

Annual Report 2005

CellaVision AB (publ)

2005 Annual Report for CellaVision AB (publ)

Corporate ID 556500-0998

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SUMMARY OF 2005

- ▶ Net sales increase of 30% to SEK 39 million (29.8)
- ▶ Operating loss improved by SEK 10 million to SEK -16.5 million (-26.6) and net loss to SEK -16.7 million (-24.9)
- ▶ Net loss per share amounted to SEK -0.81 (-1.31)
- ▶ Monthly average cash flow before changes in working capital amounted to MSEK -0.7 (-1.6)
- ▶ The Swedish Industrial Development Fund (IF) set-off loan of SEK 10 million by payment in new shares
- ▶ New share issue added CellaVision SEK 15.2 million in proceeds
- ▶ Cash and bank holding at the year-end amounted to MSEK 17.6 (19.2)

Key data and ratios All amounts in KSEK	2005	2004	2003	2002	2001
Net sales	39 017	29 843	14 974	13 669	8 043
Operating loss	-16 489	-26 597	-39 838	-49 433	-53 037
Cash flow	-17 001	-23 944	-33 844	-44 635	-65 593
Shareholders' equity	26 561	18 148	8 069	48 664	82 604
Cash	17 588	19 157	5 068	39 239	49 654
Equity/assets ratio	57%	40%	26%	66%	72%
Number of employees	32	30	37	46	49

SHARE CAPITAL AND OWNERSHIP STRUCTURE

Ownership structure

The table below presents the CellaVision ownership structure on December 31 2005, when CellaVision had about 700 shareholders.

Shareholders	No of shares	Subscribed and paid shares ¹⁾	Total number	Ownership in %
H&B Capital LP	3 705 373	367 766	4 073 139	17,1
The Swedish Industrial Development Fund	2 974 026	613 231	3 587 257	15,0
Christer Fähræus with companies	1 882 445	181 378	2 063 823	8,6
Metallica Förvaltnings AB	1 487 105	251 862	1 738 967	7,3
Life Equity Sweden KB	1 479 900	146 883	1 626 783	6,8
Företagskapital Kompanjonfond KB	1 578 786	-	1 578 786	6,6
SIF	900 000	290 000	1 190 000	5,0
3i Group PLC	1 000 000	-	1 000 000	4,2
Other	6 571 647	421 145	6 992 792	29,4
TOTALT	21 579 282	2 272 265	23 851 547	100

1) Subscribed and paid shares as per 2005-12-31.

Warrants

In the beginning of 2005 CellaVision had one warrant program with subscription rights equivalent to 600,000 shares. This program expired December 15 2005. The closing balance of outstanding warrants was 0 as per 2005-12-31.

Share capital

On December 31 2005, CellaVision held 23,579,282 shares to a nominal value of SEK 0.15 per share, in total a share capital of KSEK 3,537. In the new share issue 2005 there was an over-subscription and a guarantee remuneration. These parts were not registered until January 2006. Regardless of the number of shares held by one shareholder, each share gives the shareholder the right to one vote. Each vote may be used at the Annual General Meeting. All shares have equal right to shares in the company's assets and profit. The table below illustrates the development since the inception of CellaVision:

All amounts in KSEK

Year	Transaction	Number of new shares	Acc. number of shares	Increase in share capital	Acc. share capital	Funds from new share issue	Acc. funds from share issues
1994	New issue	500	500	50	50	50	50
1996	New issue	150	650	15	65	1 500	1 550
1996	New issue	110	760	11	76	1 500	3 050
1997	Bonus issue	760	1 520	76	152	-	3 050
1997	Split 1000:1	1 518 480	1 520 000	0	152	-	3 050
1997	New issue	122 000	1 642 000	12	164	4 066	7 116
1997	New issue	75 000	1 717 000	8	172	1 500	8 616
1998	New issue	100 000	1 817 000	10	182	4 500	13 116
1998	New issue	158 000	1 975 000	16	198	8 690	21 806
1999	New issue	1 296 750	3 271 750	130	327	25 935	47 741
1999	New issue	333 332	3 605 082	33	361	10 000	57 741
2000	Bonus issue	0	3 605 082	180	541	-	57 741
2000	New issue	1 354 454	4 959 536	203	744	74 495	132 236
2000	Warrants	2 500	4 962 036	0	744	150	132 386
2000	Warrants	1 000	4 963 036	0	744	40	132 426
2000	Warrants	2 000	4 965 036	0	745	80	132 506
2000	Warrants	22 000	4 987 036	3	748	1 100	133 606
2000	Warrants	88 000	5 075 036	13	761	4 400	138 006
2000	Warrants	3 000	5 078 036	0	762	120	138 126
2000	Warrants	11 500	5 089 536	2	763	690	138 816
2001	Warrants	15 000	5 104 536	2	766	900	139 716
2001	Bonus issue	5 104 536	10 209 072	766	1 531	-	139 716
2001	New issue	2 656 070	12 865 142	399	1 930	73 042	212 758
2002	Warrants	94 610	12 959 752	14	1 944	1 892	214 650
2002	New issue	545 455	13 505 207	82	2 026	15 000	229 650
2003	-	-	13 505 207	-	2 026	-	229 650
2004	New issue	6 645 504	20 150 711	997	3 023	33 227	262 877
2005	New issue	3 428 571	23 579 282	514	3 537	24 000	286 877
2006	New issue	272 265	23 851 547	40	3 577	1 906	288 783

THE BOARD'S REPORT

The Board and the CEO of CellaVision AB (publ), corporate ID 556500-0998, submit this report for the financial year January 1 2005 to December 31 2005.

The operation

CellaVision AB (publ) is an emerging high-tech company with a core competence in development of software for automatic image analysis of cells and cell changes and for applications in health and medical care. The company offers cutting-edge expertise in sophisticated image processing, image analysis and automated microscopy. The company currently focuses on the following three products: CellaVision™ DM96, CellaVision™ DM8 and DiffMaster™ Octavia. CellaVision DM and DiffMaster Octavia are systems used to facilitate blood-cell analysis. CellaVision also markets two software products, CellaVision™ Diff IQ and CellAtlas™. CellaVision Diff IQ is a combination of educational and proficiency tool which allows the laboratory to ensure that staff is trained to report differential results which are consistent with laboratory standards and CellAtlas is a Web-based reference cell image library to be used for educational purposes.

