

XENETIC BIOSCIENCES (UK) LIMITED

ANNUAL REPORT

FOR THE YEAR ENDED

31st DECEMBER 2014



Company Registration Number 03213174

XENETIC BIOSCIENCES (UK) LIMITED

ANNUAL REPORT

FOR THE YEAR ENDED 31st DECEMBER 2014

| CONTENTS | PAGE |
|---|-------------|
| Officers and professional advisers | 1 |
| Report of the Directors | 2 |
| Independent auditor's report to the members | 14 |
| Statement of comprehensive loss | 16 |
| Balance sheet | 17 |
| Statement of cash flows | 18 |
| Statement of changes in equity | 19 |
| Notes to the financial statements | 20 |

XENETIC BIOSCIENCES (UK) LIMITED

OFFICERS AND PROFESSIONAL ADVISERS

| | |
|--------------------------|--|
| Directors | Scott Maguire (Chief Executive Officer) Colin W. Hill (Chief Financial Officer) |
| Company secretary | Colin W. Hill |
| Registered office | 5th Floor 15 Whitehall London SW1A 2DD |
| Auditor | Ernst & Young LLP Apex Plaza Forbury Road Reading RG1 1YE |
| Bankers | Bank of Scotland 33 Old Broad Street London EC2N 1HW |
| Solicitors | Pinsent Masons LLP 30 Crown Place London EC2A 4ES |

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

The Directors present their report and the financial statements for the year ended 31st December 2014.

STATUS OF THE COMPANY

At the date of this Annual Report, the Company is a wholly owned-subsiidiary of a publicly-listed US corporation, Xenetic Biosciences Inc (NASDAQ:XBIO), formerly General Sales and Leasing, Inc ("GSL"), this being pursuant to a successful merger with GSL on terms set out in a Scheme of Arrangement ("SoA") voted through by shareholders on 17 December 2013 and sanctioned by the High Court of England and Wales on 23 January 2014.

On 31st March 2014, by Special Resolution, the Company changed its name and registered status to Xenetic Biosciences (UK) Limited ("XENUK" or "the Company").

The Company (formerly the group's AIM-listed UK parent company pre-the 2014 merger with GSL) is an intermediate holding company within the US-quoted Xenetic Biosciences group. The Company holds 100% of the equity of the undernoted subsidiary companies:

- Lipoxen Technologies Limited – a wholly owned UK-subsiidiary;
- SymbioTec GmbH - a wholly owned German subsidiary;
- Xenetic Bioscience Inc - a wholly owned US subsidiary.

As the Company no longer is a UK publicly-quoted enterprise, as a private limited company it is not required to produce Consolidated Accounts; consequently the Financial Statements included in this Annual Report relate only to the business of the Company.

REPORTS INCLUDED HEREIN BY REFERENCE

The primary purpose of delivering annual reports and accounts to shareholders is to better inform them of the financial status of the reporting entity.

As all of XENUK, Lipoxen Technologies Limited (LTL), SymbioTec GmbH (SYM) and Xenetic Bioscience Inc (XTI) contribute to the performance and results of the entire US Xenetic Group (XBIO Group), it is recommended that, with a view to obtaining a full understanding of the overall group's activities, readers should familiarise themselves with all regulatory filings for the entire US group, as filed with the United States Securities and Exchange Commission (SEC).

While the SEC's filing requirements are extensive, particular attention should be directed towards the XBIO Group's quarterly 10-Q filings through 30 September 2016, and its annual 10-K filings for the financial years ended 31 December 2014 and 2015.

IMPORTANT NOTE

*The XBIO Group's US SEC regulatory filings can be accessed through the undernoted website:
<https://www.sec.gov/edgar/searchedgar/companysearch.html>*

Readers are strongly commended to access this data source as the gaining of the detailed data and information contained therein is critical to reaching a full understanding of the status of the XBIO Group.

*They should also access the information that is publicly available on the XBIO Group website
at: www.xeneticbio.com*

XENETIC BIOSCIENCES (UK) LIMITED

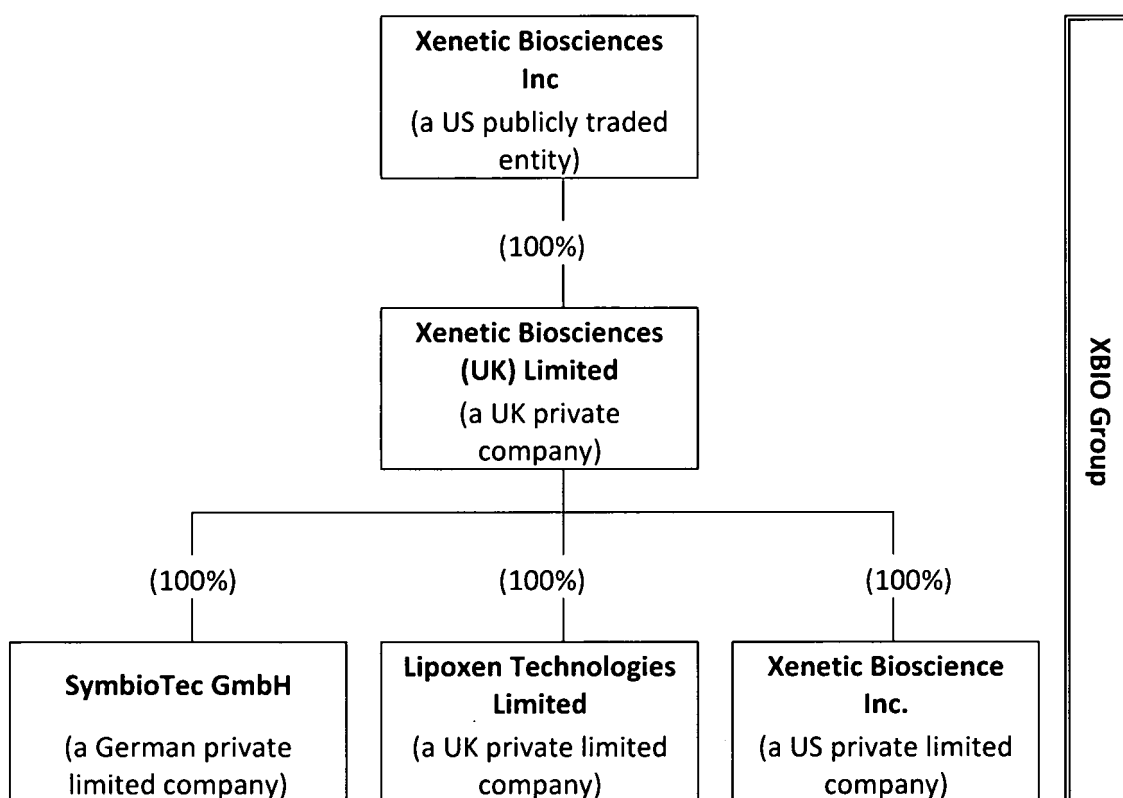
REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

PRINCIPAL ACTIVITIES

The principal activity of the Company during the year was to act as a holding company.

GROUP ORGANISATION

For a better understanding of the corporate relationships that exist across the XBIO Group, please see below the Structure Diagram of the entire Xenetic Group of companies, which hereinafter shall be referred to as the "XBIO Group", "XBIO" being the publicly-traded entity with Ticker Symbol: NASDAQ:XBIO



The nature of the activities carried out by individual entities across the XBIO Group are more fully described elsewhere, but can be summarised as follows:

Xenetic Biosciences Inc (XBIO)

The parent company of the XBIO Group responsible for group strategy, investment, executive management and finance. It was the entity with which the former UK parent company (see below) merged in January 2014 (the US merger). This entity serves as the public face of the group and is the primary source of funding for the group through its access to the capital markets of the United States and elsewhere.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

GROUP ORGANISATION (CONTINUED)

Xenetic Biosciences (UK) Limited (XenUK) Formerly Xenetic Biosciences plc, this was the UK publicly-traded company until January 2014 when it became a wholly-owned subsidiary of the new US parent company. It serves now only as an intermediate holding company for the three operating subsidiaries shown above. It has no clinical responsibility but retains certain contractual employment relationships with certain members of executive management notably that of Scott Maguire, XBIO's Chief Executive Officer.

Lipoxen Technologies Limited (LTL) LTL was the original company in the creation (or acquisition) of all of the Group's core technologies - save for OncoHist, which is held by SymbioTec (*post*). It remains the principal holder of the XBIO Group's Intellectual Property and Patent Portfolio assets. Prior to the US merger, and for some 9 months thereafter, LTL carried out scientific and preclinical operations from the UK group's laboratory facilities in London, activities that were ultimately moved *in toto* to the Group's current laboratory and Head Office facility in Lexington, MA, USA.

LTL remains the principal entity in all respects for the ongoing development of its core technologies and product candidate initiation and development based on those technologies held by it. In that regard, the US operating subsidiary Xenetic Bioscience Inc (XTI) acts as LTL's agent and/or service provider as regards all such activities as the relevant IP shall remain vested entirely in LTL.

Xenetic Bioscience Inc (XTI) XTI is a private US corporation whose activities are focussed on technology and product development on behalf of the entities in whom the relevant IP is vested, those being LTL and SymbioTec. While product development strategy is set by the parent company's board it is executed as regards all clinical matters through XTI acting on the instructions of the corporate holders of the relevant IP.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

GROUP ORGANISATION (CONTINUED)

Symbiotec GmbH (SYM)

SYM is a private German company, formerly with operations in Saarbrücken prior to its acquisition by XenUK in January 2012, consequent to which all scientific operations were transferred to London and, later, to Lexington.

SYM is the owner and holder of the IP relating to the Group's important OncoHist technology, the development of which is treated in exactly the same manner as for those technologies and product candidate vested in LTL.

GOING CONCERN

The Company depends for funding upon its US-listed ultimate parent company, Xenetic Biosciences, Inc ("XBIO"). The Directors have received a letter of comfort from XBIO confirming XBIO's intention to provide such level of financial support to the Company for a period of at least 12 months from the date of this Report such that the Company will be able to meet its obligations as they fall due.

Since its inception, the business of the Group has incurred, and continues to incur, significant losses from operations. The business has historically relied upon the proceeds of public and non-public financing activities by its parent company to support the working capital requirements necessary to pursue the on-going research, development and commercialisation of its intellectual property and know-how performed by its subsidiaries, including the Company.

On November 7, 2016, Xenetic Biosciences Inc (NASDAQ: XBIO) issued for cash \$10 million of units consisting of Series B preferred stock and warrants.

As of December 31, 2016, the Group held cash and deposits of \$4.1m.

On January 5, 2017, the Group – through its wholly owned subsidiary Lipoxen Technologies Limited – received a \$3 million milestone cash payment from Shire plc (LSE: SHP, NASDAQ: SHPG) related to Shire's advancing the Phase 1/2a clinical study for the PSA-Recombinant SHP656 or Factor VIII ("FVIII") being developed as a long-acting therapeutic for the treatment of haemophilia. This milestone payment is the first in a series of clinical-milestone-dependent payments which would fall due based upon the successful progression to market of the SHP656 molecule; the total potential amount due under payments to be made in respect of clinical, regulatory and sales milestones and sales royalties is \$100m.

