

Appendix 4D

Cochlear Limited Half Yearly Report As at 31 December 2015

Results for announcement to the market

| | | Movement from 31 December 2014 | | \$A000 |
|---|-----------|-----------------------------------|-----------|----------------|
| Sales Revenue | up | 32% | to | 581,720 |
| Total Revenue | up | 27% | to | 558,088 |
| Earnings before interest and taxes (EBIT) | up | 30% | to | 130,967 |
| Net profit for the period attributable to members | up | 32% | to | 94,033 |
| Basic earnings per share (cents) | up | 31% | to | 164.7 |
| Dividend (cents) | up | 22% | to | 110.0 |
| | | | | |
| Net tangible assets per share at 31 December 2015 (cents) | up | 100% | to | 315.9 |
| Net tangible assets per share at 31 December 2014 (cents) | | | | 157.9 |

| Dividends | Amount per security | Franked amount per security | Conduit foreign income per security |
|---|------------------------|--------------------------------|--|
| Interim dividend per share (cents) | 110.0c | 110.0c | 0.0c |
| Previous corresponding period (cents) | 90.0c | 31.5c | 36.0c |
| | | | |
| Record date for determining entitlements to the dividend | 11 March 2016 | | |
| Dividend payment date | 1 April 2016 | | |
| No dividend reinvestment plans were in operation during or since the half-year. | | | |

Refer to the attached Directors' Report for an explanation of the above movements.

Cochlear Limited and its controlled entities

ACN 002 618 073

Interim Financial Report

31 December 2015

Cochlear Limited and its controlled entities
Directors' Report
For the half year ended 31 December 2015

The directors present their report, together with the consolidated interim financial report for Cochlear Limited (the Company) and its controlled entities for the half year ended 31 December 2015 and the auditors' review report thereon.

Directors

The directors of the Company during or since the end of the interim period are:

| Name | Period of directorship |
|---|--|
| <i>Non-executive directors</i> | |
| Mr Rick Holliday-Smith, <i>Chairman</i> | Director since March 2005 |
| Mrs Yasmin Allen | Director since August 2010 |
| Mr Glen Boreham, AM | Director since January 2015 |
| Professor Edward Byrne, AC | Director since July 2002 |
| Ms Alison Deans | Director since January 2015 |
| Mr Andrew Denver | Director since February 2007 |
| Mr Donal O'Dwyer | Director since August 2005 |
| <i>Executive director</i> | |
| Dr Chris Roberts, <i>CEO/President</i> | Director from February 2004 to August 2015 |
| Mr Chris Smith, <i>CEO/President</i> | Director since September 2015 |

Principal activities and review of operations and results

Other than as discussed in this report, there were no significant changes in the nature of operating activities during the half year ended 31 December 2015 and the results of those operations are set out below.

Review of operations

The following provides a summary of Cochlear's performance for the half year ended 31 December 2015.

| | 31 Dec 2015 | 31 Dec 2014 |
|---|----------------|----------------|
| | \$000 | \$000 |
| Total Revenue | 558,088 | 438,346 |
| Sales revenue | 581,720 | 440,481 |
| Earnings before interest and tax (EBIT) | 130,967 | 100,458 |
| Profit attributable to members | 94,033 | 71,375 |
| Basic earnings per share (cents) | 164.7 | 125.3 |
| Diluted earnings per share (cents) | 164.4 | 124.9 |
| Interim dividend per share (cents) | 110.0 | 90.0 |

Product highlights

| | 31 Dec 2015 | 31 Dec 2014 | % Change | Constant Currency |
|---|----------------|----------------|--------------|-------------------|
| | \$000 | \$000 | | |
| Cochlear implants (units) | 14,748 | 11,689 | ↑ 26% | |
| <i>Sales revenue</i> | | | | |
| Cochlear implants | 362,709 | 271,224 | ↑ 34% | ↑ 17% |
| Services (sound processor upgrades and accessories) | 146,298 | 111,781 | ↑ 31% | ↑ 16% |
| Bone conduction and acoustic implants | 72,713 | 57,476 | ↑ 26% | ↑ 9% |
| Total Sales revenue | 581,720 | 440,481 | ↑ 32% | ↑ 16% |

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Cochlear implants – 62% of sales revenue

Cochlear implant unit sales grew 26% (12% excluding the benefit of ~1,700 China tender units) driven by both market growth and modest improvements in share in some markets.

There has been a strong uptake of the Nucleus® Profile implants since release in FY15.

The results also reflect earlier investments in sales and marketing capabilities including direct-to-consumer activities and field expansion in markets including the United States (US) and Germany. These initiatives help build awareness of implantable hearing solutions and support further penetration into the adult segment.

Services (sound processor upgrades and accessories) – 25% of sales revenue

Services sales revenue increased 31% (16% in constant currency) driven by the continuing strong uptake of the Nucleus 6 Sound Processor.

With the launch of the Nucleus 6 for Nucleus 22 recipients this half, the latest sound processor is now compatible with all generations of implants.

Continued strong uptake of the Nucleus 6 is expected over the next few years with the current penetration rate still below 20%.

Accessories growth was supported by True Wireless™ and the Aqua+ for Nucleus 6 users.

As part of the commitment to provide recipients with great customer service and support, the business commenced the rollout of its membership programme, Cochlear Family and personalised online portal, MyCochlear.com, which connects recipients directly with Cochlear.

Bone conduction and acoustic implants – 13% of sales revenue

Bone conduction and acoustic implant sales revenue grew 26% (9% in constant currency) with solid performance across all regions.

The Baha® 5 System, which was launched in FY15 and includes the sound processor and smart app made for iPhone, continued its rollout during the first half.

The Baha 5 SuperPower, the latest and most powerful product on the market, was launched in selected markets in Europe in December 2015. It will be launched into other markets over the next 18 months as regulatory approvals are obtained.