The company's products are sold to hospital-laboratories and independent commercial laboratories. Today CellaVision is represented in Europe, the U.S. and to some extent in Asia. CellaVision markets and sells its products through a number of exclusive distributors except for the Nordic market where CellaVision sell direct. A wholly owned subsidiary in USA, CellaVision Inc. serves as a support-unit to the American distributor.

CellaVision's vision is to create a new global de facto standard for digital microscopy analysis, thereby contributing to improving the quality of medical treatment and more cost-efficient health care.

Sales, results, and investments

Net sales amounted to SEK 39.0 million (29.8) – an increase of 31 percent compared to last year. The European market accounts for 64% (47) of the turnover, the US market for 30% (53), and the remaining world market for 6% (0). The gross profit amounted to SEK 19.6 million (10.5). The gross profit has been affected by a write-down of inventory for DiffMaster Octavia with SEK 1.4 million (1.2). The gross profit in percent of sales amounted to 50% (35). The considerable improvement in gross profit is due to the lower costs of production of the products Cellavision DM8 and Cellavision DM96 as compared to their predecessor DiffMaster Octavia. The net loss for the Group

amounted to SEK -16.7 million (-24.9). The overhead expenses for the Group amounted to SEK 36.1 million (37.1).

During 2005 the company has not undertaken any development projects in phases in which expenditures should be capitalized. Depreciations of SEK 3.8 million (3.8) on capitalized development expenditures, were booked as costs of goods sold. Capital expenditures amounted to SEK 0.1 million (0.1) during the period.

Financial risks

Financing

CellaVision concluded a new share issue in December 2005. This share issue of MSEK 14 was over subscribed and it gave the company a capital injection of MSEK 15,2. By this issue The Swedish Industrial Fund became the second largest owner after H&B Capital. The proceeds will be used to:

- Finance the continued commercial exploitation of the Company's products in the US, Europe and Asia.
- Improve competitiveness by reducing production costs in part through a new hardware platform.
- Develop the payment model towards a lower customer investment, however with annual licensing fees, in order to enter the market more quickly and to increase the share of recurring income from customers.
- Continue product development within the area of hematology, specifically bone marrow and body fluids.

Besides the above items, the proceeds will be used to cover the company's working capital needs.

Foreign currency and credit risks

The company operations carry a number of financial risks which are handled by the finance policy taken by the board. The major part of the company expenses is tied to the Swedish crown (SEK), while customer invoicing and production costs are mainly in foreign currencies (predominantly USD, Euro and CHF), which increases the company's exposure to currency fluctuations. All contractual inflows are secured to 100 percent. Forecasted exposure is not secured, with consideration to historical uncertainty in order income. The company believes there is no significant credit risk in relation to any specific customer or counterpart. Customers in the international market are well established hematology companies and distributors with high

solvency. In the Nordic region the customers are hospitals with public financing.

Liquid assets and financing

Liquid assets amounted to SEK 17.6 million (19.2) at the end of the year. The negative cash flow before changes in working capital has been reduced by 50% compared to the corresponding period in 2004. The average monthly cash flow before changes in working capital, amounted to SEK -0.7 million (1.6) throughout the year.

In the last quarter, a new share issue was directed to The Swedish Industrial Development Fund (IF). This new share issue of SEK 10 million was set-off against a former loan from IF at the same amount. In connection to this, the company issued a public new share issue. The new share issue raised SEK 15.2 million. As a result of these share issues the Swedish Industrial Development Fund (IF) is now the second largest share holder with 15% ownership. The largest share holder is H&B Capital with 17,1% ownership.

During the fourth quarter, the company amortized the loan of SEK 2.2 million from Landstingets Fond för Teknikupphandling och Produktutveckling (LFTP), that has been in place since 1997. Instead the company took a new loan of the same amount from Nordea Bank.

The consolidated shareholder's equity as per December 31 2005 amounted to MSEK 26.6 (18.1) and the total equity per share to SEK 1.29 (0.95).

Market and sales

Sales continue to grow well with a total increase of 30% compared to 2004. An even stronger sales growth was expected, but was not met due to lower sales than expected in the USA. The fourth quarter was therefore not as strong as earlier years. Europe and Asia account for about 75% of system sales during the year. The U.S. market sales pace is lower than last year when the U.S. represented about 50% of the total sales volume in the same period. This can be explained by a lower sales level within the diagnostic industry in general and that the first CellaVision orders in the U.S. in 2004 were driven by orders from customers that can be seen as "early adopters", i.e., customers that are very receptive to new technology.

CellaVision™ DM8, which was launched in March, is showing positive response on the market. The product is developed for the mid-sized laboratories with its semi-automated slide handling. The CellaVision DM8 can share database with CellaVision™ DM96, installed at the same or at a remote location, allowing centralized database management.

In the Nordic region, the hospitals in Odense and Hvidovre (Denmark), Helsinki University Hospital HUCS (Finland), and the University Hospital in Trondheim (Norway) are new customers using CellaVision products. Rigshospitalet in Copenhagen is the first customer to have replaced two DiffMaster instruments with a CellaVision DM96.

New distribution agreements in several new countries have been signed, amongst others France, Italy, the United Arab Emirates (UAE), and a number of countries in Asia Pacific.

Over six hundred laboratories have installed the evaluation version of CellaVision™ Diff IQ. The Diff IQ software is a combination of educational and proficiency tool which allows the laboratory to ensure that staff working with morphology is trained to report differential results which are consistent with laboratory standards. The program is available for download on the CellaVision webpage. After evaluation, the program usage can be extended by an annual license fee. In addition, databases with interesting patient cases can be purchased.

Purchase and Production

Purchases has to largest extent been handled within the own organization. The production of components is outsourced to a number of sub-contractors while final assembly and quality control is handled by CellaVision AB, Lund. During the year CellaVision signed a manufacturing agreement with Kitron AB in Flen for complete production of CellaVision DM96. The product has previously been manufactured in Switzerland with final assembly and tests performed by CellaVision in Lund. CellaVision has selected a certified producer that will make the assembly and the final testing of the CellaVision DM96 according to the European IVDD and the U.S. FDA requirements. The site change is primarily related to sales development and the significant volume increase. The change will also have a positive impact of manufacturing cost. The manufacturing transfer of CellaVision DM96 to Kitron Flen is now being implemented. The objective is to have the system in production at Kitron in the second quarter 2006.