The Group has produced a cash flow projection for the period of 12 months from the date of this report which, subject to receipt of a US\$5m clinical milestone payment (expected to become receivable in Q2 2017), indicates that the Group – and therefore the Company – would have adequate working capital for the 12 months from the date of this report to support its currently planned activities. However, and as has been noted in previous reports, the timing of the attainment of any clinical milestone is indeterminate due to the uncertainties and risks inherent in the clinical development process; accordingly, it is not possible to predict precisely when those receipts may occur, if ever.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

GOING CONCERN (CONTINUED)

While the financial statements herein have been prepared on a going concern basis, if the Group does not successfully raise additional working capital by October 2017, either by the expected receipt of the US\$5m clinical milestone, or otherwise via a planned external fundraising in that timeframe, there can be no assurance that it will be able to continue its operations as currently planned. The raising of additional working capital represents a material uncertainty which casts significant doubt about the ability to continue as a going concern. Until the Group achieves commercialization of its technology or receives significant and regular cash flows from its current collaborations or from planned out-licensing of its technology, the Group expects the trend of accessing capital markets to finance its working capital needs to continue beyond the next 12 months.

While there can be no absolute assurance on the matter, the Group directors have reasonable expectations that the US\$5m milestone will be received in the expected timeframe above. As the Group directors have recently successfully up-listed the Group to NASDAQ in November 2016, and in further consideration of the recently announced clinical advances in the Shire FVIII candidate, they also have reasonable expectations that, as is planned in the course of Q2 FY17, they could successfully obtain such new capital as may be necessary to meet the Group's obligations as they fall due and to fund its operations and clinical pipeline developments as currently planned for the next 12 months from the date of this report.

Accordingly, the accompanying financial statements do not include any adjustments related to the recoverability or classification of asset-carrying amounts or the amounts and classification of liabilities that may result should the Company be unable to continue as a going concern.

DIRECTORS AND THEIR INTERESTS

The Directors who served the Company during the year, together with the beneficial interests in the shares of the Company of those in office at the year end, were as follows:

| | Ordinary Shares of 0.5p | | Share options | |
|-------------------------------|-------------------------|-----------|---------------|-----------|
| | 2014 | 2013 | 2014 | 2013 |
| Sir Brian Richards | - | 2,262,606 | - | 203,486 |
| Scott Maguire | - | 1,401,361 | - | 7,747,346 |
| Colin W. Hill | - | 1,825,420 | - | 1,547,096 |
| Professor Gregory Gregoriadis | - | 4,650,208 | - | 406,974 |
| Dr Dmitry D. Genkin | - | - | - | - |
| Firdaus J. Dastoor | - | 1,125,000 | - | - |
| Roman Knyazev | - | - | - | - |
| Artur Isaev | - | - | - | - |

Notes

1. Roman Knyazev resigned as a Director on 1st May 2014
2. Artur Isaev resigned as a Director on 1st May 2014
3. Firdaus J. Dastoor resigned as a Director on 1st May 2014
4. Professor Gregory Gregoriadis resigned as a Director on 1st May 2014
5. Dr Dmitry D. Genkin resigned as a Director on 1st May 2014
6. Sir Brian Richards resigned as a Director on 1st May 2014
7. Remaining shareholdings and options were transferred to the new ultimate parent company on 23rd January 2014 as result of the merger described above.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

THIRD PARTY INDEMNITY PROVISIONS

The Company has purchased insurance to cover its Directors and Officers against liabilities arising against them in that capacity.

STRATEGIC REPORT

Although the Company is prohibited from applying the small company exemption relating to the preparation of financial statements on the basis that it is a member of an ineligible group, the Company has applied the exemption from the preparation of the strategic report on the basis that it meets the criteria of being a small company. However, readers are directed to the **Important Note** (*ante*) advising readers to access the XBIO Group's regulatory filings with the US Securities and Exchange Commission (SEC) made in respect of the parent public company.

RESULTS

The trading results for the year and the Company's financial position at the end of the year are shown in the attached financial statements.

DIVIDEND

No dividend has been proposed.

BRANCHES

The Company has no branch operations.

EMPLOYEES

The Company does not employ more than 250 persons and so no disclosure on employment matters is required.

POLITICAL DONATIONS

The Company made no such donations either in the period covered by this Report or in the post balance sheet period to date.

SUBSEQUENT EVENTS

This Directors Report is for the 12 months to 31 December 2014, and so "Subsequent Events" covers a period from 1st January 2015 to the date of this Report. While detailed disclosures and public statements have been made on a continuing basis by XBIO (the Company's Ultimate Holding Company – "UHC") in the USA, the principal subsequent events that have occurred at a Group level are summarised below under the headings of "Key Clinical Updates" and "Key Financial and Board Updates". Clinical updates relate to the business and IP of the Company and its subsidiaries while Financial and Board updates relate to the overall XBIO Group.

Key Clinical Updates

On 14 July 2015, XBIO announced that it has completed treatment of the second cohort of its Phase 2 dose-escalation study with its lead drug candidate ErepoXen® for the treatment of anaemia in pre-dialysis chronic kidney disease patients. The 12 patients enrolled in this cohort received a biweekly injection of ErepoXen® until haemoglobin levels reached the

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

SUBSEQUENT EVENTS (CONTINUED)

Key Clinical Updates (continued)

therapeutic range. The patients then received injections of ErepoXen® every 4 weeks (extended dosing interval) during maintenance for a total trial time of 17 weeks.

On 16th September 2015, XBIO announced that it has commenced the third cohort of its Phase 2 dose-escalation study with its lead drug candidate ErepoXen® for the treatment of anaemia in pre-dialysis chronic kidney disease patients. In an effort to accelerate the recruitment rate, Xenetic has expanded the clinical research sites beyond Australia to now include locations in South Africa. Subjects from this third cohort study will receive injections of ErepoXen® every two weeks until haemoglobin levels reach therapeutic levels. The patients will then receive injections of ErepoXen® every 4 weeks (extended dosing interval) during maintenance for a total trial time of 17 weeks.

The data from the second cohort showed that 91% of the enrolled patients had an increase in haemoglobin levels over time, and that in 75% of the enrolled patients, haemoglobin levels rose into the therapeutic range. The third cohort is designed to further increase the patient's haemoglobin levels into mid-therapeutic range. The study is being performed at nine clinical sites in Australia and six new clinical sites in South Africa. Patient treatment has commenced in Australia. National and local regulatory approvals have been granted in South Africa and patient treatment is expected to start in September. This cohort is expected to be completed in Q2, 2016 (please refer to further update below).

On 18th August 2016, XBIO announced that it has commenced a collaboration with Excivion Ltd. ("Excivion") to develop a vaccine against Zika and dengue viruses. As part of the collaboration, Xenetic's proprietary IMUXEN™ Technology will be used to develop the vaccine. Excivion is a private UK company that has developed a proprietary antigen design platform for viral vaccines which it is applying to flavivirus infections.

On 19th August 2016, XBIO announced that an Investigational New Drug (IND) application for the Group's product candidate, Virexxa® (sodium cridanomod), has been allowed to proceed by the U.S. Food and Drug Administration (FDA). This enables Xenetic to initiate a Phase 2 clinical study of Virexxa in conjunction with progestin therapy for the treatment of endometrial cancer in women with recurrent or persistent disease who have failed progestin monotherapy. The primary objective of the study is to assess the anti-tumour activity of Virexxa. Secondary objectives include assessment of additional efficacy, pharmacokinetic and safety/tolerability parameters. Further translational objectives are to observe the effect of Virexxa in combination with progestins, on the levels of progesterone receptor (PrR) and activated progesterone receptors (APrR) in tumour tissues .

On 10th October 2016, XBIO announced positive topline data from the third cohort of its Phase 2 dose-escalation study with its lead drug candidate ErepoXen® for the treatment of anaemia in pre-dialysis chronic kidney disease patients. This trial is being conducted for Xenetic by Novotech (Australia) Pty Ltd.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

SUBSEQUENT EVENTS (CONTINUED)

Key Clinical Updates (continued)

The third cohort of the Phase 2, open label, sequential dose finding study to evaluate the safety, pharmacodynamics (PD) and pharmacokinetics (PK) of multiple doses of ErepoXen was launched in October 2015 and was conducted in Australia and South Africa. As in the previous cohorts, patients in the third cohort of this study received injections of ErepoXen every two weeks until haemoglobin levels reached therapeutic levels. The patients then received injections of ErepoXen every 4 weeks (extended dosing interval) during maintenance for a total trial time of 17 weeks.

Professor Simon D Roger M.D., FRACP, Director of Renal Medicine, Gosford Hospital, Australia and Principal Investigator of the study, said, "The results achieved with ErepoXen® in these individuals with chronic kidney disease expand on the initial two cohorts, and, continue to demonstrate a reassuring safety profile. I am very pleased about the potential for ErepoXen® to act as a therapeutic agent to treat these anaemic patients and look forward to the continued study of this compound to achieve further results."

On January 6, 2017, XBIO announced that Xenetic has received a \$3 million milestone payment from Shire plc (LSE: SHP, NASDAQ: SHPG) related to Shire's advancing the Phase 1/2a clinical study for the PSA-Recombinant SHP656 or Factor VIII ("FVIII") being developed as a long-acting therapeutic for the treatment of haemophilia. The stated goal of Shire is to introduce an innovative FVIII protein that can significantly prolong the circulating half-life of the FVIII protein, with the objective of providing a once weekly treatment or reaching higher trough activity levels for greater efficacy.

Key Financial and Board Updates

On 8 July 2015, XBIO completed a US\$ 3 million Bridge Note Financing with OJSC Pharmsynthez ("Pharmsynthez") a collaborative partner of XBIO. The financing was completed by means of a 10% Convertible Promissory Note, convertible (at the option of Pharmsynthez) in whole or in part into shares of Common Stock of XBIO. Pharmsynthez also received certain 5 year warrants to purchase shares of Common Stock of XBIO. Readers are directed to the Form 8-K filed by XBIO on 8 July 2015 for further material information regarding the Bridge Note Financing.

On 16 November 2015, XBIO announced that it has entered into an Asset Purchase Agreement (the "APA") with AS Kevelt, an Estonian biotech company ("Kevelt") and OJSC Pharmsynthez ("Pharmsynthez", and together with Kevelt, "Sellers"). Pursuant to the APA, the Sellers will transfer to LTL certain intellectual property rights with respect to Virexxa™, and LTL, will receive the worldwide rights to develop, market and license Virexxa for all uses, except for certain excluded uses within the Commonwealth of Independent States (the "CIS"), in exchange for 111.5 million shares of XBIO common stock and certain other consideration. Virexxa is a Phase II oncology drug candidate which is under investigation for the treatment of certain endometrial cancers. As part of this total consideration, the Group will also acquire Kevelt's U.S. Orphan Drug designation for the use of Virexxa in the treatment of progesterone receptor negative endometrial cancer in conjunction with progesterone therapy. This transaction was completed on 29 April 2016 with an effective date of 27 April 2016 as confirmed in a Form 8-K filed with the SEC on 3 May 2016.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

SUBSEQUENT EVENTS (CONTINUED)

Key Financial and Board Updates (continued)

The APA also contains a financing component wherein XBIO will receive from Pharmsynthez up to \$3.5 million in bridge financing and a commitment of an additional \$6.5 million in financing as part of a planned Capital Raise of at least \$15 million and up-list to a national securities exchange. On 1 July 2016 XBIO received a further \$0.5 million bridge advance and on 26 August 2016 and 9 September 2016, XBIO issued promissory notes for \$0.178m and \$0.322m, respectively to Pharmsynthez. These promissory notes are convertible into common stock shares at any time at a conversion price of \$4.95 per share (subject to usual and customary adjustments) or may be applied towards the Offering at the option of Pharmsynthez. This has reduced the amount remaining available to participate in the Capital Raise to \$5.5 million.

