

# Separate Financial Statements of MorphoSys AG as of December 31, 2016 (German GAAP)

MorphoSys AG, Planegg

## Management Report

In 2016, MorphoSys continued to build a broad, advanced and valuable pipeline of biopharmaceutical compounds as part of its strategic focus on the development of proprietary programs which are the Company's main value drivers. We initiated three phase 2 trials with MOR208 in hemato-oncological indications, one of which is expected to transition into a pivotal phase 3 study in 2017. Our fifth proprietary program, MOR106, started clinical development in 2016 and was followed by MOR107 in February 2017 as the sixth proprietary program to enter clinical development. Programs in our Partnered Discovery segment also developed exceptionally well last year. Following positive phase 3 results, our partner Janssen submitted applications seeking regulatory approval for guselkumab for the treatment of psoriasis. If approved, this compound could become MorphoSys's first marketed antibody and the basis for rising, royalty-based product sales, the proceeds of which could be reinvested in the future development of our proprietary portfolio. We intend to continue pursuing the path to becoming a fully integrated, commercial biopharmaceutical company specialized in oncology.

# Operations and Business Environment

## Strategy and Company Management

### STRATEGY AND OBJECTIVES

MorphoSys's goal is to make exceptional, innovative biopharmaceuticals to improve the lives of patients suffering from serious diseases. With our successful transition from a technology provider to a drug development organization, we are well underway to reach our goal. This transition is supported by MorphoSys's powerful technology platform for generating therapeutic antibodies. Meanwhile, the Company has more than 100 drug candidates in development. Last year an application was submitted to the regulatory authorities for the first time seeking approval for an antibody based on MorphoSys's proprietary technology. Most of the development programs are conducted in partnership with pharmaceutical and biotechnology companies. MorphoSys uses the revenues generated from these partnerships to expand its proprietary development portfolio. This segment, which currently comprises 14 programs, is gaining in importance and builds on top of an even broader pipeline of programs pursued with partners. Our high number of active development programs allow us to compensate for potential setbacks that may arise during the complex drug development process and help us to maximize the value of our technology.

The Proprietary Development segment focuses on developing therapeutic agents based on the Company's proprietary technology platforms and candidates in-licensed from other companies. During clinical development, the Company determines whether and at which point it may pursue a partnership for later development and commercialization. The drug candidate can then be either completely out-licensed or developed further in cooperation with a pharmaceutical or biotechnology company (co-development). In selected cases, individual projects may be developed on a proprietary basis until they are ready for commercialization.

In the Partnered Discovery segment, MorphoSys generates antibody candidates for partners in the pharmaceutical and biotechnology industries. MorphoSys receives contractual payments including license fees for technologies and funded research, as well as success-based milestone payments and royalties on product sales. The funds generated from these partnerships support the Company's long-term business model and help fund its proprietary development activities.

Both segments are based on the Company's innovative technologies. Growth is driven mainly by HuCAL, the industry's most successful antibody library in terms of the number of clinical development candidates produced, and the follow-on platform Ylanthia, which is today's largest known library based on antibody Fab fragments. The acquisition of the biopharmaceutical company Lanthio Pharma B.V. in May 2015 secured for MorphoSys access to an innovative platform of therapeutic peptides. Additionally, the Company uses its financial resources to expand and deepen its technological base, for example through in-licensing. The in-licensed programs MOR208 and MOR209/ES414 and the acquisition of Lanthio Pharma are good examples of how we are successfully implementing this strategy.

The Company's goal is to maximize the portfolio's full value by investing in proprietary drug candidates while maintaining financial discipline and strict cost control to ensure increasing enterprise value.

## COMPANY MANAGEMENT AND PERFORMANCE INDICATORS

MorphoSys pays equal attention to financial and non-financial indicators when steering the Company. These indicators help to monitor the success of strategic decisions and give the Company the opportunity to take quick corrective action when necessary. The Company's management also monitors and evaluates selected early indicators so that it can thoroughly assess a project's progress and act promptly when problems occur.

### FINANCIAL PERFORMANCE INDICATORS

Our financial performance indicators are described in detail in the section "Analysis of Net Assets, Financial Position and Results of Operations." Earnings before interest and taxes (EBIT), revenues, operating expenses, segment results and liquidity are the key financial indicators we use to measure our operating performance. Segment performance is reviewed monthly, and the budget for the current financial year is revised and updated on a quarterly basis. Every year, the Company prepares a mid-term plan for the three subsequent years. A thorough cost analysis is prepared regularly and used to monitor the Company's adherence to financial targets and make comparisons to previous periods.

MorphoSys's business performance is influenced by factors such as milestone and license payments, research and development expenses, other operating cash flows, existing liquidity resources, expected cash inflows and working capital. These indicators are also routinely analyzed and evaluated with special attention being paid to the income statement, existing and future liquidity and available investment opportunities. The net present value of investments is calculated using discounted cash flow models.

### NON-FINANCIAL PERFORMANCE INDICATORS

For reporting purposes, MorphoSys uses the Sustainable Development Key Performance Indicators (SD KPIs) recommended by the SD KPI standard. These indicators include success in proprietary research and development (SD KPI 1) and achievements in partnered programs as benchmarks for the commercialization rate (SD KPI 2). In the past five years, there have been no product recalls, fines or settlements as the result of product safety or product liability disputes (SD KPI 3).

To secure its lead in the market for therapeutics, MorphoSys relies on the steady progress of its product pipeline, not only in terms of the number of therapeutic antibody candidates (114 at the end of the reporting year) but also based on the progress of its development pipeline and prospective market potential. Because successful products are based on superior technologies, another key performance indicator is the progress of the Company's technology development. In addition to the quality of our research and development, our professional management of partnerships is also a core element of our success and refers to new contracts as well as the continued strategic development of existing alliances. Details on these performance indicators can be found in the section "Research and Development and Business Performance".

The non-financial performance indicators described in the section "Sustainable Business Development" are also used to manage MorphoSys AG successfully.

**TAB. 1: SUSTAINABLE DEVELOPMENT KEY PERFORMANCE INDICATORS (SD KPIS) AT MORPHOSYS (DECEMBER 31)**

	2016	2015	2014	2013	2012
	(number of individual antibodies)				
<b>Proprietary Development</b>					
Programs in Discovery	8	8	5	3	2
Programs in Preclinic	1	2	2	0	0
Programs in Phase 1	2	1	1	1	1
Programs in Phase 2 <sup>1)</sup>	3	3	2	2	2
<b>Total<sup>1)</sup></b>	<b>14</b>	<b>14</b>	<b>10</b>	<b>6</b>	<b>5</b>
	(number of individual antibodies)				
<b>Partnered Discovery</b>					
Programs in Discovery	54	43	40	37	34
Programs in Preclinic	22	25	25	22	20
Programs in Phase 1	10	9	8	6	8
Programs in Phase 2	12	9	8	8	6
Programs in Phase 3	2	3	3	2	1
<b>Total</b>	<b>100</b>	<b>89</b>	<b>84</b>	<b>75</b>	<b>69</b>

<sup>1)</sup> Thereof one out-licensed program: MOR103/GSK3196165, out-licensed to GSK.

#### LEADING INDICATORS

MorphoSys monitors a variety of leading indicators to monitor the macroeconomic environment, the industry and the Company itself on a monthly basis. At the Company level, economic data is gathered on the progress of the segments' individual programs. MorphoSys uses general market data and external financial reports to acquire information on early macroeconomic indicators, such as industry transactions, changes in the legal environment and the availability of research funds, and reviews this data carefully.

For active collaborations, there are joint steering committees that meet regularly to update and monitor the programs' progress. These ongoing reviews give the Company a chance to intervene early when there are any negative developments and provide it with information on expected milestones and related payments well in advance. Partners in non-active collaborations regularly provide a written report to MorphoSys so that we can follow the progress of ongoing therapeutic programs.

The business development area uses market analyses to get an indication of the market's demand for new technologies. By continuously monitoring the market, MorphoSys can quickly respond to trends and requirements and initiate its own activities or partnerships.

Before a therapeutic product is developed, a target product profile (TPP) is created and continually updated during the development process. This approach gives an early indication of the properties the product should possess to be successful in the market and answers important questions, such as the level of efficacy to be achieved and whether development should be focused on improving the safety profile or changing the drug candidate's dosage form. The TPP also includes a detailed description of how the product could be positioned in the market and the relevant patient groups. By continuously

monitoring the criteria and their fulfillment, the Company can always take the key factors into account during product development and respond promptly to any changes.

## Organizational Structure

### ORGANIZATION OF MORPHOSYS AG

MorphoSys AG develops and commercializes high-quality antibodies for therapeutic applications. The activities of the two business segments are based on leading-edge proprietary technologies. The Proprietary Development segment combines all of the Company's proprietary research and development of therapeutic compounds. MorphoSys initially develops its proprietary and in-licensed compounds independently with the option to bring them into partnerships or out-license them. As of January 1, 2016, the development of proprietary technologies is now also conducted in this segment. The second business segment, Partnered Discovery, uses MorphoSys's cutting-edge technologies to make human antibody-based therapeutics on behalf of partners in the pharmaceutical industry. All business activities within the scope of these collaborations are reflected in this segment.

In the 2016 financial year, the Company was located at the registered office of MorphoSys AG as ultimate parent company, first in the Martinsried district, since autumn in the Steinkirchen district of the municipality of Planegg near Munich. In autumn 2016, MorphoSys AG moved to the Company's new headquarters, which is also located in the municipality of Planegg near Munich. The central corporate functions such as accounting, controlling, human resources, legal, patent, corporate communications and investor relations, as well as the two segments Proprietary Development and Partnered Discovery, are located at these new headquarters. The subsidiary Sloning BioTechnology GmbH was located at Planegg/Steinkirchen as well. The subsidiary Lanthio Pharma B.V. and its subsidiary LanthioPep B.V. in Groningen, the Netherlands, are largely autonomous and independently managed. These subsidiaries have their own research and development laboratories, general management and administration, as well as human resources, accounting and business development departments.

### LEGAL STRUCTURE OF MORPHOSYS: COMPANY MANAGEMENT AND SUPERVISION

MorphoSys AG, a German stock corporation listed in the Prime Standard segment of the Frankfurt Stock Exchange, is the parent company of the MorphoSys Group. In accordance with the German Stock Corporation Act, the Company has a dual management structure with the Management Board as the governing body, whose four members are appointed and supervised by the Supervisory Board. The Supervisory Board is elected by the Annual General Meeting and currently consists of six members. Detailed information concerning the Company's management and control and its corporate governance principles can be found in the Corporate Governance Report. The Senior Management Group, consisting of 22 managers from various departments, supports the Management Board of MorphoSys AG.

## Business Activities

### DRUG DEVELOPMENT

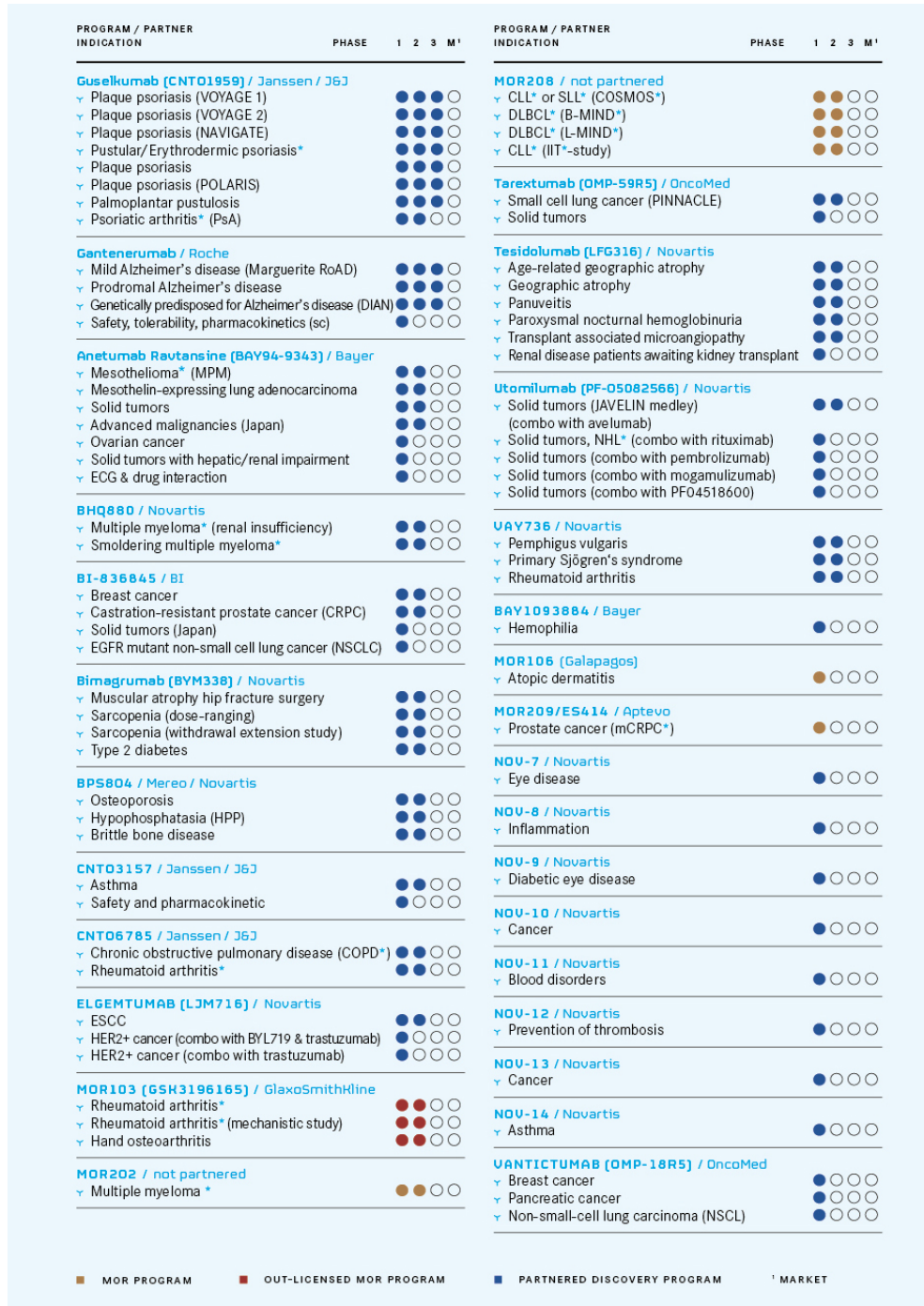
MorphoSys develops drugs using its own research and development (R&D) and in cooperation with pharmaceutical and biotechnology partners. Our core business activity is developing new treatments for patients suffering from serious diseases. The Company possesses one of the broadest pipelines in the

biotechnology industry with 114 individual therapeutic antibody programs at the end of 2016, 29 of which are in clinical development.

#### **TECHNOLOGIES**

MorphoSys has developed a number of technologies providing direct access to fully human antibodies for treating diseases. One of the most widely known MorphoSys technologies is HuCAL, which is a collection of billions of fully human antibodies and a system for their optimization. Another is Ylanthia, which represents the next generation of antibody technology and is currently the largest known antibody library in Fab format. Ylanthia is based on an innovative concept for generating highly specific and fully human antibodies. MorphoSys expects Ylanthia to set a new standard for the pharmaceutical industry's development of therapeutic antibodies in this decade and beyond. Slonomics gives MorphoSys a patented, fully automated technology for gene synthesis and modification for generating highly diverse gene libraries in a controlled process. The lanthipeptide technology developed by Lanthio Pharma B.V., a fully owned MorphoSys subsidiary, is a valuable addition to our existing library of antibodies and opens up new possibilities for discovering potential drugs based on stabilized peptides.

FIG. 1: MORPHOSYS'S PRODUCT PIPELINE (DECEMBER, 31 2016)



**PROPRIETARY DEVELOPMENT**

An important goal of MorphoSys is to increase enterprise value through the proprietary development of therapeutic programs. To achieve this goal, the Company is focusing on cancer indications and selected programs in inflammatory diseases.



## ONCOLOGY

The ability of monoclonal antibodies to bind with specific antigens on tumors, and unleash a therapeutic effect in patients, has led to their dominant role in targeted cancer therapies. According to a study by the QuintilesIMS Institute, expenditure in oncology is expected to be approximately US\$ 75 billion worldwide in 2016 and increase to US\$ 120-135 billion in the year 2021. MorphoSys is currently investing in the clinical development of three cancer programs: MOR208, MOR202 and MOR209/ES414.

**MOR208** is directed against the target molecule CD19, which is implicated in many B cell malignancies. The market research firm Decision Resources expects the therapeutic market for the B cell malignancy non-Hodgkin's lymphoma (NHL) to reach approximately US\$ 19 billion in 2025. Current biological therapies for the treatment of B cell malignancies, including the blockbuster rituximab (trade name Rituxan<sup>®</sup>), obinutuzumab (trade name Gazyva<sup>®</sup>) and ofatumumab (trade name Arzerra<sup>®</sup>) are directed against the CD20 target molecule. Because the target molecule CD19 is expressed on a larger number of B cell subtypes, CD19 antibodies may offer a more promising therapeutic approach. The activity of MOR208 is enhanced by a modification in the Fc part of the antibody, which is intended to lead to higher antibody-dependent cell-mediated cytotoxicity (ADCC) and an improvement in antibody-dependent cellular phagocytosis (ADCP), and thereby more effective tumor cell killing. The most advanced therapeutic approach against CD19 is currently the bispecific antibody blinatumomab (trade name Blyncto<sup>®</sup>) approved for acute lymphoblastic leukemia (ALL). Other clinical programs directed against the same target molecule use alternative approaches to increase the antibody's efficacy, for example by coupling with toxic substances or changing the antibody's glycosylation pattern. Another therapeutic approach against CD19 is the CAR-T technology. This therapy extracts a certain type of immune cells (T cells) from the patients' blood that are then altered outside of the body so that they can be better directed to the patients' tumor cells and kill them. When these T cells are later re-administered into the patients' blood via infusion, they subsequently bind and destroy targeted cancer cells. Alternative approaches using small molecules are also being developed in the field of B cell malignancies.

**MOR202** is directed against the CD38 target molecule and is currently being developed for the treatment of multiple myeloma (MM). After MorphoSys regained its rights to MOR202 from Celgene in March 2015, the Company continued developing MOR202 independently. Although MM is a relatively small area of oncology in terms of frequency of occurrence, the MM market has shown strong growth in recent years. Significant achievements in clinical practice and the introduction of effective new treatments have helped the market expand. However, there is still untapped market potential in terms of therapies that have better survival rates and lower side effects compared to currently available compounds. Despite significantly higher survival rates, the disease is seldom curable and a majority of patients experience a relapse. This has increased the attractiveness of alternative treatments, such as those targeting CD38. The approval of the CD38 antibody daratumumab (trade name Darzalex<sup>®</sup>) by the FDA (Food and Drug Administration) in November 2015 validated this treatment approach.

MorphoSys and its partner Aptevo Therapeutics (formerly Emergent BioSolutions) have been developing **MOR209/ES414** since 2015 in a phase 1 clinical study in patients suffering from metastatic castration-resistant prostate cancer (mCRPC). MOR209/ES414 is a bispecific anti-PSMA/anti-CD3 antibody based on Aptevo's (formerly Emergent) ADAPTIR<sup>™</sup> platform (modular protein technology). The immunotherapeutic protein is intended to activate the body's T cell immune response against prostate cancer cells bearing prostate specific membrane antigen (PSMA), an antigen commonly over-expressed in this tumor. The anti-CD3 binding domains of the compound selectively bind to the T cell receptor on cytotoxic T cells, which become activated when the anti-PSMA binding domains crosslink them to the cancer cells. Prostate cancer is the most commonly occurring cancer in men with approximately

900,000 new cases annually worldwide. As preclinical *in vitro* and *in vivo* studies have shown, MOR209/ES414 redirects T cell cytotoxicity toward prostate cancer cells expressing PSMA.

#### INFLAMMATORY AND AUTOIMMUNE DISEASES

Chronic inflammatory and autoimmune diseases affect millions of patients worldwide and impose an enormous social and economic burden. The QuintilesIMS Institute estimates the global market for the treatment of autoimmune diseases amounted to roughly US\$ 45 billion in the year 2016 and should increase to US\$ 75–90 billion in 2021.

**MOR103/GSK3196165** is a HuCAL antibody, which MorphoSys fully licensed to GlaxoSmithKline (GSK) in 2013. GSK is developing the antibody independently and bears all of the related costs. MorphoSys participates in the compound's development and commercialization through milestone payments up to a total of € 423 million and through tiered, double-digit royalties on net sales. In 2013, MorphoSys received an upfront payment of € 22.5 million. MOR103/GSK3196165 is directed against the target molecule GM-CSF (granulocyte macrophage colony-stimulating factor), a central player in the emergence of inflammatory diseases such as rheumatoid arthritis (RA). Biotechnologically produced drugs already comprise the majority of this market's total revenue. The overall market for RA drugs is growing steadily and Datamonitor expects it will reach US\$ 18 billion in the year 2020. MorphoSys estimates that MOR103/GSK3196165 has the potential to be the first marketed anti-GM-CSF antibody.

**MOR106**, the first drug candidate for identifying and developing new antibody therapies jointly developed with Belgian company Galapagos NV, has been in phase 1 clinical development for atopic dermatitis since 2016. MOR106 is the first publicly disclosed monoclonal antibody targeting IL-17C in clinical development worldwide. MOR106 selectively targets and inhibits IL-17C, which is associated with inflammatory skin disorders. Atopic dermatitis, also known as atopic eczema, is a chronic pruritic (itching) inflammatory skin disease. According to a report by the market research firm GlobalData in 2015, there were 66.3 million atopic dermatitis patients in the nine major markets (US, Germany, UK, France, Italy, Spain, Japan, China and India) in 2014.

The acquisition of the Dutch pharmaceutical company Lanthio Pharma B.V. in 2015 enhanced MorphoSys's proprietary portfolio with the addition of **MOR107** (formerly LP2). MOR107 is a novel lanthipeptide that has demonstrated potent angiotensin II type 2 (AT2) receptor-dependent activity in preclinical *in vivo* studies, and has potential to treat a variety of diseases.

#### INFLUENCING FACTORS

A political goal of many countries is to provide proper medical care for the public as demographic change drives the need for new forms of therapy. Cost-cutting could slow down the industry's development. As part of their austerity measures, governments in Europe, the United States and Asia have tightened their healthcare restrictions and are closely monitoring drug reimbursement.

Generic competition, which is already common in the field of small molecule drugs, now poses an increasing challenge to the biotechnology industry because of drug patent expiries. The technological barriers for generic biopharmaceuticals, or biosimilars, will remain high. Nevertheless, many drug manufacturers, particularly those from Europe and Asia, are now entering this market and placing more competitive pressure on established biotechnology companies. In the US, the approval of biosimilars as an alternative form of treatment has been very slow; they are, however, gaining more attention because of increasing pressure in the healthcare sector to reduce costs. Industry experts believe the global market for biosimilars will reach US\$ 20 billion in 2025.

## PARTNERED DISCOVERY

In the Partnered Discovery segment, MorphoSys applies technologies for the research, development and optimization of therapeutic antibodies as drug candidates in partnership with pharmaceutical and biotechnology companies. While the development costs are borne by the respective partners, MorphoSys profits from research financing, milestone payments and potential royalties on the sales of products from successful programs.

The Company's largest relationship to date is the strategic alliance formed in 2007 with Novartis – a pharmaceutical partner with a growing pipeline of biotechnologically developed drugs – which is scheduled to end at the end of November 2017. This alliance was expanded in 2012 through a supplementary cooperation agreement under which the companies collaborate on creating therapeutic antibodies using MorphoSys's next generation antibody platform Ylanthia in addition to HuCAL.

Partnered discovery programs for drug development include not only programs in MorphoSys's core areas of oncology and inflammatory diseases, but also those in indications where the Company has not yet established proprietary expertise.

Examples of partnered discovery programs include:

**Guselkumab**, a HuCAL antibody targeting IL-23, is being developed by MorphoSys's partner Janssen in **plaque psoriasis** and psoriatic arthritis (PsA). In November 2016, Janssen submitted an application seeking approval of guselkumab for the treatment of moderate to severe plaque psoriasis in the US and Europe. If approved, guselkumab would be the first marketed HuCAL antibody. Psoriasis is a chronic, autoimmune inflammatory disorder characterized by abnormal itching and physically painful skin areas. It is estimated that as many as 125 million people worldwide have psoriasis with approximately 25% suffering from cases that are considered moderate to severe. Independent market experts forecast the market for psoriasis to grow from € 7.5 billion in 2014 to € 12 billion in the year 2024.

**Anetumab ravtansine** (BAY 94-9343), a HuCAL antibody-drug conjugate (ADC) against the target mesothelin, is a potential treatment for **mesothelioma** and other solid tumors which is being developed by Bayer. Bayer believes if the potentially pivotal phase 2 study in mesothelioma, which started in early 2016, shows positive results, the next step could be an application for regulatory approval. Mesothelioma is a tumor that develops in the lungs primarily as a result of exposure to asbestos. Bayer highlighted this program (as a *Lighthouse Project*) in September 2016 as a promising compound with extraordinary potential. Bayer believes the peak sales potential for this compound is in excess of € 2 billion per year.

**Utomilumab** (PF-05082566) is a HuCAL antibody developed by Pfizer in the field of **immuno-oncology**. The compound is directed against the target 4-1BB (CD137) on T cells and is currently being tested in several phase 1/2 clinical trials in both solid and hematological tumors. According to Pfizer, preclinical findings show the combination of utomilumab with checkpoint inhibitors could strengthen the immune response against cancer.

**Gantenerumab** is a HuCAL antibody developed by MorphoSys's partner Roche targeting amyloid beta. It adds a potential treatment for **Alzheimer's disease** to MorphoSys's pipeline. This compound is being investigated in several clinical studies to see if there is a positive effect from intervening at an early stage in the disease's progression. In two of these studies, Roche is evaluating the compound in around 1,000 patients with mild Alzheimer's disease and 800 patients with prodromal Alzheimer's disease.

Roche has converted these trials into open-label studies to test higher doses after the temporary discontinuation of earlier studies at the end of 2014. There are currently no drugs that fundamentally improve the course of Alzheimer's disease.

#### **INNOVATION CAPITAL**

Several years ago, MorphoSys started its Innovation Capital initiative to combine the traditional investment approach of an industry partner with the cooperative elements of compound development as flexibly as possible. This allowed the Company to make selective investments in promising young companies whose products and technologies may potentially benefit MorphoSys. One example for this initiative is the investment in Lanthio Pharma in 2012 and the acquisition of the all remaining shares in the company in 2015.

## **Research and Development and Business Performance**

#### **2016 BUSINESS PERFORMANCE**

MorphoSys's business is strongly focused on advancing its therapeutic programs in research and development to increase the Company's value. With the clinical development of proprietary programs as the focal point of the Company, we strive to gain access to novel disease-specific target molecules, advanced product candidates and innovative technology platforms to expand our proprietary development pipeline. MorphoSys also participates in the development success of its partners' therapeutic programs. The first of these antibodies based on MorphoSys's technology is approaching the market.

The key measures of value and success of MorphoSys's research and development include:

- collaborations and partnerships with other companies to broaden the Company's technology base and pipeline of compounds and commercialize its therapeutic programs
- the initiation of projects and the progression of individual development programs
- clinical and preclinical research results
- regulatory guidance of health authorities to pursue commercialization of individual therapeutic programs
- robust patent protection to secure MorphoSys's market position

#### **COLLABORATIONS AND PARTNERSHIPS**

##### **PROPRIETARY DEVELOPMENT**

In May 2016, MorphoSys and the University of Texas MD Anderson Cancer Center announced a long-term strategic alliance. With MorphoSys applying its Ylanthia technology platform, the partners plan to work together to identify, validate and develop novel anti-cancer antibodies up to the clinical proof of concept. The alliance aims to investigate numerous targets in a variety of oncology indications. MorphoSys and MD Anderson will conduct early clinical studies of therapeutic antibody candidates after which MorphoSys has the option to continue developing selected antibodies in later stages of clinical development for its own proprietary pipeline.

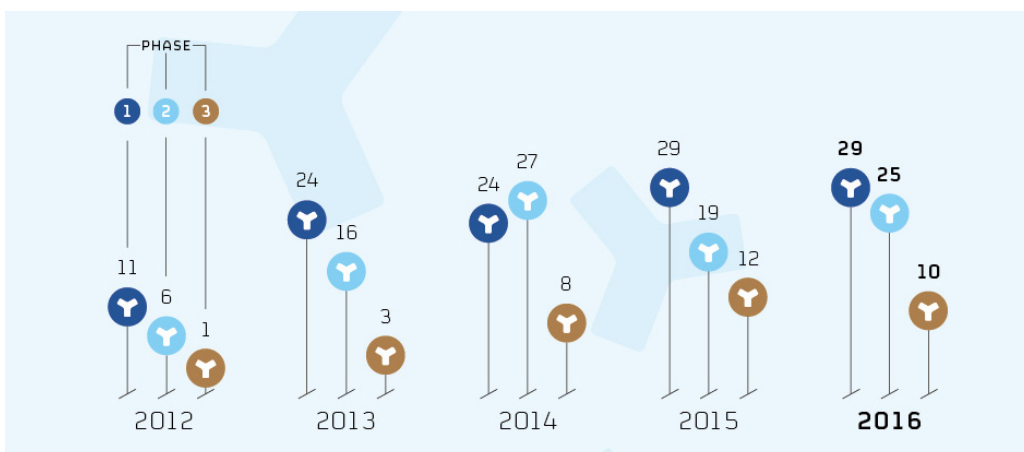
**PARTNERED DISCOVERY**

In November 2016, MorphoSys and LEO Pharma announced a strategic alliance for the discovery and development of therapeutic antibodies for the treatment of skin diseases. The objective of the alliance is to identify novel, antibody-based therapeutics for unmet medical needs that will be valuable additions to both companies' development pipelines. MorphoSys will apply its Ylanthia technology platform to generate fully human antibody candidates against the targets selected by LEO Pharma and will conduct all development activities up to the start of clinical testing. LEO Pharma will be responsible for clinical development and commercialization of resulting drugs in all indications outside of cancer. In skin cancer indications, MorphoSys will have options to co-develop and, in Europe, co-promote the respective antibody drugs. In addition, MorphoSys will have certain options to develop and commercialize therapeutic programs arising from the collaboration in other cancer indications. MorphoSys will receive R&D funding as well as success-based development, regulatory and commercial milestone payments, plus royalties on net sales of drugs commercialized by LEO Pharma. Assuming all development, regulatory and sales objectives are achieved, milestone payments could add up to € 111.5 million per antibody program.

**PROJECT INITIATIONS AND PROGRESS, TRIAL EXTENSIONS**

During the 2016 financial year, the number of therapeutic programs in the MorphoSys pipeline grew to a total of 114 (December 31, 2015: 103 programs) Proprietary Development and Partnered Discovery projects. At the end of 2016, MorphoSys had 14 projects (December 31, 2015: 14) in its Proprietary Development portfolio, five of which were in clinical development and nine in preclinical development or the discovery phase. The number of programs being pursued by our partners in the Partnered Discovery segment grew to a total of 100 (December 31, 2015: 89), 24 of which were in clinical development, 22 in preclinical development and 54 in the discovery phase. MorphoSys's partnered and proprietary clinical pipeline currently comprises 29 unique antibody molecules that are being evaluated in more than 60 clinical trials.

**FIG. 2: ACTIVE CLINICAL STUDIES WITH MORPHOSYS ANTIBODIES (DECEMBER 31)**



#### PROPRIETARY DEVELOPMENT

Based on clinical results obtained with MOR208, MorphoSys initiated a phase 2 trial program in 2016 for its further development in combination with other cancer drugs for B-cell-based malignancies.

- A trial initiated in April 2016 is evaluating MOR208 in combination with lenalidomide in patients suffering from relapsed or refractory diffuse large B cell lymphoma (DLBCL) (L-MIND study). The trial is designed as an open-label, single-arm study with the primary endpoint being the overall response rate (ORR) and multiple secondary endpoints, including progression-free survival (PFS), overall survival (OS) and time to progression (TTP). In August 2016, MorphoSys announced the successful completion of the safety run-in phase of the L-MIND trial. No unexpected safety signals were detected and the trial was continued as planned.
- In September 2016, MorphoSys disclosed that the first patient had been dosed in the safety evaluation part of a phase 2/3 clinical combination trial of MOR208. The B-MIND (Bendamustine-MOR208 IN DLBCL) trial will evaluate the safety and efficacy of MOR208 combined with the chemotherapeutic agent bendamustine in comparison to rituximab plus bendamustine. This trial will enroll 330 adult patients worldwide with relapsed or refractory DLBCL who are not eligible for autologous stem cell transplantation. The trial's phase 2 safety run-in is currently evaluating the safety and tolerability of MOR208 with bendamustine in comparison to rituximab plus bendamustine. After the safety run-in, the trial will transition into a pivotal phase 3 trial, planned to start in 2017.
- In addition to the two combination studies with MOR208 in DLBCL, MorphoSys announced in December 2016 the start of a phase 2 combination study with MOR208 in a further indication. The trial which has been named COSMOS (CLL patients assessed for ORR & Safety in MOR208 Study), is designed to evaluate the safety and efficacy of MOR208 in combination with idelalisib in patients with relapsed or refractory chronic lymphocytic leukemia (CLL) or small lymphocytic lymphoma (SLL). The patients enrolled must have been refractory or shown relapse or intolerance to a prior therapy with a BTK inhibitor such as ibrutinib. This patient cohort shows a particularly high medical need.

The HuCAL antibody MOR202 targeting CD38 is currently being evaluated in a phase 1/2a dose-escalation study alone and in combination with the immunomodulatory cancer drugs (IMiDs) lenalidomide and pomalidomide, in each case with dexamethasone, in patients with relapsed/refractory multiple myeloma (MM). In this trial, a growing number of patients in the reporting year were treated with the highest dose cohort of 16 mg/kg MOR202 in combination with lenalidomide and pomalidomide.

MOR209/ES414, which we are co-developing with our partner Aptevo Therapeutics (a spin-off of Emergent BioSolutions), is in a phase 1 trial in patients suffering from metastatic castration-resistant prostate cancer. The first patient was recruited for the trial according to the amended trial protocol in the fourth quarter of 2016.

The HuCAL antibody MOR103/GSK3196165, which was out-licensed to GlaxoSmithKline (GSK), is currently being developed in a phase 2b study in patients with rheumatoid arthritis. In April 2016, GSK announced the initiation of a phase 2a clinical trial to investigate the safety and efficacy of MOR103/GSK3196165 in patients with inflammatory hand osteoarthritis. GSK also initiated a mechanistic phase 2a trial of MOR103/GSK3196165 in rheumatoid arthritis to further investigate the GM-CSF signaling pathway.

In 2016, MOR106 became the fifth drug candidate from MorphoSys's proprietary pipeline in clinical development. In April, MorphoSys and its development partner Galapagos NV announced the initiation

of a phase 1 clinical trial to evaluate MOR106 in healthy volunteers. The trial was expanded at the end of September to include patients suffering from atopic dermatitis after MOR106 showed favorable safety results in healthy volunteers during the first phase of the study. MOR106 is the first antibody generated using MorphoSys's proprietary Ylanthia technology to enter clinical development. This phase 1 trial investigates the safety, tolerability and pharmacokinetic profile of MOR106 in single ascending doses in healthy volunteers as well as multiple ascending doses in patients with atopic dermatitis. MOR106 is the first publicly disclosed antibody targeting IL-17C in clinical development worldwide. Galapagos and MorphoSys jointly discovered MOR106 and are co-developing this compound in clinical studies.

#### **PARTNERED DISCOVERY**

In January 2016, MorphoSys's partner Bayer initiated a phase 2 clinical study in mesothelioma with the HuCAL-based antibody drug conjugate anetumab ravtansine (BAY 94-9343) which targets mesothelin. MorphoSys recognized the related milestone payment in the first quarter of 2016. Bayer's objective is to apply for market approval based on the results of this study, if successful.

On April 21, 2016, MorphoSys announced that its partner Novartis confirmed that a phase 2b/3 study investigating the HuCAL antibody bimagrumab (BYM338) in the rare disease sporadic inclusion body myositis (sIBM) did not meet its primary endpoint. All three of the phase 3 studies in this indication were discontinued. The HuCAL antibody's active phase 2 clinical trials in sarcopenia, a form of age-related muscle loss, and muscular atrophy after hip operations continued as planned. In December 2016, Novartis announced on the website [clinicaltrials.gov](http://clinicaltrials.gov), that a phase 2 trial with bimagrumab in another indication will be started. This trial is designed to assess the safety, pharmacokinetics and efficacy of the HuCAL antibody versus a placebo in around 60 obese patients with type 2 diabetes.

In July and October of 2016, MorphoSys announced the receipt of milestone payments from Novartis. These payments were triggered by the initiation of phase 1 clinical trials with novel HuCAL antibodies for the prevention of thrombosis and in the field of cancer. The number of HuCAL antibodies investigated by Novartis in clinical trials rose to a total of 14 after the initiation of a clinical study of a further HuCAL antibody in the field of asthma in 2016.

