# Appendix 4D

# Cochlear Limited
# Half Yearly Report
# As at 31 December 2014

**Results for announcement to the market**

| | | Movement | | $A000 |
|---|---|---|---|---|
| **Sales Revenue** | **up** | **17%** | **to** | **440,481** |
| Revenue | up | 18% | to | 438,346 |
| Earnings before interest, taxes and patent dispute provision (EBIT) | up | 103% | to | 100,458 |
| Net profit for the period before patent dispute provision | up | 94% | to | 71,375 |
| **Net profit for the period attributable to members** | **up** | **240%** | **to** | **71,375** |
| Basic earnings per share (cents) | up | 239% | to | 125.3 |
| Dividend (cents) | down | 29% | to | 90.0 |

| | | | | |
|---|---|---|---|---|
| Net tangible assets per share at 31 December 2014 (cents) | up | 22% | to | 157.9 |
| Net tangible assets per share at 31 December 2013 (cents) | | | | 128.9 |

| **Dividends** | Amount per security | Franked amount per security | Conduit foreign income per security |
|---|---|---|---|
| Interim dividend per share (cents) | 90.0c | 31.5c | 36.0c |
| Previous corresponding period (cents) | 127.0c | 0.0c | 30.0c |

| | |
|---|---|
| Record date for determining entitlements to the dividend | 5 March 2015 |
| Dividend payment date | 26 March 2015 |

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 2014**

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 2014 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** |
|---|---|
| *Non-executive directors* | |
| Mr Rick Holliday-Smith, *Chairman* | Director since March 2005 |
| Mrs Yasmin Allen | Director since August 2010 |
| Mr Paul Bell | Director from August 2005 to October 2014 |
| Mr Glen Boreham | 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 |
| | |
| *Executive director* | |
| Dr Chris Roberts, *CEO/President* | Director since February 2004 |

### 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 2014 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 2014.

| | **2014** | **2013** |
|---|---|---|
| | **$000** | **$000** |
| **Revenue** | **438,346** | **371,060** |
| Sales revenue | 440,481 | 376,967 |
| Earnings before interest and tax and patent dispute provision * (EBIT) | 100,458 | 49,425 |
| Net profit after tax but before patent dispute provision * | 71,375 | 36,826 |
| Patent dispute provision, net of tax* | - | (15,781) |
| **Profit attributable to members** | **71,375** | **21,045** |
| Basic earnings per share (cents) | 125.3 | 37.0 |
| Diluted earnings per share (cents) | 124.9 | 36.9 |
| Interim dividend per share (cents) | 90.0 | 127.0 |

*The patent dispute provision costs were nil for the six months ended 31 December 2014 and $22,545,000 before tax and $15,781,000 after tax for the six months ended 31 December 2013.

### Revenue

A focus for the first half of fiscal year ended 31 December 2014 (H1 F15) was continuing the sales momentum for products launched during the fiscal year ended 31 June 2014 (F14). Feedback on these products throughout the half was extremely positive. These products continue to improve the lives of the hearing impaired in line with Cochlear's mission.

Total revenue for H1 F15 was $438.3 million, up 18% on H1 F14. Sales, excluding FX contracts, were $440.5 million, up 17%. In constant currency (that is restating H1 F14 at H1 F15 FX rates) H1 F15 sales were up 15%.

Cochlear implant sales revenue, which included sound processor upgrades, was $383.0 million, up 16% on the prior year and up 14% in constant currency.

Sales of sound processor upgrades of $82.2 million were up 98%. The doubling of revenue from sound processor upgrades reflected strong market enthusiasm for the Nucleus® 6 Sound Processor.

Cochlear implant (CI) unit sales were 11,689, in line with H1 F14. CI unit growth was stronger in developed countries, for example Western Europe up 8% and North America up 17%. This was offset by weaker CI unit tender sales in developing countries.

Bone Anchored Solutions, (including acoustic implant sales) of $57.5 million were up 25% and up 22% in constant currency again reflecting the impact of the Baha® 4 and Baha Attract Systems.

The Australian dollar (AUD) depreciated against the United States dollar (USD) during the half which benefits foreign sales when translated into AUD. From a translation perspective, sales benefited by net $7.3 million. Offsetting this was a loss from FX contracts. FX contract losses were $2.2 million for H1 F15 compared to a loss of $5.9 million in H1 F14.

Regional performance:

- Americas sales of $195.3 million were up 30% on H1 F14, (up 26% in constant currency).