On 29 February 2016, XBIO announced the appointment of renowned chemist and Nobel Laureate, Dr. Roger D. Kornberg to the XBIO Board of Directors.

Dr. Kornberg is a member of the U.S. National Academy of Sciences and the Winzer Professor of Medicine in the Department of Structural Biology at Stanford University. He earned his bachelor's degree in chemistry from Harvard University in 1967 and his Ph.D. in chemical physics from Stanford in 1972. He became a postdoctoral fellow at the Laboratory of Molecular Biology in Cambridge, England and then an assistant professor of biological chemistry at Harvard Medical School in 1976, before moving to his present position as professor of structural biology at Stanford Medical School in 1978.

In 2006, Dr. Kornberg was awarded the Nobel Prize in Chemistry in recognition for his studies of the molecular basis of Eukaryotic Transcription, the process by which DNA is copied to RNA. Dr. Kornberg is also the recipient of several awards, including the 2001 Welch Prize, the highest award granted in the field of chemistry in the United States, and the 2002 Leopold Mayer Prize, the highest award granted in the field of biomedical sciences from the French Academy of Sciences.

On 1 June 2016, XBIO announced that its Board of Directors approved a proportional 1-for-33 reduction and reverse stock split of its issued and outstanding common stock in preparation for its planned uplisting to the NASDAQ Capital Market ("NASDAQ"). The reverse stock split became effective and its common stock began trading on a post-split basis at the open of trading on Wednesday June 1, 2016.

The reverse stock split is intended to fulfil the stock price requirements for listing on NASDAQ since the requirements include that XBIO's common stock must maintain a minimum closing price for 30 of 60 trading days.

On 11 July 2016, XBIO announced that it has appointed Jeffrey F. Eisenberg to the XBIO's Board of Directors.

Mr. Eisenberg is a life sciences executive with over 20 years of operational experience and a successful track record in value creation in both private and public companies. Over the course of his career, he has led all crucial areas of R&D, operations, manufacturing/quality, business development, strategic partnering, product development, commercialization, and talent management.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

SUBSEQUENT EVENTS (CONTINUED)

Key Financial and Board Updates (continued)

On 1st November 2016, XBIO announced its common stock will begin trading on The NASDAQ Capital Market under the symbol "XBIO" on November 7, 2016. XBIO also announced the pricing of its public offering of an aggregate of 2,424,242 units, consisting of (i) 484,849 units, consisting of one share of Convertible Series B Preferred Stock and a Class A Warrant to purchase one share of common stock and (ii) 1,939,393 units consisting of one share of Convertible Series B Preferred Stock and a Class B Warrant to purchase one share of common stock, at a public offering price of \$4.125 per unit. The total gross proceeds of the public offering were approximately \$10 million before the underwriter's discount and expenses.

In connection with its new listing on The NASDAQ Capital Market, November 4, 2016 was the last day Xenetic's common stock will trade on the OTCQB.

On 5th November 2016, XBIO announced it has appointed Jeffrey F. Eisenberg as Chief Operating Officer.

Mr. Eisenberg is a life science executive with over 20 years of operational experience who has been serving on Xenetic's Board of Directors since July 2016. Over the course of his career, Mr. Eisenberg has led all crucial areas of R&D, operations, manufacturing/quality, business development, strategic partnering, product development, commercialization, and talent management.

On 7th November 2016, XBIO announced the closing of its public offering of an aggregate of 2,424,242 units, consisting of (i) 484,849 units, consisting of one share of Convertible Series B Preferred Stock and a Class A Warrant to purchase one share of common stock and (ii) 1,939,393 units consisting of one share of Convertible Series B Preferred Stock and a Class B Warrant to purchase one share of common stock, at a public offering price of \$4.125 per unit. OPKO Health, Inc. (NASDAQ:OPK) along with other healthcare institutional investors participated in the offering.

As previously announced, in connection with the closing of its public offering, XBIO commenced trading of its common stock on 7th November 2016 on The NASDAQ Capital Market under the symbol "XBIO."

Ladenburg Thalmann & Co. Inc. acted as the sole book running manager for the offering.

The total gross proceeds of the public offering are approximately \$10 million before the underwriter's discount and expenses. The net proceeds from this offering will be used to fund the research and development of Xenetic's product candidates, including Virexxa, as well as future development programs, potential in licensing of products or technology, potential in licensing of products or technology, capital expenditures, working capital, repayment of existing indebtedness, and other general corporate purposes.

The shares and warrants described above were offered by Xenetic pursuant to a registration statement on Form S-1 previously filed with, and subsequently declared effective by the Securities and Exchange Commission ("SEC"). A final prospectus supplement relating to the offering was filed with the SEC and is available, along with the accompanying base prospectus, on the SEC's website at <http://www.sec.gov> or from Ladenburg Thalmann & Co. Inc., Prospectus Department, 570 Lexington Avenue, 11th Floor, New York, New York 10022, by calling (212) 409-2000.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31st DECEMBER 2014

SUBSEQUENT EVENTS (CONTINUED)

Key Financial and Board Updates (continued)

On 22nd November 2016, XBIO announced that it has appointed Edward J. Benz, Jr., M.D., to XBIO's Board of Directors.

Dr. Benz is a renowned expert in blood disorders and is board certified in both haematology and internal medicine. He is an active clinical haematologist and a National Institutes of Health (NIH) funded researcher with a focus on the molecular basis and genetics around inherited blood disorders. Prior to joining the Xenetic Board, Dr. Benz served as President and CEO Emeritus of Dana-Farber Cancer Institute and the Richard and Susan Smith Professor of Medicine and Professor of Genetics at Harvard Medical School. During Dr. Benz's tenure at Dana-Farber, the institute experienced exponential growth, including an increase of fund-raising to more than \$200 million a year from a network of 300,000 donors, a tripling of the number of patients seeking treatment, and a growth in revenues from \$265 million to more than \$1 billion.

On 4th January 2017, XBIO announced that it has appointed Curtis A. Lockshin, Ph.D. as Chief Scientific Officer.

Dr. Lockshin is a life science executive with an extensive background in cross-functional R&D management, with a particular focus on drug discovery, preclinical and clinical development. Dr. Lockshin is an inventor on numerous patents related to small-molecule therapeutics, biomaterials and optical biosensors.

On January 6, 2017, XBIO announced that Xenetic has received a \$3 million milestone payment from Shire plc (LSE: SHP, NASDAQ: SHPG) related to Shire's advancing the Phase 1/2a clinical study for the PSA-Recombinant SHP656 or Factor VIII ("FVIII") as noted in the clinical update section above.

Readers are directed both to the current SEC filings by XBIO and to the XBIO website for details of all events that have been the subject to Press Releases and/or SEC filings in the period 1 January 2015 to the date of this Report.

FUTURE DEVELOPMENTS & RESEARCH AND DEVELOPMENT

As Group strategy is directed from the UHC, readers are directed to the Form 10-Q filed on 14 November 2016 which sets out in detail the current status and development expectations of all of the aforementioned drug candidates and activities of strategic partners.

DIRECTORS' RESPONSIBILITIES STATEMENT

The Directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the Company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the Directors must not approve the financial statements unless they are satisfied that they present fairly the financial position and cash flows of the Company and of the financial performance of the Company for that year.

XENETIC BIOSCIENCES (UK) LIMITED

REPORT OF THE DIRECTORS

FOR THE YEAR ENDED 31st DECEMBER 2014

DIRECTORS' RESPONSIBILITIES STATEMENT (CONTINUED)

In preparing these financial statements, the Directors are required to:

- select suitable accounting policies in accordance with IAS 8: *Accounting Policies, Changes in Accounting Estimates and Errors* and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements;
- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable the users to understand the impact of particular transactions, other events and conditions on the financial position and financial performance;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

DISCLOSURE OF INFORMATION TO AUDITOR

Each Director has confirmed that:

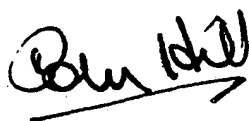
- so far as the Director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- he has taken all the steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given in accordance with Section 418 of the Companies Act 2006.

SMALL COMPANY PROVISIONS

This report has been prepared in accordance with the special provisions for small companies under Part 15 of the Companies Act 2006.

This report was approved by the Board on 17 February 2017 and signed on its behalf by:



Colin Hill
Director

Company Registration Number 03213174

XENETIC BIOSCIENCES (UK) LIMITED

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF XENETIC BIOSCIENCES (UK) LIMITED

We have audited the financial statements of Xenetic Biosciences (UK) Limited for the year ended 31 December 2014 which comprise the statement of comprehensive loss, the balance sheet, the statement of cash flows, the statement of changes in equity and the related Notes 1 to 20. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As explained more fully in the Directors' Responsibilities Statement set out on pages 12 and 13 the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing our audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

XENETIC BIOSCIENCES (UK) LIMITED

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF XENETIC BIOSCIENCES (UK) LIMITED

OPINION ON FINANCIAL STATEMENTS

In our opinion:

- the financial statements give a true and fair view of the state of the Company's affairs as at 31 December 2014 and of its loss for the year then ended;
- the financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

EMPHASIS OF MATTER – GOING CONCERN

In forming our opinion on the financial statements, which is not modified, we have considered the adequacy of disclosures made in Note 2 to the financial statements concerning the Company's ability to continue as a going concern, which indicate the existence of a material uncertainty which may cast significant doubt over the Company's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the Company was unable to continue as a going concern.

OPINION ON OTHER MATTER PRESCRIBED BY THE COMPANIES ACT 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Company's financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the Directors were not entitled to take advantage of the small companies' exemption from the requirement to prepare a Strategic Report or in preparing the Directors' Report.



