ASX Announcement

19 February 2024

Cochlear Limited Financial Results

For the half year ended December 2023

Sales revenue increased 25% (20% in constant currency*) to $1,113 million, with strong growth in cochlear implants and sound processor upgrades. Cochlear implant units increased 14% driven by the consolidation of recent market share gains and strong market growth across both developed and emerging markets, as well as all age segments. Services revenue increased 35% (29% in CC) driven by strong upgrade demand for the recently released Cochlear™ Nucleus® 8 Sound Processor.

- Sales revenue increased 25% (20% in CC) to $1,113m
- Statutory net profit increased 35% (21% in CC) to $191m
- Underlying net profit** increased 35% (21% in CC) to $192m
- Underlying net profit margin was 17% (18% pre cloud investment), nearing our 18% target
- Strong balance sheet and cash flow generation supports the 29% increase in the interim dividend to $2.00 per share, representing a 68% payout of underlying net profit
- FY24 underlying net profit guidance range upgraded to $385-400m on 8 February, a 26-31% increase on FY23

	HY24	HY23	Change % (reported)	Change % (CC)*
Sales revenue ($m)	1,113.4	892.6	⬆ 25%	⬆ 20%
Underlying net profit ($m)**	**191.8**	**141.6**	**⬆ 35%**	**⬆ 21%**
% Underlying net profit margin**	17%	16%		
% Underlying net profit margin (pre cloud investment)**	18%	17%		
One-off and non-recurring items after-tax ($m)	(0.4)	-		
Statutory net profit ($m)	**191.4**	**141.6**	**⬆ 35%**	**⬆ 21%**
Underlying earnings per share**	$2.92	$2.15	⬆ 36%	⬆ 22%
Interim dividend per share	$2.00	$1.55	⬆ 29%	

*Constant currency (CC) removes the impact of foreign exchange (FX) rate movements to facilitate comparability of operational performance (refer p7).
**Excluding one-off and non-recurring items (refer p7).

Operational review

$m	HY24	HY23	Change % (reported)	Change % (CC)	Sales Mix
Cochlear implants (units)	24,193	21,249	⬆ 14%		
Sales revenue					
Cochlear implants	648.5	513.1	⬆ 26%	⬆ 22%	59%
Services (sound processor upgrades and other)	348.9	258.6	⬆ 35%	⬆ 29%	31%
Acoustics	116.0	120.9	⬆ (4%)	⬆ (9%)	10%
Total sales revenue	**1,113.4**	**892.6**	**⬆ 25%**	**⬆ 20%**	**100%**

Cochlear implants

Cochlear implant units increased 14% to 24,193 units, with strong growth across both developed and emerging markets. Sales revenue increased 26% (22% in CC) to $648.5 million. Sales revenue increased 18% in CC after adjusting for the impact of the technology exchange program in HY23, with around $20 million in revenue deferred from the first to the second half. Comparable average selling price increased around 3% in CC as a result of positive country mix and price increases in some countries.

Developed market units grew around 15% with strong growth across all markets driven by the consolidation of market share gains following the launch of the Nucleus® 8 Sound Processor as well as strong market growth. Implant growth has been strong across all segments – children, adults and seniors. We continue to see an improving trend in adult referral rates in key markets, in part driven by initiatives to improve awareness and access for adult cochlear implant candidates.

Emerging market units grew around 10% with strong growth across a broad range of countries including China, India, Central Europe and the Middle East.

Services

Services revenue increased 35% (29% in CC) to $348.9 million, with strong uptake of the new sound processor across the developed markets. Emerging markets also performed well with growing rates of sound processor upgrade penetration across many markets.

Acoustics

Acoustics revenue decreased 4% (down 9% in CC) to $116.0 million with lower demand for Cochlear™ Baha® 6 Max Sound Processors following three years of strong upgrade demand. The 3 Tesla MRI compatible Cochlear™ Osia® 2 System was launched in the US late in the half, with strong demand from December.