- EMEA (Europe, Middle East and Africa) sales of $181.6 million were up 7% (up 7% in constant currency).

- Asia Pacific sales of $63.6 million was up 10% (up 8% in constant currency).

  There was no China Central Government tender sale booked in this half or in H1 F14. Approximately 1,900 units are expected to be delivered in H2 F15 as part of a China Central Government tender. This is similar to the number supplied in H2 F14.

**Profit**

Cost of goods sold (COGS) of $127.4 million gave a COGS/sales margin of 28.9%. This is at historic and H2 F14 levels, but an improvement compared to 32.8% on H1 F14, which had been high due to lower manufacturing volumes in the first quarter of F14.

Expenses of $210.5 million were up 6% on H1 F14, excluding the H1 F14 patent dispute provision of $22.5 million.

A provision of USD20.0 million ($22.5 million) was expensed in H1 F14 in relation to the patent dispute lawsuit by the Alfred E. Mann Foundation for Scientific Research (AMF) and Advanced Bionics LLC (AB) in the USA. No further amount has been expensed or released from this provision during H1 F15.

Selling, general and administration (SG&A) expenses were up 13% to $151.2 million, including an increase for short and long term incentives. Incentives in F14 were less than 100% of target. In H1 F15, an additional provision of $1.4 million was made for doubtful debts including in developing countries.

Investment in research and development (R&D) of $61.4 million was down 6%. This reflects the deliberate strategy to hold the F15 R&D expenditure at approximately the F14 levels. R&D for the half was 14.0% of total revenue compared to 17.5% of total revenue for H1 F14.

Earnings before interest and tax (EBIT) of $100.5 million for H1 F15 was $73.6 million higher than that for the prior year. EBIT to total revenue of 22.9% was higher than last years of 7.2%.

Excluding the patent dispute provision in H1 F14, EBIT in H1 F15 of $100.5 million was up $51.1 million (103%) on H1 F14. EBIT to total revenue was 22.9% compared to 13.3% in H1 F14 and 23.1% in H2 F14.

Net interest expense increased 19% to $5.5 million due to higher borrowings. Interest cover was 18 times (H1 F14: 6 times).

The effective tax rate was 24.8% (H1 F14: 5.8%). Excluding the patent dispute provision in F14, the effective tax rate increased by 6.9 percentage points, as the R&D tax concession benefit remained largely unchanged despite the higher profit.

Net profit after tax (NPAT) increased 240% to $71.4 million.

Excluding the patent dispute provision in F14, NPAT increased 94%.

**Financial position**

Inventories of $138.5 million were up 8% from 30 June 2014 ($128.6 million). This reflects a build-up of strategic inventories, including inventory for the H2 F15 delivery of the China Central Government tender. Inventory days increased to 199 days (30 June 2014, 189 days) but is down from 208 days at 31 December 2013.

Trade receivables of $208.3 million were up 3% from 30 June 2014 ($201.3 million). In constant currency, trade receivables were down 2%. Debtors days increased to 85 (June 2014, 74 days) reflecting the impact of tender sales which often have extended credit terms.

The liability associated with forward exchange contracts of $36.2 million increased by $26.9 million (30 June 2014, $9.3 million), reflecting the fall in the AUD against the USD.

The product recall provision was reduced by a net $1.4 million to $20.2 million at 31 December 2014 from June 2014.

The provision for patent dispute was unchanged at USD20.0 million. Due to the appreciation of the USD, the AUD amount of the provision increased to $24.6 million (30 June 2014, $21.3 million)

Intangible assets of $231.3 million (30 June 2014, $234.1 million) are a significant proportion of Cochlear's total assets. Foreign exchange movements accounted for $0.3 million of the decrease. Some $169.9 million of this total relates to goodwill arising from the earlier acquisitions of businesses, principally the Entific business in 2005. All intangible assets are tested for impairment on an annual basis. There were no impairments or write-downs of intangible assets in H1 F15.

The Board has declared a dividend of $0.90 per share, franked to 35%, which will be paid on 26 March 2015 based on a record date of 5 March 2015. This is consistent with the August and October 2014 payout guidance of approximately 70% of NPAT.

Net debt was $171.6 million at 31 December 2014, down $9.7 million (June 2014, $181.3 million) reflecting strong profits and working capital management. Dividends of $72.5 million were paid in the half.

Cash generated from operating and investing activities for H1 F15 was $79.5 million, up from $19.7 million in H1 F14.