Regional review

| Sales revenue | 31 Dec 2015 | 31 Dec 2014 | % Change | Constant |
|---------------------------------------|----------------|----------------|--------------|--------------|
| | \$000 | \$000 | | Currency |
| Americas | 264,081 | 195,292 | ↑ 35% | ↑ 11% |
| EMEA (Europe, Middle East and Africa) | 210,420 | 181,599 | ↑ 16% | ↑ 18% |
| Asia Pacific | 107,219 | 63,590 | ↑ 69% | ↑ 55% |
| Total Sales revenue | 581,720 | 440,481 | ↑ 32% | ↑ 16% |

Americas (US, Canada and Latin America) – 46% of sales revenue

Sales revenue increased 35% to \$264.1 million (11% in constant currency).

The highlight was the growth in the US with cochlear implant unit sales up ~10% driven by both market growth and modest share gains. Growth overall has been driven by new product capabilities such as Nucleus 6 True Wireless compatibility as well as strategic growth initiatives commenced over the past few years.

The expanded field sales organisation, direct-to-consumer marketing and new customer relationship management system (Salesforce.com) has supported accelerated market growth.

Cochlear Limited and its controlled entities
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Services revenue increased by over 20% in constant currency driven by upgrades to the Nucleus 6 Sound Processor. The uptake by Nucleus 22 recipients has been enthusiastic since launch in November 2015.

Services revenue in the US is biased to the first half reflecting the seasonal impact of the annual US reimbursement cycle.

Overall Latin American sales revenue declined as a result of deteriorating conditions in Brazil. Excluding Brazil, Latin American sales revenue increased by 25% in constant currency.

EMEA (Europe, Middle East and Africa) – 36% of sales revenue

Sales revenue increased 16% to \$210.4 million (up 8% in constant currency) with solid performances across Western Europe, particularly Germany, while sales in Eastern Europe declined.

The highlight was the performance of the German business which grew units by over 10% driven by market growth and improvements in share. Germany is seeing some positive results from growth initiatives including candidate recruitment programmes, field sales expansion and broadening of cochlear implant indications.

Sales revenue in the Middle East grew strongly. While coming off a lower sales base in HY15, the Middle East is benefitting from Cochlear's expanded presence since the opening of a new office in Dubai.

Asia Pacific (Australasia and Asia) – 18% of sales revenue

Sales revenue increased 69% to \$107.2 million (up 55% in constant currency).

Australasian sales revenue increased by 12%, benefiting from field sales expansion, investment in training and clinical tools as well as new marketing programmes.

The Melbourne Cochlear Care Clinic, which was opened in FY15, manages the after care of recipients. It has continued to deliver high levels of service to recipients as well as driving incremental Services revenue. The success of this clinic model is being expanded to other markets.

China performed strongly in both the private pay and tender markets. The region benefitted from a Chinese Central Government tender of around 1,700 units, with no tender sale units in the first half of FY15. A further ~300 units associated with the tender will be delivered in the second half of FY16.

In December 2015, Cochlear was awarded a further 2,100 tender units with the majority of sales expected to be delivered in the first half of FY17.

Financial review

Profit and loss

| | 31 Dec 2015 | 31 Dec 2014 | Change |
|------------------------------|-------------|-------------|---------|
| | \$000 | \$000 | \$000 |
| Costs of goods sold | 171,278 | 127,369 | 43,909 |
| <i>% of sales revenue</i> | 29.4% | 28.9% | |
| Research and development | 70,193 | 61,360 | 8,833 |
| Selling and general expenses | 158,870 | 122,686 | 36,184 |
| Administration expenses | 34,717 | 28,559 | 6,158 |
| Other income | (7,937) | (2,086) | (5,851) |
| EBIT | 130,967 | 100,458 | 30,509 |
| <i>% of total revenue</i> | 23.5% | 22.9% | |

EBIT increased by \$30.5 million to \$131.0 million, with the operating margin (EBIT to total revenue) increasing by 0.6% to 23.5%.

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Directors' Report
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Cost of goods sold (COGS) increased \$44.0 million to \$171.3 million, primarily as a result of growing volumes. COGS as a percentage of sales revenue increased by 0.5% to 29.4% reflecting product and geographic mix as well as the higher COGS associated with the initial introduction of the Nucleus Profile series implant, offset by changes in FX. An inventory write-down of \$5.1 million was booked during the first half with the majority related to older generation sound processors and components.

Investment in research and development (R&D) increased \$8.8 million to \$70.2 million which is consistent with Cochlear's stated commitment to continue to invest in research and development to strengthen its technology leadership position and follows several years of limited incremental investment in R&D.

Selling and general expenses increased by \$36.2 million to \$158.8 million. The 30% increase reflects the increased investment in market growth initiatives as well as the impact on translation of the depreciation of the Australian dollar. In constant currency, the increase in selling and general expenses was 15%.

Corporate administration increased by \$6.1 million to \$34.7 million driven by investments in processes and systems.

Other income increased by \$5.8 million. A \$5.2 million increase in FX gains on asset translation is included in this line item.

Foreign currency impacts on income statement

| Income statement impacts | \$000 |
|---|----------------------|
| Sales revenue and expenses (translation impact) ¹ | |
| - Sales revenue | 62,589 |
| - Total expenses including tax | (30,054) |
| | <u>32,535</u> |
| FX contract gains/(losses) on hedged sales (transaction impact) | |
| - FX losses – HY15 | (2,135) |
| - FX losses – HY16 | (23,632) |
| | <u>(21,497)</u> |
| Asset translation (translation impact) | |
| - FX gain on asset translation – HY15 | 578 |
| - FX gain on asset translation – HY16 | 5,836 |
| | <u>5,258</u> |
| Total benefit to net profit from changing FX rates | <u>16,296</u> |

1. HY16 actual v HY16 at HY15 rates.

Cochlear derives over 90% of revenue in foreign currencies with around 50% of costs denominated in foreign currency. As most of the cash is repatriated to Australia to fund operating and investing activities including R&D and dividends, expected cash flows are hedged back to Australian dollars to provide some certainty around near term cash flow.

