Financial statements

Consolidated interim financial statements for the first nine months of 2017

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Pharmacovigilance Officer

Consolidated interim financial statements

Consolidated statements of income and comprehensive income
(unaudited)

Consolidated income statement

	Nine months ended 30 September	
(thousands of €, except share and per share data)	**2017**	**2016**
Revenues	87,870	50,009
Other income	18,484	15,031
Total revenues and other income	**106,354**	**65,040**
Research and development expenditure	(149,226)	(96,739)
General and administrative expenses	(17,783)	(15,511)
Sales and marketing expenses	(1,898)	(1,272)
Total operating expenses	**(168,907)**	**(113,522)**
Operating loss	**(62,552)**	**(48,482)**
Fair value re-measurement of share subscription agreement	–	57,479
Other financial income	3,663	2,642
Other financial expenses	(26,805)	(3,500)
Profit / loss (–) before tax	**(85,694)**	**8,138**
Income taxes	(161)	(71)
Net income / loss (–)	**(85,855)**	**8,067**
Net income / loss (–) attributable to:		
Owners of the parent	(85,855)	8,067
Basic income / loss (–) per share	**(1.75)**	**0.18**
Diluted income / loss (–) per share	**(1.75)**	**0.17**
Weighted average number of shares – basic (in thousands of shares)	48,996	45,527
Weighted average number of shares – diluted (in thousands of shares)	48,996	47,054

Consolidated statements of comprehensive income

	Nine months ended 30 September	
(thousands of €)	2017	2016
Net income / loss (–)	**(85,855)**	**8,067**
Items that may be reclassified subsequently to profit or loss:		
Fair value adjustment of available-for-sale financial assets	(62)	(122)
Translation differences, arisen from translating foreign activities	(569)	(816)
Other comprehensive income, net of income tax	**(631)**	**(938)**
Total comprehensive income attributable to:		
Owners of the parent	(86,486)	7,129

Consolidated statements of financial position
(unaudited)

(thousands of €)	30 September 2017	31 December 2016
Assets		
Intangible assets	747	1,023
Property, plant and equipment	15,279	14,961
Deferred tax assets	1,957	1,957
Non-current R&D incentives receivables	65,894	54,188
Non-current restricted cash	1,215	1,098
Other non-current assets	2,442	2,880
Non-currents assets	**87,535**	**76,107**
Inventories	304	300
Trade and other receivables	7,481	9,728
Current R&D incentives receivables	10,259	10,154
Cash and cash equivalents	1,218,856	973,241
Current restricted cash	–	6,570
Other current assets	6,939	7,239
Current assets	**1,243,838**	**1,007,232**
Total assets	**1,331,373**	**1,083,338**
Equity and liabilities		
Share capital	233,192	223,928
Share premium account	992,893	649,135
Other reserves	(1,062)	(1,000)
Translation differences	(1,659)	(1,090)
Accumulated losses	(186,432)	(112,272)
Total equity	**1,036,932**	**758,701**
Pension liabilities	3,734	3,520
Provisions	56	63
Finance lease liabilities	–	9
Other non-current liabilities	1,534	2,469
Non-current deferred income	134,586	214,785
Non-current liabilities	**139,910**	**220,846**

(thousands of €)	30 September 2017	31 December 2016
Finance lease liabilities	23	54
Trade and other payables	48,437	31,269
Current tax payable	835	1,022
Accrued charges	1,391	619
Deferred income	103,845	70,827
Current liabilities	**154,530**	**103,791**
Total liabilities	**294,440**	**324,637**
Total equity and liabilities	**1,331,373**	**1,083,338**

Consolidated cash flow statements
(unaudited)

