KARO BIO

Press Release

October 16, 2002

QUARTERLY REPORT JULY-SEPTEMBER 2002

- **Significant preclinical milestone reached in the collaboration with Merck & Co., Inc. Milestone payment received.**
- **The collaboration with Bristol-Myers Squibb extended for six months.**
- **Significant progress made in exploratory research in the launch of a new project and in successful application of the Molecular Braille® technology.**
- **The loss after financial items decreased to MSEK 37.4 (65.0). Operating result excluding goodwill depreciation improved by MSEK 29.4 to MSEK 21.2 (-8.2).**
- **Group net sales increased to MSEK 76.8 (47.6).**
- **Cash flows from operating activities amounted to MSEK 8.3 (52.8). Cash and cash equivalents and short-term investments amounted to MSEK 235.2 (306.9) at the end of the period.**

Operations

Karo Bio is a leading drug discovery company in the field of nuclear receptor biology and medicinal chemistry. The Company develops receptor-selective and tissue-selective pharmaceuticals for treatment of major disorders. Karo Bio has operations in Sweden and in USA.

Karo Bio has four strategic partnerships with international pharmaceutical companies for development of innovative therapies for the treatment of common diseases. Karo Bio also runs several internal projects in various clinical areas where the Company has competitive advantages for discovery of new pharmaceuticals that target nuclear receptors. Exploratory studies in novel nuclear receptor areas are conducted to maintain a strong pipeline. These studies cover new indications for well characterized receptors as well as discovery and characterization of new receptors.

Strategic Partnerships

Women's Health Care - Merck & Co., Inc.

An important pre-clinical milestone in the collaboration with Merck & Co., Inc. was reached in July, which triggered a milestone payment to Karo Bio in the third quarter. Karo Bio may receive additional future milestone payments from Merck & Co., Inc., dependent upon the successful progression of compounds to and through clinical trials and approval as well as royalties on sales of such compounds.

In October 1997 Karo Bio and Merck & Co., Inc. initiated a three-year drug discovery collaboration in the field of estrogen receptors. In October 2000 the collaboration was extended for two additional years. The program has successfully reached its primary drug discovery objectives, the identification of estrogen receptor subtype selective compounds with potential for multiple clinical indications.

The research collaboration phase is based on estrogen receptors as targets for the discovery of drugs that may be useful for disorders primarily in the field of women's health care. Under the terms of the agreement, which will remain in full force and effect, the research collaboration phase of this program is scheduled to be completed at the end of October 2002. Merck & Co., Inc. has exclusive, worldwide rights for all compounds identified during the collaboration and is responsible for their further pre-clinical and clinical development

Atherosclerosis - Wyeth Pharmaceuticals

Karo Bio collaborates with Wyeth Pharmaceuticals for development of novel treatments for atherosclerosis with the novel liver X-receptor (LXR) as drug discovery target. Targeting LXR may lead to development of drugs for both prevention and treatment of atherosclerosis. The collaboration was initiated in September 2001 and important progress has been made to date.

Diabetes - Abbott Laboratories

In the field of type 2 diabetes Karo Bio collaborates with Abbott Laboratories for development of pharmaceuticals that have the capacity to normalize the elevated glucose output from liver, which is associated with type 2 diabetes. A lead compound has been shown to lower blood glucose in animal models of diabetes by lowering liver production of glucose. Pre-clinical studies are continuing to determine if the compound is a clinical candidate.

Obesity - Bristol-Myers Squibb

In a joint collaboration, Karo Bio and Bristol-Myers Squibb are targeting the thyroid hormone receptor for treatment of obesity. Natural thyroid hormone increases body metabolism and burns calories but cannot be used for treatment of obesity due to cardiac side effects. Karo Bio and Bristol-Myers Squibb have successfully developed technical approaches to identify compounds that avoid the side effects. The first clinical development compound was removed from development in March this year and may be replaced with a back-up compound that is currently progressing to the final stages of pre-clinical evaluation. The drug discovery collaboration has also recently been prolonged for an additional six months.

Technology Outlicensing

Karo Bio's BioKey® technology is well suited for high throughput screening. The technology has been successfully applied to over 100 molecular targets for Karo Bio's internal programs and for collaborations with several U.S. and European partners, including Aventis Pharma, Bayer AG, GPC Biotech, and Boehringer Ingelheim

Pharmaceuticals. During the period, scientific milestones have been reached in the Aventis Pharma collaboration.

Internal Projects

Male Hormone Replacement Therapy and Prostate Cancer

The androgen receptor (AR) is the receptor for the male sex hormone and the receptor has the potential to become a significant drug target for numerous disorders. The key to success in this field is access to know-how and technologies that enable development of receptor and tissue selective drugs for important clinical indications such as prostate cancer, male hormone replacement therapy, acne, alopecia and hirsutism. Karo Bio is uniquely positioned in the field with access to a strong drug discovery technology which has been significantly reinforced during the period with receptor structures, identification of unique BioKeys® and development of Molecular Braille® fingerprints for selection of promising lead compounds. The technology base is perfectly suitable for discovery and selection of specific drugs. In addition, Karo Bio has exclusive European patent protection for AR as a drug discovery target.