The Australian dollar (AUD) depreciated against most of the major currencies during the half which provided an overall benefit of \$16.3 million to net profit for HY16. The key impacts include:

- A net benefit to sales revenue of \$62.6 million from translating foreign sales into AUD; and
- FX contract losses were \$23.6 million for HY16 compared with a loss of \$2.2 million in HY15. This is consistent with Cochlear's long-term hedging policy.

Cochlear Limited and its controlled entities
Directors' Report
For the half year ended 31 December 2015

Capital employed

| | 31 Dec 2015 | 30 June 2015 | Change |
|--------------------------------|----------------|----------------|---------------|
| | \$000 | \$000 | \$000 |
| Trade receivables | 258,420 | 236,728 | 21,692 |
| Inventories | 150,784 | 145,861 | 4,923 |
| Less: Trade and other payables | (107,295) | (99,858) | (7,437) |
| Working capital | 301,909 | 282,731 | 19,178 |
| <i>Debtor days</i> | 81 | 83 | (2) |
| <i>Inventory days</i> | 161 | 193 | (32) |
| Property, plant and equipment | 80,533 | 80,809 | (276) |
| Intangible assets | 234,725 | 228,531 | 6,194 |
| Other net liabilities | (68,960) | (96,182) | 27,222 |
| Capital employed | 548,207 | 495,889 | 52,318 |

Capital employed increased by \$52.3 million to \$548.2 million since 30 June 2015 primarily as a result of an increase in working capital and a reduction in other net liabilities.

Working capital increased by \$19.2 million to \$301.9 million as a result of strong sales growth.

Trade receivables increased \$21.7 million to \$258.4 million. In constant currency, trade receivables increased by 6%. Debtors days declined two days to 81 days reflecting the strong sales during the half.

Inventories increased \$4.9 million to \$150.8 million. Inventory days reduced 32 days to 161 days reflecting the reduction in stock which had been built up in June 2015 ahead of tender shipments made during the half and the higher sales.

Property, plant and equipment remained largely unchanged.

Intangible assets increased by \$6.2 million to \$234.7 million as a result of revaluation to period end FX rates. All intangible assets are tested for impairment on an annual basis. There were no impairments or write-downs of intangible assets in HY16.

The provision for patent dispute has remained unchanged at \$21.3 million since 30 June 2015. Other net liabilities reduced by \$27.2 million largely reflecting higher tax payments made during the half.

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Directors' Report
For the half year ended 31 December 2015

Cash flow

| | 31 Dec 2015 | 31 Dec 2014 | Change |
|--------------------------------------|---------------|---------------|-----------------|
| | \$000 | \$000 | \$000 |
| EBIT | 130,967 | 100,458 | 30,509 |
| Depreciation and amortisation | 16,328 | 14,273 | 2,055 |
| Changes in working capital and other | (19,261) | 1,522 | (20,783) |
| Net finance costs | (6,375) | (5,436) | (939) |
| Taxation paid | (48,119) | (20,875) | (27,244) |
| Operating cash flow | 73,540 | 89,942 | (16,402) |
| Capital expenditure | (13,427) | (7,768) | (5,659) |
| Other | (3,334) | (2,683) | (651) |
| Free cash flow | 56,779 | 79,491 | (22,712) |

Free cash flow decreased by \$22.6 million to \$56.8 million. An increase in EBIT of \$30.5 million was offset by a net investment in working capital to fund business growth and an increase in taxation paid.

The \$27.2 million increase in taxation paid was driven by improved profitability and changes to the timing of Australian tax payments. The effective tax rate has remained at approximately 25%.

Net debt

| | 31 Dec 2015 | 30 June 2015 | Change |
|-----------------------------------|----------------|----------------|----------------|
| | \$000 | \$000 | \$000 |
| Loans and borrowings: | | | |
| Current | 168,426 | 168,159 | 267 |
| Non-current | 44,687 | 44,552 | 135 |
| Total debt | 213,113 | 212,711 | 402 |
| Cash | (80,251) | (72,208) | (8,043) |
| Net debt | 132,862 | 140,503 | (7,641) |
| Total loan facilities | 350,000 | 350,000 | |
| Unused portion of debt facilities | 135,000 | 135,000 | |

Net debt reduced by \$7.6 million to \$132.9 million since 30 June 2015. At 31 December 2015, there was \$350.0 million in total loan facilities and the unused portion of the bank facility was \$135.0 million.

Dividends

| | 31 Dec 2015 | 31 Dec 2014 | % Change |
|------------------------------------|-------------|-------------|----------|
| Interim ordinary dividends (cents) | 110.0c | 90.0c | 22% |
| Payout ratio % | 67% | 72% | |
| Franking % | 100% | 35% | |
| Conduit foreign income % | 0% | 40% | |

Strong free cash flow generation and the continued strength of the balance sheet has supported the payment of an interim dividend of 110.0 cents per share, franked at 100%, representing a payout of 67% of net profit.

The Record date for determining dividend entitlements is 11 March 2016 and the interim dividend will be paid on 1 April 2016.

Cochlear Limited and its controlled entities

Directors' Report

For the half year ended 31 December 2015

2016 Financial outlook

For FY16, net profit expectations have been adjusted up to a range of \$180-190 million with the increase in guidance driven primarily by FX. This guidance range would deliver net profit growth in a range of 23-30% on last year.

Cochlear has made steady progress in the first half. It has continued to invest in technology and market expansion activities that underpin the long-term growth of the company.

Cochlear believes the strong market acceptance of recently launched products, including Nucleus Profile implants, the Nucleus 6 Sound Processor with True Wireless and for Nucleus 22 implant recipients, have driven market growth across many countries over the past 12 months.

Looking forward, Cochlear has an exciting pipeline of products to be released over the next 18 months across all categories of its business.