	Nine months ended 30 September	
(thousands of €)	2017	2016
Cash and cash equivalents at beginning of year	**973,241**	**340,314**
Net income / loss (–)	(85,855)	8,067
Adjustments for:		
Tax expense	161	71
Other net financial expenses	23,142	858
Fair value re-measurement of share subscription agreement	–	(57,479)
Depreciation of property, plant and equipment	2,701	2,428
Amortization of intangible fixed assets	510	649
Net realized loss on foreign exchange transactions and net other financial expenses paid	(503)	(192)
Share-based compensation	11,697	7,201
Decrease in provisions	(8)	(5)
Increase in pension liabilities	214	183
Gain on sale of fixed assets	–	(14)
Operating cash flows before movements in working capital	**(47,942)**	**(38,232)**
Increase in inventories	(3)	(1)
Increase in receivables	(8,240)	(14,727)
Increase / decrease (–) in payables	16,464	(1,841)
Increase / decrease (–) in deferred income	(47,180)	258,878
Cash generated / used (–) in operations	**(86,901)**	**204,077**
Interest paid	(42)	(37)
Interest received	903	726
Income taxes paid	(191)	(477)
Net cash flows generated / used (–) in operating activities	**(86,231)**	**204,289**
Purchase of property, plant and equipment	(2,986)	(3,627)
Purchase of and expenditure in intangible fixed assets	(233)	(250)
Proceeds from disposal of property, plant and equipment	–	23
Increase (–) / decrease in restricted cash	6,453	(54)
Acquisition of (–) / proceeds from sale of available-for-sale financial assets	372	(2,750)
Net cash flows generated / used (–) in investing activities	**3,605**	**(6,657)**

(thousands of €)	Nine months ended 30 September 2017	2016
Repayment of obligations under finance leases and other debts	(50)	(41)
Proceeds from capital and share premium increases, net of issue costs	348,133	391,785
Proceeds from capital and share premium increases from exercise of warrants	4,935	3,489
Net cash flows generated in financing activities	**353,018**	**395,233**
Effect of exchange rate differences on cash and cash equivalents	**(24,777)**	**(2,371)**
Increase in cash and cash equivalents	**245,615**	**590,493**
Cash and cash equivalents at end of the period	**1,218,856**	**930,807**

Consolidated statements of changes in equity
(unaudited)

(thousands of €)	Share capital	Share premium account	Translation differences	Other reserves	Accumul. losses	Total
On 1 January 2016	**185,399**	**357,402**	**(467)**	**(18)**	**(177,317)**	**364,999**
Net income					8,067	8,067
Other comprehensive income			(816)	(122)		(938)
Total comprehensive income			**(816)**	**(122)**	**8,067**	**7,129**
Share-based compensation					7,201	7,201
Issue of new shares	36,575	289,696				326,271
Share issue costs	(269)					(269)
Exercise of warrants	1,756	1,732				3,489
On 30 September 2016	**223,462**	**648,830**	**(1,283)**	**(140)**	**(162,048)**	**708,822**
On 1 January 2017	**223,928**	**649,135**	**(1,090)**	**(1,000)**	**(112,272)**	**758,701**
Net loss					(85,855)	(85,855)
Other comprehensive income			(569)	(62)		(631)
Total comprehensive income			**(569)**	**(62)**	**(85,855)**	**(86,486)**
Share-based compensation					11,697	11,697
Issue of new shares	23,331	340,593				363,924
Share issue costs	(15,837)					(15,837)
Exercise of warrants	1,770	3,165				4,935
On 30 September 2017	**233,192**	**992,893**	**(1,659)**	**(1,062)**	**(186,432)**	**1,036,932**

Notes

Basis of preparation

These condensed interim financial statements have been prepared in accordance with IAS 34 *'Interim Financial Reporting'* as adopted by the European Union. The condensed interim financial statements do not contain all information required for an annual report and should therefore be read in conjunction with Galapagos' 2016 annual report.

The condensed interim financial statements were subject to a limited review by the statutory auditor, but have not been audited.

Details of the unaudited interim results

Revenues and other income

Revenues

The following table summarizes our revenues for the nine months ended 30 September 2017 and 2016.

