Demant

# Annual Report 2018

*19 February 2019*


Søren Nielsen, President & CEO

René Schneider, CFO

# Agenda

# William Demant Holding

changes name to

Demant

# Attractive growth in hearing healthcare

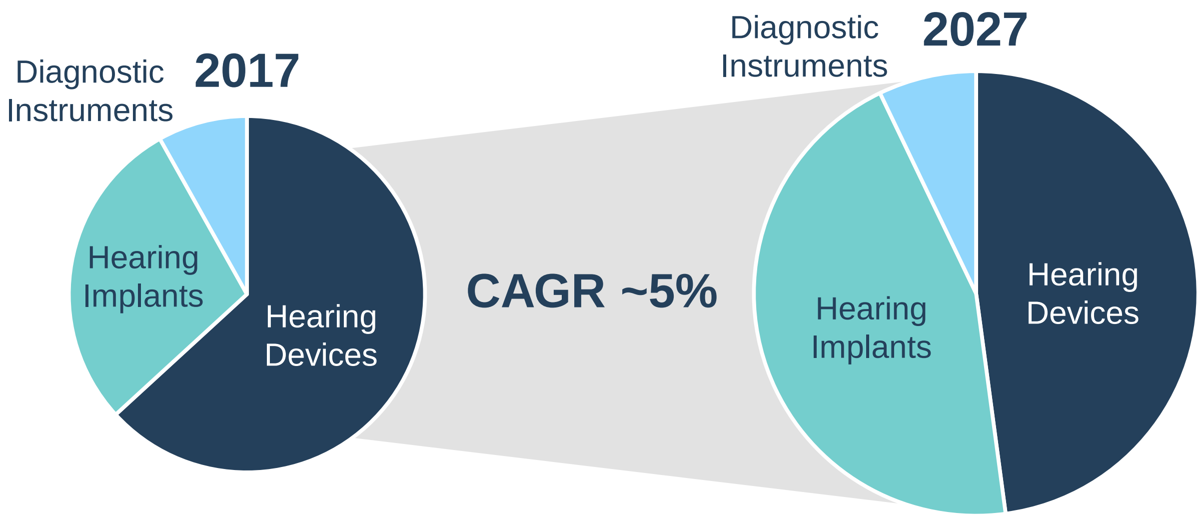
**Structural growth drivers**
- Baby-boomers in developed markets
- Ageing population across the world

**Hearing care is healthcare**
- Hearing loss may accelerate cognitive decline and lead to social isolation
- Biggest modifiable risk factor related to dementia

**Hearing Devices**
2-4%

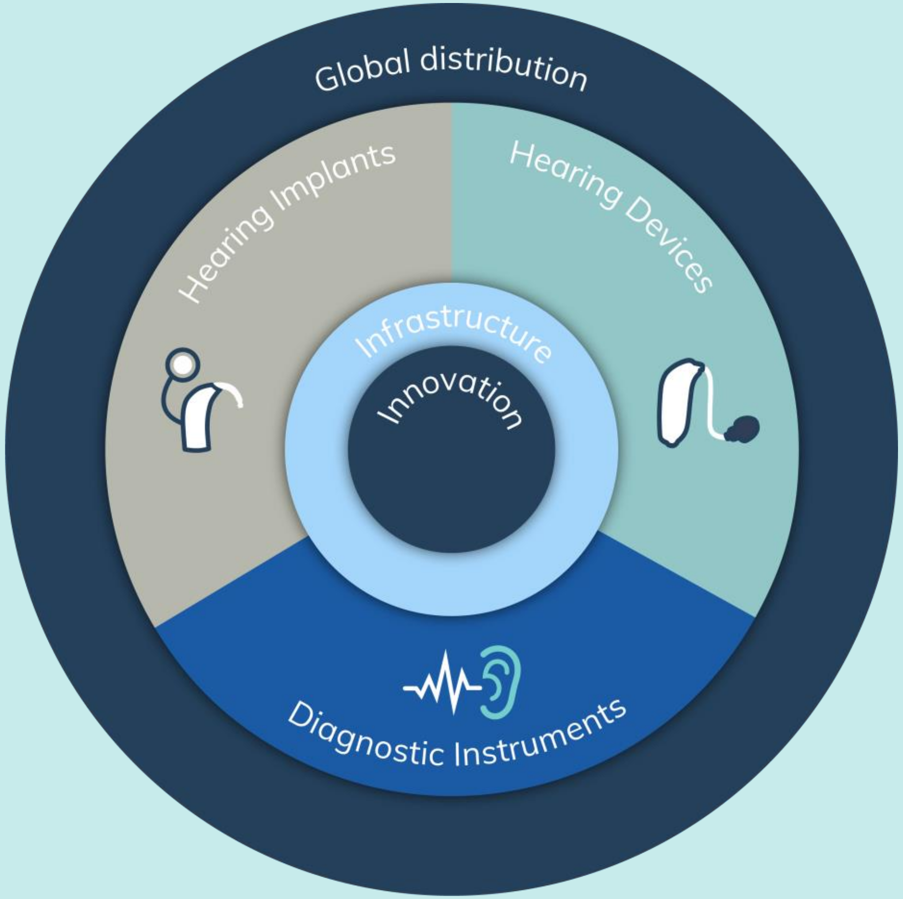
**Hearing Implants**
10-15%

**Diagnostic Instruments**
3-5%




*Note: Wholesale values*

# Strategic ambition




Demant

# Life-changing hearing health

# 2018 highlights

Demant

# 2018 highlights

9% Strong revenue growth of 9% in local currencies with substantial organic sales growth of 7%

