Mereo BioPharma Group plc
("Mereo" or the "Company" or the "Group")

Preliminary results for the year ended 31 December 2016
Continued significant progress on all programmes

London, 27 February 2017 – Mereo BioPharma Group plc (AIM: MPH), a clinical stage, UK-based, biopharmaceutical company focused on rare and specialty diseases, is pleased to announce its audited preliminary results for the year ended 31 December 2016.

Operational Highlights

- Phase 2 dose-ranging study initiated with acumapimod (BCT-197) for treatment of the underlying inflammation in patients with acute exacerbations of COPD in H1 2016
- Phase 2b dose-confirmation study initiated with BGS-649 for the treatment of hypogonadotropic hypogonadism in obese men in H1 2016 and a six month safety extension study was initiated in Q4 2016. The Group is on track to report interim analysis in March 2017
- Obtained Orphan Drug Designation in the US and the EU for BPS-804 as a treatment for osteogenesis imperfecta
- Positive Phase 1 drug-drug interaction study with acumapimod and azithromycin
- Strengthened intellectual property across the portfolio

Financial Highlights

- Admitted to the AIM market of the London Stock Exchange on 9 June 2016 following a private placement raising a further £14.8 million of capital in addition to the £56.5 million drawn down earlier in the year from the previous financing round bringing the total raised since July 2015 to £91.3 million
- Balance sheet remains strong, with cash and cash equivalents balance at 31 December 2016 of £53.6 million

Post period highlight

- Three abstracts accepted for presentation as posters at the American Thoracic Society May 2017
- BPS-804 accepted for EMA Adaptive Pathways programme, potentially enabling earlier patient access
- Richard Jones was appointed as Chief Financial Officer and we are also pleased to announce the appointment of Jerome Dauvergne as Head of Pharmaceutical Development

Dr Denise Scots-Knight, Chief Executive Officer of Mereo BioPharma Group plc commented:

"This year we have made significant progress on all three of our programmes with two now well advanced in the clinic and the third set to enter a pivotal study. We remain focused on executing against our strategy, delivering data on our current programmes and continuing to build our portfolio of differentiated, late stage products over time".

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About Mereo

Mereo is a UK-based biopharmaceutical company focused on the development of innovative medicines that aim to address unmet medical needs in rare and specialty disease areas and improve patient quality of life. The Company seeks to selectively acquire development-stage product candidates with demonstrated clinically meaningful data from large pharmaceutical companies and to rapidly progress these product candidates to subsequent value inflection points.

Mereo combines the operational discipline and efficiency of a small company with the financial resources to conduct comprehensive clinical studies. The Company has the option to directly commercialise products, for example in orphan diseases, in addition to partnering or divesting its products.

Mereo's initial portfolio consists of three mid-late stage clinical assets that were acquired from Novartis in July 2015. BPS-804 is being developed for the prevention of fractures resulting from osteogenesis imperfecta (brittle bone disease); acumapimod (BCT-197), is being developed to treat inflammation in patients with an AECOPD; and BGS-649 is a once-weekly pill to restore normal testosterone levels in men with hypogonadotropic hypogonadism.

In H1 2016 the Company initiated a Phase 2 study with acumapimod and a Phase 2b study with BGS-649. Mereo expects to commence the first pivotal trial for BPS-804 during H1 2017. Additional product opportunities, from a range of large pharmaceutical and biotechnology companies, are under active evaluation.

Current development activities

Acumapimod

In Q2 2016 we initiated a Phase 2 dose-ranging clinical trial for acumapimod in 270 AECOPD patients in the US and the EU to explore two different dosing regimens versus placebo (on top of standard of care). The study aims to demonstrate the most biologically active dose regime of acumapimod based on a primary end point of forced expiratory volume in one second (FEV1). Patients will be followed for 26 weeks after treatment to explore recurrence rates of AECOPD and number of hospitalisations. We also initiated and successfully completed a drug-drug interaction study for acumapimod with the antibiotic azithromycin in 16 healthy volunteers. This will allow acumapimod to be dosed in patients already being treated with azithromycin, an antibiotic routinely employed in this clinical indication.

BGS-649

In Q1 2016 we initiated a Phase 2b clinical study for BGS-649 in 260 hypogonadotropic hypogonadism (HH) patients to determine the lowest effective dose of the once-weekly pill. This study is comparing three doses of BGS-649 with placebo. The primary objective of this study is to demonstrate the efficacy of BGS-649 to normalise total testosterone levels in greater than 75% of subjects after 24 weeks of treatment. We are also assessing patient recorded outcomes and determining the impact of BGS-649 on luteinising hormone (LH), follicle stimulating hormone (FSH) and semen parameters. In Q4 2016 we initiated a six-month Phase 2b extension study for BGS-649 to confirm the safety of long-term treatment. This study aims to enrol up to 50% of the patients (130) from the first BGS-649 study and will include monitoring of the testosterone levels and any changes in bone mineral density. The Group has announced that it will release the outcome of a blinded interim analysis in the Phase 2b study of BGS-649 by the Independent Data Monitoring Committee (IDMC) in March 2017.