David Hales (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
Reading
17 February 2017

XENETIC BIOSCIENCES (UK) LIMITED

STATEMENT OF COMPREHENSIVE LOSS FOR THE YEAR ENDED 31st DECEMBER 2014

| | Note | 2014 £ | 2013 £ |
|--|-------------|-------------------|--------------------|
| REVENUE | 3 | 67,858 | 181,205 |
| | | <hr/> | <hr/> |
| Administrative expenses | | 486,860 | 2,797,152 |
| | | <hr/> | <hr/> |
| OPERATING LOSS | 4 | (419,002) | (2,615,947) |
| Finance income | | 45,343 | 52,508 |
| Finance costs | | (141,689) | (69,335) |
| | | <hr/> | <hr/> |
| LOSS BEFORE TAXATION | | (515,348) | (2,632,774) |
| Income tax | 7 | - | - |
| | | <hr/> | <hr/> |
| LOSS AFTER TAX AND LOSS FOR THE YEAR ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT | | (515,348) | (2,632,774) |
| | | <hr/> <hr/> | <hr/> <hr/> |

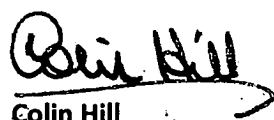
XENETIC BIOSCIENCES (UK) LIMITED

BALANCE SHEET

AS AT 31st DECEMBER 2014

| | Note | 2014 £ | 2013 £ |
|---|------|--------------------------|--------------------------|
| NON-CURRENT ASSETS | | | |
| Property, plant and equipment | 8 | 10,869 | 30,852 |
| Intangible assets | 9 | 686,250 | 686,250 |
| Investments | 10 | 15,145,030 | 15,145,030 |
| Other receivables | 11 | 15,036,240 | 16,068,377 |
| | | <u>30,878,389</u> | <u>31,930,509</u> |
| CURRENT ASSETS | | | |
| Trade and other receivables | 11 | 2,539,707 | 1,752,378 |
| Cash and cash equivalents | 17 | 1,466,947 | 2,896,446 |
| | | <u>4,006,654</u> | <u>4,648,824</u> |
| LIABILITIES | | | |
| Trade and other payables - current | 12 | (550,978) | (1,705,858) |
| | | <u></u> | <u></u> |
| NET CURRENT ASSETS | | <u>3,455,676</u> | <u>2,942,966</u> |
| NET ASSETS | | <u><u>34,334,065</u></u> | <u><u>34,873,475</u></u> |
| EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY | | | |
| Share capital | 13 | - | 3,673,742 |
| Share premium account | | 46,937,612 | 46,901,013 |
| Shares to be issued | | - | 91,663 |
| Capital redemption reserve | | 3,704,744 | - |
| Retained earnings | | (16,308,291) | (15,792,943) |
| | | <u></u> | <u></u> |
| TOTAL EQUITY | | <u><u>34,334,065</u></u> | <u><u>34,873,475</u></u> |

The financial statements were approved and authorised for issue by the Directors on 17 February 2017 and were signed on their behalf by:


Colin Hill
Director

Company Registration Number 03213174

XENETIC BIOSCIENCES (UK) LIMITED

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31st DECEMBER 2014

| | Note | 2014 £ | 2013 £ |
|---|-------------|--------------------|--------------------|
| Cash flows from operating activities | 15 | 2,043,702 | (2,263,885) |
| Interest (paid) / received | | (96,346) | 22,190 |
| Net cash inflow/(outflow) from operating activities | | 1,947,356 | (2,241,695) |
| Cash flows from investing activities | | | |
| Purchase of property, plant and equipment | | - | (645) |
| Loan to subsidiaries | | (3,438,859) | (1,716,328) |
| Net cash used in investing activities | | (3,438,859) | (1,716,973) |
| Cash flows from financing activities | | | |
| Issue of equity share capital | | 62,004 | 1,276 |
| Loan repaid to related party | | - | (9,565) |
| Net cash generated from/(used in) financing activities | | 62,004 | (8,289) |
| Net decrease in cash and cash equivalents | | (1,429,499) | (3,966,957) |
| Cash and cash equivalents at beginning of year | | 2,896,446 | 6,863,403 |
| Cash and cash equivalents at end of year | 16 | 1,466,947 | 2,896,446 |

XENETIC BIOSCIENCES (UK) LIMITED

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31st DECEMBER 2014

| | Share capital | Share premium | Shares to be issued | Capital redemption reserve | Retained earnings | Total |
|--|------------------|------------------|------------------------|----------------------------------|----------------------|-------------|
| | £ | £ | £ | £ | £ | £ |
| At 1st January 2013 | 3,672,877 | 46,900,602 | - | - | (13,160,169) | 37,413,310 |
| Loss and total comprehensive income for year | - | - | - | - | (2,632,774) | (2,632,774) |
| Shares issued for cash | 865 | 411 | - | - | - | 1,276 |
| Shares to be issued for services | - | - | 91,663 | - | - | 91,663 |
| At 31st December 2013 | 3,673,742 | 46,901,013 | 91,663 | - | (15,792,943) | 34,873,475 |
| Loss and total comprehensive income for year | - | - | - | - | (515,348) | (515,348) |
| Ordinary shares issued for cash | 31,002 | 31,002 | - | - | - | 62,004 |
| Cancellation of shares (see note 13) | (3,704,744) | - | - | 3,704,744 | - | - |
| Shares to be issued for services provided - issued by ultimate parent (see note 13) | - | - | (91,663) | - | - | (91,663) |
| Capital contribution | - | 5,597 | - | - | - | 5,597 |
| At 31st December 2014 | - | 46,937,612 | - | 3,704,744 | (16,308,291) | 34,334,065 |

All amounts are attributable to the ultimate parent company.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

1. INTERNATIONAL FINANCIAL REPORTING STANDARDS

Basis of Preparation

The Company's financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards, International Accounting Standards and IFRIC interpretations (collectively IFRS) as adopted by the European Union, and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. Xenetic Biosciences (UK) Limited is a private limited Company incorporated and domiciled in England and Wales.

During the year, the Company became a wholly owned subsidiary of a publicly listed US Corporation, Xenetic Biosciences, Inc. This being pursuant to a successful merger with General Sales and Leasing Inc. on terms set out in a Scheme of Arrangement passed by shareholders on 17th December 2013 and sanctioned by the High Court of England and Wales on 23rd January 2014. On 31st March 2014 by Special Resolution, Xenetic Biosciences plc (a public company) changed its name and registered status to Xenetic Biosciences (UK) Limited.

The principal accounting policies adopted in preparation of the financial statements are set out below. The policies have been consistently applied to all the years presented, unless otherwise stated.

The Company, which is a wholly owned intermediate parent company, is exempt from the obligation to prepare and deliver group accounts in accordance with section 401 of the Companies Act 2006 on the basis that the ultimate parent company, Xenetic Biosciences Inc, incorporated in the United States of America, produces consolidated accounts which are publicly available. These financial statements for Xenetic Biosciences (UK) Limited present information about the Company as an individual undertaking and not about its group. The Company presents its financial statements in its functional currency which is sterling.

Under section 454 of the Companies Act 2006 the directors can amend these financial statements on a voluntary basis if they subsequently prove to be defective.

Critical accounting judgements and key sources of estimation uncertainty

In the process of applying the Company's accounting policies, management makes estimates and assumptions that have an effect on the amounts recognised in the financial statements. Although these estimates are based on management's best knowledge of current events and actions, actual results may ultimately differ from those estimates.

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are those relating to the carrying value/recoverability of investments in subsidiaries and related intercompany amounts receivable, and intangible assets representing intellectual property (see notes 9 and 10 for further details).

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

1. INTERNATIONAL FINANCIAL REPORTING STANDARDS (continued) Standards, interpretations and amendments to existing standards

The following new and amended IFRS and IFRIC interpretations were effective as of 1 January 2014:

- IFRS 10 (amended) Consolidated Financial Statements
- IFRS 12 (amended) Disclosure of interest in other entities
- IAS 27 (amended) Consolidated and separate financial statements
- IAS 32 (amended) Offsetting financial assets and liabilities
- IAS 36 (amended) Recoverable amount disclosures for non-financial assets
- IAS 39 (amended) Novation of derivatives and continuation of hedge accounting
- IFRIC 21 Levies

The directors concluded that there are no areas within these standards which have a material impact to the Company.

Interpretations and revised standards that are not yet effective and have not been early adopted by the company

The following interpretations to existing standards have been published that are mandatory for the Company's future accounting but which the Company has not adopted early. Management has not yet fully assessed the impact of these new standards but does not believe they will have any material impact on the financial statements.

- IAS 19 (Amended) Defined benefit plans: employee contributions – 1 July 2014
- IFRS 10 and IAS 28 (Amended) Sale or contribution of assets between an investor and its associate or joint venture – 1 January 2016
- IFRS 10, IFRS 12 and IAS 28 (Amended) Investment entities: Applying the consolidation exemption – 1 January 2016
- IFRS 12 (Amended) Disclosure of interests in other entities – 1 January 2016
- IFRS 11 (Amended) Accounting for acquisitions of interests in joint operations – 1 January 2016
- IFRS 14 Regulatory Deferral Accounts – 1 January 2016
- IAS 16 and IAS 38 (Amended) Clarification of acceptable methods of depreciation and amortisation – 1 January 2016
- IAS 16 and IAS 41 (Amended) Agriculture – Bearer plants – 1 January 2016
- IAS 27 (Amended) Equity method in separate financial statements – 1 January 2016
- IFRS 15 Revenue from contracts with customers – 1 January 2017
- IFRS 9 Financial Instruments – 1 January 2018

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

2. ACCOUNTING POLICIES

Going Concern

The Company depends for funding upon its US-listed ultimate parent company, Xenetic Biosciences, Inc ("XBIO"). The Directors have received a letter of comfort from XBIO confirming XBIO's intention to provide such level of financial support to the Company for a period of at least 12 months from the date of this Report such that the Company will be able to meet its obligations as they fall due.

Since its inception, the business of the Group has incurred, and continues to incur, significant losses from operations. The business has historically relied upon the proceeds of public and non-public financing activities by its parent company to support the working capital requirements necessary to pursue the on-going research, development and commercialisation of its intellectual property and know-how performed by its subsidiaries, including the Company.

On November 7, 2016, Xenetic Biosciences Inc (NASDAQ: XBIO) issued for cash \$10 million of units consisting of Series B preferred stock and warrants.

As of December 31, 2016, the Group held cash and deposits of \$4.1m.

On January 5, 2017, the Group – through its wholly owned subsidiary Lipoxen Technologies Limited – received a \$3 million milestone cash payment from Shire plc (LSE: SHP, NASDAQ: SHPG) related to Shire's advancing the Phase 1/2a clinical study for the PSA-Recombinant SHP656 or Factor VIII ("FVIII") being developed as a long-acting therapeutic for the treatment of haemophilia. This milestone payment is the first in a series of clinical-milestone-dependent payments which would fall due based upon the successful progression to market of the SHP656 molecule; the total potential amount due under payments to be made in respect of clinical, regulatory and sales milestones and sales royalties is \$100m.

The Group has produced a cash flow projection for the period of 12 months from the date of this report which, subject to receipt of a US\$5m clinical milestone payment (expected to become receivable in Q2 2017), indicates that the Group – and therefore the Company – would have adequate working capital for the 12 months from the date of this report to support its currently planned activities. However, and as has been noted in previous reports, the timing of the attainment of any clinical milestone is indeterminate due to the uncertainties and risks inherent in the clinical development process; accordingly, it is not possible to predict precisely when those receipts may occur, if ever.

While the financial statements herein have been prepared on a going concern basis, if the Group does not successfully raise additional working capital by October 2017, either by the expected receipt of the US\$5m clinical milestone, or otherwise via a planned external fundraising in that timeframe, there can be no assurance that it will be able to continue its operations as currently planned. The raising of additional working capital represents a material uncertainty which casts significant doubt about the ability to continue as a going concern. Until the Group achieves commercialization of its technology or receives significant and regular cash flows from its current collaborations or from planned out-licensing of its technology, the Group expects the trend of accessing

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

2. ACCOUNTING POLICIES (continued)

Going Concern (continued)

capital markets to finance its working capital needs to continue beyond the next 12 months.

While there can be no absolute assurance on the matter, the Group directors have reasonable expectations that the US\$5m milestone will be received in the expected timeframe above. As the Group directors have recently successfully up-listed the Group to NASDAQ in November 2016, and in further consideration of the recently announced clinical advances in the Shire FVIII candidate, they also have reasonable expectations that, as is planned in the course of Q2 FY17, they could successfully obtain such new capital as may be necessary to meet the Group's obligations as they fall due and to fund its operations and clinical pipeline developments as currently planned for the next 12 months from the date of this report.