9% organic growth in wholesale business and market share gains in value despite slowdown towards end of year – product portfolio to be expanded with new premium products based on new platform

9% growth in local currencies in hearing aid retail business driven by acquisitive growth of 8% and organic growth of 1% with material differences between markets

Underlying organic growth of 10% in Hearing Implants driven by roll-out of Neuro 2 (adjusted for decision to reduce activity level in select cochlear implants markets with lower prices). Reported organic growth was 5%

Exceptional organic growth of 12% in Diagnostic Instruments and continued market share gains

Unprecedented level of resources used for R&D and digitalisation to drive future growth

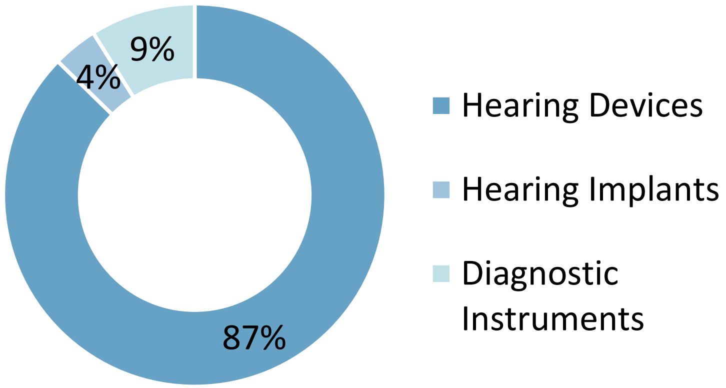
8% 8% growth in reported EBIT to DKK 2,532 million. 6% growth in adjusted EBIT to DKK 2,652 million (vs. guidance range of DKK 2.65-2.85 billion, originally DKK 2.55-2.85 billion)

Outlook 2019: Reported EBIT of DKK 2.65-2.95 billion and share buy-backs worth a minimum of DKK 1.2 billion

Demant

# Revenue by business activity

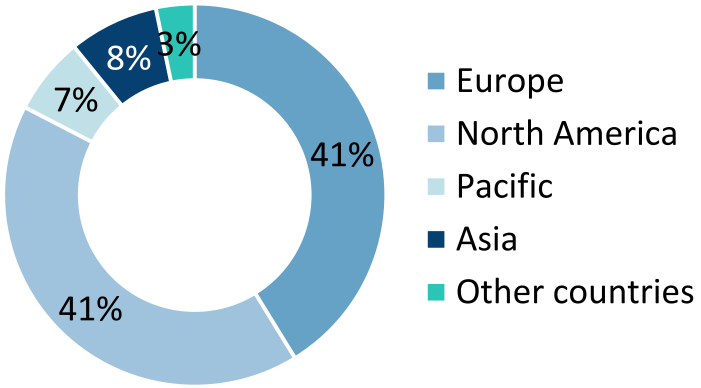
| DKK million | 2018 | 2017 | Change DKK | Change LCY | Change Organic |
|---|---|---|---|---|---|
| Hearing Devices | 12,129 | 11,495 | 5% | 9% | 6% |
| - Wholesale | | | 6% | 9% | 9% |
| - Retail | | | 6% | 9% | 1% |
| Hearing Implants | 509 | 500 | 2% | 5% | 5% |
| Diagnostic Instruments | 1,299 | 1,194 | 9% | 12% | 12% |
| **Total** | **13,937** | **13,189** | **6%** | **9%** | **7%** |




- Group revenue growth of 9% in local currencies (7% organic and 2% acquisitive)
- Organic growth in all business activities, particularly in hearing aid wholesale business and Diagnostic Instruments
- Acquisitive growth almost entirely related to hearing aid retail business
- Negative exchange rate effect of 3% resulting in reported revenue growth of 6%

# Revenue by geography

| DKK million | 2018 | 2017 | Change DKK | Change LCY | Change Organic |
|---|---|---|---|---|---|
| Europe | 5,745 | 5,437 | 6% | 6% | 5% |
| North America | 5,766 | 5,358 | 8% | 12% | 8% |
| Pacific | 911 | 946 | -4% | 3% | 1% |
| Asia | 1,059 | 960 | 10% | 14% | 14% |
| Other countries | 456 | 488 | -7% | 1% | 1% |
| **Total** | **13,937** | **13,189** | **6%** | **9%** | **7%** |