Inflammatory Disorders

There is a great need for improvement of treatment of inflammatory disorders. Anti-inflammatory steroids are the most powerful anti-inflammatory agents known today but have a number of side effects that restricts the broad use of these important pharmaceuticals. The glucocorticoid receptor is the target for the anti-inflammatory steroids. Karo Bio believes that its leading technology can discover new and more selective drugs with anti-inflammatory effects but with significantly reduced side effects. During the period important progress has been made in identification of active compounds and the company is working intensely to further optimize these by making chemical analogs.

Skin Disorders

Karo Bio has developed KB002611 which is a product for prevention of steroid induced skin atrophy and with potential use for other skin disorders. Karo Bio is marketing this product as an in licensing opportunity for specialist companies in the field.

Exploratory Studies

Karo Bio continues to strengthen its pipeline of new projects through internal drug discovery and by collaborations within its scientific network. A new project has been launched which in the near future will be marketed as a new partnership opportunity. Progress in compound characterization and selection has also been made in several projects through the application of the Molecular Braille® technology and compound libraries have been expanded significantly.

Organization

By the end of the period, Karo Bio had 135 employees (126). Of these, 37 (36) are based in the United States and 109 (104) are engaged in research.

Result, Cash Flow and Financing

Group net sales for the third quarter increased by MSEK 29.2 to MSEK 76.8 compared to MSEK 47.6 for the same period last year. The increase in revenue relates primarily to the significant preclinical milestone payment received from Merck & Co, Inc. in the third quarter this year, even though a milestone payment from Bristol-Myers Squibb was recorded in the corresponding quarter last year. Both milestone payments were fully recorded as revenue in the respective quarter.

Group expenses decreased by MSEK 0.3 to MSEK 116.0 (116.3). The decrease is the net effect of the increased activity in the research organization, and lower cost in non-R&D organization.

The operating loss for the quarter improved to MSEK 39.2 (68.6). Operating result excluding goodwill depreciation amounted to MSEK 21.2 (-8.2). Goodwill depreciation amounts to MSEK 60.4 and is included in reported operating expenses and also operating result.

Financial income for the third quarter amounted to MSEK 1.8 (3.6). Currency exchange fluctuations pertaining to liabilities in US dollars are included in financial net, leading to a lower financial net in combination with the relatively low yield in the interest rate market compared to previous periods.

Cash flows from operating activities for the third quarter amounted to MSEK 8.3 (52.8). The strong cash flow in the third quarter 2002 is primarily the net effect from increase in revenues and changes in working capital. The very strong cash flow in the third quarter 2001 relates to the receipt of the down payment from Wyeth Pharmaceuticals, which had a material effect on changes in working capital. Significant factors affecting change in working capital 2002 are reduction of unearned revenue, primarily from down payments received but not yet recorded as revenue, and reductions of payables to vendors.

Capital investments in equipment amounted to MSEK 0.3 (9.2).

Cash and cash equivalents and short-term investments amounted to MSEK 235.2 (306.9) at end of period, while the corresponding amount for previous quarter was 227.2.

Loss per share for the third quarter amounted to SEK 3.11 (5.41), based on the weighted average number of shares outstanding and excluding dilution. The Group’s equity ratio as of period-end was 79.6% (81.3%) and equity per share at period-end was SEK 29.70 (53.57).

Shareholders' Equity

Shareholders' equity increased during the third quarter by kSEK 12 from the exercise of warrants.

At period-end, warrants representing 358 777 shares were outstanding. The warrants were issued in conjunction with the acquisition of Karo Bio USA, Inc. in 2000 (21 144 warrants) and the implementation of the Incentive Program 2001 (340 000 warrants). The outstanding warrants will lead to no dilution of earnings per share in 2002, as a conversion to shares would lead to an improvement of earnings per share.

The Company's share capital amounted to SEK 60 263 285 at the end of the period representing 12 052 657 shares at a par value of SEK 5. Total consolidated shareholder's equity amounted to MSEK 358.0 (643.9) at the end of the period.

Accounting and Valuation Principles

This quarterly report has been prepared in accordance with the Swedish Financial Accounting Standards Council's (the Council) standard RR 20 for interim reports. The accounting and valuation principles applied are consistent with provisions of the Swedish Annual Accounts Act and standards issued by the Council. The principles applied are unchanged compared to what was applied in the Annual Report for 2001.

Amounts or figures in parentheses indicate comparative figures for the corresponding period last year. Amounts are expressed in Swedish Kronor (SEK) or thousands (kSEK) or millions (MSEK) of Kronor as indicated.