Accordingly, the accompanying financial statements do not include any adjustments related to the recoverability or classification of asset-carrying amounts or the amounts and classification of liabilities that may result should the Company be unable to continue as a going concern.

Intangible Assets

Intellectual property comprises in-process research and development which has been purchased. Purchased intellectual property is recognised at cost.

Revenue

Revenue is stated net of sales taxes, rebates and discounts. Revenue is recognised as follows:

Management fees

Management fees represent amounts charged to subsidiaries and other entities for management time and expenses. Revenue is recognised in the period in which it is earned.

Interest income

Interest income is accounted for on a cash received basis and not on an accruals basis.

Impairment

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation or depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised for the amount by which the asset's carrying value exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

The expected cash flows generated by the assets are discounted using asset specific discount rates which reflect the risks associated with the groups of assets. These risks

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

2. ACCOUNTING POLICIES (continued)

Impairment (continued)

vary with the nature and the location of the cash generating units. Any impairment loss is charged to the statement of comprehensive loss in the year concerned. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows (cash-generating units).

Property, plant and equipment

All property, plant and equipment assets are stated at cost less accumulated depreciation.

Depreciation is provided to write off the cost less the estimated residual value of property, plant and equipment on a straight line basis over their estimated useful economic lives as follows:

| | | |
|------------------------|---|---------|
| Leasehold improvements | - | 4 years |
| Computer equipment | - | 4 years |
| Plant | - | 5 years |

Financial instruments

Financial assets and financial liabilities are recognised on the Company's balance sheet when the Company becomes a contractual party to the instrument.

Financial assets other than hedging instruments can be divided into the following categories: loans and receivables, financial assets at fair value through profit or loss, available-for-sale financial assets and held-to-maturity investments. Financial assets are assigned to the different categories by management on initial recognition, depending on the purpose for which the investments were acquired.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date which are classified as non-current assets. The Company's loans and receivables comprise 'other receivables' and 'cash and cash equivalents' in the balance sheet. The Company has no other financial assets.

Financial liabilities and equity instruments issued by the Company are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities. Equity instruments issued by the Company, other than equity-settled share-based payments which are described below, are recorded at the proceeds received net of direct issue costs.

Trade receivables

Trade receivables are measured at initial recognition at fair value and are subsequently measured at amortised cost less impairment losses. Appropriate provisions for estimated irrecoverable amounts are recognised in statement of comprehensive loss account when there is objective evidence that the asset is impaired.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

2. ACCOUNTING POLICIES (continued)

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, bank balances and deposits repayable on demand.

Trade payables

Trade and other payables are measured at initial recognition at fair value and are subsequently measured at amortised cost.

Operating lease agreements

Operating lease rentals are charged in the statement of comprehensive loss account on a straight line basis over the lease term.

Foreign currencies

Monetary assets and liabilities in foreign currencies are translated into sterling at the rate ruling at the balance sheet date. Transactions in foreign currencies are translated into sterling at the rate of exchange ruling at the date of the transaction. Exchange differences are taken into account when arriving at the operating loss.

Pension costs

Company contributions to money purchase pension schemes are charged to the statement of comprehensive loss as incurred.

Share based payments

In accordance with IFRS 2 "Share-based Payments", the Company measures the fair value of equity settled transactions with employees at the grant date of the equity instruments. The fair value is calculated using an appropriate valuation model and requires assumptions regarding dividend yields, risk-free interest rates, share price volatility and expected life of an employee share option, plus the likelihood of meeting other performance-related vesting objectives where applicable. The arising expense is charged to the statement of comprehensive loss account on a straight-line basis over the expected vesting period.

Share options granted to employees over the equity instruments of the Company prior to the events of 23rd January 2014 referred to in note 14 are valued at the date of grant using the Black-Scholes option pricing model and are charged to the statement of comprehensive loss over the vesting period of the option. A corresponding credit is recognised in retained earnings.

Shares issued under the Joint Share Ownership Plan ("JSOP") over the equity instruments of the Company prior to the events of 23rd January 2014 referred to in note 14 which vest immediately are valued at the date of grant using the Black-Scholes option pricing model. JSOP shares issued with share price targets are valued at the date of grant using a Monte Carlo simulation approach as this allows the fair value to reflect the interaction of the Black-Scholes formula and the performance targets. These amounts are charged to the statement of comprehensive loss over the expected period to vesting of the shares.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

2. ACCOUNTING POLICIES (continued)

Share based payments (continued)

A corresponding credit is recognised in retained earnings.

For equity-settled share-based payments in relation to acquisitions, the entity shall measure the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity shall measure their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.

Warrants to subscribe for new equity in the Company prior to the date of the scheme of arrangement referred to in note 14 are valued at the date of grant using the Black-Scholes option pricing model. The excess of this amount over the consideration received for the grant is charged to the statement of comprehensive loss. A corresponding credit is recognised in retained earnings.

As explained more fully in note 14, on 23rd January 2014 the share options and warrants held in this Company were transferred to the new parent company, Xenetic Bioscience Inc. Ongoing charges calculated using the methods referred to above under IFRS 2 continue to be charged to the statement of comprehensive loss with the corresponding credit reflected in the share premium reserve.

Equity

Share capital is determined using the nominal value of shares that have been issued.

The share premium account includes any premiums received on the initial issuing of the share capital. Any transaction costs associated with the issue of shares are deducted from the share premium account, net of any related income tax benefits.

The shares to be issued reserve represents the value of services received from a supplier who has irrevocably agreed to accept settlement of the amount owed in the form of shares in the Company.

Share capital and the associated share premium relating to cancelled shares is transferred to the capital redemption reserve by way of a movement in reserves.

Taxation

The tax expense recognised in the statement of comprehensive loss represents the sum of the current and deferred tax.

The tax expense is based on the taxable profit for the year. Taxable profit differs from the loss as reported in the statement of comprehensive loss because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

2. ACCOUNTING POLICIES (continued)

Taxation (continued)

Tax income arises from the UK legislation regarding the treatment of certain qualifying research and development costs, allowing for the surrender of tax losses attributable to such costs in return for a tax rebate.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised.

3. SEGMENTAL ANALYSIS

The revenue and loss before tax are attributable to the one principal activity of the Company.

The net assets of the Company at 31st December 2014 and 31st December 2013 are wholly attributable to the principal activity. The Company comprises one operating segment for reporting purposes. Management measures performance and allocates resources based on the results of this one segment only.

An analysis of turnover (by location of customer) is given below:

| | 2014 | 2013 |
|--------|---------------|----------------|
| | £ | £ |
| Europe | 67,858 | 181,205 |
| | 67,858 | 181,205 |

The following customers accounted for greater than 10% of the Company's revenues:

| | 2014 | 2013 |
|------------|---------------|----------------|
| | £ | £ |
| Customer 1 | 30,000 | 120,000 |
| Customer 2 | 27,858 | - |
| Customer 3 | 10,000 | 61,205 |
| | 67,858 | 181,205 |

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

4. OPERATING LOSS

Operating loss is stated after charging/(crediting):

| | 2014 | 2013 |
|--|----------------|--------------|
| | £ | £ |
| Depreciation of owned property, plant and equipment | 19,983 | 15,205 |
| Operating lease payments: | | |
| - land and buildings | 27,940 | 27,302 |
| Net loss on foreign currency translation | 141,688 | 65,468 |
| Share option - equity settled | 5,597 | 10,296 |
| Costs relating to reverse takeover by Xenetic Biosciences Inc. | - | 1,598,692 |
| | ===== | ===== |

The Company bears the expense of share options and JSOP shares granted by its ultimate parent company to employees of the Company, and of warrants to subscribe for shares in the ultimate parent company to customers of the Company. Full details relating to share options, JSOP shares and warrants are set out in Note 14.

The operating lease payments relate to office accommodation used by the Company under a formal lease arrangement with The Crown Estates for the lease of corporate offices in London. The lease is for a period of 5 years at £32,763 per annum with an expiry date of 19th March 2017 with a break clause (exercisable at the sole discretion of the Company) after 3 years on 20th March 2015. On 20th September 2014 the Company exercised its discretion and exercised its right under the break clause to break the lease.

5. AUDITOR'S REMUNERATION

Services provided by the Company's auditor

| | 2014 | 2013 |
|---|---------------|--------------|
| | £ | £ |
| Fees payable to the Company's auditor for the audit of the Company's financial statements (2013: For the audit of the Parent Company and consolidated financial statements) | 10,000 | 404,551 |
| | ===== | ===== |

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

6. PARTICULARS OF EMPLOYEES

The remuneration of the Directors (who also comprise the group of key management personnel) paid by the Company or a subsidiary Company was as follows:

| | Salaries and short-term benefits £ | Share- based payments £ | Pension contributions £ | Total 2014 £ | Total 2013 £ |
|----------------------------------|---|----------------------------------|-------------------------------|--------------------|--------------------|
| Sir Brian Richards | - | - | - | - | - |
| Scott Maguire | 346,678 | - | 39,600 | 386,278 | 638,144 |
| Colin W. Hill | 164,307 | - | 18,432 | 182,739 | 188,530 |
| Professor Gregory Gregoriadis | 29,250 | - | - | 29,250 | 90,000 |
| Dr Dmitry D. Genkin | - | - | - | - | - |
| Firdaus J. Dastoor | - | - | - | - | - |
| Roman Knyazev | - | - | - | - | - |
| Artur Isaev | - | - | - | - | - |
| Total | 540,235 | - | 58,032 | 598,267 | 916,674 |

During the year, Scott Maguire exercised 6,200,250 options to purchase ordinary shares for 1p each and made a gain of £248,010 on the exercise of these options. During the year, no directors received additional share options under long term incentive arrangements. The charge in 2013 comprised salaries and short-term benefits of £798,600, share-based payments of £60,042 and pension contributions of £58,032.

The number of Directors who accrued benefits under pension schemes was as follows:

| | 2014 No | 2013 No |
|------------------------|------------|------------|
| Money purchase schemes | 2 | 2 |

In addition to the above, certain amounts were charged by Directors or by companies controlled by Directors to the Company or a subsidiary Company for the provision of consultancy services during the period as outlined in note 18.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

7 INCOME TAX EXPENSE

(a) Analysis of expense in the period

| | 2014 £ | 2013 £ |
|--|-----------|-----------|
| Current tax: | | |
| UK corporation tax based on the results for the year at 21.5% (2013 – 23.25%) | - | - |
| Current tax for the period | - | - |

(b) Factors affecting the tax credit for the year

The tax credit for the year differs from the standard rate of 21.5% (2013 – 23.25%) as follows:

| | 2014 £ | 2013 £ |
|---|-----------|-------------|
| Loss on ordinary activities before tax | (515,348) | (2,632,774) |
| Loss on ordinary activities multiplied by the standard rate of corporation tax | (110,800) | (612,120) |
| Effects of: | | |
| Tax effect of non-deductible items | 22,586 | 374,394 |
| Temporary timing differences on which deferred tax is not recognised | 4,296 | 3,385 |
| Unrelieved tax losses arising in the year | 83,918 | 234,341 |
| Current tax for the period | - | - |

The Company has corporation tax losses available for offset against future profits of the same trade of approximately £6,250,000 (2013 - £5,800,000). The deferred taxation asset not provided for in the accounts due to the uncertainty that future taxable profits will be available to allow recovery of the asset is approximately £1,250,000 (2013 - £1,160,000).

