MEDICALgorithmics
INNOVATIVE SOLUTIONS IN MEDICINE

Consolidated Annual Report
MEDICALgorithmics Capital Group

for 2018

This report includes:

- Letter from the CEO
- Consolidated Financial Statements
- Directors' Report on the Activities of the Capital Group and Medicalgorithmics S.A.
- Management Statements

Dear Shareholders, Colleagues, Clients and Friends,

I am hereby presenting the Annual Report of Medicalgorithmics Group of Companies and Medicalgorithmics S.A. for 2018.

Medicalgorithmics is a technological company, listed on the Warsaw Stock Exchange since 2011, and in the main listing since 2014. We have developed technology and we create diagnostic devices used in the area of telecardiology. We operate on a global scale. Our main recipients are clients in the USA. The flagship product of Medicalgorithmics, namely PocketECG, constitutes complete diagnostic technology for detecting heart arrhythmia. Last year, we have carried out a record-high number of monitoring sessions using this device. We conducted approximately 100 examinations, which translates into 30 million hours of monitoring of patients' hearts.

The benefits of PocketECG are noticed by more and more specialists, patients and business partners. One of the key events for us in 2018 was acquiring a new strategic partner, i.e. m-Health Solutions Inc. from Canada. Furthermore, in July 2018 Medicalgorithmics signed subsequent agreements for distribution of services with the use of PocketECG technology with Vingmed Group companies in Norway and Sweden.

This means that the cooperation will be expanded with the Scandinavia-based group that Medicalgorithmics has been cooperating with in Denmark since 2017. At the beginning of 2019, we started growing sales in India, establishing cooperation there with a recognized global medical and pharmaceutical corporation, i.e. Abbott, through an affiliate that we have appointed. This year, we plan to significantly increase the number of activated PocketECG devices beyond the USA as compared to 2018.

In the discussed year, we undertook a number of efforts to support the sales process on global markets, as a result of which, we concluded the above-mentioned partnership agreements. We participated in several international industry-specific conferences, including the biggest scientific congress regarding electrophysics, namely Heart Rhythm Society in the USA. Such events are very important for further awareness of our technology on a global scale, and thus, expanding the group of recipients of our diagnostic solutions. From the point of view of sales in the USA, appointing Peter Pellerito in October 2018 as CEO of Medi-Lynx, an affiliate we established, was also an important event for our company. Peter Pellerito has experience supported by success in managing companies operating in the industry of medical devices. I believe that this will be a significant support for the team and it will be positively reflected in the operational activity and results of Medi-Lynx.

Last year, we completed advanced works on our new product: PocketECG CRS. It is a system for cardiologic rehabilitation of patients with circulatory system diseases, which can be used in hospitals, clinics as well as at the patient's home. We received permission from the Food and Drug Administration (FDA) for its sales in the USA. Works on commercialising this product are underway.

To sum up last year, it should be mentioned that we have started a review of strategic options in October. Certainly, many of you wonder what this means. In 2018, the Group's results were below our expectations, despite investments into sales, marketing and new products. This resulted in a decrease of the list price of Medicalgorithmics on the Warsaw Stock Exchange. Due to the above, we are in the process of carrying out in-depth analyses of the possibilities to change the sales model in the USA, aimed primarily at restoring revenue growth rates. We are aware that at the starting stage, this change may not support financial results of the company but there are multiple signs that this is the only path to achieving medium- and long-term development goals. The selection of a strategic option will be an important factor shaping the Group's development and we hope that it will also have a positive impact on the expansion of the scale of operations and also on the increase in the value of the company.

To conclude, I would like to thank everyone who contributed to growing the Group and increasing the quality of services we provide. Most of all, I am grateful to the team for its professionalism and involvement. I would like to thank our clients and shareholders for their trust.

Marek Dziubiński

President of the Management Board

CONSOLIDATED
FINANCIAL STATEMENTS
OF THE CAPITAL GROUP
MEDICALGORITHMICS
FOR 2018

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	PLN '000		EUR '000	
Consolidated statement of financial position	**31.12.2018**	**31.12.2017**	**31.12.2018**	**31.12.2017**
Non-current assets	227 170	228 573	52 830	54 802
Intangible assets	210 454	196 900	48 943	47 208
Long-term financial assets	200	10 910	47	2 616
Current assets	88 912	60 708	20 677	14 555
Short-term receivables	22 781	23 951	5 298	5 742
Short-term financial assets	5 942	4 226	1 382	1 013
Cash and cash equivalents	60 189	32 531	13 997	7 800
Long-term liabilities	13 257	67 649	3 083	16 219
Short-term liabilities	72 063	17 899	16 759	4 291
Equity attributable to Shareholders of the Parent Company	189 864	168 913	44 154	40 498
Share capital	361	361	84	86
Non-controlling interests	40 898	34 820	9 511	8 348
Number of shares	3 606 526	3 606 526	3 606 526	3 606 526
Book value per ordinary share (PLN/EUR)	52.64	46.84	12.24	11.23

Consolidated statement of comprehensive income	**01.01.2018-31.12.2018**	**01.01.2017-31.12.2017**	**01.01.2018-31.12.2018**	**01.01.2017-31.12.2017**
Sales revenue	199 404	203 354	46 733	47 908
Profit on sales	28 149	42 305	6 597	9 966
Operating profit	24 724	41 820	5 794	9 852
Profit before tax	21 573	36 592	5 056	8 621
Net profit	18 948	33 653	4 441	7 928
– attributable to Shareholders of the Parent Company	14 416	25 539	3 379	6 017
– attributable to non-controlling interests	4 532	8 114	1 062	1 911
Net profit attributable to Shareholders of the Parent Company per share (in PLN) – basic	4.00	7.08	0.94	1.67

Consolidated statement of cash flows	**01.01.2018-31.12.2018**	**01.01.2017-31.12.2017**	**01.01.2018-31.12.2018**	**01.01.2017-31.12.2017**
Net cash flows from operating activities	44 232	28 611	10 366	6 741
Net cash flows from investing activities	2 407	(22 026)	564	(5 189)
Net cash flows from financing activities	(18 981)	(21 594)	(4 448)	(5 087)
Total net cash flows	27 658	(15 009)	6 482	(3 536)

Method of conversion of selected figures into EUR:

- The presented selected items of the statement of financial position presented were converted using the mid-rate quoted by the National Bank of Poland (NBP) for 31 December 2018, i.e. EUR/PLN 4.3000, and for 31 December 2017, i.e. EUR/PLN 4.1709.
- The presented selected items of the statement of comprehensive income and the statement of cash flows were converted based on the arithmetic mean of the mid-rates quoted by the NBP for the last day of each month of the financial period from 1 January 2018 to 31 December 2018, i.e. EUR/PLN 4.2669, and from 1 January 2017 to 31 December 2017, i.e. EUR/PLN 4.2447.

		31.12.2018	31.12.2017
Intangible assets	15	210 454	196 900
Property plant and equipment	16	14 685	17 249
Financial assets	17	200	10 910
Deferred income tax assets	14	1 831	3 514
Non-current assets		**227 170**	**228 573**
Trade and other receivables	18	22 781	23 951
Financial assets	17	5 942	4 226
Cash and cash equivalents	19	60 189	32 531
Current assets		**88 912**	**60 708**
TOTAL ASSETS		**316 082**	**289 281**

		31.12.2018	31.12.2017
Share capital	20.1	361	361
Supplementary capital		124 622	124 622
Reserve from the valuation of the incentive scheme	20.6	-	5 312
Retained earnings		72 032	58 434
Foreign exchange differences	24.3	(7 151)	(19 816)
Equity attributable to Shareholders of the Parent Company		**189 864**	**168 913**
Non-controlling interests		**40 898**	**34 820**
Provisions	21	1 790	1 170
Deferred tax liabilities	14	3 306	2 250
Credits and loans		216	-
Liabilities in respect of bonds and other financial liabilities	23	7 479	63 794
Other liabilities		80	120
Accruals and deferred income	22	386	315
Long-term liabilities		**13 257**	**67 649**
Credits and loans		111	873
Liabilities in respect of bonds and other financial liabilities	23	58 399	7 887
Trade and other liabilities	22	10 717	7 522
Income tax liabilities	22	264	311
Accruals and deferred income	22	2 572	1 306
Short-term liabilities		**72 063**	**17 899**
Total liabilities		**85 320**	**85 548**
TOTAL EQUITY AND LIABILITIES		**316 082**	**289 281**

III Consolidated statement of comprehensive income

		01.01.2018-31.12.2018	01.01.2017-31.12.2017
Sales revenue	7	**199 404**	**203 354**
Raw materials and consumables used		(9 085)	(6 250)
Employee benefits	8	(110 549)	(106 581)
Amortization and depreciation	9	(11 579)	(12 470)
Third-party services	10	(33 831)	(30 411)
Other		(6 211)	(5 337)
Total costs of sales		**(171 255)**	**(161 049)**
Profit on sales		**28 149**	**42 305**
Other operating revenue	11	348	748
Other operating expenses	11	(3 773)	(1 233)
Operating profit		**24 724**	**41 820**
Finance income	12	712	614
Finance costs	12	(3 863)	(5 842)
Net finance costs		**(3 151)**	**(5 228)**
Profit before tax		**21 573**	**36 592**
Income tax	13	(2 625)	(2 939)
Net profit from continuing operations		**18 948**	**33 653**
Net profit for the reporting period attributable to Shareholders of the Parent Company		14 416	25 539
Net profit for the reporting period attributable to non-controlling interests		4 532	8 114
		18 948	**33 653**
Other comprehensive income			
Currency translation differences		11 357	(24 979)
Exchange differences on loans constituting a part of net investments in subsidiaries		5 264	(12 809)
Deferred tax on valuation of exchange differences on loans		(1 000)	2 345
Other comprehensive income		**15 621**	**(35 443)**
Other comprehensive income attributable to Shareholders of the Parent Company		12 665	(28 525)
Other comprehensive income attributable to non-controlling interests		2 956	(6 918)
Total comprehensive income for the reporting period			
Comprehensive income for the reporting period attributable to Shareholders of the Parent Company		27 081	(2 986)
Comprehensive income for the reporting period attributable to non-controlling interests		7 488	1 196
		34 569	**(1 790)**
Net profit attributable to Shareholders of the Parent Company per share (in PLN)			
– basic		4.00	7.08
– diluted		4.00	7.08

	Share capital	Supplementary capital	Incentive scheme valuation reserve	Retained earnings	Foreign exchange differences	Equity attributable to Shareholders of the Parent Company	Non-controlling interests
Equity as at 1 January 2018	**361**	**124 622**	**5 312**	**58 434**	**(19 816)**	**168 913**	**34 820**
Comprehensive income for the reporting period							
Net profit for the current reporting period	-	-	-	14 416	-	14 416	4 532
Other comprehensive income	-	-	-	-	12 665	12 665	2 956
	-	**-**	**-**	**14 416**	**12 665**	**27 081**	**7 488**
Transactions recognized directly in equity							
Dividend payment	-	-	-	(5 121)	-	(5 121)	(1 410)
Valuation of the incentive scheme	-		(5 312)	4 303	-	(1 009)	-
Total contributions from and distributions to owners	**-**	**-**	**(5 312)**	**(818)**	**-**	**(6 130)**	**(1 410)**
Equity as at 31 December 2018	**361**	**124 622**	**-**	**72 032**	**(7 151)**	**189 864**	**40 898**

	Share capital	Suppleme ntary capital	Incentive scheme valuation reserve	Retained earnings	Foreign exchange differenc es	Equity attributable to Shareholders of the Parent Company	Non-controlling interests
Equity as at 1 January 2017	**361**	**124 622**	**3 170**	**40 108**	**8 709**	**176 970**	**37 976**
Comprehensive income for the reporting period							
Net profit for the current reporting period	-	-	-	25 539	-	25 539	8 114
Other comprehensive income	-	-	-	-	(28 525)	(28 525)	(6 918)
	-	**-**	**-**	**25 539**	**(28 525)**	**(2 986)**	**1 196**
Transactions recognized directly in equity							
Dividend payment	-	-	-	(7 213)	-	(7 213)	(4 352)
Valuation of the incentive scheme	-	-	2 142	-	-	2 142	-
Total contributions from and distributions to owners	**-**	**-**	**2 142**	**(7 213)**	**-**	**(5 071)**	**(4 352)**
Equity as at 31 December 2017	**361**	**124 622**	**5 312**	**58 434**	**(19 816)**	**168 913**	**34 820**

Cash flows from operating activities		01.01.2018-31.12.2018	01.01.2017-31.12.2017
Net profit for the reporting period		**18 948**	**33 653**
Depreciation of property plant and equipment		4 969	5 481
Amortization of intangible assets		6 610	6 989
Income tax		3 625	(594)
Change in trade and other receivables		633	(5 725)
Change in accruals prepayments and deferred income		952	483
Change in trade and other liabilities		3 088	(14 265)
Change in provisions		537	756
Valuation of the incentive scheme	20.6	-	2 142
Net finance (income)/costs		333	82
Tax paid		(1 338)	(3 608)
Foreign exchange differences		2 220	(863)
Interest		3 582	3 940
Other		73	140
		44 232	**28 611**
Cash flows from investing activities			
Proceeds from sale of investment certificates	17	8 661	15 885
Acquisition of subsidiaries		(167)	-
Expenditure on intangible assets		(5 050)	(35 652)
Expenditure on property plant and equipment		(1 383)	(2 179)
(Acquisition)/sale of other investments		346	(80)
		2 407	**(22 026)**
Cash flows from financing activities			
Dividend payment	20.3	(5 121)	(11565)
Distribution of Medi-Lynx profit to a minority shareholder		(1 410)	-
Proceeds from credits taken out		-	804
Repayment of credit card debt and loans		(1 633)	-
Interest paid on bonds	23	(2 748)	(2 753)
Repayment of financial liabilities	23	(8 069)	(8 080)
		(18 981)	**(21 594)**
Total net cash flows		**27 658**	**(15 009)**
Opening balance of cash and cash equivalents		32 531	47 540
Closing balance of cash		**60 189**	**32 531**

1. General information

Unless the context requires otherwise, such terms contained herein as the "Company", "Medicalgorithmics", the "Parent" or other expressions with a similar meaning and their grammatical inflections refer to Medicalgorithmics S.A., whereas terms such as the "Group", the "Medicalgorithmics Group" and other expressions with a similar meaning and their grammatical inflections refer to the Group comprising Medicalgorithmics S.A. and its consolidated subsidiaries.

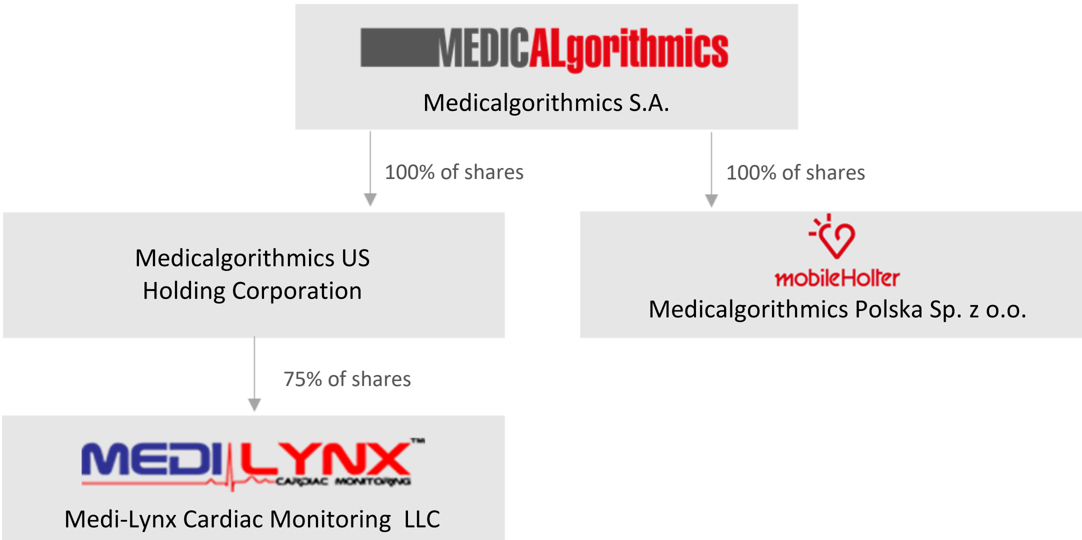
The term "Consolidated financial statements" means the consolidated financial statements of the Medicalgorithmics Capital Group prepared as at 31 December 2018, covering the period from 1 January 2018 to 31 December 2018 and containing relevant comparative figures for the corresponding period of 2017.

2. Information about the Capital Group

The Medicalgorithmics Capital Group is composed of Medicalgorithmics S.A. and its subsidiaries.
The Parent Company holds:

- 100% of shares in Medicalgorithmics US Holding Corporation ("MDG HoldCo"), representing 100% of the votes at the General Meeting of Shareholders;
- 100% of shares in Medicalgorithmics Polska Sp. z o.o. ("Medicalgorithmics Polska", "MDG Polska");
- 75% of shares in Medi-Lynx Cardiac Monitoring, LLC ("Medi-Lynx") with its registered office in Plano, Texas, USA, through MDG HoldCo.

The composition of the Medicalgorithmics Capital Group and its organizational and equity links as at 31 December 2018 are presented below:



Business profile

The Medicalgorithmics Capital Group operates in the field of advanced telemedicine technologies. The Group is a provider of cardiac diagnostic solutions, particularly in the field of ECG analysis.

The principal areas of operations of the Capital Group are:

- provision of ECG monitoring services;
- provision of information technology and biotechnology services;
- scientific research and development;
- manufacture of electro-medical equipment.

The Group provides services in over a dozen countries on several continents, including North and South America, Europe and Australia. Currently, the United States is the largest market. The expansion of sales on the American market was possible owing to the openness of this market to medical innovations and the high level of reimbursement of cardiac diagnostic services by private and public insurers.

Key competitive advantages of the Group:

- advanced technology for mobile cardiac telemetry;
- flexible business model tailored to the specificity of the market;
- a team of top professionals in the areas of IT systems, programming, medical devices, digital signal processing and project management.

The key source of the Group's revenues is the sale of diagnostic services provided to patients in the United States using the proprietary PocketECG system for remote monitoring of heart disorders. PocketECG is a complete diagnostic technology for cardiac arrhythmia detection that provides physicians with current access to the ECG signal and the best diagnostic report on the market with statistical analysis of the data. One of the features that distinguish PocketECG from other competing devices is the transmission of full ECG signal. The system has been approved for trading in the United States by the U.S. Food and Drug Administration (FDA). The system also bears the CE mark indicating that the device complies with the requirements of the European Union directives.

In addition to cardiac telemetry, the Group's products and solutions are used in the cardiac safety industry, i.e. in clinical trials of drugs for cardiac safety. Moreover, the Group collaborates closely with cardiovascular diagnostic and monitoring centres.

3. Information about the Parent Company

Medicalgorithmics S.A. is a joint-stock company registered in Poland. The Parent Company was established on the basis of a notarial deed registered in Repertory A No 1327/2005 of 23 June 2005. In 2011, the Company's shares made their debut on the NewConnect market, an alternative system of trading outside a regulated market operated by the Warsaw Stock Exchange. Since 3 February 2014 the shares of Medicalgorithmics S.A. have been listed on the regulated market of the Warsaw Stock Exchange.

The Parent Company is entered in the Register of Entrepreneurs kept by the District Court for the capital city of Warsaw in Warsaw, 12th Commercial Division of the National Court Register, under KRS number 0000372848.

The Parent Company was assigned a Statistical ID No (REGON) 140186973 and a Tax ID No (NIP) 5213361457. The Parent Company has its registered office in Warsaw at Al. Jerozolimskie 81, 02-001 Warsaw.

Management Board

As at the balance sheet date and as at the date of preparation and publication of these consolidated financial statements, the Management Board and Supervisory Board of the Parent Company were composed of the following persons:

Marek Dziubiński – President of the Management Board

On 21 September 2018, Maksymilian Sztandera submitted his resignation from the position of the Company's Chief Financial Officer, effective as of the date of resignation.

Supervisory Board

On 26 June 2018, the Annual General Meeting of Shareholders changed the composition of Medicalgorithmics S.A.'s Supervisory Board. The General Meeting dismissed all of the existing Supervisory Board Members, i.e. Mr Marek Tatar, Mr Marcin Hoffmann, Mr Jan Kunkowski, Mr Piotr Żółkiewicz and Mr Artur Małek. Subsequently, the General Meeting appointed the following Supervisory Board Members:

Michał Wnorowski, Chairperson of the Supervisory Board, Member of the Audit Committee
Grzegorz Grabowicz, Member of the Supervisory Board, Chairman of the Audit Committee
Artur Małek, Member of the Supervisory Board, Member of the Audit Committee
Marek Tatar, Member of the Supervisory Board
Krzysztof Urbanowicz - Member of the Supervisory Board

4. Basis for preparation of the consolidated financial statements

4.1. Declaration of compliance

The annual consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards, as endorsed by the European Union (the "EU IFRSs").

The EU IFRSs comprise all International Accounting Standards ("IASs"), International Financial Reporting Standards ("IFRSs") and related Interpretations, other than those listed below which are awaiting endorsement by the European Union ("EU") and other than Standards and Interpretations that have been endorsed by the European Union but are not yet effective.

The Capital Group did not elect to apply early new Standards and Interpretations that have been issued and endorsed by the European Union and will become effective after the reporting date.

The financial statements were prepared based on the assumption that the Group entities will continue as going concerns in the foreseeable future, i.e. in particular for a period of at least 12 months from the balance sheet date.

4.2. First-time adoption of standards and interpretations in 2018

The accounting policies applied in preparing these consolidated financial statements are consistent with the policies applied in preparing the Group's consolidated financial statements for the year ended 31 December 2017, save for the effect of application of the following new or amended standards and new interpretations effective for annual periods beginning on or after 1 January 2018.

- IFRS 9 "Financial instruments" − endorsed by the EU on 22 November 2016 (effective for annual periods beginning on or after 1 January 2018),
- IFRS 15 "Revenue from Contracts with Customers" – amendments to IFRS 15 "Revenue from Contracts with Customers" – endorsed by the EU on 22 September 2016 (effective for annual periods beginning on or after 1 January 2018);
- Amendments to IFRS 15 "Revenue from Contracts with Customers" – clarifications to IFRS 15 "Revenue from Contracts with Customers" – endorsed by the EU on 31 October 2017 (effective for annual periods beginning on or after 1 January 2018);
- IFRIC 22 "Foreign Currency Transactions and Advance Consideration Transactions" – endorsed by the EU on 28 March 2018 (effective for annual periods beginning on or after 1 January 2018);
- Amendments to IFRS 2 "Share-Based Payments" – Classification and measurements of share-based payment transactions – endorsed by the EU on 27 February 2018 (effective for annual periods beginning on or after 1 January 2018);
- Amendments to IAS 40 "Investment Property" – transfers of investment property – endorsed by the EU on 14 March 2018 (effective for annual periods beginning on or after 1 January 2018);
- Amendments to IFRS 4 "Insurance Contracts" – Applying IFRS 9 "Financial Instruments" with IFRS 4 "Insurance Contracts" – endorsed by the EU on 3 November 2017 (effective for annual periods beginning on or after 1 January 2018 or as of the date of first-time adoption of IFRS 9 "Financial Instruments");
- Amendments to various standards (IFRS 1 and IAS 28) introduced as part of the annual improvements process – "Annual Improvements to IFRSs 2014-2016 Cycle", primarily to remove inconsistencies and clarify wording.

All the above amendments have been analyzed by the Management Board and do not have a material impact on the financial position and performance of the Group.

The effect of applying the new IFRS 15 "Revenue from Contracts with Customers" and IFRS 9 "Financial Instruments", effective as of 1 January 2018, is presented in Note 4.5 to these financial statements.

4.3. Standards and interpretations coming into effect after the balance sheet date

The following standards and interpretations have been issued by the International Accounting Standards Board or the International Financial Reporting Interpretations Committee, but are not effective yet:

- IFRS 16 "Leases" – endorsed by the EU on 31 October 2017 (effective for annual periods beginning on or after 1 January 2019);
- Amendments to IFRS 9 "Financial Instruments" – prepayment features with negative compensation – endorsed by the EU on 22 March 2018 (effective for annual periods beginning on or after 1 January 2019);
- IFRIC 23 "Uncertainty over Income Tax Treatments" – endorsed by the EU on 23 October 2018 (effective for annual periods beginning on or after 1 January 2019);
- Amendments to IAS 28 "Investments in Associates and Joint Ventures" – long-term interests in associates and joint ventures (effective for annual periods beginning on or after 1 January 2019).

The Group did not opt for early adoption of those new standards or amendments to the existing standards and interpretations.

The Group estimates that, with the exception of IFRS 16 "Leases" effective as of 1 January 2019, the above standards, interpretations and amendments would not have a material effect on its financial statements if applied by the Group as at the balance sheet date. The effect of applying IFRS 16 on the Group's financial statements is described in Note 4.6 to these financial statements.

4.4. New standards and Interpretations not yet endorsed by the EU:

There are no major differences between the IFRS as endorsed by the EU and the regulations issued by the International Accounting Standards Board (IASB), with the exception of the following new standards, amendments to standards and new interpretation which were not yet endorsed by the EU as at the date of publication of the financial statements (the following effective dates refer to the full versions of respective standards):

- IFRS 14 “Regulatory Deferral Accounts” (effective for annual periods beginning on or after 1 January 2016) – the European Commission has decided not to launch the endorsement process of this interim standard until the final version of IFRS 14 is issued;
- IFRS 17 “Insurance Contracts” (effective for annual periods beginning on or after 1 January 2021);
- Amendments to IFRS 3 “Business combinations” − definition of a business (effective for business combinations for which the acquisition date is on or after the beginning of the first annual period beginning on or after 1 January 2020 and to asset acquisitions that occur on or after the beginning of that period);
- Amendments to IFRS 10 “Consolidated Financial Statements” and IAS 28 “Investments in Associates and Joint Ventures” – Sale or contribution of assets between an investor and its associate or joint venture, and further amendments (the effective date of the amendments has been postponed until research into the equity method is completed);
- Amendments to IAS 1 “Presentation of financial statements” and IAS 8 “Accounting policies, changes in accounting estimates and errors” – definition of materiality (effective for annual periods beginning on or after 1 January 2020);
- Amendments to IAS 19 “Employee Benefits” – plan amendment, curtailment or settlement (effective for annual periods beginning on or after 1 January 2019);
- Amendments to various IFRSs (IFRS 3, IFRS 11, IAS 12 and IAS 23) introduced as part of the annual improvements process – “Annual Improvements to IFRSs 2015-2017 Cycle”, primarily to remove inconsistencies and clarify wording (effective for annual periods beginning on or after 1 January 2019);
- Amendments to References to the Conceptual Framework in IFRS Standards (effective for annual periods beginning on or after 1 January 2020).

The Group estimates that none of those new standards, amendments to existing standards and interpretations would have had a material impact on its financial statements had they been applied by the Group as at the balance sheet date.

The scope of regulations endorsed by the EU still does not include hedge accounting for portfolios of financial assets and liabilities with respect to which relevant rules have not been endorsed for use in the EU.

The Group estimates that the application of hedge accounting with respect to its portfolio of financial assets or liabilities in accordance with IAS 39 “Financial Instruments: Recognition and Measurement” would not have had any material effect on its financial statements if these regulations had been endorsed as at the reporting date.

4.5. Effect of applying new accounting standards that became effective in 2018 on the Group's financial statements

a. IFRS 15 “Revenue from contracts with customers”

As regards amendments to IFRS 15 “Revenue from contracts with customers”, the Management Board has analyzed the effect of the standard on the Group’s financial position, performance and scope of disclosures in the financial statements.

The above analysis focused primarily on the moment of recognition of revenue from sales of products. Based on its analyses, the Management Board did not identify any significant changes to the accounting policies applied by the Group in this area.

b. IFRS 9 “Financial instruments”

IFRS 9 affects the classification and measurement of financial assets which depends on the characteristics of cash flows and the business model related to the assets in question. The new standard also unifies the impairment model for all financial instruments. The new standard requires expected credit losses to be recognized when the financial instruments are recognized for the first time and include all the expected losses from the entire life of the instruments earlier than previously.

The Group analyzed the impact of IFRS 9 on the financial statements and, due to the limited extent of changes, adopted a partially retrospective approach to transition to the new standard. At the time of adoption of IFRS 9, the Group analyzed the history of impairment losses on receivables and came to the conclusion that the possible application of the expected credit loss model would not materially affect the amount of impairment losses recognized by the Group and therefore decided to continue the current approach. For a detailed description of the methodology used to calculate impairment losses on financial assets, see Note 5.7.

The table below presents changes in the classification of financial instruments as at 1 January 2018, i.e. the date of initial application of IFRS 9. Application of the new standard replacing the existing IAS 39 did not result in any changes in the methodology of measurement of financial assets and liabilities. The amortized cost method and the fair value through profit or loss method for investment certificates continue to be the principal measurement method, hence the carrying amount of financial assets and liabilities at the date of adoption of IFRS 9 is the same as that resulting from IAS 39.

	Classification in accordance with:		**Carrying amount in accordance with IAS 39 and IFRS 9 as at 1 January 2018**
	IAS 39	**IFRS 9**	
Financial assets			
Cash and cash equivalents	Loans and receivables (amortized cost)	Amortized cost	32 531
Trade and other receivables	Loans and receivables (amortized cost)	Amortized cost	20 939
Investment certificates	Financial assets at fair value through profit or loss	Financial assets at fair value through profit or loss	14 936

IFRS 9 did not change the classification of financial liabilities.

4.6. Standards that will become effective in 2019

a. IFRS 16 “Leases”

IFRS 16 “Leases”, published by the International Accounting Standards Board on 13 January 2016, is effective for annual periods beginning on or after 1 January 2019.

The new standard establishes principles for the recognition, measurement, presentation and disclosure of leases. All lease transactions result in the lessee acquiring a right-of-use asset and incurring a lease liability. Thus, IFRS 16 abolishes the operating and finance lease classification and provides a single lessee accounting model The lessee will be required to recognize:

- assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value, and
- depreciation of the leased asset separately from interest on the lease liability.

IFRS 16’s approach to lessor accounting is substantially unchanged from its predecessor, IAS 17. Lessors continue to classify leases as operating or finance leases, with each of them subject to different accounting treatment.

The Group will apply IFRS 16 as of 1 January 2019. The Group intends to apply a simplified retrospective approach and will not restate comparative data for the year preceding the initial application of the new standard. With respect to leases previously classified as operating leases, right-of-use assets will be recognized as at 1 January 2019, measured at the amount equal to the lease liability at the date of initial application of IFRS 16, i.e. 1 January 2019.

Effect of IFRS 16 on the financial statements

The Group reviewed all leases not terminated as at 31 December 2018. As at the balance sheet date, the value of undiscounted, irrevocable operating lease liabilities in accordance with IAS 17 amounts to PLN 25,365 thousand. The Group decided that it will apply simplified IFRS 16 requirements to leased assets of low value (up to PLN 100 thousand) and short-term leases. Payments relating to these leases will continue to be recognized on a straight-line basis over the lease term as an expense in profit or loss. For other leases recognized as operating leases as at 31 December 2018, the Group estimated that the right-of-use assets would amount to approximately PLN 23,793 thousand as at 1 January 2019, while the lease liabilities would amount to PLN 23,793 thousand. The interest rate used to split the lease payments into interest and principal portions was set at the level of the planned debt service cost (2.52%). In 2019, the analysis of the effect of IFRS 16 on the Company's operations will continue and the Company's final estimates may change.

The estimated effect of the application of IFRS 16 on the recognition of the right-of-use assets and related financial liabilities as at 1 January 2019 is presented in the table below:

	Estimated effect as at 1 January 2019
Non-current assets	
Property plant and equipment	23 793
Finance lease liabilities	
Finance lease liabilities – long-term	19 205
Finance lease liabilities – short-term	4 588

Following initial recognition, these assets will be measured at cost (i.e. initial value less depreciation). Interest on lease liabilities will be recognized in profit or loss except when they meet the criteria for capitalization in the carrying amount of the asset under construction that is financed by the liability.