Scheduled Releases of Financial Information

Karo Bio intends to distribute financial reports as follows:

- Quarterly Report October – December
  and Full Year Report 2002 February 7, 2003

Financial reports, press releases and other information is available on Karo Bio's website www.karobio.com

CONDENSED CONSOLIDATED INCOME STATEMENT (kSEK)

	July - September		January - September	
	2002	**2001**	**2002**	**2001**
Net sales	76 753	47 629	153 131	98 593
Operating expenses				
Administrative expenses	-13 041	-17 363	-46 190	-51 733
Research and development expenses	-41 216	-35 038	-131 719	-107 953
Depreciation of goodwill	-60 449	-60 449	-181 347	-181 347
Other operating expenses	-1 278	-3 422	-1 481	-3 625
	-115 984	-116 272	-360 737	-344 658
Operating loss	**-39 231**	**-68 643**	**-207 606**	**-246 065**
Financial net	1 804	3 643	10 950	7 973
Loss after financial items	**-37 427**	**-65 000**	**-196 656**	**-238 092**
Tax	-	-	-	-
LOSS FOR THE PERIOD	**-37 427**	**-65 000**	**-196 656**	**-238 092**
Other depreciation included in operating expenses	*-5 498*	*-5 156*	*-16 927*	*-11 458*
Loss per share (SEK) [*)]				
- weighted average number of shares outstanding	-3.11	-5.41	-16.33	-19.82
- shares outstanding at end of period	-3.11	-5.40	-16.32	-19.80
Number of shares outstanding (000)				
- weighted average during period	12 052	12 023	12 040	12 014
- weighted average during period, fully diluted	12 411	12 411	12 411	12 291
- at end of period	12 053	12 026	12 053	12 026
- at end of period, fully diluted	12 411	12 411	12 411	12 411

[*)] The outstanding warrants lead to no dilution of earnings per share in 2002, as a conversion to shares would lead to an improvement of earnings per share for the full year.

CONDENSED CONSOLIDATED BALANCE SHEET (kSEK)

	September 30		December 31
	2002	**2001**	**2001**
Assets			
Licenses and similar rights	16 314	26 179	23 713
Goodwill	154 798	396 594	336 145
Equipment	32 113	35 252	38 762
Other current assets	11 256	26 817	7 408
Cash, cash equivalents and short-term investments	235 212	306 895	282 298
TOTAL ASSETS	**449 693**	**791 737**	**688 326**
Shareholders' equity and liabilities			
Shareholders' equity	357 973	643 940	557 683
Non-current liabilities	8 343	13 741	13 939
Current liabilities	83 377	134 056	116 704
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES	**449 693**	**791 737**	**688 326**

CONDENSED CONSOLIDATED CASH FLOW STATEMENT (kSEK)

	July - September		January - September	
	2002	**2001**	**2002**	**2001**
Operating activities				
Operating loss before financial items	-39 231	-68 643	-207 606	-246 065
Depreciation	65 947	65 605	198 274	192 805
	26 716	**-3 038**	**-9 332**	**-53 260**
Financial income received and expenses paid	1 678	5 598	5 982	7 244
Cash flow from operating activities before changes in working capital	**28 394**	**2 560**	**-3 350**	**-46 016**
Changes in working capital	-20 081	50 262	-34 867	52 096
Cash flow from operating activities	**8 313**	**52 822**	**-38 217**	**6 080**
Investing activities				
Investment in licenses and similar rights	-	-	-5 110	-10 700
Investment in equipment	-281	-9 156	-3 892	-17 584
Cash flow from investing activities	**-281**	**-9 156**	**-9 002**	**-28 284**
Cash flow from operations	**8 032**	**43 666**	**-47 219**	**-22 204**
Financing activities				
Proceeds from new share issues	12	21	133	133
Cash flow from financing activities	**12**	**21**	**133**	**133**
Cash flow for the period	**8 044**	**43 687**	**-47 086**	**-22 071**
Liquid assets at the end of the period	**235 212**	**306 895**	**235 212**	**306 895**

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (kSEK)

	July - September		January - September	
	2002	**2001**	**2002**	**2001**
Amount at beginning of period	**393 684**	**708 883**	**557 682**	**881 597**
Translation difference	1 704	36	-3 186	302
New issues of shares - warrants exercise	12	21	133	133
Loss for the period	-37 427	-65 000	-196 656	-238 092
Amount at end of period	**357 973**	**643 940**	**357 973**	**643 940**

EQUITY DATA

	September 30		December 31
	2002	**2001**	**2001**
Equity ratio	79.6%	81.3%	81.0%
Equity per share at the end of period, SEK	29.70	53.55	46.37
Equity per share at the end of period, fully diluted, SEK	28.84	51.88	44.93

Huddinge, October 16, 2002

Björn Nilsson
President & CEO

For further information, please contact

Björn Nilsson, President & CEO tel. +46 8 608 60 20, Per Otteskog, Senior Vice President Investor Relations & Corporate Communications, tel. +46 8 608 60 18, or Bertil Jungmar, Vice President Finance & Administration, tel. +46 8 608 60 52.

This report has not been subject to review by the Company's independent auditor.

Legal disclaimer

This Quarterly Report includes statements that are forward looking and actual results may differ materially from those stated. In addition to the factors discussed, among other factors that may affect results are developments within research programs, including development in pre-clinical and clinical trials, the impact of competing research programs, the effect of economic conditions, the effectiveness of the Company's intellectual property rights and preclusions of potential third party's intellectual property rights, technological development, exchange rate and interest rate fluctuations, and political risks.