	Nine months ended 30 September	
(thousands of €)	**2017**	**2016**
Recognition of non-refundable upfront payments and license fees	53,526	17,562
Milestone payments	25,918	17,567
Reimbursement income	2,319	9,238
Other revenues	6,108	5,641
Total revenues	**87,870**	**50,009**

Revenues for the nine months ended 30 September 2017 (€87.9 million vs. €50.0 million for the nine months ended 30 September 2016) were higher due to increased revenue recognition of the upfront payment from Gilead related to the filgotinib program, which is recognized in function of the costs incurred, and due to an increase in milestone payments.

The following table summarizes the revenue recognition of upfront payments and license fees for the nine months ended 30 September 2017 and 2016.

Agreement	Upfront received	Upfront and license fees received	Recognition as from	Revenue recognized, nine months ended 30 September 2017	Revenue recognized, nine months ended 30 September 2016	Outstanding balance in deferred income as at 30 September 2017
	(thousands of $)	(thousands of €)		(thousands of €)		
Gilead collaboration agreement for filgotinib	300,000	275,558	January 2016	46,632	14,500	203,305
Gilead collaboration agreement for filgotinib	N.A.	39,003(*)	January 2016	6,600	2,052	28,776
ThromboGenics license agreement for integrin antagonists	N.A.	1,000	April 2016		1,000	
Sirion Biotech license agreement for RNA interference (RNAi) technologies	N.A.	10	June 2016		10	
Servier collaboration agreement for osteoarthritis	N.A.	6,000	August 2017	293		5,707
Total recognition of non-refundable upfront payments and license fees				**53,526**	**17,562**	**237,788**

(*) deferred income of €39 million recognized upon signing of the share subscription agreement with Gilead as required under IAS 39.

For the first nine months of 2017, €53.2 million of deferred income related to the Gilead collaboration agreement was recognized as revenue in function of costs incurred, applying the percentage of completion method. This revenue recognition consisted of €46.6 million related to the upfront license fee and €6.6 million related to the deferred income triggered by the accounting treatment of the share subscription agreement with Gilead under IAS 39. The outstanding balance of deferred income from the Gilead collaboration agreement at 30 September 2017 amounted to €232.1 million, of which €130.6 million reported as non-current deferred income.

Under the collaboration agreement with Servier for osteoarthritis, we received a license fee payment of €6.0 million end of July 2017. The license fee revenue is recognized over the estimated period of our involvement. As such, an amount of €0.3 million was recognized as license revenue for the nine months ended 30 September 2017.

Other income

The following table summarizes our other income for the nine months ended 30 September 2017 and 2016.

	Nine months ended 30 September	
(thousands of €)	**2017**	2016
Grant income	690	1,451
Other income	17,794	13,581
Total other income	**18,484**	**15,031**

Other income increased in the first nine months of 2017 (€18.5 million vs. €15.0 million in the first nine months of 2016), mainly driven by higher income from R&D incentives.

Results

We realized a net loss of €85.9 million for the first nine months of 2017, compared to a net profit of €8.1 million for the first nine months of 2016. Last year's net profit was primarily driven by €57.5 million non-cash fair value gain from the re-measurement of the financial asset triggered by the share subscription agreement with Gilead.

We reported an operating loss amounting to €62.6 million for the first nine months of 2017, compared to an operating loss of €48.5 million for the first nine months of 2016.

Our R&D expenses for the first nine months of 2017 were €149.2 million, compared to €96.7 million for the first nine months of 2016. This planned increase was due mainly to an increase of €37.0 million in subcontracting costs, mostly for our filgotinib and cystic fibrosis programs. Furthermore, personnel costs increased in 2017, explained by a planned increase in headcount, as well as higher costs for warrants and bonus plans as a result of the increase of our share price.

Our G&A and S&M expenses were €19.7 million for the first nine months of 2017, compared to €16.8 million for the first nine months of 2016. This increase mainly resulted from higher costs recognized in relation to the warrants and bonus plans as a result of the increase of the Galapagos share price, as well as a planned slight headcount increase.

