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COCHLEAR FINANCIAL RESULTS
FOR THE SIX MONTHS ENDED DECEMBER 2016

Positive momentum continues across all markets

- **Net profit of $111.4m, up 19%**
- **Cochlear implant units up 10% to 16,234 with around 10% growth across both developed and emerging markets**
- **Sales revenue up 4% in Australian dollars (8% in constant currency) to $604.4 million with constant currency growth delivered across all product categories and regions**
- **Market leadership position supported by successful new product launches, continued investment in market growth initiatives and R&D activities**
- **Interim dividend up 18% to $1.30 per share, fully franked**
- **FY17 net profit guidance maintained at $210-225m, up around 10-20% on FY16**

A$m	**HY17**	**HY16**	**Change %**
Sales revenue	604.4	581.7	⬆ 4%
FX contracts gain / (loss)	4.8	(23.6)	
Total revenue	609.2	558.1	⬆ 9%
Earnings before interest & tax (EBIT)	**156.4**	**131.0**	⬆ **19%**
Net finance costs	(3.4)	(4.7)	⬇ 28%
Taxation expense	(41.6)	(32.3)	⬆ 29%
Net profit	**111.4**	**94.0**	⬆ **19%**
Basic earnings per share	$1.94	$1.65	⬆ 18%
Interim dividend per share	$1.30	$1.10	⬆ 18%
Franking %	100%	100%	

FINANCIAL HIGHLIGHTS

- Sales revenue of $604.4 million, up 4% in Australian dollars (8% in constant currency);
- Net profit of $111.4 million, up 19%;
- Basic earnings per share of $1.94 per share, up 18%; and
- Interim dividend of $1.30 share, up 18%, franked at 100%, representing a payout of 67% of first half net profit.

OVERVIEW

HY17 operational highlights

Cochlear's Chief Executive Officer & President Chris Smith said, "The positive momentum we have experienced over the past few years has continued into FY17 with strong and consistent growth in units delivered across all regions.

"Cochlear implant unit growth was 10%, an increase of 16% when excluding the impact of Chinese Central Government tender units. Developed market units grew around 10% with highlights including continued strong performances from the United States (US) and Western Europe. Emerging market units also grew around 10% with continuing strong growth in India and China Other with solid improvements in Latin America and Central & Eastern Europe.

"We have strengthened our market position by continuing to expand our portfolio with market-leading products. During the half Cochlear™ Kanso™, our first off-the-ear sound processor and the Nucleus® Profile™ Slim Modiolar electrode, the world's slimmest electrode, were launched across Europe and the US. We are experiencing strong uptake of both products, with a notable uptick in unit growth during the second quarter in those markets.

"Cochlear continues to demonstrate its commitment to being the technology leader in our industry with ongoing investment in research and development (R&D). During the half we invested $72.2 million, 12% of sales revenue, with a pipeline of new products expected to be launched over the coming years.

"The Services business, which includes sound processor upgrades and accessories, delivered constant currency revenue growth of 3%. The Americas and EMEA both grew revenue by around 6% in constant currency driven by continuing demand for the Nucleus 6 Sound Processor.

"The Acoustics business had a strong half with sales growth of 20% in constant currency, driven by the uptake of Baha® 5 Power and SuperPower sound processors across all regions."

Strong financial position

Mr Smith said, "Cochlear has delivered a strong profit result with net profit of $111 million, up 19%. Free cash flow increased by 50% to $85 million and has supported the 18% increase in the interim dividend and a $24 million reduction in net debt since June 2016."

Solid progress made against business priorities

"Cochlear's priorities are focused on the customer with initiatives aimed at accelerating market growth through global expansion of awareness and increased market access initiatives. With a growing recipient base, now numbering over 450,000, we are actively strengthening our servicing capability to provide products, programs and digital services to support the lifetime relationship with our recipients.

"We made progress against our business priorities in the half. These remain focused on growing the core; building a service business; shaping the organisation and value creation. The key areas of focus have been on continuing to expand the sales force across major developed and emerging markets, expanding our direct-to-consumer programs in the US, Australia, Germany and the UK and building greater engagement with our recipient base," said Mr Smith.

2017 financial outlook

For FY17, Cochlear continues to expect net profit to be within a range of $210-225 million, an increase of around 10-20% on FY16. Mr Smith said, “We continue to experience positive momentum across the business with investments made in product development and market growth initiatives expected to underpin growth in the second half. The balance sheet position and free cash flow generation remain strong and we continue to target a dividend payout ratio of around 70% of net profit.”