As previously advised, there are a number of factors that will impact second half earnings:

- Services sales revenue is expected to be weighted to the first half given the seasonality of US upgrade sales;
- The China tender of ~2,000 units is around the same level for the full year as FY15. ~1,700 units were booked in HY16 with ~300 units forecast in the second half;
- Ongoing investments in technology and market expansion activities will be weighted to the second half; and finally
- A weighted average United States dollars (USD)/ AUD FX rate of approximately 72c is now forecast for the full year (previously 75c).

The balance sheet position and free cash flow generation remain strong. The business will continue to target a dividend payout ratio of around 70% of net profit.

Non-IFRS financial measures

Given the significance of the FX movements the directors believe the presentation of non-IFRS financial measures is useful for the users of this document as they reflect the underlying financial performance of the business.

The non-IFRS financial measures included in this document have been calculated on the following basis:

- Constant currency: restatement of IFRS financial measures in comparative years using F16 FX rates.

These non-IFRS financial measures have not been subject to review or audit. However, KPMG have separately undertaken a set of procedures to agree the non-IFRS financial measures disclosed to the books and records of the consolidated entity.

Dividends

Dividends paid or declared by the Company since the end of the previous financial year are:

\$000

In respect of the previous year:

A final ordinary dividend of 100.0 cents per share, franked to 100% with Class C (100%)
franking credits, in respect of the year ended 30 June 2015, paid on 1 October 2015. 57,168

The interim dividend in respect of the current financial year has not been provided for in this financial report as it was not declared until after 31 December 2015. Since the end of the financial half-year, the directors declared an interim dividend of 110.0 cents 100% franked amounting to a total of \$62.9m.

**Cochlear Limited and its controlled entities
Directors' Report
For the half year ended 31 December 2015**

Lead Auditor's Independence Declaration under Section 307C of the Corporations Act

The lead auditor's independence declaration is set out on page 11 and forms part of the Directors' Report for the half year ended 31 December 2015.

Rounding off

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July, 1998, and in accordance with the Class Order, amounts in the Financial Report and Directors' Report have been rounded off to the nearest one thousand dollars, unless otherwise stated.

Dated at Sydney this 11th day of February 2016.

Signed in accordance with a resolution of the directors:



Director



Director



Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To: the directors of Cochlear Limited

I declare that, to the best of my knowledge and belief, in relation to the review for the financial half year ended 31 December 2015 there have been:

- (i) no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the review; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the review.

KPMG

KPMG

Cameron Slapp, Partner

Sydney, 11 February 2016

Cochlear Limited and its controlled entities
Interim Income Statement
For the half year ended 31 December 2015

| | Note | 31 Dec 2015 \$000 | 31 Dec 2014 \$000 |
|--|------|----------------------|----------------------|
| Revenue | 2.2 | 558,088 | 438,346 |
| Cost of sales | 2.3 | (171,278) | (127,369) |
| Gross profit | | 386,810 | 310,977 |
| Selling and general expenses | | (158,870) | (122,686) |
| Administration expenses | | (34,717) | (28,559) |
| Research and development expenses | | (70,193) | (61,360) |
| Other income | 2.4 | 7,937 | 2,086 |
| Results from operating activities | | 130,967 | 100,458 |
| Finance income - interest | | 130 | 90 |
| Finance expense - interest | | (4,814) | (5,542) |
| Net finance expense | | (4,684) | (5,452) |
| Profit before income tax | | 126,283 | 95,006 |
| Income tax expense | 3 | (32,250) | (23,631) |
| Net profit | | 94,033 | 71,375 |
| Basic earnings per share (cents) | 2.5 | 164.7 | 125.3 |
| Diluted earnings per share (cents) | 2.5 | 164.4 | 124.9 |

The notes on pages 17 to 23 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities
Interim Statement of Comprehensive Income
For the half year ended 31 December 2015

| | 31 Dec 2015 | 31 Dec 2014 |
|--|----------------|-----------------|
| | \$000 | \$000 |
| Net profit | 94,033 | 71,375 |
| <i>Other comprehensive income</i> | | |
| Items that may be reclassified subsequently to profit or loss: | | |
| Foreign currency translation differences | 8,192 | 12,556 |
| Effective portion of changes in fair value of cash flow hedges, net of tax | (12,660) | (25,527) |
| Net change in fair value of cash flow hedges transferred to the income statement, net of tax | 16,542 | 1,494 |
| Total items that may be reclassified to profit or loss | 12,074 | (11,477) |
| Other comprehensive income / (loss) for the period, net of tax | 12,074 | (11,477) |
| Total comprehensive income for the period | 106,107 | 59,898 |

The notes on pages 17 to 23 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities
Interim Balance Sheet
For the half year ended 31 December 2015

| | Note | 31 Dec 2015 | 30 Jun 2015 |
|--------------------------------------|------|----------------|----------------|
| | | \$000 | \$000 |
| Assets | | | |
| Cash and cash equivalents | | 80,251 | 72,208 |
| Trade and other receivables | | 271,733 | 249,744 |
| Forward exchange contracts | | 2,276 | 3,853 |
| Inventories | | 150,784 | 145,861 |
| Current tax assets | | 5,182 | 3,606 |
| Prepayments | | 15,758 | 13,754 |
| Total current assets | | 525,984 | 489,026 |
| Other receivables | | 2,728 | 63 |
| Forward exchange contracts | | 1,610 | 1,910 |
| Property, plant and equipment | | 80,533 | 80,809 |
| Intangible assets | | 234,725 | 228,531 |
| Deferred tax assets | | 78,557 | 68,717 |
| Total non-current assets | | 398,153 | 380,030 |
| Total assets | | 924,137 | 869,056 |
| Liabilities | | | |
| Trade and other payables | | 107,295 | 99,858 |
| Foreign exchange contracts | | 18,851 | 24,162 |
| Loans and borrowings | 5.1 | 168,426 | 168,159 |
| Current tax liabilities | | 14,459 | 20,645 |
| Employee benefit liabilities | | 37,177 | 43,223 |
| Provisions | | 30,649 | 26,652 |
| Deferred revenue | | 23,102 | 20,585 |
| Total current liabilities | | 399,959 | 403,284 |
| Foreign exchange contracts | | 8,848 | 10,961 |
| Loans and borrowings | 5.1 | 44,687 | 44,552 |
| Employee benefit liabilities | | 11,949 | 11,479 |
| Provisions | 4.1 | 43,349 | 43,394 |
| Total non-current liabilities | | 108,833 | 110,386 |
| Total liabilities | | 508,792 | 513,670 |
| Net assets | | 415,345 | 355,386 |
| Equity | | | |
| Share capital | | 157,180 | 144,136 |
| Reserves | | (16,151) | (26,201) |
| Retained earnings | | 274,316 | 237,451 |
| Total equity | | 415,345 | 355,386 |