At 31 December 2014, debt facilities of $350.0 million were in place with remaining terms of 18 months and 3.5 years. At 31 December 2014, the unused portion of the facility was $117.0 million. All bank covenants were met at 31 December 2014.

**Outlook**

Cochlear expects ongoing steady progress including in H2 F15. Regulatory approval has been obtained for products releasing in H2 F15 including:

- Nucleus Profile with Slim Straight electrode in Europe,

- Nucleus Profile with Contour Advance® electrode in the USA,
- Wireless Accessories for Nucleus 6 in all regions,
- SmartSound® iQ for Nucleus 6 Hybrid in the USA, and
- Aqua+ Accessory for Nucleus 6 in Europe.

Cochlear will continue investing in SG&A to support these product launches.

Cochlear continues to invest in long-term market growth initiatives and an extensive R&D program that will improve patient outcomes, broaden indications and improve access.

**Non-IFRS financial measures**

Given the significance of the FX movements and patent dispute 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 F15 FX rates
- Excluding patent dispute provision: IFRS measures adjusted for the expense of the patent dispute provision.

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 127.0 cents per share, franked to 20% with Class C (20%) franking credits, in respect of the year ended 30 June 2014, paid on 25 September 2014. | 72,469 |

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 2014. Since the end of the financial half-year, the directors declared an interim dividend of 90.0 cents 35% franked amounting to a total of $51.4m.

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

The lead auditor's independence declaration is set out on page 7 and forms part of the Directors' Report for the half year ended 31 December 2014.

**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 10th day of February 2015.

Signed in accordance with a resolution of the directors:

Director                                        Director

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

I declare that, to the best of my knowledge and belief, in relation to the review for the financial half year ended 31 December 2014 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, 10 February 2015

# Cochlear Limited and its controlled entities
# Interim Income Statement
# For the half year ended 31 December 2014

| | Note | 31 Dec 2014<br>$000 | 31 Dec 2013<br>$000 |
|---|---|---|---|
| Revenue | 6(a) | 438,346 | 371,060 |
| Cost of sales | 6(b) | (127,369) | (123,669) |
| **Gross profit** | | **310,977** | **247,391** |
| | | | |
| Selling and general expenses | | (122,686) | (114,276) |
| Administration expenses | | (28,559) | (19,351) |
| Patent dispute provision | 12 | - | (22,545) |
| Research and development expenses | | (61,360) | (65,057) |
| Other income | 6(c) | 2,086 | 1,255 |
| Other expenses | 6(d) | - | (537) |
| **Results from operating activities** | | **100,458** | **26,880** |
| | | | |
| Finance income | 6(e) | 90 | 150 |
| Finance expense | 6(e) | (5,542) | (4,740) |
| **Net finance expense** | 6(e) | **(5,452)** | **(4,590)** |
| | | | |
| **Profit before income tax** | | **95,006** | **22,290** |
| | | | |
| Income tax expense | 10 | (23,631) | (1,245) |
| | | | |
| **Net profit** | | **71,375** | **21,045** |
| | | | |
| Basic earnings per share (cents) | 7 | 125.3 | 37.0 |
| Diluted earnings per share (cents) | 7 | 124.9 | 36.9 |

The notes on pages 14 to 24 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 2014

| | 31 Dec 2014 $000 | 31 Dec 2013 $000 |
|---|---|---|
| **Net profit** | **71,375** | **21,045** |
| **Other comprehensive income** | | |
| **Items that will not be reclassified subsequently to profit or loss** | | |
| Defined benefit plan actuarial losses | - | (34) |
| **Total items that will not be reclassified to profit or loss** | **-** | **(34)** |
| **Items that may be reclassified subsequently to profit or loss** | | |
| Foreign currency translation differences | 12,556 | 27,929 |
| Effective portion of changes in fair value of cash flow hedges, net of tax | (25,527) | (16,212) |
| Net change in fair value of cash flow hedges transferred to the income statement, net of tax | 1,494 | 4,135 |
| **Total items that may be reclassified to profit or loss** | **(11,477)** | **15,852** |
| **Other comprehensive (loss) / income for the period, net of income tax** | **(11,477)** | **15,818** |
| **Total comprehensive income for the period** | **59,898** | **36,863** |

