

**Company announcement** no 2019-06

7 May 2019

Interim Management Statement covering the period year-to-date

**Successful launch of Oticon Opn S drives growth acceleration after slow start to the year****Product launches expected to drive market share gains in 2019****Maintaining outlook for EBIT of DKK 2.65-2.95 billion with material skew towards second half-year**

- Overall, growth for the Group has been solid year-to-date driven by organic growth combined with growth from acquisitions and a minor positive exchange rate effect. The Group has seen growth acceleration after a slow start to 2019 where we saw weak momentum in the hearing aid wholesale business prior to new product launches taking effect and a significant, negative one-off impact of the new hearing healthcare reform in France. Sales lost as a result of the reform have negatively impacted EBIT for Hearing Devices by approx. DKK 50 million, particularly in our hearing aid retail business. Our increased R&D efforts in 2018 have naturally impacted R&D costs year-to-date, but the year-over-year impact will gradually decrease. Similarly, we have year-to-date seen acquisitive growth in distribution costs, but the year-over-year effect will diminish significantly from the middle of the second quarter.
- Organic growth in Hearing Devices has mainly been driven by our hearing aid wholesale business, which has delivered solid organic growth thanks to a strong uptake of the new Oticon Opn S product family since its launch, which took place at scale in most major markets at the end of March and in April. With its best-in-class audiology and highly robust lithium-ion rechargeable battery technology, Opn S has been very well received, and growth for our hearing aid wholesale business has accelerated in line with plans after a slow start to the year. During April, we launched new product families in our Bernafon and Sonic brands, and we also announced Philips HearLink, our first portfolio of hearing aids under the Philips brand. While the launches by Bernafon, Sonic and Philips will support future growth, they have not had a material impact on sales year-to-date.
- In our hearing aid retail business, growth has year-to-date been driven primarily by acquisitions, and we have additionally seen positive – albeit low – organic growth despite the significant, negative one-off impact from the new hearing healthcare reform in France. Notably, we have seen positive organic growth in both the US and Australia.
- Our Hearing Implants business activity has seen strong organic growth driven by very strong growth in our cochlear implants (CI) business, which has exceeded the estimated market growth rate despite a negative impact from our decision a year ago to reduce our activity level in select CI markets with lower prices. In our bone anchored hearing systems (BAHS) business, organic growth has been solid while we prepare for the launch at the end of the first half-year of our new and ground-breaking Ponto 4 BAHS sound processor based on the Velox S platform used in Oticon Opn S.
- In line with our plans, Diagnostic Instruments has continued to deliver strong organic growth, first and foremost driven by our US-based businesses. However, growth has been broadly based across regions, brands and product categories, reflecting a combination of positive global market trends, a high level of innovation and strong commercial execution.
- Sennheiser Communications, our 50/50 joint venture with Sennheiser KG, has year-to-date generated strong growth driven by the Mobile Music and Enterprise Solutions segments, particularly in North America, as well as profit in line with last year.
- We maintain our expectation to generate organic sales growth above market level in 2019, accelerating through the year as a reflection of the timing of new product launches. Based on exchange rates as of 6 May 2019 and including the impact of exchange rate hedging, we continue to expect a positive exchange rate effect of 1% on revenue in 2019. We continue to guide for a reported operating profit (EBIT) of DKK 2,650-2,950 million with a material skew towards the second half-year, as we expect EBIT for the first half-year to be around or slightly lower than reported EBIT in the first half of 2018. We also still expect to deliver substantial growth in our cash flow from operating activities (CFFO) and to buy back shares worth a minimum of DKK 1.2 billion. We aim for a gearing multiple of 1.8-2.3 measured as net interest-bearing

debt (NIBD) relative to EBITDA, corresponding to an unchanged gearing multiple of 1.5-2.0 before the implementation of IFRS 16.