In October, MorphoSys announced that its licensee Janssen Research & Development, LLC (Janssen) reported positive results from a phase 3 clinical study of guselkumab in 837 patients with moderate to severe plaque psoriasis ("VOYAGE 1" study). Janssen reported that both of the trial's co-primary endpoints were met, including improving the symptoms of psoriasis, while delivering clear or almost clear skin (measured by the parameters IGA 0 or 1 and PASI 90) at week 16 in patients receiving guselkumab, compared to those receiving a placebo. Janssen also reported that all major secondary endpoints achieved statistical significance in comparisons of guselkumab versus adalimumab (Humira®). In November 2016, Janssen submitted a regulatory filing to the U.S. Food and Drug Administration (FDA) and to the European Medicines Agency (EMA) for the treatment of adults living with moderate to severe plaque psoriasis.

In November 2016, MorphoSys announced that its licensee Janssen Research & Development, LLC (Janssen) had presented positive results from a phase 2a clinical study evaluating guselkumab in patients with active psoriatic arthritis (PsA). The data published by Janssen showed that a substantially higher percentage of patients receiving guselkumab achieved at least a 20 percent improvement in signs and symptoms of the disease (ACR 20) at week 24, the study's primary endpoint, compared with patients receiving placebo. Janssen announced that it will now evaluate the compound further in a phase 3 program in PsA.

## CLINICAL STUDY DATA FROM CURRENT PROJECTS

### PROPRIETARY DEVELOPMENT

In 2016, MorphoSys announced data from clinical studies of its proprietary drug programs MOR202 and MOR208 at several industry conferences.

Current data from a phase 2a clinical study with anti-CD38 antibody **MOR208** in patients with subtypes of relapsed or refractory non-Hodgkin's lymphoma (NHL) was presented at the American Society of Clinical Oncology (ASCO) 2016 Annual Meeting (June), the Congress of the European Hematology Association (EHA) in June, the Annual Conference of the German, Austrian and Swiss Associations of Hematology and Medical Oncology (DGHO) in October and the Annual Meeting of the American Society of Hematology (ASH) in December. This data primarily concerned the patient subgroup analysis and the duration of response to continued therapy. In June 2016, MorphoSys also announced the publication of a clinical case report from this study in the Journal of Medical Case Reports.

This open-label, multi-center phase 2a study is evaluating the efficacy and safety of weekly doses of 12 mg/kg MOR208 in 92 pre-treated patients with various subtypes of relapsed/refractory NHL. Included in this study were patients with diffuse large B cell lymphoma (DLBCL) and patients with indolent NHL (iNHL) including follicular lymphoma (FL). All patients had received at least one prior rituximab-containing therapy. The most recent data presented at the ASH Annual Meeting in December 2016 showed continued long-lasting responses in patients after more than 26 months, confirming results from previous trials. Three patients with DLBCL and six with iNHL showed ongoing response to therapy; seven of whom achieved a complete response (CR) and two with a partial response (PR). The overall response rate (ORR) was 36% in the DLBCL subgroup and 33% in iNHL patients (both based on evaluable patients). The progression-free survival rate (PFSR) after 12 months was 39% for both subgroups. In addition to the patients with an objective response (PR or CR), the majority of patients with stable disease (SD) had a reduction in target lesion size (5/6 DLBCL and 14/17 iNHL). The duration of progression-free survival (PFS) was similar in patients with rituximab non-refractory and rituximab refractory tumors who were treated with MOR208. This shows that MOR208 demonstrated clinical activity independent of any response to previous anti-CD20-based therapies.

Updated results for safety and clinical activity from another ongoing phase 2 study with MOR208 were announced at the ASH Annual Meeting in December 2016. In this investigator-initiated trial (IIT) conducted by scientists at the Ohio State University, MOR208 is being evaluated in various CLL patient populations, among others, in combination with the immunomodulator lenalidomide. The trial also includes a fourth cohort of CLL patients with identified resistance mutations to ibrutinib in which MOR208 was added to the ibrutinib therapy. According to the abstract submitted at the ASH conference, of the group of CLL patients with ibrutinib-resistant cells in the study, four out of seven patients had already been receiving MOR208 in addition to ibrutinib for at least three cycles of 28 days each, and no patient had developed progressive disease at the time the abstract data was submitted. Preliminary data show activity in patients in all cohorts, including ibrutinib-resistant CLL patients.

MorphoSys's anti-CD38 antibody **MOR202** is currently being evaluated in an ongoing phase 1/2a clinical study in pre-treated patients suffering from relapsed/refractory multiple myeloma. Updated results on safety and tolerability from this study were released at several conferences in 2016, including the ASCO Annual Meeting and EHA Congress in June, the DGHO Annual Meeting in October and the ASH Annual Meeting in December. This study is a dose-escalation study investigating MOR202 alone and in combination with the immunomodulatory drugs (IMiDs) lenalidomide (Len) and pomalidomide



(Pom), plus dexamethasone (Dex). The study's results were consistent with earlier data and generally showed further improved responses as the number of patients in the higher dosing cohorts increased. MOR202 showed encouraging clinical response rates, especially in combination with IMiDs, with a very short 2-hour infusion time with rare and comparatively mild infusion-related reactions (IRRs) of grades 1 and 2 occurring in just 7% of patients. No unexpected safety signals were observed.

The latest presentation at the ASH Annual Meeting in December 2016 reported the following early efficacy data for MOR202:

- The patients receiving MOR202 plus Len/Dex showed an objective response rate of 91% (10 out of 11 patients) across all clinically relevant dose cohorts (8 mg/kg and 16 mg/kg). All 7 patients in the highest dosing cohort of 16 mg/kg MOR202 plus Len/Dex showed an initial overall response (OR) to therapy.
- Of the heavily pre-treated patients in the cohort treated with a combination of MOR202 (dose cohorts 8 mg/kg and 16 mg/kg) and Pom/Dex, 4 out of 7 patients showed an overall response; although, at the time of evaluation, two patients in the highest dose cohort of 16 mg/kg had been in treatment for only a relatively short time. Of the 4 patients showing an overall response, 2 patients achieved a complete response (CR).
- Of the patients treated with MOR202 alone in combination with Dex (dose cohort of 4 mg/kg, 8 mg/kg and 16 mg/kg), 29% (5 out of 17) responded to therapy. The median progression-free survival (PFS) of these patients was 4.7 months.
- In 14 of the 19 cases observed, patients are still showing response to therapy with the longest response to date being 14 months.
- Biomarker data suggests that the antibody's CD38 expression on the surface of the MM patients' bone marrow plasma cells is preserved during MOR202 therapy.

#### **PARTNERED DISCOVERY**

During the reporting year, partners of MorphoSys continued to develop HuCAL antibodies and presented their progress and data on the following programs at scientific conferences, such as the Annual Conference of the American Society of Clinical Oncology (ASCO) in Chicago in June 2016:

- Bayer presented an ongoing pivotal phase 2 study in mesothelioma with the HuCAL antibody-drug conjugate anetumab ravtansine.
- Bayer also presented data from a phase 1 study of anetumab ravtansine in patients with solid tumors.
- Pfizer presented phase 1 data from its study of the anti-4-1BB antibody PF-05082566 (utomilumab) in combination with pembrolizumab in patients with solid tumors.
- Boehringer Ingelheim presented first phase 1b data from a phase 1b/2 study of BI-836845 in patients with breast cancer.
- OncoMed published data from a phase 1b study of tarextumab in small cell lung cancer.
- OncoMed also published data from a phase 1b study of vantictumab in breast cancer.

#### **REGULATORY EVENTS**

##### **PARTNERED DISCOVERY**

In November 2016, MorphoSys's partner Janssen submitted applications in the United States (FDA) and Europe (EMA) seeking approval of the HuCAL antibody guselkumab for the treatment of adults living with moderate to severe plaque psoriasis. If approved, guselkumab could become the first marketed

antibody based on MorphoSys's technology. In this case, MorphoSys would benefit from royalties on net sales.

## PATENTS

During the 2016 financial year, MorphoSys continued to consolidate and expand the patent protection of its development programs and its growing technology portfolio, which are the Company's most important value drivers.

On April 4, 2016, MorphoSys announced that it filed a lawsuit in the United States (U.S.) District Court of Delaware against Janssen Biotech, and Genmab, A/S for patent infringement of U.S. Patent Number 8,263,746. This patent, which is owned by MorphoSys, describes and claims antibodies with particular features that bind to CD38. By its complaint, MorphoSys seeks redress for the infringing manufacture, use and sale of Janssen's and Genmab's daratumumab, an antibody targeting CD38.

At the end of the financial year, the Company maintained over 50 different proprietary patent families worldwide in addition to the numerous patent families it pursues with its partners.

## Development on Company Level and in Subsidiaries

In September 2016, MorphoSys announced the establishment of a Scientific Advisory Board (SAB), which was set up to advise the Company on strategic issues and future perspectives within its research and development activities. The inaugural members are Dr. Günther R. Adolf (previously at Boehringer Ingelheim, Vienna, Austria), Prof. Dr. Bruce D. Cheson (Georgetown University Hospital, Washington D.C., USA), Dr. Sergio Quezada (University College London Cancer Institute, London, UK) and Dr. Raymond W. Sweet (previously at Janssen, J&J, Pennsylvania, USA).

In September 2016, MorphoSys's Dutch subsidiary Lanthio Pharma B.V., specializing in the development of lanthipeptides, announced the appointment of Axel Mescheder, MD as Chief Medical Officer. Dr. Mescheder has more than 20 years of management experience in R&D for the pharmaceutical and biotechnology industry. At Lanthio Pharma, Dr. Mescheder will be primarily focused on developing Lanthio Pharma's lanthipeptide portfolio, and preparing and executing the clinical development of MOR107.

In November 2016, MorphoSys completed a private placement via an accelerated book building process raising gross proceeds of approximately € 115.4 million. MorphoSys issued 2,622,088 new shares from authorized capital to institutional investors in Europe and North America at a price of € 44.00 per share. The offering represented approximately 9.9% of the registered pre-transaction common stock and brought the total number of shares to 29,159,770. The new shares were admitted to trading on the Frankfurt Stock Exchange following their issue. The Company intends to use the proceeds in particular to fund the further clinical development of its proprietary programs. Furthermore, the proceeds of the transaction will be used to advance pre-clinical assets as well as to fund potential in-licensing of oncology product candidates or additional technologies.

## Headcount Development

Motivated, exceptionally skilled employees who are both creative and dedicated are the foundation of MorphoSys's success. On December 31, 2016, MorphoSys AG had 333 employees (December 31, 2015: 352), 127 of whom hold PhD degrees (December 31, 2015: 136). MorphoSys AG employed an average of 342 employees in 2016 (2015: 345).

A competitive remuneration system and favorable working environment are crucial factors when competing for the best employees. To be a competitive employer, MorphoSys compares the Company's compensation with that paid by other companies in the biotech industry and similar sectors and makes adjustments when necessary. The remuneration system at MorphoSys includes fixed compensation and a variable annual bonus that is linked to the achievement of corporate goals. Individual goals promote both the employees' personal development and the achievement of key corporate goals.

In addition, a "spot bonus" (given "on the spot") is promptly awarded to employees for exceptional accomplishments. We made significant use of this instrument during the reporting year.

A detailed overview of headcount development and MorphoSys's activities to promote successful long-term human resource development can be found in the section "Sustainable Business Development."

## Development of the Business Environment

Forecasts by the International Monetary Fund (IMF) predict a slowdown in global economic growth to 3.1% in 2016 (2015: 3.2%). This slightly lower forecast reflects the rather subdued outlook for the advanced economies after the Brexit vote in the UK in June 2016 and weaker than expected growth in the United States.

Although the market's response to the Brexit vote has been somewhat moderate, increasing economic, political and institutional uncertainty, coupled with a decline in trade and finance between the UK and the rest of the European Union, is expected to have a negative impact on the overall economy, especially in the UK. As a result, the 2016 growth forecast for the advanced economies was reduced to 1.6% (2015: 2.1%). After five years of declining growth rates, the emerging and developing economies are expected to report slightly higher growth of 4.1% (2015: 4.1%). The outlook for these countries varies but is generally less optimistic than in the past. Based on its outlook published in January 2017, the IMF expects the economic recovery in the eurozone to continue and projects growth of 1.7% for 2016 (2015: 2.0%). The 2016 forecast for Germany is also 1.7% (2015: 1.5%), with growth being driven by strong domestic demand. The US economy has lost momentum in recent quarters and expectations are for growth of 1.6% for the whole of 2016 (2015: 2.6%). The impact on the US and global economy after the election of Donald Trump is not yet clear. The global economy's growth engine, China, is expected to grow 6.7% (2015: 6.9%) thereby remaining within its official target range of 6.5 to 7%, thanks to policy measures and strong credit growth. Russia continues to be stuck in a recession, although the economic trend improved slightly with a projected decline of just 0.6% in 2016 compared to a reported -3.7% in 2015. The Brazilian economy continued to contract (2016 forecast: -3.5% vs. 2015: -3.8%).

MorphoSys takes into account all potential macroeconomic risks and opportunities when conducting business activities. Political uncertainty in the global markets did not cause the Company to refrain from or change any of its key activities in the past financial year. MorphoSys's operations were also not affected by any fluctuations within individual countries and, therefore, in this respect were not directly impacted by global economic developments.

### CURRENCY DEVELOPMENTS

The euro and the US dollar continued to edge toward parity in 2016. Following the rate increase by the US Federal Reserve in December 2016, further rate increases are expected in 2017. There is little

evidence that the European Central Bank is planning to change the course of its monetary policy characterized by negative interest rates and large bond buying programs. These policies have placed pressure on the euro in 2016 causing it to reach a 13-year low in mid-December as it fell below the US\$ 1.05 threshold. At the end of 2015, the euro was still at US\$ 1.09. After the election of Donald Trump, Citigroup revised its forecast and now expects the euro to fall to \$ 0.98 in the next six to 12 months.

Because most of the Company's business is transacted in euros and US dollars, changes in these currencies could have an effect on MorphoSys's future costs and revenues. Continued weakness in the euro versus the US dollar has a direct influence on the Company's operating results because a growing share of its costs stem from clinical studies conducted in the United States. MorphoSys deals with this risk with appropriate hedge accounting measures.

## REGULATORY ENVIRONMENT

The healthcare industry's regulatory environment is dominated by continually rising product quality, safety and efficacy requirements, which places ever-higher demands on the companies involved. Novel drugs are required to demonstrate a significant benefit over existing therapies in order to be approved, gain the market's acceptance and be financially reimbursed. In the United States, which represents the world's largest healthcare market, it is not yet clear what type of health policy will be pursued by the new Trump administration. Discussions have ranged from a withdrawal to an adaptation of the Affordable Care Act, but further details have not yet been disclosed.

The US Food and Drug Administration (FDA) approved a total of 22 medications in 2016, including six for the treatment of cancer, or half of the previous year's number (2015: 45). In the period from 2006 to 2014, the FDA approved an average of 28 new compounds every year. Nevertheless, a strong importance is still placed on the industry's continued commitment to innovation and developing technologically better products and optimizing already approved treatments.

## DEVELOPMENT OF THE PHARMACEUTICAL AND BIOTECHNOLOGY SECTORS

In comparison to an exceptionally strong year for the global pharmaceutical industry in 2015, the outlook for the industry in 2016 turned somewhat discouraging. Analysts expect the largest ten pharmaceutical companies to generate growth of just 2% p.a. on average in 2016 and 2017. Experts cite two main causes for the growth slowdown: one is the decline in new innovative drugs in 2016 and the corresponding decline in the number of approvals; the other is fear of a growing price pressure in the United States.

Political uncertainty for both the overall economy and the pharmaceutical industry has increased with the November 2016 election of Donald Trump as the new US president. Initially, the pharma industry was concerned it would be forced to face stricter price controls under a Clinton administration. These concerns have died down with Trump's election win. In addition, a public petition in California demanding price caps for drugs in state-funded healthcare programs, which received strong public attention, was lost in November 2016. In early January 2017, Trump stirred up the industry again with his criticism of drug pricing and the location policies of US pharmaceutical companies. This resulted in a painful loss for the pharmaceutical indices on the stock markets. Given the sharp rise in prices for certain products, such as Mylan's EpiPen, which led to hearings in the US Congress and caused nationwide criticism in 2016, the public demands for price controls continue to exist.

A report from the International Trade Administration of the US Department of Commerce expects worldwide pharmaceutical sales to grow annually by 4.9%, or from roughly US\$ 1 trillion to US\$ 1.3 trillion between 2015 and 2020. The demand for pharmaceutical products is being driven by a variety of demographic and economic trends, including a rapidly aging world population and the associated increased incidence of chronic diseases, increasing urbanization and greater disposable income, higher public health spending and a growing demand for more effective treatments.

The market for cancer drugs – the most important market for MorphoSys’s development pipeline – is one of the most attractive and fastest-growing segments of the pharmaceutical market. The US market research institute QuintilesIMS Institute estimates that, in 2015, the worldwide oncology market amounted to US\$ 107 billion. A continuous increase in innovative therapies is the market’s key driver. The report from IMS expects the global market for oncology products to grow between 7.5% and 10.5% and reach US\$ 150 billion in 2020. The majority of this growth is a result of the broader diversity of new products, especially immunotherapies, which is offsetting the decline in some of the existing therapies with poorer clinical results. IMS also expects insurers to negotiate harder with manufacturers and introduce new payment models to achieve better prices for drugs. The World Health Organization (WHO) anticipates a 70% increase in the number of cancer-related diseases worldwide over the next 20 years.

According to the global auditing company PricewaterhouseCoopers (PWC), the number of mergers and acquisitions in the pharmaceutical and healthcare sector in 2016 declined significantly compared to the prior year. A total of 387 M&A transactions with a reported total value of US\$ 197.0 billion were completed in 2016 compared to 435 transactions with a reported value of US\$ 286.6 billion in the same period of 2015.

Further information on the development of the stock market environment can be found in the section “Shares and the Capital Market.”

## **DEVELOPMENT OF THE ANTIBODY SECTOR**

The year 2016 was a very dynamic and successful year for the clinical development of therapeutic antibodies. The FDA granted regulatory approval to seven antibodies – after a record of nine antibodies in the prior year. In a follow-up article to the scientific magazine mAbs Journal’s article “Antibodies to watch in 2016,” the Antibody Society disclosed that by the middle of 2016 a total of 53 antibodies were in phase 3 clinical trials (year-end 2015: 53), of which 15 are intended for treating cancer (year-end 2015: 17).

In November 2016, an application for regulatory approval was submitted to the FDA for guselkumab, a compound derived with the help of MorphoSys’s technology. The application was submitted after a phase 3 clinical trial conducted by MorphoSys’s development partner Janssen delivered positive results for this compound in psoriasis.

Antibody compounds in the field of cancer immunotherapy continued to dominate the headlines in 2016. Clinical data shown in 2015 further corroborated the efficacy of the anti-PD1 and anti-PD-L1 antibodies, which act by blocking immune checkpoints. These compounds, which trigger the body’s own immune system using antibodies to identify and kill tumor cells, were again a dominant theme at the spring 2016 ASCO Meeting, the world’s premier cancer conference.

In 2016, the following antibodies received their first regulatory approval:

- Zinplava<sup>®</sup> (bezlotoxumab) against Clostridium difficile infections
- Lartruvo<sup>®</sup> (olaratumab) against soft tissue sarcoma
- Zinbryta<sup>®</sup> (daclizumab) for multiple sclerosis
- Tecentriq<sup>®</sup> (atezolizumab) used to treat the most common form of bladder cancer
- Cinqair<sup>®</sup> (reslizumab) against severe asthma
- Taltz<sup>®</sup> (ixekizumab) for moderate to severe manifestations of psoriasis
- Anthim<sup>®</sup> (obiltoximab) for the treatment of inhalation anthrax

After the FDA granted first-time approval to a biosimilar (Zarxio<sup>®</sup>, filgrastim-sndz) in 2015, approval of the first biosimilar antibody followed in April 2016, namely Inflectra<sup>®</sup> (infliximab-dyyb). Inflectra<sup>®</sup> is the biosimilar of Remicade<sup>®</sup> (infliximab).

# Analysis of Net Assets, Financial Position and Results of Operations

## Revenues

Compared to the previous year, revenues decreased as planned by 53% to € 48.7 million (2015: € 102.7 million). Revenues in the comparable period 2015 included a one-off effect in the amount of approx. € 59 million due to the termination of the collaboration with Celgene for the co-development and joint commercialization of MOR202 resulting in the release of hitherto deferred revenues. The Proprietary Development und Partnered Discovery segments contributed € 2.0 million (2015: € 58.3 million) and € 46.6 million (2015: € 44.4 million) to total revenue, respectively. Refer to the notes for the impact on the annual financial statements due to the first-time application of the Accounting Directives Implementation Act (Bilanzrichtlinie-Umsetzungsgesetz).

Of total revenues, € 1.9 million (2015: € 2.2 million) related to companies located in Germany and € 2.8 million (2015: 58.7 Mio. €) to biotechnology and pharma companies as well as non-profit organizations located in North America. Revenues in the amount of € 44.0 million were generated with companies located in Europe and Asia (2015: € 41.8 million).

## Cost of Goods Sold

Cost of goods sold mainly comprised research and development expenses and increased by € 12.1 million to € 94.8 million (2015: € 82.7 million). This change was primarily resulting from higher costs in connection with intangible assets in the amount of € 13.7 million (2015: € 3.8 million), mainly due to the partial impairment of the MOR209/ES414 program in the amount of € 10.1 million. Furthermore, costs for external services increased (2016: € 44.4 million; 2015: € 36.8 million) due to higher expenses for proprietary development, particularly for external laboratory services.

Those effects were partly offset by lower personnel expenses (2016: € 26.7 million; 2015: € 30.4 million), mainly impacted by lower taxable monetary benefits from the allocation of share-based payments as well as by lower personnel expenses from performance shares in connection with LTI plans.

## Selling Expenses

Selling expenses increased by € 0.4 million to € 2.5 million (2015: € 2.1 million), mainly as a result of higher personnel costs and higher costs for external services.

## General Administration Expenses

General administration expenses amounted to € 18.6 million (2015: € 17.5 million). This increase was mainly caused by higher costs for external services (2016: € 5.2 million; 2015: € 2.8 million). The



increase in costs for external services mainly resulted from expenses in connection with the capital increase carried out in November 2016.

## Other Operating Income, Other Operating Expenses, Other Interest and Similar Income as well as Other Interest and Similar Expenses

Other operating income amounted to € 6.6 million and decreased by € 10.1 million compared to 2015. This item primarily included effects from the taxation of monetary benefits in connection with the exercise of share-based payment programs by employees of the Company as well as from the release of accruals and provisions.

Other operating expenses decreased from € 1.0 million in 2015 to € 0.5 million in 2016. The main drivers for the increased other operating expenses in the previous year were realized losses from financial derivatives as well as a one-time effect from an impairment of other assets.

Other interest and similar income decreased from € 1.7 million in 2015 to € 1.2 million in 2016, and mainly comprised interest income from bank deposits and financial investments.

## Income from Investments

In financial year 2016, there were no distributions to MorphoSys AG. In financial year 2015, an amount of € 0.02 million from retained earnings of the subsidiary Poole Real Estate Ltd. was distributed to MorphoSys AG.

## Income from Other Securities and Loans Presented under Financial Assets as well as Losses from Other Securities and Loans Presented under Financial Assets

Income from other securities and loans presented under financial assets in the amount of € 0.3 million (2015: € 0.1 million) were composed of realized gains from securities. Losses from other securities and loans presented under financial assets amounted to € 0.9 million in financial year 2016 (2015: € 0.4 million) and comprised unrealized losses from the valuation as well as realized losses from the sale of securities.

## Impairment of Financial Assets and of Current Securities

In financial year 2016, there was no impairment of financial assets and current securities. In financial year 2015, an impairment on the share in Poole Real Estate Ltd. in the amount of € 0.04 million was accounted for.

## Income Tax

Given the positive result from ordinary activities in financial year 2015, a tax income for losses carried back for income tax purposes in the amount of € 0.2 million was recorded.

## Result after Taxes / Net Profit / Net Loss

The aforementioned effects led to a result after taxes in the amount of € -60.2 million (2015: € 13.7 million) and a net loss in the amount of € -60.2 million (2015: net profit of € 13.6 million).

## Financial Position

### PRINCIPLES OF FINANCIAL MANAGEMENT

At MorphoSys, the primary objective of financial management is to have sufficient liquidity reserves available for the continued growth of the Company at all times. The main sources of this liquidity are the operational business activities of the various parts of the Company and the resulting cash inflows. Scenario projections and cash flow projections are used to determine the liquidity requirements.

### INVESTMENTS

MorphoSys's investments in property, plant and equipment amounted to € 2.4 million and increased by € 1.1 million in comparison to the previous year. Depreciation of property, plant and equipment slightly increased compared to the previous year and amounted to € 1.7 million in 2016 (2015: € 1.5 million).

In 2016, the Company invested € 0.1 million (2015: € 7.1 million) in intangible assets, namely for software licenses. Amortization of intangible assets remained unchanged in comparison to the previous year and amounted to € 0.8 million in 2016 (2015: € 0.8 million). In financial year 2016, an impairment in the amount of € 10.1 million was recognized on the in-process R&D program MOR209/ES414.

### LIQUIDITY

As of December 31, 2016, the Company held liquid funds, bank deposits, other securities presented under current assets and other financial assets in the amount of € 343.8 million, compared to € 286.6 million on December 31, 2015.

The increase in liquidity mainly resulted from the capital increase (€ 115.4 million) carried out in November 2016. This effect was partly compensated by the consumption of cash for operating activities in 2016 as well as for the repurchase of shares for the long-term incentive programs of the Company.

## Net Assets

### ASSETS

Total assets increased by € 65.7 million to € 445.3 million as of December 31, 2016 compared to € 379.6 million as of December 31, 2015. The increase in other assets (+ € 110.1 million) and shares in affiliated companies (+ € 7.5 million) as well as in deferred revenue (+ € 4.8 million) was compensated by a reduction in liquid funds and securities in the amount of € 44.5 million in total as well as a reduction in intangible assets (- € 11.4 million). The movement in shares in affiliated companies was affected by a capital increase in Lanthio Pharma B.V. The decrease in intangible assets resulted from the partial impairment of the in-process R&D program MOR209/ES414. The movement in other assets, liquid funds and securities arose from the capital increase in November 2016 and from the consumption of liquid funds in the course of operating activities.

### ACCRUALS AND LIABILITIES

As of December 31, 2016, accruals amounted to € 31.2 million, compared to € 27.2 million in the previous year. The increase of other provisions from € 25.7 million to € 29.7 million was mainly caused by higher accrued expenses for outstanding invoices for external laboratory services (2016: € 15.9 million; 2015: € 13.8 million).

Trade accounts payable increased from € 0.3 million to € 8.4 million. The increase arose from liabilities for external laboratory services not due as of the balance sheet date.

### EQUITY

As of December 31, 2016, equity totaled € 404.1 million compared to € 349.5 million on December 31, 2015.

The number of shares issued totaled 29,159,770 as of December 31, 2016, of which 28,763,760 shares were outstanding (December 31, 2015: 26,537,682 shares issued and 26,103,012 shares outstanding).

On November 15, 2016, a total of 2,622,088 shares were issued in the context of a cash capital increase from Authorized Capital 2014-I and fully exhausted the Authorized Capital 2014-I. As a result, the number of authorized ordinary shares fell by 2,622,088 shares, from 13,206,421 as of December 31, 2015 to 10,584,333 shares.

In comparison to December 31, 2015, the number of ordinary shares of conditional capital declined from 7,086,000 to 6,752,698. At the Annual General Meeting on June 2, 2016, Conditional Capital 2003-II in the amount of € 36,000 and Conditional Capital 2011-I in the amount of € 6,600,000 were canceled. Offsetting this effect was the new creation of Conditional Capital 2016-I in the amount of € 5,307,536 and Conditional Capital 2016-III in the amount of € 995,162.

On December 31, 2016, the Company held 396,010 shares of treasury stock valued at € 14,648,212, representing a decline compared to December 31, 2015 (434,670 shares, € 15,827,946) of € 1,179,743. The reason for this decline was the transfer of 90,955 shares of treasury stock valued at € 3,361,697 to the Management Board and Senior Management Group from the 2012 long-term incentive (LTI) program. The vesting period for this LTI program expired on April 1, 2016 and October 1, 2016,

respectively, and beneficiaries were given the option to receive a total of 90,955 shares within six months. Offsetting this amount was MorphoSys's repurchase of 52,295 of its own shares via the stock exchange at a weighted-average price per share of € 41.69 for a total value of € 2,179,963.

As of December 31, 2016, additional paid-in capital amounted to € 408.0 million, compared to € 295.2 million as of December 31, 2015. The increase by € 112.8 million resulted from the premium generated in the capital increase of 2,622,088 shares in November 2016.

Net loss for 2016 in the amount of € -60.2 million was netted with the accumulated profit 2015 (€ 14.9 million), and the resulting accumulated deficit in the amount of € -45.4 million was carried forward.

## Financing

As of December 31, 2016, the Company's equity ratio amounted to 91% compared to 92% on December 31, 2015. The Company has currently no financial debt vis-à-vis financial institutions.

## Off-Balance-Sheet Financing

MorphoSys does not use any off-balance-sheet financing instruments such as the sale of receivables, asset-backed securities, sale-and-leaseback transactions or contingent liabilities in combination with non-consolidated special-purpose entities.

## Credit Rating

There is no agency currently assessing the creditworthiness of MorphoSys.

## Comparison of Actual Business Results Versus Forecasts

MorphoSys demonstrated solid financial performance during the 2016 reporting year. A detailed comparison of the Company's forecasts versus the actual results can be found in Table 6.

TAB. 2: COMPARISON OF ACTUAL BUSINESS RESULTS VERSUS FORECASTS

	2016 Targets	2016 Results
<b>Financial targets</b>	Revenue between € 44 million and € 49 million	Revenue of € 48.7 million
	Expenses for proprietary product and technology development of € 73 million to € 80 million	Expenses for proprietary product and technology development of € 75.6 million
	Result before Taxes of € -58 million to € -68 million	Result before Taxes of € -60.3 million
<b>Proprietary Development</b>	MOR208 <ul style="list-style-type: none"> <li>Initiation of the L-MIND trial (in combination with lenalidomide in DLBCL)</li> <li>Initiation of the B-MIND trial (in combination with bendamustine in DLBCL)</li> <li>Initiation of the COSMOS trial (in combination with idelalisib in CLL)</li> </ul>	MOR208 <ul style="list-style-type: none"> <li>Initiation of the L-MIND trial in April</li> <li>Initiation of the B-MIND trial in September</li> <li>Initiation of the COSMOS trial in December</li> </ul>
	MOR202 <ul style="list-style-type: none"> <li>Continuation of the phase 1/2a study in additional cohorts with the recommended dose of 16 mg/kg alone and in combination with pomalidomide and lenalidomide</li> </ul>	MOR202 <ul style="list-style-type: none"> <li>Presentation of clinical data from the ongoing phase 1/2a study at the ASCO Annual Meeting in June, the German, Austrian and Swiss Associations of Hematology and Medical Oncology in October and the annual ASH meeting in December</li> </ul>
	MOR209/ES414 <ul style="list-style-type: none"> <li>Continuation of the adapted phase 1 trial in mCRPC under the cooperation with Aptevo Therapeutics, a spin-off of Emergent BioSolutions</li> </ul>	MOR209/ES414 <ul style="list-style-type: none"> <li>Recruitment in the fourth quarter of 2016 of the first patient for the trial under the adapted trial protocol</li> </ul>
	MOR106 <ul style="list-style-type: none"> <li>Initiation of a phase 1 trial as part of the co-development program with Galapagos</li> </ul>	MOR106 <ul style="list-style-type: none"> <li>Initiation of a phase 1 trial in healthy volunteers in April; evaluation in patients suffering from atopic dermatitis started in September</li> </ul>
	MOR107 <ul style="list-style-type: none"> <li>Initiation of a phase 1 trial</li> </ul>	MOR107 <ul style="list-style-type: none"> <li>Preparations for initiating phase 1 trial completed in 2016; start of phase 1 study with healthy volunteers in February 2017</li> </ul>
	In-licensing of one or more targets and compounds to strengthen the proprietary development portfolio	<ul style="list-style-type: none"> <li>No target or compound in-licensed</li> </ul>
	Ongoing development of the lanthipeptide technology	<ul style="list-style-type: none"> <li>Ongoing development of the lanthipeptide technology in the reporting year</li> </ul>

	2016 Targets	2016 Results
	Initiation and continuation of new development programs in the area of antibody discovery and preclinical development	<ul style="list-style-type: none"> <li>• Initiation of a strategic partnership with MD Anderson Cancer Center to discover and develop new antibodies against cancer</li> </ul>
<b>Partnered Discovery</b>	Progress of partnered discovery programs	<ul style="list-style-type: none"> <li>• Net addition of 11 partnered discovery programs</li> <li>• Positive results from a phase 3 study with the HuCAL antibody guselkumab in plaque psoriasis; Janssen submitted application for regulatory approval in the United States and Europe</li> <li>• Initiation of a pivotal phase 2 trial by partner Bayer with the HuCAL antibody anetumab ravtansine (BAY 94-9343) as a potential treatment for mesothelioma</li> <li>• Initiation of a phase 1 trial by Novartis with a HuCAL antibody to prevent thrombosis</li> <li>• Initiation of a phase 1 trial by Novartis with a HuCAL antibody against cancer</li> <li>• Initiation of a strategic partnership with LEO Pharma to discover and develop novel antibodies for the treatment of skin diseases; MorphoSys has co-development and co-commercialization options in the area of cancer</li> </ul>

## The Management Board's General Assessment of Business Performance

The 2016 financial year marked a successful year for the Group overall. We successfully expanded our pipeline and increased the number of development programs to 114 by the end of 2016 (2015: 103). We significantly strengthened our liquidity through a capital increase that yielded € 115.4 million in gross proceeds. As a result, the Company can continue to develop its programs from a position of strength. Furthermore, the first antibody based on MorphoSys's technologies has been filed for regulatory approval in the United States and Europe.

The Company's revenue in the 2016 financial year decreased to € 48.7 million and result before taxes declined to € -60.3 million. The main cause of the decline in revenue and negative result before taxes was the termination of the Celgene cooperation and the related one-off effect in the amount of roughly € 59 million in 2015. Our equity ratio of 91% and liquidity of € 343.8 million underscore the Company's very sound financial position.

The Proprietary Development business segment saw a clear maturation of its pipeline consisting of 14 active compounds (year-end 2015: 14). Three phase 2 combination studies were started with MOR208 in blood cancer indications. The ongoing dose-escalation study with MOR202 in multiple myeloma tests the drug at higher doses. Updated results were presented at major medical conferences. In our cooperation with Galapagos, MOR106 began clinical development in atopic dermatitis. The phase 1 study of MOR209/ES414 was resumed by our development partner Aptevo, with a new dosage regimen. Partner GSK launched two phase 2a studies with MOR103/GSK3196165 in hand osteoarthritis and rheumatoid arthritis. Preparations continued for the first clinical trial with MOR107, the active substance acquired as part of the acquisition of Lanthio Pharma. In addition, our cooperation with MD Anderson Cancer Center increased our access to innovative targets in cancer medicine.

The Partnered Discovery segment also progressed very well. Its pipeline significantly expanded and matured. The HuCAL antibody guselkumab, developed by Janssen, met the study endpoint in a phase 3 study in plaque psoriasis, after which Janssen applied for regulatory approval in the United States and Europe in November. Guselkumab could become the first antibody on the market based on MorphoSys's technologies - a momentous event in the history of the Company. The antibody bimagrumab missed its primary endpoint in a phase 3 study in sIBM but ongoing phase 2 trials in two other indications continue and a phase 2 development in a new indication was started. Partner Bayer launched a pivotal phase 2 study with anetumab ravtansine in mesothelioma. With a total of 100, we ended the year with a record number of programs (year-end 2015: 89).

## Accounting Judgments

In preparing the 2016 separate financial statements, no accounting policies or accounting options were used that differ from those in prior years and that, if used or exercised differently, would have had a material effect on the Company's net assets, financial position, results of operations or balance sheet structure. Information on the effects of the Management Board's use of estimates, assumptions and judgments can be found in the Notes to the Separate Financial Statements.

## Outlook and Forecast

MorphoSys is focusing a growing amount of its efforts on the development of its proprietary drug candidates. By continually expanding its development pipeline and focusing on areas of therapy with a high unmet medical need such as oncology and inflammatory diseases, MorphoSys intends to raise its potential for future growth and value appreciation and, at the same time, limit the overall risk inherent in developing novel drugs. These activities are enhanced through a large number of partnered programs, which we believe will yield higher revenues from royalties, which we can increasingly use to finance our proprietary programs.

### General Statement on Expected Development

MorphoSys's strategic focus is on the development of a broad and sustainable pipeline of innovative drug candidates, both on a proprietary basis and with partners. The foundation for achieving this is the Company's continued investment in the development of innovative and proven technologies. In the therapeutic area, the commercialization of these technologies provides contractually secured cash flows from long-term partnerships with major pharmaceutical companies. MorphoSys also plans to profit from the successful development of drug candidates through milestone payments and royalties from product sales as soon as the drugs are commercialized.