The notes on pages 14 to 24 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 2014

| | Note | 31 Dec 2014 | 30 Jun 2014 |
|---|---|---|---|
| | | $000 | $000 |
| **Current assets** | | | |
| Cash and cash equivalents | | 58,871 | 56,127 |
| Trade and other receivables | | 227,329 | 214,953 |
| Inventories | | 138,495 | 128,613 |
| Current tax receivables | | 9,759 | 8,600 |
| Prepayments | | 13,414 | 12,586 |
| **Total current assets** | | **447,868** | **420,879** |
| **Non-current assets** | | | |
| Trade and other receivables | | 1,061 | 5,505 |
| Property, plant and equipment | | 75,122 | 75,776 |
| Intangible assets | | 231,304 | 234,115 |
| Deferred tax assets | | 72,403 | 52,761 |
| **Total non-current assets** | | **379,890** | **368,157** |
| **Total assets** | | **827,758** | **789,036** |
| **Current liabilities** | | | |
| Trade and other payables | | 85,030 | 78,644 |
| Foreign exchange contracts | | 24,677 | 6,643 |
| Loans and borrowings | 13 | 3,061 | 3,141 |
| Current tax liabilities | | 16,297 | 8,442 |
| Provisions | 12 | 61,677 | 57,557 |
| Deferred revenue | | 18,497 | 15,151 |
| **Total current liabilities** | | **209,239** | **169,578** |
| **Non-current liabilities** | | | |
| Foreign exchange contracts | | 11,505 | 2,624 |
| Loans and borrowings | 13 | 227,417 | 234,274 |
| Provisions | 12 | 58,151 | 53,355 |
| **Total non-current liabilities** | | **297,073** | **290,253** |
| **Total liabilities** | | **506,312** | **459,831** |
| **Net assets** | | **321,446** | **329,205** |
| **Equity** | | | |
| Share capital | | 144,136 | 144,136 |
| Reserves | | (38,856) | (32,191) |
| Retained earnings | | 216,166 | 217,260 |
| **Total equity** | | **321,446** | **329,205** |

The notes on pages 14 to 24 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 2014

| | Issued capital $000 | Treasury reserve $000 | Translation reserve $000 | Hedging reserve $000 | Share based payment reserve $000 | Retained earnings $000 | Total equity $000 |
|---|---|---|---|---|---|---|---|
| Balance at 1 July 2014 | 152,599 | (8,463) | (52,630) | 476 | 19,963 | 217,260 | 329,205 |
| **Total comprehensive income** | | | | | | | |
| Net profit | - | - | - | - | - | 71,375 | 71,375 |
| **Other comprehensive income** | | | | | | | |
| 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) for the period** | **-** | **-** | **12,556** | **(24,033)** | **-** | **71,375** | **59,898** |
| **Transactions with owners, recorded directly in equity** | | | | | | | |
| Share based payments transactions | - | - | - | - | 4,457 | - | 4,457 |
| Deferred tax recognised in equity | - | - | - | - | 355 | - | 355 |
| Dividends to shareholders | - | - | - | - | - | (72,469) | (72,469) |
| **Total transactions with owners** | **-** | **-** | **-** | **-** | **4,812** | **(72,469)** | **(67,657)** |
| **Balance at 31 December 2014** | **152,599** | **(8,463)** | **(40,074)** | **(23,557)** | **24,775** | **216,166** | **321,446** |

The notes on pages 14 to 24 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 2014

| | Issued capital $000 | Treasury reserve $000 | Translation reserve $000 | Hedging reserve $000 | Share based payment reserve $000 | Retained earnings $000 | Total equity $000 |
|---|---|---|---|---|---|---|---|
| Balance at 1 July 2013 | 128,196 | (9,408) | (54,974) | (16,680) | 39,221 | 268,156 | 354,511 |
| **Total comprehensive income** | | | | | | | |
| Net profit | - | - | - | - | - | 21,045 | 21,045 |
| **Other comprehensive income** | | | | | | | |
| Defined benefit plan actuarial losses | - | - | - | - | - | (34) | (34) |
| Foreign currency translation differences | - | - | 27,929 | - | - | - | 27,929 |
| Effective portion of changes in fair value of cash flow hedges, net of tax | - | - | - | (16,212) | - | - | (16,212) |
| Net change in fair value of cash flow hedges transferred to the income statement, net of tax | - | - | - | 4,135 | - | - | 4,135 |
| **Total other comprehensive income / (loss)** | **-** | **-** | **27,929** | **(12,077)** | **-** | **(34)** | **15,818** |
| **Total comprehensive income / (loss) for the period** | **-** | **-** | **27,929** | **(12,077)** | **-** | **21,011** | **36,863** |
| **Transactions with owners, recorded directly in equity** | | | | | | | |
| Share based payments transactions | - | - | - | - | 3,490 | - | 3,490 |
| Dividends to shareholders | - | - | - | - | - | (72,442) | (72,442) |
| **Total transactions with owners** | **-** | **-** | **-** | **-** | **3,490** | **(72,442)** | **(68,952)** |
| **Balance at 31 December 2013** | **128,196** | **(9,408)** | **(27,045)** | **(28,757)** | **42,711** | **216,725** | **322,422** |