BPS-804

During the year we obtained Orphan Drug Designation for BPS-804 in the US and the EU, which provides significant benefits for the product. Following submissions to and discussions with the regulators, we are progressing BPS-804 towards a potentially pivotal dose-ranging study in 120 patients with OI using a novel biomarker (HRpQCT). Post the period end, earlier this month BPS-804 was accepted to participate in the European Medicine Agency's (EMA) Adaptive Pathways programme. The adaptive pathway approach is part of the EMA's efforts to improve timely access for patients to new medicines, primarily in areas of high medical need. The pivotal Phase 2b study for BPS-804 in OI is expected to commence in H1 2017.

Chairman and Chief Executive Officer's statement
Introduction

The Group's strategy is to generate shareholder value by acquiring clinical stage products according to our exacting criteria, as an increasing number of pharmaceutical and biotechnology companies face R&D and financial challenges. We then seek to finance and develop such products to an optimum value inflection point. Patients benefit from this approach by having access to medicines that otherwise may remain underdeveloped by larger pharmaceutical companies.

The Group plans to build a broad and diverse portfolio of acquired orphan disease products and develop them through clinical studies to regulatory approval and then plans to commercialise them directly. Orphan disease products are an attractive opportunity for smaller companies to commercialise. Due to the lack of existing treatments, orphan drugs can be fast-tracked to the market and can involve smaller clinical trials, with lower development costs. The development of these products often involves close co-ordination with patient organisations and a limited number of treatment sites allowing for relatively easy identification of the patient population and therefore a small sales infrastructure.

For speciality products, the Group plans to partner or sell the product upon completion of additional clinical studies which may be for dose-ranging optimisation or, in certain cases, the Phase 3 studies required for product approval and registration.

By acquiring products with clinical efficacy and safety data the Group aims to reduce some of the development risks involved and to accelerate the availability of these drugs for patients. Such well characterised clinical-stage products will have received significant investment whilst being developed by major pharmaceutical companies.

Our product selection process has a clear set of criteria and typically means that we acquire products that already have compelling proof of concept data or a well-established scientific proof of mechanism in the disease indication we plan to pursue.

This is the case for the Group's initial portfolio, comprising of three products acquired from Novartis in 2015; acumapimod (BCT-197) for acute exacerbations of chronic obstructive pulmonary disease (AECOPD), BGS-649 for hypogonadotropic hypogonadism (HH) and BPS-804 for osteogenesis imperfecta (OI, also known as brittle bone disease). Each of these products was acquired with proof-of-concept data in the target clinical indication we intend to pursue.

Our acquisition structures are intended to align the interests of the Group and our shareholders with those of the pharmaceutical company through the use of equity and downstream payments based on success, rather than substantial upfront cash payments. Another key feature of our business model is the comprehensive nature of the clinical studies we undertake. These are designed to answer the key questions which are important to both patients and their physicians, as well as the regulators and payers.

Our values and our people

The Group has grown significantly over the past 18 months and we now employ over 20 full-time staff in our London headquarters. We seek to attract and retain highly experienced individuals in clinical development, clinical operations, manufacturing, intellectual property and quality assurance and support them with strong leadership at the executive and Board level. This internal expertise is leveraged with external organisations such as the clinical research organisation ICON and external contract manufacturers. This combination has allowed the Group to efficiently and effectively transfer the three programmes from Novartis and to make significant progress this year with a lean internal infrastructure. The successful growth to date is a result of the hard work, enthusiasm, experience and skills of all our employees who show a strong affiliation with Mereo and our mission to deliver innovative medicines to patients.

Our Board members have significant operational experience in large and small pharmaceutical companies and in clinical research organisations. They provide valuable strategic input into our development programmes and into the overall direction of the Group.

In October 2016 Richard Bungay notified us of his intention to step down as CFO/COO and as a Board member of Mereo. Richard left the company on 13 January 2017 and we would like to thank him for his contribution to the Group during the past 18 months.

In November 2016 we announced the appointment of Richard Jones as CFO and a Board member of Mereo. Richard joined the company on 30 January 2017. Previously, Richard was the CFO of Shield Therapeutics plc from April 2011 and a board member from early 2010. Prior to that, Richard was an investment banker in the healthcare sector at Investec and Brewin Dolphin. We are also pleased to announce the appointment of Jerome Dauvergne as Head of Pharmaceutical Development. Jerome is currently Head of External Manufacturing at Ipsen Biopharm Ltd and he will join the Group on 2 May 2017.

From founding the Group only 18 months ago we have made outstanding progress, acquiring and integrating our first three programmes from Novartis and advancing into them into the clinic. We would

like to thank Board members and our staff for their important contributions during this successful period, and also our shareholders for their continued support.

Recent developments and outlook
The Group is expecting to deliver a number of key clinical milestones in 2017.