R&D

The increased sales and number of customer sites have resulted in that significant development resources have been related to improving and customising the existing product portfolio and dealing with changes and quality deficiency in components. Resources have also been used to reduce manufacturing costs. The company has finalized development and released into production the new software 1.4 for the products CellaVision DM96 and DM8. This new release contains new and further improved features. The release also contains

the new software product CellaVision Diff IQ, a tool for education and proficiency testing. The company has during the second half year adapted the CellaVision DM96 to handle glass slides with two-dimensional bar codes. Also, the software used in CellaVision DM96 has been adapted to a contiguous research application to peripheral blood.

CellaVision has a patent portfolio containing 17 innovations, which so far have generated 21 patents.

R&D expenses during 2005 were MSEK 11.5 (14.3), nothing has been capitalized during the year (0).

Organization and employees

The CellaVision Group consists of CellaVision AB, the parent company, and two subsidiaries: CellaVision International AB and CellaVision Inc. At year-end, the Group employed 32 (30) persons in CellaVision AB and CellaVision Inc. CellaVision International AB has no employees.

The Board

The board held 12 minuted meetings in 2005; two were held as teleconferences. The board has

appointed a committee to deal with financing issues. Each month, the board receives reports on the company's activities, cash flow, profit/loss, and financial position.

Proposed treatment of loss—Parent company

Balance brought forward	0
The year's loss	20 853 155
Total	20 853 155

The Board and the CEO propose that the accumulated loss of SEK 20,853,155 will be balanced against the share premium reserve, which will be reduced by an equivalent amount. On December 31 2005, the consolidated accumulated loss amounted to KSEK 21,200. Appropriation of restricted reserves in the other group companies is not necessary.

INCOME STATEMENT

Amount in KSEK	Note	<i>Group</i>		<i>Parent company</i>	
		JAN 1 – DEC 31 2005	JAN 1 – DEC 31 2004	JAN 1 – DEC 31 2005	JAN 1 – DEC 31 2004
Net sales	1	39 017	29 843	37 187	27 529
Cost of goods sold	8, 9	-19 390	-19 338	-18 912	-19 090
Gross profit		19 627	10 505	18 275	8 439
Selling expenses	9	-13 556	-11 432	-16 794	-14 200
Administrative expenses		-10 795	-11 274	-10 794	-11 273
Research and development expenses		-11 470	-14 305	-11 470	-14 305
Other operating expenses		-295	-91	-175	-245
Operating loss	2, 3, 4, 5, 6, 7, 8	-16 489	-26 597	-20 958	-31 584
<i>Income/loss from financial investments</i>					
Interest income	10	163	1 920	512	1 912
Interest expenses		-407	-216	-407	-216
Loss after financial items		-16 733	-24 893	-20 853	-29 888
Tax	11	0	0	0	0
Net loss		-16 733	-24 893	-20 853	-29 888
Earnings per share		-0,81	-1,31	-1,01	-1,57
Diluted earnings per share		-0,81	-1,31	-1,01	-1,57

BALANCE SHEET – ASSETS

Amount in KSEK	Note	Group		Parent company	
		31 DEC 2005	31 DEC 2004	31 DEC 2005	31 DEC 2004
Subscribed, not paid, capital		1 266	0	1 266	0
Fixed assets					
<i>Intangible fixed assets</i>					
Capitalized development expenditures	5	881	4 645	881	4 645
Other intangible assets	6	0	0	3 638	7 275
Total intangible fixed assets		881	4 645	4 519	11 920
<i>Tangible fixed assets</i>					
Equipment	7	1 302	2 398	963	1 489
Total tangible fixed assets		1 302	2 398	963	1 489
<i>Long- term financial assets</i>					
Shares in group companies	12	0	0	100	100
Total long term financial assets		0	0	100	100
Total fixed assets		2 183	7 043	5 582	13 509
Current assets					
<i>Inventories</i>					
Finished products and goods for resale		12 432	6 482	12 432	6 482
Advances to suppliers		1 021	2 276	1 021	2 276
Total inventories		13 453	8 758	13 453	8 758
<i>Current receivables</i>					
Accounts receivable		9 101	6 426	8 904	6 318
Other receivables		1 863	2 714	1 802	2 670
Receivables, Group companies		0	0	54	45
Prepaid expense and accrued income	13	786	1 018	786	1 018
Total current receivables		11 750	10 158	11 546	10 051
Cash and bank deposits		17 588	19 157	17 285	18 244
Total current assets		42 791	38 073	42 284	37 053
TOTAL ASSETS		46 240	45 116	49 132	50 562

BALANCE SHEET – SHAREHOLDERS' EQUITY & LIABILITIES

Amount in KSEK	Note	Group		Parent company	
		31 DEC 2005	31 DEC 2004	31 DEC 2005	31 DEC 2004
Shareholders' equity					
<i>Restricted equity</i>					
Share capital ¹		3 537	3 023	3 537	3 023
Not registered share capital		40	0	40	0
Other statutory reserves		2 207	2 207	2 187	2 187
Additional paid-in capital		41 977	47 785	41 977	47 785
Total restricted equity		47 761	53 015	47 741	52 995
<i>Retained losses</i>					
Balance brought forward		-4 467	-9 974	0	0
The year's result		-16 733	-24 893	-20 853	-29 888
Total retained losses		-21 200	-34 867	-20 853	-29 888
Total shareholders' equity		26 561	18 148	26 888	23 107
Provisions		1 240	1 020	1 240	1 020
<i>Long-term liabilities</i>					
Interest bearing payable to credit institutions ²	14	0	10 000	0	10 000
Total long-term liabilities		0	10 000	0	10 000
<i>Current liabilities</i>					
Liabilities to credit institutions ²	14	8 793	6 897	8 793	6 897
Accounts payable		3 147	4 021	3 151	3 972
Other liabilities		409	378	383	339
Liabilities, Group companies		0	0	3 120	1 316
Accrued expense and prepaid income	15	6 090	4 652	5 557	3 911
Total current liabilities		18 439	15 948	21 004	16 435
TOTAL SHAREHOLDERS' EQUITY & LIABILITIES		46 240	45 116	49 132	50 562
Pledged assets	16	10 553	8 045	10 553	8 045

¹ The registered share capital in the parent company is distributed, as per December 31 2005, on 23 579 282 shares at a nominal value of SEK 0.15 each.