Application of practical expedients

In applying IFRS 16 for the first time, the Group will apply the following practical expedients permitted by the standard:

- application of a single discount rate (at the level of planned debt service cost – 2.52%) to a portfolio of leases with similar characteristics,
- the treatment of operating lease agreements for which the remaining lease term is less than 12 months as at 1 January 2019 or for which the term is shorter than the normal operating cycle of the Group as short-term leases,
- exclusion of initial direct costs from the measurement of the right-of-use asset on the date of initial application, and
- the use of hindsight (i.e. knowledge gained after the fact) in determining the lease period if the agreement contains options to prolong or terminate the lease.

4.7. Basis of measurement

These financial statements were prepared under the historical cost convention, except with respect to financial assets measured at fair value through profit or loss (investment certificates).

4.8. Presentation and functional currency

The figures contained in the financial statements are presented in Polish zlotys ("PLN"), rounded to the nearest thousand without decimal places. The Polish zloty is the functional currency of Medicalgorithmics S.A. and its subsidiary, Medicalgorithmics Polska Sp. z o.o. The functional currency of subsidiaries, Medi-Lynx and MDG HoldCo, is the US dollar ("USD").

a. Conversion of financial statements of subsidiaries whose functional currency is different than PLN

As at the balance sheet date, assets and liabilities of subsidiaries whose functional currency is different than PLN are translated into the Group's presentation currency (PLN) using the exchange rate effective as at the balance sheet date, and their statements of comprehensive income are translated using the weighted average exchange rate for the respective financial period. Equity is translated using the average exchange rate announced by the National Bank of Poland as at the date on which control was acquired by the Parent Company. In the case of a new issue of additional shares, they are converted using the average exchange rate announced for the particular currency by the National Bank of Poland for the date on which the capital increase was entered in the register. Any exchange differences arising from such conversion are recognised in other comprehensive income and accumulated in a separate component of equity. On disposal of an entity, the deferred exchange rate differences accumulated in equity and related to a given entity are taken to profit or loss.

b. Conversion of items denominated in currencies other than the functional currency

Transactions denominated in currencies other than the functional currency of the company in question are converted into its functional currency at the foreign exchange rate prevailing on the transaction date. As at the balance sheet date, monetary assets and liabilities denominated in currencies other than the functional currency of the company in question are converted into its functional currency using the average exchange rate for the respective currency set by the Central Bank of the country in which the company has its registered office, as effective at the end of the reporting period. Foreign exchange gains and losses arising on translation are recognized as finance income (costs), or, where the accounting policies so provide, capitalised in assets. Non-monetary assets and liabilities recognized at historical cost denominated in a currency other than the functional currency are stated at the historical exchange rate effective on the transaction date. Non-monetary assets and liabilities measured at fair value and denominated in a currency other than the functional currency are translated using the exchange rate effective on the date of the fair value measurement. Gains or losses resulting from the translation of non-monetary assets and liabilities recognised at fair value are recognised in accordance with the recognition of the gain or loss on the change in fair value (that is, in other comprehensive income or in profit or loss, respectively, depending on where the change in fair value is recognised).

4.9. Judgments and estimates made

The financial statements of the Parent Company and all its subsidiaries were included in the consolidated financial statements using the full method. The preparation of financial statements in accordance with the EU IFRSs requires the Management Board to make judgements, estimates and assumptions that affect the application of the adopted accounting principles and the presented amounts of assets, liabilities, revenue and expenses whose actual values may differ from the estimates.

The estimates and assumptions associated with them are verified on an ongoing basis.

A revision of accounting estimates is recognised in the period in which the estimate was revised or in current and future periods if the revision affects both the current and future periods.

In particular, significant areas of uncertainty with respect to the estimates made and judgements made in applying the accounting principles that had the most significant impact on the figures disclosed in the financial statements relate, in particular, to:

- intangible assets (estimates concerning forecasts used in impairment tests and estimates of amortisation rates for intangible assets);
- property, plant and equipment (estimates of depreciation rates applied);
- fair value and impairment in relation to financial assets, including shares in subsidiaries;
- trade receivables and other financial assets, including loans granted (at each balance sheet date the Capital Group assesses whether there is any objective evidence that a component of receivables or group of receivables is impaired; if the recoverable amount of an asset is less than its carrying amount, the Capital Group recognizes an impairment write-down to the present value of planned cash flows);
- sales revenue generated by Medi-Lynx (revenue estimates based on historical cash inflows for the provided services);
- provisions for liabilities and trade liabilities;
- inventories (assessment of the likelihood that inventories are impaired; the determination of impairment requires estimating the net realizable values);
- deferred tax assets (assessment of recoverability of assets and estimates of potential impairment write-downs);
- deferred tax provisions.

4.10. Authority approving the financial statements for publication

The Management Board of the Parent Company is the authority approving the financial statements for publication.

5. Significant accounting policies

The accounting policies presented below have been applied with respect to all the reporting periods presented in the financial statements by the Capital Group.

5.1. Consolidation principles

a. Subsidiaries

Subsidiaries are entities controlled by the Parent Company. Control exists when the Parent Company has the power to manage directly or indirectly the financial and operating policies of an entity in order to obtain benefits from its activities. In assessing the degree of control the existing and potential voting rights are taken into account that may be exercised or converted as at the reporting date. Financial statements of subsidiaries are consolidated from the date of assuming control over subsidiaries to the date on which such control ceases to exist.

b. Consolidation adjustments

Balances of settlements between the Group’s entities, transactions concluded within the Group and any resulting unrealized gains or losses, as well as revenues and costs of the Group are eliminated at consolidation. Unrealized gains arising from transactions with associates are eliminated from the consolidated financial statements to the extent of the Group's interest in the entity. Unrealized losses are eliminated from the consolidated financial statements according to the same rule as unrealized gains, until there are indications of impairment.

5.2. Goodwill

Goodwill arising on acquisition of subsidiaries is recognized as an intangible asset. The fair value of consideration transferred does not include amounts related to the settlement of earlier links. As a rule, such amounts are recognized in profit or loss for the current period. Acquisition costs (other than costs of issuing debt or equity instruments) which the Group incurs in connection with a business combination are accounted for as costs of the period in which the costs are incurred.

Following the initial recognition, goodwill is recognized at acquisition cost, less cumulative impairment losses. Acquisition of non-controlling interests is disclosed as a transaction with owners. Accordingly, no goodwill is recognized for such transaction. Adjustments to non-controlling interests are performed based on the pro-rata value of acquired net assets of a given subsidiary.

5.3. Property, plant and equipment

Property, plant and equipment were carried at cost less accumulated depreciation and impairment. Land is not depreciated. Property, plant and equipment include own fixed assets, leasehold improvements, fixed assets under construction and third-party fixed assets accepted for use by the Group (where the terms of the contract transfer substantially all potential rewards and risks incidental to their ownership to the Group), and constitute assets used in the supply of goods or provision of services, for administrative purposes or to be leased to third parties, and their expected useful life exceeds one year. The cost of property, plant and equipment comprises costs incurred to acquire or construct an item of property, plant and equipment, including capitalised interest accrued up until the date when the fixed asset is placed in service. Subsequent expenditure are included in the carrying amount where an inflow of economic benefits to the Group is probable. Day-to-day maintenance costs of property, plan and equipment are recognized in profit or loss of the current period.

The cost of an item of property, plant and equipment comprises its purchase price, including import duties and non-refundable purchase taxes after deducting trade discounts and rebates, any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management, and estimated cost of dismantling and removing the asset and restoring the site on which it was located, the Group is obliged to incur. Property, plant and equipment, other than fixed assets under construction and land, are depreciated. The depreciable amount is the cost of an asset less its residual value, and depreciation is calculated based on the useful life of the asset assumed by the Group and verified on a periodical basis. Depreciation commences when an asset is available for use and ceases at the earlier of: the date that the asset is classified as held for sale, the date that the asset is derecognized, the date that the recoverable amount of the asset becomes higher than its carrying amount or the date that the asset is fully depreciated. The Capital Group has adopted the following useful lives for particular categories of fixed assets:

Buildings and structures: 10 to 50 years;
Technical equipment and machinery: 5 to 25 years;
Vehicles: 3 to 10 years;
Equipment: 5 to 10 years;
Computer hardware: up to 3 years;
Leasehold improvements and fixed assets used under lease agreements: period remaining until the expiry of the contract.

Gains or losses arising from the derecognition of an item of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the item, and recognized in profit or loss of the current period.

5.4. Intangible assets

The Capital Group recognizes intangible assets only if:

a) it is probable that future economic benefits that are attributable to the asset will flow to the Capital Group; and
b) the cost of the asset can be measured reliably.

An intangible asset is measured initially at cost. Intangible assets are amortized. Amortization rates were determined taking into account the assets' useful lives. Intangible assets are amortized on a straight-line basis over the following period:

Client bases: 20 years
Completed development work: 2 to 10 years;
Economic copyrights – licenses: 2 to 5 years.

Expenditure on research is recognized as an expense when it is incurred. Prior to the commencement of production or use of new technological solutions, development costs are capitalized in intangible assets if the Capital Group can demonstrate the following:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale;
- its intention to complete the intangible asset and use or sell it;
- its ability to use or sell the intangible asset;
- how the intangible asset will generate probable economic benefits. Among other things, the Capital Group should demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset;
- the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset;
- its ability to measure the expenditure attributable to the intangible asset during its development reliably.

Development costs with a pre-defined useful life are amortized. Amortization commences when an asset is ready for its intended use and ceases when the asset is classified as held for sale or derecognized.
The amortization period is equal to the useful life of an asset.

The amortization period and the amortization method adopted are reviewed at least at each financial year end. Development costs are amortized over the expected period of earning revenue from the sale of the product. The Company does not amortize development costs with an indefinite useful life.

Intangible assets with indefinite useful lives are tested for impairment on an annual basis, following the guidelines in IAS 36 "Impairment of assets".

Borrowing costs (e.g. interest on credits and loans or exchange differences on foreign currency credits and loans) that are directly attributable to the acquisition or production of an asset are capitalised as part of the cost of such an asset. Net financing costs include interest paid on the debt calculated using the effective interest rate, interest on cash invested by the Capital Group, dividends due, foreign exchange gains or losses; and gains and losses on hedging instruments carried through profit or loss.

5.5. Financial instruments

Financial assets are classified in one of the following categories:

a) measured at amortized cost;
b) measured at fair value through other comprehensive income;
c) measured at fair value through profit or loss.

Classification of debt financial assets depends on the business model for the management of groups of financial assets and on the nature of the contractual cash flows for a given financial asset. Financial assets are classified at initial recognition and their classification may change only if the business model of managing financial assets changes. The principal financial asset management models include the business model whose objective is to hold assets in order to collect contractual cash flows, the model whose objective is to hold assets in order to collect contractual cash flows and sell the assets, and a model of holding assets for other purposes (in principle, it is a model whose objective is to hold assets in order to sell them). The Group has adopted the principle that the sale of a financial asset shortly before its maturity does not constitute a change in the business model from the model whose objective is to hold assets in order to collect contractual cash flows to the model whose objective is to hold assets in order to collect contractual cash flows and sell the assets or the model of holding assets for other purposes.

Financial assets are derecognized when rights to receive cash flows from the assets have expired or when the Group has transferred the rights to receive cash flows to a third party and has transferred substantially all risks and rewards of ownership.

a. Financial assets measured at amortized cost

A financial asset is measured at amortized cost if the following two conditions are met:

a) the asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and
b) its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding.

Loans advanced, trade receivables and other receivables subject to IFRS 9 are classified by the Group as measured at amortized cost. Financial assets are measured at amortized cost using the effective interest rate method. Long-term receivables subject to IFRS 9 are discounted as at the balance sheet date. Trade receivables with maturities of less than 12 months are measured at nominal value less expected credit losses.

b. Financial assets measured at fair value through profit or loss

Short-term financial assets measured at fair value through profit or loss include assets acquired in order to achieve economic benefits resulting from short-term price changes. Short-term financial assets are initially recognized at cost and measured at fair value as at the balance sheet date. Gains or losses on measurement of financial assets are recognized in profit or loss as finance income or expenses.

Financial assets measured at fair value through profit or loss include short-term investments in securities, including acquired units in investment funds.

c. Financial assets measured at fair value through other comprehensive income

The Group recognizes gains/losses on measurement of investments in debt and equity instruments disclosed by the Company on initial recognition in other comprehensive income. Dividends from equity instruments at fair value through other comprehensive income are recognized by the Group as income in profit or loss.

As at the balance sheet date, the Group did not classify any financial assets into this category.

5.6. Non-derivative financial liabilities

The Capital Group recognizes subordinated liabilities and liabilities under outstanding debt securities at the date on which they arise. All other financial liabilities, including liabilities at fair value through profit or loss, are recognized at the trade date, or the date on which the Capital Group becomes party to an agreement under which it is obliged to deliver the financial instrument. The Capital Group derecognizes a financial liability when the liability has been repaid, written off or is time barred. Financial assets and a financial liabilities are offset and the net amount is presented in the statement of financial position when, and only when, the Capital Group has a legally enforceable right to set off the recognized amounts or intends either to settle on a net basis, or to realize the asset and settle the liability simultaneously.

The Capital Group classifies non-derivative financial liabilities as other financial liabilities. Such financial liabilities are initially recognized at fair value plus any directly attributable transaction costs. Following initial recognition, such liabilities are measured at amortized cost using the effective interest rate method. Other financial liabilities include credits, loans and other debt instruments, overdraft facilities, trade liabilities and other liabilities.

5.7. Impairment losses on assets

Financial assets (including receivables)

Financial assets not classified as at fair value through profit or loss are assessed at the end of each reporting period to determine whether there is objective evidence that they are impaired.

The Group uses the following approaches to estimate impairment of financial assets:

- general approach,
- simplified approach.

The Group applies the general approach to financial assets measured at fair value through other comprehensive income and to financial assets measured at amortized cost, except for trade receivables.
In the general approach, the Group estimates the impairment loss on financial assets on the basis of a three-stage model based on the change in credit risk of financial assets since their initial recognition. If credit risk of a given financial asset has not increased significantly since initial recognition (stage 1), the Group recognizes 12-month expected credit losses. If the Group identifies a significant increase in credit risk of financial assets (stages 2 and 3), the Group recognizes lifetime expected credit losses for the affected financial assets. As at each reporting date, the Group analyses whether there is any indication of a significant increase in credit risk of its financial assets.

At the time of adoption of IFRS 9, the Group analyzed the history of impairment losses on receivables and came to the conclusion that the possible application of the expected credit loss model would not materially affect the amount of impairment losses recognized by the Group and therefore decided to continue the current approach. For a detailed description of the methodology used to calculate impairment losses on financial assets, see Note 18.

Given the nature of trade receivables, impairment losses on receivables remained relatively flat compared to impairment losses calculated in accordance with the rules in force before 1 January 2018, despite the introduction of the changes provided for in the standard. The effect of implementation of IFRS 9 on the Group's retained earnings was immaterial.

Non-financial assets

The carrying amounts of non-financial assets, other than inventories and deferred tax assets, are reviewed at the end of each reporting period to determine whether there is any indication of impairment. If any such indication exists, then the Capital Group's recoverable amount is estimated by the Company.

The recoverable amount of an asset is the greater of its net realizable value and its value in use. An impairment loss is recognized when the carrying amount of an asset is higher than its recoverable amount. Impairment losses are recognized in profit or loss for the current period.

An impairment loss in respect of goodwill is not reversed. For other assets, impairment losses recognized in previous periods are reviewed at the end of each reporting period to determine whether there is any evidence of decrease in or complete reversal of the impairment loss. Impairment losses can be reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of amortization or depreciation, if no impairment loss had been recognized.

5.8. Employee benefits

In the event of termination of employment, the Capital Group's employees are entitled to benefits provided for by the Polish labor law, including, but not limited to, an allowance for unused holiday leave and compensation for the obligation to refrain from engaging in any activity competitive to the employer's business. In the subsidiary, Medi-Lynx, a provision is recognized for employee benefits in respect of Paid Time Off (PTO). The benefit is customary and results from the internal policy of Medi-Lynx.

Therefore, the Capital Group recognizes provisions for future employee benefits on account of unused holidays for previous periods and unpaid allowances. This provision is calculated by multiplying the number of days of unused leaves by the daily cost of remuneration for each employee.

Due to their immateriality, the Capital Group does not recognize provisions for retirement severance pays and jubilee awards.

Following the introduction of the Parent Company's incentive scheme, it was decided to recognize a provision for future bonuses in the form of equity-settled share-based payments. The amount of the provision results from an actuarial valuation and is recognized in the Parent Company's reserve capital in accordance with IFRS 2 "Share based payments".

The amount of the provision is reviewed annually, depending on the progress of the incentive scheme, and recognized in the Parent Company's accounts as per the actual implementation of the scheme. In the event of any change to the terms and conditions of the incentive scheme (including its cancellation) or grant of the remaining entitlements, remeasurement at the date of such change is required in accordance with IFRS 2.

5.9. Provisions

A provision is recognized when the Capital Group has a present legal or constructive obligation resulting from past events, which can be reliably estimated and which is likely to cause an outflow of economic benefits when discharged. Provisions are recognized in the amount equal to the best estimate of expenditure required to discharge the present obligation as at the end of the reporting period, taking into account the risks and uncertainties associated with events and circumstances leading to its discharge.

5.10. Cash and cash equivalents

Cash and cash equivalents include cash in hand and cash in bank accounts as well as deposits and short-term securities with maturities of up to three months.

5.11. Equity

Equity disclosed in the Parent Company's financial statements comprises:

a) The share capital recognized in the amount specified in the Articles of Association and entered in the court register;
b) The share premium is reported as a separate item in equity. Share issue costs decrease the balance of equity;
c) Supplementary capital recognized in accordance with the Commercial Companies Code;
d) Capital reserve from incentive scheme measurement recognized based on an actuarial valuation that is reviewed on an annual basis;
e) Retained earnings comprising retained earnings from previous years and profit or loss for the current financial period.

5.12. Revenue

In these financial statements, the Group applied IFRS 15 “Revenue from contracts with customers” for the first time. The standard contains a “Five-step model” of recognizing revenue from contracts with customers. In accordance with IFRS 15, revenue is recognized in an amount that reflects the consideration to which the entity expects to be entitled in exchange for promised goods or services to customers.

The new standard replaces all the existing requirements concerning revenue recognition in accordance with IFRS.

The Five-step model includes:

Identifying the contract with a customer

A contract with a customer meets its definition when all the following criteria are met: the parties to the contract have approved the contract and are committed to perform their respective obligations; the Group can identify each party's rights regarding the goods or services to be transferred; the Group can identify the payment terms for the goods or services to be transferred; the contract has commercial substance; and it is probable that the Group will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer.

Identifying performance obligations

At contract inception, the Group assesses the goods or services promised in a contract with a customer and identifies as a performance obligation each promise to transfer to the customer either a good or service (or a bundle of goods or services) that is distinct or a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

Determining the transaction price

The Group considers the terms of the contract and its customary business practices to determine the transaction price. The transaction price is the amount of consideration to which the Group expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes, fuel charge, excise duty).

The consideration promised in a contract with a customer may include fixed amounts, variable amounts, or both.

Allocating the transaction price to each performance obligation

The objective when allocating the transaction price is for the Group to allocate the transaction price to each performance obligation (or distinct good or service) in an amount that depicts the amount of consideration to which the Group expects to be entitled in exchange for transferring the promised goods or services to the customer.

Recognition of revenue at the moment of satisfaction of performance obligations

The Group recognizes revenue when (or as) the Group satisfies a performance obligation by transferring a promised good or service (i.e. an asset) to a customer (the customer obtains control of that asset). Revenue is recognized as the amounts of the transaction price that is allocated to that performance obligation. The Group transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognizes revenue over time, if one of the following criteria is met:

- the customer simultaneously receives and consumes the benefits provided by the Group's performance as the Group performs;
- the performance creates or enhances an asset that the customer controls as the asset is created or enhanced;
- the performance does not create an asset with an alternative use to the Group and the Group has an enforceable right to payment for performance completed to date.

The Medicalgorithmics Group operates in the field of advanced telemedicine technologies and is a provider of cardiac diagnostic solutions, particularly in the field of ECG analysis. In its records, the Group recognizes the following types of revenue:

- Revenue from sales of a cardiac diagnostic system (the PocketECG system)
- Revenue from diagnostic services

<u>Revenue from sales of cardiac diagnostic devices</u>

At the consolidated level, revenue from the sales of the PocketECG system represents a marginal part of the Group's revenue (Note 7 to these financial statements). This revenue is generated by Medicalgorithmics S.A. This Company operates on a subscription model, which means that it derives revenue from sales of devices, and then from subscriptions for their use and use of the related software and server infrastructure.

In the opinion of the Management Board, according to the economic substance of the contracts, sales of the PocketECG system and the PocketECG system maintenance services constitute a single performance obligation the use of the PocketECG device depends to a large extent on the use of the software and server infrastructure).

The Group transfers control of the system over time and, therefore, satisfies a performance obligation and recognizes revenue over time. The progress towards satisfaction of the obligation is determined by the Group using input methods.

Revenue is measured on the basis of the transaction price to which the Group expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties. The estimated transaction price reflects a reliable estimate of the expected contractual consideration based on the entity's experience and capacity to satisfy such performance obligations.

An estimate of the transaction price includes any expectations known to the entity in the prevailing contractual or business circumstances about the actual amount of consideration for the transfer of the goods or services, including, in particular, those that result in a price concession. The transaction price includes the part of variable consideration for which it is highly probable that no adjustment of a significant portion of revenue will be necessary in the future.

A reliable estimate of the transaction price is assessed at each balance sheet date.

Revenue from services

The Group’s primary source of revenue is the sales of diagnostic services provided to patients in the United States. Actual revenue of the Capital Group are generated mainly at the level of insurers refunding medical services performed using PocketECG devices. Recipients of services provided by the Capital Group include primarily hospitals, hospital networks, clinics, doctors, doctors’ groups.

As regards services provided, the Group recognizes revenue when the performance obligation is satisfied. Satisfaction of a performance obligation is understood as the performance of a patient's ECG examination service using a Pocket ECG device and the analysis of the results of the examination. Revenue is recognized on a one-off basis when the examination is completed and settled.

The Group collaborates with the majority of private insurers without any long-term contracts determining the rates for examinations. Revenue is measured on the basis of the estimated transaction price to which the Group expects to be entitled in exchange for the examination service. In accordance with industry practice, the Group applies a model where revenue estimates are based on historical cash inflows for the services provided. The insurer's rates for each type of examination are estimated on the basis of average payments during the 12-month period ending six months before the date of assessment. An estimate of the transaction price includes any expectations known to the entity in the prevailing contractual or business circumstances about the actual amount of consideration for the performance of particular types of examinations. A reliable estimate of the transaction price is assessed at each balance sheet date.

Historical analyses of payments for services enabled the estimation that the average payment period for services provided is up to 9 months. After this period, impairment losses are recognized for all outstanding receivables.

5.13. Finance income and costs

Finance income comprises interest income on funds invested by the Capital Group, fair value gains on financial instruments at fair value and realized differences between the purchase price and the price at which financial assets measured at fair value through profit or loss are sold or exchanged. Interest income is recognized in profit or loss of the period on the accrual basis using the effective interest rate method. Income from fair value measurement (including of transactions completed) is recognized in profit or loss of the period on the accrual basis, using the fair value measurement methods.

Finance costs comprise interest expense on borrowings, impairment losses recognized on financial assets and fair value losses on financial instruments at fair value.

Foreign exchange gains and losses are reported on a net basis under finance income or finance costs, as appropriate.

5.14. Income tax

Deferred tax assets and liabilities are offset if the Capital Group has a legally enforceable right to offset current tax liabilities and assets, and if they relate to income taxes levied by the same tax authority on the same taxable entity, or on different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realize the assets and settle the liabilities simultaneously.

Deferred tax assets are recognized in respect of tax loss carryforwards, tax credits and deductible temporary differences only to the extent that it is expected that taxable income will be generated against which such assets can be realized.

Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Income tax comprises current and deferred tax. Current and deferred income tax is recognized in profit or loss for the period except to the extent that it relates to a business combination or items recognized directly in equity or in other comprehensive income.

Current tax is the expected income tax payable or receivable in respect of taxable income for the year, determined using tax rates enacted or substantively enacted at the reporting date, and any adjustment to income tax payable in respect of previous years' income.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities and their amounts used for tax purposes. Deferred tax is not recognized for the following temporary differences: initial recognition of assets or liabilities from a transaction that is not a business combination and that affects neither profit or loss for the period, nor taxable income, differences relating to investments in subsidiaries and jointly controlled entities to the extent it is not probable they will be disposed of in the foreseeable future. In addition, deferred tax is not recognized in relation to temporary differences arising on initial recognition of goodwill. Deferred tax is measured at tax rates that are expected to be applied when temporary differences reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

6. Segment reporting

The core business of the Capital Group comprises:

- provision of ECG monitoring services;
- scientific research and development;
- manufacture of electro-medical equipment;
- provision of information technology and biotechnology services.

The Capital Group operates mainly outside of Poland, particularly in the US. The operations are classified within a single segment, which includes both sales of diagnostic and IT services, and devices that are products related to the services offered.

In the reporting period, the Group did not discontinue any operations and no operations are expected to be discontinued in the following period.

The Capital Group identifies its operating segments in accordance with IFRS 8 "Operating segments".

In accordance with IFRS 8, operating segments should be identified based on internal reports on those elements of the Capital Group that are regularly reviewed by the decision makers who make decisions about resources to be allocated to the segment and assess its performance. On this basis, the Capital Group identifies only one operating segment, comprising the provision of systemic and algorithmic solutions for cardiac diagnostics, particularly for ECG analysis. This segment comprises sales of services and the supply of cardiac diagnostic devices that enable these tasks to be accomplished.

As there is only one operating segment, the Capital Group does not present separate financial data for this segment. Accordingly, all its assets and liabilities as well as revenue and expenses are allocated to this segment. At the Capital Group level, the Management Board does not review the results of operations by any other types of activities and does not have separate financial data.

7. Sales revenue structure

By type	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Revenue from sales of services	197 597	202 609
Revenue from sales of devices	1 807	745
Total revenue	**199 404**	**203 354**

By territory	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Domestic sales	546	394
Export sales	198 858	202 960
Total revenue	**199 404**	**203 354**

The decrease in revenue was largely attributable to a 3% decline in the average USD/PLN exchange rate and a decrease in revenue from other partners, excluding Medi-Lynx, related to the termination of collaboration with AMI/Spectocor in February 2017.

These declines were partially offset by an organic increase in Medi-Lynx revenue (+3%).For detailed information, see Section III.1 of the Directors' Report on the operations of the Medicalgorithmics Capital Group and Medicalgorihmics S.A. in 2018.

8. Employee benefits

	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Remuneration	(108 416)	(103 092)
Incentive scheme	-	(2 142)
Social security and other employee benefits	(2 133)	(1 347)
	(110 549)	**(106 581)**

The increase in costs of employee benefits was caused primarily by an increase in the headcount due to the need to handle the planned increased volume of patients after the acquisition of AMI/Spectocor's client base. For detailed information, see Section III.1 of the Directors' Report on the operations of the Medicalgorithmics Capital Group and Medicalgorihmics S.A. in 2018.

9. Amortization and depreciation

The annual depreciation and amortization expense amounted to PLN 11,579 thousand and decreased as compared to 2017 mainly due to the lower average USD/PLN exchange rate.

The most significant component of the amortization and depreciation expense is the amortization of client bases held by the Group (the Medi-Lynx client base recognized as a result of the final settlement of the purchase price and AMI/Spectocor client base acquired following the settlement agreement of 28 December 2016). According to the Management Board's estimates, the client bases will bring economic benefits and will be amortized over a period of 20 years. The cost of amortization in 2018 amounted to PLN 5 728 thousand.

Due to the fact that the Group classifies the PocketECG devices as fixed assets, the value of the equipment used by Medi-Lynx to provide diagnostic services is depreciated over a period of 3 years.

In 2018, the total cost resulting from the above amounted to PLN 2 988 thousand (PLN 3 694 in 2017).

10. Third-party services

	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Lease and rental	(5 355)	(4 376)
Telecommunication and Internet services	(5 130)	(5 945)
IT services	(694)	-
Accounting and financial audit services	(1 557)	(1 667)
Advisory services	(4 876)	(4 741)
Transport and courier services	(5 673)	(4 681)
Monitoring services	(2 464)	(1 994)
Leases	(21)	(101)
Maintenance services	(2 126)	(2 065)
Marketing services	(2 854)	(1 954)
Other third-party services	(3 081)	(2 887)
	(33 831)	**(30 411)**

In the reporting period, the Group recorded an increase in costs of third-party services, as compared to the corresponding period. It is mainly attributable to an increase in lease and lease costs related to the lease of additional office space in Warsaw and servers, an increase in transport costs related to higher volume of examinations and higher costs of marketing services related to an intensive marketing and sales campaign launched in the second quarter of 2017, as well as to monitoring services. Additionally, in 2018 – unlike in the corresponding period – the Company incurred costs of IT services. IT services include consultancy on programming and maintenance of the IT environment. For more information, see Section III.1 of the Directors' Report on the operations of the Medicalgorithmics Capital Group and Medicalgorithmics S.A. in 2018.

11. Other operating revenue and expenses

	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Settlement of subsidies	315	509
Reversal of impairment losses on receivables	-	213
Other	33	26
Other operating revenue	**348**	**748**
Impairment losses on receivables	(96)	-
Impairment losses on inventories	(680)	-
State tax	(1 405)	-
Other	(1 592)	(1 233)
Other operating expenses	**(3 773)**	**(1 233)**

Other operating expenses for the period from 1 January 2018 to 31 December 2018 include USD 0.4 million of costs of additional tax liability in Medi-Lynx, identified following a tax audit and recognized in the second quarter of 2018.

On 21 August 2018, the Company notified in its current report No 30/2018 of a tax audit carried out by the Texas Controller of Public Accounts which identified a potential sales tax and excise tax liability of USD 1.9 million on the part of Medi-Lynx for the period from 1 July 2014 to 31 December 2017.

As announced in Current Report No 31/2018, the Group received an opinion of tax advisors which pointed to significant irregularities in the findings of the Office regarding a significant portion of the potential tax liability (USD 1.5 million).

Based on the opinion of tax advisors, the Management Board of the Company decided to include in the financial result for 2018 the cost of the undisputed portion of the tax liability, amounting to USD 0.4 million. This liability was paid by Medi-Lynx in the third quarter of 2018.

Due to significant doubts as to the correctness of the Office's findings, the Management Board decided to submit a request for reconsideration of the matter concerning the disputed portion of the liability and to refrain from recognizing a provision for this portion.

For detailed information on the tax audit, see Current Report No 30/2018 and Current Report No 31/2018.

In the reporting period, the Company recognized an impairment loss on inventories of PLN 680 thousand in other operating expenses, relating primarily to components used in the production of PocketECG CDMA equipment, from which the Group is departing.

12. Finance income and costs

	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Interest income	130	14
Foreign exchange differences	518	-
Revaluation of investments at fair value through profit or loss	-	600
Other	64	-
Finance income	**712**	**614**
Interest	(3 512)	(4 107)
Foreign exchange differences	-	(1 356)
Other	(351)	(379)
Finance costs	**(3 863)**	**(5 842)**
Net finance costs	**(3 151)**	**(5 228)**

13. Effective tax rate

	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Profit before tax	21 573	36 592
Tax at the tax rate applicable in Poland	(4 099)	(6 952)
Non-tax-deductible costs	(310)	(342)
Difference between the tax rate in Poland and USA	(303)	(1 431)
Amortization of goodwill for tax purposes	1 582	2 044
Effect of US tax rate change	-	862
Relief for Research and Development	485	240
Non-taxable revenue	63	102
Other tax-deductible costs (e.g. settlement with DOJ)	-	1 027
Other	(43)	1 511
Tax reported in the statement of comprehensive income	**(2 625)**	**(2 939)**

Following the change in the tax rate in the United States from 34% to 21%, which came into force on 1 January 2018, the Group remeasured its deferred tax liabilities as at 31 December 2017.