Net other financial expenses for the first nine months of 2017 amounted to €23.1 million, compared to net other financial expenses of €0.9 million for the first nine months of 2016, and were primarily attributable to €24.8 million of unrealized exchange loss on our cash position in U.S. dollars as a consequence of the fluctuation of the EUR / U.S. dollar exchange rate in the first nine months of 2017. We expect to use this cash held in U.S. dollars to settle our future payables in U.S. dollars, which will be primarily linked to our global collaboration with Gilead for the development of filgotinib.

Financial results in 2016 were primarily driven by the fair value re-measurement of the share subscription agreement.

Segment information

	Segment information for the nine months ended 30 September 2017			
(thousands of €)	R&D	Fee-for-services	Inter-segment elimination	Group
External revenue	81,830	6,040		87,870
Internal revenue		4,024	(4,024)	
Other income	18,469	14		18,484
Revenues & other income	**100,299**	**10,078**	**(4,024)**	**106,354**
Segment result	**(50,774)**	**(81)**		**(50,855)**
Unallocated expenses[1]				(11,697)
Operating loss				**(62,552)**
Financial (expenses) / income				(23,142)
Result before tax				**(85,694)**
Income taxes				(161)
Net loss				**(85,855)**

(1) Unallocated expenses consist of expenses for warrant plans under IFRS 2.

(thousands of €)	Segment information for the nine months ended 30 September 2016 R&D	Fee-for-services	Inter-segment elimination	Group
External revenue	44,525	5,484		50,009
Internal revenue		3,901	(3,901)	
Other income	14,898	133		15,031
Revenues & other income	**59,423**	**9,518**	**(3,901)**	**65,040**
Segment result	**(40,546)**	**(736)**		**(41,281)**
Unallocated expenses[1]				(7,201)
Operating loss				**(48,482)**
Financial (expenses) / income				56,621
Result before tax				**8,138**
Income taxes				(71)
Net income				**8,067**

(1) Unallocated expenses consist of expenses for warrant plans under IFRS 2.

The basis of accounting for any transactions between reportable segments is consistent with the valuation rules and with transactions with third parties.

Liquid assets position

Cash, cash equivalents and restricted cash totaled €1,220.1 million at 30 September 2017.

A net increase of €245.6 million in cash and cash equivalents was recorded during the first nine months of 2017, compared to an increase of €590.5 million during the first nine months of 2016. Net cash used in operating activities amounted to €86.2 million in the first nine months of 2017. Furthermore, €3.6 million was generated in investing activities primarily driven by the release of restricted cash to cash and cash equivalents for €6.6 million.

Financing activities generated €353.0 million of cash, consisting of €348.1 million proceeds from the U.S. public offering and €4.9 million proceeds from warrant exercises. Finally €24.8 million of negative unrealized exchange rate differences were reported on cash and cash equivalents.

Restricted cash amounted to €7.7 million at 31 December 2016, and decreased by €6.5 million to €1.2 million at 30 September 2017. This decrease is primarily explained by the full release of the escrow account containing the remaining €6.6 million of proceeds from the sale of the service division to Charles River Laboratories International, Inc. in 2014, as a final agreement between the parties was reached.

On 30 September 2017, restricted cash was comprised of €0.5 million and €0.7 million bank guarantees on real estate lease obligations in Belgium and in the Netherlands, respectively.

Cash and cash equivalents amounted to €1,218.9 million at 30 September 2017 and were comprised of cash and cash at banks, short-term bank deposits and money market funds that are readily convertible to cash and are subject to an insignificant risk of changes in value. Our cash management strategy may allow short-term deposits with an original maturity exceeding three months while monitoring all liquidity aspects. Cash and cash equivalents comprised €792.6 million of term deposits with an original maturity longer than three months but which are available upon one month's notice. Cash at banks was mainly composed of savings accounts and current accounts. We maintain our bank deposits in highly rated financial institutions to reduce credit risk. Cash invested in highly liquid money market funds represented €149.8 million, aim at meeting short-term cash commitments, while reducing the counterparty risk of investment.