Key guidance considerations for the second half of FY17:

- continued strong momentum in unit growth;
- Chinese Central Government tender units now expected to be below FY16 levels with the next tender expected during the third quarter;
- expect R&D expenditure for FY17 to be similar to FY16;
- an approximate $1.5 million full year net profit impact from the reduction in R&D tax concession rate from 40% to 38.5%, announced in September 2016 by the Australian Federal Government and effective from 30 June 2016; and
- forecasting a weighted average AUD/USD FX rate of 75 cents for FY17 versus 73 cents in FY16.

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PRODUCT & SERVICE HIGHLIGHTS

	HY17	HY16	Change %	Constant currency
Cochlear implants (units)	16,234	14,748	↑ 10%	
Sales revenue *(A$m)*				
Cochlear implants	377.1	362.7	↑ 4%	↑ 8%
Services (sound processor upgrades and accessories)	144.8	146.3	↓ 1%	↑ 3%
Acoustics (bone conduction and acoustic implants)	82.5	72.7	↑ 13%	↑ 20%
Total sales revenue	**604.4**	**581.7**	↑ **4%**	↑ 8%

Cochlear implants – 62% of sales revenue

Cochlear implant revenue grew 4% in Australian dollars (8% in constant currency) and unit sales grew 10% (16% excluding the benefit of Chinese Central Government tender units) with around 10% growth across both developed and emerging markets.

Developed markets grew around 10% with highlights including continued strong performances from the United States (US) and Western Europe with Korea and Japan also performing well. Emerging markets grew strongly with continuing strong growth in India and China Other with solid improvements in Latin America and Central & Eastern Europe.

There has been a strong uptake of the Nucleus Profile implants since release in FY15. During the half, the electrode portfolio was expanded with a full market release of the new Slim Modiolar electrode (CI532) in Europe, the US and Canada.

Kanso was released during the half as a sound processor option for new implant systems in the US and Europe, with sales contributing to second quarter revenue. Kanso is a discrete, easy-to-use, off-the-ear sound processor that delivers the same hearing performance as the Nucleus 6 Sound Processor. Uptake has exceeded expectations and contributed to market share gains during the half.

The increase in sales revenue also reflects continued investments in market growth initiatives including direct-to-consumer activities and field expansion across many markets. These initiatives help build awareness of implantable hearing solutions and support further penetration into the adult segment.

Services (sound processor upgrades and accessories) – 24% of sales revenue

Services sales revenue declined by 1% in Australian dollars (an increase of 3% in constant currency). Constant currency sales growth of around 6% was delivered across both the Americas and EMEA driven by the continuing uptake of the Nucleus 6 Sound Processor.

As part of the commitment to increase recipient engagement and provide recipients with great customer experience, the business continued to rollout a number of service-oriented programs. These programs include the recipient membership program, Cochlear Family, and MyCochlear.com, a personalised online portal to connect recipients directly with Cochlear.

Cochlear Family membership is growing rapidly, with membership almost doubling over the past six months. Recruitment continues to be a priority with Cochlear Family members upgrading their sound processors at a significantly higher rate than that of non-members.

Acoustics (bone conduction and acoustic implants) – 14% of sales revenue
Acoustics, which includes bone conduction and acoustic implant sales revenue, grew 13% in Australian dollars (20% in constant currency) with solid performances across all regions.

Sales growth was driven by the strong uptake of the Baha 5 Power and Baha 5 SuperPower sound processors which were released during FY16.

The Baha 5 System provides the widest range of sound processors, including the industry's smallest, smartest and most powerful head-worn bone conduction solutions for those with single-sided deafness or who have conductive or mixed hearing loss. The Baha 5 System is also the only hearing implant system with MFi (made for iPhone) capabilities, allowing direct streaming between the sound processor and iPhones.

REGIONAL REVIEW

Sales revenue *(A$m)*	**HY17**	**HY16**	**Change %**	**Constant currency**
Americas	285.2	264.1	⬆ 8%	⬆ 12%
EMEA (Europe, Middle East & Africa)	207.9	210.4	⬇ 1%	⬆ 6%
Asia Pacific	111.3	107.2	⬆ 4%	⬆ 4%
Total sales revenue	**604.4**	**581.7**	⬆ 4%	⬆ 8%

Americas (US, Canada & Latin America) – 48% of sales revenue
Sales revenue increased by 8% in Australian dollars (12% in constant currency). The highlight was the growth in the US with cochlear implant unit sales up around 10%. Growth overall has been driven by new product introductions and growing services revenue, supported by awareness building initiatives which continue to drive overall market growth rates. The success of Kanso, released in October, contributed to momentum during the second quarter.

The expanded field sales organisation, direct-to-consumer marketing and new customer relationship management system (Salesforce.com) have also supported continuing strong market growth rates.

Overall Latin American unit growth and sales revenue have recovered well after declining in FY16.