Financial review

We delivered sales revenue of $1,113 million, an increase of 25% (20% in CC), driven by strong growth in cochlear implants and sound processor upgrades.

The gross margin was 74%, a point below last year and our 75% longer-term target. The gross margin decline was driven by inventory write-downs and the commencement of production at Chengdu which offset the benefit of improved average selling price. Operating expenses increased 19% (16% in CC) reflecting growing investment in R&D and market growth activities.

Cloud computing-related investment of $17 million was in line with the prior half year and forms part of the around $150 million investment being made in cloud-based technology solutions, with around $80 million invested since FY21.

Underlying net profit increased 35% (21% in CC) to $192 million. The underlying net profit margin was 17% (18% excluding the impact of cloud computing-related expenses), and is a point below our 18% longer-term target.

The balance sheet remains strong with net cash of $485 million, with operating cash flows sufficient to fund investing activities and capital expenditure whilst delivering dividends to shareholders. An interim dividend of $2.00 per share has been determined, an increase of 29% on last year and representing a payout of 68% of underlying net profit.

FY24 outlook

As we look to the future, we remain confident of the opportunity to grow our markets. There remains a significant, unmet and addressable clinical need for cochlear and acoustic implants that is expected to continue to underpin the long-term sustainable growth of the business. Our clear growth opportunity and strategy, combined with a strong balance sheet, mean we are well placed to create value for our stakeholders now, and over the long term.

For FY24, we expect the positive momentum of the first half to continue into the second half and on 8 February increased underlying net profit guidance to $385-400 million, which represents a 26-31% increase on FY23. The upgrade was 8% above the midpoint of the prior guidance of $355-375 million advised in August 2023. We expect profit growth to be driven by a combination of revenue growth and improved net profit margin.

Cochlear implant trading conditions continue to be strong across most markets, with an improving trend in adult referral rates in many developed countries. We have maintained the market share gains made in FY23, with strong market growth across the first half. The key change to our expectations is that we now expect to achieve 10-15% growth in our cochlear implant units for FY24 compared to the high single-digit growth expected in August.

The Services segment is growing strongly with strong demand for upgrades to the Nucleus® 8 Sound Processor.

Acoustics growth rates are expected to be lower than FY23, with continuing growth from the rollout of the Osia® 2 System to be moderated by a smaller contribution from upgrades to the Baha® 6 Max Sound Processor. The new 3 Tesla MRI compatible Osia® 2 System has just been launched in the US and expected to be progressively launched across the rest of the world as regulatory approvals are obtained.

We are continuing our investment in R&D and market growth activities to support long-term market growth, with an anticipated investment of around 12% of sales revenue in R&D.

Cloud computing-related investment is expected to be around $34 million ($24 million after tax) in FY24.

Guidance is based on a 66 cent AUD/USD, a cent below the 67 cents guided in August (67.5 cent average in FY23) and a 61 cent AUD/EUR (64.4 cent average in FY23).

Capital expenditure is expected to be $70-90 million.

The Board maintains a dividend policy that targets a 70% payout of underlying net profit.

The on-market share buyback is being paused given the current high interest rate environment. $73 million in shares have been repurchased since the buyback commenced in March 2023.

Guidance does not factor in any impact from the proposed acquisition of Oticon Medical, which is targeted to complete by the end of June 2024, with integration costs currently estimated at $30 million.