² Total interest-bearing liabilities as per December 31 2005 amounted to 8.793 (6.897)

Changes in shareholders' equity

Group	Share capital 1,2	Other statutory reserves	Additional paid-in capital	Retained losses	Total
Shareholders' equity 2003-12-31	2 026	2 207	57 141	-53 305	8 069
New share issue	997	0	32 231	0	33 228
Fundraising costs	0	0	- 600	0	- 600
VAT refund re. fundraising costs in prior periods	0	0	2 028	0	2 028
Appropriation of losses	0	0	- 42 139	42 139	0
The year's result	0	0	0	- 24 893	- 24 893
Transfer between restricted equity and retained losses	0	0	- 876	876	0
Translation difference	0	0	0	316	316
Shareholders' equity 2004-12-31	3 023	2 207	47 785	-34 867	18 148
New share issue	554	0	24 725	0	25 279
Fundraising costs	0	0	-645	0	-645
Appropriation of losses	0	0	-29 888	29 888	0
The year's result	0	0	0	-16 733	-16 733
Translation difference	0	0	0	512	512
Shareholders' equity 2005-12-31	3 577	2 207	41 977	-21 200	26 561
Parent company	Share capital 1,2	Other statutory reserves	Additional paid-in capital	Retained losses	Total
Shareholders' equity 2003-12-31	2 026	2 187	56 265	-42 139	18 339
New share issue	997	0	32 231	0	33 228
Fundraising costs	0	0	- 600	0	- 600
VAT refund re. fundraising costs in prior periods	0	0	2 028	0	2 028
Appropriation of losses	0	0	- 42 139	42 139	0
The year's result	0	0	0	- 29 888	- 29 888
Shareholders' equity 2004-12-31	3 023	2 187	47 785	-29 888	23 107
New share issue	554	0	24 725	0	25 279
Fundraising costs	0	0	-645	0	-645
Appropriation of losses	0	0	-29 888	29 888	0
The year's result	0	0	0	-20 853	-20 853
Shareholders' equity 2005-12-31	3 577	2 187	41 977	-20 853	26 888

¹ Each share correspond to one vote per share and each shareholder, with the right to vote, may use all its voting rights without limitations at the annual general meeting. All shares bestow the same right to the Company net assets and result.

² SEK 40 thousand represent not registered share capital as per 2005-12-31. This part of the share capital was registered on the 11th of January 2006.

CASH FLOW STATEMENT

Amount in KSEK	<i>Group</i>		<i>Parent company</i>	
	JAN 1 – DEC 31 2005	JAN 1 – DEC 31 2004	JAN 1 – DEC 31 2005	JAN 1 – DEC 31 2004
Operating activities				
Operating loss	-16 489	-26 597	-20 958	-31 584
<i>Adjustment for non cash items</i>				
Depreciation of tangible/intangible assets	5 406	5 330	8 272	8 508
Write-down of inventory	1 440	1 200	1 440	1 200
Currency changes	-212	0	-212	0
Change in accrued expenses	1 761	572	2 098	703
Tax paid	-6	-263	0	-263
Interest income received	163	348	161	340
Interest paid	-507	-57	-507	-57
Cash flow from operating activities before changes in working capital	-8 444	-19 467	-9 706	-21 153
<i>Changes in working capital</i>				
Increase/decrease in inventory	-6 135	-2 981	-6 135	-2 981
Increase/decrease in accounts receivables	-2 649	-1 915	-2 586	-2 164
Increase/decrease in other current receivables	851	-2 990	860	-1 559
Increase/decrease in accounts payable	-880	1 978	-821	1 947
Increase/decrease in other current liabilities	389	789	1 848	1 249
Cash flow from operating activities	-16 868	-24 586	-16 540	-24 661
<i>Investing activities</i>				
Capitalized development expenditures	0	0	0	0
Sales of tangible fixed assets	0	756	0	756
Acquisition of tangible fixed assets	-133	-114	-133	-71
Cash flow from investing activities	-133	642	-133	685
<i>Financing activities</i>				
New share issue	24 000	33 228	24 000	33 228
Fundraising cost	-632	-600	-632	-600
Paid out VAT refund	0	689	0	689
Dividends	0	0	350	0
Loans raised	4 048	4 745	4 048	4 745
Loans repaid	-12 152	-1 425	-12 152	-1 425
Loans written-off	100	1 414	100	1 414
Cash flow from financing activities	15 364	38 051	15 714	38 051
Changes in cash and cash equivalents	-1 637	14 107	-959	14 075
Translation difference	68	-18	0	0
Liquid assets at year's start	19 157	5 068	18 244	4 169
LIQUID ASSETS AT END OF PERIOD	17 588	19 157	17 285	18 244

Accounting principles

General

The annual report was prepared according to the Annual Accounts Act and Swedish general accepted accounting principles. CellaVision follows all Swedish Financial Accounting Standards Council's recommendations and statements, except for RR27 (financial instruments: disclosure and presentation) and RR29 (employee benefits).

Consolidated accounts

Financial statements include CellaVision AB (parent company), CellaVision International AB and CellaVision Inc. (wholly owned subsidiaries). The purchase method was used to prepare the consolidated accounts. Consolidation of subsidiaries' assets and liabilities are reported at market value, according to an acquisition analysis. If the purchase value exceeds net assets in the subsidiary, the difference between the purchase value and the estimated market value constitutes group goodwill, which is amortized over an estimated economic life.

Internal invoicing and internal intercompany financial balances were eliminated from the group accounts. The Group applies the current-rate method for translating foreign subsidiary accounts. All assets and liabilities in CellaVision Inc. are translated at the closing day rate¹, while all items in the income statement are translated at the average rate².

Translation differences occur because of (1) the difference between the income statement's average rate and the year-end closing-day rate and (2) net assets being translated at a different rate at the year's end compared to the rate at the year's start. The translation differences related to the net profit/loss and long-term financial intercompany balances are charged directly against shareholders' equity. For other translation differences, see the "Exchange gains and losses" heading in this chapter.