*"I'm very pleased to see that we have succeeded in once again delivering industry-leading innovation with our new flagship hearing aid Oticon Opn S – a huge technological leap forward in terms of audiology and rechargeability. We've already seen very positive feedback and uptake by customers, and we're confident that Opn S will continue to drive strong growth acceleration. We're also seeing positive trends in our well-operated and profitable Diagnostic Instruments business activity as well as strong growth in Hearing Implants where we're getting ready for a big new launch. After a slow start to the year, we expect to gain market share as a Group in 2019 driven by several high-profile product introductions as well as continuous growth in our retail business,"* says Søren Nielsen, President & CEO of Demant.

## **Hearing Devices**

### *Market trends*

We estimate that the global hearing aid market has seen growth rates year-to-date in line with our general expectation of 4-6% unit growth per year when adjusting for high growth in the NHS in the UK due to stock-building in preparation for Brexit. According to statistics from the Hearing Industries Association (HIA), unit sales in the US increased by 2.5% in the first quarter of the year, with growth in the commercial part of the US market of 1.5% and growth in Veterans Affairs (VA) of 6.7%. No later than in August 2020, the Food and Drug Administration (FDA) is expected to introduce draft legislation to establish a new over-the-counter (OTC) category of hearing aids in the US. As a member of HIA, we monitor and analyse developments closely and are in active dialogue with the FDA. We maintain our view that any impact of the new OTC category will be limited.

Overall unit growth in Europe has been very strong driven in large part by high orders placed by the NHS as they have built stock in preparation for Brexit. We have also seen strong unit growth in Germany, Italy as well as in several other countries. In France, we have also seen very solid growth albeit with significant fluctuations as a new hearing healthcare reform took effect on 1 January 2019, entailing a number of different elements. These include increased reimbursement for hearing aid users, eligibility for renewal every four years, a mandatory trial period of 30 days, a mandatory warranty period of four years and an ambition to increase the number of trained audiologists in France to meet demand. Overall, the regulatory changes have resulted in a significant, negative one-off impact year-to-date for our Hearing Devices business activity of approx. DKK 50 million on EBIT, particularly in our hearing aid retail business, but we are generally positive about the potential impact of the reform over the coming years.

There are no reliable industry statistics available on the development of prices in the global hearing aid wholesale market, but we believe that the value growth rate year-to-date has been consistent with our medium- to long-term estimate of 2-4% when adjusting for the extraordinary growth in the NHS as described above. As part of this estimate, we continue to expect a slightly negative price development going forward driven by channel and geography mix shifts and a competitive business environment. ASPs on the hearing aid retail market vary significantly across markets because of differences in reimbursement schemes, customer preferences and different product mixes, but we lack reliable market statistics.

### *Wholesale*

Year-to-date, our hearing aid wholesale business has delivered solid organic growth in value above the estimated market growth rate of 2-4%. The slowing growth momentum that we saw in the final months of 2018, due to weak growth in sales in the premium segment, carried over into the first months of 2019 and has had a significant effect on growth year-to-date. However, following the roll-out of the novel Oticon Opn S, which took place at scale in most major markets at the end of March and in April, we have seen growth acceleration in line with our plans.

Based on the new and unique Velox S platform, the new Opn S products deliver industry-leading audiology with significantly improved outcomes for end-users than its predecessor, the ground-breaking Oticon Opn.

Moreover, the products feature a high-performing lithium-ion rechargeable battery that makes charging quick, efficient and simple and has more than enough battery time for a full day's use. Feedback from customers and end-users has been very positive thus far as evidenced by an internal study where 96% of respondents preferred Opn S to the highly successful Opn. Oticon Opn S was initially rolled out in four styles and at the top-three price points, except for the rechargeable version, which until the beginning of May had only been rolled out at the top price point. In addition, Oticon has introduced Opn Play, a paediatric family of hearing aids based on the Velox S platform.

In April, our Bernafon and Sonic brands also launched new product families, Viron and Captivate, respectively, which both offer improved sound experience and lithium-ion rechargeable solutions. These product families will support our overall growth throughout the year.

On 10 April 2019, we announced the launch of Philips HearLink, a completely new portfolio of Philips-branded hearing solutions. We are confident that the unique combination of first-class hearing technology and a well-known end-user brand will help us address new customer segments globally and thus not only be a strong supplement to our existing hearing aid brand portfolio, but also help us gain further market share over the coming years.