(c) Factors that may affect future tax charges

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realised or the liability settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

The Finance Act 2013, which includes a reduction in the UK corporate tax rate to 21% from April 2014 and 20% from April 2015 was enacted by 31 December 2014 and so UK deferred tax assets and liabilities have been calculated accordingly at 20%.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

8. PROPERTY, PLANT AND EQUIPMENT

| | Leasehold improvements £ | Plant £ | Furniture and equipment £ | Total £ |
|---|---|--------------------|--|--------------------|
| COST | | | | |
| At 1st January 2013 | 42,023 | 800,000 | 18,526 | 860,549 |
| Additions | - | - | 645 | 645 |
| | <hr/> | <hr/> | <hr/> | <hr/> |
| At 31st December 2013 and 31st December 2014 | 42,023 | 800,000 | 19,171 | 861,194 |
| | <hr/> <hr/> | <hr/> <hr/> | <hr/> <hr/> | <hr/> <hr/> |
| DEPRECIATION | | | | |
| At 1st January 2013 | 10,506 | 800,000 | 4,631 | 815,137 |
| Charge for the year | 10,506 | - | 4,699 | 15,205 |
| | <hr/> | <hr/> | <hr/> | <hr/> |
| At 31st December 2013 | 21,012 | 800,000 | 9,330 | 830,342 |
| Charge for the year | 14,262 | - | 5,721 | 19,983 |
| | <hr/> | <hr/> | <hr/> | <hr/> |
| At 31st December 2014 | 35,274 | 800,000 | 15,051 | 850,325 |
| | <hr/> <hr/> | <hr/> <hr/> | <hr/> <hr/> | <hr/> <hr/> |
| NET BOOK VALUE | | | | |
| At 31st December 2014 | 6,749 | - | 4,120 | 10,869 |
| | <hr/> <hr/> | <hr/> <hr/> | <hr/> <hr/> | <hr/> <hr/> |
| At 31st December 2013 | 21,011 | - | 9,841 | 30,852 |
| | <hr/> <hr/> | <hr/> <hr/> | <hr/> <hr/> | <hr/> <hr/> |

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

9. INTANGIBLE ASSETS

| | Intellectual Property £ |
|--|--|
| COST | |
| At 31st December 2013 and 31st December 2014 | 686,250 |

The assets acquired are assets relating to intellectual property and development rights acquired by the Company on behalf of the Group which are not used in launched products as the related products are in early stage development. These assets have not yet begun to be amortised but have been tested for impairment by assessing their value-in-use as they have an indefinite useful life. Value-in-use calculations for each drug programme to which the intellectual property is associated are utilised to calculate the recoverable amount. Key assumptions for the value-in-use calculations are as follows:

- Launch dates of products employing these technologies – launch dates reflect management’s most recent information on the expected date of launching products;
- Development costs to obtain regulatory approval – costs are estimated net of any contributions expected from collaborative arrangements with existing or future partners;
- Sales projections – these are based on management’s projections using external market data;
- Discount rates – the discount rate is estimated on a pre-tax basis reflecting the risk associated with the assets, giving a rate of 12 per cent;
- Cash flow projections – cash flow projections are made usually to the expiry of the patent which confers certain protection against generic competition; this is greater than five years;
- Probability of successful development – management estimates probabilities of success for each phase of development based on industry averages and knowledge of specific programmes.

These assets were tested for impairment at 31st December 2014. At this stage, the key sensitivity is the successful completion of clinical trials and, therefore, full impairment is expected should such trials be unsuccessful.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

10. INVESTMENTS

| | Group companies £ |
|--|-------------------------|
| COST | |
| At 31st December 2013 and 31st December 2014 | 15,145,030 |

The Company owns the whole of the issued share capital of Lipoxen Technologies Limited, a company incorporated in England and Wales engaged in research into drug delivery systems. This investment is measured at cost.

The Company also owns the entire issued share capital of SymbioTec GmbH, a company registered in Germany which is principally involved with early stage clinical trials for its patent-protected drug candidate, OncoHist. This investment is measured at cost.

The Company also owns the entire issued share capital of Xenetic Bioscience Inc., a company registered in the United States of America. This investment is held at cost.

After an impairment assessment undertaken by the board whereby the current value of the estimated future cash flows relating to the projects being undertaken by the subsidiaries on behalf of the group, it is the view of the Board that no impairment of the carrying value of the Company's investments has occurred during the year as their value in use is in excess of the carrying value.

11. TRADE AND OTHER RECEIVABLES

| | 2014 £ | 2013 £ |
|-----------------------------------|-------------------|-------------------|
| Due in more than one year: | | |
| Receivables from subsidiaries | 15,036,240 | 12,717,711 |
| Loan to JSOP Trustees | - | 3,350,666 |
| | <u>15,036,240</u> | <u>16,068,377</u> |
| Due within one year: | | |
| Receivables from subsidiaries | 2,338,259 | 1,597,838 |
| Receivables from parent | 120,192 | - |
| Other receivables | 59,823 | 135,170 |
| Prepayments and accrued income | 21,433 | 19,370 |
| | <u>2,539,707</u> | <u>1,752,378</u> |

The Company's receivables from its subsidiaries and parent are payable on demand. It is the view of the Board that no impairment of the carrying value of the Company's trade and other receivables has occurred during the year.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

12. TRADE AND OTHER PAYABLES

| Current | 2014 | 2013 |
|-------------------------------|----------------|------------------|
| | £ | £ |
| Trade payables | 74,001 | 543,864 |
| Loan payable to related party | 253,368 | 413,053 |
| Other payables | - | 6,938 |
| Accrued expenses | 223,609 | 742,003 |
| | <u>550,978</u> | <u>1,705,858</u> |

13. SHARE CAPITAL

| | 2014 | | 2013 | |
|---|------|----------|----------------|------------------|
| | No | £ | No | £ |
| Allotted, called up and fully paid | | | | |
| Ordinary shares of 0.5p each | 1 | - | 408,048,486 | 2,040,242 |
| Deferred shares of 0.01p each | Nil | - | 16,335,000,000 | 1,633,500 |
| | | <u>-</u> | | <u>3,673,742</u> |

Deferred shares

The rights attached to the deferred shares are as follows:

- (a) no entitlement to any dividend;
- (b) on a winding-up, an entitlement to receive an amount equal to the nominal value of each share, but only after an amount of £50,000,000 per share has been paid to the holders of the issued and fully paid ordinary 0.5 pence shares;
- (c) no right to attend or vote at a general meeting; and
- (d) an obligation to permit the Company to transfer the shares to such person as the Company may determine, without receiving any payment.

Significant event

Following the exercise of share options, 6,200,250 ordinary shares were issued on 22nd January 2014 for a cash consideration of £62,003.

On 23rd January 2014, the High Court of England and Wales sanctioned a Scheme of Arrangement ("SoA") voted through by shareholders on 17th December 2013. Xenetic Biosciences Inc., the ultimate parent company incorporated in the United States of America, consummated a reverse merger ("the Acquisition") pursuant to a written plan of reorganisation, in which the ultimate parent company merged with Xenetic Biosciences (UK) Limited, such that Xenetic Biosciences (UK) Limited became a wholly

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

13. SHARE CAPITAL (continued)

Significant event (continued)

owned subsidiary of Xenetic Biosciences Inc. Upon completion of the Acquisition, Xenetic Biosciences Inc. acquired all issued and outstanding shares of capital stock of Xenetic Biosciences (UK) Limited. As a result, 132,545,504 shares of the Xenetic Biosciences, Inc.'s common stock were newly issued and, immediately following the Acquisition, there were 136,045,504 shares of common stock issued and outstanding.

As part of this SoA, the Company issued 1 Ordinary Share of £0.005 to Xenetic Biosciences Inc. at par for cash and the pre-existing entire share capital of the Company (post the exercise of certain share options as discussed below) was reduced to nil and all shares were extinguished and immediately a capital redemption reserve equal to the total amount of share capital was created. In addition, all amounts held within reserves for shares to be issued at the date of the SoA referred to above were transferred to the ultimate parent company as the shares are to be issued by Xenetic Biosciences Inc.

14 SHARE BASED PAYMENT TRANSACTIONS

Significant event

On 23rd January 2014, Xenetic Biosciences Inc., the ultimate parent company incorporated in the United States of America, consummated a reverse merger ("the Acquisition") pursuant to a written plan of reorganisation, in which the ultimate parent company merged with Xenetic Biosciences (UK) Limited, such that Xenetic Biosciences (UK) Limited became a wholly owned subsidiary of Xenetic Biosciences Inc. Upon completion of the Acquisition, Xenetic Biosciences, Inc. acquired all issued and outstanding shares of capital stock of Xenetic Biosciences (UK) Limited.

As part of the events referred to above, all options and warrants previously held in the Company prior to the 23rd January 2014 were transferred to the new parent company, Xenetic Biosciences Inc (NASDAQ:XBIO), at a rate of 56 share options or warrants in Xenetic Biosciences Inc. for every 175 share options or warrants previously held in this Company.

Share options

Prior to the Acquisition outlined above the Company utilised two forms of share option plan, being:

1. the Lipoxen plc Unapproved Share Option Plan (the "Unapproved Plan"); and,
2. the Lipoxen plc 2007 Share Option Scheme incorporating Enterprise Management Incentives (EMI) provisions ("the EMI Plan").

Share options are held by option holders in either the Unapproved Plan or the EMI plan. All options in both plans are settled in equity when the options are exercised. Since the formal adoption of the 2007 Scheme at the Company's AGM held in July 2009 employee awards have been made only under the more recent plan by virtue of the favourable tax treatment that this plan can confer on both the Company and awardees.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

14 SHARE BASED PAYMENT TRANSACTIONS (continued)

Share options (continued)

Subsequent to the acquisition, the Unapproved plan and the EMI plan were converted to reflect the new shares issued by the ultimate parent company under the Scheme of Arrangement related to the acquisition. As part of the conversion, option holders under the Unapproved and EMI plans have the right to subscribe for a number of shares of common stock in the ultimate parent company (the "Replacement Option Shares"). The number of replacement option shares is determined in the same manner in which the shareholders of Xenetic Biosciences (UK) Limited were given the right to acquire shares of common stock in the ultimate parent company according to the acquisition.

The aggregate exercise price payable in US dollars for replacement option shares is the same as the aggregate exercise price in pounds sterling of the original options, using a foreign currency exchange rate for pounds sterling into US dollars quoted by Barclays Bank plc at 12 noon Greenwich Mean Time on 23 January 2014, the date of the acquisition.

The Company continues to bear the expense of share options now granted by the ultimate parent company to employees of the Company for services to the Company and of warrants to subscribe for shares in its ultimate parent company to customers of the Company.

All options are settled in equity when the options are exercised. Options vest based on one or more of: time employed by the group, individual performance, and market performance. The maximum term of options is 10 years. The IFRS2 share option charge incurred by the company in respect of the expense it bears for employees and customers for the year was £5,597 (2013: £10,296). As these amounts are immaterial, no further disclosures are required.

Shares issued under the Joint Share Ownership Plan (JSOP)

In 2012 XENUK issued 28,082,127 ordinary shares in under the terms of its JSOP. Following the significant events that occurred on 23rd January 2014 all of these JSOP shares were transferred to the new parent company, Xenetic Biosciences Inc. (NASDAQ: XBIO) on the basis outlined above.