As a result of this change, in the corresponding period the Group obtained a tax benefit of approximately PLN 862 thousand.

14. Deferred tax assets and liabilities

	31.12.2018	31.12.2017
Exchange differences on investments in subsidiaries	500	1 500
Provision for costs	575	1 210
Impairment losses on inventories	129	-
Interest on bonds	101	102
Valuation of FIZ certificates	120	202
Costs of acquisition of Medi-Lynx *	339	339
Other	67	161
Gross deferred tax assets	**1 831**	**3 514**

	31.12.2018	31.12.2017
Difference between the tax base and book value of intangible assets and property plant and equipment	2 285	1 573
Settlement of expenditure on Research and Development	849	364
Other	172	313
Gross deferred tax liabilities	**3 306**	**2 250**

	31.12.2018	31.12.2017
Change in deferred tax reported in the statement of comprehensive income	**(1 730)**	**2 838**
Change in deferred tax recognized directly in equity	**(1 009)**	**-**
Net deferred tax assets/liabilities of which:	**(1 475)**	**1 264**
Deferred tax assets	1 831	3 514
Deferred tax liabilities	(3 306)	(2 250)

* Included in the acquisition price of the Company for tax purposes and in current expenses for accounting purposes.

15. Intangible assets

Gross value of intangible assets	Goodwill	Client bases	Costs of completed development works	Development works in progress	Other	Total
Gross value as at 1 January 2018	**77 482**	**110 103**	**5 937**	**13 148**	**1 864**	**208 534**
Increases	766	-	-	4 640	572	**5 978** *
Decreases	-	-	-	-	-	**-**
Foreign exchange differences	6 145	8 805	-	-	57	**15 007**
Gross value as at 31 December 2018	**84 393**	**118 908**	**5 937**	**17 788**	**2 493**	**229 519**
Accumulated amortization and impairment losses						
Accumulated amortization and impairment losses as at 1 January 2018	**-**	**5 505**	**5 027**	**-**	**1 102**	**11 634**
Amortization	-	5 945	455	-	554	**6 954** *
Foreign exchange differences	-	440	-	-	37	**477**
Accumulated amortization and impairment losses as at 31 December 2018	**-**	**11 890**	**5 482**	**-**	**1 693**	**19 065**
Net value						
As at 1 January 2018	**77 482**	**104 598**	**910**	**13 148**	**762**	**196 900**
As at 31 December 2018	**84 393**	**107 018**	**455**	**17 788**	**800**	**210 454** *

* the increases in the gross value, accumulated amortization and net value relate to, among others, intangible assets acquired as a result of the acquisition of shares in Medicalgorithmics Polska Sp. z o.o. (formerly: Kardiosystem Monitoring Sp. z o.o.). As at 31 December 2018, the net value of intangible assets recognized in the Group's consolidated financial statements on account of the acquisition of the subsidiary, Medicalgorithmics Polska, amounted to approximately PLN 27 thousand.

Gross value of intangible assets	Goodwill	Client bases	Costs of completed development works	Development works in progress	Other	Total
Gross value as at 1 January 2017	**92 890**	**132 179**	**5 937**	**9 723**	**1 791**	**242 520**
Increases	-	-	-	3 425	213	**3 638**
Foreign exchange differences	(15 408)	(22 076)	-	-	(140)	**(37 624)**
Gross value as at 31 December 2017	**77 482**	**110 103**	**5 937**	**13 148**	**1 864**	**208 534**
Accumulated amortization and impairment losses						
Accumulated amortization and impairment losses as at 1 January 2017	**-**	**-**	**4 311**	**-**	**826**	**5 137**
Amortization	-	5 505	716	-	343	**6 564**
Foreign exchange differences	-	-	-	-	(67)	**(67)**
Accumulated amortization and impairment losses as at 31 December 2017	**-**	**5 505**	**5 027**	**-**	**1 102**	**11 634**
Net value						
As at 1 January 2017	**92 890**	**132 179**	**1 626**	**9 723**	**965**	**237 383**
As at 31 December 2017	**77 482**	**104 598**	**910**	**13 148**	**762**	**196 900**

Goodwill

a. Medi-Lynx Cardiac Monitoring LLC

Company	Acquisition date	Acquired share in net assets	Acquisition price (USD '000)	Fair value of acquired net assets (USD '000)	Goodwill (USD '000)
Medi-Lynx Cardiac Monitoring LLC	30.03.2016	75%	34 210	11 984	22 226

On 30 March 2016, Medicalgorithmics S.A. acquired 75% of shares in Medi-Lynx with its registered office in Plano, Texas, USA, through its subsidiary, MGD HoldCo.

The acquisition of the subsidiary resulted in the creation of a positive goodwill on acquisition of Medi-Lynx in the consolidated financial statements of the Medicalgorithmics Capital Group. A goodwill is the excess of the consideration paid over the fair value of the acquired identifiable net assets of the subsidiary. The goodwill determined as at 31 December 2016 amounted to USD 22 226 thousand.

Goodwill is tested for impairment on an annual basis (or more frequently if there are any indications of impairment). Impairment losses are recognized as an expense in the period and are not reversed in the subsequent period. As a result of the test conducted at the end of 2018, the Parent Company's Management Board did not find any indications of impairment of goodwill.

Goodwill is amortized for tax purposes at the level of the subsidiary, MDG HoldCo (included in the consolidated financial statements). As at 31 December, the remaining tax value of goodwill to be amortized amounts to USD 25 470 thousand.

Goodwill recognized on acquisition results mainly from the service business model adopted by Medi-Lynx, based primarily on human capital and relations with medical units. These main components enable the provision of top quality medical services in a very prospective US market.

In particular, the following measurable benefits from the acquisition are expected:

- an increase in turnover on the US market;
- improved utilization of PocketECG devices;
- increased efficiency of product distribution channels.

b. Medicalgorithmics Polska Sp. z o.o. (formerly: Kardiosystem Monitoring Sp. z o.o.)

On 2 July 2018, the Company acquired all shares in Kardiosystem Monitoring sp. z o.o. The price for acquiring shares in Kardiosystem was PLN 167 thousand, wherein the contract provides for additional payment up to PLN 350 thousand due in 2019–2023 depending on achieving assumed yearly sales goals. On 26 November 2018, the company changed its name to Medicalgorithmics Polska Sp. z o.o.

The acquisition of the subsidiary resulted in the creation of a positive goodwill on acquisition of Medicalgorithmics Polska Sp. z o.o. in the consolidated financial statements of the Medicalgorithmics Capital Group. A goodwill is the excess of the consideration paid, value of shares in the subsidiary and fair value as at the date of acquisition of shares in the subsidiary's share capital over the fair value of the acquired identifiable net assets of the subsidiary.

The financial effects of the acquisition of shares in Medicalgorithmics Polska Sp. z o.o. were accounted for in the financial statements for the third quarter of 2018 on the basis of fair value estimates. As at 31 December 2018, the Capital Group adjusted the preliminary amounts recognized in connection with the acquisition of Medi-Lynx.
The goodwill determined as at 31 December 2018 amounted to USD 766 thousand.

Company	Acquisition date	Acquired share in net assets	Acquisition price (PLN '000)	Fair value of acquired net assets (PLN '000)	Goodwill (PLN '000)
Medicalgorithmics Polska Sp. z o.o.	02.07.2018	100%	167	(599)	766

Goodwill is tested for impairment on an annual basis (or more frequently if there are any indications of impairment). Impairment losses are recognized as an expense in the period and are not reversed in the subsequent period. In 2018 impairment of assets indication were not found.

Net sales revenue and net profit (loss) of Medicalgorithmics Polska for the period from 1 January 2018 to the acquisition date are presented in the following table:

Company	Acquisition date	Net loss until the date of acquisition of shares (PLN '000)	Revenue until the date of acquisition of shares (PLN '000)
Medicalgorithmics Polska Sp. z o.o.	02.07.2018	(145)	556

The Management Board estimates that had the acquisition of Medicalgorithmics Polska occurred on 1 January 2018, the total aggregated revenue of the Medicalgorithmics Group for 2018 would have amounted to PLN 199 960 thousand, and the aggregated net profit for that period would have amounted to PLN 18,794 thousand. At the same time, the Management Board believes that the fair value of assets and liabilities as at 1 January 2018 would be similar to the fair value of assets and liabilities as at the acquisition date, i.e. 2 July 2018.

The main purpose for purchasing Medicalgorithmics Polska was to combine the sales forces of both companies and to create a common range of systems for arrythmia diagnostics and cardio tele rehabilitation addressed to hospitals and doctor's surgeries in Poland. This will facilitate an increase in sales of the Group's products and services on the Polish market.

Medicalgorithmics Polska's competitive advantage comprises a qualified and experienced team of physicians and electro-cardiology technicians who are responsible for analyzing ECG records and preparing detailed diagnostic reports from tests. Furthermore, Medicalgorithmics Polska has permanent relationships with heath care facility representatives in Poland. Medicalgorithmics Polska provides analysis and monitoring services with respect to cardiac telemetry at the heart monitoring center, and the Company's sales department is responsible for acquiring new customers and after-sales service.

Accounting for the financial effects of the acquisition of shares in Medicalgorithmics Polska is presented below (PLN '000):

	Fair values recognized on acquisition of shares
Intangible assets	34
Property plant and equipment	502
Non-current assets	**536**
Trade and other receivables	143
Cash and cash equivalents	-
Current assets	**143**
Total assets	**679**
Credits and loans	1 088
Trade and other liabilities	190
Total liabilities	**1 278**
NET ASSETS	**(599)**
Acquired share in net assets	100%
Fair value of acquired net assets	(599)
Purchase price	167
Goodwill	**766**

Client bases

a. Medi-Lynx's client base (net value at the balance sheet date: USD 11 368 thousand)

Following the acquisition of shares in Medi-Lynx, a client base was identified in the process of allocating the purchase price. The client base contains data on:

- clients;
- types of services provided to them (examinations carried out);
- major payers – insurers covering the costs of the examinations performed.

The client base was valued using the comparative method (second level of the fair value hierarchy). The Medi-Lynx's client base was valued based on a transaction in which similar client bases were purchased from two unrelated entities, AMI/Spectocor. This transaction was carried out by the Capital Group in December 2016.

b. AMI client base (net value at the balance sheet date USD 17 096 thousand)

In December 2016, the Capital Group acquired a client base from two companies, AMI and Spectocor. This base contains a similar structure, divided into the same major payers and the same types of examinations as the identified Medi-Lynx's client base. The purchase price of the AMI/Spectocor's base amounted to USD 18 995 thousand.

The Group tests its customer bases for impairment on an annual basis and amortizes their value over a period of 20 years from the date of acquisition. Following customer retention tests, the Group did not revise its estimates of the economic useful lives of the client bases acquired.

Impairment test

As at 31 December 2018, the Group tested the goodwill recognized on acquisition of subsidiaries and Medi-Lynx and AMI client bases. The tests indicated no need to recognize any impairment losses. The Management Board believes that no reasonably possible change of any of the key assumptions referred to above could result in the carrying amount of the CGUs exceeding their recoverable amount.

The impairment test was carried out on the basis of calculation of expected cash flows, estimated based on historical performance and expectations concerning the future growth of the market. Cash flow projections for identified cash generating units have been prepared on the basis of assumptions derived from historical experience adjusted to the plans in progress. These cash flows represent the best estimate of the Management Board for the next 4 years.

Main assumptions underlying the computation of the value in use are as follows:

- Expected increase in the Group's revenue derived from the expected average rates for examinations and the expected volume of examinations – in the context of a change in the business model and signing long-term service contracts directly with key private insurers (i.e. in-network contracts).

  The Group assumes that if this model is changed, although it will result in lower reimbursement rates for a single service, the Group will secure access to new clients and, as a consequence, significantly increase the sales volume. The Group is of the opinion that this strategy will allow the Group to achieve sustained annual revenue growth and implement its business growth strategy, as well as increase the security and stability of the Group's revenue. The Group assumes:

- gradual signing of long-term contracts between 2019 and 2022. In the last year of the forecast, long-term contracts will account for approximately 65% of Medi-Lynx's revenue,
- year-on-year increase in the volume of examinations in 2019-2022 as a result of increased share of long-term contracts (at least 11% in 2019 and 17-18% in 2020-2022),
- A decrease in average rates per examination by 20-58% depending on the service provided, however, the share of Event-type examination, where the biggest drop in average rate for examination is expected, will be gradually reduced in the structure of revenue.

According to the Group's best estimates, the growth will be generated primarily by new customers. At the same time, the cash flows generated from the recognized client bases will remain at a similar level.

- Discount rate based on the weighted average cost of capital and reflecting the current market assessment of the time value of money and the risk related to the business object of the cash-generating unit. For the purpose of the test, the WACC of 11.87% was applied as the discount rate.
- Growth rate after the forecast period at the level of 1%.
- In order to effect a change in the business model, the Management Board estimates the average year-on-year increase in operating expenses at approximately 13%. This increase will be driven by increased sales activities and will primarily relate to salaries of the sales department, marketing expenses and business travel expenses.

The values assigned to the above assumptions and other variables reflect the Group's experience adjusted for expected changes in the period covered by the business plan; however, they may be affected by unforeseeable economic, political or legal developments.

In addition, the Group carried out a sensitivity analysis of the test outcome to changes in the discount rate and sensitivity analysis of the assumptions underlying the change in the business model with respect to the increase in the volume of examinations and the rate for examinations. The sensitivity analysis did not indicate that a change in assumptions would lead to the recognition of impairment losses, i.e. the carrying amount would not be higher than the recoverable amount.

The estimated recoverable amounts (USD ‘000) are as follows:

	Net value as at 31 December 2018	**Estimated recoverable amount**
Goodwill of Medi-Lynx	22 226	35 297
Medi-Lynx client base	11 368	25 241
AMI client base	17 096	20 739

Costs of completed development works

As at the balance sheet date, expenditure on development works was capitalised by the Capital Group as intangible assets. The object of the development works is the PocketECG system. It is currently the most technologically advanced solution offered by the Group. The basic technological advantage of the solution is the integration of the device, which previously consisted of two separate components, into a specially developed recorder of a smartphone type based on the Android operating system. Moreover, the functionality of the device has been extended. Medicalgorithmics was awarded financial support for the implementation work in the project, concerning the development of earlier versions of the system within the framework of the programme of the Foundation for Polish Science – Innovator. The net value of the project is PLN 455 thousand. The project will be amortized until 31 December 2019.

The above development works were carried out in part with co-financing from European Union funds, whose non-amortized value as at 31 December 2018 amounted to PLN 315 thousand (31 December 2017: PLN 629 thousand). According to the rules adopted by the Capital Group, the value of subsidies received is recorded under deferred income and recognized over time in accordance with the period of amortization of the development expenditure incurred.

Development works in progress

The Group conducts a number of development works to improve the existing products and services, and also develops new solutions. At present, the key development projects for the Group are:

- PocketECG CRS – device and system for cardiac rehabilitation;
- PocketECG 12Ch – device and system for remote, instant ECG description (12-channel ECG).
- ECG TechBot – software using a set of algorithms for automatic analysis and interpretation of the ECG signal based on deep learning methods.

Early this year, the company launched the promotion the remote cardiac rehabilitation system, PocketECG CRS. Pilot implementations were carried out in several renowned hospitals in Poland. The PocketECG CRS was cleared by the Food and Drug Administration (FDA) under the procedure 510(k). Following FDA'a approval, the Company will soon initiate actions to commercialize the new system in the U.S.

As part of the ECG Techbot project, the research team continued work on a set of algorithms for automatic analysis and interpretation of ECG signal (algorithms for rhythm analysis, classification of morphology, detection of waves).

As regards PocketECG 12Ch, the work was suspended at the stage of the YOKE prototype. The development of algorithms continues under the TechBot project, and work on the complete product (HW+SW) will resume after the global version of the PDA with LTE has been developed.

The PocketECG CRS PocketECG 12Ch projects are financed from own funds. ECG TechBot is co-financed by the National Centre for Research and Development (“NCBiR”) from public funds. The estimated total cost of project implementation as well as the total amount of eligible costs is PLN 11 188 thousand, with the maximum value of co-financing set at PLN 6 335 thousand.

Key costs capitalized as development works in progress include the costs of salaries of the R&D staff. As at the balance sheet date, the Group updated its assessment of the potential of target markets and the impact of commercialization of new products on the Group's performance. With respect to PocketECG CRS, the potential of the US, Canadian, Indian and Polish markets will allow the product to be commercialized in the coming periods and generate sufficient cash flows to cover the expenditures incurred. In the case of PocketECG 12Ch, the launch of commercialization is scheduled for 2022. In the opinion of the Management Board of the Company, development works will be completed and will produce the expected economic effects.

16. Property plant and equipment

Gross value of property plant and equipment	Buildings and structures	Machinery and equipment, including computer hardware	Other fixed assets	Leasehold improvements	Total
Gross value as at 1 January 2018	**1 816**	**22 805**	**1 821**	**480**	**26 922**
Increases	376	4 360	195	152	**5 083** *
Decreases	-	(92)	(4)	-	**(96)** *
Change in inventories	-	(2 768)	-	-	**(2 768)**
Foreign exchange differences	146	1 059	123	-	**1 328**
Gross value as at 31 December 2018	**2 338**	**25 364**	**2 135**	**632**	**30 469**
Accumulated depreciation and impairment losses					
Accumulated depreciation and impairment losses as at 1 January 2018	**413**	**7 860**	**1 255**	**145**	**9 673**
Depreciation	220	4 676	480	55	**5 431** *
Foreign exchange differences	22	578	80	-	**680**
Accumulated depreciation and impairment losses as at 31 December 2018	**655**	**13 114**	**1 815**	**200**	**15 784**
Net value					
As at 1 January 2018	**1 403**	**14 945**	**566**	**335**	**17 249**
As at 31 December 2018	**1 683**	**12 250**	**320**	**432**	**14 685** *

* the increases in the gross value, accumulated amortization and net value relate to, among others, fixed assets acquired as a result of the acquisition of shares in Medicalgorithmics Polska Sp. z o.o. (formerly: Kardiosystem Monitoring Sp. z o.o.).

As at 31 December 2018, the net value of fixed assets recognized in the Group's consolidated financial statements on account of the acquisition of the subsidiary, Medicalgorithmics Polska, amounted to approximately PLN 418 thousand.

Gross value of property plant and equipment	Buildings and structures	Machinery and equipment including computer hardware	Other fixed assets	Leasehold improvements	Total
Gross value as at 1 January 2017	**1 501**	**23 189**	**2 340**	**381**	**27 411**
Increases	566	3 475	415	99	**4 555**
Decreases	-	-	(522)	-	**(522)**
Change in inventories	-	(1 854)	-	-	**(1 854)**
Foreign exchange differences	(251)	(2 005)	(412)	-	**(2 668)**
Gross value as at 31 December 2017	**1 816**	**22 805**	**1 821**	**480**	**26 922**
Accumulated depreciation and impairment losses					
Accumulated depreciation and impairment losses as at 1 January 2017	**129**	**3 922**	**1 145**	**103**	**5 299**
Depreciation	306	4 524	248	42	**5 120**
Foreign exchange differences	(22)	(586)	(138)	-	**(746)**
Accumulated depreciation and impairment losses as at 31 December 2017	**413**	**7 860**	**1 255**	**145**	**9 673**
Net value					
As at 1 January 2017	**1 372**	**19 267**	**1 195**	**278**	**22 112**
As at 31 December 2017	**1 403**	**14 945**	**566**	**335**	**17 249**

The Capital Group neither recognized nor reversed any impairment losses. The Capital Group does not use fixed assets under finance lease agreements. However, the Company is a lessee under operating lease agreements. Payments on this account are disclosed in Note 26 to these financial statements. The Capital Group has no liabilities secured on its assets.

Recognition of PocketECG devices at the consolidated level in 2018

From the Group's perspective, PocketECG devices meet the definition of fixed assets. Therefore, they are disclosed as non-current assets in the consolidated financial statements, whereas at the Parent Entity level they are disclosed as inventories. As at 31 December 2018, the Group reviewed the assumptions for the economic useful lives of PocketECG CDMA devices and decided to accelerate their depreciation. These devices will remain in service and will be fully depreciated by the end of 2019.

17. Financial assets

	31.12.2018	31.12.2017
Investment certificates	5 942	14 936
Shares	200	200
Financial assets	**6 142**	**15 136**
of which long-term portion	200	10 910
of which short-term portion	5 942	4 226

Investment certificates

As at 31 December 2018, the Group holds 61,699 investment certificates of the fund Bezpiecznych Obligacji Fundusz Inwestycyjny Zamknięty (the "Fund") managed by Copernicus Capital TFI S.A. (the "Investment Fund Company"). As at 31 December 2018, the value of a single investment certificate was determined at PLN 96.31. The fair value of a single certificate is measured by the Investment Fund Company. The Fund invests primarily in debt securities quoted on the Catalyst market (level 1 of the fair value hierarchy). Investment certificates are measured at fair value through profit or loss.

On 6 April 2018, 42 500 certificates of the total value of PLN 4,276 thousand were redeemed. On 4 October 2018, further 46 000 certificates of the total value of PLN 4 586 thousand were redeemed. After the balance sheet date, i.e. on 28 January 2019, the Company requested the redemption of the remaining 61,699 certificates. They will be redeemed at the beginning of April 2019. As at 31 December 2018, the Company reported all investment certificates held (with a total value of PLN 5 942 thousand) as short-term financial assets.

18. Receivables

	31.12.2018	31.12.2017
Trade receivables	18 277	19 612
Budgetary receivables	2 072	1 058
Other receivables	62	269
Prepayments and deferred expenses	2 370	3 012
	22 781	**23 951**
Long-term	-	-
Short-term	22 781	23 951

The fair value of receivables approximates their book value. As at 31 December 2018, the total value of past due trade receivables for which no impairment losses were recognized amounts to PLN 1 516 thousand.

For information on the Capital Group's exposure to credit and currency risk on receivables, see Note 24.

	31.12.2018	31.12.2017
Insurance policies and deposits	1 247	665
Trade fairs	133	114
Subscriptions	6	23
Advisory services	19	19
Prepaid employee benefits	112	859
IT costs – licenses software	195	280
Prepaid rental costs	280	163
Other	378	889
Prepayments and deferred expenses	**2 370**	**3 012**
Long-term portion	-	-
Short-term portion	2 370	3 012

The ageing structure of trade receivables as at the end of the reporting period was as follows:

	Gross value	Impairment write-down	Net value
non-matured	16 762	-	16 762
past due 1-30 days	1 211	-	1 211
past due 31-60 days	146	-	146
past due more than 61 days	261	103	158
	18 380	**103**	**18 277**

Receivables recognized by the Group in the US in relation to insurers who reimburse service fees are estimated based on the Group's actual cash inflow. Historical analyses of payments for services enabled the estimation that the average payment period for services provided is up to 9 months. After this period, impairment losses are recognized for all outstanding receivables. According to the accounting policy, the impairment loss on estimated payments from insurers is deducted directly from the amount of revenue from sales of medical services. Following the analyses carried out, the Group did not recognize any impairment losses on receivables in 2018.

19. Cash and cash equivalents

	31.12.2018	31.12.2017
Cash in hand	7	11
Cash at banks	44 554	22 838
Short-term deposits	15 628	9 682
	60 189	**32 531**

For information on the Capital Group's exposure to interest rate risk and a sensitivity analysis of financial assets and liabilities, see Note 24 of explanatory notes to the financial statements.

The Group invests surplus funds in short-term deposits. The maturity of deposits usually fluctuates around one to two months. The interest rate is fixed and negotiated each time the funds are invested.

20. Equity

20.1. Share capital of the Parent Company

	Ordinary shares ('000)	
	31.12.2018	**31.12.2017**
Number of shares at beginning of period	3 607	3 607
Number of fully-paid shares at end of period	**3 607**	**3 607**

20.2. Ordinary shares

As at 31 December 2018, the registered share capital of the Parent Company was divided into 3,607 thousand ordinary shares with the nominal value of PLN 0.10 each. No shares were issued in 2018.

20.3. Dividends paid

Pursuant to resolution No 16/06/2018 of the Ordinary Shareholders' Meeting of Medicalgorithmics S.A., on 30 July 2018 the Parent Company paid out a dividend to shareholders in the aggregate amount of PLN 5 121 thousand, i.e. PLN 1.42 per share.

The dividend was paid for all 3 607 thousand shares in the Company.

20.4. Basic and diluted earnings per share

	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Profit for the reporting period attributable to shareholders of the Parent Company (in PLN '000)	14 416	25 539
Weighted average number of ordinary shares (in thousands of shares)	3 607	3 607
Basic profit per share in PLN (net profit/weighted average number of shares)	**4.00**	**7.08**
Diluted profit per share in PLN (net profit/weighted average number of diluted shares)	**4.00**	**7.08**

The subscription warrants issued referred to in Note 20.6 have no dilutive effect because the average market value of ordinary shares in a particular period does not exceed the exercise price of warrants (the warrants are not "in the money").

20.5. Shareholding structure of the Parent Company as at the date of publication of the financial statements

Shareholder	Number of shares	% of shares
Aegon OFE	193 863	5.4%
Marek Dziubiński (President of the Management Board)	400 000	11.1%
NN OFE	451 000	12.5%
OFE PZU	365 408	10.1%
Other shareholders	2 196 255	60.9%
Number of shares	**3 606 526**	**100.0%**

In the period from 1 January 2018 to 31 December 2018, the Parent Company did not acquire any treasury shares and does not hold any treasury shares.

20.6. Incentive scheme

On 26 February 2016, the Extraordinary General Meeting adopted an incentive scheme (equity-settled share-based payments) for management staff and key employees of the Company as well as key individuals providing services to the Company, covering the years 2016–2025. For a detailed description of the incentive scheme and conditions of its introduction, see Section I.14 of the Directors' Report on operations of the Medicalgorithmics Capital Group and Medicalgorithmics S.A. in 2018.

As at 31 December 2018, the Company remeasured the incentive scheme based on current estimates regarding the fulfilment of financial criteria. To the best of its knowledge, the Company's Management Board decided to assume that it is impossible to meet the non-market condition. This assumption applies to all tranches of options offered under the incentive scheme (i.e. no non-market conditions will be fulfilled in any of the tranches). In accordance with IFRS 2 "Share based payments", such an assumption has the effect that no amount should be recognized as an expense of the scheme.

Pursuant to the Annex to the Actuarial Report of 1 March 2019, the Company derecognized the provision for future payments of bonuses in the form of equity-settled share-based payments recognized in previous periods. The total effect of the derecognition of the provision recognized in previous years, amounting to PLN 5 312 thousand, was recognized directly in the supplementary capital. The costs of the incentive scheme recognized in 2018 in the amount of PLN 2 227 thousand were derecognized through profit or loss.

21. Provisions

	31.12.2018	31.12.2017
Holiday pay accrual	1 708	1 082
Other	82	88
	1 790	**1 170**

22. Trade and other liabilities accruals and deferred income

	31.12.2018	31.12.2017
Trade liabilities	1 446	2 207
Salaries and wages payable	8 389	5 002
Budgetary liabilities	833	311
Other liabilities	49	2
	10 717	**7 522**
Income tax liabilities	264	311

Accruals and deferred income

	31.12.2018	31.12.2017
Subsidies	700	630
Other	2 258	991
	2 958	**1 621**
of which long-term	386	315
of which short-term	2 572	1 306

Accruals and deferred income include the value of subsidies received by the Capital Group from the European Union funds for development works. For more detail on the object of the subsidy and the corresponding values, see Note 15. Other accruals and deferred income include mainly settlements at Medi-Lynx related primarily to incurred but not yet invoiced costs of services and goods purchased (including monitoring services) and accrued state fees.

23. Liabilities in respect of bonds and other financial liabilities

	31.12.2018	31.12.2017
Liabilities in respect of bonds	50 472	50 274
Liabilities arising from acquisition of shares in Medi-Lynx	15 406	21 407
Financial liabilities	**65 878**	**71 681**
of which long-term	7 479	63 794
of which short-term	58 399	7 887

	Liabilities in respect of bonds	Liabilities arising from acquisition of shares in Medi-Lynx	Total
Value as at 1 January 2018	**50 274**	**21 407**	**71 681**
Interest accrued	2 746	660	3 406
Settlement of issue costs	200	-	200
Interest paid	(2 748)	(284)	(3 032)
Repayment of liability arising from acquisition of shares in Medi-Lynx	-	(6 377)	(6 377)
Value as at 31 December 2018	**50 472**	**15 406**	**65 878**

Issue and redemption of bonds

In the second quarter of 2016, the Group issued 50 000 long-term bonds with a nominal value of PLN 1 thousand each. The term of the bonds is 3 years. Their redemption date is 21 April 2019. The bonds bear interest at a variable rate. The interest rate is set at the base level of WIBOR for six-month PLN deposits (WIBOR 6M) plus a variable interest margin depending on the Company's financial debt ratio. The purpose of the issue was to finance an investment in a subsidiary, Medi-Lynx Cardiac Monitoring, LLC (redemption of short-term A0 series bonds). The remaining portion of proceeds from the issue was used to finance the Company's working capital. Interest on bonds is due on a semi-annual basis. The Group holds own funds sufficient to repay its liabilities on account of bonds issued. The Parent Company also intends to obtain third-party financing in the form of a current credit facility to secure its current liquidity.

Liabilities arising from acquisition of shares in Medi-Lynx

Other financial liabilities also include a promissory note against the seller of Medi-Lynx Cardiac Monitoring, LLC shares, i.e. Medi-Lynx Monitoring. As at 31 December 2018, the outstanding amount was USD 3,980 thousand, including interest accrued in the amount of USD 119 thousand. Payments are spread over two equal instalments amounting to USD 1 990 thousand, payable on 30 March 2019 and 30 March 2020. Liabilities bear interest at a fixed interest rate.

Financial liabilities are measured at amortized cost using the effective interest rate method. The amount presented in short-term financial liabilities corresponds to liabilities in respect of bonds whose redemption date is 21 April 2019 and the next instalment of liability arising from the acquisition of Medi-Lynx, payable on 30 March 2019.

24. Financial risk management

The Capital Group is exposed to the following risks arising from the use of financial instruments:

- credit risk;
- liquidity risk;
- market risk;
- business risk.

The Management Board of the Parent Company is responsible for establishing and supervising the risk management by the Capital Group.

The Capital Group's risk management policy is to identify and analyses the risks to which the Capital Group is exposed, to set appropriate limits and controls, and to monitor the risk and the extent of matching the limits to the risk. The risk management policies and systems are reviewed on a regular basis to take account of changes in the market environment and the Capital Group's business.

Using such tools as training, management standards and procedures, the Capital Group seeks to build a stimulating and constructive control environment, in which all employees understand their respective roles and responsibilities.

This note presents risks classified as financial risks. The analysis of other risk factors is presented in the Directors' Report.

24.1. Credit risk

Credit risk is the risk of financial loss to the Capital Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk is mainly connected with receivables, bonds, loans granted and investment certificates.

The Capital Group's exposure to credit risk results mainly from individual characteristics of each customer. Five largest counterparties generated jointly approx. 77% of the Group's sales revenue in 2018. As at 31 December 2018, receivables from five largest counterparties accounted for about 63% of total trade receivables.
As a result of the acquisition of shares in Medi-Lynx and the acquisition of AMI's client base in 2016, the credit risk has been significantly reduced. Actual revenue of the Capital Group are generated mainly at the level of insurers refunding medical services performed using PocketECG devices. Recipients of services provided by the Capital Group will primarily include hospitals, hospital networks, clinics, doctors, doctors' groups.

Management of credit risk associated with the investment certificates held is the responsibility of the fund managing those assets and follows from the provisions of its statutes. The main components of fund investments in which the Capital Group holds investment certificates are debt securities in the form of bonds listed on the Catalyst market.