Growth in 2019 has so far been driven by strong unit growth, whereas ASP growth has been negative. This is the result of mix changes where very strong unit sales to the NHS and to customers in Asia, particularly China, have diluted our global ASP. Additionally, our unit growth in the premium segment was weak prior to the launch of Oticon Opn S, and combined with growth in sales of the mid-priced products launched in August 2018, this has also had a dilutive impact on our ASP compared to last year. The negative ASP growth year-to-date has naturally impacted profitability, but having now launched our new premium products, we expect the negative ASP trend to reverse throughout the remainder of 2019.

Growth in North America has been flat year-to-date, with strong growth in sales to VA compensating for a slow start to the year in terms of sales to independent hearing care professionals because of a negative development in the product mix. With our new product launches, we have seen material growth acceleration and we expect this trend to continue, particularly in the premium segment. Similarly, we significantly strengthened our product offering to VA when we introduced Oticon Opn S to this channel at the beginning of May, which will also support growth in 2019.

Driven by strong performances in several of the major markets, we have seen very solid organic growth in Europe, particularly in units. In the UK, we have seen very high growth due to large orders placed by the NHS, as they have started to build stock in preparation for Brexit. Furthermore, we have also seen strong growth in Italy and Spain as well as in France despite a minor negative one-off impact at the beginning of the year of the new hearing healthcare reform. Growth in Europe has generally been strong after the introduction of Oticon Opn S.

Our Asia region delivered high organic growth driven by very strong performances in China, Japan and South Korea. We have seen modest growth in the Pacific and Other regions.

To help further expand our position as a leading hearing aid manufacturer, we significantly increased our R&D spend in 2018, primarily in the second quarter of the year. Naturally, this step-up in our R&D effort has impacted our R&D costs year-to-date, but the year-over-year impact will gradually diminish through the year.

#### *Retail*

Growth in our hearing aid retail business has primarily been driven by acquisitions, and we have additionally seen positive – albeit low – organic growth despite the significant, negative one-off impact from the new hearing healthcare reform in France. We have also seen positive organic growth in both the US and Australia, and we expect to see gradually improving organic growth in our retail business throughout the year.

In North America, we have seen significant acquisitive growth, primarily related to the acquisition in the first half of 2018 of the remaining shares of a US-based store network, which was previously recognised as investments in associates. Along with minor bolt-on acquisitions, this has naturally also added to growth in distribution costs year-to-date. Whereas Canada saw a soft start to the year, organic growth in the US has been positive as a result of improvements in our marketing activities, both centrally and at store level. Meanwhile, we continue our work on harmonising the branding of our US-based store network, which will help us further improve marketing efficiency, and we expect this process to be completed by the end of the year.

Organic growth in Europe has been impacted by significant, negative growth in France where the introduction of the new hearing healthcare reform resulted in materially lower invoicing levels in January and to a lesser extent in February. The lower invoicing levels are the result of the introduction of a mandatory 30-day trial period, which has in effect postponed the recognition of a significant portion of revenue, but underlying trends in France remain healthy and the situation has now normalised. We thus expect solid organic growth in France for the remainder of the year, as we continue to benefit from having a strong infrastructure and a market-leading brand. Meanwhile, we have seen positive growth contributions from other markets in Europe, including the UK and Poland.

After a challenging 2018, our retail activities in Australia have improved, and organic growth has been positive year-to-date. We have adjusted our business model to become more aligned with current market conditions where free-to-client hearing aids make up a larger proportion of the overall mix than in previous years.

### **Hearing Implants**

Our Hearing Implants business activity has seen strong organic growth driven by very strong growth in our CI business despite a negative impact from our decision a year ago to reduce our activity level in select CI markets with lower prices. Growth in CI has been driven by broad-based progress in Europe, particularly in Germany, in Brazil, which is an important CI market, and in various export markets.