Revenues from R&D funding, license and milestone payments and a strong liquidity position enable MorphoSys to further expand its commercial operations by investing in the development of proprietary drugs and technologies. The Management Board expects the following developments in 2017:

- Higher investments in proprietary product candidates by continuing ongoing clinical studies and initiating new clinical studies.
- Continued expansion of proprietary development activities through potential in-licensing, company acquisitions, co-development and new proprietary development activities.
- New strategic agreements based on proprietary technologies focused on gaining access to innovative target molecules and compounds.
- Investments in technology development to maintain the Company's leading position in therapeutic antibodies and related technologies, such as lanthipeptides.

### Strategic Outlook

MorphoSys's business model is based on its proprietary technologies, including the HuCAL and Ylanthia antibody libraries, the Slonomics platform and the lanthipeptide library. We want to continue to use these technologies to develop innovative drug candidates so that patients have access to better treatment alternatives. MorphoSys's management intends to continue expanding the Company's proprietary portfolio of drug candidates and increase its investment in its proprietary development portfolio, particularly in the areas of oncology and inflammatory diseases. MorphoSys will also continue to concentrate on using and expanding its technologies in fast-growing, innovation-driven areas of the life sciences sector.



In the Proprietary Development segment, MorphoSys develops proprietary therapeutic antibodies and peptides, primarily in the areas of oncology and inflammatory diseases. Decisions to enter into alliances to develop MorphoSys's proprietary candidates will be made on an individual basis. In some cases projects can remain in proprietary development for a longer period – even until their commercialization.

The Partnered Discovery segment generates contractually secured cash flows based on long-term cooperation agreements. The majority of development candidates derives from the partnership with Novartis. As previously mentioned, MorphoSys expects the partnership with Novartis to terminate at the end of November 2017 in accordance with the contract and does not believe that Novartis will exercise its option to extend the contract. The companies are currently discussing how to ensure that the ongoing projects are completed as smoothly as possible. The development of candidates from this partnership continues even after the contract expires and can lead to further milestone payments and royalties. The Company's broad partnered pipeline promises an impressive number of market-ready, therapeutic antibodies in the coming years and financial participation in the form of royalty payments from product sales. During the 2017 financial year, we expect a decision by the regulatory authorities in the United States and Europe on an application for approval of one of our partner's product candidates. A positive decision could result in the first marketed antibody based on MorphoSys technology as early as 2017. We also expect results from a pivotal phase 2 study for a second product candidate.

For the foreseeable future, MorphoSys plans to invest a substantial portion of its financial resources in proprietary R&D. The Management Board believes that this is the best way to expand the Company's portfolio of proprietary development candidates and strengthen its technology platform, and thereby maximize the Company's value.

## Expected Economic Development

The International Monetary Fund (IMF) expects the global economy to grow 3.4% in 2017, or slightly higher than in 2016 (estimated at 3.1%). Brexit and lower-than-expected growth in the United States continue to put pressure on global interest rates because these events are predicted to lead to a long-lasting continuation in expansive monetary policy.

Advanced economies are anticipated to grow 1.8% in 2017 compared to a forecast of 1.6% for 2016. The IMF expects moderate growth of 1.5% for the eurozone, pointing out that the unemployment rate in some of the key European countries will be even higher in ten years than prior to the crisis. There is still risk of weaker economic development in light of Brexit, the refugee crisis and potential protectionist measures of the new US government. The IMF expects economic growth in Germany to reach 1.4% in 2017 (2016E 1.7%). Record employment figures, increasing nominal and real wages and low energy costs are fueling private consumption. However, challenges such as an aging population and a return to normal interest rate levels remain. The IMF is projecting a rise in US economic growth in 2017 to 2.2% compared to expected growth of 1.6% in 2016.

According to the IMF, growth in the emerging and developing countries in 2017 is expected to reach 4.6% (2016E: 4.2%). Growth in China should equal 6.2% in 2017 (2016E: 6.6%) while Russia is expected to resume growth with a positive 1.1%, after an expected drop of 0.8% in 2016. The trend in Brazil is also expected to turn around with growth in 2017 expected at 0.5% following a projected decline of 3.3% in 2016.

## Expected Development of the Life Sciences Sector

After four years (2012–2015) of outstanding performance for biotechnology shares, during which the NASDAQ Biotechnology Index more than tripled, the leading biotechnology index worldwide lost round 22% of its value in 2016 for its worst annual performance since 2002. Based on a poll by the industry news service BioCentury, investors expect the sector to improve in 2017 and report positive performance for the year overall. Industry experts expect M&A activity in 2017 to be high and believe the sector's relative valuation is attractive. However, uncertainty is expected to remain high due to the new and difficult-to-read Trump administration, whereby most experts expect the political environment under a Republican-led US Congress to be industry-friendly overall.

Fundamentally, the sector is still on a strong footing. Scientific advances and a growing understanding of biological relationships, such as those in combination therapies in immuno-oncology, coupled with a continued high medical need – particularly in cancer and chronic inflammatory diseases – and an aging population in the industrialized countries, lead industry experts to expect more innovation and new drug approvals. After the number of FDA approvals for new molecular entities declined from 45 in 2015 to 22 in the year 2016, BioCentury listed a potential 33 approvals for 2017 at the beginning of the year, including the approval of established drugs in new indications.

## Future Research and Development and Expected Business Performance

### PROPRIETARY DEVELOPMENT

The Company's R&D budget for proprietary drug development will rise again in the 2017 financial year compared to the prior year. The majority of investment will fund the clinical development of the proprietary drug candidates MOR208, MOR202, MOR209/ES414, MOR106 and MOR107. Most of the investment within this group will be dedicated to the clinical development of MOR208. Further investment will be made in the area of target molecule validation and antibody and technology development. We will continue to seek cooperation with academic institutes to gain access to new target molecules and technologies.

The plans for the Company's proprietary portfolio in 2017 include:

- Presentation of the first interim results of the phase 2 trial with MOR208 in combination with lenalidomide in DLBCL (L-MIND study).
- Completion of the phase 2 safety part of the B-MIND study and initiation of the pivotal phase 3 part of the study in which MOR208 will be tested in combination with bendamustine in comparison to rituximab and bendamustine in DLBCL.
- Initiation of another study arm of the phase 2 COSMOS trial with MOR208 in CLL in addition to the ongoing study arm of the combination of MOR208 and idelalisib in order to test MOR208 with a further combination partner.
- Completion of the phase 1/2a dose-escalation trial in multiple myeloma, including the results of MOR202 in the highest dose of 16 mg/kg alone and in combination with pomalidomide and lenalidomide.
- Continuation of the phase 1 trial of MOR209/ES414 with adapted dose regimen in mCRPC as part of the Aptevo cooperation.

- Completion of the phase 1 trial of MOR106 co-developed with Galapagos in atopic dermatitis.
- Initiation of a phase 1 study of MOR107 in healthy volunteers (started in February 2017).
- Initiation and continuation of new development programs in the field of antibody identification and preclinical development.

Based on information from the clinicaltrials.gov database, the Company also expects the possible publication of data from a phase 2b study of MOR103/GSK3196165 in rheumatoid arthritis and from a phase 2a study in hand osteoarthritis conducted by its partner GSK.

#### **PARTNERED DISCOVERY**

MorphoSys will concentrate foremost on increasing the value of its current proprietary development pipeline using secured cash flows from its Novartis contract, which is scheduled to end at the end of November 2017, and the Company's strong liquidity, which was reinforced by the capital increase executed in November 2016. MorphoSys plans additional collaborations with pharmaceutical and biotechnology companies based on the Ylanthia technology, similar to its partnership with LEO Pharma established in the reporting year.

The first partner-developed therapeutic antibody based on MorphoSys technology could receive market approval in 2017. MorphoSys also believes regulatory authorities may make a decision in the second half of 2017 on Janssen's application for the approval of guselkumab to treat adults with moderate to severe psoriasis. According to clinicaltrials.gov, anetumab ravtansine, an antibody-drug conjugate developed by Bayer, may report results in 2017 from a pivotal phase 2 trial in mesothelioma. MorphoSys assumes, that this could lead to an application for regulatory approval. Based on other information from clinicaltrials.gov, results may be disclosed from up to 31 different clinical studies in various phases conducted by partners with antibodies based on MorphoSys technology in 2017.

## Expected Personnel Development

The number of employees in the Proprietary Development segment is expected to remain fairly unchanged during the 2017 financial year. The number of employees in the Partnered Discovery segment is expected to decline slightly.

## Expected Development of the Financial Position and Liquidity

MorphoSys has a solid financial base and predictable revenues. Revenues will be derived mainly from its collaboration with Novartis. MorphoSys expects the partnership with Novartis to terminate at the end of November 2017 in accordance with the contract and does not believe that Novartis will exercise its option to extend the contract. Slightly lower revenues are therefore expected for the full year. In addition, MorphoSys receives success-based milestone payments for the successful development of product candidates. Based on the factors, the Management Board expects revenue in the 2017 financial year to reach a range of € 46 million to € 51 million, of which a majority will be generated by the Partnered Discovery segment. This forecast does not take into account any additional revenue from future collaborations and/or licensing partnerships.

The Company was able to substantially strengthen its liquidity by successfully executing a capital increase in the gross amount of € 115.4 million in November 2016, allowing Morphosys to continue developing its proprietary pipeline from a position of strength.

Based on management's current projections, R&D expenses for proprietary programs and technology development in 2017 are expected to be in the range of € 81 million to € 91 million. In addition to continuing the ongoing studies for MOR208, MOR202, MOR209/ES414 and MOR106, MorphoSys initiated a clinical study of MOR107 in February 2017. R&D expenses in the Partnered Discovery segment are expected to be at roughly the same level as the previous years.

The Company's result before taxes in 2017 is expected to be in the range of € -70 million to € -80 million. This guidance does not take into account any potential in-licensing or co-development of further development candidates. The Partnered Discovery segment is expected to generate a clearly positive operating result in 2017, which is anticipated to be slightly lower than in 2016 due to the contractual expiration of the cooperation with Novartis at the end of November 2016. MorphoSys expects the Proprietary Development segment to report a significant operating loss brought on by higher R&D expenses for proprietary programs, as planned.

In the years ahead, there will be an increasing effect on the net assets and financial position from one-time events, such as in-licensing and out-licensing proprietary product candidates, major milestone payments as well as royalties related to HuCAL or Ylanthia antibodies that reach the market. Just as failures in drug development can have a negative impact on MorphoSys, these types of events can lead to a significant change in our financial targets. Near-term revenue growth depends on the Company's ability to enter new partnerships and/or out-license proprietary programs.

At the end of the 2016 financial year, MorphoSys had liquid funds of € 343.8 million (December 31, 2015: €286.6 million). This rise is a result of the capital increase executed in November. The proceeds of this capital increase were partially offset by proprietary research and development expenses and the buyback of shares for the Company's long-term incentive programs. The projected loss in 2017 will cause a decline in liquidity. MorphoSys considers its solid cash position as an advantage that can be used to accelerate its future growth through strategic activities such as the in-licensing of compounds and investments in promising companies. Available liquidity can also be used to fund high research and development for the Company's proprietary portfolio of therapeutic antibodies.

#### **DIVIDEND**

Under German accounting principles, MorphoSys AG is reporting an accumulated loss in its separate financial statements, which does not permit the Company to pay a dividend for the 2016 financial year. In view of the anticipated losses in the year 2017, the Company expects to continue to report an accumulated loss. MorphoSys will invest further in the development of proprietary drugs and intends to do further in-licensing and acquisitions so that it can create additional shareholder value and open up new growth opportunities. Based on these plans, the Company does not expect to pay a dividend in the foreseeable future.

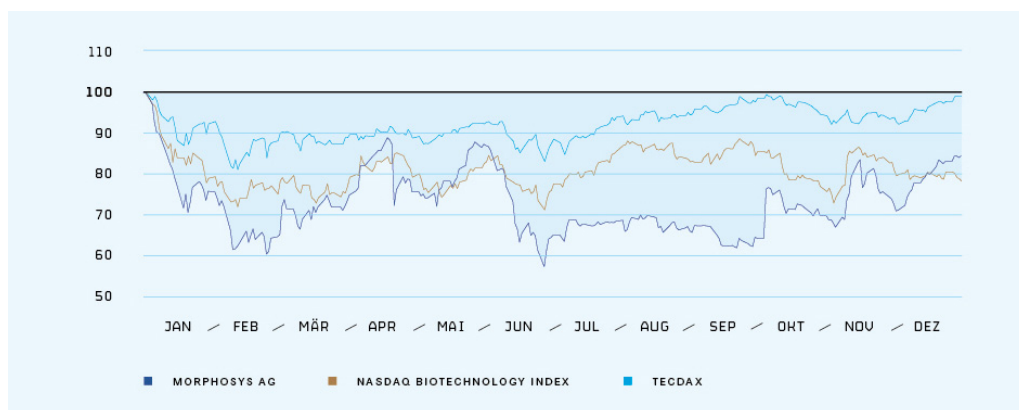
This outlook is based on the Management Board's assumptions and takes into account all of the factors known at the time of preparing this annual report that could influence the Company in 2017 and beyond. Future results may differ from the expectations described in the section "Outlook and Forecast." The key risks are described in the risk report.

## Shares and the Capital Market

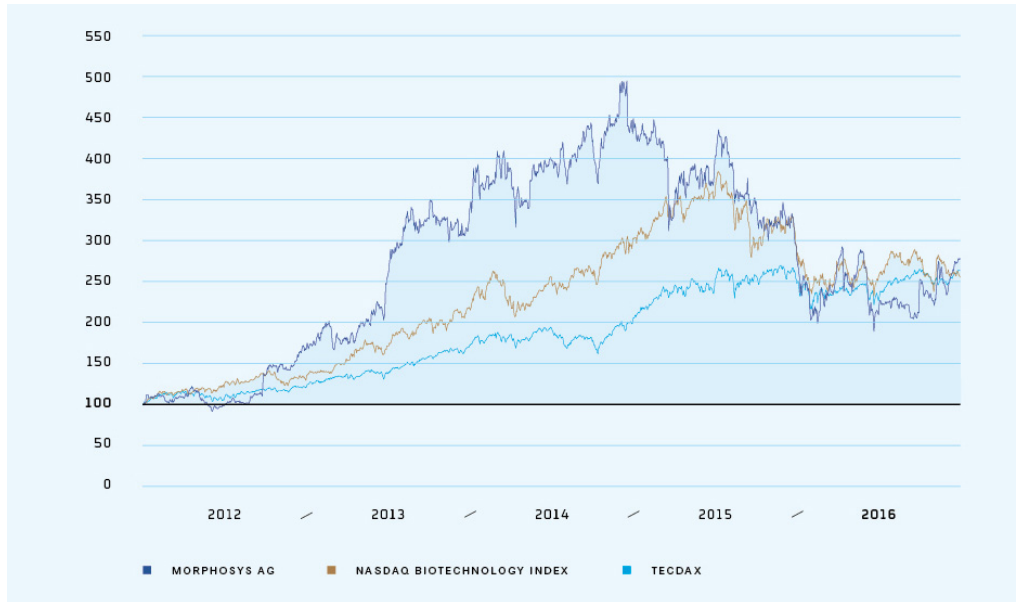
The MorphoSys AG share price started the reporting year at € 57.65. Shortly after the year began, the pharmaceutical and biotechnology shares experienced massive downturns with the NASDAQ Biotechnology Index falling as much as 28%. MorphoSys shares suffered disproportionately from this negative development and fell to their first low for the year in February with a drop of almost 40%. The shares tried to recover as the year progressed but remained volatile due to the industry's negative news flow. Novartis's announcement of disappointing results from a partner phase 2b/3 RESILIENT study with bimagrumab also hurt the MorphoSys share price. The shares began to regain strength with the announcement of positive phase 3 trial results with guselkumab and the corresponding regulatory approval submission by partner Janssen in the fourth quarter. A successful capital increase placed with selected institutional investors in November confirmed the renewed confidence in MorphoSys. The shares closed the financial year at € 48.75 per share and a market capitalization of € 1.42 billion.

Although MorphoSys shares declined 15% for the year, their performance was still within the benchmark range. While the TecDAX fell only 1% for the year, the NASDAQ Biotechnology Index experienced a sharp decline of 22%. Sentiment remained poor following some setbacks in major indications, such as Alzheimer's disease, and in new technologies, such as CAR-T, and due to the ongoing debate on healthcare prices in the US.

**FIG. 3: PERFORMANCE OF THE MORPHOSYS SHARE IN 2016 (JANUARY 1, 2016 = 100%)**



**FIG. 4: COMPARISON OF THE MORPHOSYS SHARE PRICE DEVELOPMENT BETWEEN 2012 AND 2016 (JANUARY 1, 2012 = 100%)**



## Stock Market Development

Stock markets also began the year 2016 with heavy losses, but the year as a whole saw fewer disruptions than in 2015. The surprising Brexit decision and the outcome of the US presidential election caused uncertainty, but have not led to any lasting market volatility. After getting off to a weak start, Germany's leading DAX index gained 7% for the year accompanied by high volatility. Low interest rates continued to provide support in a market with little positive momentum. The US Dow Jones Index, in contrast, after performing poorly in 2015, regained its former strength and climbed even higher following the presidential election.

Investments in the biotechnology sector are generally of a long-term nature. The lack of a solid framework and the loss of faith in the sector in 2016 caused investors to turn increasingly to short-term investments such as futures and index certificates. MorphoSys continued to expand its investor relations activities during the year, focusing its efforts once again on Europe and the United States. The greatest understanding and interest in investing in biotechnology companies continues to be in the United States.

## Liquidity and Index Membership

The average daily trading volume in MorphoSys shares for all of the regulated market's trading platforms combined fell 35% year-on-year to € 9.7 million (2015: € 14.9 million). The difficult trading year for biotechnology shares significantly discouraged investors from buying shares. The trading volume in shares traded on the TecDAX, the index for the 30 largest technology stocks on the Frankfurt Stock Exchange, also fell more than 11% on average with the drop being attributed to the general

uncertainty surrounding Brexit. By the end of 2016, MorphoSys ranked 11th in the TecDAX in terms of trading volume (2015: 8th) and 11th in terms of market capitalization (2015: 10th).

The average daily trading volume in MorphoSys shares on alternative trading platforms (“dark pools”) in 2016 was approximately € 4.4 million, or 103,700 shares (2015: approx. 89,800 shares valued at € 5.8 million), representing a year-on-year increase of 15%.

## Common Stock

The Company’s common stock increased in 2016 to 29,159,770 shares, or € 29,159,770.00. This increase is the result of the capital increase executed on November 15, 2016 in the form of a private placement via an accelerated bookbuilding process. The issue of 2,622,088 new shares from authorized capital to institutional investors in Europe and North America at a price of € 44.00 per share yielded gross proceeds of € 115.4 million. The execution of the capital increase was entered into the commercial register on November 17, 2016, and on November 21, 2016 the new shares were admitted for trading on the Frankfurt Stock Exchange.

MorphoSys issued stock options and non-interest-bearing convertible bonds respectively under its employee incentive program until 2013. In 2011, the Company introduced a performance-based long-term incentive (LTI) program for the first time. In the following years, similar LTI- programs have been established. The Company repurchases shares annually for these programs, a detailed description of which can be found in the Corporate Governance Report contained in this Annual Report. In the 2016 reporting year, a total of 90,995 treasury shares were issued to the Management Board and the Senior Management Group under the performance-based LTI program. For more information, please refer to the Notes. Stock options were not issued to the Management Board, the Senior Management Group nor the workforce in the reporting year. Convertible bonds were not exercised.

**TAB. 3: KEY DATA FOR THE MORPHOSYS SHARE (DECEMBER 31)**

	2016	2015	2014	2013	2012
Total stockholders’ equity (in million €)	404.1	349.5	337.7	346.4	192.1
Number of shares issued (number )	29,159,770	26,537,682	26,456,834	26,220,882	23,358,228
Market capitalization (in million €)	1,422	1,530	2,027	1,464	685
Closing price in € (Xetra)	48.75	57.65	76.63	55.85	29.30
Average daily trading volume ( in million €)	9.7	14.9	11.9	6.9	1.9
Average daily trading volume (in% of common stock)	0.78	0.87	0.65	0.59	0.38

## International Investor Base

Various voting right notifications were issued during the reporting year in accordance with Section 26 (1) of the German Securities Trading Act (WpHG). These notifications were published on the MorphoSys website and can be found under Media and Investors – Stock Information – Shareholder Structure.

According to the definition given by the Deutsche Börse, 98.6% of MorphoSys AG's shares were in free float at the end of the reporting year.

**TAB. 4: MORPHOSYS AG SHAREHOLDER STRUCTURE**

Shareholdings in MorphoSys AG exceeding 3% <sup>1)</sup>	
Baillie Gifford & Co	5.41%
Mark N. Lampert/BVF	4.17%
Schroder International Selection Fund	3.03%

1) According to voting right notifications pursuant to Section 26 (1) WpHG

An overview of the current shareholder structure can also be found on the Company's website (Media and Investors – Stock Information – Shareholder Structure).

## Annual General Meeting

The Management and Supervisory Boards of MorphoSys AG welcomed shareholders to the Company's 18th Annual General Meeting in Munich on June 2, 2016. The shareholders and proxies attending represented more than 54.1% of the common stock of MorphoSys AG (2015: 50.8% of the common stock).

Eight of the nine agenda items submitted for resolution were adopted by a clear majority. The resolution for the creation of Authorized Capital 2016-II and the authorization to grant subscription rights to the MorphoSys AG Management Board, governing bodies of affiliated companies in Germany and abroad and selected executives of MorphoSys AG and affiliated companies in Germany and abroad (Performance Share Plan 2016) (Amendment to the Articles of Association) was supported by 72.25% of the common stock present but did not receive the 75% majority of votes necessary.

## Investor Relations Activities

During the 2016 financial year, MorphoSys continued to strengthen its communication with the capital markets. The Company took part in over 20 international investor conferences and held an Investor's Event in Chicago, IL, USA in June on the occasion of the ASCO Annual Meeting, the world's largest conference for cancer. Several road shows were held at various locations in both Europe and the USA. The strongest interest continued to be in the United States where a large number of specialized healthcare investors are located. Currently, approximately 30% of MorphoSys AG shares are held by institutional investors based in the USA.

The Management Board held conference calls with the publication of the annual, half-yearly and quarterly results to report past and expected business developments and answer questions from analysts and investors.



The key topics when speaking with investors were the progress of the Company's pipeline and the development of the proprietary portfolio, which had a total of 14 active programs at the end of the reporting year. Investors were particularly interested in the clinical results of our partnered programs, especially the data and plans for the pivotal studies.

There were a total of 14 analysts covering MorphoSys shares at the end of 2016. Four of these analysts had initiated coverage of the shares in 2016.

**TAB. 5: ANALYST RECOMMENDATIONS (DECEMBER 31, 2016)**

Buy/Overweight	Hold	Sell	n/a
10	3	0	1

*Buy/Overweight; Hold; Sell; n/a = not available (no rating)*

Detailed information on MorphoSys shares, financial ratios, the Company's strategic direction and the Company's recent developments can be found on the Company's website (Media and Investors).

## Sustainable Business Development

MorphoSys is aware of its responsibility to present and future generations and sees sustainable behavior as a prerequisite for long-term business success. As a biotechnology company conducting both research and drug development, observing the highest ecological, social and ethical standards is a top priority and a key component of MorphoSys's corporate culture. The following section describes the Company's sustainability strategy and the activities carried out during the reporting year that are used as non-financial performance indicators. The financial performance indicators are presented in the section "Analysis of Net Assets, Financial Position and Results of Operations." Information on MorphoSys's management structure and corporate governance practices can be found in the Corporate Governance Report.

### Sustainable Corporate Management

Sustainability is a hallmark of MorphoSys's corporate management and plays a major role in the pursuit of corporate goals and contributing value to society. This applies to the short- and long-term objectives of all levels of management and is reflected in the Company's core task of developing even more effective and safer drugs. To ensure lasting business success, the Company incorporates environmental and social responsibility into its daily business and bases its business model on sustainable growth that protects the interests of its shareholders, creates long-term value and weighs the Company's actions in terms of their impact on the environment, society, patients and employees. This business model is reflected internally in a progressive human resources policy that takes employees' needs seriously.

The Company's long-term and sustainable business success rests on innovative research and development to meet the major challenge of providing comprehensive healthcare in the future. Because of a growing and aging population, biotechnology-derived drugs represent a growing portion of the overall healthcare system. In the opinion of management, all aspects of the current business model of MorphoSys support the sustainable investment interests of its shareholders.

A comprehensive risk management system ensures that factors that could threaten sustainable corporate performance are identified early and corrected if necessary. MorphoSys only assumes risk when there is an opportunity to increase the Company's enterprise value. At the same time, a great effort is made to systematically identify new opportunities and leverage its business success (more information on risks and opportunities can be found in the Risk and Opportunity Report).

Company-wide compliance with the sustainability strategy is monitored by the entire Management Board, chaired by the Chief Financial Officer. The Code of Conduct's credo, which is available in German and English and applies to employees Company-wide, regulates the strategy's implementation in daily operations. Employee training on general and specific sections of the Code of Conduct is conducted regularly to ensure that the guidelines are understood and implemented. The Compliance Committee consists of five members and is available to employees at any time. The Compliance Officer, who is also a member of the committee, coordinates the elements of MorphoSys's Compliance Management System. More information on this subject can be found in the Corporate Governance Report. Employees can ask for advice on all matters concerning legal compliance and corporate responsibility and report any suspected violations. If preferred, this may be done on an anonymous basis. Violations are systematically pursued, and appropriate remedial action is taken. No such violations have been reported to date, and the Company believes it is unlikely in the future that any serious offenses of that kind would occur which could materially affect the Company's net assets, financial position and results of operations.

Detailed information on the KPIs for sustainable development used by MorphoSys is provided in the section “Strategy and Company Management”. The following report on the implementation of MorphoSys’s corporate strategy and the Company’s sustainable business development is based on the recommendations of the German Sustainability Code originally presented by the Council for Sustainable Development in October 2011 and last updated in 2016.

## Non-Financial Performance Indicators

### ETHICAL STANDARDS AND COMMUNICATION WITH STAKEHOLDERS

The highest scientific and ethical principles for conducting human clinical trials and animal testing are anchored in MorphoSys’s Code of Conduct, which is modeled after the “Declaration of Helsinki” of the World Medical Association (WMA). Strict adherence to applicable national and international regulations is mandatory for all MorphoSys employees and sub-contractors.

Because European legislation prescribes the performance of animal testing to determine the toxicity, pharmacokinetics and pharmacodynamics of drug candidates, the biotechnology industry cannot forgo this type of testing. Animal studies are given to contract research organizations (CROs) by MorphoSys because the Company does not have laboratories suitable for this type of research. In the course of product development, MorphoSys contracts out animal studies according to the principles of good animal welfare and the respectful treatment of animals as set out in national and European regulations. MorphoSys introduced a quality assurance and control system with written standard operating procedures (SOPs) that are continually updated to ensure that the Company only deals with contract research organizations that adhere to local, national and international regulations for animal studies. Studies are carried out only after the approval of the relevant ethics committee and under the constant supervision of a veterinarian.

Institutes cooperating with MorphoSys must comply with ethical principles and legal regulations for research involving animals and, in certain cases, have the Good Laboratory Practice (GLP) quality assurance certification. This is how MorphoSys ensures it fulfills its moral obligation for the respectful treatment of animals. The Company also conducts on-site inspections of the research institute’s study centers that include a review of the staff’s skills and training as well as animal welfare. These inspections are carried out during the audits conducted prior to contract awards.

The Declaration of Helsinki mentioned above also defines the ethical principles MorphoSys follows when dealing with healthy volunteers and patients in clinical trials. MorphoSys carries out clinical trials in accordance with Good Clinical Practice (GCP), and testing is conducted in compliance with the relevant provisions on privacy and confidentiality. Protecting the rights, safety and welfare of all clinical trial participants has the highest priority at MorphoSys. Clinical trials are initiated only after the approval of the relevant independent ethics committee and/or institutional review board. Before participating in a clinical trial, each participant must voluntarily submit an informed consent.

The goal of MorphoSys’s business activities is to improve patients’ health through its scientific work. The Company can only achieve this goal if its activities are socially accepted. Achieving this acceptance requires a continuous and open dialog with stakeholders so that MorphoSys can understand potential concerns with regard to biotechnological approaches and explain the Company’s activities and their benefits. To accomplish this, MorphoSys is active in a variety of ways that range from participation in public information events to active support of the Communication and Public Relations task force of BIO Deutschland e.V.

## PROCUREMENT

The Central Purchasing and Logistics Department is responsible for purchasing external goods, consulting and services for MorphoSys in specified areas. During the reporting year, this department continued to work on increasing the efficiency of the systems and processes already in place to achieve long-term improvements in procurement management. It also supported the introduction of a clinical sourcing strategy for purchasing clinical materials and aided in forming strategic partnerships with selected suppliers. All of MorphoSys's selected suppliers worldwide agree to comply with the relevant anti-corruption standards, human rights practices and data protection laws.

## ENVIRONMENTAL PROTECTION AND OCCUPATIONAL SAFETY

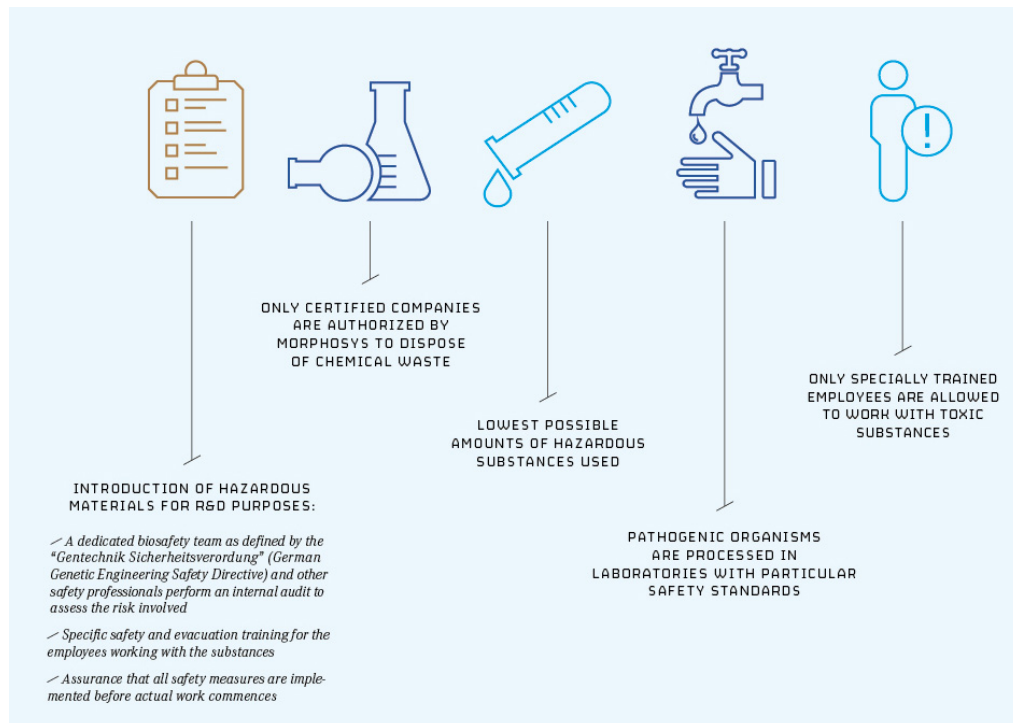
Because the biotechnology industry is subject to stringent regulatory requirements, environmental protection and occupational safety are important tasks of Company management. The Technical Operations Department with its subdivisions monitors Company-wide compliance with all relevant requirements. In addition to strict compliance with all legal requirements, MorphoSys makes a tremendous effort to maintain sustainable environmental management and the effective protection of its employees.

MorphoSys was certified for the seventh consecutive year as a "bicycle-friendly company" for its participation in the "Bike to Work" initiative sponsored by the German Bicycle Club (ADFC) and a German health insurance company. MorphoSys also offers employees an extensive range of preventative healthcare options, such as autogenic training, ball sports, weight training and marathons.

With one reportable occupational accident in the reporting year, the number of accidents was at the same very low level as in the previous year, placing the ratio of reportable accidents at MorphoSys significantly below the average ratio in Germany (22.8 reportable occupational accidents per 1,000 full-time employees in the latest survey conducted in 2015).

MorphoSys tries to minimize the amount of harmful substances used in its laboratories. Only those who are specially trained are allowed to work with toxins. Work involving contagious pathogens can only be carried out in secure laboratories. MorphoSys only uses certified companies to dispose of chemical waste and also refrains from labeling antibodies with radioactive substances.

FIG. 5: OCCUPATIONAL SAFETY AT MORPHOSYS



## QUALITY ASSURANCE

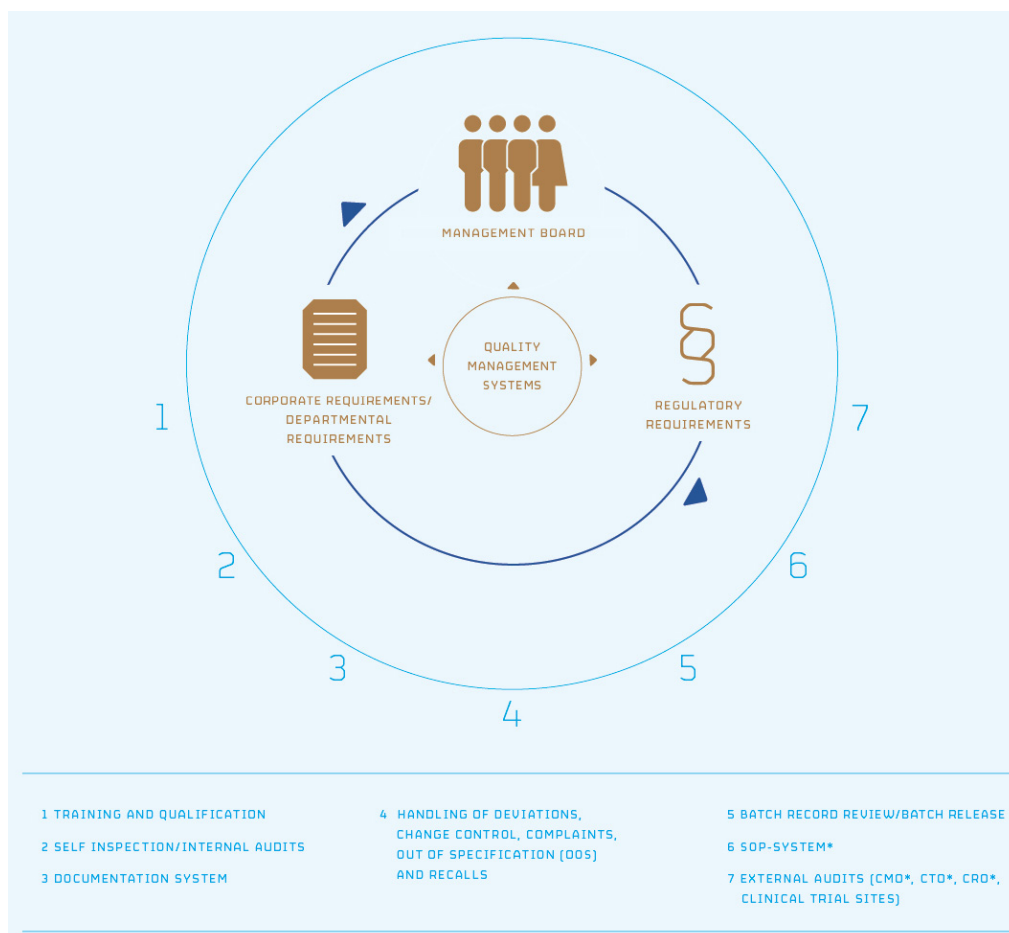
Biopharmaceutical companies bear a special responsibility to comply with the highest quality and safety standards. MorphoSys follows detailed procedures and stringent rules in drug development to avoid safety risks that may pose a threat to patients and, in turn, the Company's financial situation. This is how the Company ensures the quality of the investigational medicinal products, keeps risks to volunteers and patients in clinical studies as low as possible and ensures that the data are measured reliably and processed correctly.

To control and regulate these processes in its own development department, MorphoSys created an integrated quality management system that complies with the principles of Good Manufacturing Practice (GMP), Good Clinical Practice (GCP) and Good Laboratory Practice (GLP). An independent quality assurance department ensures that all development activities comply with national and international laws, rules and guidelines. The Quality Assurance Manager reports to and coordinates activities with the Chief Executive Officer to meet the stringent quality standards, ensure product quality and data integrity, as well as the safety of volunteers and patients in clinical trials.

The Quality Assurance Department prepares an annual review plan using a risk-based approach that is used when auditing the contract research institutes, suppliers and contract manufacturers selected for clinical studies as well as MorphoSys's own departments.

MorphoSys holds a manufacturing license for the approval of tested compounds for its proprietary development activities, and was also issued a certificate from the German authorities of Upper Bavaria confirming the Company's compliance with Good Manufacturing Practice (GMP) standards and guidelines.

FIG. 6: QUALITY MANAGEMENT SYSTEM AT MORPHOSYS



## INTELLECTUAL PROPERTY

Proprietary technology and the drug candidates derived therefrom are MorphoSys's most valuable assets. Therefore, it is critical to the Company's success that these assets are protected by appropriate measures such as patents and patent filings. Only through these means MorphoSys can ensure that these assets are exclusively utilized. It is also the reason our Intellectual Property (IP) Department seeks out the best strategy to protect all of the Company's products and technologies. The rights of third parties are also actively monitored and respected.