The Group has announced it will release the outcome of a blinded interim analysis in the Phase 2b study of BGS-649 by the Independent Data Monitoring Committee (IDMC) in March 2017. This follows the enrolment of 93 patients out of a total of 260 patients expected in the study. They will have received at least one month's treatment at this point. Following this analysis, any doses either not expected to normalise testosterone at 24 weeks or with significant safety concerns will be dropped and the study will continue with remaining doses versus placebo until patients have received six months' treatment. Any doses that have been dropped at the interim analysis will also be dropped from the 6 month safety extension study. As per the trial design, the Group will continue to be completely blinded to the study, including information on dosing, until it is complete.

The Phase 2 study for acumapimod in AECOPD and the Phase 2b study for BGS-649 in HH are expected to read out as planned in H2 2017.

Following consultation with regulators the BPS-804 programme for osteogenesis imperfecta was accepted into the Adaptive Pathways programme in the EU as announced earlier this month. We expect to start the pivotal Phase 2b study for BPS-804 in OI in H1 2017.

These data points are each important in demonstrating our ability to successfully transfer programmes from major pharmaceutical companies, to rapidly execute comprehensive clinical studies and also to validate our selection criteria for the product acquisitions.

The Group continues to seek further product opportunities to accelerate growth with the aim of becoming a leading player in the development and commercialisation of novel therapies for rare and speciality diseases with high unmet medical needs. Our plan is to use our first mover advantage to add additional product opportunities such that in the longer term we have between five and seven products under development. Mereo is looking to become the partner of choice for pharmaceutical and large biotechnology companies as they look to unlock the potential in their development pipelines and deliver promising drug candidates to patients. During the period, we have seen strong interest from a range of pharmaceutical companies to partner with us in respect of a significant number of specific product opportunities. We remain confident of delivering on our strategy.

Dr Denise Scots-Knight
Chief Executive Officer

Peter Fellner
Non-Executive Chairman

27 February 2017

Financial review

The financial statements are presented for the year ended 31 December 2016; comparative data is shown for the Group's first accounting period, from the parent company's incorporation on 10 March 2015 to the financial year end on 31 December 2015.

During June 2016, the Group raised gross proceeds of £14.8 million in a private placement with institutional investors and additionally drew down the remaining balance of £56.5 million gross proceeds from the £76.5 million private financing round that was completed in July 2015, in total therefore the Group raised £71.3 million gross proceeds in 2016, £68.3 million net of expenses. This will enable the Group to continue to fund its existing programmes for each of its three current product candidates to achieve key value inflection points in 2017 and 2018, as detailed in the Strategic Report.

On 9 June 2016, following completion of the private placement, the Company's shares were admitted to trading on the AIM market of the London Stock Exchange under the ticker symbol "MPH".

The Group is structured to provide flexibility for the eventual sale, licensing or commercialisation of its product candidates, with each being developed within a wholly owned subsidiary company. External research and development activities are contracted directly by the Group's subsidiary companies, with the parent company employees providing services on an "arm's-length" basis to facilitate efficient development of product candidates. It is envisaged that future product acquisitions can be added to the Group with modest increases in internal resource.

Revenue

The Group did not generate any revenue from product sales or licensing activities during the period.

Research and development expenses

Research and Development (R&D) expenses during the period amounted to £24.6 million (2015: £5.4 million). Excluding a non-cash charge relating to share-based payments, adjusted R&D expenses were £22.8 million (2015: £5.0 million). This expenditure primarily related to payments to contract research organisations (CROs) for the ongoing and planned clinical trials for each of the Group's product candidates and to contract manufacturing organisations (CMOs) for the provision of drug products to support the clinical studies. R&D expenses are expected to increase in 2017, with the planned initiation of the first pivotal clinical study and associated manufacturing activities for the Group's orphan disease candidate BPS-804 alongside the ongoing clinical studies for acumapimod and BGS-649, both of which are expected to read out as planned H2 2017.

Administrative expenses

Administrative expenses during the period amounted to £11.6 million (2015: £7.7 million). Excluding share based payments and one off advisory fees adjusted administrative expenses amounted to £5.7 million (2015:£5.2 million). This expenditure primarily related to employee-related expenses, including the Board and executive management, costs of the Group's premises and professional advisors' fees. Underlying administrative expenses are expected to increase in 2017 ahead of inflation reflecting a small planned increase in headcount and a full year's cost relating to being a listed company.

Financial income

The Group earns interest on its cash reserves from short-term deposits. Interest earned during the period amounted to £0.2 million (2015: £0.03 million). The Group has benefited during 2016 from holding a significant amount of its cash in US Dollars (see below), where the available interest rates have been higher than those available for Sterling deposits, reflecting the underlying base rates and future base rate

expectations. In addition, the group registered a non-cash gain on these deposits of £2.3 million (2015:£nil) from the gain on translation of these deposits at the year-end reflecting a strengthening of the US Dollar against Sterling during the year.