(thousands of €)	30 September 2017	31 December 2016
Cash at banks	276,502	357,630
Term deposits	792,551	515,632
Money market funds	149,801	99,977
Cash on hand	2	2
Total cash and cash equivalents	**1,218,856**	**973,241**

On 30 September 2017, our cash and cash equivalents included $255.6 million held in U.S. dollars, which could generate unrealized exchange gain or loss in our financial results in accordance with the fluctuation of the EUR/U.S. dollar exchange rate as our functional currency is EUR. We expect to use this cash held in U.S. dollars to settle our future payables in U.S. dollars, which will be primarily linked to our global collaboration with Gilead for the development of filgotinib.

Furthermore, our balance sheet held R&D incentives receivables from the French government (*Crédit d'Impôt Recherche*[3]) amounting to €42.0 million as of 30 September 2017, to be received in yearly tranches from 2017 to 2021. Our balance sheet also held R&D incentives receivables from the Belgian government amounting to €34.2 million as of 30 September 2017, to be received in yearly tranches from 2018 until 2027.

Capital increase

On 6 April 2017, 247,070 warrants were exercised at various exercise prices (with an average exercise price of €16.33 per warrant), resulting in a share capital increase (including issuance premium) of €4.0 million and the issuance of 247,070 new shares. The closing price of the Galapagos share on that date was €84.60.

On 21 April 2017 our U.S. public offering of 4,312,500 American Depositary Shares ("ADSs") was fully underwritten, at a price of $90.00 per ADS, before underwriting discounts, for gross proceeds of €363.9 million. Underwriting discounts and offering expenses amounted to €15.8 million. As such, net proceeds amounted to €348.1 million.

On 20 June 2017, 52,030 warrants were exercised at various exercise prices (with an average exercise price of €12.14 per warrant) resulting in a share capital increase (including issuance premium) of €0.6 million and the issuance of 52,030 new shares. The closing price of the Galapagos share on that date was €70.66.

On 21 September 2017, 28,100 warrants were exercised at various exercise prices (with an average exercise price of €9.55 per warrant) resulting in a share capital increase (including issuance premium) of €0.3 million and the issuance of 28,100 new shares. The closing price of the Galapagos share on that date was €84.62.

On 30 September 2017, Galapagos NV's share capital was represented by 50,895,778 shares. All shares were issued, fully paid up and of the same class.

[3] *Crédit d'Impôt Recherche* refers to an innovation incentive system underwritten by the French government.

(thousands of €, except share data)	Number of shares	Share capital	Share premium	Share capital and share premium
On 1 January 2017	**46,256,078**	**223,928**	**649,135**	**873,063**
6 April 2017: exercise of warrants	**247,070**	**1,337**	**2,697**	**4,034**
21 April 2017: U.S. public offering				
ADSs (fully paid)	4,312,500	23,331	340,593	363,924
Underwriter discounts and offering expenses (paid)		(15,790)		(15,790)
Offering expenses still to be paid at 30 September 2017		(47)		(47)
Total U.S. public offering	**4,312,500**	**7,494**	**340,593**	**348,087**
20 June 2017 : exercise of warrants	**52,030**	**281**	**350**	**632**
21 September 2017: exercise of warrants	**28,100**	**152**	**117**	**269**
On 30 September 2017	**50,895,778**	**233,192**	**992,893**	**1,226,085**

Contingencies and commitments

Contractual obligations and commitments

We entered into lease agreements for offices and laboratories which qualify as operating leases. We also have certain purchase commitments, principally with CRO subcontractors.