The notes on pages 14 to 24 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 2014

| | 31 Dec 2014 | 31 Dec 2013 |
|---|---|---|
| | **$000** | **$000** |
| **Cash flows from operating activities** | | |
| Cash receipts from customers | 440,141 | 402,668 |
| Cash payments to suppliers and employees | (325,495) | (350,926) |
| Grant and other income received | 1,508 | 1,216 |
| Interest received | 99 | 166 |
| Interest paid | (5,436) | (4,821) |
| Income taxes paid | (20,875) | (14,692) |
| **Net cash from operating activities** | **89,942** | **33,611** |
| | | |
| **Cash flows from investing activities** | | |
| Acquisition of property, plant and equipment | (7,768) | (10,247) |
| Acquisition of enterprise resource planning system | (2,683) | (3,661) |
| **Net cash used in investing activities** | **(10,451)** | **(13,908)** |
| | | |
| **Cash flows from financing activities** | | |
| Repayment of borrowings | (79,382) | (18,500) |
| Proceeds from borrowings | 72,382 | 74,500 |
| Dividends paid by the parent | (72,469) | (72,442) |
| **Net cash used in financing activities** | **(79,469)** | **(16,442)** |
| | | |
| **Net increase in cash and cash equivalents** | **22** | **3,261** |
| | | |
| **Cash and cash equivalents at 1 July** | 56,127 | 52,689 |
| Effect of exchange rate fluctuation on cash held | 2,722 | 4,042 |
| **Cash and cash equivalents at 31 December** | **58,871** | **59,992** |

The notes on pages 14 to 24 are an integral part of these consolidated interim financial statements.

## Basis of preparation

### 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 2014 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 2014 is available upon request from the Company's registered office at 1 University Avenue, Macquarie University NSW 2109, Australia or at www.cochlear.com.

### 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 2014. This report should also be read in conjunction with any public announcements made by Cochlear Limited during the half year ended 31 December 2014 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 10 February 2015.

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.

### 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 2014.

### 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 2014.

## Performance for the half year

### 5. Segment reporting

| | Americas | EMEA[i] | Asia Pacific | Total |
|---|---|---|---|---|
| | $000 | $000 | $000 | $000 |
| **Information about reportable segments** | | | | |
| **Half year ended 31 December 2014** | | | | |
| External revenue | 195,292 | 181,599 | 63,590 | 440,481 |
| Reportable segment profit | 100,002 | 84,910 | 15,535 | 200,447 |
| **Half year ended 31 December 2013** | | | | |
| External revenue | 149,964 | 169,147 | 57,856 | 376,967 |
| Reportable segment profit | 63,461 | 72,656 | 11,535 | 147,652 |

| | 31 Dec 2014 | 31 Dec 2013 |
|---|---|---|
| | $000 | $000 |
| **Reconciliation of reportable segment revenue** | | |
| External revenue | 440,481 | 376,967 |
| Foreign exchange gains on hedged sales | (2,135) | (5,907) |
| Total revenue | 438,346 | 371,060 |
| **Reconciliation of reportable segment profit or loss** | | |
| Total profit for reportable segments | 200,447 | 147,652 |
| Corporate and other net expenses | (97,854) | (92,320) |
| Foreign exchange loss on hedged sales | (2,135) | (5,907) |
| Patent dispute provision | - | (22,545) |
| Net finance expense | (5,452) | (4,590) |
| Profit before income tax | 95,006 | 22,290 |

(i) Europe, Middle East and Africa.