Taxation

The Company's subsidiaries conduct all research and development activities and consequently are responsible for submitting claims under the UK research and development small or medium-sized enterprise ("R&D tax credit") scheme. The R&D tax credit scheme provides additional taxation relief for qualifying expenditure on R&D activities, with an option to surrender a portion of tax losses arising from qualifying activities in return for a cash payment from HM Revenue & Customs (HMRC). The Company's subsidiaries received the first R&D tax cash repayment during the year, totalling £0.9 million, in respect of the claim for the period ended 31 December 2015. The R&D tax credit receivable in the balance sheet of £5.3 million is an estimate of the cash repayments the Company's subsidiaries expect to qualify for in respect of activities during the year ended 31 December 2016; however, as at the date of this announcement these amounts have not yet been agreed with HMRC.

Loss per share

Basic Loss per share for the year was 63 pence (2015: 101 pence). On an adjusted non-GAAP basis, excluding one-off items and share based payments, Loss per share was 51 pence (a comparative 2015 adjusted loss per share has not been presented after taking into account that the company was formed in 2015 and therefore the nature of the operating expenses was not comparable between 2015 and 2016). Taking account that Admission and the associated fund raising occurred part way through the year, on an adjusted non-GAAP proforma basis, Loss per share was 36 pence.

For definitions of adjusted and proforma adjusted loss per share please see note 6.

Liquidity, cash, cash equivalents and money market investments

The Group's cash, cash equivalents and money market investments at the period end totalled £53.6 million (2015: £12.2 million).

During June 2016, the Group raised gross proceeds of £14.8 million in a private placement with institutional investors, of which £3.4 million was in the form of a convertible loan, and additionally drew down the remaining balance of £56.5 million gross proceeds from the £76.5 million private financing round that was completed in July 2015, in total therefore the Group raised £71.3 million gross proceeds in 2016, £68.4 million net of expenses.

The net cash outflow from operating activities in 2016 was £27.4 million against an operating loss of £33.7 million, with the major reconciling items being the non-cash charge for share-based payments of £7.5 million, the R&D credit received of £0.9 million and other movements in working capital of £2.0 million.

A significant component of the Group's clinical trial expenditure is denominated in US Dollars. The Group has in place a conservative hedging strategy in respect of its USD requirements that ensures that sufficient Sterling is converted to US Dollars at any time to cover up to the next 12 months anticipated operational requirements. At the time of Brexit, the Group therefore had significant US Dollar deposits converted at favourable rates. The Group continues to purchase US Dollars on an ongoing basis based on this policy and utilises a conservative assumption when considering the cash funding requirements for its operational activities.

Other balance sheet items

Intangible assets at the year-end were £25.8 million (2015: £25.8 million), representing the value assigned to the Group's product candidates acumapimod, BGS-649 and BPS-804 upon acquisition from Novartis. The Group has performed an annual review of the value in use for these programmes at 31 December 2016 and has concluded that there is no impairment at that date.

Future commitments to Novartis will be recognised as an expense in the same period when related future cash inflows from product sales or outlicensing or other monetisation of the programs by the Group are earned.

Trade and other receivables (including R&D tax credit receivable of £5.3 million) at the year-end were £7.2 million (2015: £1.6 million) and trade and other payables were £3.2 million (2015: £4.0 million) at the year end.

Outlook

Overall, the Group believes it is well positioned and well-funded to execute on its business strategy and to progress its existing products through the current trial programmes in 2017 and 2018.

Richard Jones
Chief Financial Officer
27 February 2017

Consolidated statement of comprehensive loss
for the year ended 31 December 2016

	Notes	31 December 2016	10 March 2015 to 31 December 2015
		£	£
Research and development expenses	4	(24,562,502)	(5,445,015)
Administrative expenses		(11,616,816)	(7,716,344)
Operating loss		(36,179,318)	(13,161,359)
Net finance income		195,141	25,717
Net foreign exchange gain		2,262,626	-
Loss before tax		(33,721,551)	(13,135,642)
Taxation	5	5,331,271	946,681
Loss for the period, attributable to equity holders of the parent		(28,390,280)	(12,188,961)
Other comprehensive income/(loss) for the period, net of tax		-	-
Total comprehensive (loss) for the period, net of tax and attributable to the equity holders of the parent		(28,390,280)	(12,188,961)
Basic and diluted loss per share for the period	6	(£0.63)	(£1.01)
Non-GAAP measure			
Adjusted loss per share for the period	6	(0.51)	
Proforma adjusted loss per share	6	(0.36)	