MorphoSys's core technologies, which include the Ylanthia antibody library and the Slonomics technology, the basis for the Company's success. Each of these technologies is protected by a number of patent families that protect various aspects of these assets. Meanwhile, most of these patents have been granted in all of the key regions, including the markets of Europe, the United States and Asia.

The same is true for our development programs. In addition to the patents that protect the drug candidates themselves, other patent applications were also filed that cover other aspects of the programs. The relevant patents and associated protection certificates for development candidates MOR103/GSK3196165 (out-licensed to GSK) and MOR202 are expected to expire in 2031. The MOR208

program is also protected by various patents scheduled to expire in 2029 (US patent) and 2027 (European patent), aside from any possible regulatory or patent office extensions.

The programs developed in cooperation with or for partners are also fully secured by patent protection. MorphoSys's patent department works closely with the relevant partners. The patents covering these drug development programs have durations that significantly exceed those of the underlying technology patents.

MorphoSys also monitors the activities of its competitors and initiates any necessary actions. In April 2016, MorphoSys filed a patent infringement lawsuit against Janssen Biotech and Genmab. This lawsuit is still in progress.

MorphoSys's patent attorneys currently maintain over 50 different patent families worldwide in addition to the numerous patent families the Company pursues with its partners. The patent portfolio is routinely analyzed and adapted to the Company's corporate strategy.

## HUMAN RESOURCES

MorphoSys follows a progressive human resources policy for the long-term retention of professionally and personally suitable employees from a variety of fields. In an industry such as the biotechnology industry, where success largely depends on the creativity and commitment of staff, factors like employee retention and employee satisfaction are crucial for success. At the end of the reporting year, MorphoSys had employees representing 31 different nationalities (2015: 29) employed at the Company for an average of 6.9 years (2015: 6.0 years).

Employees have access to a broad range of in-house and external training programs, advanced education, specialized continuing education and development programs and industry conferences. MorphoSys promotes not only ongoing professional education but also the personal development of its employees and in some cases even offers support through customized coaching.

MorphoSys requires all executives with management responsibility to take part in management seminars created exclusively for the Company. The training is based on several thematically related components that aim to provide not only theoretical knowledge but also prepare participants for the special demands placed on the Company's executives.

MorphoSys also actively promoted the professional career paths of specialists and experts during the reporting year. The intended goal of this type of career promotion, which is also available to employees without personnel responsibilities, is to continue to maintain flat hierarchies and place traditional management and professional career paths on equal footing, also in terms of titles and compensation structures.

MorphoSys offers in-house vocational training to open up promising career prospects, particularly for young people. In awarding apprenticeships, the Company has been very successful in considering students who are equally suitable but do not have a diploma. On December 31, 2016, MorphoSys had one trainee in the IT department and six biology laboratory trainees (December 31, 2015: three IT trainees; six biology laboratory trainees).

As articulated in the Company's credo, transparent communication between employees is a central aspect of MorphoSys's corporate culture. One example is the employees' use of the Company's intranet to obtain target-group-specific information. MorphoSys also has a bi-weekly general meeting in which the Management Board presents the Company's latest developments to employees, answers questions and provides an opportunity for employees to present selected projects. Employees' questions and

feedback can be taken directly in the meeting or submitted in advance in writing – anonymously if desired.

MorphoSys maintains a Facebook career page to promote employer branding. The target group is potential applicants who want to learn more about the Company. The page presents employee profiles and reports on a variety of activities extending beyond the typical workday to give an authentic and modern impression of the Company.

New employees are helped to become familiar with the Company through extensive onboarding activities. Employees can learn about the Company's processes in two-day orientation seminars with presentations from all operating departments and by participating in laboratory tours.

Free athletic and relaxation options, back strengthening activities, soccer, volleyball and basketball, as well as autogenic training and massage for a fee, all work to promote health and socializing among employees of all departments.

Providing feasible concepts for reconciling a professional career with personal life is a strategic success factor for progressive companies. For many years, MorphoSys has been offering employees a diverse range of options, such as flexible working hours and special part-time employment arrangements. Modern IT equipment also allows employees to work during business trips or from their home office without interruption. MorphoSys makes it easier for employees with families to re-enter the workforce and combine work and family life. The Company cooperates with an external provider offering employees additional services related to care and nursing.

MorphoSys makes every effort to protect employees from workplace hazards and maintain their health through preventative measures. The extremely low number of occupational accidents illustrates the success of the Company's strict monitoring of all occupational protection and safety measures. During the reporting year, there was one reportable occupational accident. MorphoSys tries to maintain the low number of accidents and the highest level of employee safety and well-being through the help of policies and training from the Department of Health and Occupational Safety and by offering routine medical examinations.



## Risk and Opportunity Report

MorphoSys operates in an industry characterized by constant change and innovation. The challenges and opportunities in the healthcare sector are influenced by a wide variety of factors. Global demographic changes, medical advances and the desire to increase quality of life provide excellent growth opportunities for the pharmaceutical and biotechnology industries; however, companies must also grapple with growing regulatory requirements in the field of drug development as well as cost pressure on the healthcare systems.

MorphoSys makes a great effort to identify new opportunities and to leverage its business success to generate a lasting increase in enterprise value. Entrepreneurial success, however, is not achievable without conscious risk-taking. Through its worldwide operations, MorphoSys is confronted with a number of risks that could affect its business. MorphoSys's risk management system identifies these risks, evaluates them and takes suitable action to avert risk and reach its corporate objectives. A periodic strategy review ensures that there is a balance of risk and opportunity. MorphoSys only assumes risk when there is an opportunity to increase the Company's enterprise value.

### Risk Management System

The risk management system is an essential element of MorphoSys's corporate governance and ensures the Company adheres to good corporate governance principles and complies with regulatory requirements.

MorphoSys has a comprehensive system in place to identify, assess, communicate and deal with risks throughout the Company. The risk management system identifies risk at a very early stage, making it possible to take action to limit operating losses and avoid risks that could jeopardize the Company. All actions to minimize risk are assigned to risk officers, most of whom belong to MorphoSys's Senior Management Group.

All material risks in the various business segments and the Company as a whole are assessed using a systematic risk process that is carried out twice a year. Risks are assessed by comparing their quantifiable financial impact on MorphoSys with their probability of occurrence with and without initiating a risk mitigation process. This method is applied over a 12-month assessment period as well as a period of three years to include risks related to the Company's proprietary development that have longer durations. Additionally, there is a strategic risk assessment that spans more than three years. An overview of MorphoSys's current risk assessment activities can be found in Tables 10 and 11.

Risk managers enter their risks into a Company-wide IT platform that makes monitoring, analyzing and documenting risks much easier. The risk management system distinguishes risk owners from risk managers. Risk owners are typically the relevant department heads (usually members of the Senior Management Group). Risk managers can be department employees when the risks that fall under their area of responsibility are included in the risk management system. Risk owners and risk managers are required to update their risks and assessments at half-yearly intervals. The process for this is coordinated and led by the Corporate Finance & Corporate Development Department, which is also responsible for monitoring the evaluation process and summarizing the key information. The

information is regularly presented to the Management Board who, in turn, presents the results to the Supervisory Board twice a year. The entire evaluation process is based on standardized forms for the evaluations. Risk management and monitoring activities are carried out by the relevant managers. The changes in the risk profile resulting from these activities are recorded at regular intervals. An audit by external consultants ensures the ongoing development of the risk management system and that any potential changes in the Company's risk areas are promptly incorporated. The risk and opportunity management system combines a bottom-up approach for recognizing both short- and medium-term risks with a top-down approach in the area of strategic risks and opportunities. The top-down approach systematically identifies global strategic risks and opportunities and completes the overview of the overall risks and opportunities. Examples include environmental and industry risks, personnel risks and other risks that may result from the public perception of the Company. As part of the top-down approach, workshops are held twice per year with selected members of the Senior Management Group. Within these workshops the strategic risks and opportunities in different areas of the Company are assessed and discussed including those exceeding a period of three years. The evaluation process is solely qualitative. These risks are listed in Table 11.

## Principles of Risk and Opportunity Management

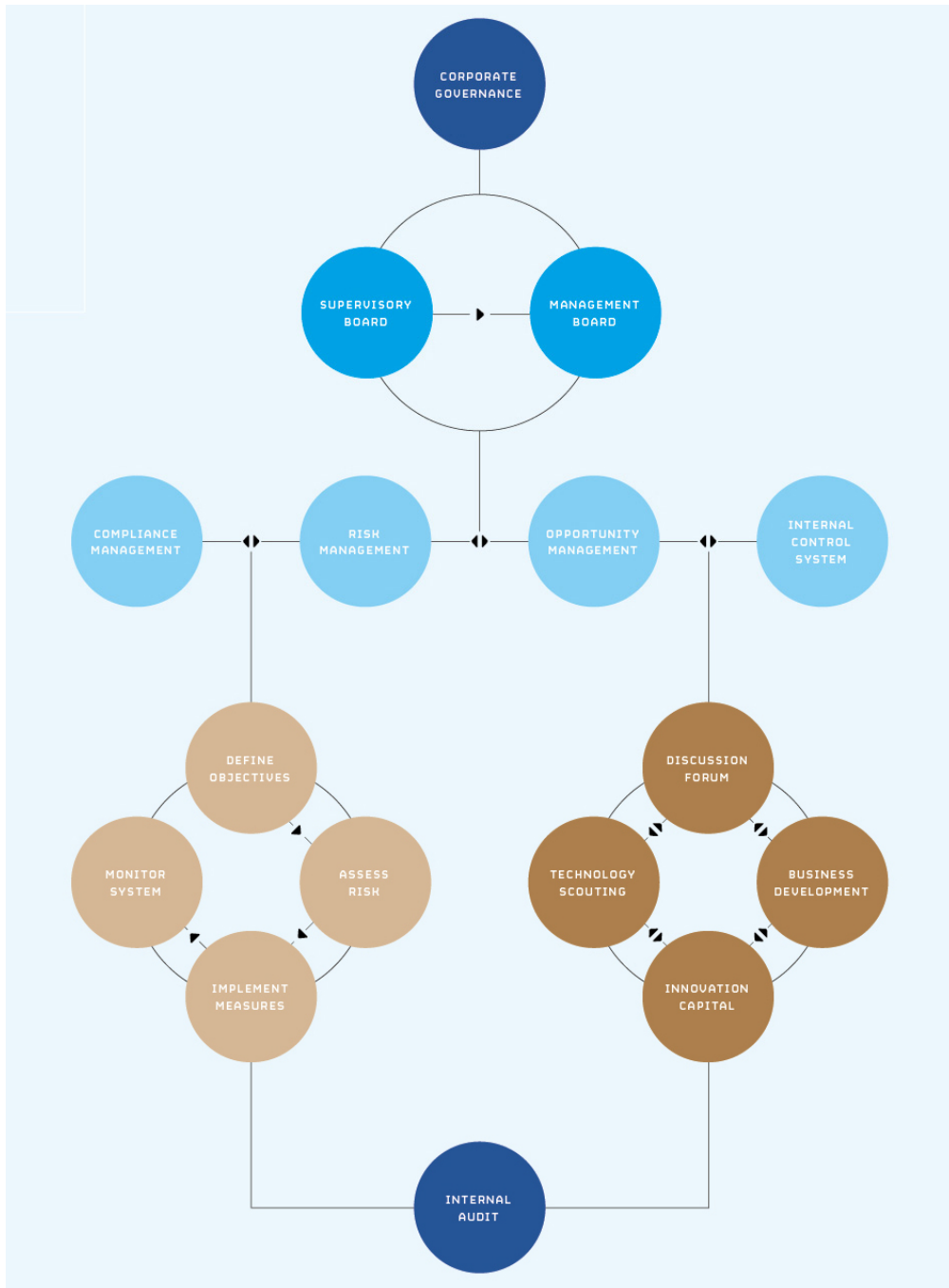
MorphoSys continually encounters both risks and opportunities. These could have a potential material impact on the net assets and financial position as well as a direct effect on intangible assets, such as the Company's image in the sector or the Company's trademark.

MorphoSys defines risk as an internal or external event that has an immediate impact on the Company and includes an assessment of the potential financial impact on the Company's targets. There is a direct relationship between opportunity and risk. Seizing opportunities has a positive influence on Company targets, whereas risk emergence has a negative influence.

## Responsibilities Under the Risk and Opportunity Management System

The Management Board of MorphoSys AG is responsible for the risk and opportunity management system and ensures that all risks and opportunities are evaluated, monitored and presented in their entirety. The Corporate Finance & Corporate Development Department coordinates the implementation of actions and reports regularly to the Management Board. The Supervisory Board has appointed the Audit Committee to monitor the effectiveness of the risk management system. The Audit Committee periodically reports its findings to the entire Supervisory Board, which is also directly informed by the Management Board twice a year.

FIG. 7: THE RISK AND OPPORTUNITY MANAGEMENT SYSTEM AT MORPHOSYS



## Accounting-Related Internal Control System

MorphoSys employs extensive internal controls, Group-wide reporting guidelines as well as other measures, such as employee training and ongoing professional education with the goal of maintaining accurate bookkeeping and accounting and ensuring reliable financial reporting in the consolidated financial statements and group management report. This essential component of Group accounting consists of preventative, monitoring and detection measures intended to ensure security and control in accounting and operating functions. Detailed information about the internal control system for financial reporting can be found in the Corporate Governance Report.

## Risks

### RISK CATEGORIES

MorphoSys divides its key risks into the following six categories.

- Financial risk (includes risk resulting from insolvencies and payment defaults; license fees; research funding and milestones that are lower than planned or anticipated; and risks associated with any form of financing and financial instruments, such as cash investments, bank failures, currencies, (negative) interest rates, taxes, debt collection and lack of funding)
- Operational risk (risk, for example, in the areas of procurement/production, customers and personnel, as well as risk related to preclinical or clinical trial results and other risk specific to the biotechnology industry)
- Strategic risk (for example mergers and acquisitions (M&A), shareholdings, R&D, corporate image, superior development projects and technologies of competitors and portfolio development)
- External risk (risk beyond the Company's control, such as economic, political and legal risk; as well as risk specific to companies in the biotechnology and pharmaceutical industries, such as the risk to intellectual property protection or in the regulatory environment when seeking the approval of new drugs)
- Organizational risk (includes risk concerning IT, facilities management, succession planning, business interruption and process delays as a result of the high complexity and number of projects)
- Compliance risk (for example, non-compliance with US FDA and European EMA regulations, quality management policies, accounting standards, corporate governance or violations of the German Stock Corporation Act)

### FINANCIAL RISK

MorphoSys's financial risk management seeks to limit financial risk and reconciles this risk with the requirements of its business.

Financial risk can arise in relation to licensing agreements, for example when projects (products or technologies) do not materialize, are delayed or out-licensed to a different degree than originally planned. Risk also arises when revenues do not reach their projected level or when costs are higher than planned due to higher resource requirements. Detailed project preparations, such as those made through in-depth exchanges with internal and external partners and consultants, ensure the optimal starting point early in the process and are important for minimizing risk. Financial risk related to the Company's proprietary programs was reduced in 2013 by successfully partnering MOR103/GSK3196165. The financial risk relating to the fully proprietary programs MOR202 and

MOR208 remains entirely with MorphoSys. MorphoSys retains some risk with respect to the clinical development of programs introduced into partnerships; for example, MOR106 and MOR209/ES414. The early termination of development partnerships may force MorphoSys to bear future development costs alone and have a major impact on the Company's income statement and financial planning.

Continuing economic difficulties in Europe indicate that potential bank insolvencies still pose a financial risk. For this reason, MorphoSys continues to invest only in funds and bank instruments deemed safe – to the extent this is possible and can be estimated – and that have maintained their high rating and/or are secured by a strong partner. MorphoSys has simulated various scenarios and set up appropriate contingency plans. A further risk is the receipt of adequate interest on financial investments, particularly in light of today's negative key interest rates.

In future, MorphoSys will continue to spend substantial resources on the development of product candidates, including the identification of target molecules and drug candidates, the conducting of preclinical studies and clinical trials, the manufacturing of material and the support of collaborations and joint development of programs as well as the acquisition of new technologies and the in-licensing of new development candidates. The current financial resources and expected future cash in-flows should be sufficient to meet the Company's current and near-term capital requirements. However, it is not guaranteed that funding will be sufficient in the long term at all times.

#### **OPERATIONAL RISK**

Operational risk includes risks related to the exploration and development of proprietary drug candidates.

The termination of a clinical trial prior to out-licensing to partners – which does not necessarily imply the failure of an entire program – can occur when the trial data does not produce the expected results, shows unexpected adverse side effects or is compiled incorrectly. Clinical trial design and drafts of development plans are always completed with the utmost care. This gives the trials the best opportunity to show clinically relevant data in clinical testing and persuade regulatory agencies and potential partners. External experts also contribute to the Company's existing internal know-how. Special steering committees and panels are formed to monitor the progress of clinical programs.

Antibody production is a significant cost factor in the development of drugs. The Company's obligation to comply with international drug regulatory agencies' requirements at every step of production in order to ensure the highest quality compounds and patient safety plays a critical role in its costs. The production process for biopharmaceuticals is usually performed in cell culture systems with several thousand liters of culture volume and requires a number of steps to be carried out under strict supervision and controlled conditions until the individual investigational medicinal products are ready for use in patients. Therefore, depending on the phase of the project, lead times of up to one to two years must be scheduled for the supply of antibody material. This planning, coupled with early strategic financial investments, represent major factors in drug development because of the high complexity and risk involved in both the production process and clinical trial planning, which can have a considerable effect on the speed and cost of development.

Any changes with respect to clinical trials such as the trial's design or the speed at which patients can be recruited can have a negative impact on the trial's economic feasibility and potential. Such a case occurred at the end of 2016 when MorphoSys recognized a partial impairment on the carrying amount of MOR209/ES414 due to a significant delay in recruiting patients.

Operational risk can arise from the non-renewal of the cooperation agreement with Novartis. The current agreement ends end of November 2017. Novartis has the option to extend this agreement for an additional two years. Should Novartis decide not to exercise this option, MorphoSys would stand to lose annual revenues of approximately €40 million as of the 2018 financial year. At this time, MorphoSys believes that the contract with Novartis will not be extended.

#### **STRATEGIC RISK**

Access to sufficient financing options also poses a strategic risk for the Company. Following MorphoSys's decision to develop its proprietary portfolio in-house, the financing of research and development is now a key focus. Risks in this respect can arise from a lack of access to capital. MorphoSys mitigates these risks by forming multidisciplinary teams responsible for overseeing the budget when adding to the proprietary portfolio. The Company also employs various departments and external consultants to ensure the smooth execution of capital market transactions.

A further strategic risk is the danger that a development program introduced into a partnership may fail. Partnerships can be terminated prematurely, forcing MorphoSys to search for new development partners or bear the substantial cost of further development alone. This may result in a delay or even the termination of the development of individual candidates and could lead to additional costs and a potential long-term loss of revenue for MorphoSys due to delayed market entry. The termination of our partnership with Celgene for MOR202 is an example of the type of risk described.

Another strategic risk is that missed M&A opportunities or failed M&A transactions could block access to strategically important assets. To minimize this risk, MorphoSys has a number of qualified teams who screen the market to ensure that MorphoSys does not miss any acquisition opportunities.

#### **EXTERNAL RISK**

MorphoSys faces external risk with respect to intellectual property, among others. The patent protection of MorphoSys's proprietary technologies and compounds is especially important. To minimize risks in this area, MorphoSys keeps a vigilant eye on published patents and patent applications and analyzes the corresponding results. The Company also develops strategies to circumvent external patents that may one day be relevant before they are issued or takes other appropriate action. Through the years, MorphoSys has seen increasing success with this strategy and has created ample leeway for its proprietary technology platforms and products for many years to come. Risks can also arise from enforcing the Company's patents against third parties. External risks can also emerge from changes in the regulatory environment. These risks are minimized by providing ongoing training to the relevant personnel and by audits and discussions with external experts. It is also conceivable that competitors challenge patents of MorphoSys companies or that MorphoSys concludes that MorphoSys's patents or patent families are infringed by competitors, which may prompt MorphoSys to take legal action against competitors. This type of legal action, particularly when it occurs in the USA, involves high costs and poses a significant financial risk.

As an internationally operating biotechnology company with numerous partnerships and an in-house research and development department for developing drug candidates, MorphoSys is subject to a number of regulatory and legal risks. These risks include those related to patent, competition, tax and antitrust law, potential liability claims from existing partnerships and environmental protection. The Regulatory Affairs department is also affected by this risk in terms of the feedback it receives from regulators on study design. Future legal proceedings are conceivable and cannot be anticipated. Therefore, we cannot rule out that we may incur expenses for legal or regulatory judgments or

settlements that are not or cannot be partially or fully covered by insurance and may have a significant impact on our business and results.

#### **ORGANIZATIONAL RISK**

The Proprietary Development and Technical Operations areas, among others, are subject to organizational risk. Proprietary Development may face quality problems or delays within the organization if the number of programs or their complexity increases. To reduce complexity and thereby reduce risk, the Company introduced uniform procedures and monitors their compliance by means of routine audits.

Risk in the Technical Operations area concerns procedures that may cause lasting damage, business interruptions or accidents involving harmful or polluting substances. Measures taken to avoid these types of disruptions include the routine inspection and maintenance of equipment and facilities and providing training and tutorials for the employees concerned. These risks are reduced even further using electronic monitoring systems. Financial risk in this area is generally covered by insurance. Additional information on MorphoSys's operating environment can be found in the section "Sustainable Business Development."

#### **COMPLIANCE RISK**

Compliance risk can arise when quality standards are not met or business processes are not conducted properly from a legal standpoint. To counter this risk, MorphoSys is committed to having its business operations meet the highest quality standards as set out in the Sustainability Report. The system is also routinely checked by external specialists and subjected to repeat testing by an internal, independent in-house quality assurance department.

Specific risk can arise, for example, when the internal quality management system does not meet the legal requirements or when there is no internal system for detecting quality problems. If the internal controls are not able to detect violations of Good Manufacturing Practice (GMP), Good Clinical Practice (GCP) or Good Laboratory Practice (GLP) then this also would represent a compliance risk.

Inadequate or late financial communication can lead to fines or even lawsuits. Annual General Meetings conducted incorrectly may lead to legal disputes with shareholders resulting in significant costs from attempts to prevent either a challenge to or repeat of the Annual General Meeting. Pending decisions for corporate actions, such as capital increases, could also be compromised. To minimize these risks, the preparation and execution of the Annual General Meeting and all related documents and processes are carefully reviewed and monitored by the relevant internal departments as well as external lawyers and, regarding the annual report, by the auditors.

#### **THE MANAGEMENT BOARD'S EVALUATION OF THE OVERALL RISK SITUATION AT MORPHOSYS**

MorphoSys's Management Board considers the overall risk to be appropriate and trusts in the effectiveness of the risk management system in relation to changes in the environment and the needs of the ongoing business. It is the Management Board's view that the MorphoSys's continued existence is not jeopardized. This conclusion is based on several factors that are summarized as follows:

- MorphoSys AG has an exceptionally high equity ratio.
- The Management Board firmly believes that MorphoSys is well positioned to cope with any adverse events that may occur.

- The Company participates in a comprehensive portfolio of preclinical and clinical programs in partnerships with a number of large pharmaceutical companies and has a strong base of technologies for expanding the Company's proprietary portfolio.

Despite these factors, it is impossible to rule out, control or influence risk in its entirety.

## Opportunities

Leading antibody technologies, excellent know-how and a broad portfolio of validated clinical programs have made MorphoSys one of the world's leading biotechnology companies in the field of therapeutic antibodies. This therapeutic class is now one of the most successful in the industry, and there is an impressive number of pharmaceutical and biotechnology companies in the field of antibodies that could potentially become customers or partners for MorphoSys's products and technologies. Due to this fact and thanks to the Company's extensive technological and product development expertise, MorphoSys has identified a number of future growth opportunities.

MorphoSys's technologies for developing and optimizing therapeutic antibody candidates have distinct advantages that can lead to higher success rates and shorter development times in the drug development process. The transfer and application of MorphoSys's core capabilities – even those outside of the field of antibodies – opens up new opportunities for the Company because many classes of compounds have similar molecular structures. The Innovation Capital initiative seizes previously unavailable opportunities by making MorphoSys a strategic investor in young, innovative companies and allowing it to use synergies effectively.

### OPPORTUNITY MANAGEMENT SYSTEM

The opportunity management system is an important component of MorphoSys's corporate management and is used to identify opportunities early and generate added value for the Company.

Opportunity management is based on four pillars:

- a routine discussion forum involving the Management Board and selected members of the Senior Management Group,
- the Company's business development activities,
- a technology scouting team, and
- the Innovation Capital initiative.

Committees discuss specific opportunities and decide what action should be taken to exploit these opportunities. The meetings and their outcomes are recorded in detail, and any subsequent action is reviewed and monitored. The Group's Business Development Team takes part in numerous conferences and in the process identifies different opportunities that can enhance the Company's growth. These opportunities are presented and evaluated within the committee using an evaluation process. The Technology Scouting Team searches specifically for innovative technologies that can generate synergies with MorphoSys's technological infrastructure and identify new therapeutic molecules. These outcomes are also discussed and evaluated in interdepartmental committees. The Innovative Capital initiative already described also allows MorphoSys to participate in these early innovations and make it possible



for the Company to use them in the future. A proven process for evaluating opportunities gives MorphoSys a qualitative and replicable evaluation.

#### **GENERAL STATEMENT ON OPPORTUNITIES**

Increased life expectancy in industrialized countries and rising incomes and living standards in emerging countries are expected to drive the demand for more innovative treatment options and advanced technologies. Scientific and medical progress has led to a better understanding of the biological process of disease and paves the way for new therapeutic approaches. Innovative therapies, such as fully human antibodies, have reached market maturity in recent years and have led to the development of commercially successful medical products. Therapeutic compounds based on proteins – also referred to as “biologics” – are less subject to generic competition than chemically produced molecules because the production of biological compounds is far more complex. The sharp rise in both the demand for antibodies and the interest in this class of drug candidates can be seen by the acquisitions and significant licensing agreements made over the past two to three years.

#### **MARKET OPPORTUNITIES**

MorphoSys believes its antibody platforms HuCAL, Ylanthia, Slonomics and the in-licensed lanthipeptide technology can all be used to develop products addressing high unmet medical needs.

#### **THERAPEUTIC ANTIBODIES – PROPRIETARY DEVELOPMENT**

It is reasonable to assume that the pharmaceutical industry will increase the level of in-licensing new drugs to refill its pipelines and replace key products and blockbusters that have lost patent protection. MorphoSys's most advanced compounds MOR103/GSK3196165, MOR202 and MOR208 place the Company in an excellent position to capitalize on the needs of pharmaceutical companies.

Secured cash flows from the Partnered Discovery segment have allowed MorphoSys to strengthen its proprietary portfolio continuously. By investigating new disease areas, MorphoSys will continue to expand its proprietary portfolio by adding clinical trials using the Company's key drug candidates. MorphoSys intends to enhance its portfolio with additional programs and in doing so could take advantage of existing and future opportunities for co-development or partnerships. The Company is also looking for more opportunities to in-license interesting drug candidates.

Drug candidates MOR208 and MOR202 may give MorphoSys its first opportunity to market a drug on its own.

#### **THERAPEUTIC ANTIBODIES – PARTNERED DISCOVERY**

By developing drugs with a number of partners, MorphoSys has been able to spread the risk inextricably linked with drug development over a broader spectrum. With 100 individual therapeutic antibodies currently in partnered development programs, it is becoming more likely that MorphoSys will have an opportunity to participate financially in marketed drugs. Our partner Janssen, for example, submitted an application to the US Food and Drug Administration (FDA) in November of 2016 to receive regulatory approval for guselkumab.

## **TECHNOLOGY DEVELOPMENT**

MorphoSys continues to invest in its existing and new technologies to defend its technological leadership. MorphoSys established a new technology platform with Ylanthia that, in contrast to its previous version HuCAL, is eligible for broader licensing to different partners. Commercialization of the Ylanthia antibody library began in 2012.

These types of technological advances can help the Company expand its list of partners and increase not only the speed but also the success rate of its partnered and proprietary drug development programs. New technology modules that enable the production of antibodies against novel classes of target molecules can also provide access to new disease areas in which antibody-based treatments are underrepresented.

Technology development is carried out by a team of scientists whose focus is the further development of MorphoSys technologies. MorphoSys not only develops technology internally but also uses external resources to enhance its own activities. A good example of this is the Company's acquisition of Lanthio Pharma, a Dutch company developing lanthipeptides.

## **ACQUISITION OPPORTUNITIES**

In the past, MorphoSys has proven its ability to acquire compounds and technologies that accelerate its growth. Potential acquisition candidates are also systematically presented, discussed and evaluated during the routine meetings described above between the Management Board and selected members of the Senior Management Group. After these meetings, promising candidates are reviewed in terms of their strategic synergies and evaluated by internal specialist committees. Protocols are completed on all candidates and evaluations are systematically archived for follow-up and monitoring. A proprietary database helps administer this information and keep it available.

MorphoSys plans to move forward with its acquisition strategy in the year ahead in order to enhance its existing portfolio and technology platform and secure access to patents and licenses for novel proprietary technologies and products.

## **FINANCIAL OPPORTUNITIES**

Exchange rate and interest rate developments can positively or negatively affect the Company's financial results. Interest rate and financial market developments are continuously monitored to promptly identify and take advantage of opportunities.

TAB. 6: SUMMARY OF KEY SHORT- AND MEDIUM-TERM RISKS AT MORPHOSYS

	1-Year Assessment	3-Year Assessment
<b>Financial risk</b>		
Risk of missing revenue targets/incorrect budgeting	●●● High	●●● High
Risk of lower interest rates and bank insolvencies	●● Moderate	●● Moderate
<b>Operational risk</b>		
Risk related to development of proprietary antibodies	●●● High	●●● High
Risk related to non-extension of cooperation agreement with Novartis (financial loss)	●● Moderate	● Low
<b>Strategic risk</b>		
Risk of failure to receive financing	● Low	●● Moderate
Risk of missed acquisition opportunities	● Low	●● Moderate
<b>External risk</b>		
Patent-related risk (related to lawsuits, patent situation of technology platform, new national/international regulations)	●● Moderate	●● Moderate
Risk related to regulatory provisions	● Low	● Low
<b>Organizational risk</b>		
Risk due to growing number and complexity of programs	●● Moderate	●● Moderate
Risk in the technical operations area	● Low	● Low
<b>Compliance risk</b>		
Quality risk related to legal requirements	●● Moderate	●● Moderate
Legal risk	● Low	● Low

## Legend

- Low risk: low probability of occurrence, low impact
- Moderate risk: moderate probability of occurrence, moderate impact
- High risk: moderate probability of occurrence, moderate to strong impact
- Catastrophic risk: high probability of occurrence, severe impact

TAB. 7: SUMMARY OF KEY LONG-TERM RISKS AT MORPHOSYS

Segment	Risk	Order of Importance
Proprietary Development	Lack of competitiveness of the MorphoSys pipeline	1
Partnered Discovery	Delay or termination of partnered programs	2
Proprietary Development	Lack of funding for the MorphoSys pipeline	3
Proprietary Development	Insufficient expansion of the MorphoSys pipeline	4
Proprietary Development	Inability to build a sales structure	5

## Legend

Declining importance of risk from 1 to 5, whereby 1 represents the most important risk.

# Statement on Corporate Governance and Corporate Governance Report

The Statement on Corporate Governance and the Corporate Governance Report are available on the Company's website under Media and Investors – Corporate Governance.

## Statement on Corporate Governance Under Sec. 289a (HGB) for the 2016 Financial Year

In the Statement on Corporate Governance under Sec. 289a HGB, the Management Board and the Supervisory Board report on corporate governance. In addition to the annual Declaration of Conformity in accordance with Sec. 161 of the Stock Corporation Act (AktG), the Statement on Corporate Governance also includes relevant information on corporate governance practices and other aspects of corporate governance, including a description of the working practices of the Management Board and Supervisory Board.

### **DECLARATION OF CONFORMITY WITH THE GERMAN CORPORATE GOVERNANCE CODE (THE "CODE") OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD OF MORPHOSYS AG**

The Management Board and Supervisory Board of MorphoSys AG declare the following under Sec. 161 of the German Stock Corporation Act:

1. Since the last Declaration of Conformity on December 3, 2015, MorphoSys AG has complied with the recommendations of the "Government Commission on the German Corporate Governance Code" in the version from May 5, 2015 with the following exception:  
There is no cap on the overall or individual variable remuneration components of Management Board members' remuneration (see Item 4.2.3 Para. 2 sentence 6 of the Code). Based on the Supervisory Board's existing limitations for the Management Board's variable remuneration components and their annual allocation, the Supervisory Board does not believe that an additional cap is required.
2. MorphoSys will continue to comply with the recommendations of the "Government Commission on the German Corporate Governance Code" in the version dated May 5, 2015 with the exceptions described under Item 1.

Planegg, December 2, 2016

MorphoSys AG

On behalf of the Management Board:

Dr. Simon Moroney  
Chief Executive Officer

On behalf of the Supervisory Board:

Dr. Gerald Möller  
Chairman of the Supervisory Board

## RELEVANT INFORMATION ON CORPORATE GOVERNANCE PRACTICES

MorphoSys ensures compliance with laws and rules of conduct through the Company-wide application of the following documents: the Code of Conduct, the Compliance Management Handbook and supplementary internal guidelines.

MorphoSys's Code of Conduct sets out the fundamental principles and key policies and practices for business behavior. The Code is a valuable tool for employees and executives, particularly in business, legal and ethical situations of conflict. It reinforces the principles of transparent and sound management and fosters trust in the Company from the financial markets, business partners, employees and the public. Compliance with the Code of Conduct is carefully monitored. The Company-wide application of the Code is overseen by the Compliance Committee, and the Code itself is routinely reviewed and updated when necessary. The Code of Conduct can be downloaded from the Company's website under Media and Investors – Corporate Governance.

The Compliance Handbook describes MorphoSys's Compliance Management System (CMS) and is intended to ensure compliance with all legal regulations as well as set out high ethical standards that apply to both the management and all employees. The Management Board has overall responsibility for the compliance management system and is required to report regularly to the Audit Committee and the Supervisory Board. In carrying out its compliance responsibility, the Management Board has assigned the relevant tasks to various offices at MorphoSys.

The Compliance Officer arranges the exchange of information between the internal compliance-relevant posts. The Compliance Officer monitors the Company's existing CMS and implements the CMS through appropriate measures and decisions taken on an individual basis. The Compliance Officer is the employee contact person for all compliance-related issues and implements the compliance requirements defined by the Compliance Committee.

The Compliance Officer is supported by a Compliance Committee that meets at regular intervals. The Compliance Committee supports the Compliance Officer in the implementation and monitoring of the CMS. The Compliance Committee is particularly responsible for the identification and discussion of all compliance-relevant issues and thus makes it possible for the Compliance Officer as well as the other members of the Compliance Committee to periodically verify MorphoSys's compliance status and, if necessary, update the CMS.

More information on MorphoSys's Compliance Management System can be found in the Corporate Governance Report.

## COMPOSITION OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD

### MANAGEMENT BOARD

The Management Board of the Company consists of a Chief Executive Officer and three other members. A schedule of responsibilities defines the different areas of responsibility as follows:












- Dr. Simon Moroney, Chief Executive Officer, responsible for Strategy and Planning; Compliance & Quality Assurance; Internal Audit; Human Resources; Business Development & Portfolio Management; Legal; the coordination of individual areas of the Management Board; representation of the Management Board to the Supervisory Board.


- Jens Holstein, Chief Financial Officer, responsible for Accounting and Taxes; Controlling; Corporate Finance & Corporate Development; Risk Management; IT; Technical Operations; Procurement & Logistics; Corporate Communications & Investor Relations; Environmental Social Governance (ESG).
- Dr. Marlies Sproll, Chief Scientific Officer responsible for Development Partnerships & Technology Development; Target Molecule & Antibody Research; Protein Chemistry; Alliance Management; Intellectual Property.
- Dr. Arndt Schottelius, Chief Development Officer (up to February 28, 2017), responsible for Preclinical Development; Clinical Research; Clinical Operations; Drug Safety & Pharmacovigilance; Regulatory Affairs; Project Management.
- Dr. Malte Peters, Chief Development Officer (since March, 1, 2017), responsible for Preclinical Research; Clinical Development; Clinical Operations; Drug Safety & Pharmacovigilance; Regulatory Affairs; Project Management.

#### SUPERVISORY BOARD

As of December 31, 2016, the MorphoSys AG Supervisory Board consisted of six members who oversee and advise the Management Board. The current Supervisory Board consists of professionally qualified members who represent MorphoSys AG shareholders. Dr. Gerald Möller, acting Chairman of the Supervisory Board, coordinates the Board's activities, chairs the Supervisory Board meetings and represents the interests of the Supervisory Board externally. All Supervisory Board members are independent, as defined in the German Corporate Governance Code, and have many years of experience in the biotechnology and pharmaceutical industries. The members were duly elected by the shareholders during the 2015 Annual General Meeting. The Chairperson of the Supervisory Board is not a former member of MorphoSys AG's Management Board. The members of the Supervisory Board and its committees are listed in the table below.