EMEA (Europe, Middle East and Africa) – 34% of sales revenue
Sales revenue declined by 1% in Australian dollars (an increase of 6% in constant currency) with solid performances across the region.

Unit growth across Western Europe was around 10% with the highlight being strong growth in the UK and Spain. Investments in market growth initiatives and the positive reception to Kanso, CI532 and the Baha 5 Power and SuperPower sound processors drove both market share and market growth across many markets.

Central and Eastern Europe also performed well. The region is benefiting from Cochlear's expanding presence, new indications for cochlear implantation as well as multi-year efforts in building neonatal screening.

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

Sales revenue increased by 4% in Australian dollars (4% in constant currency) with solid growth experienced across many markets including Japan, Korea, China Other and India.

China Other performed well, boosted by the expansion of Cochlear's field sales presence. The result includes 1,100 Chinese Central Government tender units, which compares to around 1,700 units in HY16.

India represents a small but rapidly growing market. The growing number of clinics, expansion of the field force and improvements in reimbursement all contributed to double-digit unit growth.

FINANCIAL REVIEW

Major expenses

A$m	HY17	HY16	Change
Cost of goods sold	176.2	171.3	4.9
% of sales revenue	*29.2%*	*29.4%*	*(0.2) pts*
Selling and general expenses	165.2	154.3	10.9
Administration expenses	44.3	38.1	6.2
Research and development expenses	72.2	71.3	0.9
% of sales revenue	*11.9%*	*12.3%*	*(0.4) pts*
Other income	(5.1)	(7.9)	2.8
EBIT	156.4	131.0	25.4
% of total revenue	*25.7%*	*23.5%*	*2.2 pts*

EBIT increased by $25.4 million, up 19%, to $156.4 million, with the operating margin (EBIT to total revenue) increasing by 2.2 points to 25.7%.

Cost of goods sold (COGS) increased $4.9 million to $176.2 million, primarily as a result of growing volumes. COGS as a percentage of sales revenue decreased by 0.2% to 29.2%, reflecting the impact of changes in foreign exchange (FX) rates and product and geographic sales mix.

Selling and general expenses increased by $10.9 million to $165.2 million. The 7% increase reflects the increased investment in the sales force and marketing activities.

Investment in research and development (R&D) increased 1% to $72.2 million, representing 11.9% of sales revenue, and is down 0.4 points on HY16.

Other income decreased by $2.8 million to $5.1 million. Other income primarily reflects FX gains on asset translation.

Foreign currency (FX) impacts on the income statement

	A$m
Transaction impacts	
Reported FX contract gains/(losses) on hedged sales	
- FX gains – HY17	4.8
- FX losses – HY16	(23.6)
	28.4
Translation impacts	
Sales revenue & expenses[1]	
- Sales revenue	(24.2)
- Total expenses including tax	12.6
	(11.6)
Reported asset translation impacts	
- FX gain on asset translation – HY17	2.6
- FX gain on asset translation – HY16	5.8
	(3.2)

1. HY17 actual v HY16 at HY17 rates

Transaction impacts

Cochlear utilises currency hedging to provide some certainty around near-term cash flow. Over 90% of revenue and around 50% of costs are denominated in foreign currency. Most of the cash that is generated is repatriated to Australia to fund operating and investing activities, including R&D and dividends. In order to provide some certainty around near-term cash flow, expected cash flows are hedged back to Australian dollars (AUD).

In HY17, the AUD appreciated against most of the major currencies compared to HY16 rates. FX gains on hedged sales were $4.8 million as FX contracts roll off. This compared to FX losses on hedged sales of $23.6 million in HY16.

Translation impacts

The key translation impacts from translating foreign sales, expenses and assets into AUD include:

- a net reduction to sales revenue of $24.2 million;
- a net reduction in expenses of $12.6 million; and
- a net benefit to net profit of $2.6 million from the translation of assets, primarily trade receivables. This compares to a $5.8 million net benefit in HY16.

Capital employed

A$m	31 Dec 2016	30 Jun 2016	Change $
Trade receivables	280.0	268.5	11.5
Inventories	154.5	154.1	0.4
Less: Trade and other payables	(109.6)	(110.3)	0.7
Working capital	324.9	312.3	12.6
Debtor days	*84*	*85*	*(1)*
Inventory days	*168*	*169*	*(1)*
Property, plant and equipment	91.8	86.9	4.9
Intangible assets	212.0	224.3	(12.3)
Other net liabilities	(47.5)	(57.1)	9.6
Capital employed	**581.2**	**566.4**	**14.8**

Capital employed increased by $14.8 million to $581.2 million since 30 June 2016 primarily as a result of an increase in working capital.

Working capital increased by $12.6 million to $324.9 million largely reflecting increased sales.

Trade receivables increased $11.5 million to $280.0 million. Debtors days reduced by one day to 84 days.