In our BAHS business, organic growth has been solid despite limited growth in the BAHS market due to the lack of new product launches. With our planned launch of the new Ponto 4 sound processor at the end of the first half-year, we expect to see a material acceleration of the growth rate in the second half-year. Ponto 4 features the smallest design on the market and is based on the latest hearing aid platform from Oticon, Velox S, ensuring market-leading audiology combined with 2.4 GHz Bluetooth connectivity. This is a strong testament to synergies and collaborations across our business activities, which ultimately benefit end-users.

### **Diagnostic Instruments**

In Diagnostic Instruments, we have seen continued, strong organic growth in line with our plans thanks to continuously positive market trends and a solid competitive position in terms of both product offering and distribution. Our US-based businesses have been the most significant growth drivers year-to-date, but we have also seen strong performances in our Asia region. Most product categories have contributed to growth, including audiometers as well as impedance, fitting, otoacoustic emission (OAE) and auditory brainstem response (ABR) equipment, and all brands have seen solid growth, particularly MAICO and Grason-Stadler. Overall, growth has been broadly based across regions, brands and product categories.

### **Personal Communication**

Sennheiser Communications, our 50/50 joint venture with Sennheiser KG, has year-to-date performed slightly better than expected and has generated strong organic growth driven by the Mobile Music and Enterprise Solutions segments. Our growth has been particularly strong in North America, but we currently have great potential for growth in most of our markets. Overall, profit has year-to-date been in line with last year.

As communicated in September 2018, we and Sennheiser have decided to end our successful joint venture and let the Enterprise Solutions and Gaming headsets segments continue as an independent business as part of the Demant Group and the Mobile Music headsets segment continue as part of the Sennheiser Con-

sumer business. The separation is scheduled to take place on 1 January 2020. Until then, Sennheiser Communications will continue as before, while Sennheiser and Demant prepare the separation in order to ensure a seamless and smooth transition for employees, customers, suppliers and partners.

## **Other matters**

### *Acquisitions*

In 2019, we have continued to make acquisitions in Hearing Devices, and we expect the cash flow to acquisitions for the full-year to be slightly below the level seen in 2018. A significant proportion of the acquisitions we expect to make in 2019 involve taking full ownership of assets in which we have previously held a minority share, predominantly in our hearing aid retail business.

### *Share buy-back*

The Company has year-to-date bought back 1,303,140 shares worth a total of DKK 264 million, corresponding to an average purchase price of DKK 202.23. Following the cancellation of 7,080,940 shares as approved by the Annual General Meeting on 19 March 2019, the Company's holding of treasury shares corresponds to approx. 0.5% of the share capital as of today.

### *IFRS 16*

Issued in January 2016, IFRS 16 Leases requires lessees to recognise nearly all leases in the balance sheet with effect from 1 January 2019. Management has decided to use the modified transition method, whereby comparative figures are not restated. Please refer to Note 9.1 of our Annual Report 2018 for more details on the expected impact of the new accounting standards.

## **Outlook for 2019**

We maintain our expectation to generate organic sales growth above market level in 2019, accelerating through the year as a reflection of the timing of new product launches. Based on exchange rates as of 6 May 2019 and including the impact of exchange rate hedging, we continue to expect a positive exchange rate effect of 1% on revenue in 2019. We continue to guide for a reported operating profit (EBIT) of DKK 2,650-2,950 million with a material skew towards the second half-year, as we expect EBIT for the first half-year to be around or slightly lower than reported EBIT in the first half of 2018. We also still expect to deliver substantial growth in our cash flow from operating activities (CFFO) and to buy back shares worth a minimum of DKK 1.2 billion. We aim for a gearing multiple of 1.8-2.3 measured as net interest-bearing debt (NIBD) relative to EBITDA, corresponding to an unchanged gearing multiple of 1.5-2.0 before the implementation of IFRS 16.

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Demant will host a conference call on 7 May 2019 at 14:00 CET. To attend this call, please use one of the following dial-ins: +45 3544 5577 (DK), +44 3333 000 804 (UK) or +1 6319 131 422 (US). The pin code is 25966762#. A presentation for the call will be uploaded to [www.demant.com](http://www.demant.com) shortly before the call.

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