In 2010 XENUK issued 5,318,479 ordinary shares under the terms of its JSOP. Following the significant events that occurred on 23rd January 2014 all of these JSOP shares were transferred to the new parent company, Xenetic Biosciences Inc. (NASDAQ: XBIO) on the basis outlined.

Share warrants

The Company previously granted warrants to subscribe for 7,500,000 Ordinary Shares to Serum Institute of India Limited in January 2012 with further warrants issued to Synbio LLC for 11,080,000 Ordinary shares in 2011 and warrants issued to Baxter International Inc. for 14,338,430 Ordinary Shares in 2010.

On 23rd January 2014, all of these warrants were transferred to the new parent company, Xenetic Biosciences Inc. (NASDAQ: XBIO) on the basis outlined above.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

15. RECONCILIATION OF LOSS BEFORE TAXATION TO NET CASH FLOW FROM OPERATING ACTIVITIES

| | 2014 | 2013 |
|---|--------------------|--------------------|
| | £ | £ |
| Loss before taxation | (419,002) | (2,632,774) |
| Adjustments for: | | |
| Shares to be issued | (91,663) | 91,663 |
| Capital contribution | 5,597 | - |
| Depreciation | 19,983 | 15,205 |
| Investment income | - | (52,508) |
| Finance costs | - | - |
| | (485,085) | (2,578,414) |
| Decrease/(increase) in receivables | 3,683,667 | (634,125) |
| (Decrease)/increase in payables | (1,154,880) | 948,654 |
| Net cash inflow/(outflow) from operating activities | 2,043,702 | (2,263,885) |

16. CASH AND CASH EQUIVALENTS

| | 2014 | 2013 |
|--|--------------------|--------------------|
| | £ | £ |
| Cash and cash equivalents at beginning of year | 2,896,446 | 6,863,403 |
| Net movement in cash and cash equivalents in the year | (1,429,499) | (3,966,957) |
| Cash and cash equivalents at end of year (see Note 17) | 1,466,947 | 2,896,446 |

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

17. FINANCIAL INSTRUMENTS

Financial assets and liabilities were held as follows:

| | 2014 | 2013 |
|---|-------------------|-------------|
| | £ | £ |
| Assets | | |
| Loans and receivables: | | |
| Receivables from subsidiaries | 17,494,691 | 14,315,549 |
| Loan to JSOP Trustees | - | 3,350,666 |
| Cash and cash equivalents | 1,466,947 | 2,896,446 |
| Total financial assets | 18,961,638 | 20,562,661 |
| Liabilities | | |
| Financial liabilities measured at amortised cost: | | |
| Trade payables | 74,001 | 543,864 |
| Loan from related party | 253,368 | 413,053 |
| Accrued expenses | 223,609 | 742,003 |
| Total financial liabilities | 550,978 | 1,698,920 |

The Company is a holding company. Whilst it is therefore exposed to some financial risk this is significantly less than a trading company which has significant receivables, payables and inventories.

The Directors consider that the carrying value of the financial assets and financial liabilities approximates their fair value.

The Company is not subject to credit risk and foreign currency risk of trade receivables as it had no such balances at either balance sheet date. The trade payables are considered to have a maturity date of 3 months or less. Of the amounts due by related parties, a net credit balance of £ 645,276 is denominated in a currency other than Sterling and is subject to exchange rate fluctuations. Financial instruments to mitigate exchange rate risk are not used by the Company.

All financial liabilities (except for amounts owed to group undertakings) are payable within 12 months. The loans from related parties are denominated in US dollars and is subject to exchange rate fluctuations. Financial instruments to mitigate exchange rate risk are not used by the Company.

Cash and cash equivalents comprise cash on hand of £178 and balances at bank of £1,466,769, of which £1,337,407 is held in US dollar denominated accounts and £17,625 is held in euro denominated accounts. Whilst the bank balances are held with a reputable financial institution, the maximum exposure to credit risk is the carrying value of the balances as disclosed above.

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XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

17. FINANCIAL INSTRUMENTS (continued)

A 5% increase or decrease in the US dollar/sterling exchange rate would have increased or decreased the reported sterling carrying amount of the US dollar denominated financial assets by approximately £67,000 and the US dollar financial liabilities by approximately £12,500. A 5% increase or decrease in the euro/sterling exchange rate would have had an immaterial impact on the carrying amounts of the euro denominated financial assets and liabilities.

Foreign currency risk

Foreign currency risk refers to the risk that the value of a financial commitment or recognised asset or liability will fluctuate due to changes in foreign currency exchange rates. The Company monitors its foreign currency risk through cash flow forecasting and currency is held in foreign currency bank accounts only to the extent that it is required for operational activities.

Interest rate risk

Interest rate risk is the risk that the value of a financial instrument or cash flows associated with it will fluctuate due to changes in market interest rates.

The Company has financial assets in the form of cash and cash equivalents. These are considered to be short term liquid assets and as a result the exposure to interest rate risk is not considered to be significant.

On this basis no sensitivity analysis has been prepared on the grounds that there would not be a material impact on either the carrying values of the respective assets, the net loss for the year or the equity at the end of the period.

Liquidity risk

The Company maintains sufficient cash and cash equivalents. Management reviews cashflow forecasts to determine whether the Company has sufficient cash reserves to continue with its principal activities. The Company has no significant external financial liabilities and no external borrowings outside the Xenetic Biosciences Inc. group.

Capital management

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern. The Company has no external debt and does not therefore have a strategy in terms of maintaining a certain debt to equity ratio. Rather capital is managed with a view to generating further cash and cash equivalents which can be used in the furtherance of the Company's aims and objectives.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

18. RELATED PARTY TRANSACTIONS

The Company (including its subsidiary) was charged the following amounts by Directors or by companies controlled by Directors for the provision of consultancy services:

| | 2014 | 2013 |
|--------------------|---------------|-------------|
| | £ | £ |
| Sir Brian Richards | 25,000 | 75,000 |
| Dr Dmitry Genkin | 17,000 | 51,000 |
| Firdaus Dastoor | 1,000 | 3,000 |
| Roman Knyazev | 1,000 | 3,000 |
| Artur Isaev | 1,000 | 3,000 |

Synbio LLC

During 2011 the Company negotiated a short term unsecured loan facility of up to \$1.70 million from Synbio LLC, a company which is now a substantial shareholder in the Company. This loan bears interest (rolled up) at 0.67% per month and is repayable by agreement between the parties. The balance owed to Synbio LLC at 31st December 2014 was £253,368 (2013 - £413,053). This loan was subsequently settled in December 2016.

Xenetic Biosciences Inc.

During the year, the Company has advanced monies to its Parent Company, Xenetic Biosciences Inc. on an interest free basis. The balance owed by Xenetic Biosciences Inc. at 31st December 2014 was £120,192.

Lipoxen Technologies Limited

The Company charged a management charge of £30,000 (2013 - £120,000) to its subsidiary, Lipoxen Technologies Limited, during the year. The Company continued to advance monies to the subsidiary during the year to fund the ongoing development of the Group's technology. The balance receivable from the subsidiary at 31st December 2014 was £15,036,240 (2013 - £12,717,711).

SymbioTec GmbH

The Company has advanced monies on loan to its subsidiary, SymbioTec GmbH. This loan bears interest (rolled up) at 0.85% per month and is repayable upon demand at any time. The balance owed by SymbioTec GmbH at 31st December 2014 was £360,937 (2013 - £324,386). The Company charged a management charge of £27,858 to SymbioTec during the year and advanced monies to fund the ongoing development of SymbioTec's technology. The balance owed by SymbioTec to the Company at 31st December 2014, excluding the loan referred to above, was £759,392 (2013 - £768,094).

Xenetic Bioscience Inc.

The Company advanced monies to its subsidiary, Xenetic Bioscience Inc., to fund its operations. The balance owed at 31st December 2014 was £1,217,930 (2013 - £505,358).

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

19. SUBSEQUENT EVENTS

The subsequent events note covers the period from 1st January 2015 to the date of this Report. While detailed disclosures and public statements have been made on a continuing basis by XBIO (the Company's Ultimate Holding Company – "UHC") in the USA, the principal subsequent events that have occurred at a Group level are summarised below under the headings of "Key Clinical Updates" and "Key Financial and Board Updates". Clinical updates relate to the business and IP of the Company and its subsidiaries while Financial and Board updates relate to the overall XBIO Group.

Key Clinical Updates

On 14 July 2015, XBIO announced that it has completed treatment of the second cohort of its Phase 2 dose-escalation study with its lead drug candidate ErepoXen® for the treatment of anaemia in pre-dialysis chronic kidney disease patients. The 12 patients enrolled in this cohort received a biweekly injection of ErepoXen® until haemoglobin levels reached the therapeutic range. The patients then received injections of ErepoXen® every 4 weeks (extended dosing interval) during maintenance for a total trial time of 17 weeks.

On 16th September 2015, XBIO announced that it has commenced the third cohort of its Phase 2 dose-escalation study with its lead drug candidate ErepoXen® for the treatment of anaemia in pre-dialysis chronic kidney disease patients. In an effort to accelerate the recruitment rate, Xenetic has expanded the clinical research sites beyond Australia to now include locations in South Africa. Subjects from this third cohort study will receive injections of ErepoXen® every two weeks until haemoglobin levels reach therapeutic levels. The patients will then receive injections of ErepoXen® every 4 weeks (extended dosing interval) during maintenance for a total trial time of 17 weeks.

The data from the second cohort showed that 91% of the enrolled patients had an increase in haemoglobin levels over time, and that in 75% of the enrolled patients, haemoglobin levels rose into the therapeutic range. The third cohort is designed to further increase the patient's haemoglobin levels into mid-therapeutic range. The study is being performed at nine clinical sites in Australia and six new clinical sites in South Africa. Patient treatment has commenced in Australia. National and local regulatory approvals have been granted in South Africa and patient treatment is expected to start in September. This cohort is expected to be completed in Q2, 2016.

On 18th August 2016, XBIO announced that it has commenced a collaboration with Excivion Ltd. ("Excivion") to develop a vaccine against Zika and dengue viruses. As part of the collaboration, Xenetic's proprietary IMUXEN™ Technology will be used to develop the vaccine. Excivion is a private UK company that has developed a proprietary antigen design platform for viral vaccines which it is applying to flavivirus infections.

On 19th August 2016, XBIO announced that an Investigational New Drug (IND) application for the Group's product candidate, Virexxa® (sodium cridanimod), has been allowed to proceed by the U.S. Food and Drug Administration (FDA). This enables Xenetic to initiate a Phase 2 clinical study of Virexxa in conjunction with progestin therapy for the

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

19. SUBSEQUENT EVENTS (continued)

Key Clinical Updates (continued)

treatment of endometrial cancer in women with recurrent or persistent disease who have failed progestin monotherapy. The primary objective of the study is to assess the anti-tumour activity of Virexxa. Secondary objectives include assessment of additional efficacy, pharmacokinetic and safety/tolerability parameters. Further translational objectives are to observe the effect of Virexxa in combination with progestins, on the levels of progesterone receptor (PrR) and activated progesterone receptors (APrR) in tumour tissues.