Detailed financial review

Profit and loss

$m	HY24	HY23	Change % (reported)	Change % (CC)
Sales revenue	**1,113.4**	**892.6**	**25%**	**20%**
Cost of sales	**285.8**	**226.9**	**26%**	**25%**
% Gross margin	*74%*	*75%*		
Selling, marketing and general expenses	330.5	275.4	20%	16%
Research and development expenses	127.3	102.6	24%	21%
% of sales revenue	*11%*	*11%*		
Administration expenses (excluding cloud investment)	84.6	76.2	11%	11%
Administration expenses (cloud investment)	16.9	17.3	(2%)	(2%)
Operating expenses	**559.3**	**471.5**	**19%**	**16%**
Other income / (expenses)	1.9	(1.1)		
FX contract gains losses	(14.9)	(7.4)		
EBIT (underlying)*	**255.3**	**185.7**	**37%**	**23%**
*% EBIT margin**	*23%*	*21%*		
Net finance income	5.1	2.0		
Income tax expense*	(68.6)	(46.1)		
% Effective tax rate	*26%*	*25%*		
Underlying net profit*	**191.8**	**141.6**	**35%**	**21%**
*% Underlying net profit margin**	*17%*	*16%*		
*% Underlying net profit margin (pre cloud investment)**	*18%*	*17%*		
One-off and non-recurring items (after-tax):				
Share of losses on equity-accounted investments	(0.4)	-		
Statutory net profit	**191.4**	**141.6**	**35%**	**21%**

* Excluding one-off and non-recurring items (refer p7).

Sales revenue increased 25% (20% in CC) to $1,113.4 million and underlying net profit increased 35% (21% in CC) to $191.8 million. Statutory net profit increased 35% to $191.4 million.

Key points of note:

- Cost of sales increased 26% (25% in CC) to $285.8 million. The gross margin declined by one percentage point to 74%, below our long-term target gross margin of 75%. The gross margin decline was driven by inventory write-downs and the commencement of production at Chengdu which offset the benefit of improved average selling price. A $15.6 million write-down in the value of inventories largely relates to components for older generation products which are being progressively obsoleted;
- Selling, marketing and general expenses increased 20% (16% in CC) to $330.5 million reflecting continued investment in market growth activities, standard of care and market access initiatives;
- Investment in R&D increased 24% (21% in CC) to $127.3 million with continued investment made in key R&D projects and development of the product and services pipeline; and
- Administration expenses (excluding cloud investment) increased 11% to $84.6 million primarily driven by increases in IT licensing and people costs.

Cash flow

$m	HY24	HY23	Change
EBIT (underlying)	255.3	185.7	69.6
Depreciation and amortisation	43.1	37.3	5.8
Increase in working capital and other	(84.0)	(85.3)	1.3
Net interest received	5.1	2.0	3.1
Income taxes paid	(62.4)	(50.6)	(11.8)
Operating cash flow	**157.1**	**89.1**	**68.0**
Capital expenditure	(42.7)	(42.7)	-
Other net investments	(5.1)	(17.9)	12.8
Free cash flow	**109.3**	**28.5**	**80.8**
Outlay from exercise of share options and performance rights	(2.4)	-	(2.4)
Payments for share buyback	(43.0)	-	(43.0)
Dividends paid	(114.7)	(95.4)	(19.3)
Payment of lease liability and other	(19.5)	(14.4)	(5.1)
Decrease in net cash	**(70.3)**	**(81.3)**	**11.0**

Operating cash flow increased $68.0 million to $157.1 million, with free cash flow increasing $80.8 million to $109.3m.

Key points of note:

- EBIT (underlying) increased $69.6 million as a result of strong business performance;
- Capital expenditure (capex) was in line with last year and includes investment in the upgrade of the Lane Cove facility and stay-in-business capex; and
- Payments for share buyback reflects the $43.0 million outlay for the repurchase of ordinary shares as part of the on-market share buyback.

Capital employed

$m	Dec23	Jun23	Change
Trade receivables	379.3	388.4	(9.1)
Inventories	321.5	311.5	10.0
Less: Trade payables	(247.1)	(270.4)	23.3
Working capital	**453.7**	**429.5**	**24.2**
*Working capital / sales revenue**	*20%*	*22%*	
Property, plant and equipment	279.7	276.7	3.0
Intangible assets	458.7	444.1	14.6
Investments and other financial assets	155.2	188.1	(32.9)
Other net liabilities	(50.7)	(145.1)	94.4
Capital employed	**1,296.6**	**1,193.3**	**103.3**
Funding sources:			
Equity	1,781.8	1,748.8	33.0
Less: Net cash	(485.2)	(555.5)	70.3
Capital employed	**1,296.6**	**1,193.3**	**103.3**

* Dec23 calculation based on doubling HY24 sales revenue.