**TAB. 8: COMPOSITION OF THE SUPERVISORY BOARD**

	Position	Initial Appointment	End of Term	Audit Committee	Remuneration and Nomination Committee	Science and Technology Committee
Dr. Gerald Möller	Chairman	1999	2018			
Dr. Frank Morich	Deputy Chairman	2015	2017			
Karin Eastham 	Member	2012	2018			
Klaus Kühn 	Member	2015	2017			
Dr. Marc Cluzel	Member	2012	2018			
Wendy Johnson	Member	2015	2017			

 Independent financial expert

 Chairperson

 Member

## WORKING PRACTICES OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD

To ensure good corporate governance, a guiding principle of the cooperation between the Management Board and Supervisory Board at MorphoSys AG is the open, comprehensive and regular communication of information. The dual board system prescribed by the German Stock Corporation Act clearly differentiates between a company's management and supervision. The responsibility of both boards is clearly stipulated by the legislator and the boards' bylaws and Articles of Association. The boards work closely together to make decisions and take actions for the Company's benefit. Their stated objective is to sustainably increase the Company's value.

Management Board members have their own area of responsibility defined in the schedule of responsibilities and regularly report to their Management Board colleagues. Cooperation among Management Board members is governed by the bylaws. The Supervisory Board ratifies both the schedule of responsibilities and the bylaws. Management Board meetings are typically held weekly and chaired by the Chief Executive Officer. During these meetings, resolutions are passed concerning dealings and transactions that, under the bylaws, require the approval of the entire Management Board. At least half of the Management Board's members must be present to pass a resolution. Management Board resolutions are passed by a simple majority and, in the event of a tied vote, the Chief Executive Officer's vote decides. For material events, each Management Board or Supervisory Board member can call an extraordinary meeting of the entire Management Board. Management Board resolutions can also be passed outside of meetings by an agreement made orally, by telephone or in writing (also by email). A written protocol is completed for each meeting of the full Management Board and is submitted for approval to the full Management Board and for signature to the Chief Executive Officer at the following meeting.

Management Board strategy workshops are also held, in which the Company-wide strategic objectives are developed and prioritized.

The Management Board promptly and comprehensively informs the Supervisory Board in writing and at Supervisory Board meetings about planning, business development, the Company's position, risk management and other compliance issues. Extraordinary meetings of the Supervisory Board are also called for material events. The Management Board involves the Supervisory Board in the strategy, planning and all fundamental Company issues. In addition to routine Supervisory Board meetings, a strategy meeting takes place between the Management Board and Supervisory Board once annually to discuss MorphoSys's strategic direction. The Management Board's bylaws specify that material business transactions require the approval of the Supervisory Board. Detailed information on the cooperation of the Management Board and Supervisory Board and important items of discussion during the 2016 financial year can be found in the Report of the Supervisory Board.

The Supervisory Board holds a minimum of two meetings per calendar half-year and at least six meetings per full calendar year. The Supervisory Board has supplemented the Articles of Association with rules of procedure that apply to its duties. In accordance with these rules, the Chairperson of the Supervisory Board coordinates the activities of the Supervisory Board, chairs the Supervisory Board meetings and represents the interests of the Supervisory Board externally. The Supervisory Board typically passes its resolutions in meetings but resolutions may also be passed outside of meetings in writing (also by email), by telephone or video conference.

The Supervisory Board has a quorum when at least two-thirds of its members (including either the Chairperson or Deputy Chairperson of the Supervisory Board) take part in the vote. Resolutions of the Supervisory Board are generally passed with a simple majority unless the law prescribes otherwise. In the event of a tied vote, the Chairperson of the Supervisory Board's vote decides.

Protocols are completed for Supervisory Board meetings and resolutions passed outside of meetings. A copy of the Supervisory Board's protocol is made available to all Supervisory Board members. The Supervisory Board conducts an efficiency evaluation regularly in accordance with the recommendation in Item 5.6 of the Code.

#### COMPOSITION AND WORKING PRACTICES OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD COMMITTEES

The Management Board has not formed any committees.

The Supervisory Board has three committees: the Audit Committee, the Remuneration and Nomination Committee and the Science and Technology Committee. The members of the three committees formed by the Supervisory Board are professionally qualified.

**TAB. 9: PARTICIPATION OF SUPERVISORY BOARD MEMBERS  
SUPERVISORY BOARD MEETINGS**

Name	by phone		by phone				by phone		by phone	
	01/15/ 2016	02/24/ 2016	03/16/ 2016	06/01/ 2016	07/21/ 2016	10/12/ 2016	10/13/ 2016	11/08/ 2016	11/15/ 2016	12/08/ 2016
Dr. Gerald Möller	X	X	X	X	X	X	X	X	X	X
Dr. Marc Cluzel	X	X	X	X	X	X	X	X	X	X
Karin Eastham	X	X	X	X	by phone	-	-	X	X	-
Wendy Johnson	X	X	X	X	by phone	X	X	X	X	X
Klaus Kühn	X	X	X	X	X	X	X	X	X	X
Dr. Frank Morich	X	X	X	X	X	X	X	X	X	X

#### MEETINGS OF THE AUDIT COMMITTEE

Name	by phone		by phone		by phone	
	02/24/ 2016	03/16/ 2016	04/29/ 2016	07/21/ 2016	11/03/ 2016	12/07/ 2016
Karin Eastham	X	X	X	by phone	-	-
Wendy Johnson	X	X	X	-	X	X
Klaus Kühn	X	X	X	X	X	X



**MEETINGS OF THE REMUNERATION AND NOMINATION COMMITTEE**

Name	by phone		by phone		by phone		by phone		by phone		by phone		by phone	
	01/15/2016	02/23/2016	03/16/2016	04/01/2016	04/13/2016	05/20/2016	06/01/2016	06/29/2016	07/19/2016	08/22/2016	08/31/2016	09/08/2016	10/12/2016	12/08/2016
Dr. Gerald Möller	X	X	X	X	X	X	X	X	X	X	X	X	X	X
Dr. Marc Cluzel	X	X	X	X	X	X	X	X	X	X	X	X	X	X
Karin Eastham	X	X	X	X	X	X	X	X	X	X	X	X	-	-

**MEETINGS OF THE SCIENCE AND TECHNOLOGY COMMITTEE**

Name			by phone		by phone		by phone	
	02/24/2016	06/01/2016	06/30/2016	07/21/2016	10/05/2016	10/12/2016	11/07/2016	12/08/2016
Dr. Marc Cluzel	X	X	X	X	X	X	X	X
Wendy Johnson	X	X	X	-	X	X	X	X
Frank Morich	X	X	X	X	X	X	X	X

**AUDIT COMMITTEE**

The main task of the Audit Committee is to support the Supervisory Board in fulfilling its supervisory duties with respect to the accuracy of the annual and consolidated financial statements, the activities of the auditor and internal control functions, such as risk management, compliance and internal auditing. The Audit Committee submits a recommendation to the Supervisory Board for the election at the Annual General Meeting of an independent auditor. The members of the Audit Committee are Klaus Kühn (Chairperson), Karin Eastham and Wendy Johnson. Klaus Kühn and Karin Eastham fulfill the prerequisite of being independent financial experts.

**REMUNERATION AND NOMINATION COMMITTEE**

The Remuneration and Nomination Committee is responsible for preparing and reviewing the Management Board's compensation system annually before its final approval. When necessary, the Committee searches for suitable candidates to appoint to the Management Board and Supervisory Board and submits appointment proposals to the Supervisory Board. The Committee also prepares the contracts made with Management Board members. The members of the Remuneration and Nomination Committee are Ms. Karin Eastham (Chairperson), Dr. Gerald Möller and Dr. Marc Cluzel.

**SCIENCE AND TECHNOLOGY COMMITTEE**

The Science and Technology Committee advises the Supervisory Board on matters concerning proprietary drug and technology development and prepares the relevant Supervisory Board resolutions. The members of the Science and Technology Committee are Dr. Marc Cluzel (Chairperson), Dr. Frank Morich and Ms. Wendy Johnson.

The Supervisory Board members' biographies can be found on the MorphoSys website under Company - Management - Supervisory Board.

## Corporate Governance Report

At MorphoSys, responsible, sustainable and value-oriented corporate governance is a high priority. Good corporate governance is an essential aspect of MorphoSys's corporate management and forms the framework for the Company's management and supervision, which includes the Group's organization, commercial principles and tools for its guidance and control.

The German Corporate Governance Code ("the Code") provides a standard for the transparent monitoring and management of companies that strongly emphasizes shareholder interests. Many of the corporate governance principles contained in the Code have been practiced at MorphoSys for many years. Corporate governance issues at MorphoSys AG are detailed in the Statement on Corporate Governance under Sec. 289a HGB. The statement also contains the annual Declaration of Conformity, relevant information on corporate governance practices and a description of the Management Board and Supervisory Board's working practices. Additional information can be found in this Corporate Governance Report.

### COMMUNICATION WITH THE CAPITAL MARKETS

At MorphoSys, a key principle of corporate communication is to simultaneously and fully inform institutional investors, private shareholders, financial analysts, employees and all other stakeholders of the Company's situation through regular, transparent and timely communication. Shareholders have immediate access to the information provided to financial analysts and similar recipients and can obtain this information in both German and English. The Company is firmly committed to following a fair information policy.

Regular meetings with analysts and investors in the context of road shows and individual meetings play a central role in investor relations at MorphoSys. Conference calls accompany publications of quarterly results and give analysts and investors an immediate opportunity to ask questions about the Company's development. Company presentations for on-site events, visual and audio recordings of other important events as well as conference call transcripts are also available on the Company's website to all interested parties.

The Company's website [www.morphosys.com](http://www.morphosys.com) serves as a central platform for current information on the Company and its development. Financial reports, analyst meetings and conference presentations, as well as press releases and ad hoc statements, are also available. The important regularly scheduled publications and events (annual reports, interim reports, annual general meetings and press and analyst conferences) are published in the Company's financial calendar well in advance.

### ESTABLISHMENT OF SPECIFIC TARGETS FOR THE COMPOSITION OF THE SUPERVISORY BOARD

MorphoSys AG's Supervisory Board has a total of six members. The Supervisory Board believes a ratio of at least two non-German members, or at least two members having extensive international experience, provides a fair share of diversity given the Company's international orientation. The Supervisory Board currently meets this ratio.

The Supervisory Board also strives to have at least four independent members. The Supervisory Board currently meets this ratio. Material and lasting conflicts of interest should be avoided, particularly those arising from activities for major competitors. No such conflict of interest currently exists.

It is also intended to maintain the current number of women on the Supervisory Board. The Supervisory Board has two female members and the Company intends to maintain this ratio in the future.

The age limit of 75 years contained in the Supervisory Board's bylaws is currently respected, but the Supervisory Board may make an exception to this provision in specific cases.

At the Annual General Meeting, the Supervisory Board intends to propose an initial two-year period of office for Supervisory Board members. The Supervisory Board intends to allow reappointment only once for an additional term of three years but reserves the right to make exceptions in specific cases and permit members to be reappointed for a third or potentially fourth term of three years each.

The Supervisory Board intends to respect the targets described in future election proposals.

#### **WOMEN'S QUOTA FOR THE SUPERVISORY BOARD, MANAGEMENT BOARD AND THE TWO MANAGEMENT LEVELS BELOW THE MANAGEMENT BOARD**

In July 2015, the Supervisory Board established a women's quota for the Supervisory Board and Management Board, which continues to apply:

"MorphoSys AG's Supervisory Board has a total of six members. Two of those members are women, which places the current ratio of female members on the Company's Supervisory Board above 30%, at 33.33%. The Supervisory Board intends to maintain this ratio in the future."

The Company continues to meet this target ratio.

In July 2015, the Supervisory Board established a women's quota for the Management Board, which continues to apply:

"The Management Board of MorphoSys AG has a total of four members, one of whom is a woman, placing the current ratio of female members on the Company's Management Board below 30% at 25%. The Supervisory Board intends to maintain this ratio in the future."

The Company continues to meet this target ratio.

In July 2015, the Management Board established a women's quota for first management level below the Management Board, which continues to apply:

"At the time of the decision, the first management level below the Management Board (the Senior Management Group) consisted of 20 members, seven of whom were women, placing the level of female representation at this management level above 30%, at 35%. The Management Board intends to continue to maintain a minimum ratio of 30%."

The Company continues to meet this target ratio.

In July 2015, the Management Board established a women's quota for the second management level below the Management Board, which continues to apply:

“At the time of the decision, the second management level below the Management Board (executives outside of the Senior Management Group) consisted of 48 members, 19 of whom were women, placing the level of female representation at this management level above 30%, at 39.59%. The Management Board intends to continue to maintain a minimum ratio of 30%.”

The Company continues to meet this targeted ratio.

## REMUNERATION REPORT

The Remuneration Report presents the principles, structure and amount of Management Board and Supervisory Board remuneration. The report complies with the legal provisions and gives consideration to the Code's recommendations.

### MANAGEMENT BOARD REMUNERATION

The Management Board's remuneration system is intended to provide an incentive for performance-oriented and sustainable corporate management. Therefore, the aggregate remuneration of the Management Board members consists of different components: fixed components, an annual cash bonus based on the achievement of corporate targets (short-term incentive - STI), a variable compensation component with a long-term incentive (long-term incentive - LTI) and other remuneration components. Variable remuneration components with long-term incentive consist of performance share plans from the current and prior years as well as a convertible bond program from the year 2013. Management Board members also receive fringe benefits in the form of non-cash benefits, mainly the use of a company car and the payment of insurance premiums. All remuneration packages are reviewed annually for their scope and appropriateness by the Remuneration and Nomination Committee and compared to the results of an annual Management Board remuneration analysis. The amount of compensation paid to Management Board members highly depends on their individual areas of responsibility, their personal achievement of goals, the Company's economic situation and success and the Company's business prospects versus its competition. All decisions concerning adjustments to remuneration packages are made by the entire Supervisory Board. The Management Board's remuneration and index-linked pension scheme were last adjusted in July 2016.

### OVERVIEW

In the 2016 financial year, total benefits of € 4,383,658 (2015: € 4,521,009) were granted to the Management Board in accordance with the provisions of the German Corporate Governance Code.

Of the total remuneration for the year 2016, € 2,596,366 was cash compensation and € 1,787,292, or 41%, resulted from personnel expenses for share-based compensation (performance share plan and convertible bond plan) (remuneration with long-term incentive - LTI).

The total amount of benefits paid to the Management Board in the 2016 financial year amounted to € 5,070,618 (2015: € 9,508,884). In addition to cash compensation payments of € 2,672,333 (2015: € 2,869,901), this amount includes mainly the relevant value of the transfer of treasury stock from a performance-based share plan (share-based compensation) amounting to € 2,398,285 (2015: €

4,622,005) under German tax law. Since there were no convertible bonds exercised in 2016, the total amount for 2016 does not include proceeds from the exercise of convertible bonds (2015: € 2,016,978).

As of April 1, 2016, a total of 57,967 of the Management Board's shares of treasury stock from the 2012 performance-based share plan were vested because the vesting period for this LTI program had expired. The beneficiaries had the option to receive the shares within a six-month period ending on October 4, 2016. All transactions in MorphoSys shares executed by members of the Management Board were reported as required by law and published in the Corporate Governance Report as well as on the Company's website.

In accordance with the requirements of Sec. 4.2.5 Para. 3 of the Code, the following table provides detailed mandatory information on the remuneration of the individual Management Board members.

Please note that the following tables are provided in the context of the German Corporate Governance Report and differ from the information on Management Board remuneration presented in the Notes of this Annual Report. These differences are due to the varying presentation requirements under the Corporate Governance Code and IFRS (International Financial Reporting Standards), the EU-wide accounting standard since 2005.

**TAB. 10: COMPENSATION OF THE MANAGEMENT BOARD IN 2016 AND 2015 (DISCLOSURE IN ACCORDANCE WITH THE GERMAN CORPORATE GOVERNANCE CODE)**

**BENEFITS GRANTED TO THE MANAGEMENT BOARD**

in €	Dr. Simon Moroney Chief Executive Officer				Jens Holstein Chief Financial Officer			
	2015	2016	2016	2016	2015	2016	2016	2016
			(Minimum)	(Maximum)			(Minimum)	(Maximum)
Fixed Compensation	445,736	463,457	463,457	463,457	302,384	314,405	314,405	314,405
Fringe Benefits	36,887	34,270	34,270	34,270	39,735	46,300	46,300	46,300
<b>Total Fixed Compensation</b>	<b>482,623</b>	<b>497,727</b>	<b>497,727</b>	<b>497,727</b>	<b>342,119</b>	<b>360,705</b>	<b>360,705</b>	<b>360,705</b>
One -Year Variable Compensation <sup>1</sup>	238,692	210,873	0	405,525	161,926	143,054	0	275,105
Multi-Year Variable Compensation:								
2013 Convertible Bonds Program <sup>2</sup> (Vesting Period 4 Years)	164,969	33,964	33,964	33,964	168,984	34,791	34,791	34,791
2015 Long-Term Incentive Program <sup>3</sup> (Vesting Period 4 Years)	441,159	0	0	0	302,149	0	0	0
2016 Long-Term Incentive Program <sup>3</sup> (Vesting Period 4 Years)	0	563,820	0	2,255,280	0	369,397	0	1,477,588
<b>Total Variable Compensation</b>	<b>844,820</b>	<b>808,657</b>	<b>33,964</b>	<b>2,694,769</b>	<b>633,059</b>	<b>547,242</b>	<b>34,791</b>	<b>1,787,484</b>
Service Cost	138,280	142,096	142,096	142,096	90,800	92,875	92,875	92,875
<b>Total Compensation</b>	<b>1,465,723</b>	<b>1,448,480</b>	<b>673,787</b>	<b>3,334,592</b>	<b>1,065,978</b>	<b>1,000,822</b>	<b>488,371</b>	<b>2,241,064</b>

<sup>1</sup> The one-year compensation granted for the 2016 financial year represents the bonus accrual for 2016 that will be paid in February 2017. The bonus granted for the 2015 financial year was paid in February 2016.

<sup>2</sup> Stock-based compensation plans not issued on an annual basis. The fair value was determined pursuant to the regulations of IFRS 2 "Share-based Payment." For plans that are not issued annually, the pro rata share of personnel expenses resulting from share-based payments is presented for each financial year.

<sup>3</sup> Stock-based compensation plans issued annually. The fair value was determined pursuant to the regulations of IFRS 2 "Share-based Payment." For plans issued annually, the personnel expenses resulting from share-based payments are presented for the entire term at the time of issue.

Dr. Arndt Schottelius Chief Development Officer				Dr. Marlies Sproll Chief Scientific Officer				Total			
2015	2016	2016 (Minimum)	2016 (Maximum)	2015	2016	2016 (Minimum)	2016 (Maximum)	2015	2016	2016 (Minimum)	2016 (Maximum)
302,384	309,759	309,759	309,759	302,384	314,405	314,405	314,405	1,352,888	1,402,026	1,402,026	1,402,026
29,889	28,388	28,388	28,388	22,954	24,141	24,141	24,141	129,465	133,099	133,099	133,099
<b>332,273</b>	<b>338,147</b>	<b>338,147</b>	<b>338,147</b>	<b>325,338</b>	<b>338,546</b>	<b>338,546</b>	<b>338,546</b>	<b>1,482,353</b>	<b>1,535,125</b>	<b>1,535,125</b>	<b>1,535,125</b>
156,635	140,940	0	271,039	156,635	143,054	0	275,105	713,888	637,921	0	1,226,774
112,990	23,263	23,263	23,263	112,990	23,263	23,263	23,263	559,933	115,281	115,281	115,281
302,149	0	0	0	302,149	0	0	0	1,347,606	0	0	0
0	369,397	0	1,477,588	0	369,397	0	1,477,588	0	1,672,011	0	6,688,044
<b>571,774</b>	<b>533,600</b>	<b>23,263</b>	<b>1,771,890</b>	<b>571,774</b>	<b>535,714</b>	<b>23,263</b>	<b>1,775,956</b>	<b>2,621,427</b>	<b>2,425,213</b>	<b>115,281</b>	<b>8,030,099</b>
94,064	95,473	95,473	95,473	94,085	92,876	92,876	92,876	417,229	423,320	423,320	423,320
<b>998,111</b>	<b>967,220</b>	<b>456,883</b>	<b>2,205,510</b>	<b>991,197</b>	<b>967,136</b>	<b>454,685</b>	<b>2,207,378</b>	<b>4,521,009</b>	<b>4,383,658</b>	<b>2,073,726</b>	<b>9,988,544</b>

**PAYMENTS DURING THE FINANCIAL YEAR:**

in €	Dr. Simon Moroney Chief Executive Officer		Jens Holstein Chief Financial Officer	
	2015	2016	2015	2016
	Fixed Compensation	445,736	463,457	302,384
Fringe Benefits	36,887	34,270	39,735	46,300
<b>Total Fixed Compensation</b>	<b>482,623</b>	<b>497,727</b>	<b>342,119</b>	<b>360,705</b>
One -Year Variable Compensation <sup>1</sup>	324,696	238,692	220,271	161,926
Multi-Year Variable Compensation:				
2010 Convertible Bonds Program <sup>2</sup> (Vesting Period 4 Years)	737,148	0	0	0
2011 Long-Term Incentive Program <sup>2</sup> (Vesting Period 4 Years)	1,513,045	0	1,036,320	0
2012 Long-Term Incentive Program <sup>2</sup> (Vesting Period 4 Years)	0	794,430	0	574,467
Other <sup>3</sup>	0	0	0	0
<b>Total Variable Compensation</b>	<b>2,574,889</b>	<b>1,033,122</b>	<b>1,256,591</b>	<b>736,393</b>
Service Cost	138,280	142,096	90,800	92,875
<b>Total Compensation</b>	<b>3,195,792</b>	<b>1,672,945</b>	<b>1,689,510</b>	<b>1,189,973</b>

<sup>1</sup> The one-year variable compensation presented here represents the bonus paid in the respective financial year for the previous financial year.

<sup>2</sup> The date and value of the payments is the date and value applicable under German tax law. Therefore, this table shows the non-cash benefits arising in the respective financial year from the difference between the exercise or conversion price and the stock market price at the time of exercising the convertible bonds or at the time of transfer of own shares from a performance share plan.

<sup>3</sup> No compensation recovery claims against the Management Board existed in 2016 or 2015.



Dr. Arndt Schottelius Chief Development Officer		Dr. Marlies Sproll Chief Scientific Officer		Total	
2015	2016	2015	2016	2015	2016
302,384	309,759	302,384	314,405	1,352,888	1,402,026
29,889	28,388	22,954	24,141	129,465	133,099
<b>332,273</b>	<b>338,147</b>	<b>325,338</b>	<b>338,546</b>	<b>1,482,353</b>	<b>1,535,125</b>
215,208	156,635	210,144	156,635	970,319	713,888
0	0	1,279,830	0	2,016,978	0
1,036,320	0	1,036,320	0	4,622,005	0
0	489,233	0	540,155	0	2,398,285
0	0	0	0	0	0
<b>1,251,528</b>	<b>645,868</b>	<b>2,526,294</b>	<b>696,790</b>	<b>7,609,302</b>	<b>3,112,173</b>
94,064	95,473	94,085	92,876	417,229	423,320
<b>1,677,865</b>	<b>1,079,488</b>	<b>2,945,717</b>	<b>1,128,212</b>	<b>9,508,884</b>	<b>5,070,618</b>

#### FIXED REMUNERATION AND FRINGE BENEFITS

The non-performance-related remuneration of the Management Board consists of fixed remuneration and additional benefits, which primarily include the use of company cars, as well as subsidies for health, welfare and disability insurance. The Chief Financial Officer, Mr. Jens Holstein, receives an additional expense allowance for maintaining two households.

#### PENSION EXPENSES

The Company also provides payments to Management Board members equal to a maximum of 10% of the member's fixed annual salary plus any payable taxes. This compensation is intended for the members' individual retirement plans. Additionally, all Management Board members participate in a pension plan in the form of a provident fund, which was introduced in cooperation with Allianz Pensions-Management e.V. The pension obligations of the provident fund will be met by Allianz Pensions-Management e.V. These pension obligations are not pension benefit plans.

#### PERFORMANCE-BASED COMPENSATION (SHORT-TERM INCENTIVE - STI)

Members of the Management Board each receive performance-based compensation in the form of an annual bonus payment of up to 70% of the gross base salary when 100% of the member's targets have been achieved. These bonus payments are dependent on the achievement of corporate targets specified by the Supervisory Board at the start of each financial year. They are based on the Company's performance measured by revenue, operating result, the progress of the partnered pipeline and the Company's proprietary pipeline. At the start of the year, the Supervisory Board assesses the degree to which corporate goals were achieved in the prior year and uses this information to determine the bonus. The bonus may not exceed 125% of the target amount (corresponding to 87.5% of the gross base salary).

Performance-based compensation can be omitted if goals are not achieved. The bonus for the 2016 financial year will be paid in February 2017.

#### **LONG-TERM INCENTIVE COMPENSATION (LONG-TERM INCENTIVE - LTI)**

In 2011, MorphoSys introduced a new, long-term incentive compensation plan (Performance Share Plan) for the Management Board and members of the Senior Management Group. The LTI program is based on the allocation of shares linked to the achievement of predefined performance targets over a four-year period.

Each year, the Supervisory Board determines the number of shares to be allocated to the Management Board. On April 1, 2016, the Management Board was granted 35,681 shares. Each Management Board member received an entitlement benefit for a specific number of shares. For more information, please refer to the Notes of the Separate Financial Statements and the explanation on share buybacks in the Corporate Governance Report.

The Supervisory Board sets the long-term performance targets along with the allocation of shares for a given year. The target for the 2016 LTI program was the performance of the MorphoSys share compared to a benchmark index consisting equally of the NASDAQ Biotechnology Index and the German TecDAX Index. LTI program participants are awarded shares annually based on the daily relative performance of the MorphoSys share versus the benchmark index. There is a hurdle of 50% and a cap of 200% for the price performance in any given year. For example, if the relative performance of the MorphoSys shares versus the benchmark index is less than 50%, participants will not receive any entitlement benefits for the relevant year. Participants also do not receive entitlement benefits for additional shares when the share price performance exceeds 200%.

The ultimate number of performance shares allocated to the LTI program participants is determined at the completion of the program, namely after four years. This calculation incorporates the number of shares initially allocated after adjusting for the share price development of the MorphoSys share versus the benchmark index and a “company factor” that is determined at the Supervisory Board’s discretion. This company factor is a number between zero and two that is set by the Supervisory Board based on the Company’s situation. The company factor’s predefined default value is one.

#### **MISCELLANEOUS**

Management Board members were not granted any loans or similar benefits in the reporting year nor have they received any benefits from third parties that were promised or granted based on their position as a member of the Management Board.

#### **TERMINATION OF MANAGEMENT BOARD EMPLOYMENT CONTRACTS/CHANGE OF CONTROL**

If a Management Board member’s employment contract terminates due to member’s death, the member’s spouse or life partner is entitled to the fixed monthly salary for the month of death and the 12 months thereafter. In the event of a change of control, Management Board members are entitled to exercise their extraordinary right to terminate their employment contracts and receive any outstanding fixed salary for the remainder of the agreed contract period. Moreover, in such a case, all convertible bonds and performance shares granted will become vested immediately and can be exercised after the expiration of the statutory vesting period. A change of control has occurred when (i) MorphoSys transfers assets or a substantial portion of its assets to unaffiliated third parties, (ii) MorphoSys merges with an unaffiliated company or (iii) a shareholder or third party holds 30% or more of MorphoSys’s voting rights.

### SUPERVISORY BOARD REMUNERATION

The remuneration of Supervisory Board members is governed by the Company's Articles of Association and a corresponding Annual General Meeting resolution on Supervisory Board remuneration. In the 2016 financial year, Supervisory Board members received fixed compensation, attendance fees and expense allowances for their participation in Supervisory Board and committee meetings. Each Supervisory Board member has received annual fixed compensation (€ 85,400 for Chairpersons, € 51,240 for Deputy Chairpersons and € 34,160 for all other members) for their membership of the Supervisory Board. The Chairperson receives € 4,000 for each Supervisory Board meeting chaired and the other members receive € 2,000 for each Supervisory Board meeting attended. For committee work, the committee Chairperson receives € 12,000 and other committee members each receive € 6,000. Committee members also receive € 1,200 for their participation in a committee meeting. Participation in a Supervisory Board or committee meeting by telephone or video conference results in a 50% reduction in compensation for meeting participation. In certain cases, a fixed expense allowance is granted for travel time for meetings personally attended. Therefore, Supervisory Board members residing outside of Europe who personally take part in a Supervisory Board or committee meeting are entitled to a fixed expense allowance of € 2,000 (plus any sales tax due) for additional travel time in addition to attendance fees and reimbursed expenses.

Supervisory Board members are also reimbursed for travel expenses and value-added taxes (VAT) on their compensation.

In the 2016 financial year, Supervisory Board members received a total of € 529,680 (2015: € 529,270) excluding the reimbursement of travel expenses. This amount consists of fixed compensation and attendance fees for participating in Supervisory Board and committee meetings.

No loans were granted to Supervisory Board members by the Company.

The table below details the Supervisory Board's remuneration.

**TAB. 11: COMPENSATION OF THE SUPERVISORY BOARD IN 2016 AND 2015**

in €	Fixed Compensation		Attendance Fees <sup>1</sup>		Total Compensation	
	2016	2015	2016	2015	2016	2015
Dr. Gerald Möller	91,400	93,521	43,400	36,200	134,800	129,721
Dr. Frank Morich <sup>2</sup>	57,240	37,324	26,800	14,200	84,040	51,524
Dr. Marc Cluzel	52,160	50,089	34,600	28,000	86,760	78,089
Karin Eastham	52,160	50,089	24,400	36,800	76,560	86,889
Wendy Johnson <sup>2</sup>	46,160	30,099	33,800	26,400	79,960	56,499
Klaus Kühn <sup>2</sup>	46,160	30,099	21,400	14,200	67,560	44,299
Dr. Walter Blättler <sup>3</sup>	-	16,188	-	13,000	-	29,188
Dr. Daniel Camus <sup>3</sup>	-	16,188	-	8,400	-	24,588
Dr. Geoffrey Vernon <sup>3</sup>	-	20,073	-	8,400	-	28,473
<b>Total</b>	<b>345,280</b>	<b>343,670</b>	<b>184,400</b>	<b>185,600</b>	<b>529,680</b>	<b>529,270</b>

<sup>1</sup> The attendance fee contains expense allowances for the attendance on Supervisory Board and committee meetings.

<sup>2</sup> Dr. Frank Morich, Wendy Johnson and Klaus Kühn joined the Supervisory Board of MorphoSys AG on May 8, 2015.

<sup>3</sup> Dr. Walter Blättler, Dr. Daniel Camus and Dr. Geoffrey Vernon left the Supervisory Board of MorphoSys AG on May 8, 2015.

## HOLDINGS OF MANAGEMENT BOARD AND SUPERVISORY BOARD MEMBERS

The members of the Management Board and the Supervisory Board hold more than 1% of the shares issued by the Company. All shares, performance shares and convertible bonds held by each member of the Management Board and the Supervisory Board are listed below.

**TAB. 12: DIRECTORS' HOLDINGS**

Shares	01/01/2016	Additions	Sales	12/31/2016
<b>Management Board</b>				
Dr. Simon Moroney	495,238	18,976	0	514,214
Jens Holstein	4,000	12,997	9,997	7,000
Dr. Arndt Schottelius	2,000	13,397	5,000	10,397
Dr. Marlies Sproll	50,752	12,997	6,237	57,512
<b>Total</b>	<b>551,990</b>	<b>58,367</b>	<b>21,234</b>	<b>589,123</b>
<b>Supervisory Board</b>				
Dr. Gerald Möller	11,000	0	0	11,000
Dr. Frank Morich	1,000	0	0	1,000
Dr. Marc Cluzel	500	0	0	500
Karin Eastham	2,000	0	0	2,000
Wendy Johnson	500	0	0	500
Klaus Kühn	0	0	0	0
<b>Total</b>	<b>15,000</b>	<b>0</b>	<b>0</b>	<b>15,000</b>

Convertible Bonds	01/01/2016	Additions	Forfeitures	Exercises	12/31/2016
<b>Management Board</b>					
Dr. Simon Moroney	88,386	0	0	0	88,386
Jens Holstein	90,537	0	0	0	90,537
Dr. Arndt Schottelius	60,537	0	0	0	60,537
Dr. Marlies Sproll	60,537	0	0	0	60,537
<b>Total</b>	<b>299,997</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>299,997</b>

<b>Performance Shares</b>	<b>01/01/2016</b>	<b>Additions</b>	<b>Forfeitures</b>	<b>Allocations</b>	<b>12/31/2016</b>
<b>Management Board</b>					
Dr. Simon Moroney	44,164	12,032	0	18,976	37,220
Jens Holstein	30,248	7,883	0	12,997	25,134
Dr. Arndt Schottelius	30,248	7,883	0	12,997	25,134
Dr. Marlies Sproll	30,248	7,883	0	12,997	25,134
<b>Total</b>	<b>134,908</b>	<b>35,681</b>	<b>0</b>	<b>57,967</b>	<b>112,622</b>

#### **DIRECTORS' DEALINGS**

In accordance with the relevant legal provisions (Sec. 15a of the German Securities Trading Act (WpHG) until July 2, 2016 and Article 19 Para. 1 (a) of the Market Abuse Regulation (MAR) from July 3, 2016) the members of MorphoSys AG's Management Board and Supervisory Board and persons related to such members are required to disclose any trading in MorphoSys shares.

During the reporting year, MorphoSys received the following notifications under Sec. 15a WpHG and Article 19 Para. 1 (a) MAR listed in the table below.

TAB. 13: DIRECTORS' DEALINGS 2016

Party Subject to the Notification Requirement	Function	Date of Transaction in 2016	Type of Transaction	Number of Stocks/ Derivatives	Average Share Price	Transaction Volume
Dr. Arndt Schottelius	CDO	11/18/2016	Sale of MorphoSys AG shares; the shares sold derive from the Long-Term Incentive (LTI) Program 2012 of MorphoSys and have been granted after a four-year waiting period on 10/01/2016	1,500	€ 45.935	€ 68,902.175
Dr. Arndt Schottelius	CDO	11/17/2016	Sale of MorphoSys AG shares; the shares sold derive from the Long-Term Incentive (LTI) Program 2012 of MorphoSys and have been granted after a four-year waiting period on 10/01/2016	3,500	€ 44.617	€ 156,160.300
Jens Holstein	CFO	06/07/2016	Sale of MorphoSys AG shares; the shares sold derive from the Long-Term Incentive (LTI) Program 2012 of MorphoSys and have been granted after a four-year waiting period on 04/01/2016	9,997	€ 47.017	€ 470,028.949
Dr. Marlies Sproll	CSO	05/13/2016	Sale of MorphoSys AG shares; the shares sold derive from the Long-Term Incentive (LTI) Program 2012 of MorphoSys and have been granted after a four-year waiting period on 04/01/2016	3,100	€ 45.1284	€ 139,898.040
Dr. Marlies Sproll	CSO	05/12/2016	Sale of MorphoSys AG shares; the shares sold derive from the Long-Term Incentive (LTI) Program 2012 of MorphoSys and have been granted after a four-year waiting period on 04/01/2016	3,137	€ 43.8891	€ 137,680.107
Dr. Arndt Schottelius	CDO	01/12/2016	Purchase of MorphoSys AG shares	400	€ 48.55	€ 19,420,00

## AVOIDING CONFLICTS OF INTEREST

Management Board and Supervisory Board members are required to refrain from any actions that could lead to a conflict of interest with their duties at MorphoSys AG. Such transactions or the secondary employment of Management Board members must be disclosed immediately to the Supervisory Board and are subject to the Board's approval. The Supervisory Board, in turn, must inform the Annual General Meeting of any conflicts of interest and their handling. In the 2016 financial year, a potential conflict of interest arose regarding a possible transaction. As a precautionary measure, the affected Supervisory Board member did not take part in the corresponding meeting of the Supervisory Board. The transaction in question was not consummated.

## STOCK REPURCHASES

By resolution of the Annual General Meeting on May 23, 2014, MorphoSys is authorized in accordance with Sec. 71 Para. 1 no. 8 AktG to repurchase its own shares in an amount of up to 10% of the existing common stock. This authorization can be exercised in whole or in part, once or several times by the Company or a third party on the Company's behalf for the purposes specified in the authorizing resolution. It is at the Management Board's discretion to decide whether to carry out a repurchase on a stock exchange, via a public offer or through a public invitation to submit a bid.

In March 2016, MorphoSys repurchased a total of 52,295 of its own shares based on the authorization from the year 2014. The Company plans to use these shares for a long-term incentive program for the Management Board and Senior Management Group. The authorization also permits the shares to be used for other lawful purposes.

## INFORMATION TECHNOLOGY

The main topics for the Information Technology department in the 2016 financial year included IT security and compliance and the design and construction of a new, future-oriented IT infrastructure for the move to the Company's new premises.

In designing the new IT infrastructure, emphasis was placed on achieving less complexity, more flexibility and a high level of security. Our new data centers are protected by state-of-the-art building technology and fire extinguishing systems.

The planning and construction of the new building's network and media technology infrastructure is based on the latest standards combining both safety and user-friendliness.

An internal CERT (Computer Emergency Response Team) has been established and is trained regularly in areas such as IT forensics and hacking methods to deal appropriately with any threats. Security-related system messages or user notifications are analyzed in detail. In a few cases, additional external IT security experts were used for a detailed analysis, whereby no serious security incidents occurred.