Balance sheet
as at 31 December 2016

	Notes	Group 31 December 2016	Group 31 December 2015	Company 31 December 2016	Company 31 December 2015
		£	£	£	£
Assets					
Non-current assets					
Property, plant and equipment		173,869	204,517	173,869	204,517
Investments		-	-	67,754,682	421,352
Intercompany receivables		-	-	-	35,699,919
Intangible assets		25,812,941	25,812,941	-	-
Other receivables		-	-	-	-
		25,986,810	26,017,458	67,928,551	36,325,788
Current assets					
Prepayments		1,102,146	253,926	1,102,146	253,926
R&D tax credits		5,331,271	946,681	-	-
Other receivables		767,009	396,022	767,009	396,022
Cash and short-term deposits	7	53,577,571	12,247,986	53,577,571	12,247,986
		60,777,997	13,844,615	55,446,726	12,897,934
Total assets		86,764,807	39,862,073	123,375,277	49,223,722
Equity and liabilities					
Equity					
Issued capital	8	193,022	59,221	193,022	59,221
Share premium	8	99,975,399	26,212,880	99,975,399	26,212,880
Other capital reserves	8	12,667,562	21,660,105	12,667,562	21,660,105
Accumulated Profit / (loss)		(33,579,241)	(12,188,961)	3,031,229	(2,827,315)
Total equity		79,256,742	35,743,245	115,867,212	45,104,891
Non-current liabilities					
Provisions		1,172,424	141,311	1,172,424	141,311
Convertible loan	9	3,126,526	-	3,126,526	-
		4,298,950	141,311	4,298,950	141,311
Current liabilities					
Trade and other payables		3,209,115	3,977,517	3,209,115	3,977,520
Total liabilities		7,508,065	4,118,828	7,508,065	4,118,831
Total equity and liabilities		86,764,807	39,862,073	123,375,277	49,223,722

Consolidated and Company statement of cash flows for the year ended 31 December 2016

	Notes	Group		Company	
		31 December 2016	Period ended 31December 2015	31 December 2016	Period ended 31 December 2015
		£	£	£	£
Operating activities					
Loss before tax	1	(33,721,551)	(13,135,642)	(1,141,456)	(2,827,315)
Adjustments to reconcile loss before tax to net cash flows:					
Depreciation of property, plant and equipment		32,940	11,361	32,940	11,361
Share-based payment expense	8	6,494,018	2,982,265	4,905,559	2,560,916
Provision for social security contributions on employee share options		1,031,109	141,311	794,960	121,346
Interest received		(374,906)	(25,717)	(374,906)	(299,759)
Interest on convertible loan		179,765	-	179,765	-
Capitalisation of Intercompany balances		-	-	(29,808,806)	-
Working capital adjustments:					
(Increase) in receivables		(1,219,202)	(649,948)	(1,219,202)	(10,565,215)
Increase / (decrease) in payables		(768,402)	3,977,517	(768,402)	4,025,774
Tax received		946,681	-	-	-
Net cash flows from operating activities		(27,399,548)	(6,698,853)	(27,399,548)	(6,972,892)
Investing activities					
Purchase of property, plant and equipment		(3,467)	(215,878)	(3,467)	(215,878)
Disposal of property, plant and equipment		1,175	-	1,175	-
Investment in subsidiaries		-	-	-	(3)
Interest received		374,906	25,717	374,906	299,759
Net cash flows used in investing activities		372,614	(190,161)	372,614	83,878
Financing activities					
Proceeds from issue of ordinary shares	8	67,888,820	20,005,000	67,888,820	20,005,000
Transaction costs on issue of shares	8	(2,995,864)	(868,000)	(2,995,864)	(868,000)
Proceeds from issue of convertible loan		3,463,563	-	3,463,563	-
Net cash flows from financing activities		68,356,519	19,137,000	68,356,519	19,137,000
Net increase in cash and cash equivalents		41,329,585	12,247,986	41,329,585	12,247,986
Cash and cash equivalents at beginning of the period		12,247,986	-	12,247,986	-
Cash and cash equivalents at 31 December	7	53,577,571	12,247,986	53,577,571	12,247,986

Significant non-cash transaction

During the year the Directors of the Company signed a solvency statement with the agreement of all shareholders and undertook a capital reduction, reducing the share premium account by £7,000,000 and reducing the accumulated losses by the same amount.

During the year, 8,697,480 shares were issued to Novartis Pharma AG (for nil consideration). The fair value of these was £1.84 per share.

During the period ended 31 December 2015 the Company issued two bonus shares of £0.001 in nominal value for each ordinary shares held. The post-bonus share capital was consolidated such that each ordinary shareholder received one share for every three held. The total number of ordinary shares remained at 19,740,296 but the nominal value is now £0.003

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Consolidated statement of changes in equity

	Issued capital	Share premium	Other capital reserves	Accumulated losses	Total equity
	£	£	£	£	£
As at 10 March 2015	**-**	**-**	**-**	**-**	**-**
Loss for the period to 31 December 2015	-	-	-	(12,188,961)	(12,188,961)
Issue of share capital	19,740	27,067,420	-	-	27,087,160
Issue of bonus share capital	39,481	(39,481)	-	-	-
Share-based payments - share options	-	-	2,982,265	-	2,982,265
Shares to be issued	-	-	18,677,840	-	18,677,840
Profit on transfer of loan notes for equity	-	52,941	-	-	52,941
Transaction costs on issuance of share capital	-	(868,000)	-	-	(868,000)
At 31 December 2015	**59,221**	**26,212,880**	**21,660,105**	**(12,188,961)**	**35,743,245**
Loss for the year to 31 December 2016	-	-	-	(28,390,280)	(28,390,280)
Issue of share capital	107,709	67,781,112	-	-	67,888,821
Share-based payments – share options	-	-	6,185,067	-	6,185,067
Share-based payments – LTIPS	-	-	133,601	-	133,601
Share-based payments – deferred bonus shares	-	-	175,350	-	175,350
Redemption of shares to be issued	26,092	15,977,271	(16,003,363)	-	-
Equity element of convertible loan	-	-	516,802	-	516,802
Share capital reduction	-	(7,000,000)	-	7,000,000	-
Transaction costs on issuance of share capital	-	(2,995,864)	-	-	(2,995,864)
At 31 December 2016	**193,022**	**99,975,399**	**12,667,562**	**(33,579,241)**	**79,256,742**