The notes on pages 17 to 23 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities
Interim Statement of Changes in Equity
For the half year ended 31 December 2015

| Amounts \$000 | Issued capital | Treasury reserve | Translation reserve | Hedging reserve | Share based payment reserve | Retained earnings | Total equity |
|--|----------------|------------------|---------------------|-----------------|-----------------------------|-------------------|-----------------|
| Balance at 1 July 2014 | 152,599 | (8,463) | (52,630) | 476 | 19,963 | 217,260 | 329,205 |
| <i>Total comprehensive income</i> | | | | | | | |
| Net profit | - | - | - | - | - | 71,375 | 71,375 |
| <i>Other comprehensive income</i> | | | | | | | |
| Foreign currency translation differences | - | - | 12,556 | - | - | - | 12,556 |
| Effective portion of changes in fair value of cash flow hedges, net of tax | - | - | - | (25,527) | - | - | (25,527) |
| Net change in fair value of cash flow hedges transferred to the income statement, net of tax | - | - | - | 1,494 | - | - | 1,494 |
| Total other comprehensive income / (loss) | - | - | 12,556 | (24,033) | - | - | (11,477) |
| Total comprehensive income / (loss) | - | - | 12,556 | (24,033) | - | 71,375 | 59,898 |
| Transactions with owners, recorded directly in equity | | | | | | | |
| Share based payment transactions | - | - | - | - | 4,457 | - | 4,457 |
| Deferred tax recognised in equity | - | - | - | - | 355 | - | 355 |
| Dividends to shareholders | - | - | - | - | - | (72,469) | (72,469) |
| Balance at 31 December 2014 | 152,599 | (8,463) | (40,074) | (23,557) | 24,775 | 216,166 | 321,446 |
| Balance at 1 July 2015 | 152,599 | (8,463) | (32,541) | (20,547) | 26,887 | 237,451 | 355,386 |
| <i>Total comprehensive income</i> | | | | | | | |
| Net profit | - | - | - | - | - | 94,033 | 94,033 |
| <i>Other comprehensive income</i> | | | | | | | |
| Foreign currency translation differences | - | - | 8,192 | - | - | - | 8,192 |
| Effective portion of changes in fair value of cash flow hedges, net of tax | - | - | - | (12,660) | - | - | (12,660) |
| Net change in fair value of cash flow hedges transferred to the income statement, net of tax | - | - | - | 16,542 | - | - | 16,542 |
| Total other comprehensive income | - | - | 8,192 | 3,882 | - | - | 12,074 |
| Total comprehensive income | - | - | 8,192 | 3,882 | - | 94,033 | 106,107 |
| Transactions with owners, recorded directly in equity | | | | | | | |
| Performance shares vested | - | 2,068 | - | - | (2,068) | - | - |
| Share options exercised | 5,435 | 5,541 | - | - | (3,438) | - | 7,538 |
| Share based payment transactions | - | - | - | - | 5,059 | - | 5,059 |
| Deferred tax recognised in equity | - | - | - | - | (1,577) | - | (1,577) |
| Dividends to shareholders | - | - | - | - | - | (57,168) | (57,168) |
| Balance at 31 December 2015 | 158,034 | (854) | (24,349) | (16,665) | 24,863 | 274,316 | 415,345 |

The notes on pages 17 to 23 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities
Interim Statement of Cash Flows
For the half year ended 31 December 2015

| | 31 Dec 2015 | 31 Dec 2014 |
|--|-----------------|-----------------|
| | \$000 | \$000 |
| <i>Cash flows from operating activities</i> | | |
| Cash receipts from customers | 544,572 | 440,141 |
| Cash paid to suppliers and employees | (418,752) | (325,495) |
| Grant and other income received | 2,101 | 1,508 |
| Interest received | 113 | 99 |
| Interest paid | (6,375) | (5,436) |
| Income taxes paid | (48,119) | (20,875) |
| Net cash from operating activities | 73,540 | 89,942 |
| <i>Cash flows from investing activities</i> | | |
| Acquisition of property, plant and equipment | (13,427) | (7,768) |
| Acquisition of enterprise resource planning system | (3,334) | (2,683) |
| Net cash used in investing activities | (16,761) | (10,451) |
| <i>Cash flows from financing activities</i> | | |
| Repayment of borrowings | (57,110) | (79,382) |
| Proceeds from borrowings | 57,110 | 72,382 |
| Proceeds from exercise of share options, net | 7,538 | - |
| Dividends paid | (57,168) | (72,469) |
| Net cash used in financing activities | (49,630) | (79,469) |
| Net increase in cash and cash equivalents | 7,149 | 22 |
| Cash and cash equivalents at 1 July | 72,208 | 56,127 |
| Effect of exchange rate fluctuation on cash held | 894 | 2,722 |
| Cash and cash equivalents at 31 December | 80,251 | 58,871 |

The notes on pages 17 to 23 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities

Notes to the Interim Financial Statements

For the half year ended 31 December 2015

1 Basis of preparation

1.1 Reporting entity

Cochlear Limited (the Company) is a company domiciled in Australia. The Consolidated Interim Financial Report of the Company as at and for the half year ended 31 December 2015 comprises the Company and its subsidiaries (together referred to as Cochlear or the Consolidated Entity). Cochlear's Consolidated Annual Financial Report as at and for the year ended 30 June 2015 is available upon request from the Company's registered office at 1 University Avenue, Macquarie University NSW 2109, Australia or at www.cochlear.com.