Carrying amount of financial assets reflects the maximum exposure to credit risk. The maximum credit risk exposure at the end of the reporting period was as follows:

	31.12.2018	31.12.2017
Financial assets (investment fund certificates)	5 942	14 936
Loans and receivables	20 411	20 939
Cash and cash equivalents	60 189	32 531
	86 542	**68 406**

The maximum credit risk exposure for loans and trade receivables at the end of the reporting period by geographical region and customer type was as follows:

	31.12.2018	31.12.2017
Poland	185	63
United States of America	17 106	19 000
Other regions	986	549
	18 277	**19 612**
Institutional clients	18 277	19 612

24.2. Liquidity risk

Liquidity risk is a risk that the Capital Group may face difficulties in performing its obligations under financial liabilities which should be discharged by payment in cash or by transfer of other financial assets. The Capital Group manages the liquidity risk by ensuring, to the maximum extent possible, that the Capital Group has sufficient liquid assets to pay its liabilities when due, both in business-as-usual and in crisis situations, without exposing the Capital Group to unacceptable losses or reputational damage.

Usually, the Capital Group is provided with sufficient cash on demand to cover the expected operating expenses over a 60-day period, including financial liabilities. However, this policy does not cover extreme situations that cannot be predicted on the basis of rational premises, such as natural disasters. According to the Management Board of the Parent Company, the current proceeds from operations will ensure the Company's financing in 2018. The Capital Group does not expect the projected cash flows, discussed in the maturity analysis, to occur significantly earlier or in amounts materially different from those presented.

31.12.2018	Carrying amount	Contractual cash flows	Less than 12 months	More than 12 months
Credit card debt	39	39	39	-
Liabilities in respect of credits and loans	288	288	72	216
Trade and other liabilities	10 981	10 981	10 981	-
Bonds	50 472	50 472	50 472	-
Other financial liabilities	15 406	15 406	7 927	7 479
	77 186	**77 186**	**69 491**	**7 695**

31.12.2017	Carrying amount	Contractual cash flows	Less than 12 months	More than 12 months
Credit card debt	873	873	873	-
Trade and other liabilities	7 833	7 833	7 833	-
Bonds	50 274	50 274	336	49 938
Other financial liabilities	21 407	21 407	7 551	13 856
	80 387	**80 387**	**16 593**	**63 794**

On 21 April 2019, the Group will redeem the bonds referred to in Note 23 to these financial statements. The Group holds consolidated own funds sufficient to repay its liabilities on account of bonds issued. Furthermore, the Parent Company is at an advanced stage of negotiations aimed at obtaining financing in the form of a current loan to ensure its current liquidity.

24.3. Market risk

Market risk is related to changes in such market factors as foreign exchange rates and interest rates which affect the Capital Group's performance or the value of financial instruments it holds. The objective behind market risk management is to maintain and control the Capital Group's exposure to market risk within assumed limits, while seeking to optimize the rate of return.

In order to manage market risk, the Capital Group may buy and sell derivative instruments and assume financial liabilities. All transactions take place within guidelines set by the Management Board of the Parent Company.

Currency risk

The Group executes most of its transactions in USD. The Group's currency risk is related to the fact that the presentation currency of these financial statements (PLN) is different from the functional currencies of some of the Group's companies (Medi-Lynx, MDG HoldCo).

The table below presents the sensitivity of total income to probable fluctuations in exchange rates on a ceteris paribus assumption. The amounts presented in the table represent a change in the value of the balance sheet item. Exchange differences on translation as at 31 December 2018, assuming a 5% change in the exchange rate of specific currencies as at 31 December 2018.

Impact of financial instruments on total comprehensive income (on account of translation of operations with functional currency other than PLN)	Increase of the exchange rate	Total impact	Decrease of the exchange rate	Total impact
PLN - USD	+5%	5 541	-5%	(5 541)

As at the reporting date, the Parent Company held a loan (granted in USD) granted to a consolidated foreign operation (MDG HoldCo). In accordance with IAS 21, this monetary item forms part of the net investment in a foreign operation. In the consolidated financial statements, foreign exchange differences on these loans (recognized under net finance income in the separate financial statements) are recognized in other comprehensive income. An increase/decrease in the PLN/USD exchange rate by 5% would result in an increase/decrease in foreign exchange differences on intercompany loans being a part of a net investment in a subsidiary presented under foreign exchange differences in the balance sheet by PLN 3,663/(3,663) thousand. The table below presents foreign exchange differences recognized in equity in the consolidated financial statements.

Foreign exchange differences	31.12.2018
Exchange differences on translating foreign operations	(11 415)
Exchange differences on intercompany loans constituting a part of net investments in subsidiaries	5 264
Deferred tax on valuation of exchange differences on loans	(1 000)
	(7 151)

Interest rate risk

The structure of floating-interest-rate financial instruments as at the end of the reporting period is presented below:

	31.12.2018	31.12.2017
Financial assets	-	-
Financial liabilities	50 472	50 274
	50 472	**50 274**

Sensitivity analysis of cash flows from floating-interest-rate financial instruments

A change of an interest rate by 100 basis points would increase (decrease) equity and pre-tax profit by the amounts shown below. The following analysis is based on the assumption that other variables, in particular exchange rates, remain unchanged.

	Profit or loss for current period		Equity	
Effect in PLN '000	Increase by 100 bps	Decrease by 100 bps	Increase by 100 bps	Decrease by 100 bps
31.12.2018				
Floating-rate financial instruments	(97)	98	(97)	98
Sensitivity of cash flows (net)	**(97)**	**98**	**(97)**	**98**
31.12.2017				
Floating-rate financial instruments	(503)	503	(503)	503
Sensitivity of cash flows (net)	**(503)**	**503**	**(503)**	**503**

Comparison between fair values and carrying amounts

The table below presents a comparison between fair values of financial assets and liabilities and values presented in the consolidated statement of financial position:

		31.12.2018		31.12.2017	
	Category according to IFRS	Carrying amount	Fair value	Carrying amount	Fair value
Trade and other receivables	Financial assets at amortized cost	20 411	20 411	20 939	20 939
Investment certificates bonds	Financial assets at fair value through profit or loss	5 942	5 942	14 936	14 936
Cash and cash equivalents	Financial assets at amortized cost	60 189	60 189	32 531	32 531
Trade and other liabilities	Other financial liabilities	10 717	10 717	7 522	7 522
Liabilities in respect of bonds	Other financial liabilities	50 472	50 472	50 274	50 274
Other financial liabilities	Other financial liabilities	15 814	15 814	22 400	22 400

24.4. Business risk

Business risk is related to the Group's business activities and is understood as the risk of incurring losses resulting from adverse changes in the business environment. Nearly 97% of the Group's consolidated revenue is generated from the provision of diagnostic services to patients in the United States, and therefore the Group is exposed to certain risks resulting from the specific nature of the healthcare market in this country.

Key factors of business risk include:

- possible revision of medical examinations refund fees and payments received from private and state insurers. During the reporting period, an event occurred which resulted in a possible reduction of the reimbursement rates and payments received for examinations.

  As disclosed in a current report, on 14 January 2019 a subsidiary, Medi-Lynx, received a notification from MultiPlan Inc., a network of providers of medical services offered to private health insurers. According to this notification, the reimbursement rates for Medi-Lynx services used to settle with the customers of certain insurers using the MultiPlan network and resulting from the agreement concluded between Medi-Lynx and MultiPlan on 1 June 2016 will no longer apply.

  This event entails the risk of a decline in Medi-Lynx's revenue. Payments received by Medi-Lynx in 2018 from all insurers using the MultiPlan network accounted for approx. 21.6% of Medi-Lynx revenue for 2018, i.e. USD 11.7 million. The Group estimates that the change in rates will result in a reduction in revenue by USD 8.4 million annually, assuming the volume of sales of 2018. Immediately after receipt of notification from MultiPlan, the Management Board of Medi-Lynx started talks on the terms of provision of its services via the MultiPlan network in order to secure revenue and ensure that a portion of payment requests will continue to be paid at MultiPlan rates by the majority of insurers using the network.

  This event is a materialization of the risk of reduced reimbursement levels related to the out-of network model of cooperation with private insurers, adopted by Medi-Lynx.

- changes in the range of services reimbursed by individual insurers – although the subsidiary, Medi-Lynx, provides medical services to a dispersed group of recipients (patients in many different medical institutions, clinics and hospital networks), the number of payers (insurers) is limited. If one of the key insurers were to stop reimbursing the medical procedure provided by Medi-Lynx, this change could have a material adverse effect on the Group's operating results.

25. Capital management

During the year, there were no changes in the Capital Group’s approach to capital management. The Capital Group is not subject to external capital requirements. The policy of the Parent Company’s Management Board is to maintain a sound capital base so as to preserve the confidence of shareholders, investors and trading partners, and ensure the future growth of business operations. The Parent Company’s Management Board seeks to strike a balance between a higher rate of return achievable with higher debt levels and the benefits and security offered by a solid capital base.

As at the end of the reporting period, the ratio of the Capital Group’s net debt to adjusted equity was as follows:

Item	**31.12.2018**	**31.12.2017**
Interest-bearing credits loans and bonds	66 205	72 554
Trade and other liabilities	10 717	7 522
Less cash and cash equivalents	(60 189)	(32 531)
Net debt	**16 733**	**47 545**
Equity	**189 864**	**168 913**
Equity and net debt	**206 597**	**216 458**
Leverage ratio	**8.1%**	**22.0%**

26. Operating leases

Below are detailed minimum lease payments under irrevocable operating lease agreements related primarily to lease fees for office space in Poland and the United States:

	31.12.2018
up to 1 year	5 154
1–5 years	19 904
more than 5 years	307
	25 365

In August 2012, the Company signed an agreement to lease office space in Warsaw with the lease period commencing on 1 October 2012. In the reporting period, the Company renegotiated the lease terms, which resulted in the signing of a new lease agreement in May 2018. Under the new agreement, the lease area was increased and the lease rate was changed. The current lease period runs from 1 July 2018 to 30 May 2024.

In 2018, Medi-Lynx renegotiated the lease agreement for office space in Plano (Texas). Under the annexed agreement, the lease area was increased and the lease rate was changed.

27. Contingent liabilities

The Parent Company is a party to agreements for the EU co-financing of investment projects aimed at the development of the products and services offered. A failure to meet the conditions set for the relevant development work may give rise to the risk that the grants received will have to be repaid. The subsidies received are secured with promissory notes. As at the balance sheet date, the risk described above was assessed as doubtful. The Parent Company carries out its works in accordance with the schedule.

The Parent Company endorses an interest-bearing promissory note issued by a subsidiary, MDG HoldCo with its registered office in the US to Medi-Lynx Monitoring, Inc. as a payment for the purchase of shares in Medi-Lynx. Detailed information about the security is provided in Note 23 to these financial statements.

On 16 July 2018 Medicalgorithmics established security for the Company's liabilities resulting from the lease of usable area in the building at Al. Jerozolimskie 81 in Warsaw in the form of an irrevocable and unconditional bank guarantee in the total amount of PLN 404 thousand.

The beneficiary of the guarantee is Central Tower 81 Sp. z o.o. (the lessor). The guarantee is valid from the date of issue to 30 August 2024.

Regulations concerning corporate income tax, personal income tax, value added tax and contributions to social security undergo relatively frequent changes, often resulting in the absence of any established regulations or legal precedents for reference. Moreover, the existing regulations sometimes lack clarity, leading to differing opinions as regards the legal interpretation of tax provisions, both between state authorities and between authorities and the private sector. Tax settlements as well as other settlements (including those related to customs duties or foreign currencies) may be inspected by authorities which are competent to impose significant penalties. Any additional liabilities resulting from such inspections need to be paid with interest. In the light of the above, the tax risk in Poland is higher than usual tax risk in countries with better-developed tax systems. Tax declarations can be audited over a period of five years. In consequence, the amounts presented in the financial statements may change at a later date, after the final amount is determined by tax authorities. The Capital Group was subject to control by the tax authorities. Tax authorities have got the right to inspect books and accounting records. Within five years of the end of the year which relevant tax return was filed, they may impose additional tax charges, including interest and other penalties (see Note 11). In the opinion of the Management Board, there were no circumstances that could lead to significant liabilities in this respect.

28. Transactions with executives

During the reporting period, the Management Board and the Supervisory Board of the Parent Company received the following remuneration:

	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Remuneration of the Management Board Members	3 372	7 445
Remuneration of the Supervisory Board	376	171

Pursuant to the Annex to the Actuarial Report of 1 March 2019, the Company derecognized the provision for future payments of bonuses in the form of equity-settled share-based payments recognized in previous periods. The total effect of the derecognition of the provision recognized in previous years, amounting to PLN 5 312 thousand, was recognized directly in the supplementary capital. The costs of the incentive scheme recognized in 2018 in the amount of PLN 2 227 thousand were derecognized through profit or loss. Additionally, as at 31 December 2018 the Parent Company recognized a provision of PLN 1.5 million for remuneration for the Management Board.
Previously, the variable remuneration of the President of the Management Board was calculated on the basis of the previous financial year's performance and paid in the year to which it related. As a consequence of the amendment to internal regulations, the remuneration included in costs of 2018 includes both the portion paid out in 2018 and the portion to be paid out in 2019.

29. Employment structure

	31.12.2018	31.12.2017
Number of employees (in FTEs)	476	495

As at the report date (26 March 2019), the Capital Group had 442 employees (in FTEs).

30. Information about significant legal proceedings

In the reporting period, there were no proceedings pending before a court, arbitration body or public administration authority concerning the Group’s liabilities or receivables, the value of which would constitute, individually or jointly, at least 10% of the Company’s equity.

31. Information on the entity authorized to audit financial statements

On 11 June 2018, at a meeting of the Supervisory Board of the Parent Company, CSWP Audyt spółka z ograniczoną odpowiedzialnością spółka komandytowa with a registered office in Warsaw, ul. Kopernika 34, 00-336 Warsaw, entered in the Register of Entrepreneurs of the National Court Register under KRS No 0000402544 and entered in the list of audit companies kept by the National Council of Statutory Auditors under No 3767, was appointed as the entity authorized to audit the Group’s consolidated financial statements for 2018 and 2019 and to review the Group’s interim consolidated financial statements for the first half of 2018 and 2019.

The auditor's remuneration for the audit of the annual consolidated financial statements for 2018 amounted to PLN 64 thousand, while for the review of the consolidated interim financial statements for the first half of 2018 – to PLN 26 thousand.

32. Events after the balance sheet date

On 22 January 2019, the Company acquired 97% of new shares in Algotel Solutions Private Limited, based in India (“Algotel Solutions”), as a result of which the Company became the owner of these shares. All the new shares were subscribed for the Company against a cash contribution of USD 48 550. The company is in the process of acquiring the remaining shares in Algotel Solutions and will ultimately hold 100% of shares.

The business of the acquired company includes distribution of the PocketECG system in India. Through Algotel Solutions, Medicalgorithmics S.A. launched its expansion into the prospective Indian market, characterized by a strong sales potential (large population, dynamic economic growth). Algotel Solutions is in the process of changing its name to Medicalgorithmics India Private Limited, to enable closer identification of the Indian company with the Medicalgorithmics Group.

As disclosed in a current report No 5/2019 of 1 March 2019, on 14 January 2019 a subsidiary, Medi-Lynx, received a notification from MultiPlan Inc. (“MultiPlan”), a network of providers of medical services offered to private health insurers. According to this notification, the reimbursement rates for Medi-Lynx services used to settle with the customers of certain insurers using the MultiPlan network and resulting from the agreement concluded between Medi-Lynx and MultiPlan on 1 June 2016 will no longer apply.

This event entails the risk of a decline in Medi-Lynx's revenue. Payments received by Medi-Lynx in 2018 from all insurers using the MultiPlan network accounted for approx. 21.6% of Medi-Lynx revenue for 2018, i.e. USD 11.7 million. Immediately after receipt of notification from MultiPlan, the Management Board of Medi-Lynx started talks on the terms of provision of its services via the MultiPlan network in order to secure revenue and ensure that a portion of payment requests will continue to be paid at MultiPlan rates by the majority of insurers using the network.

It should be noted that one of the Group's strategic medium-term objectives is changing the business model by signing long-term service contracts directly with key private insurers (in-network contracts). The Group assumes that if this goal is achieved, although it will result in lower reimbursement rates for a single service, the Group will secure access to new clients and, as a consequence, significantly increase the sales volume.

The Group is of the opinion that this strategy will allow Medi-Lynx to achieve sustained annual revenue growth and implement its business growth strategy, as well as increase the security and stability of Medi-Lynx's revenue.

There were no events after the balance sheet date other than those disclosed in these financial statements that should be disclosed or included in these financial statements.

Marek Dziubiński
President of the Management Board

Warsaw 26 March 2019

DIRECTORS' REPORT

ON THE OPERATIONS OF

THE MEDICALGORITHMICS CAPITAL GROUP

AND

MEDICALGORITHMICS S.A.

FOR 2018

I. Overview of the Capital Group's operations

I. 1. Business profile of the Group

The Medicalgorithmics Group operates in the field of advanced telemedicine technologies. The Group is a provider of cardiac diagnostic solutions, particularly in the field of ECG analysis.

The principal areas of operations of the Capital Group are:
- provision of ECG monitoring services;
- provision of information technology and biotechnology services;
- scientific research and development;
- manufacture of electro-medical equipment.

The Group provides services in over a dozen countries on several continents, including North and South America, Europe, Asia and Australia. Currently, the United States is the largest market.

Main competitive advantages of the Capital Group are as follows:
- breakthrough technology in the field of mobile cardiac telemetry;
- effective business model based on subscription revenue;
- a team of top professionals in the areas of IT systems, programming, medical devices, digital signal processing and project management.

The Group's primary source of revenue is the sale of diagnostic services provided to patients in the United States. These services are provided using PocketECG, the Medicalgorithmics S.A.'s proprietary solution, used for remote monitoring of heart disorders. Among the available devices for monitoring heart work, the PocketECG system stands out by, among others, the longest time of home arrhythmia monitoring, remote online access to complete monitoring records and full statistical analysis of cardiac arrhythmias. In particular, the system serves to diagnose and detect the following arrhythmias: asymptotic, rare and irregular arrhythmias, and atrial fibrillation leading to stroke.

The PocketECG system has been approved for trading in the United States by the U.S. Food and Drug Administration (FDA). The system also bears the CE mark indicating that the device complies with the requirements of the European Union directives.

In addition to cardiac telemetry, the Group's products and solutions are used in the cardiac safety industry, i.e. in clinical trials of drugs for cardiac safety. Moreover, the Group collaborates closely with cardiovascular diagnostic and monitoring centres.

I. 2. Composition of the Capital Group

The Parent Company of the Group is Medicalgorithmics S.A. (the "Parent Company", "Company", "Issuer"), a joint-stock company registered in Poland, established in 2005. In 2011, the Company's shares made their debut on the NewConnect market, an alternative system of trading outside a regulated market operated by the Warsaw Stock Exchange. Since 3 February 2014 the shares of Medicalgorithmics S.A. have been listed on the regulated market of the Warsaw Stock Exchange.

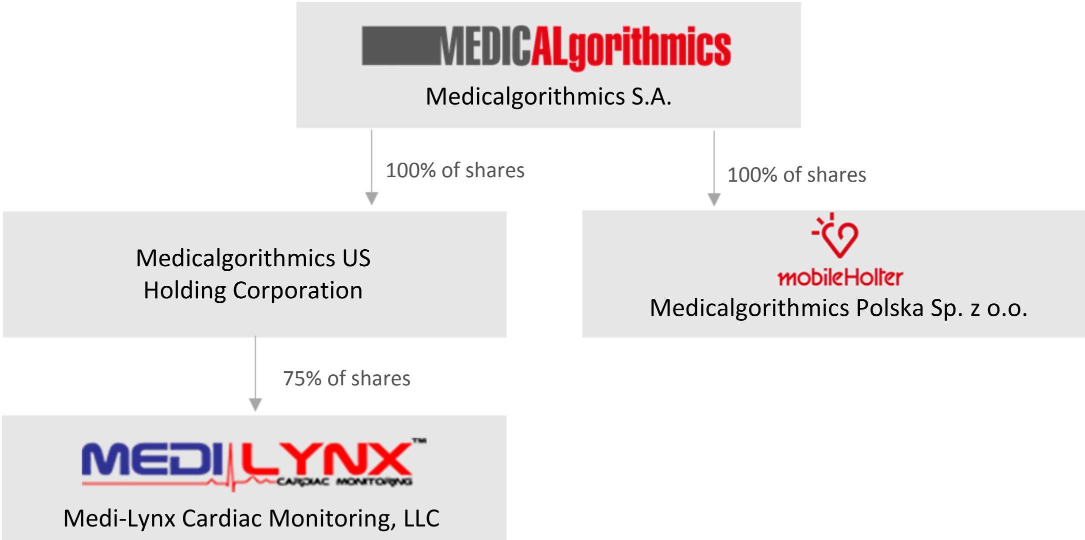
The Medicalgorithmics Capital Group is composed of Medicalgorithmics S.A. and its subsidiaries. The Parent Company holds:

- 100% of the share capital of Medicalgorithmics US Holding Corporation ("MDG HoldCo") with its registered office in Wilmington, Delaware, USA;
- 100% of the share capital of Medicalgorithmics Polska Sp. z o.o. (formerly: Kardiosystem Monitoring Sp. z o.o. "Medicalgorithmics Polska", "MDG Polska") with its registered office in Warsaw;
- 75% of shares in Medi-Lynx Cardiac Monitoring, LLC ("Medi-Lynx") with its registered office in Plano, Texas, USA, through MDG HoldCo.

On 2 July 2018, the Parent Company acquired all shares in Kardiosystem Monitoring sp. z o.o. The price for acquiring shares in Kardiosystem was PLN 167 thousand, wherein the contract provides for additional payment up to PLN 350 thousand due in 2019–2023 depending on achieving assumed yearly sales goals. For more information, see Note 15 to the Group's consolidated financial statements for 2018. On 26 November 2018, the company changed its name to Medicalgorithmics Polska Sp. z o.o.

The financial statements of the Parent Company and all its subsidiaries were included in the consolidated financial statements using the full method.

The composition of the Medicalgorithmics Capital Group and its organizational and equity links as at 31 December 2018 are presented below:



The structure of the Capital Group changed after balance sheet date. As described in Note 32 to the Group's consolidated financial statements for 2018, on 22 January 2019 the Company acquired 97% of new shares in Algotel Solutions Private Limited, based in India (“Algotel Solutions”), as a result of which the Company became the owner of these shares. All the new shares were subscribed for the Company against a cash contribution of USD 48 550. The company is in the process of acquiring the remaining shares in Algotel Solutions and will ultimately hold 100% of shares.

The business of the acquired company includes distribution of the PocketECG system in India. Through Algotel Solutions, Medicalgorithmics S.A. launched its expansion into the prospective Indian market, characterized by a strong sales potential (large population, dynamic economic growth). Algotel Solutions is in the process of changing its name to Medicalgorithmics India Private Limited, to enable closer identification of the Indian company with the Medicalgorithmics Group.

I. 3. Strategy and business model

The Medicalgorithmics Group’s strategic objective is to become a leading provider of state-of-the-art technology and services in the field of cardiac arrhythmia diagnostics in North and South America, Asia, Europe and Australia. The Group is committed to organic growth and acquisitions, rapid growth and high customer satisfaction by delivering a flexible product and service offering in the identified market niches.

Currently, the Group is working to strengthen its position in the US healthcare market, expand its operations in other countries, and further expand its territory mainly to European countries. On every new market, Medicalgorithmics is working with a minimum of one strategic sales and operational partner to minimize its operating costs and focus on technological support for patient care and the development of cardiology solutions.

The Group employs highly qualified staff and puts great emphasis on obtaining products and services of the highest quality. The Group products are patented in key markets and obtain the necessary quality and safety certificates. Some of the earned profit is spent on research and technology development so that the Group may strengthen the status of an innovative market leader.

The Group is focused on the development of cardiac diagnostic devices and services, both stationary and remote.

Strategic plans assume the development of the following areas of operation:

- Medical diagnosis;
- Cardiological rehabilitation;
- 12-channel ECG system;
- Technological support for the research industry in terms of cardiac safety of medicaments;
- Integration and programming services for collaborating medical institutions.

The unique business model developed by the Management Board of the Parent Company, which is tailored to the specific character of the Group, is a source of sustainable profitability. The technologically advanced production of the PocketECG system located in Poland ensures full control over product quality, relatively low labor costs and protection of technological secrets. The Company's products are patented in key markets and obtain the necessary quality and safety certificates.

The first market where Medicalgorithmics S.A. offered its product was the Polish market, whereas since 2010, the United States has been the primary sales market for the Company. The decision to expand into the US market was dictated by the openness of the US market to medical innovations and the high level of cardiac rehabilitation services provided by private and state insurers, which translates into significant telemedicine market value and prospects for its continued dynamic growth. Initially, in the US market, PocketECG system was sold in a subscription model, in co-operation with two strategic partners who provide diagnostic services to hospitals, clinics, cardiac surgeries and other healthcare units. In March 2016, through a company established for this purpose, Medicalgorithmics S.A. acquired 75% of shares of one of its trading partners – Medi-Lynx's. And on in December 2016 it purchased a client database from another of the trading partners. Thus, since 2017, in the US market, Medi-Lynx has been the exclusive provider of services provided by the PocketECG system to its target clients.

As a result of the above-mentioned acquisitions, the Capital Group was formed, concentrating both technological activity connected with creating innovative products and providing top quality remote cardiac diagnostic services, using its own products. Within the Group, Medi-Lynx, operating since the beginning of 2014, is the provider of these diagnostic services.

Medi-Lynx provides diagnostic services to patients in more than 35 states and earns revenue from the entities, in which the patients using the PocketECG system are insured. Services provided by Medi-Lynx are divided into three main categories, i.e. Telemetry, Event Monitoring and Holter, which are settled using Commercial Procedural Terminology (CPT). Based on the data collected by PocketECG, ECG technicians employed by Medi-Lynx produce comprehensive reports to help doctors diagnose heart disorders detected during the performed examination.

When manufacturing the PocketECG system, the Parent Company uses a number of suppliers of electronic components and sub-assemblies. Sources of supply are diversified and the Group is constantly establishing new business contacts with potential suppliers.

In addition to cardiac telemetry, the Company's products and solutions are used in clinical trials of drugs for cardiovascular safety. Moreover, the Company collaborates closely with cardiovascular diagnostic and monitoring centres.

In addition to the flagship PocketECG system, the Company also develops other innovative solutions for heart rate monitoring. The most advanced is the development of the PocketECG CRS system for hybrid cardiovascular rehabilitation, which can be used in hospitals, clinics, as well as at the patient's home.

I. 4. Segment information

The Capital Group operates mainly outside of Poland, particularly in the US. The operations are classified within a single segment, which includes both sales of diagnostic and IT services, and devices that are products related to the services offered.

I. 5. Shareholding structure of the Parent Company

The following chart and table present the shareholders of Medicalgorithmics S.A. holding 5% or more of total voting rights at the General Meeting as at the issue date of this report based on the Company's best knowledge, including changes in major holdings of shares after the issue of the previous quarterly report.

The information contained in the table is based on notifications received from shareholders in accordance with Article 69 of the *Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organized Trading, and Public Companies.*

Chart 1. Shareholding structure of Medicalgorithmics S.A.

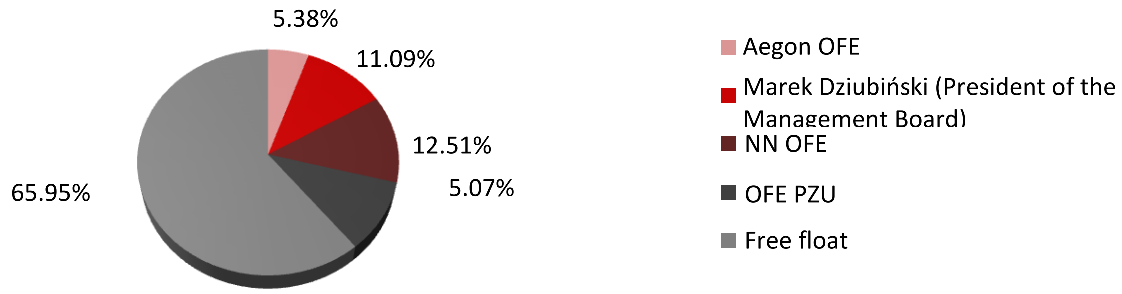


Table 1. Shareholding structure of Medicalgorithmics S.A.

Shareholder	Number of shares as at 26 March 2019	% ownership interest	Number of votes	% of total voting rights	Change in the period from 20 November 2018 to 26 March 2019
Aegon OFE	193 863	5.38%	193 863	5.38%	unchanged
Marek Dziubiński (President of the Management Board)	400 000	11.09%	400 000	11.09%	unchanged
NN OFE	451 000	12.51%	451 000	12.51%	unchanged
OFE PZU*	365 408	10.13%	365 408	10.13%	+182 578
Free float	2 196,255	60.89%	2 196 255	60.89%	+9 357
TOTAL NUMBER OF SHARES	**3 606 526**	**100.00%**	**3 606 526**	**100.00%**	

**On 22 March 2019, the Company announced in its current report No. 7/2019 that it had received a notification from the Company's shareholder in which Powszechne Towarzystwo Emerytalne PZU S.A., acting on behalf of Otwarty Fundusz Emerytalny PZU "Złota Jesień" (open-ended pension fund, OFE PZU) notified that as a result of the acquisition of 5 250 (five thousand, two hundred and fifty) shares in the Company effected on the Warsaw Stock Exchange on 19 March 2019, following its settlement on 21 March 2019, the OFE PZU holds more than 10% of the total number of votes in the Company.*

Agreements which may cause future changes in the percentages of shares held by the existing shareholders and bondholders

The adopted incentive scheme for management and key employees is described in detail in Section I.14.

I. 6. Dividend policy

Pursuant to Article 395 of the Commercial Companies Code ("CCC"), the body competent to adopt a resolution on profit distribution (or coverage of loss) and dividend payment is the Ordinary General Meeting of Shareholders which should be held within 6 months after the end of each financial year. The Ordinary General Meeting of the Company sets forth the amount of dividend, the date of determining the right to dividend (the dividend record day) and the date of dividend payment in the resolution on profit distribution for the last financial year (Article 348 § 3 of the Commercial Companies Code). Pursuant to Article 27(3) of the Company's Articles of Association, the Company's Management Board is authorized to distribute interim dividends to shareholders. The payment of interim dividend requires the consent of the Supervisory Board.

The conditions of dividend payment adopted by the General Meeting will be determined by the Company's Management Board in consultation with the National Depository for Securities. A company whose shares are admitted to stock-exchange trading is obliged to agree on decisions and provide the WSE with information on its intention to pay dividends in the manner and on terms specified in the Detailed Exchange Trading Rules.

On 29 May 2017, the Management Board adopted Resolution No 03/05/2017 on the adoption of a recommendation concerning the policy for payment of dividend from the profit earned by the Company in the financial year 2016 and thereafter.

It is the Management Board's intention that the payment of dividend from the profit earned by the Company for financial years following the financial year 2016 be set at the level of up to 50% of the Medicalgorithmics Capital Group's consolidated net profit attributable to shareholders of the parent company for a given financial year based on the consolidated financial statements and that the remaining portion of profit be allocated to supplementary capital. In the event of actual or anticipated capital needs of the Company of significant value, the Management Board's recommendations regarding the payment of dividend from the profit earned by the Company for the financial years 2017, 2018 or 2019 may be set at the level of 20% of the consolidated net profit of the Medicalgorithmics Capital Group attributable to shareholders of the parent company for a given financial year on the basis of the consolidated financial statements and the remaining part of profit may be allocated to the supplementary capital.

In addition, the possibility of dividend payment from the Company's net profit disclosed in the Company's financial statements for the financial year 2017, 2018 or 2019 may be excluded or limited due to the provisions of the terms of issue of securities (in particular bonds) issued by the Company.