1. Corporate information

Mereo BioPharma Group plc (the "**Company"** or the "parent") is a public limited company incorporated and domiciled in United Kingdom, and registered in England, and whose shares are publicly traded. The registered office is located at Fourth Floor, 1 Cavendish Place, London, W1G 0QF. The Group is principally engaged in the research and development of novel pharmaceuticals

The financial information set out above has been prepared in accordance with the recognition and measurement criteria of International Financial reporting Standards adopted by the EU (Adopted IFRS). The financial information does not constitute the group's statutory accounts for the year ended 31 December 2016. Statutory accounts for 2016 will be published and delivered to the Registrar of Companies in due course.

The auditor has reported on these accounts; their reports were unqualified, and did not include a reference to any matter to which the auditor drew attention by way of emphasis without qualifying their report and their report did not contain a statement under s498.

These results were approved by the Board of Directors on 24 February 2017.

2. Significant accounting policies

Basis of preparation

The Group and Company's annual financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union and for the Company in accordance with the Companies Act 2006.

The financial information is presented in Sterling.

3. Going concern

Though the Group and Company continues to make losses, the Directors believe it is appropriate to prepare the financial information on the going concern basis. This is because the Group's research into new products continues to progress according to plan and the funding secured in June 2016 will allow it to meet its liabilities as they fall due for at least 12 months from the date of authorisation for issue of these consolidated financial statements.

4. Segment information

For management purposes, the Group is organised into business units based on its products and has three reportable segments, as follows:

- Respiratory Unit, which develops drugs to treat respiratory diseases
- Endocrinology Disorders Unit, which develops drugs to treat endocrine disorders
- Orphan Diseases Unit, which develops drugs to treat various orphan diseases

The Executive Management Committee monitors the operating results of its business units separately as part of the process for making decisions about resource allocation and performance assessment. Segment performance is evaluated based on progress of each development program and the related development expenditure. Expenditure is measured consistently with the total expenditure included in the consolidated financial statements. The Group's financing (including finance costs and finance income) are managed on a Group basis and are only partially allocated to operating segments.

Year ended 31 December 2016	Respiratory unit	Endocrinology disorders unit	Orphan diseases unit	Total segments	Unallocated	Consolidated
	£	£	£	£	£	£
Expenses						
Research & Development	(9,733,421)	(9,431,758)	(4,804,117)	(23,969,296)	(593,206)	(24,562,502)
Administrative	(2,747,085)	(2,787,307)	(3,076,405)	(8,610,797)	(3,006, 019)	(11,616,816)
Segment operating loss	(12,480,506)	(12,219,065)	(7,880,522)	(32,580,093)	(3,599,225)	(36,179,318)
Assets						
Tax Credit	2,102,469	2,094,259	1,134,543	5,331,271	-	5,331,271
Intangible Assets	4,310,761	9,886,56	11,615,824	25,812,941	-	25,812,941

Period ended 31 December 2015	Respiratory unit	Endocrinology disorders unit	Orphan diseases unit	Total segments	Unallocated	Consolidated
	£	£	£	£	£	£
Expenses						
Research & Development	(2,399,367)	(1,393,860)	(1,437,664)	(5,230,891)	(214,124)	(5,445,015)
Administrative	(1,641,880)	(1,695,991)	(1,739,566)	(5,077,437)	(2,638,907)	(7,716,344)
Segment operating loss	(4,041,247)	(3,089,851)	(3,177,230)	(10,308,328)	(2,853,031)	(13,161,359)
Assets						
Tax Credit	300,024	290,965	355,692	946,681	-	946,681
Intangible Assets	4,310,761	9,886,356	11,615,824	25,812,941	-	25,812,941

Unallocated

The majority of payroll and related costs, and expenses relating to the Group's facilities, are not allocated to segments as these are managed centrally, as are finance income and costs.

All non-current assets held by the Group are located in the United Kingdom.

5. Income tax

The Group is entitled to claim tax credits in the United Kingdom under the UK research and development (**R&D**) small or medium-sized enterprise (**SME**) scheme, which provides additional taxation relief for qualifying expenditure on R&D activities, and includes an option to surrender a portion of tax losses arising from qualifying activities in return for a cash payment from HM Revenue & Customs (**HMRC**). The amount included in the financial statements for the represents the credit receivable by the Group for the year. The 2016 amounts have not yet been agreed with the relevant tax authorities.