1.2. Statement of compliance

The Consolidated Interim Financial Report is a general purpose financial report which has been prepared in accordance with AASB134 *Interim Financial Reporting* and the *Corporations Act 2001*, and with IAS 34 *Interim Financial Reporting*.

The Consolidated Interim Financial Report does not include all of the information required for a full annual financial report, and should be read in conjunction with Cochlear's Consolidated Annual Financial Report as at and for the year ended 30 June 2015. This report should also be read in conjunction with any public announcements made by Cochlear Limited during the half year ended 31 December 2015 in accordance with continuous disclosure obligations arising under the *Corporations Act 2001*.

The Consolidated Interim Financial Report was approved by the Board of Directors on 11 February 2016.

The Consolidated Entity is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with the Class Order, amounts in the Consolidated Interim Financial Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

1.3 Significant accounting policies

The accounting policies applied by the Consolidated Entity in this Consolidated Interim Financial Report are the same as those applied by the Consolidated Entity in the Consolidated Annual Financial Report as at and for the year ended 30 June 2015.

1.4 Estimates

The preparation of the Consolidated Interim Financial Report requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

In preparing this Consolidated Interim Financial Report, the significant judgments made by management in applying Cochlear's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the Consolidated Annual Financial Report as at and for the year ended 30 June 2015.

Cochlear Limited and its controlled entities
Notes to the Interim Financial Statements
For the half year ended 31 December 2015

2. Performance for the half year

2.1 Operating segments

| | Americas | | EMEA ⁽ⁱ⁾ | | Asia Pacific | | Total | |
|----------------------------|----------|---------|---------------------|---------|--------------|--------|----------------|----------------|
| | 2015 | 2014 | 2015 | 2014 | 2015 | 2014 | 2015 | 2014 |
| | \$000 | \$000 | \$000 | \$000 | \$000 | \$000 | \$000 | \$000 |
| Reportable segment revenue | 264,081 | 195,292 | 210,420 | 181,599 | 107,219 | 63,590 | 581,720 | 440,481 |
| Reportable segment EBIT | 143,449 | 100,002 | 86,441 | 84,910 | 34,270 | 15,535 | 264,160 | 200,447 |

(i) Europe, Middle East and Africa

Reconciliations of reportable segment revenues and profit or loss

| Revenues | Cochlear implants | Services | Total Cochlear implants | Bone conduction and acoustic implants | Reportable segment revenue | Foreign exchange losses on hedged sales | Consolidated revenue |
|-------------|-------------------|----------|-------------------------|---------------------------------------|----------------------------|---|----------------------|
| | \$000 | \$000 | \$000 | \$000 | \$000 | \$000 | \$000 |
| 31 Dec 2015 | 362,709 | 146,298 | 509,007 | 72,713 | 581,720 | (23,632) | 558,088 |
| 31 Dec 2014 | 271,224 | 111,781 | 383,005 | 57,476 | 440,481 | (2,135) | 438,346 |

| Profit or loss | Reportable segment EBIT | Corporate and other net expenses | Foreign exchange losses on hedged sales | Net finance expense | Consolidated profit before income tax |
|----------------|-------------------------|----------------------------------|---|---------------------|---------------------------------------|
| | \$000 | \$000 | \$000 | \$000 | \$000 |
| 31 Dec 2015 | 264,160 | (109,561) | (23,632) | (4,684) | 126,283 |
| 31 Dec 2014 | 200,447 | (97,854) | (2,135) | (5,452) | 95,006 |

2.2 Revenue

| | 31 Dec 2015 | 31 Dec 2014 |
|---|----------------|----------------|
| | \$000 | \$000 |
| Sale of goods revenue before hedging | 574,795 | 435,710 |
| Foreign exchange losses on hedged sales | (23,632) | (2,135) |
| Revenue from the sale of goods | 551,163 | 433,575 |
| Rendering of services revenue | 6,925 | 4,771 |
| Total revenue | 558,088 | 438,346 |

2.3 Expenses

| | 31 Dec 2015 | 31 Dec 2014 |
|---|----------------|----------------|
| | \$000 | \$000 |
| (a) Cost of sales | | |
| Carrying amount of inventories recognised as an expense | 161,579 | 120,679 |
| Write-down in value of inventories | 5,120 | 2,321 |
| Other | 4,579 | 4,369 |
| Total cost of sales | 171,278 | 127,369 |

Cochlear Limited and its controlled entities
Notes to the Interim Financial Statements
For the half year ended 31 December 2015

2.4 Other income

| | 31 Dec 2015 | 31 Dec 2014 |
|--------------------------------------|--------------|--------------|
| | \$000 | \$000 |
| Grant received or due and receivable | 523 | 905 |
| Net foreign exchange gain | 5,836 | 578 |
| Other | 1,578 | 603 |
| Total other income | 7,937 | 2,086 |

2.5 Earnings per share

Basic earnings per share

The calculation of basic EPS has been based on the following net profit attributable to equity holders of the parent entity and weighted average number of ordinary shares of the Company:

| | 31 Dec 2015 | 31 Dec 2014 |
|--|-------------------|-------------------|
| Net profit attributable to equity holders of the parent entity | \$94,033,000 | \$71,375,000 |
| <i>Weighted average number of ordinary shares (basic):</i> | | |
| Issued ordinary shares at 1 July (number) | 56,957,274 | 56,937,519 |
| Effect of options and performance shares exercised (number) | 133,123 | - |
| Effect of shares issued under Employee Share Plan (number) | 7,270 | 7,730 |
| Weighted average number of ordinary shares (basic) | 57,097,667 | 56,945,249 |
| Basic earnings per share (cents) | 164.7 | 125.3 |