As part of the Company's IT Security Awareness Campaign (ISAC) established in the prior year, additional campaigns were conducted in the reporting year to raise employees' awareness with respect to their shared responsibility and essential contribution to the Company's IT security.

**INFORMATION ON THE INTERNAL CONTROL AND RISK MANAGEMENT SYSTEM WITH REGARD TO THE ACCOUNTING PROCESS UNDER SEC. 289 PARA. 5 AND SEC. 315 PARA. 2 NO. 5 HGB**

In the 2016 financial year, MorphoSys completed a routine update of the documentation for its existing internal control and risk management system. This update serves to maintain adequate internal control over financial reporting and to ensure the availability of all controls so that financial figures can be reported as precisely and accurately as possible. The COSO (Committee of Sponsoring Organizations of the Treadway Commission) defines the corresponding COSO framework ("Internal Control - Integrated Framework"). This is the framework used by MorphoSys and is the most commonly used for the internal control of financial reporting.

System constraints make it impossible to give absolute assurance that internal controls will always prevent or completely detect all misrepresentations made in the context of financial reporting. Internal controls can only provide reasonable assurance that financial reporting is reliable and verify that the financial statements were prepared in accordance with the IFRS standards adopted by the European Union for external purposes.

The separate financial statements are subjected to numerous preparation, review and control processes so that the statements can be reported promptly to the market and shareholders. To accomplish this, the Company's executives have a coordinated plan for which all internal and external resources are made available. MorphoSys also uses a strict four-eyes principle to ensure the accuracy of the key financial ratios reported and the underlying execution of all accounting processes. Numerous rules and guidelines are also followed to ensure the strict separation of the planning, posting and execution of financial transactions. This functional separation of processes is ensured by all of the Company's operating IT systems through the appropriate assignment of rights. External service providers routinely review the implementation of and compliance with these guidelines as well as the efficiency of the accounting processes. The reporting year's most recent review showed insignificant cause for action. The appropriate corrective actions are being planned, and their implementation will be reviewed again in the following year.

Predicting future events is not the job of MorphoSys's internal control and risk management system. The Company's risk management system does, however, guarantee that business risks are detected and assessed early. The risks identified are eliminated or at least brought to an acceptable level using appropriate corrective measures. Special attention is given to risks that could jeopardize the Company.

The Management Board ensures that risks are always dealt with responsibly and keeps the Supervisory Board informed of any risks and their development. Detailed information on the risks and opportunities encountered by MorphoSys can be found in the "Risk and Opportunity Report."



## ACCOUNTING AND EXTERNAL AUDIT

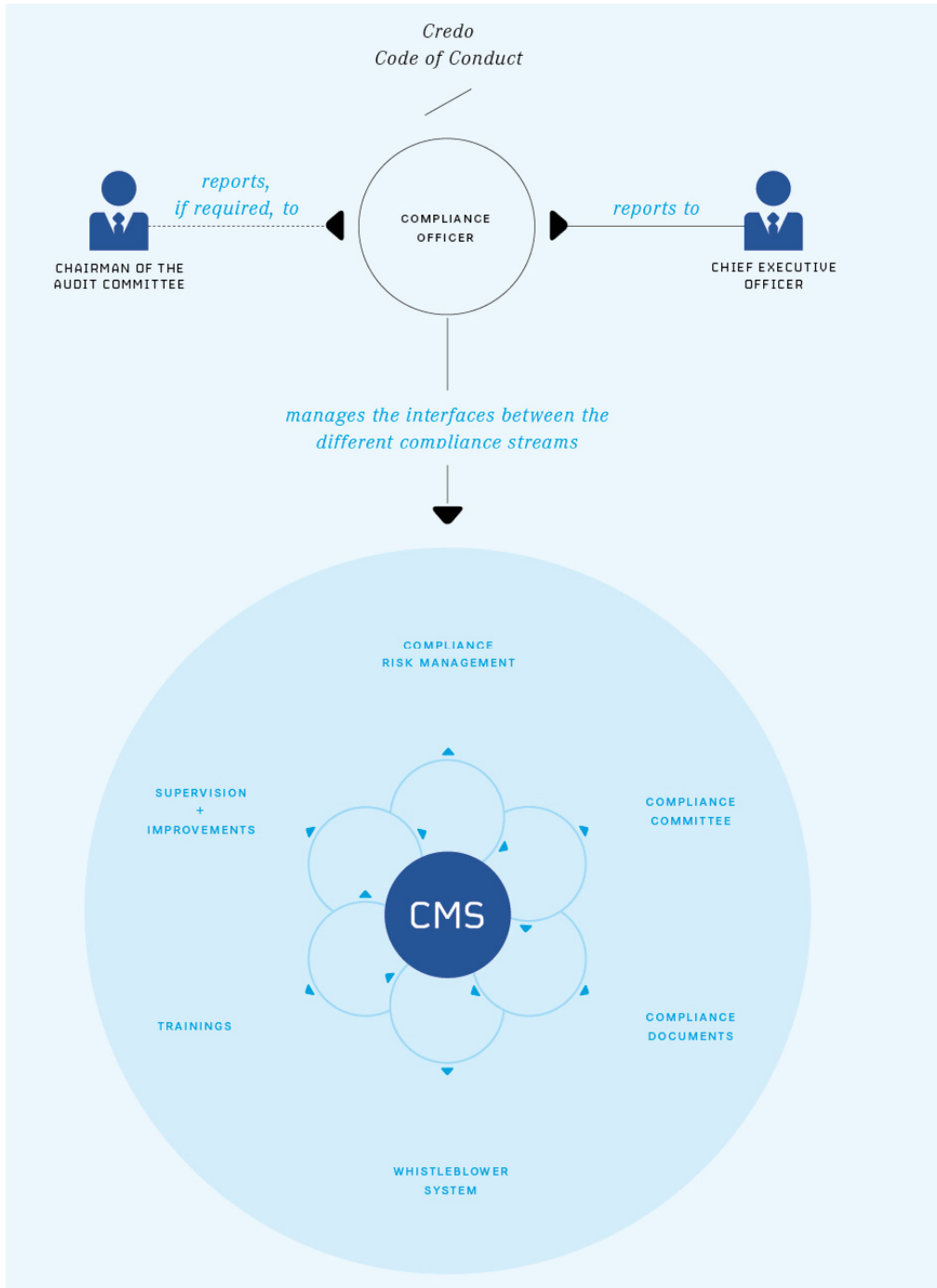
MorphoSys AG prepares its financial statements in accordance with the provisions of the German Commercial Code (HGB) and the Stock Corporation Act (AktG). The consolidated financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS), as applicable in the European Union.

For the election of the Company auditor, the Audit Committee of the Supervisory Board submits a nomination proposal to the Supervisory Board. At the 2016 Annual General Meeting, PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft was appointed auditor for the 2016 financial year. As proof of its independence, the auditor submitted a Declaration of Independence to the Supervisory Board. The lead auditor of these separate financial statements was Mr. Dietmar Eglauer, who has audited the separate financial statements since 2014. PricewaterhouseCoopers GmbH has been the auditor for MorphoSys AG since the 2011 financial year. Information on other consulting, audit and valuation services provided by PricewaterhouseCoopers GmbH to MorphoSys AG during the 2016 financial year can be found in the Notes.

## COMPLIANCE MANAGEMENT SYSTEM

The basic mechanisms of the compliance management system at MorphoSys are presented in the section “Relevant Information on Corporate Governance Practices”. In addition to this information, the responsibilities within the compliance organization are shown in Figure 8.

FIG. 8: COMPLIANCE MANAGEMENT SYSTEM (CMS)



#### **INTERNAL AUDIT DEPARTMENT**

As an element of corporate governance, the Internal Audit Department plays a key role in the Company's compliance management system. The department's main duty is to provide MorphoSys AG with a systematic and uniform approach for evaluating and improving the effectiveness of risk management and supporting the management and monitoring activities when meeting set targets. The accounting and consulting firm KPMG was reappointed by the Internal Audit Department in 2016 to perform the audit as a co-sourcing partner.

Internal auditing is based on a risk-oriented internal audit plan that is largely based on the results of the most recent risk surveys. The Management Board and Supervisory Board Committee's audit requirements and recommendations are included in the audit plan.

The Internal Audit Department reports regularly to the Management Board. The head of Internal Audit and the Chief Executive Officer both report to the Supervisory Board's Audit Committee twice annually or on an ad hoc basis when necessary.

Four audits were conducted successfully in the course of 2016. Some areas requiring action were identified and corrections were initiated or performed. Appropriate corrective action was initiated during the reporting year for any complaints. The Internal Audit Department is planning four audits in 2017.

### **Disclosures Under Sec. 289 Para 4, Sec. 315 Para. 4 HGB and Explanatory Report of the Management Board Under Sec. 176 Para. 1 Sentence 1 AktG**

#### **COMPOSITION OF COMMON STOCK**

As of December 31, 2016, the Company's statutory common stock amounted to € 29,159,770.00 and was divided into 29,159,770 no-par-value bearer shares. Excluding the 396,010 treasury shares held by the Company, the statutory common stock concerns bearer shares with voting rights granting each share one vote at the Annual General Meeting.

#### **RESTRICTIONS AFFECTING VOTING RIGHTS OR THE TRANSFER OF SHARES**

The Management Board is not aware of any restrictions that may affect voting rights, the transfer of shares or those that may emerge from agreements between shareholders.

Voting right restrictions may also arise from the provisions of the German Stock Corporation Act (AktG), such as those under Sec. 136 AktG, or the provisions for treasury stock under Sec. 71b AktG.

#### **SHAREHOLDINGS IN COMMON STOCK EXCEEDING 10% OF VOTING RIGHTS**

We have not been notified of or are aware of any direct or indirect interests in the Company's common stock that exceed 10% of the voting rights.

## **SHARES WITH SPECIAL RIGHTS CONFERRING POWERS OF CONTROL**

Shares with special rights conferring powers of control do not exist.

## **CONTROL OVER VOTING RIGHTS WITH REGARD TO EMPLOYEE OWNERSHIP OF CAPITAL**

Employees who hold shares in the Company exercise their voting rights directly in accordance with the statutory provisions and the Articles of Association as do other shareholders.

## **APPOINTMENT AND DISMISSAL OF MANAGEMENT BOARD MEMBERS AND AMENDMENTS TO THE ARTICLES OF ASSOCIATION**

The number of Management Board members, their appointment and dismissal and the nomination of the Chief Executive Officer are determined by the Supervisory Board in accordance with Sec. 6 of the Articles of Association and Sec. 84 AktG. The Company's Management Board currently consists of the Chief Executive Officer and three other members. Management Board members may be appointed for a maximum term of five years. Reappointments or extensions in the term of office are allowed for a maximum term of five years in each case. The Supervisory Board may revoke the appointment of a Management Board member or the nomination of a Chief Executive Officer for good cause within the meaning of Sec. 84 Para. 3 AktG. If a required member of the Management Board is absent, one will be appointed by the court in cases of urgency under Sec. 85 AktG.

As a rule, the Articles of Association can only be amended by a resolution of the Annual General Meeting in accordance with Sec. 179 Para. 1 sentence 1 AktG. Under Sec. 179 Para. 2 sentence 2 AktG in conjunction with Sec. 20 of the Articles of Association, the MorphoSys AG Annual General Meeting resolves amendments to the Articles of Association generally through a simple majority of the votes cast and a simple majority of the common stock represented. If the law stipulates a higher mandatory majority of votes or capital, this shall be applied. Amendments to the Articles of Association that only affect their wording can be resolved by the Supervisory Board in accordance with Sec. 179 Para. 1 sentence 2 AktG in conjunction with Sec. 12 Para. 3 of the Articles of Association.

## **POWER OF THE MANAGEMENT BOARD TO ISSUE SHARES**

The Management Board's power to issue shares is granted under Sec. 5 Para. 5 through Para. 6e of the Company's Articles of Association as of November 16, 2016 and the following statutory provisions:

1. Authorized Capital
  - a. According to Sec. 5 Para. 5 of the Articles of Association, with the Supervisory Board's consent, the Management Board is authorized to increase the Company's common stock on one or more occasions by up to € 10,584,333.00 for cash contributions and/or contributions in kind by issuing up to 10,584,333 new, no-par-value bearer shares until and including the date of April 30, 2020 (Authorized Capital 2015-I).
  - b. Shareholders are principally entitled to subscription rights in the case of a capital increase. One or more credit institutions may also subscribe to the shares with the obligation to offer the shares to shareholders for subscription. With the Supervisory Board's consent, the Management Board is, however, authorized to exclude shareholder subscription rights:

- aa) in the case of a capital increase for cash contribution, to the extent necessary to avoid fractional shares; or
- bb) in the case of a capital increase for contribution in kind; or
- cc) in the case of a capital increase for cash contribution when the new shares are placed on a domestic and/or foreign stock exchange in the context of a public offering.

The total shares to be issued via a capital increase against contribution in cash and/or in kind, excluding pre-emptive rights and based on the authorizations mentioned above, shall not exceed 20% of the common stock. The calculation used is based on either the effective date of the authorizations or the exercise of the authorizations, whichever amount is lower. The 20% limit mentioned above shall take into account (i) treasury shares sold excluding pre-emptive rights after the effective date of these authorizations (unless they service the entitlements of members of the Management Board and/or employees under employee participation programs), (ii) shares that are issued from other authorized capital existing on the effective date of these authorizations and excluding pre-emptive rights during the effective period of these authorizations, and (iii) shares to be issued during the effective period of these authorizations to service convertible bonds and/or bonds with warrants whose basis for authorization exists on the effective date of these authorizations provided that the convertible bonds and/or bonds with warrants have been issued with the exclusion of the pre-emptive rights of shareholders (unless they service the entitlements of members of the Management Board and/or employees under employee participation programs).

With the Supervisory Board's consent, the Management Board is authorized to determine the further details of the capital increase and its implementation.

The previous Authorized Capital 2014-I under Sec. 5 Para. 6 of the Articles of Association was fully used and, therefore, canceled in the context of the capital increase carried out in November 2016.

## 2. Conditional Capital

- a. According to Sec. 5 Para. 6b of the Articles of Association, the Company's common stock is conditionally increased by up to € 5,307,536.00, divided into a maximum of 5,307,536 no-par-value bearer shares (Conditional Capital 2016-I). The conditional capital increase serves solely as a means to grant new shares to the holders of conversion or warrant rights, which will be issued by the company or companies in which the Company has a direct or indirect majority interest according to the authorizing resolution of the Annual General Meeting on June 2, 2016 under Agenda Item 7 letter a). The shares will be issued at the respective conversion or exercise price to be determined in accordance with the resolution above. The conditional capital increase will only be carried out to the extent that the holders of conversion or warrant rights exercise these rights or fulfill conversion obligations under such bonds. The shares will be entitled to dividends as of the beginning of the previous financial year, provided they were issued before the start of the Company's Annual General Meeting, or as of the beginning of the financial year in which they were issued.

- b. The previous Conditional Capital 2003-II under Sec. 5 Para. 6c of the Articles of Association was canceled by a resolution of the Annual General Meeting on June 2, 2016.
- c. According to Sec. 5 Para. 6e of the Articles of Association, the Company's common stock is conditionally increased by up to € 450,000.00 through the issue of up to 450,000 new no-par-value bearer shares of the Company (Conditional Capital 2008-III). The conditional capital increase will only be executed to the extent that holders of the convertible bonds exercise their conversion rights for conversion into ordinary shares of the Company. The new shares participate in the Company's profits from the beginning of the financial year, for which there has been no resolution on the appropriation of accumulated income at the time of issuance. With the Supervisory Board's consent, the Management Board is authorized to determine the further details of the capital increase and its implementation.
- d. According to Sec. 5 Para. 6f of the Articles of Association, the Company's common stock is conditionally increased by up to € 995,162.00 through the issue of up to 995,162 new no-par-value bearer shares of the Company (Conditional Capital 2016-III). The conditional capital serves to meet the obligations of subscription rights that have been issued and exercised based on the authorization resolved by the Annual General Meeting of June 2, 2016 under Agenda Item 9 letter a). The conditional capital increase will only be executed to the extent that holders of subscription rights exercise their right to subscribe to shares of the Company. The shares will be issued at the exercise price set in each case as the issue amount in accordance with Agenda Item 9 letter a) subparagraph (8) of the Annual General Meeting's resolution dated June 2, 2016; Sec. 9 Para.1 AktG remains unaffected. The new shares are entitled to dividends for the first time for the financial year for which there has been no resolution by the Annual General Meeting on the appropriation of accumulated income. The Management Board, and the Company's Supervisory Board where members of the Management Board are concerned, is authorized to determine the additional details of the conditional capital increase and its execution.

#### **POWER OF MANAGEMENT BOARD TO REPURCHASE SHARES**

The Management Board's power to repurchase the Company's own shares is granted in Sec. 71 AktG and by the authorization of the Annual General Meeting of May 23, 2014:

Until and including the date of April 30, 2019, the Company is authorized to repurchase its own shares in an amount of up to 10% of the common stock existing at the time of the resolution (or possibly a lower amount of common stock at the time of exercising this authorization) for any purpose permitted under the statutory limits. The repurchase takes place at the Management Board's discretion on either the stock exchange, through a public offer or public invitation to submit a bid. The authorization may not be used for the purpose of trading in the Company's own shares. The intended use of treasury stock acquired under this authorization may be found under Agenda Item 9 of the Annual General Meeting of May 23, 2014. These shares may be used as follows:

- a. The shares may be redeemed without the redemption or its execution requiring a further resolution of the Annual General Meeting.
- b. The shares may be sold other than on the stock exchange or shareholder offer if the shares are sold for cash at a price that is not significantly below the market price of the Company's shares of the same class at the time of the sale.

- c. The shares may be sold for contribution in kind, particularly in conjunction with company mergers, acquisitions of companies, parts of companies or interests in companies.
- d. The shares may be used to fulfill subscription or conversion rights resulting from the exercise of options and/or conversion rights or conversion obligations for Company shares.
- e. The shares may be offered or transferred to employees of the Company and those of affiliated companies, members of the Company's management and those of affiliated companies and/or used to meet commitments or obligations to purchase Company shares that were or will be granted to employees of the Company or those of affiliated companies, members of the Company's management or managers of affiliated companies. The shares may also be used to fulfill obligations or rights to purchase Company shares that will be agreed with the Company's employees, members of the senior management and affiliates in the context of employee participation programs.

If shares are used for the purposes mentioned above, shareholder subscription rights are excluded, with the exception of share redemptions.

#### **MATERIAL AGREEMENTS MADE BY THE COMPANY THAT FALL UNDER THE CONDITION OF A CHANGE OF CONTROL AFTER A TAKEOVER BID**

In 2012, MorphoSys and Novartis Pharma AG extended their original cooperation agreement. Under this agreement, in specific cases of a change of control, Novartis Pharma AG is entitled but not obliged to take various measures that include the partial or complete termination of the collaboration agreement.

Under Sec. 29 and 30 of the German Securities Acquisition and Takeover Act (WpÜG), a change of control applies when 30% or more of the Company's voting rights are acquired.

#### **COMPENSATION AGREEMENTS CONCLUDED BY THE COMPANY WITH MANAGEMENT BOARD MEMBERS AND EMPLOYEES IN THE EVENT OF A TAKEOVER BID**

Following a change of control, Management Board members may terminate their employment contract and demand the fixed salary still outstanding until the end of the contract period. Moreover, in such a case, all stock options, convertible bonds and performance shares granted will become vested immediately and can be exercised after the expiration of the statutory vesting or blackout periods.

Following a change of control, Senior Management Group members may also terminate their employment contract and demand a severance payment equal to one annual gross fixed salary. Moreover, in such a case, all stock options, convertible bonds and performance shares granted will become vested immediately and can be exercised after the expiration of the statutory vesting or blackout periods.

The following cases constitute a change of control:

- (i) MorphoSys transfers all or a material portion of the Company's assets to an unaffiliated entity, (ii) MorphoSys merges with an unaffiliated entity or (iii) a shareholder or third party directly or indirectly holds 30% or more of MorphoSys's voting rights.

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# Separate Financial Statements of MorphoSys AG as of December 31, 2016 (German GAAP)

MorphoSys AG, Planegg



## Balance Sheet as of December 31, 2016

ASSETS		12/31/2016 in €	12/31/2016 in €	12/31/2015 in €
<b>A.</b>	<b>FIXED ASSETS</b>			
<b>I.</b>	<b>Intangible Assets</b>			
	Paid concessions, commercial property rights and similar rights and assets and licenses to such rights and assets	26,540,211	26,540,211	37,929,381
<b>II.</b>	<b>Tangible Assets</b>			
1.	Land, leasehold rights and buildings, including leasehold improvements	428,112		46,350
2.	Other equipment, furniture and fixtures	3,598,516		3,248,346
			<b>4,026,628</b>	<b>3,294,696</b>
<b>III.</b>	<b>Financial Assets</b>			
	Shares in affiliated companies	39,624,278		32,124,278
			<b>39,624,278</b>	<b>32,124,278</b>
<b>B.</b>	<b>CURRENT ASSETS</b>			
<b>I.</b>	<b>Inventories</b>			
	Raw materials, supplies and production materials	176,844		235,260
			<b>176,844</b>	<b>235,260</b>
<b>II.</b>	<b>Receivables and Other Assets</b>			
1.	Trade accounts receivable (thereof due within one year EUR 12,301,741, prior year: EUR 11,242,070)	12,301,741		11,242,070
2.	Receivables due from affiliated companies (thereof due within one year EUR 517,797, prior year: EUR 3,035,693)	517,797		3,035,693
3.	Other assets (thereof due after one year EUR 79,521,181 prior year: EUR 15,510,989)	223,662,335		113,516,472
			<b>236,481,873</b>	<b>127,794,235</b>
<b>III.</b>	<b>Securities</b>			
	Other securities	69,890,401		97,208,159
			<b>69,890,401</b>	<b>97,208,159</b>
<b>IV.</b>	<b>Cash on Hand and Cash at Banks</b>	<b>62,305,600</b>	<b>62,305,600</b>	<b>79,508,835</b>
<b>C.</b>	<b>PREPAID EXPENSES</b>	<b>6,299,580</b>	<b>6,299,580</b>	<b>1,460,780</b>
			<b>445,345,415</b>	<b>379,555,624</b>

LIABILITIES AND SHAREHOLDERS EQUITY	12/31/2016 in €	12/31/2016 in €	12/31/2015 in €
<b>A. EQUITY</b>			
<b>I. Common Stock</b> (Nominal Value of the Conditional Capital as of December 31, 2016: € 6,752,698; December 31, 2015: € 7,086,000)	29.159.770		26.537.682
Treasury Stock	-396.010		-434.670
		<b>28.763.760</b>	<b>26.103.012</b>
<b>II. Additional Paid-in Capital</b>	407.977.621	407.977.621	295.227.837
<b>III. Earnings Reserves</b>			
Other earnings reserves	12.667.285	12.667.285	13.268.841
<b>IV. Accumulated Income / (Deficit)</b>	<b>-45.353.159</b>	<b>-45.353.159</b>	<b>14.857.060</b>
		<b>404.055.507</b>	<b>349.456.750</b>
<b>B. PROVISIONS</b>			
1. Tax provisions	1.498.309		1.498.309
2. Other provisions	29.658.016		25.701.347
		<b>31.156.325</b>	<b>27.199.656</b>
<b>C. LIABILITIES</b>			
1. Bonds (thereof convertible EUR 218,293, prior year: EUR 225,000)	218.293		225.000
2. Trade Accounts Payable	8.358.489		264.126
3. Liabilities due to Affiliated Companies	134.257		134.355
4. Other liabilities (thereof due within one year EUR 781,266, prior year: EUR 1,626,011) (thereof for taxes EUR 614,929, prior year: EUR 1,625,866)	781.266		1.626.011
		<b>9.492.305</b>	<b>2.249.492</b>
<b>D. DEFERRED REVENUE</b>	<b>641.278</b>	<b>641.278</b>	<b>649.726</b>
		<b>445.345.415</b>	<b>379.555.624</b>

## Statement of income from January 1 through December 31, 2016

	2016 in €	2015 in €
<b>1. Sales</b>	<b>48,714,087</b>	<b>102,675,416</b>
2. Cost of sales	(94,760,075)	(82,655,116)
<b>3. Gross profit on sales</b>	<b>(46,045,988)</b>	<b>20,020,300</b>
4. Selling expenses	(2,504,568)	(2,129,827)
5. General administration expenses	(18,582,320)	(17,473,337)
6. Other operating income	6,646,051	16,779,449
thereof gain on exchange	192,391	154,794
7. Other operating expenses	(455,261)	(1,018,987)
thereof loss on exchange	(359,321)	(460,065)
8. Income from investments	0	16,498
thereof from affiliated companies	0	16,498
Income from other securities and loans presented under financial assets	293,553	92,115
10. Other interest and similar income	1,231,980	1,726,092
thereof interest income from the deduction of accrued interest of non-current provisions	68,762	77,817
11. Impairment of financial assets and of current securities	0	(41,906)
thereof from affiliated companies	0	(41,906)
12. Losses from other securities and loans presented under financial assets	(891,956)	(427,158)
13. Other Interest and similar expenses	(39,821)	(35,309)
thereof interest expense from the addition of accrued interest of non-current provisions	(38,829)	(35,309)
<b>14. Income tax</b>	<b>158,250</b>	<b>(3,841,345)</b>
15. Result after taxation	(60,190,080)	13,666,585
<b>16. Other taxes</b>	<b>(20,139)</b>	<b>(20,732)</b>
17. Net profit / (Net loss)	(60,210,219)	13,645,853
<b>18. Profit carried forward</b>	<b>14,857,060</b>	<b>12,299,301</b>
19. Withdrawal from Other Earnings Reserves	2,127,668	5,301,314
20. Settlement with the difference from purchase of Treasury Stock	(2,127,668)	(5,301,314)
21. Settlement with the difference from transfer of Treasury Stock	1,526,112	2,087,564
22. Allocation to Other Earnings Reserves	(1,526,112)	(13,175,658)
<b>23. Accumulated Income / (Deficit)</b>	<b>(45,353,159)</b>	<b>14,857,060</b>

# Notes to the Financial Statements

## General Information

These annual financial statements were prepared in accordance with Sec. 242 et seq. and Sec. 264 et seq. of the German Commercial Code (HGB), the corresponding provisions of the German Stock Corporation Act (AktG) and the Company's Articles of Association. The shares of MorphoSys AG (the "Company") are listed for trading in the Regulated Market (Prime Standard segment) of the Frankfurt Stock Exchange.

These annual financial statements were prepared in accordance with the regulations for large corporations. The statement of income has been structured in accordance with the cost of sales method for the purposes of comparison with the consolidated financial statements prepared pursuant to IFRS. The financial year corresponds to the calendar year.

The Company's registered office is located at Semmelweisstraße 7, 82152 Planegg, Germany. The MorphoSys AG consolidated and separate financial statements can be viewed at this address. The Company is recorded in the Commercial Register B of the District Court of Munich, Germany, under the number HRB 121023.

## Accounting and Valuation Principles

These annual financial statements were prepared on the basis of the following accounting and valuation principles.

In July 2015, the German Commercial Code was amended by the introduction of the Accounting Directives Implementation Act (Bilanzrichtlinie-Umsetzungsgesetz [BilRUG]). The Company adopted the provisions of the BilRUG in its 2016 financial statements and applied the transitional provisions under Article 75 EGHGB.

When intangible assets acquired are subject to depletion, they are amortized using the straight-line method over the course of their expected useful lives. Research and development programs under development are recognized at acquisition cost and are only subject to amortization when their usefulness has been demonstrated in studies on the efficacy of the respective antibody program. These assets are reviewed for impairment at the balance sheet date and are carried at the lower of their carrying amount or fair value.

Tangible assets are carried at acquisition cost and depreciated on a straight-line basis over their expected useful lives. Low-value assets up to a value of € 410 are fully depreciated in the year they are acquired.

Financial assets are recognized at the lower of their acquisition cost or fair value.

Pursuant to Sec. 256 HGB, inventories are measured according to the FIFO method. Inventories are not subject to third-party rights, except for the customary retention of title.

Receivables and other assets are recognized at nominal value. Risks are taken into account by means of write-downs or impairment. The realization principle is applied to non-current receivables.

The measurement of forward rate agreements qualifying as derivative financial instruments is based on the change in forward exchange curves. Recognition and measurement follow the imparity principle. Valuation units were not formed in the past financial year.

Other securities are recognized at the lower of acquisition cost or fair value in accordance with Sec. 253 Para. 4 HGB.

Cash and cash equivalents are carried at their nominal value as of the balance sheet date.

Prepayments are recognized as prepaid expenses on the balance sheet date insofar as they represent expenses for a certain period subsequent to the balance sheet date.

Capital subscribed is carried at nominal value. The nominal value of the shares repurchased is offset against the capital subscribed in accordance with Sec. 272 Para. 1a HGB, while the remaining amount of the total purchase price is offset against the other earnings reserves within equity.

Provisions cover all identifiable risks and uncertain obligations and are recognized at the settlement amount required according to prudent business judgment.

Liabilities are measured at the settlement amount. The imparity principle is applied to non-current liabilities.

Provisions have been recognized on a pro rata basis for personnel expenses resulting from long-term incentive plans introduced in 2013, 2014, 2015 and 2016 because the repurchase of treasury shares for servicing the long-term incentive plan constitutes a financial burden on the Company.

The recognition of revenue for income from collaboration and research agreements is carried on the basis of the contractual terms and takes into account the realization principle of Sec. 252 Para. 1 no. 4 HGB and the accrual-based method of Sec. 250 Para. 2 HGB based on the contract period. Upfront payments made at the time of the conclusion of a contract that grants access to MorphoSys technology (e.g., HuCAL or Ylanthia) are spread over the term during which the rights of use are granted. License fees are recognized over the contract period. Revenue from milestone payments is recognized upon the achievement of certain criteria. Service fees pertaining to research and development collaborations are recognized in the period the services were rendered.

Any total tax charge that results from a difference between the carrying amounts of assets, liabilities, accruals and deferrals prescribed by commercial law and these items' tax carrying amounts that are likely to diminish in subsequent financial years, is recognized as a deferred tax liability in the balance sheet in accordance with Sec. 274 HGB. Any total tax relief that results is not recognized as deferred tax assets in the balance sheet pursuant to the option granted in Sec. 274 Para. 1 sent. 2 HGB. The amount of the resulting tax charge and relief is measured at the Company-specific tax rates, applicable at the time the differences are reversed, and are not discounted. The line items reported are reversed as soon as the tax charge or benefit occurs or is no longer expected. The income or expense from changes in deferred tax assets or liabilities is recorded separately in the statement of income under the line item "income tax."

All amounts in this report are rounded to the nearest euro, thousand euros or million euros.

#### FOREIGN CURRENCY TRANSLATION

Current receivables and liabilities denominated in foreign currencies are translated on the basis of the mean spot exchange rate prevailing on the day of the transaction or the balance sheet date pursuant to Sec. 256a HGB. The Company did not recognize any non-current receivables or liabilities denominated in foreign currencies.

## Notes to the Balance Sheet

#### INTANGIBLE ASSETS

Paid concessions, commercial property rights and similar rights and assets, as well as licenses to such rights and assets, amounted to € 26,540k as of December 31, 2016 (December 31, 2015: € 37,929k). This sum included research and development programs under development in the amount of € 22,608k (December 31, 2015: € 32,749k). The research and development programs under development were examined for impairment as of the reporting date. The carrying amount of research and development programs under development decreased by € 10,141k as a result of a partial impairment on the MOR209/ES414 compound. No further need for impairment has been identified. In the 2016 and 2015, there were no impairment losses recognized on licenses for concessions, commercial property rights and similar rights and assets.

Asset Class	Useful Life	Amortization Rates
Paid concessions, commercial property rights and similar rights and assets and licenses to such rights and assets	8 (10) years	13 % (10) %
In-process R&D Programs	not yet subject for amortization	-
Software	3 (5) years	33 % (20) %

The development of intangible assets and the respective amortization in the financial year are presented in the statement of fixed assets.

#### FIXED ASSETS

The development of the individual line items under fixed assets and the respective depreciation in the financial year are presented in the statement of fixed assets.



Asset Class	Useful Life	Depreciation Rates
Computer Hardware	3 years	33%
Low-Value Laboratory and Office Equipment below € 410	Immediately	100%
Leasehold Improvements to Property/Buildings	10 years	10%
Office Equipment	8 years	13%
Laboratory Equipment	4 years	25%

## FINANCIAL ASSETS

As of December 31, 2016, the Company recorded interests in affiliated companies of € 39,624k (December 31, 2015: € 32,124k). This amount included the shares in Lanthio Pharma B.V. of € 33,575k (December 31, 2015: € 26,075k) and Sloning BioTechnology GmbH of € 6,049k (December 31, 2015: € 6,049k).

The increase in the carrying amount of the share in Lanthio Pharma B.V. by € 7.5 million resulted from a contribution to Lanthio Pharma B.V.'s capital reserves paid by MorphoSys AG on December 22, 2016.

The shares in affiliated companies are listed in the following overview.

	Currency	Stake in %	Equity in domestic currency	Profit / Loss for the Year in domestic currency
<b>Foreign</b>				
Lanthio Pharma B.V., Groningen, The Netherlands	€	100.00	8,548,655 <sup>2</sup>	376,836
LanthioPep B.V., Groningen, The Netherlands <sup>1</sup>	€	100.00	- <sup>2</sup>	(2,705,688)
<b>Domestic</b>				
Sloning BioTechnology GmbH, Planegg, Germany	€	100.00	4,979,833	3,442,811

<sup>1</sup> Indirect subsidiary via Lanthio Pharma B.V.

<sup>2</sup> Disclosure of equity of the Lanthio Group

## INVENTORIES

As of the balance sheet date, inventories amounted to € 177k (December 31, 2015: € 235k) and consisted exclusively of raw materials, supplies, and production materials.

## TRADE ACCOUNTS RECEIVABLE

As of December 31, 2016, MorphoSys AG recorded trade accounts receivable of € 12,302k (December 31, 2015: € 11,242k). All trade accounts receivable are due within one year. Based on the Management Board's assessment, valuation allowances were not made in the 2016 and 2015 financial years.

## RECEIVABLES DUE FROM AFFILIATED COMPANIES

As of December 31, 2016, receivables due from affiliated companies amounted to € 518k (December 31, 2015: € 3,036k) and included exclusively trade accounts receivable (December 31, 2015: € 36k).

During the reporting year, there were receivables due from Sloning BioTechnology GmbH in the amount of € 1k. As of December 31, 2015, a receivable of € 3,000k due from Sloning BioTechnology GmbH had been recorded because of a reduction in the capital reserves as a receivable due from affiliated companies.

## OTHER ASSETS

Other assets totaled € 223,662k as of December 31, 2016 (December 31, 2015: € 113,516k).

As of December 31, 2016, the Company held financial assets of € 211,630k. These were recorded under other assets and comprised various fixed deposits (December 31, 2015: € 109,870k). Interest income from these financial assets was recognized in the statement of income under the line item other interest and similar income. The risk associated with these financial instruments is primarily bank credit risk. There was no indication of impairment in the 2016 financial year.

According to the Company's hedging policy, highly probable future cash flows and clearly identifiable foreign currency receivables that are expected to be collected within a 12-month period are reviewed for hedging requirements. As of December 31, 2016, there were 11 outstanding forward rate agreements with terms of up to 12 months and a nominal value of € 15,957k (December 31, 2015: 15 forward rate agreements with a nominal value of € 14,031k). The nominal volume is equal to the contract values of the individual forward rate agreements. The fair value of these contracts as of December 31, 2016 is equivalent to an unrealized gross profit of € 520k (December 31, 2015: unrealized gross profit of € 750k and unrealized gross loss of € 25k).

Rent security deposits granted amounted to € 1,223k (December 31, 2015: € 551k) and were recognized separately under other assets.

In 2016, impairments of other assets amounting to € 7k (December 31, 2015: € 214k) were recognized.

Other assets also contained a receivable due from tax authorities from excess value-added tax payments.

## SECURITIES

Securities consisted of marketable securities in the amount of € 63,360k (December 31, 2015: € 64,089k) as well as marketable bonds of € 6,530k (2015: € 33,119k). As of December 31, 2016, impairment for unrealized losses on marketable securities was € 73k (December 31, 2015: € 0k) and € 90k (December 31, 2015: € 480k) related to marketable bonds. The changes of € 73k and € 390k were recognized in profit and loss.

## COMMON STOCK

On December 31, 2016, the Company had common stock in the amount of € 29,160k (December 31, 2015: € 26,538k) divided into 29,159,770 no-par-value bearer shares (December 31, 2015: 26,537,682 shares). With the exception of the 396,010 treasury shares (2015: 434,670 treasury shares) held by the

Company, the shares concerned are bearer shares with dividend entitlements and voting rights with each share carrying one vote at the Annual General Meeting. The increase in common stock of € 2,622k resulted from the shares created by the capital increase in November 2016.

## TREASURY STOCK

The nominal value of the Company's treasury stock is offset against common stock. The development of treasury stock is shown below.

