Based on the work we have performed, we conclude that the Management Review is in accordance with the Consolidated Financial Statements and the Parent Financial Statements and has been prepared in accordance with the requirements of the Danish Financial Statements Act. We did not identify any material misstatement in the Management Review.

Management's responsibilities for the Consolidated Financial Statements and the Parent Financial Statements
Management is responsible for the preparation of Consolidated Financial Statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the EU and additional requirements of the Danish Financial Statements Act as well as the preparation of Parent Financial Statements that give a true and fair view in accordance with the Danish Financial Statements Act, and for such internal control as Management determines is necessary to enable the preparation of Consolidated Financial Statements and Parent Financial Statements that are free from material misstatement, whether due to fraud or error.

In preparing the Consolidated Financial Statements and the Parent Financial Statements, Management is responsible for assessing the Group's and the Parent's ability to continue as a going concern, for disclosing, as applicable, matters related to going concern, and for using the going concern basis of accounting in preparing the Consolidated Financial Statements and the Parent Financial Statements unless Management either intends to liquidate the Group or the entity or to cease operations, or has no realistic alternative but to do so.

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

As part of an audit conducted in accordance with ISAs and the additional requirements applicable in Denmark, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

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

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

Copenhagen, 27 February 2019

Deloitte
Statsautoriseret Revisionspartnerselskab
Business Registration No 33 96 35 56

Erik Holst Jørgensen
State Authorised Public Accountant
MNE no. 9943

Kirsten Aaskov Mikkelsen
State Authorised Public Accountant
MNE no. 21358

Foundation information

LEO Foundation
LEO Fondet
Lautrupsgade 7, 5.
DK-2100 Copenhagen
Denmark

CVR no.: 11 62 33 36

Financial year:
1 January – 31 December

Executive Board
Jesper Mailind, CEO

Board of Trustees
Lars Olsen, Chairman
Jens Bo Olesen, Vice Chairman
Ingelise Saunders
John Carsten Mehlbye
Eivind Drachmann Kolding
Peter Schwarz
Lars Kjøller
Jannie Kogsbøll
Allan Carsten Dahl
Cristina Patricia Lage
Lotte Hjortshøj Larsen

Auditors
Deloitte
Statsautoriseret
Revisionspartnerselskab

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CVR no. 11623336
Presented and adopted at the Annual Meeting on 27 February 2019