Diluted earnings per share

The calculation of diluted EPS has been based on the following net profit attributable to equity holders of the parent entity and weighted average number of shares outstanding after adjustments for the effects of all dilutive potential ordinary shares:

| | 31 Dec 2015 | 31 Dec 2014 |
|--|-------------------|-------------------|
| Net profit attributable to equity holders of the parent entity | \$94,033,000 | \$71,375,000 |
| <i>Weighted average number of ordinary shares (diluted):</i> | | |
| Weighted average number of shares (basic) (number) | 57,097,667 | 56,945,249 |
| Effect of options, performance shares and rights unvested (number) | 84,978 | 204,879 |
| Weighted average number of ordinary shares (diluted) | 57,182,645 | 57,150,128 |
| Diluted earnings per share (cents) | 164.4 | 124.9 |

Cochlear Limited and its controlled entities
Notes to the Interim Financial Statements
For the half year ended 31 December 2015

2.6 Options and performance rights

The Company has granted options and performance rights to certain employees and key management personnel under the Cochlear Executive Incentive Plan (CEIP). The terms and conditions of the plan are disclosed in the Consolidated Annual Financial Report as at and for the year ended 30 June 2015.

Grants made in the current period to certain employee and key management personnel under the CEIP made are set out below.

| Grant date | Exercise price per option | Number of options | Number of performance rights | Contractual life |
|----------------------------|---------------------------|-------------------|------------------------------|------------------|
| August 2015 ¹ | N/A | N/A | 53,384 | 2 years |
| November 2015 ² | \$82.89 | 162,451 | 19,958 | 4 years |

1. Performance rights offered under deferred short-term incentives.

2. Options and performance shares/rights offered under long-term incentives.

2.7 Dividends

Dividends recognised in the current and prior financial period by Cochlear Limited are:

| | Cents per share | Total amount \$'000 | Franked/unfranked | Date of payment |
|-------------------------|-----------------|---------------------|-------------------|-------------------|
| 31 December 2015 | | | | |
| Final – ordinary | 100.0 | 57,168 | 100% Franked | 1 October 2015 |
| 31 December 2014 | | | | |
| Final – ordinary | 127.0 | 72,469 | 20% Franked | 25 September 2014 |

Subsequent event

Since the end of the reporting period, the directors declared the following dividend:

| | | | | |
|--------------------|-------|--------|--------------|--------------|
| Interim – ordinary | 110.0 | 62,903 | 100% Franked | 1 April 2016 |
|--------------------|-------|--------|--------------|--------------|

The financial effect of these dividends has not been brought to account in the Consolidated Interim Financial Report for the half year ended 31 December 2015 and will be recognised in subsequent financial statements.

Franked dividends declared or paid during the financial year were franked at a tax rate of 30%.

Cochlear Limited and its controlled entities
Notes to the Interim Financial Statements
For the half year ended 31 December 2015

3. Income taxes

Numerical reconciliation between income tax expense and profit before income tax

| | 31 Dec 2015 | 31 Dec 2014 |
|---|----------------|---------------|
| | \$000 | \$000 |
| Net profit | 94,033 | 71,375 |
| Income tax expense | 32,250 | 23,631 |
| Profit before income tax | 126,283 | 95,006 |
| Tax at the Australian tax rate of 30% (Dec 2014: 30%) | 37,885 | 28,502 |
| Increase in income tax expense due to: | | |
| Non-deductible expenses | 653 | 764 |
| Decrease in income tax expense due to: | | |
| Research and development allowances | (5,435) | (4,649) |
| Effect of tax rate in foreign jurisdictions | (1,091) | (1,460) |
| | 32,012 | 23,157 |
| Adjustment for prior years | 238 | 474 |
| Income tax expense on profit before income tax | 32,250 | 23,631 |

4. Operating assets and liabilities

4.1 Patent dispute

In a trial of the patent infringement lawsuit by the Alfred E. Mann Foundation for Scientific Research and Advanced Bionics LLC in January 2014, a Jury found that Cochlear Limited and its US subsidiary Cochlear Americas infringed four claims across two patents, the infringement was wilful and awarded USD 131,216,325 in damages.

On 1 April 2015, a Judge in the United States District Court in Los Angeles, California held that three of the four patent claims were invalid and Cochlear's infringement of the remaining claim was not wilful. The Judge overturned the damages awarded because three of the four claims were held to be invalid. On 21 April 2015, the Court entered Judgment on liability only and stayed a new trial on damages pending the outcome of the appeal by all parties from the Judgment to the United States Court of Appeals for the Federal Circuit.

As the patents have expired, the Judgment will not disrupt Cochlear's business or customers in the United States.

The directors have obtained external advice and are of the opinion that the facts and the law do not support the Court's decision on infringement of the one remaining claim.

The nature of the above legal process is such that final future outcomes are uncertain. The directors have made judgements and assumptions relating to their best estimate of the outcome of this litigation and actual outcomes may differ from the estimated liability.

A provision was expensed in the half year ended 31 December 2013 in relation to this dispute. No additional amount has been provided since that initial provision. The provision at 31 December 2015 is \$21.3m (30 June 2015: \$21.3m). For the purpose of determining this provision, Cochlear considered its independent damages expert's assessment prepared for the trial to estimate the liability that could result from the dispute.

Cochlear Limited and its controlled entities
Notes to the Interim Financial Statements
For the half year ended 31 December 2015

4.2 Contingent liabilities

The details of contingent liabilities are set out below. The directors are of the opinion that provisions are either adequate or are not required in respect of these matters, as it is either not probable that a future sacrifice of economic benefits will be required, or the amount is not capable of reliable measurement.

Product liability claims

Cochlear is currently and/or is likely from time to time to be involved in claims and lawsuits incidental to the ordinary course of business, including claims for damages relating to its products and services. In addition, Cochlear has received legal claims and lawsuits in various countries including the United States by recipients who have had Cochlear implant CI500 series devices stop functioning for the reason that led to the September 2011 voluntary recall of unimplanted CI500 series devices.