Revenue recognition

When ...	Then revenue consists of ...
Instruments are sold to end customers	Payment for instruments and software (SW) updates. Total revenue related to instruments and software updates is booked as income when principal risks and benefits associated with instruments are transferred to customers.

Instruments are sold to distributors

Payment for instruments and software updates. Total revenue related to instruments and software updates is booked as income when principal risks and benefits associated with instruments are transferred to distributors.

Service is sold to end customers

Payment for service of instruments. Revenue is accrued during the service contract's period and can come from one-time service and ongoing service contracts.

SW upgrades (new functions, technologies, or applications) are sold to end customers

Payment for SW upgrades. Revenue is accrued during the upgrade contract's period and can come from a one-time upgrade and ongoing upgrades contract.

Instruments are rented on a payment-per-analysis basis

Payments for instrument rental (period-based), service, and software updates.

Payment-per-analysis basis is made

Fixed and variable payments or just a fixed monthly payment. Variable payment depends on the number of analyses performed with the instrument. Revenue is accrued during the contract-specified period.

R&D expenses

Research expenses are charged against the result as they occur. Development expenses for forthcoming products are charged through the end of prototyping. Expenses are capitalized after that, and up to commercialization phase. Development expenses for existing applications and HW-platforms are charged as they occur. To effectively manage expenses, the company uses cost accounting so that all R&D expenses are allocated to projects. Examples of expenses are:

- ▶ Goods and material
- ▶ Consultant's fees for conception and design
- ▶ Salaries and remunerations

Equipment and computer depreciation is not capitalized. At new product launch, a five-year depreciation schedule goes into effect.

Exchange-rate profit and loss

Realized and unrealized exchange-rate differences and translation differences are reported as other operating expenses (i.e., differences related to

¹ Closing day rate SEK/USD: 7.9525 (6.6125).

² Average SEK/USD: 7.4775 (7.3496)

operations-based expenses and intercompany balances). Translation differences are reported as interest income and interest expenses (i.e., differences related to current financial intercompany balances).

Intangible fixed assets

Intangible assets consist of capitalized development expenses and a customer database. All assets are reported at purchase value, less accumulated, scheduled depreciation.

Tangible fixed assets

Tangible assets are instruments, equipment, and computers; all are reported at purchase value, less accumulated, scheduled depreciation.

Depreciation schedule

Scheduled depreciation is based on an asset's purchase value and its estimated economic life:

- Development expenses, 5 years
- Group goodwill, 5 years
- Instruments, 5 years
- Equipment, 5 years
- Customer database, 3 years
- Computers, 3 years

If an asset's ...	Then its ...
Depreciation is imminent	Recovery value is set.

Booked value is higher than its recovery value	Value is written down to its recovery value.
------------------------------------------------	----------------------------------------------

Recovery value is the highest of market value and usage value. Usage value is capitalized value of future payments that the asset generates.

Leasing

The Group has no financial leasing agreements. Operational leasing primarily covers office rent, computers, and vehicles.

Receivables and liabilities

Receivables are reported as expected, incoming amounts. Liabilities are reported as nominal amounts. Receivables and liabilities in foreign currencies were converted at the closing-day rate, and any unrealized exchange-rate effects were directly charged against the year's profit/loss.

All export-invoices are subject to export factoring. These are accounted for as accounts receivables. The obtained loans in each invoicing-currency are accounted for as a short term loan recalculated to SEK using year-end closing-day rate. Applicable invoices are pledged by the bank and are shown under pledged assets.

Inventories

Inventory is valued at the lower of cost (FIFO method) and net realizable value (lowest value principle). Inventory includes ready-to-sell products and components for instruments.

Cash flow statement

The cash flow statement was prepared according to the indirect method. Cash, bank balances and current, 90-day, investments are all reported as liquid assets.

Pensions

Insurance companies take over all pension commitments. All employees in Sweden are covered by the ITP-plan, operated by Alecta, except the personnel employed before May 1, 1999. Those are covered by an alternative ITP-plan where the employee is free to choose insurance company by himself. They have the same amount to their disposition, as the one's included in the ITP-plan. Employees with a salary exceeding 10 basic amounts are also offered an alternative ITP for a part of their plan. For all pension fees the company are charged a special salary tax amounting to 24,26 % of paid fees. The employees in the US subsidiary are all covered by a 410k-plan.

Segment reporting

CellaVision operation covers only one business segment, that is, systems for automatic microscopy within hematology. The income statement and balance sheet report data on this primary segment. Geographic segments (Europe and the United States) are reported as secondary segments.

Related party transactions

Transactions between the company and the Board of Directors are limited to the remunerations described in note 2. CellaVision AB and CellaVision Inc have entered a service agreement as per 2004-01-01. CellaVision Inc performs services on behalf of CellaVision AB vis-à-vis their U.S. distributor Sysmex America Inc. CellaVision Inc is remunerated for their actual expenses plus 5 %, a so called cost-plus agreement. Internal transactions and balances derived from this agreement are eliminated on a group level according to the principles described under paragraph – Consolidated accounts.

Note 1 – 2B

Note 1. Key data by geographic segment

CellaVision operation covers only one business segment, that is, systems for automatic microscopy within hematology. The income statement and balance sheet report data on this primary segment. Geographic segments (Europe and the United States) are reported as secondary segments.

Data per geographical area	2005	2004
<i>External sales per geographical area</i>		
Europe (including rest of world)	27 141 ¹	14 070 ¹
USA	11 876 ²	15 773 ²
Total	39 017	29 843
<i>Assets per geographical area</i>		
Europe (including rest of world)	49 259	52 611
USA	3 770	2 694
Group elimination	-6 789	-10 189
Total	46 240	45 116
<i>Investments in tangible fixed assets</i>		
Europe (including rest of world)	133	70
USA	-	44

¹Of which 528 (638) are rental income.

²Of which 664 (653) are rental income.