The ultimate recommendation of the Management Board concerning the distribution of profit generated in the Capital Group will be based on the market, financial and liquidity position of the Group, existing and future liabilities and provisions related thereto, determining the maximum level of debt. The Management Board's proposals concerning dividend payment take into account the capital required to support the Company's growth.

The Management Board will recommend days on which the list of shareholders entitled to receive dividends and the dividend payment dates will be determined, with due regard for the need to carry out this process in an efficient manner.

The ultimate decision on the distribution of the Company's net profit for subsequent financial years will be made by the Ordinary General Meeting of Shareholders.

On 26 June 2018, the Ordinary General Meeting of Shareholders of the Parent Company passed a resolution No 16/06/2018 on distribution of the dividend from the net profit disclosed in the Company's financial statements for the financial year ended on 31 December 2017.

The amount of profit allocated for distribution was PLN 5,121 thousand (i.e. PLN 1.42 per share). The dividend was paid for all shares in the Company. The dividend record date was 16 July 2018 and the payment date was 30 July 2018.

I. 7. Purchase of treasury shares

In the reporting period, the Parent Company did not acquire any treasury shares.

I. 8. Management Board of the Parent Company

On 21 September 2018, Maksymilian Sztandera submitted his resignation from the position of the Company's Chief Financial Officer, effective as of the date of resignation.

The composition of the Medicalgorithmics S.A. Management Board as at the date of this report was as follows:

dr Marek Dziubiński – President of the Management Board

Dr Marek Dziubiński (PhD) is a graduate of interdisciplinary studies at the Faculty of Physics, Mathematics and Computer Science of the University of Warsaw. He also completed doctoral studies at the Department of Multimedia Systems of the Faculty of Electronics, Telecommunications and Informatics of the Gdańsk University of Technology. Dr Dziubiński's PhD thesis was awarded by the Gdańsk University of Technology and received a national distinction. Marek Dziubiński is the author of numerous scientific publications, articles in scientific journals and conference papers. Over the past 18 years of his professional career, he has been involved in the development of digital signal processing algorithms, concentrating on the analysis of periodic and quasi-periodic signals. The PocketECG technology is based on a self-learning algorithm developed by Mr Dziubiński for the interpretation of ECG signals based on a limited number of signal leads, generating real-time results. Marek Dziubiński is also the author of the Company's business model.

Career:

- June 2005 – present: MEDICALGORITHMICS: President of the Management Board, Chief Technology Officer
- March 2005 – January 2006: Aud-X Team: Head of IT team
- June 2003 – August 2005: WAVEFORMATIC: Project Manager
- June 2004 – September 2005: PRESTO-SPACE: Project participant
- July 2000 – May 2003: Houpert Digital Audio: Programmer

Members of the Management Board of the Parent Company do not receive remuneration for their position in the management bodies of subsidiaries.

Table 2. Information on remuneration of the Parent Company's Management Board paid in 2018 (PLN '000)

Person	Function held in the Issuer's governing bodies	Remuneration
Marek Dziubiński	President of the Management Board	3 050
Maksymilian Sztandera	Member of the Management Board, Chief Financial Officer (until 21 September 2018)	322

Additionally, as at 31 December 2018 the Parent Company recognized a provision of PLN 1.5 million for remuneration for the Management Board. Previously, the variable remuneration of the President of the Management Board was calculated on the basis of the previous financial year's performance and paid in the year to which it related. As a consequence of the amendment to internal regulations, the remuneration included in costs of 2018 includes both the portion paid out in 2018 and the portion to be paid out in 2019.

There are no agreements concluded by and between the Company and members of the Management Board which would stipulate a compensation in the event of their resignation or dismissal from the occupied position.

I. 9. Supervisory Board of Medicalgorithmics S.A.

On 26 June 2018, the Annual General Meeting of Shareholders changed the composition of Medicalgorithmics S.A.'s Supervisory Board. The General Meeting dismissed all of the existing Supervisory Board Members, i.e. Mr Marek Tatar, Mr Marcin Hoffmann, Mr Jan Kunkowski, Mr Piotr Żółkiewicz and Mr Artur Małek. Subsequently, the General Meeting appointed new Supervisory Board Members:

The composition of the Medicalgorithmics S.A.'s Supervisory Board as at the date of this annual report was as follows:

Michał Wnorowski – Chairperson of the Supervisory Board

Michał Wnorowski is a graduate of the SGH Warsaw School of Economics and the University of Economics in Krakow. Currently, he is an independent Supervisory Board Member in the following listed companies: Alumetal, Voxel, Braster, Enter Air, Arteria. His financial market career dates back to 1995. In 2012-2016, he served as the Investment Director, managing the Long-Term Share Portfolio in the PZU Group. Previously, he served for many years as head of the team for analysis and shareholder supervisor in the PZU Group. He has many years of experience in managing investment projects, market analysis, enterprise analysis and valuation as well as securities portfolio management. He has also been involved in the restructuring and shareholder supervision of companies. He has sat on the Supervisory Boards of: Robyg, Elektrobudowa, Travelplanet.pl, EMC Instytut Medyczny, Armatura Kraków, ARM Property.

Grzegorz Grabowicz – Member of the Supervisory Board

Grzegorz Grabowicz is a graduate of the Management and Marketing Department at the University of Lodz, with a specialization in Accounting (Master's Diploma in Management and Marketing). In 2010, he received an EMBA (Executive Master of Business Administration) degree, having completed a programme run by the Nottingham Trent University and the Wielkopolska Business School at the Poznań University of Economics. He is a qualified Statutory Auditor. Currently, he is a Management Board Member at Mabion S.A., Supervisory Board Member at Skarbiec Holding S.A., and also a Supervisory Board Member at LC Corp S.A. Previously, Grzegorz Grabowicz worked in the Audit Department of Deloitte, held the posts of financial controller and chief financial officer and Vice-President of the Management Board at Magellan S.A., President of the Management Board and Chairman of the Supervisory Board at MEDFinance S.A., as well as a Supervisory Board Member at Magellan Czech Republic and Magellan Slovakia.

Artur Małek – Member of the Supervisory Board

Artur Małek is a graduate of the Faculty of Finance and Banking at the Cracow University of Economics. Since 2014 he has been a Financial Director at Calypso Fitness S.A. Previously, he held the position of a Financial Director at Benefit Systems S.A. and Noblestar Polska Sp. z o.o. Currently Artur Małek is also a Chairperson of the Supervisory Board of EFC Fitness S.A. and a Member of the Supervisory Boards at Fitness MCG Sp. z o.o., Elektrobudowa S.A., Vistula Group S.A. and Amica S.A.

Marek Tatar, Member of the Supervisory Board

Marek Tatar is a graduate and a doctoral student in the Faculty of Law and Administration at the Jagiellonian University, Attorney-at-law. He is a Managing Partner at the Tatar i Wspólnicy sp. k. law firm. Earlier he worked at the company of Elektomontaż nr 2 Kraków S.A., Dom Maklerski PENETRATOR S.A. and in Trigon Dom Maklerski S.A. Currently, Marek Tatar is also the Chairman of Supervisory Boards at CryptoTech S.A., Sunex S.A. and Supervisory Board Member in Trigon Dom Maklerski S.A. and Termo-Rex S.A.

Krzysztof Urbanowicz - Member of the Supervisory Board

Krzysztof Urbanowicz is a graduate of the Warsaw University of Technology and the University of Warsaw, the Business School at the Warsaw University of Technology (MBA) and the University of Illinois at Urbana-Champaign (MBA). He is a graduate of numerous managerial courses, including the Advanced Management Programme IESE in Spain, the Senior Directorship Program INSEAD in France and St Gallen University in Switzerland. Since 2016 he's been the President of the Management Board at Elzab S.A. Currently, Krzysztof Urbanowicz is also a Supervisory Board Member in Pamapol S.A. and a Chairman of the Supervisory Board in Elzab Soft Sp. z o.o. Previously, he held the positions of the Vice-President of the Management Board and a Member of the Management Board at Comp S.A., President of the Management Board at Elzab SA, Member of the Supervisory Board at Elzab SA., Chairman of the Supervisory Board at Micra-Metripond Kft and many others.

A new Audit Committee composed of elected members of the Supervisory Board was appointed on 27 July 2018. For details, see Section VII.7 of this report.

The table below presents shares in the Parent Company held, directly or indirectly, by members of its Management and Supervisory Boards as at the issue date of this report, and changes in the holdings after the issue date of the previous quarterly report. The information in the table is based on notifications received from members of the Management and Supervisory Boards in accordance with Article 160(1) of the *Act on Trading in Financial Instruments.*

Table 3. Company shares held by members of the Parent Company's Management and Supervisory Boards

Person	Function held in the Issuer's governing bodies	Number of directly held shares	Number of shares held indirectly[1]	Change in the period from 20 November 2018 to 26 March 2019
Marek Dziubiński	President of the Management Board	400 000	-	Unchanged
Michał Wnorowski	Chairperson of the Supervisory Board	-	-	Unchanged
Grzegorz Grabowicz	Member of the Supervisory Board	-	-	Unchanged
Artur Małek	Member of the Supervisory Board	-	-	Unchanged
Marek Tatar	Member of the Supervisory Board	-	-	Unchanged
Krzysztof Urbanowicz	Member of the Supervisory Board	-	-	Unchanged

1) An indirect holding is when a person owns shares in an entity which directly holds shares in the Company; such ownership is not equivalent to having the status of the parent of the entity which directly holds shares in the Company.

Table 4. Information on remuneration of the Parent Company's Supervisory Board in 2018 (PLN '000)

Person	Function held in the Issuer's governing bodies	Remuneration
Marcin Hoffmann	Member of the Supervisory Board (until 26 June 2018)	28
Jan Kunkowski	Member of the Supervisory Board, Member of the Audit Committee (until 26 June 2018)	40
Piotr Żółkiewicz	Member of the Supervisory Board, Member of the Audit Committee (until 26 June 2018)	40
Michał Wnorowski	Chairman of the Supervisory Board, Member of the Audit Committee (since 26 June 2018)	49
Grzegorz Grabowicz	Member of the Supervisory Board, Chairman of the Audit Committee (since 26 June 2018)	39
Artur Małek	Member of the Supervisory Board, Member of the Audit Committee (since 26 June 2018)	62
Marek Tatar	Chairman of the Supervisory Board and Chairman of the Audit Committee (until 26 June 2018), Member of the Supervisory Board (since 26 June 2018)	88
Krzysztof Urbanowicz	Member of the Supervisory Board (since 26 June 2018)	30

There are no agreements concluded by and between the Company and members of the Supervisory Board which would stipulate a compensation in the event of their resignation or dismissal from the occupied position.

I. 10. Branches operated by the Parent Company

Medicalgorithmics S. A. has no formal branches. In 2018, however, it operated in two locations: at the Company's head office was in Warsaw and in the production plant in Gdańsk.

Table 5. Branches of the Company and their locations

Name of the location	City	Address
Registered office – registered office of the Management Board	Warsaw	Al. Jerozolimskie 81, 02-001 Warszawa
Manufacturing plant	Gdańsk	Ul. Marynarki Polskiej 100, 80-557 Gdańsk

I. 11. Headcount

Information on the number of employees is presented in the table below.

Table 6. Headcount at the Parent Company and in the Capital Group

Number of employees (in FTEs)	31.12.2018	31.12.2017
Medicalgorithmics Capital Group	476	495
Medicalgorithmics S.A.	125	86

As at this report date (26 March 2019), the Parent Company and Capital Group had, respectively, 131 and 442 employees (in FTEs).

I. 12. Information on the agreement for the audit of the financial statements

On 11 June 2018, at a meeting of the Supervisory Board of the Parent Company, CSWP Audyt spółka z ograniczoną odpowiedzialnością spółka komandytowa ("CSWP") with its registered office in Warsaw, ul. Kopernika 34, 00-336 Warsaw, entered in the Register of Entrepreneurs of the National Court Register under KRS No 0000402544 and entered in the list of audit firms maintained by the National Council of Statutory Auditors under No 3767, was appointed as the entity authorized to:

a) Review the interim financial statements of Medicalgorithmics S.A. for the reporting periods ended 30 June 2018 and 30 June 2019;
b) Review the Capital Group's interim consolidated financial statements for the reporting periods ended 30 June 2018 and 30 June 2019;
c) Audit the financial statements of Medicalgorithmics S.A. for the financial years ended 31 December 2018 and 31 December 2019;
d) Audit the Capital Group's consolidated financial statements for the financial years ended 31 December 2018 and 31 December 2019.

Table 7. Remuneration of the entity authorized to audit and review financial statements (PLN '000)

	01.01.2018 - 31.12.2018	01.01.2017 - 31.12.2017
Audit of the annual separate and consolidated financial statements	109	104
Review of the interim separate and consolidated financial statements	47	47
Other services (agreement on the performance of agreed upon procedures)	4	4

I. 13. Information on changes in the key rules of managing the Company and its Capital Group

In the year ended 31 December 2018, there were no changes in the key rules of managing the Parent Company and the Capital Group. The Management Board of the Parent Company strives to harmonise the management principles in the Medicalgorithmics Group companies by implementing appropriate procedures and standards of ownership control.

I. 14. Information on the system of control of employee share plans

On 26 February 2016, the Company's Extraordinary General Meeting adopted an incentive scheme based on options for shares in Medicalgorithmics S.A., effective from 26 February 2016 to 31 December 2026. Stock options under the scheme, covering the financial years 2016−2025, will be granted in six tranches. A total of 598,000 options will be granted, broken down into the main tranche for management and additional tranche for key employees, in the following manner:

1) tranche I settled after the end of 2018 – a total of 60 000 options divided into 53 000 options in the main tranche and 7 000 options in the additional tranche,
2) tranche II settled after the end of 2019 – 58 000 options divided into 51 000 options in the main tranche and 7 000 options in the additional tranche,
3) tranche III settled after the end of 2020 – 120 000 options divided into 106 000 options in the main tranche and 14 000 options in the additional tranche,
4) tranche IV settled after the end of 2021 – 120 000 options divided into 106 000 options in the main tranche and 14 000 options in the additional tranche,
5) tranche V settled after the end of 2022 – 120 000 options divided into 106 000 options in the main tranche and 14 000 options in the additional tranche,
6) tranche VI settled no earlier than after the end of 2023, and no later than after the end of 2025 – 120 000 options divided into 106 000 options in the main tranche and 14 000 options in the additional tranche.

The Extraordinary General Meeting entrusted the Supervisory Board with oversight of the scheme's implementation, including verification of the fulfillment of grant conditions for the options and their allotment as per the adopted rules. The Parent Company's Management Board was authorized to take all actions as may be necessary to implement the scheme under the oversight of the Supervisory Board.

As at 31 December 2018, the Company remeasured the incentive scheme based on current estimates regarding the fulfilment of financial criteria. To the best of its knowledge, the Company's Management Board decided to assume that it is impossible to meet the non-market condition.

This assumption applies to all tranches of options offered under the incentive scheme (i.e. no non-market conditions will be fulfilled in any of the tranches). In accordance with IFRS 2 “Share based payments”, such an assumption has the effect that no amount should be recognized as an expense of the scheme.

Pursuant to the Annex to the Actuarial Report of 1 March 2019, the Company derecognized the provision for future payments of bonuses in the form of equity-settled share-based payments recognized in previous periods. The total effect of the derecognition of the provision recognized in previous years, amounting to PLN 5 312 thousand, was recognized directly in the supplementary capital. The costs of the incentive scheme recognized in 2018 in the amount of PLN 2 227 thousand were derecognized through profit or loss.

II. Overview of factors determining the Group's development and summary of material events related to operations of the Group in 2018

2018 saw a number of significant events related to the operations of the Parent Company and the Capital Group which may have a bearing on their development. The measures taken were closely related to strategic objectives such as sales growth and diversification in terms of geography and products.

In the fourth quarter of 2018, the Management Board of Medicalgorithmics S.A. resolved to undertake a review of strategic options for continued growth of Medicalgorithmics S.A. and its Capital Group. The review of strategic options will enable identification of possible development directions of operations, resulting in the selection of the preferred measures to achieve the long-term goal which is to ensure the best possible position for the Group on the market for advanced systems for cardiology and to maximize value for the Company’s shareholders.

The Management Board of the Company is in the process of analyzing different strategic options in all areas of the Group’s business operations; it will also consider obtaining a strategic or financial investor, entering into a strategic alliance, performing an otherwise-structured transaction as well as none of the listed measures. As at the date of this report, the Management Board has not made any decision concerning the selection of a specific strategic option and allows for the possibility that no strategic option will be selected.

Expansion of operations outside the United States

As part of the expansion of sales of the PocketECG system on new markets, the Parent Company acquired new commercial partners in 2018. In June 2018, the Company signed an agreement for the distribution and sales of the arrythmia diagnostics system with a new strategic partner from Canada, m-Health Solutions, Inc. which undertook to buy and activate a thousand PocketECG devices in the first year of cooperation. m-Health specializes in cardiovascular diagnostics and remote heart monitoring. The company has been operating on the Canadian market since 2009 and has served over 70 thousand patients in cooperation with 3 thousand physicians.

In 2018, the Group was expanded to include Medicalgorithmics Polska Sp. z o.o. The main purpose for purchasing Medicalgorithmics Polska was to combine the sales forces of both companies and to create a common range of systems for arrythmia diagnostics and cardio tele rehabilitation addressed to hospitals and doctor's surgeries in Poland. This will facilitate an increase in sales of the Group's products and services on the Polish market. Medicalgorithmics Polska's competitive advantage comprises a qualified and experienced team of physicians and electro-cardiology technicians who are responsible for analyzing ECG records and preparing detailed diagnostic reports from tests. Furthermore, Medicalgorithmics Polska has permanent relationships with heath care facility representatives in Poland. Medicalgorithmics Polska provides analysis and monitoring services with respect to cardiac telemetry at the heart monitoring center, and the Company's sales department is responsible for acquiring new customers and after-sales service.

In addition, through Algotel Solutions, Medicalgorithmics S.A. launched its expansion into the prospective Indian market, characterized by a strong sales potential (large population, dynamic economic growth).

The Company also expanded its collaboration with the Scandinavian-based Vingmed Group in the area of sales of the cardiac arrhythmia diagnostics system. Agreements have been signed with Vingmed AS from Norway and Vingmed AB from Sweden. Under the terms of the agreement, a partner is obligated to purchase and activate a minimum of 600 PocketECG devices during two years and a minimum of 20% increase in orders in subsequent years. The Vingmed Group is one of the largest corporations in Scandinavia in terms of distributing medical products and rendering services with the use thereof.

Significant events at Medi-Lynx

A significant event was the appointment of Peter G. Pellerito as CEO of Medi-Lynx. Peter G. Pellerito replaced the former Chief Executive Officer of Medi-Lynx on 16 October 2018. The new Management Board of Medi-Lynx will be primarily responsible for delivering the Group's strategic medium-term objectives, i.e. changing the business model by signing long-term service contracts directly with key private insurers (in-network contracts). The Group assumes that if this goal is achieved, although it will result in lower reimbursement rates for a single service, the Group will secure access to new clients and, as a consequence, significantly increase the sales volume. The Group is of the opinion that this strategy will allow Medi-Lynx to achieve sustained annual revenue growth and implement its business growth strategy, as well as increase the security and stability of Medi-Lynx's revenue.

Marketing services

In 2018, the Group performed a number of marketing efforts aimed at supporting the sales growth strategy and at building and strengthening the PocketECG brand image in the industry. The Group has developed a strategy on Medicalgorithmics, Medi-Lynx and PocketECG brands identification as well as a marketing communication plan. In 2018, the Group continued its efforts in the area of online marketing to strengthen the expert brand image and generate sales contacts for sales representatives in the United States. All activities were monitored and optimized owing to the implementation of a marketing automation tool, HubSpot.

An additional action geared towards sales growth was the Group's participation in the world's largest scientific conference for electrophysiologists. This annual event is organized in the US in May by the Heart Rhythm Society (HRS). A strategy has been developed to maximize the benefits from participation in this event in the area of sales and marketing. The Group also actively participated in a number of other industry conferences, promoting its solutions for cardiac rehabilitation and arrhythmia diagnostics in Poland and abroad.

Product development and R&D activities

In 2018, the Company continued its efforts aimed at the diversification of its products. Early this year, the company launched the promotion of its new proprietary product - the remote cardiac rehabilitation system, PocketECG CRS. Pilot implementations were carried out in several renowned hospitals in Poland. On July 12, 2018, the Company received a notification from the Food and Drug Administration (FDA) that the PocketECG CRS was cleared under the procedure 510(k). Following FDA'a approval, the Company initiated actions to commercialize the new system in the U.S.

In 2018, the Company continued its research and development activities. One of the projects underway was ECG TechBot, for which the Parent Company received funding from the National Centre for Research and Development at the end of 2017. It is a dedicated software using a set of algorithms for automatic analysis and interpretation of the ECG signal based on deep learning methods. The Company also continued works on the functional development of the PocketECG CRS remote cardio rehabilitation system. Another project the Company has been working on is PocketECG 12Ch – a device and system for remote, instant ECG description (12-channel ECG). Work on this project has been temporarily suspended and will resume once the global version of the PDA with LTE has been developed.

III. Discussion of the Group’s performance and the Group’s asset and financial position

III. 1. Discussion of the Group’s performance

In 2018, the Capital Group continued to implement its strategy, pursuant to which its operations were based on the innovative PocketECG system. The Group's consolidated revenue comprises mainly:

- revenue from medical services in the US market generated by Medi-Lynx;
- subscription revenue generated by Medicalgorithmics S.A. from cooperation with strategic partners, excluding Medi-Lynx;
- revenue from sales of PocketECG devices, excluding Medi-Lynx.

Medi-Lynx revenue are derived from the number of diagnostic services performed over a given period and the refund rate for research (in the case of public insurers) or the amount of contractual payments for a given procedure (in the case of private insurers). The Parent Company operates on a subscription model, which means that it earns revenue from sales of devices, and then from subscriptions for their use and use of the related software and server infrastructure.

Table 8. Key items of the statement of comprehensive income for 2018 and 2017, and changes over the last financial year

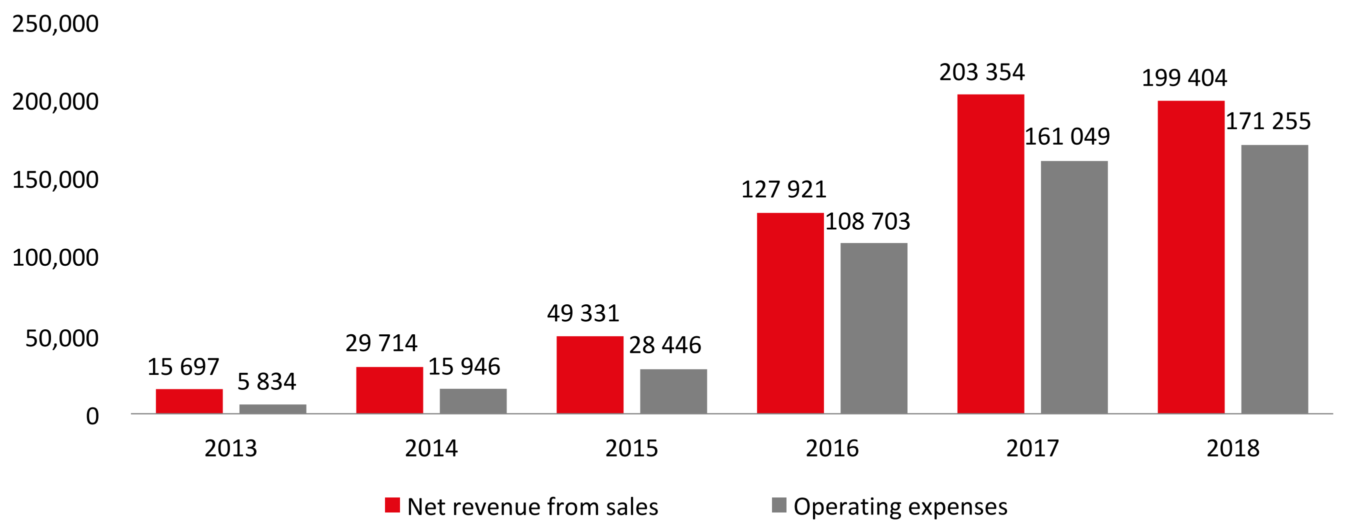
	01.01.2018-31.12.2018	01.01.2017-31.12.2017	Change	Change %
Sales revenue	199 404	203 354	(3 950)	(2%)
Operating expenses	171 255	161 049	10 206	6%
Profit on sales	28 149	42 305	(14 156)	(33%)
Other operating revenue/(expenses), net	(3 425)	(485)	(2 940)	606%
Operating profit	24 724	41 820	(17 096)	(41%)
Net finance income/(costs)	(3 151)	(5 228)	2 077	(40%)
Profit before tax	21 573	36 592	(15 019)	(41%)
Net profit, *of which*:	**18 948**	**33 653**	**(14 705)**	**(44%)**
Net profit attributable to Shareholders of the Parent Company	14 416	25 539	(11 123)	(44%)
Net profit attributable to non-controlling interests	4 532	8 114	(3 582)	(44%)
EBITDA	36 303	54 290	(17 987)	(33%)

Sales revenue

In 2018, the Capital Group's revenue amounted to PLN 199 404 thousand, down PLN 3.9 million (-2%) on 2017. The decline is mainly attributable to a 3% drop in the average USD exchange rate, which translates into a decrease in the Group's revenue by approximately PLN 6.5 million (-3%), and a decrease in revenue from other partners by PLN 2.8 million (-1.4%). These declines were partially offset by an organic increase in Medi-Lynx revenue by PLN 4.8 million (+2%).

The decrease in revenue from other by PLN 2.8 million is related to the termination of collaboration with AMI/Spectocor in February 2017. In the previous year, sales to this partner amounted to approximately PLN 4.6 million. Revenue from collaboration with other partners, excluding the impact of AMI, increased by approximately PLN 1.8 million.

Chart 2. The Group's sales revenue and operating expenses in particular years (PLN '000)



In 2018, the Group earned all of its revenue from the sales of PocketECG system. This revenue comprised the revenue from sales of devices in the amount of PLN 1.8 million (PLN 0.7 million in 2017), representing 0.9% of total revenue (0.4% in 2017), and revenue from sales of services in the amount of PLN 197.6 million (PLN 202.6 million in 2017), representing 99.1% of total revenue (99.6% in 2017).

Operating expenses

Table 9. Structure of operating expenses in 2018 and 2017 (PLN '000)

	01.01.2018-31.12.2018	01.01.2017-31.12.2017	Change	Change %
Raw materials and consumables used	9 085	6 250	2 835	45%
Employee benefits	110 549	106 581	3 968	4%
Amortization and depreciation	11 579	12 470	(891)	(7%)
Third-party services	33 831	30 411	3 420	11%
Other	6 211	5 337	874	16%
TOTAL:	**171 255**	**161 049**	**10 206**	**6%**

Raw materials and consumables used

The increase in cost of raw materials and energy used by PLN 2.8 million, i.e. by 45%, is primarily attributable to a twofold increase in the volume of devices sold (excluding Medi-Lynx, where sales revenue is eliminated during the consolidation process and the cost of production is capitalized in fixed assets). Additionally, the increase in the costs of servicing the devices sold, mainly those used by the Group which is related to a larger number of devices maintained at Medi-Lynx, that were purchased in 2017 in order to support the growing volume of examinations (acquisition of the AMI/Spectocor's client base). Revenue earned by the Parent Company on this account is eliminated in the consolidation process, and the cost of components used is recognized as the use of consumables. The increase in the volume of services provided by Medi-Lynx also translates into higher costs of additional components and materials (mainly electrodes) necessary for their performance.

Employee benefits

Costs of employee benefits increased by approximately PLN 3.9 million (+4%) year on year. The change is primarily attributable to the following factors:

(1) increased average annual headcount at Medi-Lynx which translated into an increase in costs by approximately PLN 8.9 million. The increase in headcount at Medi-Lynx followed from the acquisition of the AMI/Spectocor client base and the related need to handle the growing volume of examinations. As a result of the expected increase in the volume of medical procedures, an additional office in Pennsylvania was established in 2017.

Following the verification of sales performance, a decision was made to change the business model and, consequently, the headcount at Medi-Lynx was reduced in the fourth quarter of 2018 and in early 2019.

(2) change in the average USD exchange rate which translated into a decrease in costs by approximately PLN 3.2 million;

(3) a decrease in costs of employee benefits at the Parent Company by PLN 1.9 million. The change is primarily an effect of the actuarial revaluation described in Note 20.6 to the Consolidated Financial Statements for 2018 and resulting in a decrease in the cost of the incentive scheme by PLN 2.1 million compared to 2017, and of a lower remuneration of the Management Board.

The costs of employee benefits represent the most significant item in the structure of the Group's operating expenses (64%). The high share of costs of employee benefits results from the nature of the Group's operations, whose main resource is the people. Both at the level of the Parent Company, where the majority of employees are IT specialists and production engineers, and at the level of the subsidiary, where, among others, ECG technicians and sales and customer service specialists are employed, the operations are based on human capital.

Amortization and depreciation

In 2018, depreciation and amortization expenses decreased by PLN 0.9 million (-7%), and currently they represent nearly 7% of total operating expenses. The most significant component of the amortization and depreciation expense is the amortization of client bases held by the Group (the Medi-Lynx client base recognized as a result of the final settlement of the purchase price and AMI/Spectocor client base acquired following the settlement agreement of 28 December 2016). According to the Management Board's estimates, the client bases will bring economic benefits and will be amortized over a period of 20 years. The total amortization expense for both client bases amounted to PLN 5.7 million in 2018 and decreased by about PLN 0.2 million year on year. The change is attributable exclusively to a decrease in the average USD exchange rate.

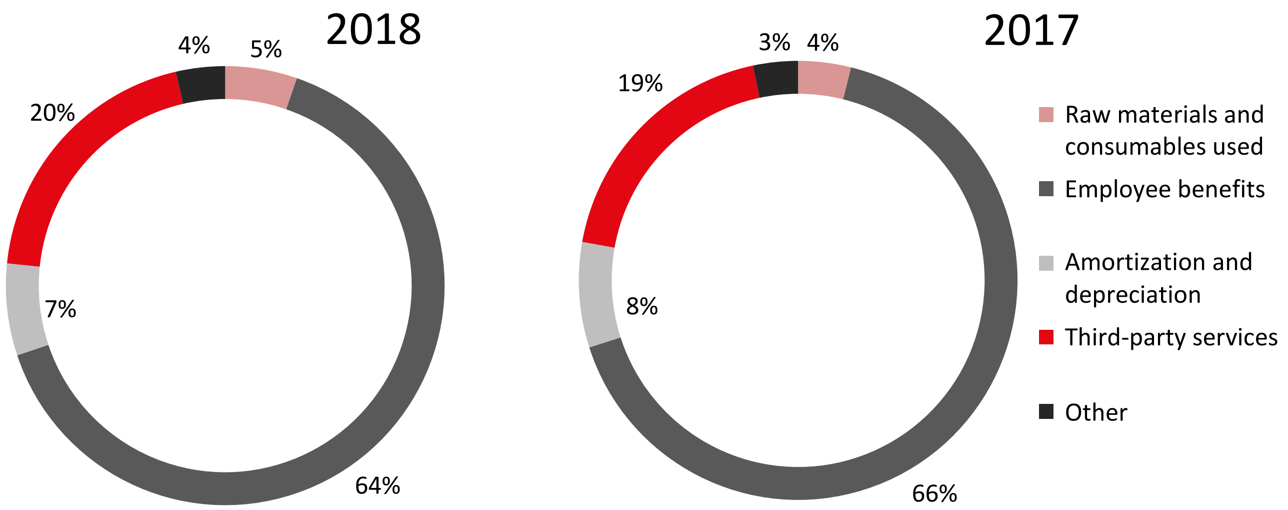
In addition, due to the fact that the Group classifies the PocketECG devices as fixed assets, the manufacturing cost of PocketECG sold to Medi-Lynx is not charged on a one-off basis to costs of raw materials and consumables used, but it is amortized over a period of 3 years, corresponding to the expected life cycle of the devices. In 2018, the total cost on this account amounted to PLN 2.9 million and decreased by approximately PLN 0.7 million year on year, mainly as a result of complete depreciation of devices acquired in 2014 (PLN 0.6 million) and a decrease in the average USD exchange rate (PLN 0.1 million).