	Number of Company Shares	Value of Capital Subscribed in €
Treasury Stock as of 31 December 2010	79,896	79,896
Repurchase of Treasury Stock	84,019	84,019
Treasury Stock as of 31 December 2011	163,915	163,915
Repurchase of Treasury Stock	91,500	91,500
Treasury Stock as of 31 December 2012	255,415	255,415
Repurchase of Treasury Stock	84,475	84,475
Treasury Stock as of 31 December 2013	339,890	339,890
Repurchase of Treasury Stock	111,000	111,000
Treasury Stock as of December 31, 2014	450,890	450,890
Repurchase of Treasury Stock	88,670	88,670
Transfer of Treasury Stock	(104,890)	(104,890)
Treasury Stock as of December 31, 2015	434,670	434,670
Repurchase of Treasury Stock	52,295	52,295
Transfer of Treasury Stock	(90,955)	(90,955)
Treasury Stock as of 31 December 2016	396,010	396,010

As of December 31, 2016, treasury stock amounted to 1.36 % (December 31, 2015: 1.64 %) of common stock.

In March 2016, the Company repurchased 52,295 MorphoSys shares with a nominal value of € 1.00 each (0.18% of common stock as of December 31, 2016) on the stock exchange and increased the amount of treasury stock accordingly. The treasury stock may be used for all purposes named in the authorization of the Annual General Meetings on May 19, 2011 and May 23, 2014, and particularly for any existing or future employee participation programs and/or to finance acquisitions. However, they may also be redeemed.

There was an offsetting effect from the transfer of 90,955 of the Company's own shares to the Management Board and Senior Management Group from the 2012 long-term incentive plan (LTI plan). The vesting period for this LTI program expired on April 1, 2016 and October 1, 2016 and provided beneficiaries a six-month option to receive a total of 90,955 shares.

## AUTHORIZED AND CONDITIONAL CAPITAL

On November 15, 2016, a total of 2,622,088 shares were issued from Authorized Capital 2014-I in the context of a cash capital increase, which fully exhausted the previous Authorized Capital 2014-I.

The cash capital increase was recorded in the commercial register on November 17, 2016. Compared to December 31, 2015, the number of authorized ordinary shares declined by 2,622,088 from 13,206,421 to 10,584,333.

Compared to December 31, 2015, the number of ordinary shares of conditional capital decreased from 7,086,000 to 6,752,698. The Annual General Meeting on June 2, 2016 canceled the Conditional Capital 2003-II amounting to € 36k and the Conditional Capital 2011-I amounting to € 6,600k. This was partly offset by the creation of Conditional Capital 2016-I amounting to € 5,308k and Conditional Capital 2016-III amounting to € 995k.

#### ADDITIONAL PAID-IN CAPITAL

As a result of the capital increase described above, additional paid-in capital developed as follows.

	in 000's €
<b>Status on January 1, 2016</b>	<b>295,228</b>
Addition in Connection with Capital Increase	112,750
<b>Status on December 31, 2016</b>	<b>407,978</b>

The rise in additional paid-in capital totaling € 112,750k resulted solely from the capital increase carried out in November 2016.

#### EARNINGS RESERVES

Other earnings reserves amounted to € 12,667k (December 31, 2015: € 13,269k).

Other earnings reserves in the 2016 financial year developed as follows.

	in 000's €
<b>Other earnings reserve as of January 1, 2016</b>	<b>13,269</b>
Settlement with the difference from purchase of Treasury Stock	(2,128)
Settlement with the difference from transfer of Treasury Stock by Allocation to Other Earnings Reserves	1,526
<b>Other earnings reserve as of December 31, 2016</b>	<b>12,667</b>

In 2016, an amount of € 2,128k was offset against other earnings reserves that resulted from the repurchase of treasury stock, especially to service the 2016 long-term incentive plan. This was partly compensated by the reclassifications of other provisions in the amount of € 1,526k related to the allocation of treasury stock from the 2012 long-term incentive plan.

#### ACCUMULATED DEFICIT

The prior year's accumulated income developed as follows in the 2016 reporting year.

	in 000's €
<b>Accumulated Income as of January 1, 2016</b>	<b>14,857</b>
Net loss	(60,210)
Withdrawal from Other Earnings Reserves	2,128
Settlement with the difference from purchase of Treasury Stock	(2,128)
Settlement with the difference from transfer of Treasury Stock	1,526
Allocation to Other Earnings Reserves	(1,526)
<b>Accumulated Deficit as of December 31, 2016</b>	<b>(45,353)</b>

The Annual General Meeting resolved to carry forward the accumulated income as of December 31, 2015.

The Company's net loss for the 2016 fiscal year of € 60,210k was offset against the prior year's accumulated income (€ 14,857k). As a result, MorphoSys AG's accumulated loss for the 2016 fiscal year amounted to € 45,353k (December 31, 2015: accumulated income of € 14,857k).

## CONVERTIBLE BONDS

### 2013 PROGRAM

On April 1, 2013, MorphoSys AG granted the Management Board and members of the Senior Management Group convertible bonds with a total nominal value of € 225,000 and divided into 449,999 bearer bonds with equal rights from "Conditional Capital 2008-III". The beneficiaries have the right to convert the bonds granted into shares of the Company. Each convertible bond may be exchanged for one of the Company's bearer shares equal to its notional interest in the subscribed capital of currently € 1. The exercise of the convertible bonds is subject to several conditions, such as the achievement of performance targets, the expiration of vesting periods, the exercisability of the conversion rights, the existence of an employment or service contract that is not under notice and the commencement of the exercise period.

The conversion price amounted to € 31.88 and was derived from the Company's share price in the XETRA closing auction of the Frankfurt Stock Exchange on the trading day preceding the issuance of the convertible bonds. The exercise of the conversion rights is admissible if, on at least one trading day during the lifetime of the convertible bonds, the Company's share price amounted to more than 120% of the price in the XETRA closing auction of the Frankfurt Stock Exchange on the trading day preceding the issuance of the convertible bonds.

The exercise of the conversion rights is only admissible after the expiration of a four-year vesting period from the grant date. In the event of a change of control, the vesting period will be shortened to two years from the grant date. For every year without a notice of termination of the employment relationship with the Company or an affiliated company, 25 % of the conversion rights will become vested. In the event of a change of control, all unvested conversion rights become vested.

If an employment or service contract of a beneficiary is terminated without notice, no further conversion rights may be vested under the above-mentioned vesting scheme. Thus, upon rendition of the notice, all conversion rights still unvested by this time will expire without substitution. In the event of a contractual notice of termination of such an employment or service contract with the beneficiary or a

mutually agreed dissolution contract, the previous sentence applies and becomes effective as of the date of termination of the employment or service contract.

The following table shows the development of the Company's convertible bond plans for employees in financial years 2016 and 2015.

	Convertible Bonds	Weighted- average Price €
<b>Outstanding as of January 1, 2015</b>	<b>530,847</b>	<b>29.58</b>
Granted	0	0.00
Exercised	(80,848)	16.79
Forfeited	0	0.00
Expired	0	0.00
<b>Outstanding as of December 31, 2015</b>	<b>449,999</b>	<b>31.88</b>
<b>Outstanding as of January 1, 2016</b>	<b>449,999</b>	<b>31.88</b>
Granted	0	0.00
Exercised	0	0.00
Forfeited	(13,414)	31.88
Expired	0	0.00
<b>Outstanding as of December 31, 2016</b>	<b>436,585</b>	<b>31.88</b>

From the grant date until December 31, 2016, one beneficiary left MorphoSys and, therefore, 13,414 convertible bonds were forfeited. On December 31, 2016, the number of vested convertible bonds totaled 327,439 shares (December 31, 2015: 225,000 shares).

The following overview includes the weighted-average exercise price as well as information on the contract duration of significant groups of convertible bonds as of December 31, 2016.

Range of Exercise Prices	Number Outstanding	Remaining Contractual Life (in Years)	Weighted- average Exercise Price (€)	Number Exercisable	Weighted- average Exercise Price (€)
€ 25.00 - € 40.00	436,585	3.25	31.88	327,439	31.88
	<b>436,585</b>	<b>3.25</b>	<b>31.88</b>	<b>327,439</b>	<b>31.88</b>

## LONG-TERM INCENTIVE PROGRAMS

On March 31, 2016, the conditions of the long-term incentive plans (LTI plan) 2012, 2013, 2014 and 2015 for the Management Board and Senior Management Group were amended to include a six-month exercise period following the four-year vesting period, during which the Company can transfer the

performance shares to the beneficiaries. Previously, under these plans, the performance shares were automatically allocated following the four-year vesting period. Beneficiaries can now choose the exercise date within the six-month exercise period. The plan modification had no impact on the fair value of the performance shares or on the period over which the personnel expenses are to be recognized.

#### **2012 LONG-TERM INCENTIVE PLAN**

On April 1, 2012, MorphoSys established a long-term incentive plan (LTI plan) for the Management Board and the Senior Management Group. The vesting period of this plan expired on April 1, 2016. The LTI plan is a performance-related share plan and is paid out in ordinary shares (performance shares) of MorphoSys AG if predefined key performance criteria are achieved. These criteria are approved annually by the Supervisory Board. The fulfillment of these criteria was set at 200 % for two years, 54 % for one year and 0 % for one year. The Supervisory Board set the “company factor” at 0.88, meaning the number of performance shares to be allocated is scaled by a factor of 0.88. This factor resulted in an adjustment of previously recognized personnel expenses of € -0.2 million in the 2016 financial year. Previously, personnel expenses resulting from the 2012 LTI program were recognized based on the assumption of a company factor of 1.0. Based on these terms and the company factor, a total of 88,663 performance shares of MorphoSys AG was allocated to beneficiaries on October 4, 2016 after the expiration of the four-year vesting period. The Management Board received 57,967 performance shares (for further information, please see the table in the section “Total Remuneration of the Management Board and Supervisory Board”), the Senior Management Group received 27,813 performance shares and former members of the Senior Management Group, who have left the Company in the meantime, received 2,883 performance shares.

On October 1, 2012, MorphoSys established another long-term incentive plan (LTI plan) for Senior Management Group members. The vesting period of this plan expired on October 1, 2016. The terms of this plan were identical to the April 1, 2012 plan. The fulfillment of the performance criteria was set at 200 % for one year, 54.8 % for one year and 0 % for two years. The Supervisory Board set the “company factor” at 1.57, meaning the number of performance shares to be allocated is scaled by a factor of 1.57. This factor resulted in an adjustment of previously recognized personnel expenses of less than € 0.1 million in the 2016 financial year. Previously, personnel expenses resulting from the 2012 LTI program were recognized based on the assumption of a company factor of 1.0. Based on these terms and the company factor, a total of 2,292 performance shares of MorphoSys AG was allocated to beneficiaries in October 2016 after the expiration of the four-year vesting period. The Senior Management Group received all of the 2,292 performance shares.

In 2016, personnel expenses from performance shares under the 2012 LTI plan amounted to € -66k (2015: € 457k).

#### **2013 LONG-TERM INCENTIVE PLAN**

On April 1, 2013, MorphoSys established another long-term incentive plan (LTI plan) for the Management Board and the Senior Management Group. The LTI plan is a performance-related share plan and will be paid out in ordinary shares (performance shares) of MorphoSys AG if predefined key performance criteria are achieved. These criteria are evaluated annually by the Supervisory Board. The grant date was April 1, 2013 and the vesting/performance period is four years. If the predefined key performance criteria for the respective period are fully met, 25 % of the performance shares become vested in each year of the four-year vesting period. The number of performance shares vested each year will be reduced or increased to the extent that the performance criteria of the respective year have been

achieved between only 50 % and 99.9 % (<100 %) or the achievement of the performance criteria has exceeded 100 % (maximum 200 %). If in one year the performance criteria are achieved by less than 50 %, no performance shares will become vested in that year. In any case, the maximum pay-out at the end of the four-year period is limited by a factor determined by the Company, which generally amounts to 1. However, in justified cases, the Supervisory Board may set this factor freely between 0 and 2, for example, if the level of payment is considered unreasonable in view of the Company's general development. The right to receive a certain allocation of performance shares under the LTI plan occurs only at the end of the four-year vesting period.

If the number of repurchased shares is not sufficient for servicing the LTI plan, MorphoSys reserves the right to pay a certain amount of the LTI plan in cash in the amount of the performance shares at the end of the vesting period, provided the cash amount does not exceed 200 % of the fair value of the performance shares on the grant date.

If a member of the Management Board prematurely ceases to hold an office at MorphoSys before expiration of the four-year performance period, the member (or the member's heirs) is entitled to performance shares determined on a precise daily pro rata basis. If a Management Board member prematurely ceases to hold an office at MorphoSys for good reason as defined by Sec. 626 Para. 2 of the German Civil Code (BGB) before expiration of the four-year performance period, the beneficiary will not be entitled to an allocation of performance shares. If a change of control occurs during the four-year vesting period, all performance shares will be considered fully vested. In each case above, the right to receive a certain allocation of performance shares under the LTI plan only occurs at the end of the four-year vesting period.

In April and May of 2013, MorphoSys repurchased 84,475 of its own shares on the stock exchange at an average price of € 33.43 per share. The repurchased shares can be used for all purposes named in the authorizations of the Annual General Meetings on May 19, 2011 and on May 23, 2014 and particularly for any existing or future employee participation schemes and/or to finance acquisitions. The shares may also be redeemed.

Of these shares, 61,600 were allocated to beneficiaries retroactively effective April 1, 2013. This included 36,729 performance shares for the Management Board (for further information, please see the table in the section "Total Remuneration of the Management Board and Supervisory Board") and 24,871 performance shares for the Senior Management Group. The number of performance shares allocated is based on the full achievement of performance criteria and a company factor of 1. On the grant date (April 1, 2013), the fair value of the performance shares was € 29.08 per share. No dividends were included in the determination of the fair value of the performance shares since the Company does not intend to distribute any dividends in the foreseeable future. From the grant date until December 31, 2016, two beneficiaries left MorphoSys and, accordingly, 881 performance shares were forfeited. For the calculation of the personnel expenses resulting from share-based payments under the 2013 LTI plan, it was initially assumed that one beneficiary will leave the Company during the four-year period. In 2016, this assumption was updated.

On October 1, 2013, MorphoSys established another long-term incentive plan (LTI plan) for Senior Management Group members. The terms of the plan were identical to the April 1, 2013 plan. A total of 549 performance shares were granted. The fair value was € 52.24 per performance share on the grant date.

In 2016, personnel expenses from performance shares under the 2013 LTI plan amounted to € 308k (2015: € 512k).



## 2014 LONG-TERM INCENTIVE PLAN

On April 1, 2014, MorphoSys established a fourth long-term incentive plan (LTI plan) for the Management Board and the Senior Management Group. The LTI plan is a performance-related share plan and will be paid out in ordinary shares (performance shares) of MorphoSys AG if predefined key performance criteria are achieved. These criteria are evaluated annually by the Supervisory Board. The grant date was April 1, 2014 and the vesting/performance period is four years. If the predefined key performance criteria for the respective period are fully met, 25 % of the performance shares become vested in each year of the four-year vesting period. The number of performance shares vested each year will be reduced or increased to the extent that the performance criteria of the respective year have been achieved between only 50 % and 99.9 % (<100 %) or the achievement of the performance criteria has exceeded 100 % (maximum 200 %). If in one year the performance criteria are met by less than 50 %, no performance shares will become vested in that year. In any case, the maximum pay-out at the end of the four-year period is limited by a factor determined by the Company, which generally amounts to 1. However, in justified cases, the Supervisory Board may set this factor freely between 0 and 2, for example, if the level of payment is regarded as unreasonable in view of the general development of the Company. The right to receive a certain allocation of performance shares under the LTI plan, however, occurs only at the end of the four-year vesting period.

If the number of repurchased shares is not sufficient for servicing the LTI plan, MorphoSys reserves the right to pay a certain amount of the LTI plan in cash in the amount of the performance shares at the end of the vesting period, provided the cash amount does not exceed 200 % of the fair value of the performance shares on the grant date.

If a member of the Management Board ceases to hold an office at MorphoSys because of termination (or if the Management Board member terminates the employment contract), resignation, death, injury, disability, by reaching retirement age (receipt of a normal retirement pension, early-retirement pension or disability pension, as long as the requirements for the disability pension entitlement are met) or under other circumstances subject to the Supervisory Board's discretion, the Management Board member (or the member's heirs) is entitled to performance shares determined on a precise daily pro rata basis.

If a member of the Management Board ceases to hold an office at MorphoSys for good reason as defined by Sec. 626 Para. 2 of the German Civil Code (BGB) and/or as defined by Sec. 84 Para. 3 of the German Stock Corporation Act (AktG), the beneficiary will not be entitled to performance shares.

If a change of control occurs during the four-year vesting period, all performance shares will become fully vested. In this case, the right to receive a certain allocation of performance shares under the LTI plan occurs only at the end of the four-year vesting period.

In March 2014, MorphoSys repurchased 111,000 of its own shares on the stock exchange at an average price of € 70.53 per share. The repurchased shares may be used for all purposes named in the authorizations of the Annual General Meetings on May 19, 2011 and May 23, 2014 and particularly for any existing or future employee participation schemes and/or to finance acquisitions. The shares may also be redeemed.

A total of 32,513 of these shares were allocated to beneficiaries on April 1, 2014 with 18,264 performance shares allocated to the Management Board (for further information, please see the table in the section “Total Remuneration of the Management Board and Supervisory Board”) and 14,249 performance shares to the Senior Management Group. The number of performance shares allocated is based on the full achievement of performance criteria and a company factor of 1. The fair value of the performance shares on the grant date (April 1, 2014) was € 62.17 per share. No dividends were included in the determination of the fair value of the performance shares because the Company does not intend to distribute any dividends in the foreseeable future. From the grant date until December 31, 2016, two beneficiaries left MorphoSys and, therefore, 889 performance shares were forfeited. For the calculation of the personnel expenses from share-based payments under the 2014 LTI plan, it was initially assumed that one beneficiary will leave the Company during the four-year period. In 2016, this assumption was updated.

In 2016, personnel expenses from performance shares under the 2014 LTI plan amounted to € 394k (2015: € 557k).

#### **2015 LONG-TERM INCENTIVE PLAN**

On April 1, 2015, MorphoSys established a fifth long-term incentive plan (LTI plan) for the Management Board and the Senior Management Group. The LTI plan is a performance-related share plan and will be paid out in ordinary shares (performance shares) of MorphoSys AG if predefined key performance criteria are achieved. These criteria are evaluated annually by the Supervisory Board. The grant date was April 1, 2015 and the vesting/performance period is four years. If the predefined key performance criteria for the respective period are fully met, 25 % of the performance shares become vested in each year of the four-year vesting period. The number of performance shares vested each year is reduced or increased to the extent that the performance criteria of the respective year have been achieved between only 50 % and 99.9 % (<100 %) or the achievement of the performance criteria exceeded 100 % (maximum 200 %). If in one year the performance criteria are met by less than 50 %, no performance shares will become vested in that year. In any case, the maximum pay-out at the end of the four-year period is limited by a factor determined by the Company, which generally amounts to 1. However, in justified cases, the Supervisory Board may set this factor freely between 0 and 2, for example, if the level of payment is regarded as unreasonable in view of the general development of the Company. The right to receive a certain allocation of performance shares under the LTI plan only occurs at the end of the four-year vesting period.

If the number of repurchased shares is not sufficient for servicing the LTI plan, MorphoSys reserves the right to pay a certain amount of the LTI plan in cash in the amount of the performance shares at the end of the vesting period, provided the cash amount does not exceed 200 % of the fair value of the performance shares on the grant date.

If a member of the Management Board ceases to hold an office at MorphoSys because of termination (or if the Management Board member terminates the employment contract), resignation, death, injury, disability, by reaching the retirement age (receipt of a normal retirement pension, early-retirement, pension or disability pension, as long as the requirements for the disability pension entitlement are met) or under other circumstances subject to the Supervisory Board’s discretion, the Management Board member (or the member’s heirs) is entitled to performance shares determined on a precise daily pro rata basis.

If a member of the Management Board ceases to hold an office at MorphoSys for good reason as defined by Sec. 626 Para. 2 of the German Civil Code (BGB) and/or as defined by Sec. 84 Para. 3 of the German Stock Corporation Act (AktG), the beneficiary will not be entitled to performance shares.

If a change of control occurs during the four-year vesting period, all performance shares will become fully vested. In this case, the right to receive a certain allocation of shares under the LTI plan occurs only at the end of the four-year vesting period.

In April 2015, MorphoSys repurchased 88,670 of its own shares on the stock exchange at an average price of € 60.79 per share for a total amount of € 5,389,984. The repurchased shares may be used for all purposes named in the authorization of the Annual General Meeting on May 23, 2014 and particularly for any existing or future employee participation schemes and/or to finance acquisitions. The shares may also be redeemed.

A total of 40,425 of these shares were allocated to beneficiaries on April 1, 2015 with 21,948 performance shares allocated to the Management Board (for further information, please see the table in the section "Total Remuneration of the Management Board and Supervisory Board") and 18,477 performance shares to the Senior Management Group. The number of performance shares allocated is based on the 100 % achievement of the performance criteria and a company factor of 1. The fair value of the performance shares as of the grant date (April 1, 2015) was € 61.40 per share. No dividends were considered in the determination of the fair value of the performance shares since the Company does not intend to distribute any dividends in the foreseeable future. From the grant date until December 31, 2016, one beneficiary left MorphoSys, and, accordingly, 696 performance shares were forfeited. For the calculation of the personnel expenses from share-based payments under the 2015 LTI plan, it was assumed that one beneficiary would leave the Company during the four-year period.

In 2016, personnel expenses from performance shares under the 2015 LTI plan amounted to € 591k (2015: € 448k).

#### **2016 LONG-TERM INCENTIVE PLAN**

On April 1, 2016, MorphoSys established a further long-term incentive plan (LTI plan) for the Management Board and the Senior Management Group. The LTI plan is a performance-based share plan paid out in ordinary shares (performance shares) of MorphoSys AG when predefined key performance criteria have been achieved. These criteria are evaluated annually by the Supervisory Board. The grant date was April 1, 2016, and the vesting/performance period is four years. If the predefined key performance criteria for the respective period are fully met, 25 % of the performance shares will vest in each year of the four-year vesting period. The number of performance shares vested each year will be reduced or increased to the extent that the performance criteria of the respective year have only been achieved between 50 % and 99.9 % (<100 %) or the achievement of the performance criteria has exceeded 100 % (maximum 200 %). If in one year the achievement of performance criteria falls below 50 %, no performance shares will vest in that year. Regardless, the maximum pay-out at the end of the four-year period is limited by a factor determined by the Company, which generally amounts to 1. In justified cases, the Supervisory Board may, however, set this factor freely between 0 and 2, for example, if the level of payment seems unreasonable in view of the Company's general development. The right to receive a certain allocation of performance shares under the LTI plan, however, occurs only at the end of the four-year vesting period.

There is a six-month exercise period following the four-year vesting period, during which the Company can transfer the performance shares to the beneficiaries. Beneficiaries are free to choose the exercise date within this exercise period.

If the number of repurchased shares is insufficient for servicing the LTI plan, MorphoSys reserves the right to pay a certain amount of the LTI plan in cash in the amount of the performance shares at the end of the vesting period provided the cash amount does not exceed 200 % of the fair value of the performance shares on the grant date.

If a member of the Management Board ceases to hold an office at MorphoSys through termination (or the Management Board member terminates the employment contract), resignation, death, injury, disability or due to reaching the retirement age (receipt of a normal retirement pension, early-retirement pension or disability pension, as long as the requirements for the disability pension entitlement are met), or under other circumstances subject to the Supervisory Board's discretion, the Management Board member (or the member's heirs) is entitled to performance shares determined on a precise daily pro rata basis.

If a member of the Management Board ceases to hold an office at MorphoSys for good reason as defined by Sec. 626 Para. 2 of the German Civil Code (BGB) and/or as defined by Sec. 84 Para 3 of the German Stock Corporation Act (AktG), the beneficiary is no longer entitled to an allocation of performance shares.

If a change of control occurs during the four-year vesting period, all performance shares will be considered fully vested. In this case, the right to receive a certain allocation of performance shares under the LTI plan occurs only at the end of the four-year vesting period.

In March 2016, MorphoSys repurchased 52,295 of its own shares on the stock exchange at an average price of € 41.69 per share for a total amount of € 2,179,963. The shares of treasury stock may be used for all purposes named in the authorization of the Annual General Meeting of May 23, 2014, particularly for any existing or future employee participation programs and/or to finance acquisitions or may also be redeemed.

A total of 68,143 of treasury shares were granted to the beneficiaries as of April 1, 2016 with 35,681 performance shares allocated to the Management Board (for further information, please see the table in the section "Total Remuneration of the Management Board and Supervisory Board") and 32,462 performance shares to the Senior Management Group. The number of performance shares granted was based on 100 % target achievement and a factor of 1. The fair value of the performance shares on the grant date (April 1, 2016) was € 46.86 per share. Dividends were not considered in the determination of the fair value of the performance shares since the Company does not intend to distribute any dividends in the foreseeable future. From the grant date until December 31, 2016, one beneficiary has left MorphoSys, and accordingly 1,464 performance shares were forfeited. For the calculation of personnel expenses resulting from share-based payments under the 2016 LTI plan, the assumption was made that one beneficiary will leave the Company during the four-year period.

In 2016, personnel expenses from performance shares under the 2016 LTI plan amounted to € 535k.

## TAX PROVISIONS

As of December 31, 2016, MorphoSys AG's tax provisions were unchanged at € 1,498k (December 31, 2015: € 1,498k).

## OTHER PROVISIONS

The provisions cover all identifiable risks and uncertain liabilities. They consist mainly of expenses for third-party laboratory services (2016: € 15,949k; 2015: € 13,761k); bonus payments (2016: € 1,879k; 2015: € 2,144k); personnel expenses resulting from performance shares under LTI plans (2016: € 4,579k; 2015: € 4,410k); onerous contracts related to leased office premises no longer used and for an onerous contract with a contract manufacturing organization for drug substances and drug products for clinical trial use (2016: € 2,625k; 2015: € 1,250k); consulting services (2016: € 572k; 2015: € 625k); license and inventor's remuneration (2016: € 80k; 2015: € 91k); outstanding vacation entitlements (2016: € 515k; 2015: € 458k); and legal consulting (2016: € 983k; 2015: € 390k).

## LIABILITIES

The maturities of the liabilities are shown in the following overview. All liabilities are unsecured.

Type	Remaining Term of Liabilities			12/31/2016	Total
	up to 1 year	1 to 5 years	more than 5 years	in 000's €	12/31/2015 in 000's €
1. Bonds, thereof convertible	218	0	0	218	225
2. Trade Accounts Payable	8,358	0	0	8,358	264
Liabilities due to Affiliated Companies	134	0	0	134	134
3. Companies	134	0	0	134	134
4. Other Liabilities	781	0	0	781	1,626
thereof Taxes	615	0	0	615	1,626

## BONDS

On December 31, 2016, the Company had liabilities related to convertible bonds granted to Management Board members and employees of MorphoSys AG amounting to € 218k (December 31, 2015: € 225k).

## TRADE ACCOUNTS PAYABLE

As of December 31, 2016, MorphoSys AG had trade accounts payable of € 8,358k (December 31, 2015: € 264k). The year-on-year increase resulted from liabilities for third-party laboratory services that were not yet due on the reporting date.

## LIABILITIES DUE TO AFFILIATED COMPANIES

As of December 31, 2016, liabilities due to affiliated companies amounted to € 134k (December 2015: € 134k), which solely contained trade accounts payable.

## OTHER LIABILITIES

Other liabilities as of December 31, 2016, mainly included liabilities to tax authorities for the deduction and payment of income tax in the amount of € 615k (December 31, 2015: € 1,626k).

## DEFERRED REVENUE

Deferred revenue consists of payments received from customers for which a service was not yet rendered. The decrease in revenue recognized from upfront payments due to services rendered in the 2015 financial year was mainly the result of the termination of the co-development agreement with Celgene.

In the years 2016 and 2015, deferred revenue developed as follows.

in 000's €	2016	2015
<b>Opening Balance</b>	<b>650</b>	<b>52,578</b>
Prepayments Received	16,829	17,142
Revenue Recognised through Release of Prepayments in line with Services Performed	(16,838)	(69,070)
<b>Closing Balance</b>	<b>641</b>	<b>650</b>

## OTHER FINANCIAL OBLIGATIONS

The following overview shows other financial obligations from rental and lease agreements, insurance and other services as of December 31, 2016.

in 000's €	Rent and Leasing	Other	Total
2017	3,150	796	3,946
2018	2,791	1	2,792
2019	2,747	0	2,747
2020	2,704	0	2,704
2021	2,704	0	2,704
more	13,875	0	13,875
<b>Total</b>	<b>27,971</b>	<b>797</b>	<b>28,768</b>

Additionally, the future payments as shown in the table below may become due for outsourced studies. These amounts could be shifted or be substantially lower due to changes in the study timeline or premature study termination.

in million €	Total 2016
up to 1 year	50.0
Between one year and five years	112.2
more than 5 years	0.0
<b>Total</b>	<b>162.2</b>

If certain milestones are achieved in the Proprietary Development segment, such as an application for an investigational new drug (IND) with regard to specific target molecules, this may trigger milestone payments to licensors. However, no further details can be published since the timing and achievement of such milestones are uncertain.

If a partner achieves certain milestones in the Partnered Discovery segment, such as the application for an investigational new drug (IND) with regard to specific target molecules or the transfer of a technology, this may trigger milestone payments to MorphoSys. However, no further details can be published since the timing and achievement of such milestones are uncertain.

Obligations may arise from enforcing the Company's patents against third parties. It is also conceivable that competitors may challenge the patents of the MorphoSys Group companies. MorphoSys may also come to the conclusion that MorphoSys's patents or patent families are infringed by competitors, which may prompt MorphoSys to take legal action against competitors. At present, there are no specific indications that liabilities have occurred as described above.

## CONTINGENT LIABILITIES

In the 2015 financial year, MorphoSys AG issued a letter of comfort for the benefit of Lanthio Pharma B.V. in which MorphoSys AG agrees to provide liquid funds of up to € 2.1 million under certain conditions for the safeguarding of a government grant. Due to a contribution to Lanthio Pharma B.V.'s capital reserves in the amount of € 7.5 million in the reporting year and € 3.5 million in 2015, the Company believes that a claim under the comfort letter is unlikely.

## Notes to the Statement of Income

### REVENUES

Revenues in the 2016 financial year decreased by 53 % to € 48,714k (2015: € 102,675k) versus the prior year. This decrease mainly originated from a one-off effect in the 2015 financial year from the termination of the MOR202 co-development and co-promotion agreement with Celgene, which resulted in the recognition of previously deferred revenue. If Sec. 277 HGB Para. 1 in the version of BilRUG had been applied, revenues in the 2015 financial year would have amounted to € 104,924k. The higher revenue under BilRUG resulted mainly from personnel expenses passed on under co-development agreements, contracts fulfilled by an affiliated company and governments grants which were previously recorded under other operating income.

In the 2016 financial year, the majority of revenues were generated from the antibody collaborations and license agreements with Novartis, Janssen, and Bayer Pharma. Revenues of the Proprietary

Development and Partnered Discovery segments contributed € 1,983k and € 46,626k to total revenues in 2016 (2015: € 58,314k and € 44,361k, respectively). Revenues not allocated to any of the segments amounted to € 105k in the reporting year. If Sec. 277 HGB Para. 1 in the version of BilRUG had been applied, revenues in the Proprietary Development and Partnered Discovery segments would have amounted to € 60,446k and € 44,386k in the 2015 financial year. Revenues not allocated to any of the segments would have amounted to € 92k in 2015.

Of total revenues, € 1,927k (2015: € 2,184k) were attributed to domestic revenues and € 2,823k (2015: € 58,692k) to biotechnology and pharmaceutical companies and non-profit organizations based in North America. Other European countries and Asia generated revenues of € 43,964k (2015: € 41,800k). If Sec. 277 HGB Para. 1 in the version of BilRUG had been applied, domestic revenues would have amounted to € 2,507k and revenues with biotechnology and pharmaceutical companies and non-profit organizations based in North America would have amounted to € 59,517k in 2015. Revenues generated in other European countries and Asia would have amounted to € 42,900k under BilRUG.

#### **COST OF GOODS SOLD**

Cost of goods sold of € 94,760k (2015: € 82,655k) included research and development costs comprising costs for external services of € 44,357k (2015: € 36,765k), personnel expenses of € 26,713k (2015: € 30,404k), costs related to intangible assets of € 13,741k (2015: € 3,757k), material costs of € 2,205k (2015: € 2,741k), infrastructure costs of € 5,203k (2015: € 6,031k) and other costs of € 2,540k (2015: € 2,958k). The decline in personnel expenses is mainly due to lower taxable non-cash employee benefits from the transfer of share-based remuneration programs to employees in the research and development area in 2016 (see explanation under "Personnel Expenses") and lower personnel expenses from the LTI plans' performance shares. The rise in costs for external services is largely the result of higher expenditures for external laboratory services for MorphoSys's proprietary product development. In 2016, MorphoSys AG recognized impairment of licenses for concessions, commercial property rights and similar rights amounting to € 10,141k (2015: € 0k). The impairment expense entirely consisted of an impairment on the in-process R&D program MOR209/ES414.

#### **SELLING EXPENSES**

Selling expenses of € 2,505k (2015: € 2,130k) included personnel expenses of € 1,722k (2015: € 1,483k), costs for external services of € 338k (2015: € 258k) and other costs of € 444k (2015: € 389k).

#### **GENERAL ADMINISTRATION EXPENSES**

General administration expenses of € 18,582k (2015: € 17,473k) contained primarily personnel expenses of € 11,244k (2015: € 13,374k), costs for external services of € 5,167k (2015: € 2,775k), costs related to intangible assets of € 452k (2015: € 302k), infrastructure costs of € 798k (2015: € 4k) and other costs of € 920k (2015: € 1,018k). The decline in personnel expenses is mainly due to the lower taxable non-cash employee benefits from the transfer of share-based remuneration programs to employees in the administrative area compared to 2015 (see explanation under "Personnel Expenses"). The rise in costs for external services resulted from the costs associated with the capital increase executed in November 2016.



## PERSONNEL EXPENSES

Personnel expenses of € 39,679k (2015: € 45,260k) consisted of wages and salaries of € 31,472k (2015: € 36,505k), social security contributions of € 3,537k (2015: € 3,462k), personnel expenses from the LTI plan's performance shares of € 1,973k (2015: € 2,673k), pension costs of € 1,038k (2015: € 970k), costs for external support staff/temporary employees of € 786k (2015: € 504k) and other costs of € 873k (2015: € 1,147k). In 2016 and 2015, other personnel expenses mainly included recruitment costs.

The decline in personnel expenses was driven mainly by lower salary expenses (€ 5,033k) due to the lower taxable non-cash employee benefits from the transfer of share-based remuneration programs to employees of MorphoSys AG.

Although MorphoSys AG executes the taxation of the non-cash benefits for active employees from the allocation and exercise of share-based remuneration, the employees are obliged to refund MorphoSys for this tax payment. In order to technically execute this taxation over the payroll, the basis for the assessment must be recorded under personnel expenses. From an accounting standpoint, this expense is offset by other operating income (see "Other Operating Income"). In 2016, this amount was € 3,714k (2015: € 9,467k). The decline in the assessment basis in 2016 was due to the lower number of transactions versus the previous year.

## MATERIAL EXPENSES

Material expenses of € 2,303k (2015: € 2,817k) mostly concerned expenses for raw materials, supplies and production materials of € 2,161k (2015: € 2,730k) and costs for printed materials of € 58k (2015: € 54k). Material expenses in the years 2016 and 2015 did not contain any purchased services.

## OTHER OPERATING INCOME

Other operating income amounted to € 6,646k compared to € 16,779k in 2015. This amount included € 3,959k (2015: € 9,706k) in refunded taxes paid as well as the correction of the assessment base for the taxation of non-cash benefits (see also the explanations on "Personnel Expenses"). Other operating income also included income related to prior periods from the release of provisions recognized in the previous year as well as other operating income of € 1,745k (2015: € 3,618k), currency gains of € 192k (2015: € 155k) and gains from currency hedges of € 750k (2015: € 1,076k).

The components of personnel expenses passed on under co-development agreements and contracts fulfilled by an affiliated company of € 1,164k (2015: € 1,931k) and government grants of € 255k (2015: € 292k), which were recorded under other operating income in the previous year, are included in revenues starting with the 2016 reporting year due to the application of Sec. 277 HGB Para. 1 in the version of BilRUG.

## OTHER OPERATING EXPENSES

Other operating expenses totaled € 455k (2015: € 1,019k) and consisted mainly of currency losses of € 359k (2015: € 460k) and impairment of other assets of € 7k (2015: € 214k). The 2015 amount also included losses from forward rate agreements of € 287k).

#### **INCOME FROM INVESTMENTS**

MorphoSys AG did not receive any dividends in the reporting year. In the 2015 financial year, MorphoSys AG received a distribution of € 16k from the profit carried forward of the subsidiary Poole Real Estate Ltd., which was liquidated in 2015.

#### **INCOME FROM OTHER SECURITIES AND LOANS PRESENTED UNDER FINANCIAL ASSETS**

Income from other securities and loans presented under financial assets of € 294k (2015: € 92k) solely comprised realized gains on marketable securities.

#### **OTHER INTEREST AND SIMILAR INCOME**

This line item in the amount of € 1,232k (2015: € 1,726k) consisted mainly of interest income from bank deposits and financial investments classified as other assets amounting to € 1,163k (2015: € 1,648k) and interest income of € 69k from the discounting of non-current provisions for personnel expenses resulting from performance shares under the LTI plan (2015: € 78k).