Cochlear carries product liability insurance and has made claims under the policies. The insurers have agreed to indemnify Cochlear in accordance with the terms and conditions of the policies including deductibles and exclusions. In the opinion of the directors, the details of the product liability insurance policies are commercially sensitive and any disclosure of these details may be prejudicial to the interests of Cochlear.

5. Financial and capital structure

5.1 Loans and Borrowings

| | 31 Dec 2015 | 30 Jun 2015 |
|---------------------------------|----------------|----------------|
| | \$000 | \$000 |
| Loans and borrowings: | | |
| Current | 168,426 | 168,159 |
| Non-current | 44,687 | 44,552 |
| Total loans and borrowings | 213,113 | 212,711 |
| Less: Cash and cash equivalents | (80,251) | (72,208) |
| Net debt | 132,862 | 140,503 |

Multi-option bank facilities - Secured bank loan

Cochlear has two bank loan facilities. The first was amended and extended in June 2013 for a period of three years and a total commitment limit of Australian dollars (AUD) 200.0 million. In December 2013, the total commitment limit was increased to AUD 250.0 million. The facility has an option to allocate a letter of credit sub-facility limit of up to AUD 30.0 million for the purpose of drawing either bank guarantees or letters of credit. This letter of credit sub-limit currently is AUD 5.0 million.

In June 2013, Cochlear negotiated a second loan facility for a period of five years. The facility has a total commitment limit of AUD 115.0 million, made up of an AUD 100.0 million loan sub-facility limit and incorporates an AUD 15.0 million letter of credit facility that was negotiated in August 2011.

Both facilities are secured by interlocking guarantees provided by certain controlled entities. Interest on the facilities is variable and charged at prevailing market rates.

Other credit facilities

Unsecured bank overdrafts

Certain unsecured bank overdrafts are payable on demand and are subject to annual review. Interest on unsecured bank overdrafts is variable and is charged at prevailing market rates.

Cochlear Limited and its controlled entities
Notes to the Interim Financial Statements
For the half year ended 31 December 2015

Secured bank loan

Cochlear has a Japanese yen (JPY) 450.0 million loan facility. It is secured by a letter of guarantee and reviewed annually. Interest is charged at prevailing market rates.

Bank guarantees

As at 31 December 2015, Cochlear had contingent liability facilities denominated in United States dollars (USD), Euros (EUR), Sterling (GBP), Indian rupees and New Zealand dollars totalling AUD 1.6 million (June 2015: AUD 1.6 million).

5.2 Financial Instruments

Fair values

The carrying amounts and estimated fair value of Cochlear's financial assets and liabilities are materially the same.

The fair value of forward exchange contracts is based upon the listed market price, if available. If a listed market price is not available, the fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using benchmark bill futures and swap rates. These fair values are provided by independent third parties.

Valuation of financial assets and liabilities

For financial asset and liabilities measured and carried at fair value, Cochlear uses the following levels to categorise the valuation methods used:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

All of Cochlear's forward exchange contracts were valued using observable market inputs (Level 2) and there were no transfers between levels during the year.

| | 31 Dec 2015 | 30 June 2015 |
|--|-------------|--------------|
| | Level 2 | Level 2 |
| | \$000 | \$000 |
| Forward exchange contracts used for hedging: | | |
| Derivative financial assets | 3,886 | 5,763 |
| Derivative financial liabilities | (27,699) | (35,123) |

There have been no transfers between levels during the year. There are no other financial assets or financial liabilities carried at fair value or valued using a Level 1 or Level 3 valuation method.

6 Other notes

6.1 Events subsequent to reporting date

Other than reported below, there has not arisen in the interval between the reporting date and the date of this financial report, any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of Cochlear, the results of those operations, or the state of affairs of Cochlear in future financial years.

Dividends

For dividends declared after 31 December 2015, see Note 2.7.

Cochlear Limited and its controlled entities
Directors' Declaration
For the half year ended 31 December 2015

In the opinion of the directors of Cochlear Limited:

1. The consolidated financial statements and notes set out on pages 12 to 23 are in accordance with the *Corporations Act 2001*, including:
 - a. giving a true and fair view of the Consolidated Entity's financial position as at 31 December 2015, and of its performance, for the six month period ended on that date; and
 - b. complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*; and
2. There are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Signed in accordance with a resolution of the directors:

Dated at Sydney this 11th day of February 2016.



Director



Director



Independent auditor's review report to the members of Cochlear Limited For the half year ended 31 December 2015

We have reviewed the accompanying interim financial report of Cochlear Limited, which comprises the consolidated interim balance sheet as at 31 December 2015, consolidated interim income statement, consolidated interim statement of comprehensive income, consolidated interim statement of changes in equity and consolidated interim statement of cash flows for the half-year period ended on that date, notes 1 to 6.1 comprising a summary of significant accounting policies and other explanatory information and the directors' declaration of the Consolidated Entity comprising the company and the entities it controlled at the half-year's end or from time to time during the half-year.

Directors' responsibility for the interim financial report

The directors of the company are responsible for the preparation of the interim financial report that gives a true and fair view in accordance with Australian Accounting Standards and the Corporations Act 2001 and for such internal control as the directors determine is necessary to enable the preparation of the interim financial report that is free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express a conclusion on the interim financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the interim financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the Consolidated Entity's financial position as at 31 December 2015 and its performance for the half-year ended on that date; and complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As auditor of Cochlear Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of an interim financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*.

Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the interim financial report of Cochlear Limited is not in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the Consolidated Entity's financial position as at 31 December 2015 and of its performance for the half-year ended on that date; and
- (b) complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*.

Emphasis of Matter

We draw attention to Note 4.1 to the interim financial statements which describes the uncertainty related to the outcome of the lawsuit filed against the Consolidated entity for alleged patent infringement. Our review report is not modified in respect of this matter.

KPMG
Sydney, 11 February 2016

Cameron Slapp, Partner