Reconciliation of the accounting loss multiplied by United Kingdom's domestic tax rate for 2016:

	Year ended 31 December 2016	Period ended 31 December 2015
Group	£	£
United Kingdom Corporation Tax R&D credit	5,331,271	946,681
Income tax credit	**5,331,271**	**946,681**
The tax credit for the year is lower than the standard rate of corporation tax in the UK of 20%. The differences are explained below		
Loss on ordinary activities before income tax	(33,721,551)	(13,135,642)
Loss on ordinary activities before tax at United Kingdom's statutory income tax rate of 20%	6,744,310	2,627,129
Expenses not deductible for tax purposes (permanent differences)	(15,116)	(438,196)
Temporary timing differences	(1,300,044)	(599,975)
Research development relief uplift	2,134,107	378,956
Tax losses carried forward to future periods	(2,231,986)	(1,021,233)
Tax credit for the period	5,331,271	946,681

A reduction in the rate of UK corporation tax to 19% from 1 April 2017 and to 17% from 1 April 2020 has been substantively enacted. UK deferred tax assets and liabilities are recognised at a rate of 17%.

At 31 December 2016, the Group had tax losses to be carried forward of approximately (£16,343,508) (2015: (£5,106,165))

Deferred tax

Deferred tax relates to the following:

	31 December 2016	31 December 2015
	£	£
Losses	2,788,396	919,110
Accelerated capital allowances	(9,883)	-
Other	2,210	3,170
Net deferred tax asset	2,770,723	922,280

The deferred tax asset has not been recognised as there is uncertainty regarding when suitable future profits against which to offset the accumulated tax losses will arise. There is no expiration date for the accumulated tax losses.

6. Loss per share

Basic loss per share is calculated by dividing the loss attributable for the period to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the period.

As net losses from continuing operations were recorded in the period, the dilutive potential shares are anti-dilutive for the earnings per share calculation.

	Year ended 31 December 2016			Period ended 31 December 2015		
	Loss £	Weighted shares	Loss per share £	Loss £	Weighted shares	Loss per share £
Group						
IFRS – basic and diluted	(28,390,280)	44,789,893	(0.63)	(12,188,961)	12,009,419	(1.01)
Adjusted – basic and diluted	(22,956,976)	44,789,893	(0.51)			
Proforma adjusted – basic and diluted	(22,956,976)	64,340,798	(0.36)			

The Company operates share option schemes which could potentially dilute basic earnings per share in future. In addition there exist within equity 1,453,520 shares to be issued which also have the potential to dilute basic earnings per share in future. There have been no other transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of authorisation of these financial statements.

The adjusted loss is calculated using the weighted average number of ordinary shares in issue during the period and after adding back non-recurring items and share based payments as illustrated in the table below. A comparative 2015 adjusted loss per share has not been presented after taking into account that the company was formed in 2015 and therefore the nature of the operating expenses was not comparable between 2015 and 2016. Adjusted profit/(loss) per share information will be disclosed in future years on a consistent basis.

The adjusted proforma loss per share is calculated using the number of ordinary shares in issue following admission to the AIM market of the London Stock Exchange (that is it assumes the admission took place on 1 January 2016 in respect of the number of shares in issue to enable better comparison in future years). As the date of admission to the AIM market was on 9 June 2016, comparatives for the previous period have not been provided.

The table below reconciles the loss used for the basic and adjusted (non-GAAP) loss per share computations

	Year-ended 31 December 2016
Group	
Loss for the period	(28,390,280)
Share based payments	6,494,018
Provision for social security on share options	1,031,109
Non capitalised IPO costs	45,000
Corporate finance costs	125,803
Net gain on foreign exchange	(2,262,626)
Adjusted loss	(22,956,976)

7. Cash and short-term deposits

Group and Company	31 December 2016	31 December 2015
	£	£
Cash at banks and on hand	421,292	647,007
Short-term deposits	53,156,279	11,600,979
	53,577,571	**12,247,986**

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short-term deposits are available immediately and earn interest at the respective short-term deposit rates.

8. Issued capital and reserves

Ordinary share capital	31 December 2016	10 March to 31 December 2015
	£	£
Balance at beginning of year / period	59,221	1
Issuances in the period	133,801	59,220
Nominal share capital as at 31 December	**193,022**	**59,221**

Ordinary shares issued and fully paid (post ordinary share split)	
At 1 January 2016	19,740,296
Issued on 9 June 2016 for private financing round	39,464,540
Issued on 9 June 2016 for private placement	5,135,962
At 31 December 2016	**64,340,798**
Nominal value at 31 December 2016	**0.003**
Issued capital at 31 December 2016	**193,022**

Ordinary shares issued and fully paid (post ordinary share split)	
At 10 March 2015 – Incorporation capital	1,000
Founders Shares	4,999,000
Issued on 29 July 2015 for private financing round	14,740,296
Bonus shares issued on 27 November 2015	39,480,592
Consolidation of post-bonus share capital	(39,480,592)
At 31 December 2015	**19,740,296**
Nominal value at 31 December 2015	**0.003**
Issued capital at 31 December 2015	**59,221**

On 29 July 2015, there was a subdivision of 5,000 ordinary shares of £1.00 in nominal value in the capital of the Company to 5,000,000 ordinary shares of £0.001 in nominal value in the capital of the Company (the "ordinary share split");

On 27 November 2015 the company issued two ordinary bonus shares of £0.001 in nominal value for each ordinary share held and consolidated the post-bonus share capital such that each ordinary shareholder received one share for every three held. The nominal value of each ordinary shares changed to £0.003.