Third-party services

At present, third-party services account for 20% of the Group's operating expenses, and their amount increased by PLN 3.4 million (11%) as compared to the corresponding period. The key items of costs of third-party services include: telecommunications and Internet services, lease and rental services as well as courier and transport services. For a breakdown of the costs of third-party services, see Note 10 to the consolidated financial statements.

The year-on-year increase in the costs of third-party services is mainly attributable to an increase in lease and lease costs related to the lease of additional office space in Warsaw and servers, an increase in transport costs related to higher volume of examinations and higher costs of marketing services related to an intensive marketing and sales campaign launched in the second quarter of 2017. Additionally, in 2018 – unlike in the corresponding period – the Company incurred costs of IT services. IT services include consultancy on programming and maintenance of the IT environment.

Chart 3. Structure of operating expenses in 2018 and 2017 (in %)



Net finance income

Table 10. Finance income and costs in 2018 and 2017 (PLN '000)

	01.01.2018-31.12.2018	01.01.2017-31.12.2017	Change	Change %
Finance income	712	614	98	16%
Finance costs	(3 863)	(5 842)	1 979	(34%)
Net finance income	**(3 151)**	**(5 228)**	**2 077**	**(40%)**

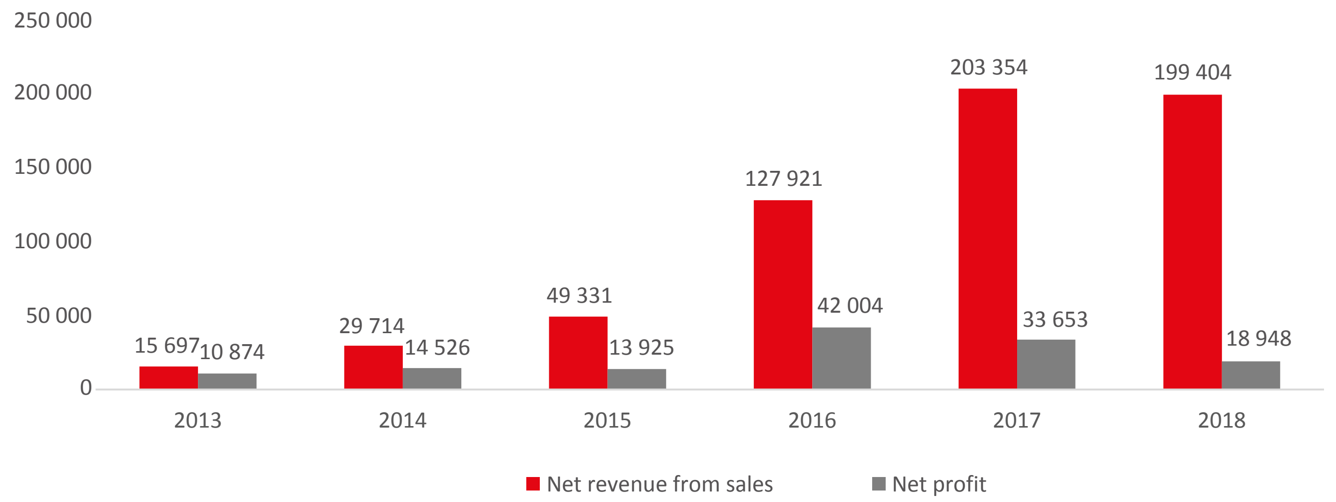
Finance costs comprise mainly interest on bonds and interest on the liability to the seller of shares in Medi-Lynx. The nominal year-on-year decrease in interest expense is primarily attributable to the partial repayment on 30 March 2018 of the liability to the seller of shares in Medi-Lynx (the amount repaid was PLN 2.0 million).

As at the reporting date, the Parent Company held a loan (granted in USD) granted to a consolidated foreign operation (MDG HoldCo). In accordance with IAS 21, this monetary item forms part of the net investment in a foreign operation. In the consolidated financial statements, foreign exchange differences (recognized under net finance income in the separate financial statements) are recognized in other comprehensive income.

Profit and profitability

Net profit generated in 2018 amounted to PLN 18.9 million and profit attributable to Shareholders of the Parent Company amounted to PLN 14.4 million. Profit before tax was encumbered with net finance costs of PLN 3.2 million, comprising mainly interest on the Group's financial liabilities. Following the repayment of a portion of financial liabilities (mainly repayment of subsequent instalments of the liability on account of the acquisition of shares in Medi-Lynx), the net finance costs in 2018 decreased by approximately PLN 1.9 million year on year. On the other hand, the positive impact of lower finance costs was offset by other operating expenses related primarily to state tax costs at Medi-Lynx – PLN 1.4 million (additional information on the provision is presented in Note 10 to the interim consolidated financial statements of Medicalgorithmics Capital Group for 2018) and impairment losses on inventories – PLN 0.7 million. The sales margin was 14% and EBITDA margin stood at 18%.

Chart 4. Net sales and net profit in PLN '000 in particular years



In 2018, return on assets (ROA) stood at 6%, down by 6 percentage points from 12% in 2017. On the other hand, return on equity (ROE) in 2018 amounted to 8% and was lower than in 2017 by 9 percentage points. The decrease in this ratio was caused by a decrease in net profit, the reasons for which have already been discussed.

Table 11. ROA and ROE in 2018 and 2017 and changes in these ratios during the last financial year

	2018	2017	Change (pp)
ROA	6%	12%	(6)
ROE	8%	17%	(9)

ROA = net profit/total assets as at the end of the period
ROE = net profit/equity as at the end of the period

Cash flows

In 2018, the Capital Group achieved a positive balance of cash flows from operating activities, mainly as a result of surplus from net profit and depreciation/amortization. The cash flows from operating activities were also significantly affected by changes in working capital. The Group recorded positive cash flows from investing activities resulting from the redemption of investment certificates offset by expenditures on research and development activities.

In turn, negative cash flows from financing activities were caused mainly by the repayment of the first part of the liability towards the seller of shares in Medi-Lynx, the dividend distribution, payout to a minority shareholder and the repayment of interest on bonds.

Table 12. Selected items of the cash flow statement for the financial years 2018 and 2017 (PLN '000)

	01.01.2018-31.12.2018	01.01.2017-31.12.2017	Change	Change %
Net cash from operating activities	44 232	28 611	15 621	55%
Net cash from investing activities	2 407	(22 026)	24 433	(111%)
Net cash from financing activities	(18 981)	(21 594)	2 613	(12%)
Total net cash flows	**27 658**	**(15 009)**	**42 667**	**(284%)**
Closing balance of cash	**60 189**	**32 531**	**27 658**	**85%**

III. 2. Asset and financial position of the Capital Group

As at 31 December 2018, total assets amounted to PLN 316.1 million which represents an increase by PLN 26.8 million (or 9%) from the end of 2017. The increase in total assets was largely attributable to the appreciation of the USD exchange rate by approximately 8% year on year. The impact of exchange rate differences resulted in an increase in total assets by PLN 16.6 million.

The tables below present the key assets the Group and sources of their financing, as well as changes in these assets during the last financial year.

Table 13. Key assets as at the end of 2018 and 2017 and changes in these assets during the last financial year

Assets (PLN '000)	31.12.2018	31.12.2017	Change	Change %
Fixed assets *including:*	**227 170**	**228 573**	**(1 403)**	**(1%)**
Intangible assets	210 454	196 900	13 553	7%
Property plant and equipment	14 685	17 249	(2 564)	(15%)
Long-term financial assets	200	10 910	(10 710)	(98%)
Current assets *including:*	**88 912**	**60 708**	**28 204**	**46%**
Trade and other receivables	22 781	23 951	(1 169)	(5%)
Short-term financial assets	5 942	4 226	1 716	41%
Cash and cash equivalents	60 189	32 531	27 658	85%
TOTAL ASSETS	**316 082**	**289 281**	**26 801**	**9%**

As at 31 December 2018, total non-current assets amounted to PLN 227.2 million and accounted for 72% of total assets. The most significant item of non-current assets were intangible assets, including client bases (PLN 107 million), goodwill recognized on the acquisition of subsidiaries, Medi-Lynx and Kardiosystem Monitoring (currently: Medicalgorithmics Polska) (PLN 84.4 million), and expenditure on research activities (PLN 17.8 million). For a description of impairment tests, see Note 15 to the consolidated financial statements for 2018. The value of non-current assets remained relatively unchanged from 2017 (-1%). The most significant changes were recorded for intangible assets (+7%) and long-term financial assets (-98%). Intangible assets increased due to high exchange rate differences (PLN +15.0 million) and additional expenditure on development works (PLN +4.6 million). Long-term financial assets decreased mainly as a result of the sale of a portion of investment certificates (PLN -8.9 million) and the recognition of all the remaining certificates as short-term assets, as they are scheduled to be redeemed in April 2019 (PLN -1.8 million).

As at 31 December 2018, total current assets amounted to PLN 88.9 million and accounted for 28% of total assets. The most significant items in this group of assets were cash (68%) and trade receivables (26%). The y/y increase in current assets (+46%) resulted mainly from the increase in cash held in bank accounts and short-term deposits (PLN +27.7 million). Excluding the effect of foreign exchange differences, cash increased by PLN 23.6 million y/y, mainly due to cash flows from operating activities. Current assets also include short-term financial assets in the form of investment certificates (PLN 5.9 million).

Table 14. Key items of equity and liabilities as at the end of 2018 and 2017 and changes in these items during the last financial year

EQUITY AND LIABILITIES (PLN '000)	31.12.2018	31.12.2017	Change	Change %
Equity attributable to Shareholders of the Parent Company	**189 864**	**168 913**	**20 951**	**12%**
Non-controlling interests	40 898	34 820	6 078	17%
Long-term liabilities ***of which:***	**13 257**	**67 649**	**(54 392)**	**(80%)**
Liabilities in respect of bonds and other financial liabilities	7 479	63 794	(56 315)	(88%)
Short-term liabilities ***including:***	**72 063**	**17 899**	**54 164**	**303%**
Liabilities in respect of bonds and other financial liabilities	58 399	7 887	50 512	640%
Trade and other liabilities	10 717	7 522	3 195	42%
Total liabilities	85 320	85 548	(228)	(0%)
TOTAL EQUITY AND LIABILITIES	**316 082**	**289 281**	**26 801**	**9%**

As at 31 December 2018, equity attributable to Shareholders of the Parent Company amounted to PLN 189.9 million (+12% y/y). The increase in equity attributable to Shareholders of the Parent Company was driven by the accumulation of profit attributable to Shareholders of the Parent Company earned in 2018 (+PLN 14.4 million) and foreign exchange gains resulting from an year-on-year increase in the USD exchange rate (+PLN 12.7 million). The amount of equity attributable to Shareholders of the Parent Company was also affected by the distribution of dividend at the Parent Company (PLN -5.1 million) and by remeasurement of the incentive scheme (PLN -1 million). As a result of the measurement, it was concluded that the scheme will not be implemented and the provision for future payments, recognized in previous periods, was derecognized. The effect of the derecognition was taken directly to the supplementary capital. Non-controlling interests of PLN 40.9 million correspond to the minority shareholding in Medi-Lynx attributable to a minority shareholder.

As at 31 December 2018, long-term liabilities amounted to PLN 13.3 million and decreased by 80% y/y. The decrease was mainly caused by the recognition of the total amount of liabilities on account of bonds as short-term liabilities (PLN -50.5 million) in connection with the forthcoming maturity date of 21 April 2019. The decrease in long-term liabilities was also affected by the repayment of another instalment of the liability on account of the purchase of Medi-Lynx shares, amounting to approximately USD 2 million.

As at 31 December 2018, short-term liabilities amounted to PLN 72.1 million, and increased by 303% y/y. This increase is mainly caused by the recognition of the entire amount of liabilities on account of bonds as a short-term liabilities (PLN +50.5 million). The increase in short-term liabilities was also driven by an increase in payroll liabilities (PLN +3.4 million), presented under trade and other liabilities in the balance sheet. These liabilities increased primarily as a result of the recognition of a provision for the remuneration of the Parent Company's Management Board (PLN +1.5 million) and the recognition of provisions for bonuses to the management and severance pays at Medi-Lynx (PLN +1.2 million, excluding the effect of changes in the USD exchange rate).

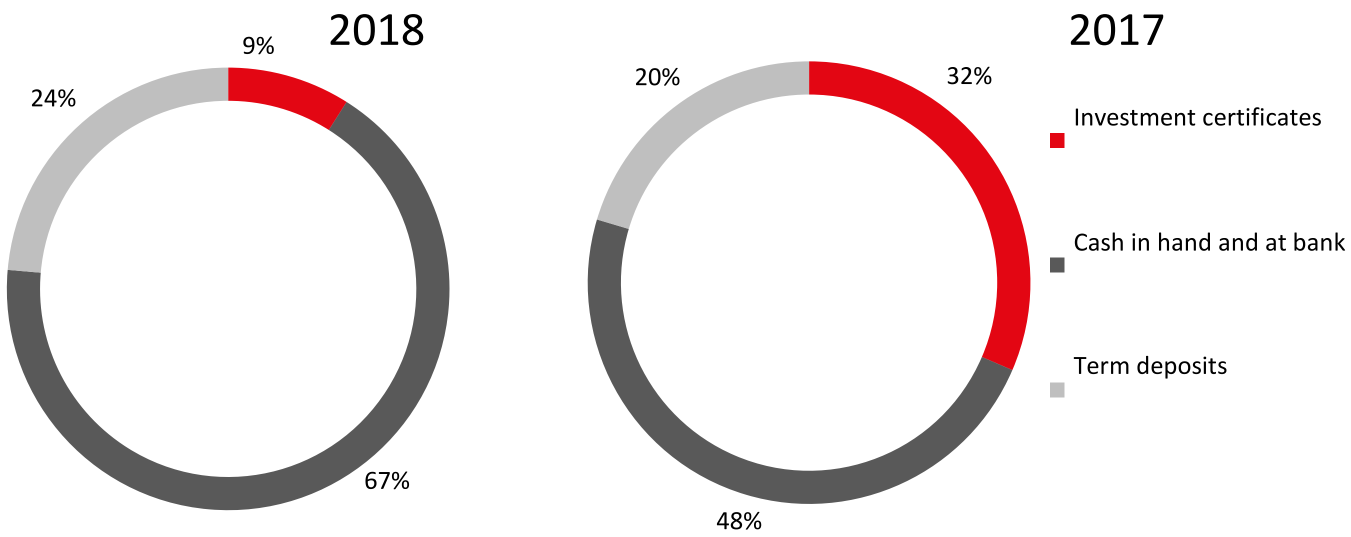
III. 3. Cash and financial assets

As at 31 December 2018, the Group has significant financial surpluses which it tries to invest in such a way as to maximize the rate of return on investment while maintaining a low level of risk.

As at 31 December 2018, the Capital Group held only investment certificates of the fund Bezpiecznych Obligacji Fundusz Inwestycyjny Zamknięty and cash in current accounts and term deposits. During 2018, in accordance with the Management Board's decision to discontinue investing cash surpluses in debt instruments and to submit, in stages, the certificates held for redemption, the Company sold a part of the investment certificates held with a total value of PLN 8.9 million. For more information, see Note 17 to the Group's consolidated financial statements for 2018.

The current financial position of the Capital Group is safe. The Group's capital management policy is to maintain a solid capital base which ensures timely settlement of liabilities, preservation of confidence of shareholders, investors and trading partners, and future growth of the Company's business.

Chart 5. Structure of financial assets as at the end of 2018 and 2017



21 April 2019 is the redemption date for bonds issued by the Company. The Group has consolidated own funds sufficient to repay its liabilities on this account. Furthermore, the Parent Company is at an advanced stage of negotiations aimed at obtaining financing in the form of a current loan to ensure its current liquidity.

Table 15. Structure of the Group's financial assets as at the end of 2018 and 2017 (PLN '000)

Financial assets	31.12.2018	31.12.2017	Change	Change %
Investment certificates – long-term	-	10 710	(10 710)	(100%)
Investment certificates – short-term	5 942	4 226	1 716	41%
Cash in hand	7	11	(4)	(39%)
Cash in bank accounts	44 554	22 838	21 716	95%
Term deposits	15 628	9 682	5 947	61%

Credits and loans received

As at the end of 2018, the Group reported a liability on account of credits in the amount of PLN 328 thousand, resulting from a loan contracted by a subsidiary, Medicalgorithmics Polska, (PLN 289 thousand) and from the credit card debt balance (PLN 39 thousand). The loan in question was contracted between Medicalgorithmics Polska and PKO Leasing S.A. on 20 June 2017. The amount of the loan is approximately PLN 350 thousand. The loan was granted for 5 years (the last instalment falls due in September 2022). The loan was earmarked for the expansion of the subsidiary's operating activities.

Issue of bonds

In 2016, the Parent Company issued bonds with a nominal value of PLN 50 000 thousand and a maturity date of 21 April 2019. The purpose of the issue was to finance an investment in a subsidiary, Medi-Lynx. For detailed information on issue, see Note 23 to the Consolidated financial statements of the Capital Group for 2018. The Group holds own funds sufficient to repay its liabilities on account of bonds issued. The Parent Company also intends to obtain third-party financing in the form of a current credit facility to secure its current liquidity.

Loans granted

The Capital Group granted only intercompany loans which are eliminated during consolidation.

Sureties and financial guarantees granted and received

Medicalgorithmics S.A. is a party to agreements for the EU co-financing of investment projects aimed at the development of the products and services offered. A failure to meet the conditions set for the relevant development work may give rise to the risk that the grants received will have to be repaid. The grants are secured by promissory notes.

As at the balance sheet date, the risk described above was assessed as doubtful. The Company carries out its works in accordance with the schedule.

The Parent Company endorses an interest-bearing promissory note issued by a subsidiary, MDG HoldCo with its registered office in the US to Medi-Lynx Monitoring, Inc. as a payment for the purchase of shares in Medi-Lynx. As at 31 December 2018, the outstanding amount was USD 3 980 thousand, including interest accrued in the amount of USD 119 thousand. Payments are spread over two equal instalments amounting to USD 1,990 thousand, payable on 30 March 2019 and 30 March 2020. Liabilities bear interest at a fixed interest rate.

In 2018, the Parent Company established security for the Company's liabilities resulting from the lease of usable area in the building at Al. Jerozolimskie 81 in Warsaw in the form of an irrevocable and unconditional bank guarantee in the total amount of PLN 404 thousand. The beneficiary of the guarantee is Central Tower 81 Sp. z o.o. (the lessor). The guarantee is valid from the date of issue to 30 August 2024.

Material off-balance sheet items

Apart from the surety described above, there are no other material off-balance sheet items.

IV. Discussion of the Company's performance and the Company's asset and financial position

IV. 1. Discussion of the Company's performance

In 2018, the Company continued its strategy and operated on the basis of the subscription model according to which it sells the devices and then charges monthly subscription fees for their use and for the use of the related software and server infrastructure.

The table below presents the key items of the Company's statement of comprehensive income for 2018 and 2017.

Table 16. Key items of the statement of comprehensive income for 2018 and 2017 and changes over the last financial year (in PLN '000)

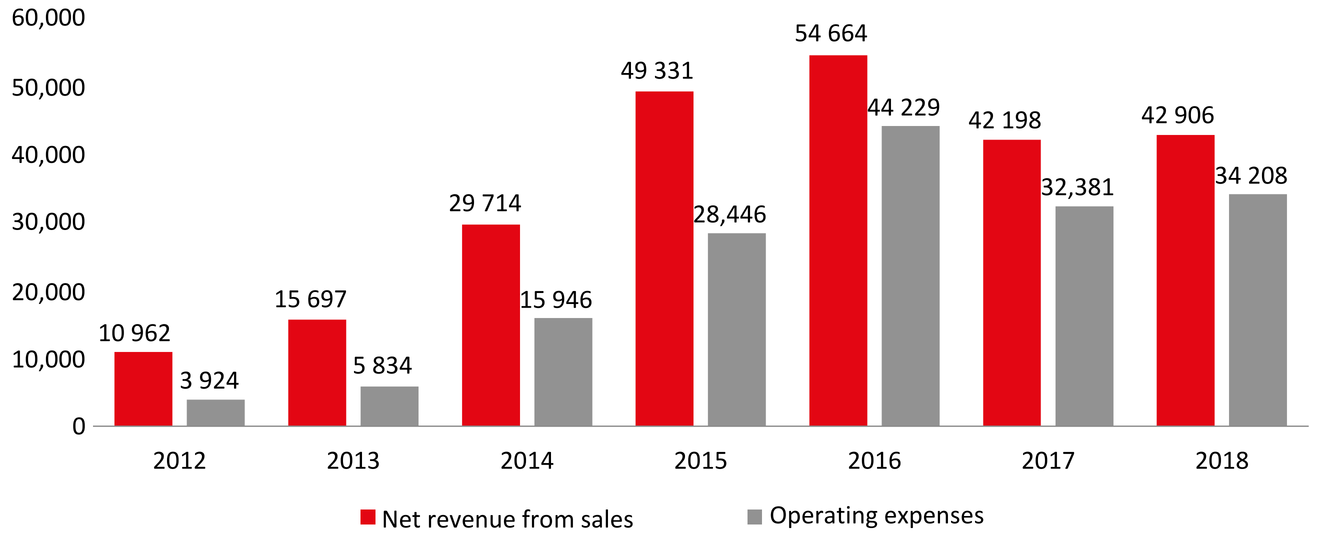
	01.01.2018-31.12.2018	01.01.2017-31.12.2017	Change	Change %
Sales revenue	42 906	42 198	708	2%
Operating expenses	34 208	32 381	1 827	6%
Profit on sales	8 698	9 817	(1 119)	(11%)
Other operating revenue net	(870)	334	(1 204)	(360%)
Net finance income/(costs)	5 904	(13 752)	19 656	(143%)
Profit/(loss) before tax	13 732	(3 601)	17 333	(481%)
Net profit/(loss)	**11 325**	**(2 830)**	**14 155**	**(500%)**
EBITDA	9 001	11 418	(2 417)	(21%)

Sales revenue

In 2018, the revenue of Medicalgorithmics S.A. amounted to PLN 42.9 million, which represents an increase by 2% as compared to 2017.

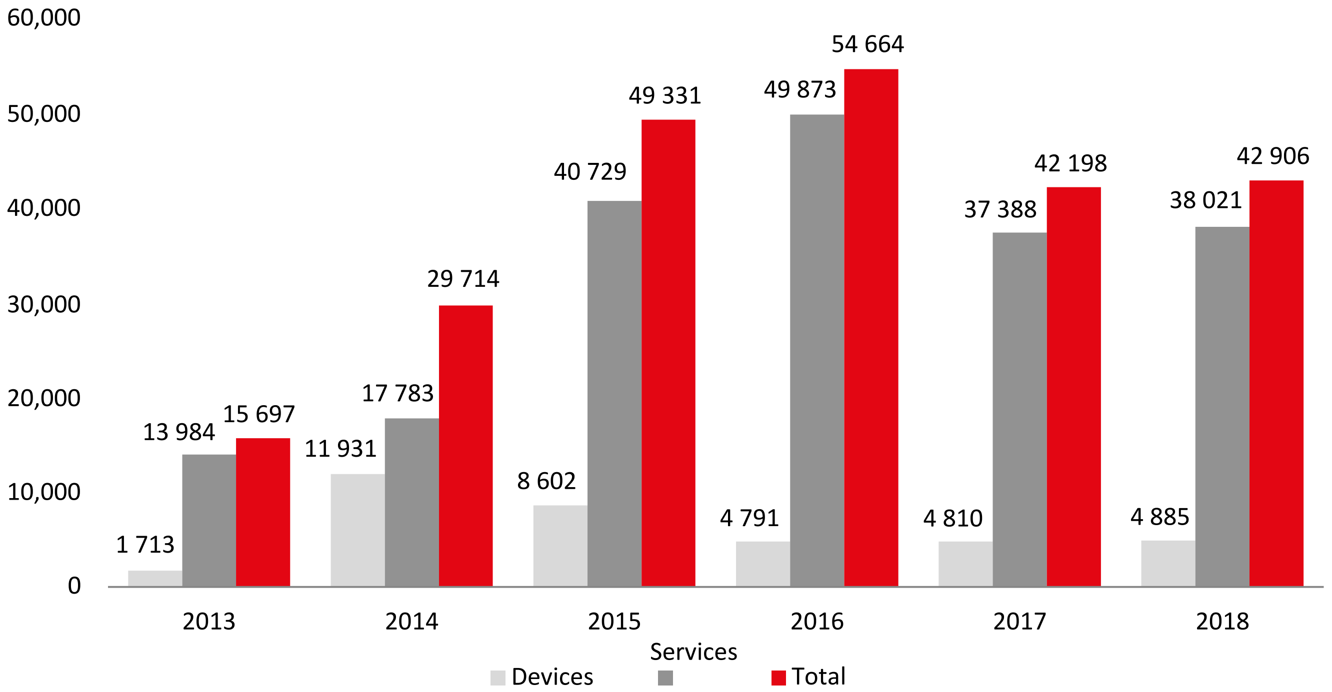
The Company's revenue is generated mainly in the United States. The year-on-year increase in revenue was primarily driven by an increase in subscription revenue from Medi-Lynx and customers outside the United States, partially offset by the termination of cooperation with the US partner, AMI Monitoring, Inc., and its subsidiary, Spectocor, LLC ("AMI/Spectocor"). Additionally, the lower average USD/PLN exchange rate also had a negative impact on the revenue level.

Chart 6. The Company's sales revenue and operating expenses in particular years (PLN '000)



In 2018, the Company earned all of its revenue from the sales of PocketECG system. This revenue comprised the revenue from sales of devices in the amount of PLN 4.9 million (PLN 4.8 million in 2017), representing 11% of total revenue (11% in 2017), and revenue from sales of services in the amount of PLN 38.0 million (PLN 37.4 million in 2017), representing 89% of total revenue (89% in 2017).

Chart 7. Sales revenue by type in particular years (PLN '000)



The Company earns the vast majority of its sales revenue in USD. In 2018, revenue in USD accounted for 94% of total sales revenue (92% in 2017).

Operating expenses

Table 17. Structure of operating expenses in 2018 and 2017 (PLN '000)

	01.01.2018-31.12.2018	01.01.2017-31.12.2017	Change	Change %
Raw materials and consumables used	6 434	5 351	1 083	20%
Employee benefits	15 283	17 243	(1 960)	(11%)
Amortization and depreciation	1 173	1 267	(94)	(7%)
Third-party services	9 375	6 746	2 629	39%
Other	1 943	1 774	169	9%
TOTAL:	**34 208**	**32 381**	**1 827**	**6%**

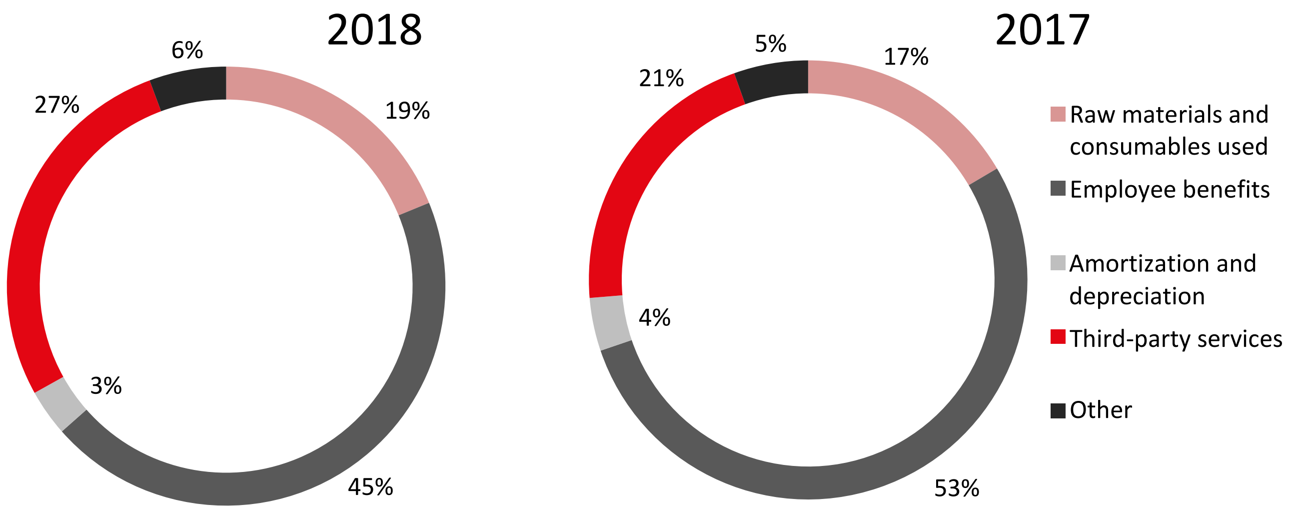
Employee benefits, comprising salaries and salary surcharges, were the most significant component of operating expenses. A high share of such expenses in the structure of expenses (45% of total operating expenses) results from the business profile of Medicalgorithmics S.A., which is mainly based on the development of new technologies in the area of manufacturing and software. The Company builds its competitive advantage on the basis of a highly qualified team. The decrease in personnel costs in relation to 2017 results from actuarial remeasurement of the incentive scheme. To the best of its knowledge, the Company's Management Board decided to assume that it is impossible to meet the non-market condition. This assumption applies to all tranches of options offered under the incentive scheme. Therefore, in accordance with IFRS 2 "Share based payments", no amount should be recognized as an expense of the scheme. For more information on the measurement of the incentive scheme, see Note 19.6 to the Financial Statements of Medicalgorithmics S.A.

The second largest item of operating expenses in 2018 were costs of third-party services (27%). Marketing costs, costs of lease of production and office space as well as costs of advisory services were the most important components of costs of third-party services. Marketing costs included an extensive marketing and sales campaign launched in 2017.

In the reporting period, the Company recorded a significant increase in costs of third-party services, as compared to the corresponding period. It results mainly from an increase in the costs of marketing services due to a year-on-year increase in the costs of marketing activities in the United States. There was also a significant increase in advisory costs, including the costs of patent and market analysis services. Additionally, in 2018 – unlike in the corresponding period – the Company incurred significant costs of IT services. IT services include consultancy on programming and maintenance of the IT environment.

Due to the sale of an increased number of devices in 2018, the Company incurred higher total production and servicing costs, which drove the increase in the item "Raw materials and consumables used". Depreciation and amortization expenses remained relatively flat as compared to the previous year.

Chart 8. Structure of operating expenses in 2018 and 2017 (in %)



Net finance income

Table 18. Finance income and costs in 2018 and 2017 (PLN '000)

	01.01.2018-31.12.2018	01.01.2017-31.12.2017	Change	Change %
Finance income	8 990	3 879	5 111	132%
Finance costs	(3 086)	(17 631)	14 545	(82%)
Net finance income	**5 904**	**(13 752)**	**19 656**	**(143%)**

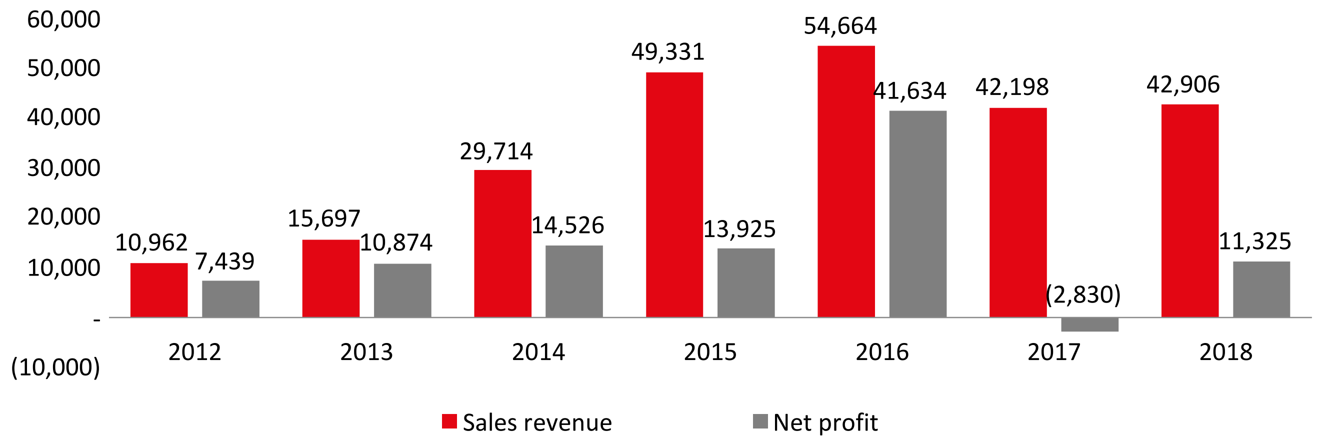
In 2018, the Company reported a net finance income of PLN 5.9 million. Finance income comprised mainly interest accrued on loans to related parties and foreign exchange gains of PLN 5.8 million related mainly to unrealized foreign exchange differences on loans to subsidiaries. Finance costs include interest expense on bonds in the amount of PLN 2.8 million and loss on the disposal of investment certificates in the amount of PLN 0.3 million.