Capital employed increased $103.3 million to $1,296.6 million since June 2023.

Key points of note:

- Working capital increased $24.2 million, declining from 22% to 20% of sales;
- Investments and other financial assets decreased $32.9 million to $155.2 million, primarily reflecting the revaluation of investments in Nyxoah and Seer;
- Other net liabilities decreased $94.4 million to $50.7 million, and includes $39.9 million reduction in employee benefit liabilities, following the payment of cash incentives, and an increase in prepayments and other receivables; and
- Net cash decreased $70.3 million to $485.2 million.

Dividends

	HY24	HY23	Change %
Interim ordinary dividend (per share)	$2.00	$1.55	29%
% Payout ratio (based on underlying net profit)	68%	72%	
% Franking	70%	35%	

An interim dividend of $2.00 per share has been determined, an increase of 29% on last year and representing a payout of 68% of underlying net profit. The interim dividend is franked at 70%.

The ex-dividend date is 21 March 2024. The record date for calculating dividend entitlements is 22 March 2024 with the interim dividend expected to be paid on 15 April 2024.

Notes

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 is not placed on any forward-looking statement.

Non-International Financial Reporting Standards (IFRS) financial measures

Cochlear uses non-IFRS financial measures to assist readers in better understanding Cochlear's financial performance. Cochlear uses three non-IFRS measures in this document: Sales revenue, Underlying net profit and Constant currency. The directors believe the presentation of these non-IFRS financial measures are useful for the users of this document as it reflects the underlying financial performance of the business. Each of these measures is described below in further detail including reasons why Cochlear believes these measures are of benefit to the reader.

These non-IFRS financial measures have not been subject to review or audit. However, Cochlear's external auditor has separately undertaken a set of procedures to agree the non-IFRS financial measures disclosed to the books and records of the group.

Sales revenue

Sales revenue is the primary revenue reporting measure used by Cochlear for the purpose of assessing revenue performance of the Consolidated Entity. It represents total revenue excluding foreign exchange contract gains/losses on hedged sales.

Underlying net profit

Underlying net profit allows for comparability of the underlying financial performance by removing one-off and non-recurring items. The determination of items that are considered one-off or non-recurring are made after consideration of their nature and materiality and is applied consistently from period to period. Underlying net profit is used as the basis on which the dividend payout policy is applied. The Financial Review section includes a reconciliation of Underlying net profit (non-IFRS) to Statutory net profit (IFRS) which details each item excluded from Underlying net profit.

Constant currency

Constant currency removes the impact of foreign exchange rate movements to facilitate comparability of operational performance for Cochlear. This is done by converting the prior comparable period net profit of entities in the group that use currencies other than Australian dollars at the rates that were applicable to the current period (translation currency effect) and by adjusting for current year foreign currency gains and losses (foreign currency effect). The sum of the translation currency effect and foreign currency effect is the amount by which EBIT and net profit is adjusted to calculate the result at constant currency.

Reconciliation of constant currency net profit

$m	HY24	HY23	Change %
Underlying net profit	**191.8**	**141.6**	**35%**
FX contract movement		(7.5)	
Spot exchange rate effect to sales revenue and expenses*		20.0	
Balance sheet revaluation*		4.1	
Underlying net profit (CC)	**191.8**	**158.2**	**21%**
One-off net gains / (losses)	(0.4)	-	
Statutory net profit (CC)	**191.4**	**158.2**	**21%**

* HY24 actual v HY23 at HY24 rates.

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