#### **IMPAIRMENT OF FINANCIAL ASSETS OR CURRENT SECURITIES**

No impairment of financial assets or current securities was recognized in the 2016 financial year. As part of a distribution made by the subsidiary Poole Real Estate Ltd. to MorphoSys AG in 2015, the carrying amount of the investment in this affiliated company was reduced by € 16k. In December 2015, the residual carrying amount from the investment in Poole Real Estate Ltd. was fully written off following its liquidation and distribution of the assets to MorphoSys AG. This resulted in an expense of € 25k.

#### **LOSSES FROM OTHER SECURITIES AND LOANS PRESENTED UNDER FINANCIAL ASSETS**

Losses from other securities and loans presented under financial assets in the amount of € 892k (2015: € 427k) included unrealized losses resulting from the measurement of and realized losses from the sale of marketable securities and bonds.

#### **OTHER INTEREST AND SIMILAR EXPENSES**

Interest expenses mainly included € 40k (2015: € 35k) for the accrued interest on non-current provisions for personnel expenses from the LTI plans' performance shares.

#### **TAXES ON INCOME**

After an income tax expense of € 3,841k in 2015, an income tax benefit of € 158k was recognized in 2016. The income tax benefit in 2016 arose from a tax loss carryback for corporate tax purposes for the 2015 financial year as defined by Sec. 8 Para. 1 KStG (Corporation Tax Act) in conjunction with Sec. 10d Para. 1 sent. 1 EStG (Income Tax Act).

As of December 31, 2016, MorphoSys AG had tax loss carryforwards for corporate tax purposes of € 47,826k and € 48,359k for trade tax purposes.

Differences between commercial law and tax law regulations resulted in the recognition of temporary differences in MorphoSys AG's balance sheet. The determination of these temporary differences was based on a tax rate of 26.675 %. The Company has opted to offset deferred tax assets against deferred tax liabilities. The resulting total deferred tax relief is not recognized in the balance sheet as deferred tax assets pursuant to the option granted in Sec. 274 Para. 1 sent. 2 HGB. The deferred differences existing as of December 31, 2016 and December 31, 2015 resulted from temporary differences from the varied recognition of acquisition costs for paid concessions, commercial property rights and similar rights and assets, licenses to such rights and assets and the recognition of provisions. In addition, a tax reconciliation item related to other securities caused temporary differences in the balance sheet under commercial law and tax law. These differences would have resulted in deferred tax assets. As of December 31, 2016 and December 31, 2015, there were no deferred differences that would have resulted in deferred tax liabilities. Accordingly, the statement of income for the 2016 and 2015 financial years did not include any tax effects from the change in recognized deferred taxes.

## Other Information

### SUPERVISORY BOARD

As of December 31, 2016, the Company's Supervisory Board members were active in the supervisory boards or comparable supervisory bodies of the following companies:

Name	Place of Residence	Year of Birth	Actual Occupation	MorphoSys Supervisory Board	Memberships in other Supervisory Boards or Executive Bodies
Dr. Gerald Möller Heidelberg, Germany Year of Birth: 1943			Chairman of the Supervisory Board of MorphoSys AG as well as member of another supervisory board and member of comparable domestic and foreign supervisory boards of commercial enterprises	Member since 1999 Chairman Member of the Remuneration & Nomination Committee	4sigma Inc., BM (Chairman of the Board of Directors) Adrenomed AG, DE (Member of the Supervisory Board) Ayoxxa Biosystems GmbH, DE (Chairman of the Advisory Board) Gentical SA, FR (Deputy Chairman of the Supervisory Board; until February 28, 2017) Invendo Medical GmbH, DE (Chairman of the Advisory Board)
Dr. Frank Morich Berlin, Germany Year of Birth: 1953			Independent Consultant of the life sciences and healthcare industries	Member since 2015 Deputy Chairman Member of the Science & Technology Committee	No memberships
Dr. Marc Cluzel Montpellier, France Year of Birth: 1955			Member of the Supervisory Board of MorphoSys AG as well as member of A comparable foreign supervisory board of a commercial enterprise	Member since 2012 Member Chairman of the Science & Technology Committee Member of the Remuneration & Nomination Committee	Moleac Pte. Ltd., SG (Member of the <i>Board of Directors</i> )
Karin Eastham Rancho Santa Fe California, USA Year of Birth: 1949			Member of the Supervisory Board of MorphoSys AG as well as member of A comparable foreign supervisory board of a commercial enterprise	Member since 2012 Member Member of the Audit Committee Chairman of the Remuneration & Nomination Committee	Illumina, Inc., USA (Member of the <i>Board of Directors</i> ) Geron Corp., USA (Member of the <i>Board of Directors</i> ) Veracyte, Inc., USA (Member of the <i>Board of Directors</i> )
Wendy Johnson San Diego, California, USA Year of Birth: 1952			Managing Director, Gemini Advisors, USA, and Interim Chief Operating Officer, AmpliPhi Biosciences Corp., USA	Member since 2015 Member Member of the Audit Committee Member of the Science & Technology Committee	AmpliPhi Biosciences, USA (Member of the <i>Board of Directors</i> )
Klaus Kühn Grevenbroich, Germany Year of Birth: 1952			Member of the Supervisory Board of MorphoSys AG as well as chairman And member of comparable domestic supervisory boards of commercial enterprises	Member since 2015 Member Chairman of the audit Committee	Flossbach von Storch AG, DE (Chairman of the Supervisory Board) Hella KGaA Hueck & Co., DE (Member of the Supervisory Board, Member of the Shareholders' Committee)

## CORPORATE GOVERNANCE

In December 2002, the Company pledged to adhere to the corporate governance principles in compliance with the provisions of the German Corporate Governance Code, which has subsequently been amended.

On December 2, 2016, the Company published the Declaration of Conformity of the Management Board and Supervisory Board pursuant to Sec. 161 AktG and made it permanently available to its shareholders. This declaration can be found on Company's website ([www.morphosys.com](http://www.morphosys.com)).

## MANAGEMENT BOARD

Dr. Simon Moroney, Chemist, Pöcking, Germany (Chief Executive Officer)

Jens Holstein, Business Administration graduate, Bad Vilbel, Germany (Chief Financial Officer)

Dr. Arndt Schottelius, Physician, Munich, Germany (Chief Development Officer until February 28, 2017)

Malte Peters, Physician, Munich, Germany (Chief Development Officer starting on March 1, 2017)

Dr. Marlies Sproll, Biologist, Munich, Germany (Chief Scientific Officer)

Management Board members do not have mandates on supervisory boards of other publicly listed companies.

## TOTAL REMUNERATION OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD

The remuneration of the Management Board and the Supervisory Board comprised fixed and variable components, as well as other remuneration. If a member is not reappointed and the employment relationship is not extended, the employment contract expires at the end of the contract period without a severance payment. Following the end of the contract, there is a six-month non-compete agreement. During this period, the Management Board member is entitled to a compensation payment of 100 % of the contractually fixed remuneration. In the year 2016, the total remuneration of the Supervisory Board, excluding reimbursements for travel costs, amounted to € 530k (2015: € 529k).

While in the management report the remuneration of the Management Board and Supervisory Board, as members of management in key positions, is presented in accordance with the provisions of the German Corporate Governance Code, the following tables show in detail the information as required according to Sec. 285 number 9 HGB.

**MANAGEMENT BOARD REMUNERATION FOR THE YEARS 2016 AND 2015:**

in €	Dr. Simon Moroney		Jens Holstein	
	Chief Executive Officer		Chief Financial Officer	
	2015	2016	2015	2016
Fixed Compensation	445,736	463,457	302,384	314,405
Fringe Benefits	36,887	34,270	39,735	46,300
One -Year Variable Compensation	238,692	210,873	161,926	143,054
<b>Total Short-Term Employee Benefits</b>	<b>721,315</b>	<b>708,600</b>	<b>504,045</b>	<b>503,759</b>
Service Cost	138,280	142,096	90,800	92,875
<b>Total Benefit Expenses - Post-Employment Benefits</b>	<b>138,280</b>	<b>142,096</b>	<b>90,800</b>	<b>92,875</b>
Multi-Year Variable Compensation <sup>1,2:</sup>				
2011 Long-Term Incentive Program (Vesting Period 4 Years)	163,702	0	112,117	0
2012 Long-Term Incentive Program (Vesting Period 4 Years)	95,271	(21,508)	65,254	(14,732)
2013 Long-Term Incentive Program (Vesting Period 4 Years)	100,367	51,796	68,744	35,460
2014 Long-Term Incentive Program (Vesting Period 4 Years)	105,431	71,049	72,213	48,655
2015 Long-Term Incentive Program (Vesting Period 4 Years)	81,892	111,115	56,091	82,436
2016 Long-Term Incentive Program (Vesting Period 4 Years)	0	105,718	0	69,263
<b>Total Stock-Based Compensation</b>	<b>546,663</b>	<b>318,170</b>	<b>374,419</b>	<b>221,082</b>
<b>Total Compensation</b>	<b>1,406,258</b>	<b>1,168,866</b>	<b>969,264</b>	<b>817,716</b>

<sup>1</sup> The fair value was determined at the grant date in accordance with the provisions of Sec. 285 no. 9a HGB. This table depicts the pro rata share of personnel expenses resulting from share-based payments for the respective financial year. Further details can be found in the Notes.

<sup>2</sup> The amounts presented deviate from those found in the consolidated financial statements because, for IFRS purposes, the fair value was determined according to the provisions of IFRS 2 "Share-based Payment". In the consolidated financial statements, this item shows the pro rata share of personnel expenses resulting from share-based payments for the respective financial year.

Dr. Arndt Schottelius Chief Development Officer		Dr. Marlies Sproll Chief Scientific Officer		Total	
2015	2016	2015	2016	2015	2016
302,384	309,759	302,384	314,405	1,352,888	1,402,026
29,889	28,388	22,954	24,141	129,465	133,099
156,635	140,940	156,635	143,054	713,888	637,921
<b>488,908</b>	<b>479,087</b>	<b>481,973</b>	<b>481,600</b>	<b>2,196,241</b>	<b>2,173,046</b>
94,064	95,473	94,085	92,876	417,229	423,320
<b>94,064</b>	<b>95,473</b>	<b>94,085</b>	<b>92,876</b>	<b>417,229</b>	<b>423,320</b>
112,117	0	112,117	0	500,053	0
65,254	(14,732)	65,254	(14,732)	291,033	(65,704)
68,744	35,460	68,744	35,460	306,599	158,176
72,213	48,655	72,213	48,655	322,070	217,014
56,091	82,436	56,091	82,436	250,165	358,423
0	69,263	0	69,263	0	313,507
<b>374,419</b>	<b>221,082</b>	<b>374,419</b>	<b>221,082</b>	<b>1,669,920</b>	<b>981,416</b>
<b>957,391</b>	<b>795,642</b>	<b>950,477</b>	<b>795,558</b>	<b>4,283,390</b>	<b>3,577,782</b>

#### SUPERVISORY BOARD REMUNERATION FOR THE YEARS 2016 AND 2015:

Supervisory Board in €	Fixed Compensation		Attendance Fees <sup>1</sup>		Total Compensation	
	2016	2015	2016	2015	2016	2015
Dr. Gerald Möller	91,400	93,521	43,400	36,200	134,800	129,721
Dr. Frank Morich <sup>2</sup>	57,240	37,324	26,800	14,200	84,040	51,524
Dr. Marc Cluzel	52,160	50,089	34,600	28,000	86,760	78,089
Karin Eastham	52,160	50,089	24,400	36,800	76,560	86,889
Wendy Johnson <sup>2</sup>	46,160	30,099	33,800	26,400	79,960	56,499
Klaus Kühn <sup>2</sup>	46,160	30,099	21,400	14,200	67,560	44,299
Dr. Walter Blättler <sup>3</sup>	-	16,188	-	13,000	-	29,188
Dr. Daniel Camus <sup>3</sup>	-	16,188	-	8,400	-	24,588
Dr. Geoffrey Vernon <sup>3</sup>	-	20,073	-	8,400	-	28,473
<b>Total</b>	<b>345,280</b>	<b>343,670</b>	<b>184,400</b>	<b>185,600</b>	<b>529,680</b>	<b>529,270</b>

<sup>1</sup> The attendance fee contains expense allowances for the attendance at Supervisory Board and Committee meetings.

<sup>2</sup> Dr. Frank Morich, Wendy Johnson and Klaus Kühn joined the Supervisory Board of MorphoSys AG on May 8, 2015.

<sup>3</sup> Dr. Walter Blättler, Dr. Daniel Camus and Dr. Geoffrey Vernon left the Supervisory Board of MorphoSys AG on May 8, 2015.

There are presently no other agreements with current or former members of the Supervisory Board.

In addition, the members of the Management Board and the Supervisory Board hold the following shares and convertible bonds of MorphoSys AG.

Shares	01/01/2016	Additions	Sales	12/31/2016
<b>Management Board</b>				
Dr. Simon Moroney	495,238	18,976	0	514,214
Jens Holstein	4,000	12,997	9,997	7,000
Dr. Arndt Schottelius <sup>1</sup>	2,000	13,397	5,000	10,397
Dr. Marlies Sproll	50,752	12,997	6,237	57,512
<b>Total</b>	<b>551,990</b>	<b>58,367</b>	<b>21,234</b>	<b>589,123</b>
<b>Supervisory Board</b>				
Dr. Gerald Möller	11,000	0	0	11,000
Dr. Frank Morich	1,000	0	0	1,000
Dr. Marc Cluzel	500	0	0	500
Karin Eastham	2,000	0	0	2,000
Wendy Johnson	500	0	0	500
Klaus Kühn	0	0	0	0
<b>Total</b>	<b>15,000</b>	<b>0</b>	<b>0</b>	<b>15,000</b>

Convertible Bonds	01/01/2016	Additions	Forfeitures	Exercises	12/31/2016
<b>Management Board</b>					
Dr. Simon Moroney	88,386	0	0	0	88,386
Jens Holstein	90,537	0	0	0	90,537
Dr. Arndt Schottelius <sup>1</sup>	60,537	0	0	0	60,537
Dr. Marlies Sproll	60,537	0	0	0	60,537
<b>Total</b>	<b>299,997</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>299,997</b>

Performance Shares	01/01/2016	Additions	Forfeitures	Allocations	12/31/2016
<b>Management Board</b>					
Dr. Simon Moroney	44,164	12,032	0	18,976	37,220
Jens Holstein	30,248	7,883	0	12,997	25,134
Dr. Arndt Schottelius <sup>1</sup>	30,248	7,883	0	12,997	25,134
Dr. Marlies Sproll	30,248	7,883	0	12,997	25,134
<b>Total</b>	<b>134,908</b>	<b>35,681</b>	<b>0</b>	<b>57,967</b>	<b>112,622</b>

<sup>1</sup> Dr. Arndt Schottelius left the Management Board of MorphoSys AG on February 28, 2017.

The Supervisory Board of MorphoSys AG does not hold any stock options, convertible bonds or performance shares.



## RELATED PARTIES

As of December 31, 2016, the Senior Management Group held 136,588 convertible bonds (December 31, 2015: 150,002 bonds) and 82,144 performance shares (December 31, 2015: 85,542 shares), which were granted by the Company. In 2016, an additional long-term incentive plan was granted to the Management Board and Senior Management Group. The Senior Management Group was granted 32,462 performance shares under this plan. In 2016, the Senior Management Group was allocated 30,105 performance shares from the 2012 LTI plan, which reduced the number of performance shares. No convertible bonds were exercised in 2016 (2015: 19,048 bonds). In 2016, a total of 2,554 performance shares were forfeited due to the departure of a beneficiary from MorphoSys.

## COMPENSATION OF THE AUDITOR

At the Company's Annual General Meeting in June 2016, the Supervisory Board was given authorization to appoint PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft (PwC GmbH), Munich, as the auditor.

In the 2016 financial year, PwC GmbH received compensation from MorphoSys in the amount of € 251,582, including audit fees in the amount of € 190,000, fees for other audit-related and valuation services of € 36,832 (audit review of the half-year financial statements) as well as fees for other services in the amount of € 24,750. PwC GmbH did not provide tax consultation services in 2016.

## HUMAN RESOURCES

As of December 31, 2016, MorphoSys AG engaged a total of 333 employees (December 31, 2015: 352) in addition to the four Management Board members and eight trainees (December 31, 2015: nine trainees).

Of these 333 employees, 280 were employed in research and development and 53 in sales, general and administration (December 31, 2015: 297 in R&D and 55 in sales, general and administration). The average number of employees in the 2016 financial year was 342 (2015: 345). Of the 342 average number of employees in 2016, a total of 287 were employed in research and development and 55 in sales, general and administration.

The 333 employees as of December 31, 2016 consisted of 22 senior executives (December 31, 2015: 20) and 311 non-executive employees (December 31, 2015: 332).

## DIVIDEND

In accordance with the resolution of the Annual General Meeting, the accumulated income as of December 31, 2015 was carried forward. The net loss in 2016 was offset against the prior year's accumulated income, resulting in an accumulated loss as of December 31, 2016. In line with the standard practice in the biotechnology industry, MorphoSys does not expect to pay a dividend in the foreseeable future. The majority of the profit generated by the Company is expected to be reinvested in the operating business, particularly in the area of proprietary drug development, in order to create additional shareholder value and to take advantage of growth opportunities.

## **MANDATORY DISCLOSURE IN ACCORDANCE WITH THE GERMAN SECURITIES TRADING ACT (WPHG)**

The Company published the following information regarding voting rights notifications pursuant to Sec. 26 Para. 1 WpHG (status as of December 31, 2016):

### **NOVARTIS AG, ON MARCH 4, 2016**

1. Issuer:  
MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany

2. Reason for notification:  
Acquisition/disposal of shares with voting rights

3. Details of person subject to the notification obligation:  
Novartis AG, Basel, Switzerland

5. Date of which threshold was crossed or reached:  
25.02.2016

6. Total positions  
new:  
% of voting rights attached to shares: 2.99 %  
% of voting rights through instruments: 0 %  
Total of both in %: 2.99 %  
Total number of voting rights of issuer: 26,537,682  
old:  
% of voting rights attached to shares: 4.09 %  
% of voting rights through instruments: n/a %  
Total of both in %: n/a %

7. Notified details of the resulting situation  
ISIN: DE0006632003  
indirect (§ 22 WpHG): 793,949  
indirect (§ 22 WpHG): 2.99 %

8. Information in relation to the person subject to the notification obligation:  
Full chain of controlled undertakings:  
Novartis AG  
Novartis Pharma AG

### **BAILLIE GIFFORD & CO, ON JUNE 3, 2016**

1. Issuer:  
MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany

2. Reason of notification:  
Acquisition/disposal of shares with voting rights

3. Details of person subject to the notification obligation:  
Baillie Gifford & Co, Edinburgh, Scotland

5. Date on which threshold was crossed or reached:  
30.05.2016

6. Total positions  
new:  
% of voting rights attached to shares: 5.90 %  
% of voting rights through instruments: 0 %  
Total of both in %: 5.90 %  
Total number of voting rights of issuer: 26,537,682  
old:  
% of voting rights attached to shares: 5.01 %  
% of voting rights through instruments: 0 %  
Total of both in %: 5.01 %

7. Notified details of the resulting situation  
ISIN: DE0006632003

indirect (§ 22 WpHG): 1565329  
 indirect (§ 22 WpHG): 5.90 %  
 8. Information in relation to the person subject to the notification obligation:  
 Full chain of controlled undertakings:  
 Baillie Gifford & Co  
 Baillie Gifford Overseas Limited; % of voting rights: 5.03 %

#### **FLOSSBACH VON STORCH SICAV, ON JUNE 14, 2016**

1. Issuer:  
 MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany  
 2. Reason of notification:  
 Acquisition/disposal of shares with voting rights  
 3. Details of person subject to the notification obligation:  
 Flossbach von Storch SICAV, Luxemburg, Luxemburg  
 5. Date on which threshold was crossed or reached:  
 07.06.2016  
 6. Total positions  
 new:  
 % of voting rights attached to shares: 4.94 %  
 % of voting rights through instruments: 0 %  
 Total of both in %: 4.94 %  
 Total number of voting rights of issuer: 26,537,682  
 old:  
 % of voting rights attached to shares: 5.67 %  
 % of voting rights through instruments: 0 %  
 Total of both in %: 5.67 %  
 7. Notified details of the resulting situation  
 ISIN: DE0006632003  
 direct (§ 21 WpHG): 1310742  
 direct (§ 21 WpHG): 4,94 %

#### **SCHRODERS PLC, ON AUGUST 9, 2016**

1. Issuer:  
 MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany  
 2. Reason of notification:  
 Acquisition/disposal of shares with voting rights  
 3. Details of person subject to the notification obligation:  
 Schroders plc, London, England  
 5. Date on which threshold was crossed or reached:  
 03.08.2016  
 6. Total positions  
 new:  
 % of voting rights attached to shares: 3.02 %  
 % of voting rights through instruments: 0 %  
 Total of both in %: 3.02 %  
 Total number of voting rights of issuer: 26,537,682  
 old:  
 % of voting rights attached to shares: n/a %  
 % of voting rights through instruments: n/a %  
 Total of both in %: n/a %  
 7. Notified details of the resulting situation  
 ISIN: DE0006632003  
 indirect (§ 22 WpHG): 801,207

indirect (§ 22 WpHG): 3.02 %

8. Information in relation to the person subject to the notification obligation:

Full chain of controlled undertakings:

Schroder Administration Limited

Schroder Investment Management Limited; % of voting rights: 3.02 %

Schroders Korea Limited

Schroders plc

Schroder Administration Limited

Schroder International Holdings Limited

Schroder International Finance B.V.

Schroder Investment Management (Luxembourg) S.A.

#### **SCHRODER INTERNATIONAL SELECTION FUND, ON AUGUST 17, 2016**

1. Issuer:

MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany

2. Reason of notification:

Acquisition/disposal of shares with voting rights

Other reason: Voluntary group disclosure

3. Details of person subject to the notification obligation:

Schroder International Selection Fund, London, England

5. Date on which threshold was crossed or reached:

09.08.2016

6. Total positions

new:

% of voting rights attached to shares: 3.71 %

% of voting rights through instruments: 0 %

Total of both in %: 3.71 %

Total number of voting rights of issuer: 26,537,682

old:

% of voting rights attached to shares: 3.02 %

% of voting rights through instruments: 0.00 %

Total of both in %: 3.02 %

7. Notified details of the resulting situation

ISIN: DE0006632003

indirect (§ 22 WpHG): 984076

indirect (§ 22 WpHG): 3.71 %

8. Information in relation to the person subject to the notification obligation:

Full chain of controlled undertakings:

Schroders plc

Schroder Administration Limited

Schroder Investment Management Limited; % of voting rights: 3.71 %

Schroders Korea Limited

Schroders plc

Schroder Administration Limited

Schroder International Holdings Limited

Schroder International Finance B.V.

Schroder Investment Management (Luxembourg) S.A.; % of voting rights: 3.03 %

#### **SCHRODER INTERNATIONAL SELECTION FUND, ON AUGUST 17, 2016**

1. Issuer:

MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany

2. Reason of notification:

Acquisition/disposal of shares with voting rights

3. Details of person subject to the notification obligation:  
 Schroder International Selection Fund, London, England  
 5. Date on which threshold was crossed or reached:  
 09.08.2016  
 6. Total positions  
 new:  
 % of voting rights attached to shares: 3.03 %  
 % of voting rights through instruments: 0 %  
 Total of both in %: 3.03 %  
 Total number of voting rights of issuer: 26,537,682  
 old:  
 % of voting rights attached to shares: n/a %  
 % of voting rights through instruments: n/a %  
 Total of both in %: n/a %  
 7. Notified details of the resulting situation  
 ISIN: DE0006632003  
 direct (§ 21 WpHG): 803,543  
 direct (§ 21 WpHG): 3.03 %

#### **FLOSSBACH VON STORCH AG, ON AUGUST 17, 2016**

1. Issuer:  
 MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany  
 2. Reason of notification:  
 Acquisition/disposal of shares with voting rights  
 3. Details of person subject to the notification obligation:  
 Flossbach von Storch AG, Köln, Germany  
 5. Date on which threshold was crossed or reached:  
 09.08.2016  
 6. Total positions  
 new:  
 % of voting rights attached to shares: 4.81 %  
 % of voting rights through instruments: 0 %  
 Total of both in %: 4.81 %  
 Total number of voting rights of issuer: 26,537,682  
 old:  
 % of voting rights attached to shares: 5.78 %  
 % of voting rights through instruments: n/a %  
 Total of both in %: n/a %  
 7. Notified details of the resulting situation  
 ISIN: DE0006632003  
 indirect (§ 22 WpHG): 1277100  
 indirect (§ 22 WpHG): 4.81 %  
 8. Information in relation to the person subject to the notification obligation:  
 Full chain of controlled undertakings:  
 Flossbach von Storch AG  
 Flossbach von Storch Invest A.A.; % of voting rights: 4.81 %

#### **FLOSSBACH VON STORCH SICAV, ON AUGUST 17, 2016**

1. Issuer:  
 MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany  
 2. Reason of notification:  
 Acquisition/disposal of shares with voting rights

## 3. Details of person subject to the notification obligation:

Flossbach von Storch SICAV, Luxemburg, Luxemburg

## 5. Date on which threshold was crossed or reached:

10.08.2016

## 6. Total positions

new:

% of voting rights attached to shares: 2.86 %

% of voting rights through instruments: 0 %

Total of both in %: 2.86 %

Total number of voting rights of issuer: 26,537,682

old:

% of voting rights attached to shares: 4.94 %

% of voting rights through instruments: 0 %

Total of both in %: 4.94 %

## 7. Notified details of the resulting situation

ISIN: DE0006632003

direct (§ 21 WpHG): 759494

direct (§ 21 WpHG): 2,86 %

**FLOSSBACH VON STORCH AG, ON SEPTEMBER 27, 2016**

## 1. Issuer:

MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany

## 2. Reason of notification:

Acquisition/disposal of shares with voting rights

## 3. Details of person subject to the notification obligation:

Flossbach von Storch AG, Köln, Germany

## 5. Date on which threshold was crossed or reached:

19.09.2016

## 6. Total positions

new:

% of voting rights attached to shares: 2.96 %

% of voting rights through instruments: 0 %

Total of both in %: 2.96 %

Total number of voting rights of issuer: 26,537,682

old:

% of voting rights attached to shares: 4.81 %

% of voting rights through instruments: 0 %

Total of both in %: 4.81 %

## 7. Notified details of the resulting situation

ISIN: DE0006632003

indirect (§ 22 WpHG): 786351

indirect (§ 22 WpHG): 2.96 %

## 8. Information in relation to the person subject to the notification obligation:

Full chain of controlled undertakings:

Flossbach von Storch AG

Flossbach von Storch Invest S.A.

**BAILLIE GIFFORD & CO, ON NOVEMBER 21, 2016**

## 1. Issuer:

MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany

## 2. Reason of notification:

Other reason: Voluntary Group Disclosure due to Issuer increasing the number of voting rights

## 3. Details of person subject to the notification obligation:

Baillie Gifford & Co, Edinburgh, Scotland

5. Date on which threshold was crossed or reached:  
17.11.2016

6. Total positions  
new:  
% of voting rights attached to shares: 5.41 %  
% of voting rights through instruments: 0 %  
Total of both in %: 5.41 %  
Total number of voting rights of issuer: 29,159,770

alt:  
% of voting rights attached to shares: 5.90 %  
% of voting rights through instruments: 0 %  
Total of both in %: 5.90 %

7. Notified details of the resulting situation  
ISIN: DE0006632003  
indirect (§ 22 WpHG): 1577507  
indirect (§ 22 WpHG): 5.41 %

8. Information in relation to the person subject to the notification obligation:  
Full chain of controlled undertakings:  
Baillie Gifford  
Baillie Gifford Overseas Limited; % of voting rights: 4.71 %

#### **MARK LAMPERT, ON NOVEMBER 25, 2016**

1. Issuer:  
MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany

2. Reason of notification:  
Acquisition/disposal of shares with voting rights

3. Details of person subject to the notification obligation:  
Mr. Mark N. Lampert

5. Date on which threshold was crossed or reached:  
17.11.2016

6. Total positions  
new:  
% of voting rights attached to shares: 4.17 %  
% of voting rights through instruments: 0 %  
Total of both in %: 4.17 %  
Total number of voting rights of issuer: 29,159,770

old:  
% of voting rights attached to shares: n/a %  
% of voting rights through instruments: n/a %  
Total of both in %: n/a %

7. Notified details of the resulting situation  
ISIN: DE0006632003  
indirect (§ 22 WpHG): 1214982  
indirect (§ 22 WpHG): 4.17 %

8. Information in relation to the person subject to the notification obligation:  
Full chain of controlled undertakings:  
Mark N. Lampert  
BVF Inc.  
BVF Partners, L.P.  
Biotechnology Value Fund II, L.P.  
Mark N. Lampert  
BVF Inc.  
BVF Partners, L.P.  
BVF Partners OS Ltd.  
Biotechnology Value Trading Fund OS L.P.

**CELGENE CORPORATION, ON NOVEMBER 29, 2016**

## 1. Issuer:

MorphoSys AG, Lena-Christ-Straße 48, 82152 Martinsried/Planegg, Germany

## 2. Reason of notification:

Other reason: Voluntary Group Disclosure due to Issuer increasing the number of voting rights

## 3. Details of person subject to the notification obligation:

Celgene Corporation, Wilmington, Delaware 19801, United States of America

## 5. Date on which threshold was crossed or reached:

17.11.2016

## 6. Total positions

new:

% of voting rights attached to shares: 2.73 %

% of voting rights through instruments: 0 %

Total of both in %: 2.73 %

Total number of voting rights of issuer: 29,159,770

old:

% of voting rights attached to shares: 3.24 %

% of voting rights through instruments: n/a %

Total of both in %: n/a %

## 7. Notified details of the resulting situation

ISIN: DE0006632003

indirect (§ 22 WpHG): 797150

indirect (§ 22 WpHG): 2.73 %

## 8 Information in relation to the person subject to the notification obligation:

Full chain of controlled undertakings:

Celgene Corporation

Celgene International Inc.

Celgene Netherlands BV

Celgene Netherlands II BV

Celgene Switzerland SA

Celgene International Sàrl

Celgene Switzerland Investment Sàrl

Celgene Alpine Investment Co., LLC



## Appropriation of Accumulated Profit/Loss

As of December 31, 2016, MorphoSys AG's accumulated loss amounted to € 45,353,158.76 (December 31, 2015: accumulated profit of € 14,857,059.50).

In €	2016
a. Allocation to Shareholders	0.00
b. Allocation to Other Earnings Reserves	0.00
c. Loss Carried Forward	(45,353,158.76)
d. Accumulated Deficit	(45,353,158.76)

## Subsequent Events

In early January 2017, MorphoSys announced that the Company's Supervisory Board has appointed Dr. Malte Peters as new Chief Development Officer. Dr. Peters will assume the position on March 1, 2017 and will succeed Dr. Arndt Schottelius, who is leaving the Company to pursue other opportunities. Dr. Schottelius has been Chief Development Officer until February 28, 2017. Dr. Peters joins MorphoSys from Sandoz, a subsidiary of Novartis, where he served as Global Head, Clinical Development Biopharmaceuticals. With effect from March 1, 2017, Dr. Peters is entitled for the period of one year to request the transfer of treasury shares held by the Company to himself up to a total amount of € 500,000.

In February 2017, MorphoSys announced that it has added a second patent with US Patent Number 9,200,061 to its lawsuit against Janssen Biotech, and Genmab, A/S. This patent claims methods of treating hematologic cancer associated with the undesired presence of CD38-positive cells by administering antibodies that bind to a specific region of the target molecule, CD38. In a hearing that took place on February 6, 2017 the District Court granted MorphoSys's request to add the 9,200,061 patent to the case.

Also in February 2017, MorphoSys announced that its fully owned subsidiary Lanthio Pharma B.V., Groningen, Netherlands, has initiated a phase 1 clinical study with MOR107. MOR107, a selective agonist of the angiotensin II receptor type 2, is a lanthipeptide based on Lanthio Pharma's proprietary technology platform and the first lanthipeptide in MorphoSys's clinical pipeline. The goal of the trial is to evaluate safety, tolerability, pharmacokinetics and pharmacodynamics in healthy male volunteers.

In March 2017, MorphoSys announced that its partner Roche plans to initiate a new pivotal phase 3 program with gantenerumab in patients with prodromal to mild Alzheimer's disease. Gantenerumab is a monoclonal antibody directed against beta amyloid based on MorphoSys's HuCAL antibody library. MorphoSys was informed that Roche intends to commence preparations for two studies and that Roche expects to start the trials later in 2017.

Also in March 2017, MorphoSys announced that its licensee Janssen has reported positive results from two phase 3 clinical studies examining guselkumab, a fully human antibody directed against IL-23 identified from MorphoSys's HuCAL antibody library, in patients with moderate to severe plaque

psoriasis. Janssen has announced to present the data from its VOYAGE 2 and NAVIGATE studies at the American Academy of Dermatology (AAD) 2017 annual meeting in Orlando, Florida/USA, from March 3-7, 2017.

Apart from that, no events occurred after the reporting date of December 31, 2016 that require reporting.

## Responsibility Statement

To the best of our knowledge, and in accordance with the applicable reporting principles, the financial statements give a true and fair view of the Company's net assets, financial position and results of operations, and the management report provides a fair review of the development and performance of the business and the position of the Company together with a description of the principal opportunities and risks associated with the Company's expected development.

Planegg, March 6, 2017

Dr. Simon Moroney  
Chief Executive Officer

Jens Holstein  
Chief Financial Officer

Dr. Malte Peters  
Chief Development Officer

Dr. Marlies Sproll  
Chief Scientific Officer

## Statement of Fixed Assets

		Aquisition and Production Cost			
		01/01/2016 in €	Additions in €	Disposals in €	12/31/2016 in €
<b>A. Fixed Assets</b>					
<b>I. Intangible Assets</b>					
	Paid concessions, commercial property rights and similar rights and assets and licenses to such rights and assets				
1.		84,296,943	56,470	500,000	83,853,413
		<b>84,296,943</b>	<b>56,470</b>	<b>500,000</b>	<b>83,853,413</b>
<b>II. Tangible Assets</b>					
	Land, leasehold rights and buildings, including leasehold improvements				
1.		1,258,697	432,598	0	1,691,295
2.	Other equipment, furniture and fixtures	15,218,092	2,002,134	226,023	16,994,203
		<b>16,476,789</b>	<b>2,434,732</b>	<b>226,023</b>	<b>18,685,498</b>
<b>III. Financial Assets</b>					
1.	Shares in affiliated companies	32,124,278	7,500,000	0	39,624,278
		<b>32,124,278</b>	<b>7,500,000</b>	<b>0</b>	<b>39,624,278</b>
		<b>132,898,010</b>	<b>9,991,202</b>	<b>726,023</b>	<b>142,163,189</b>

	Accumulated Depreciation				Net Book Values	
	01/01/2016 in €	Additions in €	Write-offs in €	Disposals in €	12/31/2016 in €	12/31/2015 in €
	46,367,562	804,453	10,141,187	0	57,313,202	37,929,381
	<b>46,367,562</b>	<b>804,453</b>	<b>10,141,187</b>	<b>0</b>	<b>57,313,202</b>	<b>37,929,381</b>
	1,212,347	50,836	0	0	1,263,183	46,350
	11,969,746	1,651,017	0	225,076	13,395,687	3,248,346
	<b>13,182,093</b>	<b>1,701,853</b>	<b>0</b>	<b>225,076</b>	<b>14,658,870</b>	<b>3,294,696</b>
	0	0	0	0	0	39,624,278
	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>39,624,278</b>
	<b>59,549,655</b>	<b>2,506,306</b>	<b>10,141,187</b>	<b>225,076</b>	<b>71,972,072</b>	<b>73,348,355</b>

## Auditor's Report

### Auditor's Report

We have audited the annual financial statements, comprising the balance sheet, the statement of income and the notes, together with the bookkeeping system and the management report of the MorphoSys AG, Planegg, for the business year from January 1 to December 31, 2016. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law and supplementary articles of incorporation are the responsibility of the Company's Board of Managing Directors. Our responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on our audit.

We conducted our audit of the annual financial statements in accordance with Article 317 of the German Commercial Code and German generally accepted standards for the audit of financial statements promulgated by the Institute of Public Auditors in Germany. Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with (German) principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Company and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by the Company's Board of Managing Directors, as well as evaluating the overall presentation of the annual financial statements and management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the annual financial statements comply with the legal requirements and supplementary provisions of the articles of incorporation and give a true and fair view of the net assets, financial position and results of operations of the Company in accordance with German principles of proper accounting. The management report is consistent with the annual financial statements, complies with legal requirements, as a whole provides a suitable view of the Company's position and suitably presents the opportunities and risks of future development.

Munich, March 6, 2017

**PricewaterhouseCoopers GmbH**  
**Wirtschaftsprüfungsgesellschaft**

Dietmar Eglauer  
Auditor

ppa. Bodo Kleinschrod  
Auditor

# Imprint

## Contact Information

### **CORPORATE COMMUNICATIONS AND INVESTOR RELATIONS**

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These separate financial statements are also available in German and are available on our website.

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