## 6. Revenue and expenses

| | 31 Dec 2014 | 31 Dec 2013 |
|---|---|---|
| | $000 | $000 |
| **(a) Revenue** | | |
| Sale of goods revenue before hedging | 435,710 | 372,818 |
| Foreign exchange losses on hedged sales | (2,135) | (5,907) |
| **Revenue from the sale of goods** | **433,575** | **366,911** |
| Rendering of services revenue | 4,771 | 4,149 |
| **Total revenue** | **438,346** | **371,060** |
| | | |
| **(b) Expenses** | | |
| **Cost of sales** | | |
| Carrying amount of inventories recognised as an expense | 120,679 | 120,162 |
| Write-down in value of inventories | 2,321 | 836 |
| Other | 4,369 | 2,671 |
| **Total cost of sales** | **127,369** | **123,669** |
| | | |
| **(c) Other income** | | |
| Grant received or due and receivable | 905 | 715 |
| Net foreign exchange gain | 578 | - |
| Other | 603 | 540 |
| **Total other income** | **2,086** | **1,255** |
| | | |
| **(d) Other expenses** | | |
| Net foreign exchange loss | - | 537 |
| **Total other expenses** | **-** | **537** |
| | | |
| **(e) Net finance expense** | | |
| Interest income | 90 | 150 |
| Interest expense | (5,542) | (4,740) |
| **Net finance expense** | **(5,452)** | **(4,590)** |

### 7. Earnings per share

#### Basic earnings per share

The calculation of basic earnings per share for the half year ended 31 December 2014 was based on net profit attributable to equity holders of the parent and a weighted average number of ordinary shares outstanding during the half year ended 31 December 2014 calculated as follows:

| | 31 Dec 2014 | 31 Dec 2013 |
|---|---|---|
| Net profit attributable to equity holders of the parent | $71,375,000 | $21,045,000 |
| **Weighted average number of ordinary shares:** | | |
| Issued ordinary shares at 1 July (number) | 56,937,519 | 56,915,289 |
| Effect of shares issued during the period (number) | 7,730 | 9,091 |
| **Weighted average number of ordinary shares** | 56,945,249 | 56,924,380 |
| Basic earnings per share (cents) | 125.3 | 37.0 |

#### Diluted earnings per share

The calculation of diluted earnings per share for the half year ended 31 December 2014 was based on net profit attributable to equity holders of the parent and a weighted average number of ordinary shares outstanding during the half year ended 31 December 2014 calculated as follows:

| | | |
|---|---|---|
| Net profit attributable to equity holders of the parent | $71,375,000 | $21,045,000 |
| **Weighted average number of ordinary shares (diluted):** | | |
| Weighted average number of shares (basic) | 56,945,249 | 56,924,380 |
| Effect of options and performance shares | 204,879 | 125,185 |
| **Weighted average number of ordinary shares (diluted)** | 57,150,128 | 57,049,565 |
| Diluted earnings per share (cents) | 124.9 | 36.9 |

### 8. 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 2014.

In October 2014 a grant was made to certain employees and key management personnel under the CEIP.

Details of the grant made in the current period are set out below.

| | Exercise price per option | Option life | Number of options | Number of performance rights |
|---|---|---|---|---|
| Options & performance rights issued in October 2014 | $68.56 | 3 – 4 years | 138,963 | 30,523 |

### 9. 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 2014** | | | | |
| Final – ordinary | 127.0 | 72,469 | 20% Franked | 25 September 2014 |
| **31 December 2013** | | | | |
| Final – ordinary | 127.0 | 72,442 | 30% Franked | 19 September 2013 |

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

### Subsequent events

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

| | Cents per share | Total amount $'000 | Franked/ unfranked | Date of payment |
|---|---|---|---|---|
| Interim – ordinary | 90.0 | 51,374 | 35% Franked | 26 March 2015 |

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 2014 and will be recognised in subsequent financial statements.

### 10. Income taxes

| | 31 Dec 2014 Reported $000 | 31 Dec 2013 Reported $000 | 31 Dec 2013 Patent dispute provision $000 | 31 Dec 2013 Before patent dispute provision $000 |
|---|---|---|---|---|
| **Numerical reconciliation between income tax expense and profit before income tax** | | | | |
| Net profit / (loss) | 71,375 | 21,045 | (15,781) | 36,826 |
| Income tax expense / (benefit) | 23,631 | 1,245 | (6,764) | 8,009 |
| **Profit / (loss) before income tax** | **95,006** | **22,290** | **(22,545)** | **44,835** |
| Income tax expense / (benefit) using the Company's domestic tax rate of 30% (Dec 2013: 30%) | 28,502 | 6,687 | (6,764) | 13,451 |
| **Increase in income tax expense due to:** | | | | |
| Non-deductible expenses | 1,137 | 1,227 | - | 1,227 |
| Effect of tax rate in foreign jurisdictions | (1,460) | (1,295) | - | (1,295) |
| **Decrease in income tax expense due to:** | | | | |
| Research and development allowances | (4,649) | (5,060) | - | (5,060) |
| Share based payment deductions | (373) | (357) | - | (357) |
| | 23,157 | 1,202 | (6,764) | 7,966 |
| Adjustment for prior years | 474 | 43 | - | 43 |
| **Income tax expense on profit before income tax** | **23,631** | **1,245** | **(6,764)** | **8,009** |