Since 1 January 2016, the following alterations to the Company's share capital have been made:

- under the subscription agreement dated 28 July 2015, as amended by an agreement dated 1 June 2016, the issue and allotment of 39,464,540 ordinary shares of £0.003 in nominal value in the capital of the Company on 9 June 2016 at a price of £1.84 per share. 39,699 of these ordinary shares were issued to WG Partners LLP, for no cash consideration, as payment for financial advisory services;
- on 21 March 2016 the Directors of the Company signed a solvency statement with the agreement of all shareholders and undertook a capital reduction, reducing the share premium account by £7,000,000 and reducing the accumulated losses by the same amount;
- under a private placement dated 9 June 2016, the issue and allotment of 5,135,962 ordinary shares of £0.003 in nominal value in the capital of the Company on 9 June 2016 at a price of £2.21 per share; and;

- on 9 June 2016, the Company's ordinary shares were admitted to trading on the AIM market of the London Stock Exchange.

	31 December 2016
	£
Share premium	
At 1 January 2016	**26,212,880**
Issuance of share capital for private financing round on 9 June 2016	**72,423,314**
Issuance of share capital for private placement on 9 June 2016	**11,335,068**
Transaction costs for issued share capital	**(2,995,863)**
Share capital reduction on 21 March 2016	**(7,000,000)**
At 31 December 2016	**99,975,399**

	31 December 2015
	£
At 10 March 2015	**-**
Issuance of share capital for private financing round on 29 July 2015	**27,067,420**
Transaction costs for issued share capital	**(868,000)**
Profit on transfer of loan notes for equity	**52,941**
Consolidation of post-bonus share capital on 27 November 2015	**(39,481)**
At 31 December 2015	**26,212,880**

Other capital reserves

	£
At 1 January 2016	21,660,105
Share-based payments expense during the period	6,494,018
Shares issued	(16,003,363)
Equity component of convertible loan instrument	516,802
At 31 December 2016	12,667,562

	£
At 10 March 2015	-
Share-based payments expense during the period	2,982,265
Shares to be issued	18,677,840
At 31 December 2015	21,660,105

Share-based payments

The Group has a share option scheme under which options to subscribe for the Group's shares have been granted to certain Executives, Non-Executive Directors and employees.

The share-based payment reserve is used to recognise the value of equity-settled share-based payments provided to employees, including key management personnel, as part of their remuneration. Of the £6,494,018 share-based payment expense in the year, £298,836 is an accelerated charge relating to 500,000 share options which were cancelled on 9 June 2016.

Shares issued / to be issued

Of the 14,740,296 ordinary shares issued on 29 July 2015, 3,849,000 shares were issued to Novartis Pharma AG (**Novartis**). This left a further 10,151,000 shares are to be issued to Novartis pro rata to their percentage shareholding as and when the Company issued further ordinary shares.

Of the 44,600,502 ordinary shares issued on 9 June 2016, 8,697,480 shares were issued to Novartis as fully paid up bonus shares (for nil consideration), the number of which was calculated to maintain its shareholding at 19.5%. The fair value of these shares was £1.84 per share. A further 1,453,520 shares are to be issued to Novartis pro rata to their percentage shareholding as and when the Company issues further ordinary shares.

9. Convertible loan note

On 3 June 2016, the Company issued 3,463,563 £1 unsecured convertible loan notes ("Notes") to Novartis Pharma AG, a related party. The Notes attract an interest rate of 4% per annum payable annually and accruing daily and constitute direct, unsecured obligations of the Company ranking ahead of any other unsecured obligations of the Company.

The noteholder shall be entitled, at any time within 36 months of the date of the instrument ("Maturity Date"), to serve a conversion notice on the Company to convert all or some only of the outstanding Notes into fully paid ordinary shares at a conversion price of £2.21 per share. To the extent the Notes are not converted at the Maturity Date, the outstanding principal amount of the Notes, together with any accrued interest, is redeemable. Upon conversion of any Notes, in addition to the relevant number of conversion shares, the noteholder is entitled to receive an additional number of ordinary shares in the Company equal to the number of conversion shares into which such Notes are to convert, multiplied by 0.93, up to a maximum aggregate number of 1,453,520 such bonus shares.

The value of the debt component of the Notes at the date of issue was calculated as £2,946,761. The cash flows attached to the Note up to the Maturity Date were calculated and discounted at an appropriate venture debt rate of 10%. The carrying amount at 31 December 2016 is £3,126,526.

The value of the equity component of the Notes at 31 December 2016 was calculated as £516,802.