On 10th October 2016, XBIO announced positive topline data from the third cohort of its Phase 2 dose-escalation study with its lead drug candidate ErepoXen® for the treatment of anaemia in pre-dialysis chronic kidney disease patients. This trial is being conducted for Xenetic by Novotech (Australia) Pty Ltd.

The third cohort of the Phase 2, open label, sequential dose finding study to evaluate the safety, pharmacodynamics (PD) and pharmacokinetics (PK) of multiple doses of ErepoXen was launched in October 2015 and was conducted in Australia and South Africa. As in the previous cohorts, patients in the third cohort of this study received injections of ErepoXen every two weeks until haemoglobin levels reached therapeutic levels. The patients then received injections of ErepoXen every 4 weeks (extended dosing interval) during maintenance for a total trial time of 17 weeks.

Professor Simon D Roger M.D., FRACP, Director of Renal Medicine, Gosford Hospital, Australia and Principal Investigator of the study, said, "The results achieved with ErepoXen® in these individuals with chronic kidney disease expand on the initial two cohorts, and, continue to demonstrate a reassuring safety profile. I am very pleased about the potential for ErepoXen® to act as a therapeutic agent to treat these anaemic patients and look forward to the continued study of this compound to achieve further results."

On January 6, 2017, XBIO announced that Xenetic has received a \$3 million milestone payment from Shire plc (LSE: SHP, NASDAQ: SHPG) related to Shire's advancing the Phase 1/2a clinical study for the PSA-Recombinant SHP656 or Factor VIII ("FVIII") being developed as a long-acting therapeutic for the treatment of haemophilia. The stated goal of Shire is to introduce an innovative FVIII protein that can significantly prolong the circulating half-life of the FVIII protein, with the objective of providing a once weekly treatment or reaching higher trough activity levels for greater efficacy.

Key Financial and Board Updates

On 8 July 2015, XBIO completed a US\$ 3 million Bridge Note Financing with OJSC Pharmsynthez ("Pharmsynthez") a collaborative partner of XBIO. The financing was completed by means of a 10% Convertible Promissory Note, convertible (at the option of Pharmsynthez) in whole or in part into shares of Common Stock of XBIO. Pharmsynthez also received certain 5 year warrants to purchase shares of Common Stock of XBIO.

Readers are directed to the Form 8-K filed by XBIO on 8 July 2015 for further material information regarding the Bridge Note Financing.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

19. SUBSEQUENT EVENTS (continued)

Key Financial and Board Updates (continued)

On 16 November 2015, XBIO announced that it has entered into an Asset Purchase Agreement (the "APA") with AS Kevelt, an Estonian biotech company ("Kevelt") and OJSC Pharmsynthez ("Pharmsynthez", and together with Kevelt, "Sellers"). Pursuant to the APA, the Sellers will transfer to LTL certain intellectual property rights with respect to Virexxa™, and LTL, will receive the worldwide rights to develop, market and license Virexxa for all uses, except for certain excluded uses within the Commonwealth of Independent States (the "CIS"), in exchange for 111.5 million shares of XBIO common stock and certain other consideration. Virexxa is a Phase II oncology drug candidate which is under investigation for the treatment of certain endometrial cancers. As part of this total consideration, the Group will also acquire Kevelt's U.S. Orphan Drug designation for the use of Virexxa in the treatment of progesterone receptor negative endometrial cancer in conjunction with progesterone therapy. This transaction was completed on 29 April 2016 with an effective date of 27 April 2016 as confirmed in a Form 8-K filed with the SEC on 3 May 2016.

The APA also contains a financing component wherein XBIO will receive from Pharmsynthez up to \$3.5 million in bridge financing and a commitment of an additional \$6.5 million in financing as part of a planned Capital Raise of at least \$15 million and up-list to a national securities exchange. On 1 July 2016 XBIO received a further \$0.5 million bridge advance and on 26 August 2016 and 9 September 2016, XBIO issued promissory notes for \$0.178m and \$0.322m, respectively to Pharmsynthez. These promissory notes are convertible into common stock shares at any time at a conversion price of \$4.95 per share (subject to usual and customary adjustments) or may be applied towards the Offering at the option of Pharmsynthez. This has reduced the amount remaining available to participate in the Capital Raise to \$5.5 million.

On 29 February 2016, XBIO announced the appointment of renowned chemist and Nobel Laureate, Dr. Roger D. Kornberg to the XBIO Board of Directors.

Dr. Kornberg is a member of the U.S. National Academy of Sciences and the Winzer Professor of Medicine in the Department of Structural Biology at Stanford University. He earned his bachelor's degree in chemistry from Harvard University in 1967 and his Ph.D. in chemical physics from Stanford in 1972. He became a postdoctoral fellow at the Laboratory of Molecular Biology in Cambridge, England and then an assistant professor of biological chemistry at Harvard Medical School in 1976, before moving to his present position as professor of structural biology at Stanford Medical School in 1978.

In 2006, Dr. Kornberg was awarded the Nobel Prize in Chemistry in recognition for his studies of the molecular basis of Eukaryotic Transcription, the process by which DNA is copied to RNA. Dr. Kornberg is also the recipient of several awards, including the 2001 Welch Prize, the highest award granted in the field of chemistry in the United States, and the 2002 Leopold Mayer Prize, the highest award granted in the field of biomedical sciences from the French Academy of Sciences.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

19. SUBSEQUENT EVENTS (continued)

Key Financial and Board Updates (continued)

On 1 June 2016, XBIO announced that its Board of Directors approved a proportional 1-for-33 reduction and reverse stock split of its issued and outstanding common stock in preparation for its planned uplisting to the NASDAQ Capital Market ("NASDAQ"). The reverse stock split became effective and its common stock began trading on a post-split basis at the open of trading on Wednesday June 1, 2016.

The reverse stock split is intended to fulfil the stock price requirements for listing on NASDAQ since the requirements include that XBIO's common stock must maintain a minimum closing price for 30 of 60 trading days.

On 11 July 2016, XBIO announced that it has appointed Jeffrey F. Eisenberg to XBIO's Board of Directors.

Mr. Eisenberg is a life sciences executive with over 20 years of operational experience and a successful track record in value creation in both private and public companies. Over the course of his career, he has led all crucial areas of R&D, operations, manufacturing/quality, business development, strategic partnering, product development, commercialization, and talent management.

On 1st November 2016, XBIO announced its common stock will begin trading on The NASDAQ Capital Market under the symbol "XBIO" on November 7, 2016. XBIO also announced the pricing of its public offering of an aggregate of 2,424,242 units, consisting of (i) 484,849 units, consisting of one share of Convertible Series B Preferred Stock and a Class A Warrant to purchase one share of common stock and (ii) 1,939,393 units consisting of one share of Convertible Series B Preferred Stock and a Class B Warrant to purchase one share of common stock, at a public offering price of \$4.125 per unit. The total gross proceeds of the public offering were approximately \$10 million before the underwriter's discount and expenses.

In connection with its new listing on The NASDAQ Capital Market, November 4, 2016 was the last day Xenetic's common stock will trade on the OTCQB.

On 5th November 2016, XBIO announced it has appointed Jeffrey F. Eisenberg as Chief Operating Officer.

Mr. Eisenberg is a life science executive with over 20 years of operational experience who has been serving on Xenetic's Board of Directors since July 2016. Over the course of his career, Mr. Eisenberg has led all crucial areas of R&D, operations, manufacturing/quality, business development, strategic partnering, product development, commercialization, and talent management.

On 7th November 2016, XBIO announced the closing of its public offering of an aggregate of 2,424,242 units, consisting of (i) 484,849 units, consisting of one share of Convertible Series B Preferred Stock and a Class A Warrant to purchase one share of common stock and (ii) 1,939,393 units consisting of one share of Convertible Series B Preferred Stock and a Class B Warrant to purchase one share of common stock, at a public offering price of \$4.125 per unit. OPKO Health, Inc. (NASDAQ:OPK) along with other healthcare institutional investors participated in the offering.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

19. SUBSEQUENT EVENTS (continued)

Key Financial and Board Updates (continued)

As previously announced, in connection with the closing of its public offering, XBIO commenced trading of its common stock on 7th November 2016 on The NASDAQ Capital Market under the symbol "XBIO."

Ladenburg Thalmann & Co. Inc. acted as the sole book running manager for the offering.

The total gross proceeds of the public offering are approximately \$10 million before the underwriter's discount and expenses. The net proceeds from this offering will be used to fund the research and development of Xenetic's product candidates, including Virexxa, as well as future development programs, potential in licensing of products or technology, potential in licensing of products or technology, capital expenditures, working capital, repayment of existing indebtedness, and other general corporate purposes.

The shares and warrants described above were offered by Xenetic pursuant to a registration statement on Form S-1 previously filed with, and subsequently declared effective by the Securities and Exchange Commission ("SEC"). A final prospectus supplement relating to the offering was filed with the SEC and is available, along with the accompanying base prospectus, on the SEC's website at <http://www.sec.gov> or from Ladenburg Thalmann & Co. Inc., Prospectus Department, 570 Lexington Avenue, 11th Floor, New York, New York 10022, by calling (212) 409-2000.

On 22nd November 2016, XBIO announced that it has appointed Edward J. Benz, Jr., M.D., to XBIO's Board of Directors.

Dr. Benz is a renowned expert in blood disorders and is board certified in both haematology and internal medicine. He is an active clinical haematologist and a National Institutes of Health (NIH) funded researcher with a focus on the molecular basis and genetics around inherited blood disorders. Prior to joining the Xenetic Board, Dr. Benz served as President and CEO Emeritus of Dana-Farber Cancer Institute and the Richard and Susan Smith Professor of Medicine and Professor of Genetics at Harvard Medical School. During Dr. Benz's tenure at Dana-Farber, the institute experienced exponential growth, including an increase of fund-raising to more than \$200 million a year from a network of 300,000 donors, a tripling of the number of patients seeking treatment, and a growth in revenues from \$265 million to more than \$1 billion.

On 4th January 2017, XBIO announced that it has appointed Curtis A. Lockshin, Ph.D. as Chief Scientific Officer.

Dr. Lockshin is a life science executive with an extensive background in cross-functional R&D management, with a particular focus on drug discovery, preclinical and clinical development. Dr. Lockshin is an inventor on numerous patents related to small-molecule therapeutics, biomaterials and optical biosensors.

On January 6, 2017, XBIO announced that Xenetic has received a \$3 million milestone payment from Shire plc (LSE: SHP, NASDAQ: SHPG) related to Shire's advancing the Phase 1/2a clinical study for the PSA-Recombinant SHP656 or Factor VIII ("FVIII") as noted in the clinical update section above.

XENETIC BIOSCIENCES (UK) LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31st DECEMBER 2014

19. SUBSEQUENT EVENTS (continued)

Key Financial and Board Updates (continued)

Readers are directed both to the current SEC filings by XBIO and to the XBIO website for details of all events that have been the subject to Press Releases and/or SEC filings in the period 1 January 2015 to the date of this Report.

20. GENERAL INFORMATION

The Company is a private limited company incorporated and domiciled in England and Wales. The Company is principally engaged as a holding company.

With effect from 23rd January 2014, Xenetic Biosciences, Inc., a company incorporated in the United States of America, has been the Company's immediate and ultimate parent company. Prior to this date, the Company had no parent company.

Accounts for the group can be obtained from 99 Hayden Ave, STE 230, Lexington, MA 02421, United States of America or www.xeneticbio.com.

There was no ultimate controlling party in 2014 or 2013.