Note 2. Personnel

A. Average number of employees	2005		2004	
	Employees	Of which men	Employees	Of which men
Parent company	28	22	27	23
Subsidiary	4	2	4	2
Total	32	24	31	25
B. Salaries and other remunerations	2005		2004	
	Board, CEO	Other	Board, CEO	Other
Parent company	1 541	11 055	1 554	11 795
Subsidiary	0	2 390	0	2 719
Total	1 541	13 445	1 554	14 514

Executives

According to the AGM's decision, the board's remuneration is SEK 350,000 (350,000) of which the board chairman gets SEK 100,000 (100,000), up to the next AGM. This amount is provided for by year end. Salary and remuneration for the parent company's CEO is KSEK 1,676 (1,808); this includes pension and excludes social charges. When terminating employment, the company must give the CEO 12-months notice, and the CEO must give 6-months notice. The CEO has the right to 12-months severance pay if (1) the company gives notice or (2) the CEO gives notice because of a serious breach of contract on the company's part. No additional severance pay is given. On 31 December 2005, the CellaVision AB board had six male board members, and the Group's executive team consisted of six persons of whom one is female (the CEO).

Absenteeism because of illness

During the period Jan 1 2005 to December 31 2005, the company had no long-term absenteeism because of illness or disability. Total illness-related absenteeism during the period amounted to 0.91%. Male absenteeism was 0.94%. Regarding female absenteeism this is not reported as the company got less than 11 females employed. Absenteeism among employees between 30 – 49, was 1.07%. CellaVision has fewer than 11 employees who are age up to 29 and 50+ and thus does not report absenteeism for this group.

Note 2C – 5

Note 2C.

C. Social security and pension expenses	2005		2004	
	Social security	Of which pension	Social security	Of which pension
Parent company	6 663	2 683	7 074	2 674
Subsidiary	512	107	438	104
Total	7 175	2 790	7 512	2 778

Note 3. Audit fees

Fees paid to the companies auditors	2005		2004	
	Group	Parent company	Group	Parent company
Statutory audit	90	90	90	90
Other assignments	195	195	195	181
Total	285	285	285	271

Note 4. Leasing expenses

	2005		2004	
	Group	Parent company	Group	Parent company
<i>Future leasing expenses referring to non terminable leasing agreements</i>				
- Within 1 year	1 972	1 963	1 473	1 358
- Later than 1 year but within 5 years	1 345	1 345	2 368	2 368
- Later than 5 years	0	0	0	0
Total ¹	3 317	3 308	3 841	3 726

¹Of which 2 256 (3 642) refers to office rent.

Note 5. Capitalized development expenditures

	2005		2004	
	Group	Parent company	Group	Parent company
Opening balance	4 645	4 645	8 409	8 409
Acquisitions	0	0	0	0
Depreciations for the year	-3 764	-3 764	-3 764	-3 764
Total	881	881	4 645	4 645

Note 6 – 7

Note 6. Other intangible assets

Customer database – U.S.

	2005		2004	
	Group	Parent company	Group	Parent company
Opening balance	0	7 275	0	0
Acquisitions	0	0	0	10 912
Depreciations for the year	0	-3 637	0	-3 637
Total	0	3 638	0	7 275

Note 7. Tangible fixed assets

	2005		2004	
	Group	Parent company	Group	Parent company
Opening balance	9 736	7 118	9 736	7 771
Acquisitions	358	358	114	69
Disposal	-305	-245	-177	-722
Closing balance	9 726	7 231	9 673	7 118
Accumulated depreciations, brought forward	-6 902	-5 629	-5 640	-4 780
Depreciations for the year	-1 480	-871	-1 520	-1 107
Reversal of accumulated depreciations on disposed assets	200	232	258	258
Accumulated depreciations carried forward	-8 182	-6 268	-6 902	-5 629
Currency translation difference	-242	0	-373	0
Residual value	1 302	963	2 398	1 489

Note 8 – 10

Note 8. Distribution of depreciations

A. Group	2005			2004		
	Cap.dev. expenses	Goodwill	Equipment	Cap.dev. expenses	Goodwill	Equipment
Cost of goods sold	-3 764	0	-416	-3 764	0	-360
Selling expenses	0	0	-509	0	0	-421
Administrative expenses	0	0	-81	0	0	-108
Research & development Expenses	0	0	-474	0	0	-631
Total	-3 764	0	-1 480	-3 764	0	-1 520

B. Parent company	2005			2004		
	Cap.dev. expenses	Other intangibles	Equipment	Cap.dev. expenses	Other intangibles	Equipment
Cost of goods sold	-3 764	0	-194	-3 764	0	-205
Selling expenses	0	-3 637	-122	0	-3 637	-162
Administrative expenses	0	0	-81	0	0	-108
Research & development expenses	0	0	-474	0	0	-631
Total	-3 764	-3 637	-871	-3 764	-3 637	-1 106

Note 9. Non-recurring items

Write-down of inventory	2005		2004	
	Group	Parent company	Group	Parent company
Cost of goods sold	1 440	1 440	1 200	1 200
Total	1 440	1 440	1 200	1 200

Note 10. Profit on financial investments

	2005		2004	
	Group	Parent company	Group	Parent company
Interest income	163	162	1 920	1 912
Dividends from Group companies	0	350	0	0
Total	163	512	1 920	1 912

Note 11 – 14

Note 11. Taxes

	2005		2004	
	Group	Parent company	Group	Parent company
Provisions in previous years	-8	0	-8	0
Tax paid	6	0	0	0
Provisions	-2	0	-8	0
Tax reported	0	0	0	0
Loss carry-forwards	256 345	246 841	237 496	228 900
Deferred tax benefit not reported	69 942	69 115	64 840	64 092

Note 12. Shares in group companies

	Corp. ID. nr.	Domi- cile	Number of shares	Par value	Capital and voting rights	Net book value
CellaVision International AB	556573-4299	Lund	1 000	100.000	100%	100.000
CellaVision Inc.		USA	10	1	100%	1

Note 13. Prepaid expense and accrued income

	2005-12-31		2004-12-31	
	Group	Parent company	Group	Parent company
Office rent	408	408	480	480
Pension fees	109	109	103	103
Accrued interest income	0	0	182	182
Other	269	269	253	253
Total	786	786	1 018	1 018

Note 14. Liabilities to credit institutions

	2005		2004	
	Group	Parent company	Group	Parent company
<i>Long-term liabilities</i>				
Landstingets fond för teknikupphandling och produktutveckling	0	0	0	0
The Swedish Industrial Development Fund ¹	0	0	10 000	10 000
Total	0	0	10 000	10 000

Note 14 cont. – 16

	2005		2004	
	Group	Parent company	Group	Parent company
<i>Current liabilities</i>				
Landstingets fond för teknikupphandling och produktutveckling	0	0	2 152	2 152
The Swedish Industrial Development Fund	0	0	0	0
Nordea Bank AB	2 200	2 200	0	0
Nordea Finans Sverige AB (publ) ²	6 593	6 593	4 745	4 745
Total	8 793	8 793	6 897	6 897

¹The Swedish Industrial Development Fund

At a special AGM in CellaVision AB the 11th of October 2002 it was decided to issue a convertible loan of 10 MSEK. An existing interest bearing loan from The Swedish Industrial Development Fund of 10 MSEK was offset against a new loan without interest. The right to conversion was not used. The loan without interest is due the 30th of June 2006. The loan was set-off against new shares in November 2005.