Net property, plant and equipment remained largely unchanged.

Intangible assets decreased by $12.3 million to $212.0 million, largely 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 HY17.

Other net liabilities decreased by $9.6 million, largely reflecting timing of tax payments.

Cash flow

A$m	HY17	HY16	Change $
EBIT	156.4	131.0	25.4
Depreciation and amortisation	16.0	16.3	(0.3)
Change in working capital and other	(29.1)	(19.4)	(9.7)
Net interest paid	(3.3)	(6.3)	3.0
Income taxes paid	(37.7)	(48.1)	10.4
Operating cash flow	**102.3**	**73.5**	**28.8**
Capital expenditure	(15.0)	(13.4)	(1.6)
Other investments	(2.2)	(3.3)	1.1
Free cash flow	**85.1**	**56.8**	**28.3**

The business generated strong cash flows with free cash flow increasing by 50% to $85.1 million, driven primarily by increased earnings and timing of tax paid.

An increase in EBIT of $25.4 million was partially offset by a net $9.7 million investment in working capital and other to fund business growth.

Income taxes paid reduced by $10.4 million to $37.7 million with taxes paid broadly in line with taxation expense for the half.

During the half, the Australian Federal Government reduced the R&D tax concession rate from 40.0% to 38.5%, effective from 30 June 2016. In FY16, Cochlear had approximately $100 million in qualifying R&D investments which had delivered a full year benefit to net profit of around $10 million. The change in legislation will reduce the tax benefit to around $8.5 million, a $1.5 million reduction in FY17 compared to FY16.

Net debt

A$m	31 Dec 2016	30 Jun 2016	Change $
Loans and borrowings			
Current	3.5	4.0	(0.5)
Non-current	169.4	189.3	(19.9)
Total debt	172.9	193.3	(20.4)
Cash and cash equivalents	(79.4)	(75.4)	(4.0)
Net debt	**93.5**	**117.9**	**(24.4)**
Total loan facilities	350.0	350.0	
Unused portion of debt facilities	175.0	155.0	

Net debt reduced by $24.4 million to $93.5 million since 30 June 2016.

At 31 December 2016, there was $350.0 million in total loan facilities and the unused portion of the bank facility was $175.0 million.

Dividends

	HY17	HY16	Change %
Interim ordinary dividend ($/share)	$1.30	$1.10	18%
Payout ratio %	*67%*	*67%*	
Franking %	*100%*	*100%*	

Strong free cash flow and the continued strength of the balance sheet have supported the payment of an interim dividend of $1.30 per share, franked at 100%, representing a payout of 67% of first half net profit.

The record date for determining dividend entitlements is 16 March 2017 and the interim dividend will be paid on 6 April 2017.

Non-IFRS financial measures

Given the significance of 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 HY17 FX rates.

The above non-IFRS financial measures have not been subject to review or audit. However, KPMG has separately undertaken a set of procedures to agree the non-IFRS financial measures disclosed to the books and records of the Consolidated Entity.

Forward looking statements

Cochlear advises that this document contains forward looking statements which may be subject to significant uncertainties outside of Cochlear's control.

No representation is made as to the accuracy or reliability of forward looking statements or the assumptions on which they are based.

Actual future events may vary from these forward looking statements and it is cautioned that undue reliance not be placed on any forward looking statement.

Appendix

Relevant FX rates

The following table includes FX contract cover and rates as at 31 December 2016:

Total FX hedges expressed in foreign currency (local currency - millions)	USD 287.5	EUR 186.4	JPY 1,853.5	Total
FX hedges expressed in $Am	393.5	291.6	23.2	708.3
% of total cover	*56%*	*41%*	*3%*	*100%*
3 year weighted average rates				
- FX contracts 31/12/16	0.73	0.64	80.0	
- FX contracts 31/12/15	0.78	0.65	87.4	
H2 FY17 weighted average rates				
FX contracts at 31/12/16	0.75	0.65	82.7	
Cover for H2 FY17 ($Am)	129.8	96.1	7.6	233.5

Summary of relevant FX rates:

	HY17	HY16	Change %
Average rates (used for translating P&L)			
USD	0.75	0.73	*3%*
Euro	0.69	0.66	*5%*
JPY	79.36	88.17	*(10%)*
GBP	0.59	0.47	*26%*
Average contract rates (used to repatriate FX to Australia)			
USD	0.76	0.84	*(10%)*
Euro	0.66	0.67	*(2%)*
JPY	85.12	89.67	*(5%)*
	HY17	FY16	
Period end rates (used for translating balance sheet)			
USD	0.72	0.74	*(3%)*
Euro	0.69	0.67	*3%*
JPY	84.78	75.41	*12%*
GBP	0.59	0.56	*5%*