Profit and profitability

In 2018, Medicalgorithmics S.A. reported a net profit of PLN 11.3 million (compared to a loss of PLN 2.8 million in the corresponding period of the previous year). The loss for 2017 was attributable, to a large extent, to foreign exchange losses included in finance costs.

In 2018, exchange rate differences on loans granted to subsidiaries had a positive effect on the net profit. This effect was partially offset by slightly higher operating expenses and higher other operating costs resulting from the impairment loss on inventories.

Chart 9. Net sales and net profit in PLN '000 in particular periods



The sales margin and EBITDA margin were 20% and 21%, respectively (23% and 27% in 2017). Despite a slight increase in revenue as compared to the corresponding period, the margin on sales for 2018 was lower, which was attributable in particular to higher costs of third-party services (mainly advisory, marketing and IT services) as compared to 2017.

Cash flows

In 2018, the Medicalgorithmics S.A achieved a positive balance of cash flows from operating activities, mainly as a result of surplus from net profit and depreciation/amortization. The cash flows from operating activities were also significantly affected by changes in working capital. The Company recorded positive cash flows from investing activities resulting from the redemption of investment certificates offset by expenditures on research and development activities. Negative cash flows from financing activities resulted from payment of dividend for 2017 and interest on bonds issued by the Company.

Table 19. Selected items of the cash flow statement for the financial years 2018 and 2017 (PLN '000)

	01.01.2018-31.12.2018	01.01.2017-31.12.2017	Change	Change %
Net cash from operating activities	11 804	7 719	4 085	53%
Net cash from investing activities	1 196	(19 330)	20 526	(106%)
Net cash from financing activities	(7 454)	(9 964)	2 510	(25%)
Total net cash flows	**5 546**	**(21 575)**	**27 121**	(126%)
Closing balance of cash	**15 750**	**10 204**	**5 546**	**54%**

IV. 2. Asset and financial position of the Company

As at 31 December 2018, total assets amounted to PLN 224.6 million which represents an increase by PLN 9.2 million (or +4%) from the end of 2017. The tables below present the key assets the Company and sources of their financing, as well as changes in these assets during the last financial year.

Table 20. Key assets as at the end of 2018 and 2017 and changes in these assets during the last financial year

ASSETS (PLN '000)	31.12.2018	31.12.2017	Change	Change %
Fixed assets *including:*	**190 913**	**188 858**	**2 055**	**1%**
Intangible assets	18 817	14 581	4 236	29%
Property plant and equipment	2 000	1 301	699	54%
Long-term financial assets	72 275	74 691	(2 416)	(3%)
Shares in subsidiaries	96 038	94 771	1 267	1%
Current assets *including:*	**33 677**	**26 564**	**7 114**	**27%**
Inventories	5 088	7 856	(2 768)	(35%)
Trade and other receivables	6 897	4 278	2 620	61%
Short-term financial assets	5 942	4 226	1 716	41%
Cash and cash equivalents	15 750	10 204	5 546	54%
TOTAL ASSETS	**224 590**	**215 422**	**9 169**	**4%**

As at 31 December 2018, total non-current assets amounted to PLN 190.9 million and accounted for 85% of total assets. The most significant components of this group of assets were shares in subsidiaries (50% of the balance of fixed assets), long-term financial assets (38%) and intangible assets (10%). Shares in subsidiaries included shares in Medi-Lynx (PLN 94.7 million) and Medicalgorithmics Polska (PLN 1.3 million). Long-term financial assets comprised mainly loans granted to a subsidiary, MDG Holdco, to finance the purchase of equity interest in Medi-Lynx, provide working capital to the subsidiary (PLN 72.1 million) and settle the liability towards AMI/Spectocor for the client base acquired from this entity. The main component of intangible assets is expenditure on development work (PLN 17.8 million) described in Note 12 to the Company's separate financial statements for 2018.

As at 31 December 2018, the balance of non-current assets remained at a similar level as at the end of 2017 (PLN +2.1 million, +1% y/y). Intangible assets increased by 29% y/y mainly due to higher expenditure on development works (PLN +4.6 million). Long-term financial assets decreased mainly as a result of the sale of a portion of investment certificates in 2018 (PLN -4.8 million) and the recognition of all the remaining certificates as short-term assets (PLN -5.9 million). The effect of these changes was partially offset by an increase in the amount of loans granted as a result of foreign exchange gains (PLN +5.1 million) and the accrual of interest on these loans for 2018 (PLN +3.7 million). Shares in subsidiaries increased due to the acquisition of 100% of shares in Kardiosystem Monitoring Sp. z o.o. (currently: Medicalgorithmics Polska Sp. z o.o.) in July 2018 (PLN +0.2 million) and the injection of capital into the acquired subsidiary (PLN +1.1 million).

As at the end of 2018, current assets amounted to PLN 33.7 million and accounted for 15% of total assets. The most significant component of this group of assets was cash and cash equivalents, accounting for 47% of total current assets. Current assets increased by PLN 7.1 million y/y (+27%), mainly due to an increase in cash and cash equivalents (PLN +5.5

million, +54%) and in trade and other receivables (PLN +2.6 million, +61%). The increase in cash is attributable to cash flows from operating activities and the sale of investment certificates. The increase in trade and other receivables was mainly driven by an increase in trade and other receivables from related entities (PLN +0.8 million) and from other entities (PLN +0.5 million), as well as an increase in receivables from the State budget, mainly arising from the settlement of VAT (PLN +1.2 million) and CIT (PLN +0.7 million) with the tax office. The effect of these changes was partially offset by a decrease in inventories by PLN 2.8 million y/y resulting from the policy of gradual reduction of inventories and more effective inventory management, as well as from the recognition of an impairment loss (PLN -0.7 million) referred to in Note 16 to the Company's separate financial statements for 2018.

Table 21. Key items of equity and liabilities as at the end of 2018 and 2017 and changes in these items during the last financial year

EQUITY AND LIABILITIES (PLN '000)	31.12.2018	31.12.2017	Change	Change %
Equity	**167 080**	**161 885**	**5 195**	**3%**
Long-term liabilities ***including:***	**2 728**	**51 482**	**(48 754)**	**(95%)**
Liabilities arising from bonds	-	49 938	(49 938)	(100%)
Short-term liabilities ***including:***	**54 782**	**2 055**	**52 727**	**2 566%**
Liabilities arising from bonds	50 472	336	50 136	14 922%
Trade and other liabilities	3 956	1 326	2 630	198%
Prepayments and deferred expenses	315	315	-	-
Total liabilities	57 510	53 537	3 973	7%
TOTAL EQUITY AND LIABILITIES	**224 590**	**215 422**	**9 168**	**4%**

As at 31 December 2018, equity amounted to PLN 167.1 million (+3% y/y). The increase in equity was driven by the accumulation of profit earned in 2018 (PLN +11.3 million). The increase in equity due to the accumulated profit of the reporting period was partially offset by the distribution of dividend for 2017 (PLN -5.1 million) and the effects of remeasurement of the incentive scheme. As a result of the measurement, the Management Board concluded that the scheme would not be implemented and the provision for future payments under the scheme, recognized in previous periods, was derecognized (PLN -5.3 million). The effect of the derecognition was taken directly to the supplementary capital (PLN +4.3 million).

As at 31 December 2018, long-term liabilities came at PLN 2.7 million, having declined by PLN 48.8 million (-95%) year on year. This decrease primarily reflected the reclassification of the long-term portion of liabilities on account of bonds to short-term liabilities in connection with the planned redemption of bonds in the second quarter of 2019 (PLN -49.9 million).

As at 31 December 2018, short-term liabilities stood at PLN 54.8 million, up by PLN 52.7 million y/y (+2 566%). This increase is mainly caused by the recognition of the entire amount of liabilities on account of bonds as a short-term liabilities (PLN +50.1 million). The balance of trade and other liabilities also increased (PLN +2.6 million y/y), mainly due to higher payroll liabilities, which included a provision for the Management Board's remuneration for 2018 (PLN +1.5 million) and trade liabilities from non-related entities (PLN +0.7 million).

IV. 3. Cash and financial assets

Medicalgorithmics S.A. has significant financial surpluses which it tries to invest in such a way as to maximize the rate of return on investment while maintaining a low level of risk.

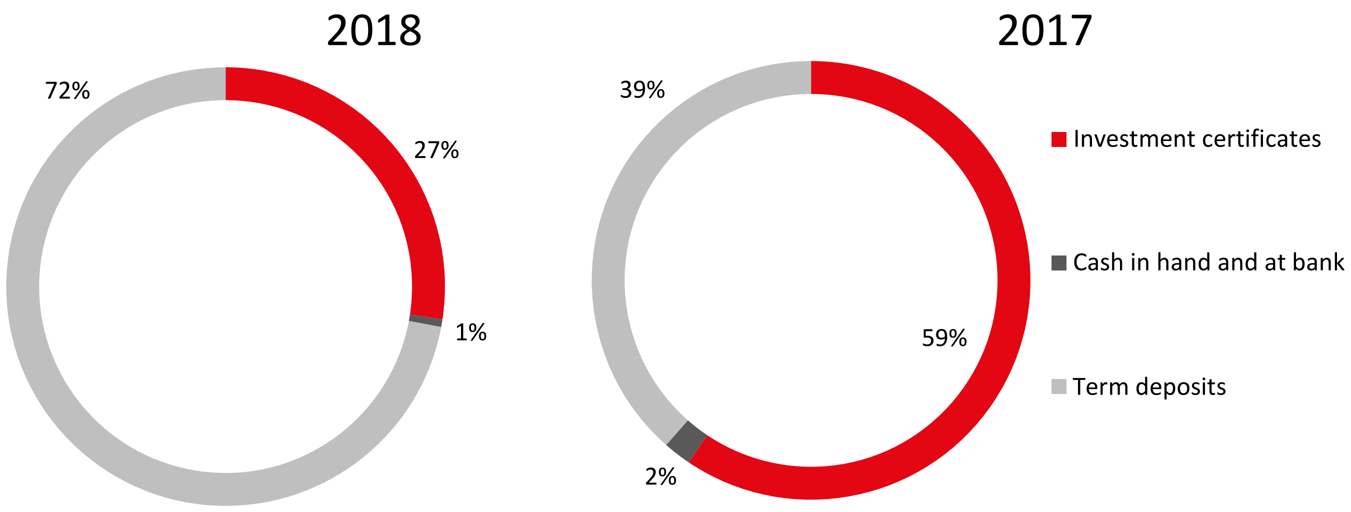
As at 31 December 2018, the Company held only investment certificates of the fund Bezpiecznych Obligacji Fundusz Inwestycyjny Zamknięty and cash in current accounts and term deposits. During 2018, in accordance with the Management Board's decision to discontinue investing cash surpluses in debt instruments and to submit, in stages, the certificates held for redemption, the Company sold a part of the investment certificates held with a total value of PLN 8.9 million. For more information, see Note 14 to the Company's separate financial statements for 2018.

The current financial position of the Company is safe. The Company's capital management policy is to maintain a solid capital base which ensures timely settlement of liabilities, preservation of confidence of capital market participants and future growth of the Company's business.

Table 22. Structure of the Company's cash and financial assets as at the end of 2018 and 2017 (PLN '000)

Financial assets	31.12.2018	31.12.2017	Change	Change %
Investment certificates – long-term	-	10 710	(10 710)	(100%)
Investment certificates – short-term	5 942	4 226	1 716	41%
Cash in hand	7	11	(4)	(39%)
Cash in bank accounts	115	511	(396)	(78%)
Term deposits	15 628	9 682	5 946	61%

Chart 10. Structure of cash and financial assets as at the end of 2018 and 2017



The redemption of bonds issued by the Company in the second quarter of 2016 is scheduled for 21 April 2019. The nominal value of bonds is PLN 50 million. The Medicalgorithmics Group holds consolidated own funds sufficient to repay its liabilities on account of bonds issued. Furthermore, the Company is at an advanced stage of negotiations aimed at obtaining financing in the form of a current loan to ensure its current liquidity.

Credits and loans received

As at the end of 2018, Medicalgorithmics S.A. reported a liability on account of credits and loans in the amount of PLN 39 thousand, resulting entirely from the credit card debt balance.

Issue of bonds

In 2016, the Company issued bonds with a nominal value of PLN 50 000 thousand and a maturity date of 21 April 2019. The purpose of the issue was to finance an investment in a subsidiary, Medi-Lynx. For more information on the issue, see Note 22 to the separate financial statements for 2018.

Loans granted

In 2016, the Company granted loans to its subsidiary, MDG HoldCo, in the total amount of USD 11 700 thousand. The purpose of the loans was to finance the acquisition of shares in Medi-Lynx and to finance the subsidiary's operating activities. In 2017, the Company granted another loan to MDG HoldCo in the amount of USD 6,813 thousand. These funds were used to settle the liabilities towards AMI/Spectocor for the client base. For detailed information on loans granted, see Note 14 to the separate financial statements for 2018.

Sureties and financial guarantees granted and received

The Company is a party to agreements for the EU co-financing of investment projects aimed at the development of the products and services offered. If the conditions for the implementation of development works are not met, there may be a risk of necessity to return the subsidies received. The grants are secured by promissory notes.

As at the balance sheet date, the risk described above was assessed as doubtful. The Company carries out its works in accordance with the schedule.

The Company endorses an interest-bearing promissory note issued by a subsidiary, MDG HoldCo with its registered office in the US to Medi-Lynx Monitoring, Inc. as a payment for the purchase of shares in Medi-Lynx. As at 31 December 2018, the outstanding amount was USD 3 980 thousand. It is spread over two equal instalments amounting to USD 1,990 thousand, payable on 30 March 2019 and 30 March 2020. Liabilities bear interest at a fixed interest rate.

In 2018, the Company established security for the Company's liabilities resulting from the lease of usable area in the building at Al. Jerozolimskie 81 in Warsaw in the form of an irrevocable and unconditional bank guarantee in the total amount of PLN 404 thousand. The beneficiary of the guarantee is Central Tower 81 Sp. z o.o. (the lessor). The guarantee is valid from the date of issue to 30 August 2024.

V. Other material information on operations of the Issuer and the Capital Group

V. 1. Ongoing research and development projects

The Parent Company conducts a number of development works to improve the current version of the PocketECG system and works on new solutions in the area of heart rate monitoring. The key development projects for the Group are:

- PocketECG CRS – device and system for cardiac rehabilitation;
- PocketECG 12Ch – device and system for remote, instant ECG description (12-channel ECG).
- ECG TechBot – software using a set of algorithms for automatic analysis and interpretation of the ECG signal based on deep learning methods.

Early this year, the company launched the promotion the remote cardiac rehabilitation system, PocketECG CRS.

Pilot implementations were carried out in several renowned hospitals in Poland. The PocketECG CRS was cleared by the Food and Drug Administration (FDA) under the procedure 510(k). Following FDA'a approval, the Company will soon initiate actions to commercialize the new system in the U.S.

As part of the ECG Techbot project, the research team continued work on a set of algorithms for automatic analysis and interpretation of ECG signal (algorithms for rhythm analysis, classification of morphology, detection of waves).

As regards PocketECG 12Ch, the work was suspended at the stage of the YOKE prototype. The development of algorithms continues under the TechBot project, and work on the complete product (HW+SW) will resume after the global version of the PDA with LTE has been developed.

The PocketECG CRS PocketECG 12Ch projects are financed from own funds. ECG TechBot is co-financed by the National Centre for Research and Development ("NCBiR") from public funds. The estimated total cost of project implementation as well as the total amount of eligible costs is PLN 11 188 thousand, with the maximum value of co-financing set at PLN 6,335 thousand.

Key costs capitalized as development works in progress include the costs of salaries of the R&D staff. As at the balance sheet date, the Group updated its assessment of the potential of target markets and the impact of commercialization of new products on the Group's performance. With respect to PocketECG CRS, the potential of the US, Canadian, Indian and Polish markets will allow the product to be commercialized in the coming periods and generate sufficient cash flows to cover the expenditures incurred. In the case of PocketECG 12Ch, the launch of commercialization is scheduled for 2022. In the opinion of the Management Board of the Company, development works will be completed and will produce the expected economic effects.

The table below presents the structure of expenditure on development work in progress. Changes in the balance of expenditure on development work in progress are also presented in Note 15 to the consolidated financial statements of the Medicalgorithmics Capital Group for 2018.

Table 23. Structure of expenditure on development works in progress at the end of 2018 and 2017 (PLN '000)

	31.12.2018	31.12.2017	Change	Change %
Salaries including overheads	11 876	8 420	3 456	41%
Other	5 912	4 728	1 184	25%
TOTAL:	**17 788**	**13 148**	**4 640**	**35%**

V. 2. Other investments in Poland and abroad

The Capital Group is currently not engaged in any investment projects other than those described in this report.

V. 3. Factors and events, especially non-recurring ones, with material bearing on financial performance

In the reporting period, there were no events, other than those described in Sections III - IV which had a material bearing on operations of the Issuer and the Capital Group and the consolidated financial statements for 2018.

V. 4. Material court, arbitration and administrative proceedings

In the period covered by this report, no proceedings were pending before a court, an arbitration body or a public administration authority concerning the Parent Company's liabilities or claims with a value equal to or higher than 10% of the Company's equity. No proceedings were also pending before a court, an arbitration body or a public administration authority concerning liabilities or claims of other Group companies with a value equal to or higher than 10% of the Group's equity.

V. 5. Related party transactions

In the discussed period, there were no transactions with related parties concluded on terms other than arm's length terms.

Transactions with Members of the Parent Company's Management Board and Supervisory Board are described in Sections I.8 and I.9 of this report.

Transactions with related parties of the Parent Company have been discussed in detail in Note 27 to the financial statements of Medicalgorithmics S.A. for 2018.

Shareholders (as related entities)

Pursuant to resolution No 16/06/2018 of the Ordinary Shareholders' Meeting of Medicalgorithmics S.A., on 30 July 2018 the Parent Company paid out a dividend to shareholders in the aggregate amount of PLN 5 121 thousand, i.e. PLN 1.42 per share.

The dividend was paid for all 3,607 thousand shares in the Company.

V. 6. The Management Board's position regarding the possibility of achieving forecasts

The Capital Group did not publish any financial forecasts for the period considered in this report or future periods.

V. 7. Information on factors which, in the Issuer's opinion, will affect its performance during at least the next year

According to the Management Board, the Capital Group's current financial condition and growth prospects do not involve any significant threats to its ability to continue as a going concern in the foreseeable future. However, there are certain factors, both internal and external, that will directly or indirectly affect the Group's financial results in the next year. The most important of them include:

- revision of medical examinations refund fees and payments for the procedure received from private insurers by the subsidiary, Medi-Lynx;
- change in the business model and signing long-term service contracts directly with key private insurers (also presented in Section II hereof);
- decrease in reimbursement rates for Medi-Lynx services used in settlements with clients of some insurers using the Multiplan network (described in Note 32 to the consolidated financial statements for 2018);
- developments on the US medical services market, where the Group generates the vast majority of its revenue;
- growing sales to partners with whom the Parent Company has signed contracts, which will help diversify and boost revenue;
- growth of cardiac diagnostics sector in countries where the Group's products are sold and level of reimbursement for services provided with PocketECG devices;
- movements in exchange rates of the currencies of countries where the Group operates.

V. 8. Prospects for the development of the Capital Group's operations in the upcoming year

The objective of the Parent Company and Group companies is to ensure a long-term increase in the company's value. For this reason, the Management Board is committed to ensuring further development that will strengthen Group’s position among the leading providers of state-of-the-art cardiac telemetry technologies, not only in the United States, but also in other countries around the world. The Group pursues its business objective by improving its own products and services in the field of telemedicine technologies, researching and searching for new directions of the Group's development, developing new algorithms and products (services) and acquiring new customers in the existing and new markets.

In order to expand and strengthen its market position, the Parent Company plans to conclude agreements with new business partners and further expand its cooperation with existing customers. In 2019, the Parent Company also intends to continue its efforts to create reimbursement codes for the long-term arrhythmia monitoring service in Germany and the UK.

Moreover, the Group will implement research and development projects to improve the current version of the PocketECG system and work on new solutions in the area of heart rate monitoring, including a hybrid cardiac telerehabilitation system and a system for remote, immediate ECG description.

The new Management Board of Medi-Lynx will implement the development strategy based on a new business model consisting in signing long-term service contracts directly with key private insurers (in-network contracts). The Group assumes that if this goal is achieved, although it will result in lower reimbursement rates for a single service, the Group will secure access to new clients and, as a consequence, significantly increase the sales volume. The Group is of the opinion that this strategy will allow Medi-Lynx to achieve sustained annual revenue growth and implement its business growth strategy, as well as increase the security and stability of Medi-Lynx's revenue.

The Group plans to continue a comprehensive information and image campaign of the PocketECG system as part of its business development in the United States, including participation in industry conferences, publications in the specialist press and numerous sales initiatives via social media. In 2019, the Group also plans to initiate pilot implementations of a new product – PocketECG CRS, a system for hybrid cardiac rehabilitation – in the United States. In addition, Medi-Lynx intends to implement a comprehensive training programme for its sales department and to increase the number of sales representatives.

V. 9. Assessment of the feasibility of investment plans

The Capital Group and the Parent Company are fully capable of financing their investment projects and assume that they are financed from equity or, if necessary, debt. Where appropriate, the Group will apply for grants for development work on new products.

V. 10. Information on sources of supply and markets

When manufacturing the PocketECG system, the Company uses a number of suppliers of electronic components and sub-assemblies. Sources of supply are diversified, however the Group is constantly establishing new business contacts with potential suppliers. There was no single counterparty whose supplies accounted from more than 10% of the Company's net sales revenue.

V. 11. Other agreements significant to the Group's business

The Capital Group and the Parent Company did not execute any agreements significant for their operations other than those mentioned above.

The Capital Group and the Parent Company did not execute any agreements in the reporting period or after the balance sheet date that could result in a change in the shareholder structure of the Parent Company.

There are also no agreements between the Capital Group or the Parent Company and its management staff, providing for compensation in the event of resignation or removal from office without a good reason, or when resignation or removal from office is caused by acquisition of the Company by another company.

V. 12. Information on any retirement and similar benefit obligations

Due to their immateriality, the Group does not recognize provisions for retirement severance pays and jubilee awards.

VI. Description of material risk factors and risk management methods

The Capital Group is exposed to various types of risk associated with its operations and environment, and these may have an impact on the performance of its strategic tasks and objectives. Threats and risks have been classified according to three categories:

- operational risk;
- financial risk;
- legal risk.

The Management Board of the Parent Company is responsible for establishing and supervising the risk management by the Capital Group. The Capital Group's risk management policy is to identify and analyses the risks to which the Capital Group is exposed, to set appropriate limits and controls, and to monitor the risk and the extent of matching the limits to the risk. The risk management policies and systems are reviewed on a regular basis to take account of changes in the market environment and the Capital Group's business. Using such tools as training, management standards and procedures, the Capital Group seeks to build a stimulating and constructive control environment, in which all employees understand their respective roles and responsibilities.

Operational risk

Risk associated with strategic objectives

The Group's strategic objective is to attain the position of a leading supplier of modern technological solutions within the field of mobile cardio diagnostics in the United States and on the EU market and the in developing countries. The Group intends to achieve the aforementioned objective by developing technologies, expanding the sales network in the United States, geographical and product diversification. On account of a number of factors which impact the effectiveness of the pursued growth strategy, the Group is unable to fully guarantee that all of its strategic objectives will be achieved. The risk of making inaccurate decisions stemming from an inappropriate assessment of a given situation or the Group's inability to adapt to changing market conditions may mean that its growth strategy will not be fully implemented, and the future financial performance may be worse than currently assumed.

Risk associated with technical breakdowns and technology development

The Group is exposed to the risk of failure of software, electronic equipment and ICT infrastructure. Frequent technical problems could induce customers (medical centres and electrophysiologists) to use competitive solutions. The Group is also exposed to errors caused by inappropriate data integration and cyber-attacks, which may affect the Group's operations and financial performance.

The Group's business is highly dependent on specialist ICT systems and technologies and the Group should ensure continuous development of the technology employed in order to remain competitive on the market. The risk of failure to adapt the Company's product to the changing technological conditions, including the LTE bands, may prevent the planned expansion on global markets.

Risk of customer concentration

The Group provides medical services to a dispersed group of recipients (patients in many different medical institutions), nevertheless the number of payers (insurers) is limited. If one of the key insurers were to stop reimbursing the medical procedure provided by Group this change could have an adverse effect on the Group's operating results. Furthermore, in most markets a single commercial partner is responsible for the Group's sales. Exclusivity clauses in agreements restrict the options for the Group using alternative distribution channels. Legal disputes between the Group and given commercial partners could potentially result in extended periods during which the value of PocketECG systems distributed by the given business partner is diminished or the distribution ceases altogether. There is also the risk of a commercial partner not performing the specified business objectives associated with increasing sales on a target market.

Risk associated with product concentration

The Group's operations are primarily based on selling a single solution - the PocketECG system and additional services stemming from the sale of the PocketECG system. In the event of a significant decrease in the market demand for PocketECG systems as a results of a loss of the competitive advantage enjoyed by the Group's technology, a downturn on the cardio diagnostics market or as a consequence of other adverse external or internal events, the Group is exposed to a risk of a significant decrease of revenues on sales, and as a consequence a deterioration of financial results and loss of financial liquidity.

Risk associated with key employees

The Group's operations are based on top managers and professionals in the areas of IT systems, programming, medical devices, digital signal processing, project management, cardio diagnostics, electrophysiology and sale of medical services. The fierce competition on the demand side of the labor market and a limited number of specialized workers and managers on the telemedical market means that attracting and retaining and appropriate staff is one of the significant challenges faced by the Group. The loss of key personnel may have an adverse effect on the Group's operations.

Risk associated with suppliers

The Group procures components for the production of PocketECG devices from a limited number of verified recipients, who guarantee high quality of products. In the event of delays in the supply of the required volume of components, a decrease in the quality or a change in the prices thereof, the Group would be forced to seek other sources of supply. Taking into account that the recipient selection and verification process is extended, possible delays, decrease in quality of the supplied elements or interruptions to component deliveries might limit of delay the production of PocketECG systems.

Risk of delays to the Group's deliveries

In conjunction with the multi-stage PocketECG device production process and the limited number of new devices available, deliveries of devices to recipients are exposed to a risk of delays in the event of a significant steep increase in orders. In the event of a rapid increase to the volume of orders for PocketECG systems, there is a potential risk of insufficient production capacity to satisfy the demand reported by recipients.

Risk of failure to obtain or retain approvals

Introducing the Group's products to trade on target markets is associated with obtaining certificates, approvals and consents appropriate for the given jurisdictions. The Group's solutions are classified as medical devices pursuant to US law and are subject to numerous Food and Drug Administration (FDA) regulations. The Company holds the necessary certificates, approvals and admissions to trade for the sold products, however there is a risk of their loss, suspension or withdrawal. Furthermore the Group may fail to obtain approvals for new or modified products.

Risk associated with industry development and competition

The global telemedicine market is developing very rapidly and this entails changes to the products available on the market as well as significant variability of industry standards and patent requirements. In conjunction with the above, there is a risk that the Group fails to adapt to rapid market changes, which might entail a deterioration to its competitive position and financial standing.

Risk of force majeure

The Group is exposed to the consequences of numerous events, the occurrence of which it is unable to foresee or for which it is unable to estimate the probability of their occurrence. Such events may include geopolitical conflicts, terrorism, natural disasters, economic crises or public health crises. The occurrence of such events, and in particular a cumulation during a single period, may significantly disrupt the Group's operations.

Financial risk

Below is a summary of financial risks. For a more detailed description of financial risk management methods and sensitivity analysis, see Note 24 to the consolidated financial statements for 2018 and Note 23 to the financial statements of Medicalgorithmics S.A. for 2018.

Liquidity risk

The Group is exposed to liquidity risk understood as loss of the ability to settle liabilities on time or to acquire funds for financing operations. In particular, this risk is associated with the settlement of trade liabilities, liabilities to public authorities and financial liabilities. In part, the Group finances its assets with borrowed capital – bonds and liabilities under promissory notes. There is a risk that the Group will experience economic difficulties and will not be able to repay the promissory note or redeem the bonds.

Credit risk

The Group is exposed to the risk of financial loss in a situation where a customer or counterparty fails to meet its contractual obligations. Credit risk to which the Group is exposed is primarily related to a significant concentration of receivables and investment certificates.

Management of the credit risk associated with the investment certificates held is at the disposal of the fund managing those assets and follows from the provisions of its statutes. The main components of fund investments in which the Group holds investment certificates are debt securities in the form of bonds listed on the Catalyst market.

Risk associated with the macroeconomic situation

The Group's operations depend on the macroeconomic situation in the markets where products and services are or will be distributed and provided, including primarily in the United States. The effectiveness, and in particular the profitability of the Group's business depends, among other things, on the economic growth rate, fiscal and monetary policy, the level of inflation and the level of health care expenditures in these countries. All these factors indirectly affect the Group's revenue and financial performance and may also affect the implementation of the Group's growth strategy.

Currency risk

The Group is exposed to currency risk related primarily to changes in the USD/PLN exchange rate. The Group reports its financial figures in PLN, whereas the majority of transactions are concluded by the Group in USD. Fluctuations in currency exchange rates primarily affect changes in the value of the Group's revenue and receivables, translated into PLN. Thus there is a risk of the Polish correctly strengthening, which will result in a decrease in margins generated on sales by the Polish company. The impact of exchange rate fluctuations on profit or loss is naturally partly offset by the fact that approximately 79% of costs are incurred in USD. The Group does not hedge its open currency positions.

Risk of terminating or reducing reimbursements

Amongst others, the Group distributes its products in public health care systems and collaborates with a number of private insurers. If one of the key insurers were to stop reimbursing the medical procedure provided by the Group or significantly reduce the reimbursement rates, this change could have a material adverse effect on the Group's operating results. In addition, consolidation processes in the private insurer market and, as a result, their growing bargaining power may also lead to lower levels of reimbursement of services than those currently applied. The model of cooperation between Medi-Lynx and private insurers with whom long term out-of-network contracts are not signed also remains a risk factor. The growing negotiating position of insurers, aided by changing regulations causes an ever growing price and legal pressure on suppliers of medical services without out-of-network agreements and may translate into the obtained rates for tests and the possibility of acquiring new customers.

Legal risk

Risk associated with liability for the product introduces to trade

Due to the fact that the Group's devices monitor the users' strategically important vital parameters - functioning of the circulation system, any irregularities in the operation of these devices may result in actions or omission by users or their physicians which are not adequate to the user's actual state of health, which may translate into a significant threat to the users' life or health. Furthermore, the Group's devices may, as a result of design faults or breakdowns, cause electric shocks, burns, poisoning or contamination with harmful substances. These incidents may result in the Group being required to pay compensation to users of its products or to the heirs of such users or other persons, as well as to satisfy recourse claims, in particular from physicians, hospitals or distributors against whom users may directly address their claims.