## Operating assets and liabilities

### 11. Goodwill

| | $000 |
|---|---|
| Carrying amount at 1 January 2014 | 184,837 |
| Effect of movements in foreign exchange | (14,578) |
| **Carrying amount at 30 June 2014** | **170,259** |
| Carrying amount at 1 July 2014 | 170,259 |
| Effect of movements in foreign exchange | (381) |
| **Carrying amount at 31 December 2014** | **169,878** |

| **12. Provisions** | **31 Dec 2014** | **30 Jun 2014** |
|---|---|---|
| | **$000** | **$000** |
| **Current** | | |
| Employee benefits | 34,197 | 31,065 |
| Warranties | 16,664 | 16,469 |
| Legal and other | 5,720 | 4,465 |
| Product recall | 5,096 | 5,558 |
| **Total current provisions** | **61,677** | **57,557** |
| **Non-current** | | |
| Employee benefits | 5,337 | 5,200 |
| Defined benefit plan | 3,376 | 3,130 |
| Warranties | 7,184 | 5,082 |
| Directors' retirement scheme | 427 | 422 |
| Make good lease costs | 2,138 | 2,139 |
| Product recall | 15,113 | 16,049 |
| Patent dispute | 24,576 | 21,333 |
| **Total non-current provisions** | **58,151** | **53,355** |

**Product recall**

On 11 September 2011, the Company initiated a worldwide voluntary recall of its unimplanted Nucleus CI500 cochlear implant range. Management has made judgments, estimates and assumptions related to probable costs arising from the recall which affect the reported amounts of assets, liabilities, income and expenses. Actual outcomes may differ from these estimates as further information is identified.

No further amount has been recognised as a charge or released as a credit in the half year ended 31 December 2014.

**Patent dispute**

On 24 January 2014, a jury verdict in the patent infringement lawsuit by the Alfred E. Mann Foundation for Scientific Research and Advanced Bionics LLC in the United States District Court in Los Angeles, California was reached. The jury found direct, contributory and wilful, but not induced infringement against Cochlear Limited and its USA subsidiary Cochlear Americas and awarded damages of USD 131.2 million against Cochlear.

No Judgment has been entered based on the verdict as important issues still remain to be decided by the Judge. These decisions may negate some of the findings of the jury and could alter the damages awarded by the jury. The directors have obtained external advice and are of the opinion that the facts and the law do not support the jury's findings and Cochlear has applied to overturn the verdict in post-trial motions filed with the District Court.

A Judgment is pending and the timing for entry of the Judgment is expected in the second half of the 2015 financial year. The lawsuit relates to two (2) expired United States Patents. As a result, the Judgment will not disrupt Cochlear's business or customers in the United States.

The directors will appeal any significant adverse Judgment to the United States Court of Appeals for the Federal Circuit. If an appeal is necessary, Cochlear will provide non-cash security to stay the execution of the Judgment against Cochlear. Providing this security will avoid the requirement for Cochlear to pay the Judgment amount prior to the outcome of the appeal.

A provision of USD 20.0 million was expensed in the half year ended 31 December 2013 in relation to this dispute. 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.

No further amount has been recognised as a charge and the provision remains at USD 20.0 million as at 31 December 2014.

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.

## Financial and capital structure

### 13. Loans and Borrowings

| | 31 Dec 2014 | 30 Jun 2014 |
|---|---|---|
| | **$000** | **$000** |
| **Current** | | |
| Secured bank loans | 3,061 | 3,141 |
| **Total current loans and borrowings** | **3,061** | **3,141** |
| | | |
| **Non-current** | | |
| Secured bank loans | 227,417 | 234,274 |
| **Total non-current loans and borrowings** | **227,417** | **234,274** |

**Unsecured bank overdrafts**

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

**Secured bank loan**

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

**Secured bank loan – multi-option credit facility**

Cochlear has two corporate loan facilities. The first was amended and extended in June 2013 for a period of three years and a total commitment limit of 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 sits at 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 existing 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.