²Exportfactoring. 80 % of the nominal invoice amount for all export is paid out as a loan from Nordea Finans Sverige AB (publ) at invoicing date. The exportfactoring limit is MSEK 11.

Note 15. Accrued expense and prepaid income

	2005		2004	
	Group	Parent company	Group	Parent company
Vacation reserve	1 861	1 708	1 474	1 346
Directors fee	398	398	397	397
Social security expenses	887	887	731	731
Other	2 944	2 564	2 050	1 437
Total	6 090	5 557	4 652	3 911

Note 16. Pledged assets

A bank guarantee of SEK 960,000 (300,000) was submitted to a customer. The bank guarantee was returned and closed in January 2006.

Nordea Finans Sverige AB (publ) pledge all export invoices that constitute the loan given by them to CellaVision AB. The pledged amount at year-end was 6.593 (4.745).

Nordea Bank AB (publ) has a chattel mortgage of 3.000 (3.000) as security for approved credits. All property of CellaVision AB is subject to the chattel mortgage.

Annual Meeting

The Annual Meeting will be held on April 25 2006 at 5 PM in CellaVision's office at Ideon in Lund: Delta 5, Scheelevägen 19A, 3 tr.

Lund, Sweden on February 23 2006

Lars Gatenbeck
Board chairman

Christer Fåhraeus

Per Sjöberg

Peter Zakrisson

Niels Freiesleben

Peter Wigforss

Yvonne Mårtensson
CEO

Our auditor's report was issued in Malmö, Sweden on February 24 2006

Deloitte AB
Per-Arne Pettersson
Authorized Public Accountant

AUDIT REPORT

To the annual meeting of the shareholders of CellaVision AB

Corporate identity number 556500-0998

We have audited the annual accounts, the consolidated accounts, the accounting records and the administration of the board of directors and the managing director of CellaVision AB for the financial year 2005-01-01 – 2005-12-31. These accounts and the administration of the company and the application of the Annual Accounts Act when preparing the annual accounts and the consolidated accounts are the responsibility of the board of directors and the managing director. Our responsibility is to express an opinion on the annual accounts, the consolidated accounts and the administration based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Sweden. Those standards require that we plan and perform the audit to obtain reasonable assurance that the annual accounts and the consolidated accounts are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the accounts. An audit also includes assessing the accounting principles used and their application by the board of directors and the managing director and significant estimates made by the board of directors and the managing director when preparing the annual accounts and consolidated accounts as well as evaluating the overall presentation of information in the annual accounts and the consolidated accounts. As a basis for our opinion concerning discharge from liability, we examined significant decisions, actions taken and circumstances of the company in order to be able to determine the liability, if any, to the company of any board member or the managing director. We also examined whether any board member or the managing director has, in any other way, acted in contravention of the Companies Act, the Annual Accounts Act or the Articles of Association. We believe that our audit provides a reasonable basis for our opinion set out below.

The annual accounts and the consolidated accounts have been prepared in accordance with the Annual Accounts Act and give a true and fair view of the company's and the group's financial position and results of operations in accordance with generally accepted accounting principles in Sweden. The statutory administration report is consistent with the other parts of the annual accounts and the consolidated accounts.

We recommend to the annual meeting of shareholders that the income statements and balance sheets of the parent company and the group be adopted, that the loss of the parent company be dealt with in accordance with the proposal in the administration report and that the members of the board of directors and the managing director be discharged from liability for the financial year.

Malmö, February 24 2006

Deloitte AB

(signature on original document)

Per-Arne Pettersson

Authorized Public Accountant

FIVE-YEAR SUMMARY

Income statement

All amount in KSEK	2005	2004	2003	2002	2001
Net sales	39 017	29 843	14 974	13 669	8 043
Cost of goods sold	-19 390	-19 338	-10 077	-8 762	-6 949
Gross profit	19 627	10 505	4 897	4 907	1 094
Selling expenses ¹	-13 556	-11 432	-17 023	-20 918	-17 737
Administrative expenses ¹	-10 795	-11 274	-10 512	-12 278	-13 185
Research and development expenses ¹	-11 470	-14 305	-16 094	-20 792	-23 509
Other operating income	0	0	0	0	370
Other operating expenses	-295	-91	-626	-352	-70
Operating loss	-16 489	-25 597	-39 358	-49 433	-53 037
Profit/loss on financial investments	-244	-1 704	-789	374	-19
Tax	0	0	309	-49	0
Net loss for the year	-16 733	-24 893	-39 838	-49 108	-53 056

¹The principal for allocating expenses between functions was changed during 2002. The income statements for prior years have been adjusted for comparability.