On 30 September 2017, we had outstanding obligations for future minimum rent payments and purchase commitments, which become due as follows:

(thousands of €)	Total	Less than 1 year	1–3 years	3–5 years	More than 5 years
Operating lease obligations	27,523	4,183	8,030	6,159	9,152
Purchase commitments	36,722	32,649	2,576	1,497	–
Total contractual obligations & commitments	**64,245**	**36,832**	**10,606**	**7,655**	**9,152**

On 31 December 2016, we had outstanding obligations for future minimum rent payments and purchase commitments, which become due as follows:

(thousands of €)	Total	Less than 1 year	1–3 years	3–5 years	More than 5 years
Operating lease obligations	27,263	4,114	6,494	5,504	11,151
Purchase commitments	27,579	27,084	495	–	–
Total contractual obligations & commitments	**54,842**	**31,198**	**6,989**	**5,504**	**11,151**

Contingent liabilities and assets

On 13 March 2014, we announced the signing of a definitive agreement to sell the service division operations to Charles River Laboratories International, Inc. (CRL) for a total consideration of up to €134 million. CRL agreed to pay us an immediate cash consideration of €129 million. The potential earn-out of €5 million due upon achievement of a revenue target 12 months after transaction closing has not been obtained. Approximately 5% of the total consideration, including price adjustments, was being held on an escrow account. Four claims were introduced by CRL, which all have been settled for a total amount of €1.3 million. In the first quarter of 2017, the remaining balance of the escrow account of €6.6 million was released in full, as final agreement between the parties was reached.

Following the divestment, we remained guarantor until early February 2017 in respect of lease obligations for certain U.K. premises. Finally, following common practice, we gave representations and warranties which are capped and limited in time (since 1 April 2016, CRL can only introduce a claim under the Tax Deed (during a period of 5 years)), and other claims related to the sale cannot be submitted anymore).

In the course of 2008, a former director of one of our subsidiaries sued for wrongful termination and seeks damages of €1.5 million. We believe that the amount of damages claimed is unrealistically high. In 2014, the court requested an external advisor to evaluate the exact amount of damages. On 29 January 2016, the court made a 1st degree judgment, dismissing all claims in full. In appeal, the 2nd degree court instructed the 1st degree court to conduct a new trial, which is currently pending. A first hearing, initially scheduled on 12 July 2017, was postponed to an undefined date. We recently filed a motion petitioning for expedient procedure in consideration of the value of the claim, overall duration of the dispute and duration of the re-trial. Considering the defense elements provided, as well as the fact that so far the court has made no decision indicating that the claim would be sustained, our board and management evaluated the risk to be remote to possible, but not likely. Accordingly, it was decided not to record any provision, as the exposure was considered to be limited.

Significant accounting policies

There were no significant changes in accounting policies applied by us in these condensed consolidated interim financial statements compared to those used in the most recent annual financial statements of 2016, except for the adoption of new standards and interpretations described below.

New standards and interpretations applicable for the annual period beginning on 1 January 2017

- Amendments to IAS 12 – Recognition of Deferred Tax Assets for Unrealized Losses
- Amendments to IAS 7 – Disclosure Initiative
- Annual Improvements to IFRS Standards 2014-2016 Cycle – Amendments to IFRS 12

The nature and the effect of these changes were taken into consideration, but the above amendments did not affect the interim condensed consolidated financial statements. We have not early adopted any other standard, interpretation, or amendment that has been issued but is not yet effective.

The assessment of the impact of IFRS 15 Revenue from Contracts with Customers (applicable for annual periods beginning on or after 1 January 2018) is still ongoing as the company assesses all contracts, performance obligations and allocation of revenues. We plan to adopt IFRS 15 on its effective date.

We are currently evaluating the guidance to determine the impact of IFRS 16 Leases (applicable for annual periods beginning on or after 1 January 2019). We plan to adopt IFRS 16 on its effective date.

Seasonality

The impact of seasonality or cyclicality on our operations is not regarded as applicable to the unaudited interim condensed consolidated financial statements.

Events after the end of the reporting period

There were no adjusting events nor material non-adjusting events to be reported.

Approval of interim financial statements

The interim financial statements were approved by the board of directors on 23 October 2017.