**Bank guarantees**

As at 31 December 2014, Cochlear has other bank guarantee facilities denominated in US dollars, Euros, Pound sterling, India rupees and New Zealand dollars totalling $1.8 million (June 2014: $1.5 million).

## 14. Financial Instruments

### Fair values

The fair values of financial assets and liabilities, together with carrying amounts shown in the balance sheet, are as follows:

| | Note | 31 Dec 2014 | | 30 Jun 2014 | |
|---|---|---|---|---|---|
| | | $000 | $000 | $000 | $000 |
| | | Carrying amount | Fair value | Carrying amount | Fair value |
| Cash and cash equivalents | | 58,871 | 58,871 | 56,127 | 56,127 |
| Trade and other receivables – current | | 227,329 | 227,329 | 214,953 | 214,953 |
| Trade and other receivables – non-current | | 1,061 | 1,061 | 5,505 | 5,505 |
| Trade and other payables – current | | (85,030) | (85,030) | (78,644) | (78,644) |
| Forward exchange contracts – liabilities current | | (24,677) | (24,677) | (6,643) | (6,643) |
| Forward exchange contracts – liabilities non-current | | (11,505) | (11,505) | (2,624) | (2,624) |
| Secured bank loans – current | 13 | (3,061) | (3,061) | (3,141) | (3,141) |
| Secured bank loans – non-current[i] | 13 | (227,417) | (228,000) | (234,274) | (235,000) |
| **Total** | | **(64,429)** | **(65,012)** | **(48,741)** | **(49,467)** |

(i) Included within carrying amount of secured bank loans is an amount of $583,268 (30 June 2014: $725,606) in relation to unamortised loan establishment fees.

### Basis for determining fair values

The following summarises the significant methods and assumptions used in estimating the fair values of financial instruments reflected in the table above.

### Forward exchange contracts

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 a risk free interest rate based upon government bonds. These fair values are provided by independent third parties.

### Non-derivative financial assets and liabilities

The fair value of cash, receivables, payables and short-term borrowings is considered to approximate their carrying amount because of their short maturity.

The directors consider the carrying amount of long-term borrowings recorded in the financial statements approximates their fair value as interest rates on loans and borrowings are variable.

### Fair value hierarchy

The table below analyses financial instruments carried at fair value, by the levels in the value hierarchy. The different levels have been defined as follows:

- 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).

| | Level 2 $000 | Total $000 |
|---|---|---|
| **31 December 2014** | | |
| **Derivative financial assets** | | |
| Forward exchange contracts used for hedging | 2,523 | 2,523 |
| **Total assets** | **2,523** | **2,523** |
| | | |
| **Derivative financial liabilities** | | |
| Forward exchange contracts used for hedging | (36,182) | (36,182) |
| **Total liabilities** | **(36,182)** | **(36,182)** |
| | | |
| **30 June 2014** | | |
| **Derivative financial assets** | | |
| Forward exchange contracts used for hedging | 10,009 | 10,009 |
| **Total assets** | **10,009** | **10,009** |
| | | |
| **Derivative financial liabilities** | | |
| Forward exchange contracts used for hedging | (9,244) | (9,244) |
| Other forward exchange contracts | (23) | (23) |
| **Total liabilities** | **(9,267)** | **(9,267)** |

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

## Other notes

### 15. 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 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.

### 16. 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 2014, see Note 9.

**Cochlear Limited and its controlled entities**
**Directors' Declaration**
**For the half year ended 31 December 2014**

In the opinion of the directors of Cochlear Limited:

1. The financial statements and notes set out on pages 8 to 24 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 2014, 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.

Dated at Sydney this 10th day of February 2015.

Signed in accordance with a resolution of the directors:

Director | Director

# Independent auditor's review report to the members of Cochlear Limited
## For the half year ended 31 December 2014

We have reviewed the accompanying interim financial report of Cochlear Limited, which comprises the consolidated interim balance sheet as at 31 December 2014, 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 16 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 2014 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 2014 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 12 to the interim financial statements which describes the uncertainty related to the outcome of the lawsuit filed against the entity for alleged patent infringement. Our review report is not modified in respect of this matter.

KPMG

KPMG
Sydney, 10 February 2015

Cameron Slapp, Partner