Balance sheet

All amount in KSEK	2005	2004	2003	2002	2001
Assets					
Intangible fixed assets	2 147	4 645	8 409	16 392	21 595
Tangible fixed assets	1 302	2 398	3 827	3 956	3 771
Current assets	42 791	38 073	18 294	53 339	89 980
Total assets	46 240	45 116	30 530	73 687	115 346
Shareholders' equity and liabilities					
Shareholders' equity	26 561	18 148	8 069	48 664	82 604
Long-term liabilities	0	10 000	13 389	13 790	9 461
Current liabilities	19 679	15 948	9 072	11 233	23 281
Total shareholders' equity and liabilities	46 240	45 116	30 530	73 687	115 346

FIVE-YEAR SUMMARY

Key data and ratios	2005	2004	2003	2002	2001
Shareholders' equity, KSEK	26 561	18 148	8 069	48 664	82 604
Capital employed, KSEK	35 354	35 045	22 944	63 369	102 427
Interest-bearing liabilities, KSEK	8 793	16 897	14 874	14 706	19 823
Net investments, KSEK	-133	-642	2 418	3 005	12 026
Cash flow, KSEK	-17 001	-23 944	-33 844	-44 635	-65 593
Interest coverage ratio	-40,10	-114,52	-128,63	-33,43	-40,48
Net debt/equity ratio	-0,33	-0,68	1,22	-0,50	-0,36
Equity/assets ratio, %	57	40	26	66	72
Percentage of risk-bearing capital, %	57	40	26	66	72
Return on equity, %	Neg.	Neg.	Neg.	Neg.	Neg.
Return on capital employed, %	Neg.	Neg.	Neg.	Neg.	Neg.
Average number of employees	32	31	38	45	42
Number of employees at end of period	32	30	37	46	49

Capital employed

Total assets minus deferred tax liabilities and non-interest-bearing liabilities.

Cash flow

Profit/loss after financial items plus depreciation, with deductions for tax paid, adjusted for a decrease/increase in working capital, excluding liquid assets, with deductions for net investments in fixed assets.

Equity/assets ratio

Shareholders' equity in relation to total assets.

Interest coverage ratio

Profit/loss after financial items plus financial expenses in relation to financial expenses.

Net debt/equity ratio

Net debt in relation to shareholders' equity. (Net debt is loan debt minus cash at the period's end.)

Net investments

Tangible and intangible investments, adjusted for divestments.

Net profit/loss per share

Net profit/loss in relation to the weighted average number of shares. Splits and share issues are accounted for.

Net profit/loss per share after full dilution

Net profit/loss in relation to the weighted average number of shares plus the number arising from full dilution. Splits and share issues are accounted for.

Number of employees, average

Number of employees at month's end, divided by 12.

Percentage of risk-bearing capital

Total of shareholders' equity and deferred tax liabilities in relation to the balance sheet total.

Return on capital employed

Profit/loss after financial items plus financial expenses in relation to average capital employed.

Return on equity

Net profit/loss in relation to average shareholders' equity.

Shareholders' equity per share

Shareholders' equity in relation to the number of shares at year-end. Splits and share issues are accounted for.

Shareholders' equity per share after full dilution

Shareholders' equity after dilution, in relation to the number of shares at year-end, if full dilution occurred. Implemented splits and share issues are accounted for.

Per share data	2005	2004	2003	2002	2001
Net loss, undiluted, SEK	-0,81	-1,31	-2,95	-3,76	-5,09
Net loss, diluted, SEK	-0,81	-1,31	-2,95	-3,76	-5,09
Shareholders' equity before dilution, SEK	1,29	0,95	0,60	3,61	6,42
Shareholders' equity after full dilution, SEK	1,29	1,84	2,09	6,04	7,41
Weighted average number of shares, undiluted	20 578	19 043	13 505	13 057	10 430
Weighted average number of shares, diluted	20 578	19 643	14 225	14 713	11 858
Number of shares at end of period, undiluted	23 579	20 151	13 505	13 505	12 865
Number of shares at end of period, diluted	23 579	20 751	14 225	15 184	14 293

BOARD

* Year of birth

Lars Gatenbeck, Chairman

Djursholm, *1956.

CEO and Partner in GZ Group that manages H&B Capital and Life Equity Sweden. Other board memberships include Aerocrine AB, Cancer-föreningen, GZ Group Holdings AB, Profdoc ASA etc.

Peter Zakrisson

Lidingö, *1961.

Partner in GZ Group that manage H&B Capital and Life Equity Sweden. Chairman of the Board in Probi AB and Besthand AB. Other board memberships: GZ Group Holding AB, H&B Capital Ltd etc.

Per Sjöberg

Ängelholm, *1948.

CEO in LPS Medical AB. Chairman of the Board in LPS Medical AB and LPOS Förvaltning AB.

Christer Fåhraeus

Lund, *1965.

Board chairman of Anoto Group AB and Respiratorius AB. CellaVision's founder and CEO until June 1998. Other board memberships: Agellis Group AB, Nextlink and Precise Biometrics AB.

Shares in CellaVision: 2,063,823

Niels Freiesleben

Hornbaek, *1951

CEO in SolarCAP A/S and Chairman of the Board in Freiesleben Management ApS, TiKi Interiör ApS and Scandinavian Import-Export GmbH.

Peter Wigforss

Bålsta, *1945.

CEO in Wigforss Consulting AB. Partner in Onoterat AB. Other board memberships includes Time Care AB.

MANAGEMENT TEAM

* Year of birth

Yvonne Mårtensson

*1953

CEO since 1998. Extensive international marketing and sales experience. Former employed by HemoCue AB, where she served her last two years as Marketing and Sales Manager in the U.S. Board member of Ortivus AB, Biolin AB and Luab (Lund University's holding company).

Shares in CellaVision: 40,000

Lars Juliusson

*1964

Sales Director. Employee since 2000. Extensive experience in selling medical optical equipment. Came to CellaVision from Zeiss, where he was a Sales Manager for the Microscopy Division in Sweden.

Shares in CellaVision: 3,000

Peter Åkerlund

*1961

CFO. Employee since 1998. Broad, deep financial management and accounting experience, most recently in a Gambro Group position.

Shares in CellaVision: 10,000

Hans-Inge Bengtsson

*1958

Quality Assurance Manager. Employee since 2001. More than 15 years of experience with blood analyses and clinical laboratories. Most recent employer was PolyPeptide Laboratory AB, where he worked as Quality Control Manager.

Shares in CellaVision: 1,200

Christian Matson

*1971

R&D Director. Employee since 1999. Came to CellaVision from Axis Communications AB, where he worked as project manager.

Shares in CellaVision: 2,000

Ron Hagner

*1954

General Manager, CellaVision Inc. Extensive sales and marketing experience within diagnostics. Was Marketing and Sales Director for Intelligent Medical Imaging Inc. and for Triangle Imaging Inc. Appointed General Manager of CellaVision Inc. in 2001, after acquisition of assets in Triangle Imaging Inc.

Shares in CellaVision: 1,000

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General Manager: Ron Hagner