The Group holds third party liability insurance in connection with its operations, purchased from a reputable insurance company and comprising a product liability insurance policy with a high sum insured and a worldwide coverage.

Risk associated with key agreements

The Group recognizes the risk associated with the failure to perform, improper performance or termination of significant agreements, including as a result of a termination by the counterparty. Failure to perform or improper performance of significant agreements may entail the occurrence of a liability for the Company on account thereof, including liability in compensation. Termination of individual significant agreements may entail a partial or total loss of revenues which the Group expected from the given agreements, wherein at the same time it does not have to go hand in hand with a proportional reduction to costs forecast in conjunction with these agreements.

Risk associated with the protection of intellectual property and company secrets

The Group's operations and its competitive position rely on ensuring comprehensive protection of the uniqueness of technical solutions introduced to the market in subsequent generations of the Company's products. There is a risk that competitors may market devices that use protected technical solutions implemented by the Company, as well as a risk that the Company's software copyrights may be infringed. The above potential infringements of the Company's intellectual property rights may require the Company to undertake legal measures and incur the related costs. Wherein there is no guarantee for the Company that such actions will be successful.

Risk associated with personal data processing

Within the scope of its operations the Company process various kinds of personal data, including sensitive data of various categories of natural persons. In particular, the Company processes data pertaining to the health of users of goods produces by the Company. In conjunction with the above, the Company is subject to personal data protection regulations in appropriate jurisdictions in which the Company has introduced its products to trade. Far-reaching regulations in this area have been adopted in the European Union, including Poland. The above leads to the risk of breaching personal data protection regulations and as a consequence to severe financial penalties or sanctions being imposed on the Company by supervisory authorities.

Risk associated with a change to the legal environment, including within the scope of tax law

The observed and expected changes to the provisions of law, and in particular applicable to business activities, labor law and social insurance, medical law and health care system law, personal data protection law, commercial law may be heading in a direction which causes the occurrence of negative consequences for the Group's operations. New legal regulations may entail interpretation problems, inconsistent court rulings, unfavorable interpretations adopted by public administration bodies, lack of cohesion between Polish and EU body of rulings. This risk exists in a particular manner within the scope of tax law, due to the high impact of regulations and the manner for their interpretation within this scope on the Company's financial situation. The planned and possible changes in the regulations governing the introduction of medical devices to the market and the financing of medical services in the Group's target markets remain a significant source of risk. Some amendments to existing legislation could significantly hinder or even reduce the scale of business.

Also regulations concerning corporate income tax, personal income tax, value added tax and contributions to social security undergo relatively frequent changes, often resulting in the absence of any established regulations or legal precedents for reference. In addition, the tax authorities are authorized to inspect the books and accounting records of the Group. There is a risk that additional financial charges may be imposed on the Group together with interest and other penalties.

VII. Statement of compliance with corporate governance standards

VII. 1. Corporate governance rules applied in the Parent Company

Medicalgorithmics S.A. accepted the corporate governance rules laid down in the Code of Best Practice for WSE Listed Companies, adopted by the Supervisory Board of the Warsaw Stock Exchange on 13 October 2015 by way of resolution No 26/1413/2015, as of the date of admission of the Company's shares to trading on the regulated market. The Code of Best Practice for WSE Listed Companies is available on the WSE website (http://www.gpw.pl) under the listed companies corporate governance tab.

In 2018, Medicalgorithmics S.A. complied with all provisions contained in this set, except for the following recommendations: I.R.2. (not applicable), IV.R.2. (not applicable), IV.R.3. (not applicable), VI.R.1., VI.R.2. and detailed rules: I.Z.1.3., I.Z.1.10. (not applicable), I.Z.1.15., I.Z.1.16., II.Z.1., II.Z.2. (partially applied), III.Z.4., IV.Z.2. (not applicable), IV.Z.5. (partially applied), V.Z.6., VI.Z.1., VI.Z.4. The justification for non-application or refraining from application, in whole or in part, of the aforementioned recommendations and detailed rules is provided below:

I.R.2. Where a company pursues sponsorship, charity or other similar activities, it should publish information about the relevant policy in its annual activity report.

This principle is not applicable. The Parent Company is not engaged in any sponsorship, charitable or similar activities.

I.Z.1. A company should operate a corporate website and publish on it, in a legible form and in a separate section, in addition to information required under the legislation:

I.Z.1.3. a chart showing the division of duties and responsibilities among members of the management board drawn up according to principle II.Z.1;

This principle is not applied. At present, the Parent Company's Management Board is composed of one person.

I.Z.1.10. financial projections, if the company has decided to publish them, published at least in the last 5 years, including information about the degree of their implementation;

This principle is not applicable. The Parent Company has not decided to publish financial projections.

I.Z.1.15. information about the company's diversity policy applicable to the company's governing bodies and key managers; the description should cover the following elements of the diversity policy: gender, education, age, professional experience, and specify the goals of the diversity policy and its implementation in the reporting period; where the company has not drafted and implemented a diversity policy, it should publish the explanation of its decision on its website;

This principle is not applied. Pursuant to the Parent Company's Articles of Association, members of the Management Board are appointed by the Supervisory Board, whereas members of the Supervisory Board are appointed by the General Shareholders' Meeting. Information on qualifications and professional experience of the persons appointed to the Management and Supervisory Boards is published in current reports and on the Parent Company's website. At the same time, the Parent Company informs that no formal diversity policy has been prepared in the form of a single document or adopted. Nevertheless, the Management Board of the Parent Company, being aware of the importance and need to ensure diversity with respect to all employees of the Parent Company, guided by the belief that such an approach has a significant impact on the effectiveness of the entire business and on building the company's position, both in the opinion of its customers, employees and other stakeholders, follows the best practices in its day-to-day operations and decisions and, above all, naturally focuses on:

a) applying the principles of equal treatment in the workplace, which means non-discrimination in any way whatsoever, either directly or indirectly, on the basis of gender, age, education, colour, religion, non-religiousness, political views, citizenship, nationality, ethnic origin, sexual orientation, gender identity, marital status, family status, lifestyle, health, disability, and the form, extent and basis of employment and the circumstances giving rise to discrimination;

b) being guided by objective substantive criteria and professionalism in the selection of employees for various job functions within the organization;

c) building diverse teams to enable their members to have a broader perspective in the process of solving problems, increased creativity, improved working atmosphere and, as a result, to ensure the transfer of knowledge and innovation;

d) treating employees with due dignity and respect as well as respecting and appreciating individual differences between team members so that each person employed can use his/her personal potential to contribute to the development of the Parent Company as a whole and its individual products;

e) creating a working environment with an atmosphere of dialogue, openness, tolerance and teamwork;

f) strengthening the corporate culture based on the mission implemented and values elaborated by the Parent Company, so that it supports a proactive attitude, self-confidence and belief that everything depends on us and on the relations between us;

g) enabling work/life balance through flexible working time, ad-hoc home working, the possibility to leave work in case of emergencies, trouble-free emergency leave.

I.Z.1.16. information about the planned transmission of a general meeting, no later than 7 days before the date of the general meeting;

This principle is not applied. The Parent Company does not broadcast general meetings.

II.Z.1. The internal division of responsibilities for individual areas of the company's activity among management board members should be clear and transparent, and a chart describing that division should be available on the company's website.

This principle is not applied. At present, the Parent Company's Management Board is composed of one person.

II.Z.2. A company's management board members may sit on the management board or supervisory board of companies other than members of its group subject to the approval of the supervisory board.

The principle is applied to a limited extent, i. e. taking into account the criterion of competitiveness of companies other than members of the Capital Group. A wider application of this principle would require an amendment to the Company's Articles of Association.

III.Z.4. At least once a year, the person responsible for the internal audit function (if such function is designated within the Company) and the Management Board shall present to the Supervisory Board their own evaluation of the effectiveness of systems and functions referred to in Principle III.Z.1, together with an appropriate report.

This principle is not applied. The Parent Company did not have a separate function of the person responsible for internal audit. The Management Board presents the Supervisory Board with an appropriate assessment on an ongoing basis. However, such an assessment is not a formal report.

IV.R.2. If justified by the structure of shareholders or expectations of shareholders notified to the company, and if the company is in a position to provide the technical infrastructure necessary for a general meeting to proceed efficiently using electronic communication means, the company should enable its shareholders to participate in a general meeting using such means, in particular through:

1) real-life broadcast of the general meeting;

2) real-time bilateral communication where shareholders may take the floor during a general meeting from a location other than the general meeting;

3) exercise of the right to vote during a general meeting either in person or through a plenipotentiary.

This principle is not applicable. Due to the current shareholding structure and for economic reasons, the Parent Company does not hold general meetings using electronic communication means. To the best of the Parent Company's knowledge, the current formula of organization of the general meeting meets the shareholders' expectations and enables proper and effective execution of rights attached to shares. The Parent Company will consider holding general meetings using electronic means of communication if it becomes aware of such expectations of a wider group of shareholders.

IV.R.3. Where securities issued by a company are traded in different countries (or in different markets) and in different legal systems, the company should strive to ensure that corporate events related to the acquisition of rights by shareholders take place on the same dates in all the countries where such securities are traded.

This principle is not applicable. The Parent Company does not issue securities outside Poland.

IV.Z.2. If this is justified by the shareholder structure of the Company, the Company ensures a generally available real-time broadcast of the proceedings of the general meeting of shareholders.

This principle is not applicable. Due to the current shareholding structure and for economic reasons, the Parent Company does not hold general meetings using electronic communication means. To the best of the Parent Company's knowledge, the current formula of organization of the general meeting meets the shareholders' expectations and enables proper and effective execution of rights attached to shares. The Parent Company will consider holding general meetings using electronic means of communication if it becomes aware of such expectations of a wider group of shareholders.

IV.Z.5. The rules of general meetings and the method of conducting the meeting and adopting resolutions must not restrict the participation of shareholders in general meetings and the exercising of their rights. Amendments of the rules of the general meeting should take effect at the earliest as of the next general meeting.

This principle is applied to the extent to which it relates to the manner of conducting the meeting and adopting resolutions. In other respects, this principle does not apply as the Parent Company did not adopt any regulations of the General Meeting.

V.Z.6. In its internal regulations, the Company determines criteria and circumstances, which may lead to the conflict of interest in the Company, and the rules of conduct, if the conflict of interest occurs or is likely to occur.

This principle is not applied. The Parent Company has not introduced any specific internal regulations concerning the resolution of conflicts of interest, considering generally applicable legal regulations in this respect as sufficient.

VI.R.1. The remuneration of members of the company’s governing bodies and key managers should follow the approved remuneration policy.

This principle is not applied. Remuneration of members of the Management Board and the Supervisory Board is determined, respectively, by the Supervisory Board and the General Meeting. The Management Board of the Parent Company has no impact on the introduction of regulations in this respect. The remuneration policy for key managers results from the Parent Company's practice, however, it has not been adopted in the form of a binding document.

VI.R.2. The remuneration policy should be closely tied to the company’s strategy, its short- and long-term goals, long-term interests and results, taking into account solutions necessary to avoid discrimination on whatever grounds.

This principle is not applied. The Parent Company does not have a formalized remuneration policy for members of the Company's governing bodies and key managers.

VI.Z.1. Incentive schemes should be constructed in a way necessary among others to tie the level of remuneration of members of the company’s management board and key managers to the actual long-term financial standing of the company and long-term shareholder value creation as well as the company’s stability.

This principle is not applied. The Management Board of the Parent Company, based on the remeasurement of the incentive scheme as at 31 December 2018 on the basis of current estimates of the fulfilment of financial criteria and to the best of its knowledge, decided to assume that it was impossible to meet one of the financial conditions of the scheme (a non-market condition). Consequently, the incentive scheme is not implemented and is currently under review. The Management Board of the Company intends to submit the issue of modification of the incentive scheme for discussion at the General Shareholders’ Meeting.

VI.Z.4. In this directors’ report, the company should report on the remuneration policy including at least the following:

1) general information about the company’s remuneration system;

2) information about the conditions and amounts of remuneration of each management board member broken down by fixed and variable remuneration components, including the key parameters of setting the variable remuneration components and the terms of payment of severance allowances and other amounts due on termination of employment, contract or other similar legal relationship, separately for the company and each member of its group;

3) information about non-financial remuneration components due to each management board member and key manager;

4) significant amendments of the remuneration policy in the last financial year or information about their absence;

5) assessment of the implementation of the remuneration policy in terms of achievement of its goals, in particular long-term shareholder value creation and the company’s stability.

This principle is not applied. The Parent Company does not have a formalized remuneration policy for members of the Company's governing bodies and key managers. With respect to the publication of information on the remuneration of the Members of the Management Board and Supervisory Board, the Parent Company applies the applicable laws. In addition, the Company publishes information on the incentive scheme in place at the Parent Company in its annual reports. At the same time, the Parent Company is of the opinion that information on the remuneration of individual managers remains strictly confidential and is protected by the Parent Company on equal terms with business secrets.

VII. 2. Key features of the Capital Group's internal control and risk management systems used in the preparation of separate and consolidated financial statements

The Management Boards of the Capital Group companies are responsible for internal control and risk management systems and their efficiency with respect to the process of preparing financial statements. The internal control system and risk management in this respect is based on the identification and assessment of risk areas accompanied by defining and taking actions aimed at minimising or eliminating them.

The internal control system at the Capital Group helps to ensure the fulfilment of the Group's tasks, as well as the achievement of long-term profitability objectives and also helps to maintain the reliability of financial reporting. It comprises a number of controls, responsibilities and the identification and assessment of risks that may adversely affect the achievement of the Capital Group's objectives. In organizational terms, the internal control system comprises functional control performed by the Management Board, managers of units and employees in accordance with their responsibilities.

In order to ensure the effective operation of the Parent Company's internal control system and risk management in the financial reporting process, the Management Board of the Parent Company has adopted and approved an accounting policy for Medicalgorithmics S.A. that complies with the International Financial Reporting Standards and is updated on an ongoing basis to reflect new regulations.

The flow of information within the Capital Group is strictly controlled in order to prepare up-to-date, reliable and complete financial statements drawn up in a reliable manner, on the basis of accounting regulations and policies. The keeping of the accounting books of the Capital Group companies in 2018 and preparation of the financial statements was entrusted to an experienced accounting firms, which apply their own control systems for the process of preparing financial statements.

The accounting books are kept in an IT system which ensures a clear division of competences, coherence of accounting records and control between ledgers. Access to this data at various levels and in various units is available via a well-developed reporting system. The IT systems are adapted on an ongoing basis to the changing accounting policies or other legal standards, which allows for high flexibility of functionalities.

The systems are protected against unauthorized access with passwords and function-based access control. Control over this access is carried out at each stage of financial statements preparation, beginning with the entering of source data, through the processing of data, to the generation of output information.

The process of preparing the separate financial statements of the Capital Group companies is carried out in close cooperation with the financial department of the Parent Company which reports directly to the Management Board of the Parent Company. Both in the Capital Group companies and in the entities responsible for keeping the Group companies' accounting books, there are a number of principles concerning the system of control, identification and assessment of risk inherent in the Group's operations, including the principle of making accounting records based only on properly drawn up and accepted documents, or checking these documents in formal, accounting and substantive terms. The information flow between the Group companies and the entities responsible for keeping the accounting books is also controlled.

Substantive control over the preparation of the consolidated financial statements is exercised by the Management Board of the Parent Company which approves quarterly, semi-annual and annual financial statements before their publication. Annual and semi-annual financial statements are audited/reviewed by an independent statutory auditor selected by the Supervisory Board of Medicalgorithmics S.A.

VII. 3. Shareholders of the Parent Company and their rights

The ownership structure of major holdings of shares in the Parent Company as at the date of publication of this report is presented in Section I.5.

All the Parent Company's shares are ordinary, bearer shares with no special control rights. The Articles of Association of Medicalgorithmics S.A. do not provide for any limitations on voting rights, such as limitations of the voting rights of holders of a given percentage or number of votes, time limits for exercising voting rights or provisions according to which the rights attaching to securities are separated from the holding of such securities As at the date of this report, there are no restrictions on the transferability of ownership rights to the Parent Company's shares, except for lock-up clauses entered into with an entity that acquired 151 thousand series F shares issued in 2016, i.e. Medi-Lynx Monitoring, Inc. Until 30 March 2018, these shares could not be disposed of, including through sale, pledge, swaps or other similar transactions. This restriction applies to a block of 50% of shares covered by the lock-up agreement until 30 March 2019, and to 25% of those shares until 30 March 2020.

VII. 4. General Meeting

The General Meeting of Medicalgorithmics S.A. is the supreme governing body of the Parent Company. The general meetings can be either ordinary or extraordinary, based on generally applicable regulations and the Articles of Association of Medicalgorithmics S.A., which are available on the Parent Company's website.

In particular, the General Meeting has the authority to:

- review and approve the Directors' Report on the Parent Company's operations and the financial statements for the previous financial year;
- appoint and dismiss the Chairman, Vice-Chairman and members of the Supervisory Board;
- grant discharge to members of the Management Board and Supervisory Board in respect of their performance of duties;
- increase and decrease the share capital;
- adopt resolutions on distribution of profit or coverage of loss;
- create and reverse capital reserves;
- determine the rules of remuneration of the Supervisory Board members;
- amend the Parent Company's Articles of Association;
- consider issues submitted to it by the Supervisory Board, Management Board or Shareholders;
- adopt resolutions on dissolution, liquidation or merger of the Parent Company;
- appoint liquidators;
- issue bonds convertible to shares and bonds with pre-emptive rights;
- issue subscription warrants;
- adopt the rules of Procedure for the Parent Company's Supervisory Board;
- determine the date on which the list of shareholders entitled to dividend for the financial year in question (the dividend record date) and the dividend payment date are established.

The Parent Company's shareholders exercise their rights in accordance with the generally applicable regulations and the Articles of Association of Medicalgorithmics S.A.

Any amendment to the Parent Company's Articles of Association requires a relevant resolution of the General Meeting adopted by a majority of three-fourths of the total vote, and an entry in the National Court Register of a constitutive nature. Amendments to the Articles of Association of Medicalgorithmics S.A. are made by the General Meeting in compliance with applicable laws and regulations, in the manner and form prescribed by the Commercial Companies Code.

VII. 5. Management Board of the Parent Company

The Management Board, chaired by the President of the Management Board, manages the Parent Company and represents it before third parties. Each member of the Management Board has the right to represent the Parent Company independently and without any limitations. The Management Board has the right to appoint commercial proxies. The Supervisory Board operates pursuant to generally applicable laws, and the Articles of Association of Medicalgorithmics S.A. All matters relating to the management of the Parent Company's affairs which are not reserved under the law or the Articles of Association for the General Meeting or the Supervisory Board, fall within the scope of powers and responsibilities of the Management Board. The power of the Management Board to make decisions to issue or buy back shares is limited by virtue of the Articles of Association. Pursuant to § 14(5) of the Articles of Association of Medicalgorithmics S.A., a resolution of the General Meeting is required to increase the share capital and issue shares. Unless stipulated otherwise in mandatory provisions of law, the Management Board decides on all matters connected with a share capital increase within the limits of the authorized share capital.

The Parent Company's Management Board is composed of 1–3 members appointed for a five-year term of office. The composition of the Management Board is determined by the Supervisory Board which appoints and dismisses its members.

As at the date of publication of this report, the Company's Management Board consisted of:

Marek Dziubiński	-	President of the Management Board

On 21 September 2018, Maksymilian Sztandera submitted his resignation from the position of the Company's Chief Financial Officer, effective as of the date of resignation.

VII. 6. Supervisory Board of the Parent Company

The Supervisory Board of Medicalgorithmics S.A. exercises ongoing supervision of the Parent Company's operations. The Supervisory Board operates pursuant to generally applicable laws, and the Articles of Association of Medicalgorithmics S.A. In accordance with the Articles of Association, the Supervisory Board consists of 5 to 9 members appointed and dismissed by the General Meeting in a manner specified in the Articles of Association. Supervisory Board members are appointed for a joint term of office of three years.

As at the date of publication of this report, the Company's Supervisory Board consisted of:

Michał Wnorowski	-	Chairman of the Supervisory Board
Grzegorz Grabowicz	-	Member of the Supervisory Board
Artur Małek	-	Member of the Supervisory Board
Marek Tatar	-	Member of the Supervisory Board
Krzysztof Urbanowicz	-	Member of the Supervisory Board

On 26 June 2018, the Annual General Meeting of Shareholders changed the composition of Medicalgorithmics S.A.'s Supervisory Board. The General Meeting dismissed all of the existing Supervisory Board Members, i.e. Mr Marek Tatar, Mr Marcin Hoffmann, Mr Jan Kunkowski, Mr Piotr Żółkiewicz and Mr Artur Małek. They were replaced by a new Supervisory Board composed of the aforementioned members.

VII. 7. Audit Committee of the Parent Company

Pursuant to the Parent Company's Articles of Association, members of the Audit Committee, including the Chairman, is appointed by the Supervisory Board from among the Supervisory Board members for the term of office of the Supervisory Board. The Audit Committee is composed of 3 members, including the Chairman, and acts as a collective body. Where permitted by generally applicable law, the Audit Committee's tasks are performed collectively by the Supervisory Board. The Audit Committee is responsible for the supervision of financial reporting in the Parent Company.

Composition of the Audit Committee

In the period from 1 January 2018 to 26 June 2018, the Audit Committee was composed of:

Marek Tatar	-	Chairman of the Audit Committee
Jan Kunkowski	-	Member of the Audit Committee
Piotr Żółkiewicz	-	Member of the Audit Committee

Piotr Żółkiewicz and Marek Tatar have skills and knowledge of accounting or auditing of financial statements. Piotr Żółkiewicz graduated from the Faculty of Management and held the following positions: Vice President of the Management Board, Chief Financial Officer at Medicalgorithmics S.A. (2012-2015), Finance and Strategy Adviser to the Management Boards at the Eko Park Group (2011-2013), Chief Financial and Operations Officer at Medicalgorithmics S.A. (2009-2012). Marek Tatar has completed a course for professional accountants (Tax Chamber in Kraków). He has been managing a company keeping full accounting records since 2009.

All Audit Committee members have the knowledge of and skills required in the industry in which the Parent Company operates. Marek Tatar has been a member of the Supervisory Board of the Parent Company since 2015. Before that, he provided legal advisory services to the Parent Company. Piotr Żółkiewicz was a Chief Financial and Operations Officer (in 2009–2012) and Vice President of the Management Board, Chief Financial Officer (2012–2015) at the Parent Company. During that period, he acquired the knowledge of and skills required in the industry in which the Parent Company operates. Jan Kunkowski has been a member of the Supervisory Board of the Parent Company since 2011.

Following the dismissal of the composition of the Supervisory Board by the Ordinary Shareholders Meeting of the Parent Company on 26 June 2018, the term of office of the then Audit Committee expired. On 27 July 2018, pursuant to § 20(11) of the Articles of Association of Medicalgorithmics S.A. and the provisions of new Act on Statutory Auditors, the Supervisory Board replaced it with a new Audit Committee, composed of the following members:

Grzegorz Grabowicz	-	Chairman of the Audit Committee
Michał Wnorowski	-	Member of the Audit Committee
Artur Małek	-	Member of the Audit Committee

The Audit Committee was composed of the above members in the period from 27 July to 31 December 2018.

All members of the Audit Committee meet the criteria of independence from the Company and other requirements specified in Article 129 of the Act of 11 May 2017 on statutory auditors, audit companies and public supervision (Journal of Laws of 2017, item 1089).

All current members of the Audit Committee have skills and knowledge of accounting or auditing of financial statements. Grzegorz Grabowicz graduated from the University of Łódź, Faculty of Management and Marketing, majoring in Accounting. He is a certified auditor and has experience in auditing financial statements acquired in an audit firm, Deloitte. Additionally, he was a member of the management and supervisory boards of companies in the financial sector. Artur Małek is a graduate of the Cracow University of Economics, the Faculty of Finance and Banking, as well as of a Postgraduate Program at the Cracow University of Economics' School of Entrepreneurship and Management, Faculty of Accounting and Finance. Artur Małek has experience in accounting confirmed by holding the functions of CFO, member of management and supervisory boards of companies listed on the Warsaw Stock Exchange. Michał Wnorowski is a graduate of the Warsaw School of Economics. His capital market career dates back to 1995. During 24 years of his professional career he worked for financial institutions managing clients' assets and served on supervisory boards and audit committees of listed and unlisted companies.

Artur Małek has the knowledge of and skills required in the industry in which the Parent Company operates. He has been a member of the Supervisory Board of the Parent Company since 2015. Additionally, Artur Małek has professional experience in the field of new technologies.

Assessment of independence of the audit firm auditing the Parent Company's financial statements

In 2018, the audit firm (CSWP) provided permitted non-audit services to the Parent Company, i.e. assurance services related to the calculation of the consolidated EBITDA ratio in connection with the terms and conditions of bonds issued by the Company in relation to quarterly financial data of the Parent Company. These services were provided on the terms and conditions specified in the contract for performance of agreed upon procedures concluded between the Parent Company and CSWP. The Committee assessed the independence of the audit firm and agreed to the provision of these services in its Resolution No 1 of 24 August 2018.

Pursuant to the Act of 11 May 2017 on Statutory Auditors, Audit Firms and Public Supervision, the Audit Committee adopted the following documents by way of Resolution No 1 of 20 October 2017:

- Policy for the provision of permitted non-audit services by an audit firm carrying out a statutory audit of the Parent Company's and the Capital Group's financial statements, by entities affiliated with that audit firm and by a member of the audit firm's network;
- Policy and procedure for appointing an audit firm to conduct statutory audit/review of the Parent Company's and the Capital Group's financial statements.

Key elements of the audit firm selection policy

Key elements of the audit firm selection policy are as follows:

- The audit firm is selected by the Company's Supervisory Board after considering the Audit Committee's recommendation;
- If the selection of an audit firm does not concern the extension of the audit agreement, the Audit Committee prepares and submits to the Supervisory Board a recommendation covering at least two audit firms selected within the procedure of collecting proposals organized by the company and indicates a reasonable preference with respect to one of them;
- The selection of the audit firm is made sufficiently in advance to allow the audit agreement to be signed or renewed in sufficient time to allow the audit firm to participate in the stock-taking of significant assets;
- When selecting an audit firm, the Audit Committee and the Supervisory Board of the Company pay particular attention to the need to maintain the independence of the audit firm and the statutory auditor, and take into account the experience of the audit firm in the statutory audit of financial statements of public-interest entities, including companies listed on the Warsaw Stock Exchange, and knowledge of the IT industry or new technologies;

- The selection of an audit firm is made taking into account the principles of rotation of the audit firm and the key statutory auditor under generally applicable law;
- The first audit agreement is concluded with the audit firm for a period of no less than two years with the option to extend it for further periods of at least two years, taking into account the principles of rotation of the audit firm and the statutory auditor.

Key elements of the policy for the provision of non-audit services by the audit firm conducting the audit

- The provision of non-audit services by an audit firm requires the approval of the Audit Committee by way of a resolution at the request of the Management Board of the Company;
- Non-audit services are provided by the auditor in accordance with the laws of general application and requirements of independence laid down for such services in the rules of professional ethics and standards governing the performance of such services, as appropriate.
- The auditor may provide permitted services to the Company or entities controlled by it only if it is justified by the interests of the Parent Company or entities controlled by it, in particular if the auditor, knowing the Company and its environment, can offer high-quality permitted services to the Company on competitive terms.

Recommendation concerning the selection of an auditing firm to perform the audit

By Resolution No 1 of 7 June 2018, the Audit Committee issued a recommendation on the selection of an audit firm, i.e. CSWP, to review the Company's financial statements and the Group's consolidated financial statements for the first half of 2018 and the first half of 2019, as well as to audit the Company's financial statements and the Group's consolidated financial statements for 2018 and 2019.

The recommendation complied with the applicable requirements. Due to the fact that the selection of the audit firm was related to the extension of the audit agreement, the recommendation was not prepared as a result of the selection procedure organized by the Company and meeting the applicable criteria.

Detailed rules of operation of the Audit Committee are regulated in the Regulations of the Audit Committee adopted by Resolution No 1 of the Supervisory Board of 20 October 2017.

Number of meetings held

The Audit Committee held 5 meetings in 2018

VIII. Basic information about the Parent Company

Medicalgorithmics S.A. is a joint-stock company registered in Poland, incorporated by a notarial deed registered in Repertory A No 1327/2005 of 23 June 2005. In 2011, the Parent Company's shares made their debut on the NewConnect market, an alternative system of trading outside a regulated market operated by the Warsaw Stock Exchange. Since 3 February 2014 the shares of Medicalgorithmics S.A. have been listed on the regulated market of the Warsaw Stock Exchange.

Registered office:	Aleje Jerozolimskie 81, 02-001 Warszawa
E-mail address:	finanse@medicalgorithmics.com
Website: Website for the Investor Relations:	www.medicalgorithmics.com www.medicalgorithmics.pl
Contact details for the media:	Piotr Owdziej (CC Group) tel.: +48 697 612 913 Piotr.Owdziej@ccgroup.pl

IX. Information about the operations of the Issuer

Registry data

The District Court for the Capital City of Warsaw in Warsaw, 12th Commercial Division of the National Court Register

KRS No 0000372848; Tax ID No (NIP) 5213361457; Statistical ID No (REGON): 140186973

Share capital

As at the date of this annual report, the share capital (registered with the National Court Register) amounts to PLN 361 thousand and comprises 3,606,526 ordinary bearer shares with a par value of PLN 0.10 per share, including:

- 1 747 200 Series A ordinary bearer shares
- 508 200 B series ordinary bearer shares
- 236 926 C series ordinary bearer shares
- 929 600 D series ordinary bearer shares
- 33 600 E series ordinary bearer shares
- 151 000 F series ordinary bearer shares

Marek Dziubiński
President of the Management Board

Warsaw 26 March 2019

X. Other representations and Information of the Parent Company's Management Board

To the best knowledge of the Management Board of the Parent Company, the annual consolidated financial statements of the Medicalgorithmics Capital Group for 2018 and the separate financial statements of Medicalgorithmics S.A. and the comparative data for 2017 were prepared in accordance with the applicable accounting policies and give a true, reliable and fair view of the Medicalgorithmics Capital Group's and Medicalgorithmics S.A.'s assets, financial position and performance, and that the Directors' Report on operations of the Medicalgorithmics Capital Group and Medicalgorithmics S.A. in 2018 gives a true picture of the Medicalgorithmics Capital Group's and Medicalgorithmics S.A.'s development, achievements and position, including a description of key risks and threats.

On behalf of the Management Board of Medicalgorithmics S.A.:

Marek Dziubiński
President of the Management Board

Warsaw, 26 March 2019

Based on the representation of the Supervisory Board of Medicalgorithmics S.A. on the selection of the audit firm to audit the financial statements of Medicalgorithmics S.A. for 2018 and the consolidated financial statements of Medicalgorithmics Capital Group for 2018 in accordance with the regulations, including regulations concerning the selection and procedure for the selection of the audit firm, the Management Board of the Parent Company hereby informs that:

- the audit firm and members of the audit team met the conditions required to issue an impartial and independent auditor's report on the financial statements of Medicalgorithmics S.A. for 2018 and an impartial and independent auditor's report on the consolidated financial statements of Medicalgorithmics Capital Group for 2018, in accordance with the applicable laws, professional standards and rules of professional ethics,
- Medicalgorithmics S.A. complies with the applicable laws governing the rotation of audit firms and lead auditors as well as with the mandatory cooling-off periods;
- Medicalgorithmics S.A. has in place a policy governing the selection of audit firms and a policy on the provision of additional non-audit services by audit firms, their related parties or members of their networks to Medicalgorithmics S.A., including services that are conditionally exempt from the prohibition on the provision of services by an audit firm.

On behalf of the Management Board of Medicalgorithmics S.A.:

Marek Dziubiński
President of the Management Board

Warsaw, 26 March 2019

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