- Strong organic growth in North America driven by hearing aid wholesale and Diagnostic Instruments
- Solid organic growth in Europe led by France and Spain
- Strong organic growth in Asia driven by high sales in China and Japan

# Update on business activities

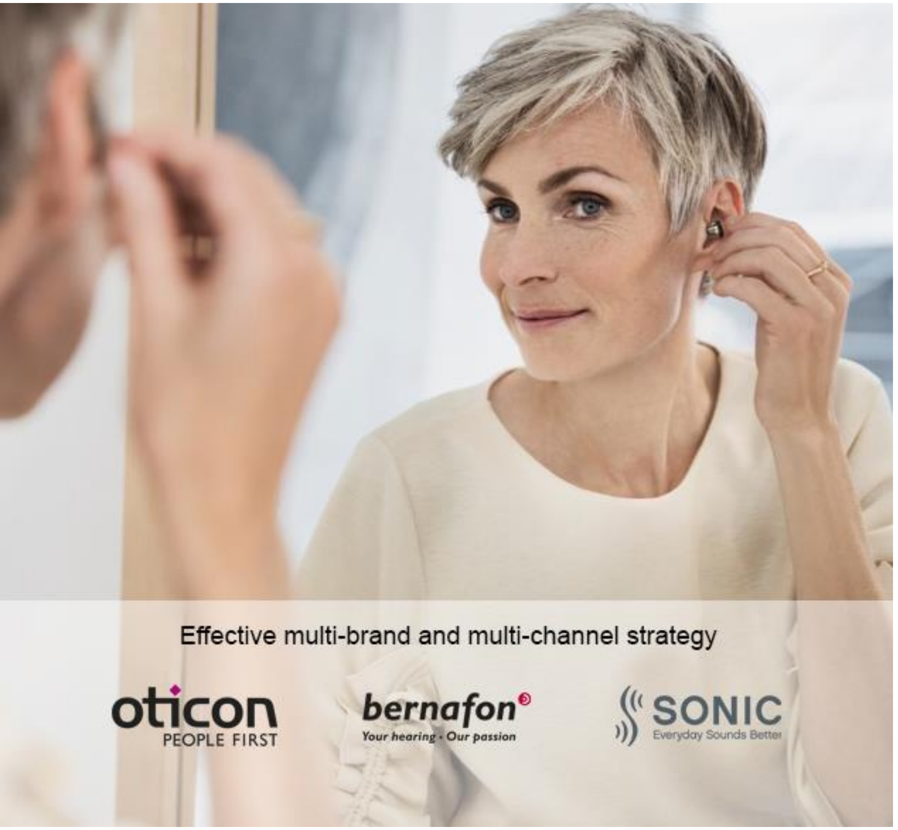
# The global hearing aid market in 2018

We estimate that the global hearing aid market grew by approx. 5% in 2018 in units, which is in line with our general expectation of 4-6% unit growth per year

- US a key driver with 5% unit growth (6% in commercial market, 2% in Veterans Affairs)
- Growth in Europe around 4% with solid growth in Germany and France partly offset by negative growth in NHS
  - Growth in France accelerated in Q4 2018 due to new reimbursement effective in 2019
- Modest growth in Japan and Australia and presumably double-digit growth in China
- Estimate flat to slightly negative wholesale ASP and overall value growth at high end of general expectation of 2-4%

| Market in 2018 | Unit growth | ASP growth |
|---|---|---|
| Hearing aid wholesale | ~5% | Flat to slightly negative |
| Hearing aid retail | | Relatively stable |

# Continued market share gains with 9% organic growth in hearing aid wholesale




- Growth driven by strong products based on world-leading technological and audiological innovation
- Portfolios significantly expanded in 2018 with new styles and more price points in all brands
- Significant growth in North America driven by the US with increasing sales to independents, VA and own retail network
- France key driver behind solid growth in Europe despite loss of sales to large customer acquired by a competitor and negative growth in the NHS
- High growth in Asia led by China and Japan

# A year of significant mix changes

- Organic growth of 11% in H1 slowed to 7% in H2 due to an increasingly competitive environment in the premium segment towards end of the year
  - Launched in June 2016, Opn represents a breakthrough in audiology based on very strong platform but now at end of life-cycle

- Significant mix changes driving increase in ASP
  - Improved product, geography and channel mix
  - Increased sales of rechargeable solutions and other accessories

Demant

# Unit and ASP growth in 2018

- Unit and ASP growth in 2018 was materially impacted by three factors with effect in H1
  - Loss of sales to a large customer in late H1 2017 (acquired by a competitor)
  - Two large but low-priced tenders in comparative period
  - Negative growth in the large public channel in the UK, NHS
- Adjusted for these factors, unit and ASP growth for 2018 was balanced at 5% each

| Reported | H1 2018 | H2 2018 | FY 2018 |
|---|---:|---:|---:|
| Unit growth | -5% | 4% | 0% |
| ASP growth | 17% | 2% | 9% |
| Total growth | 11% | 7% | 9% |

| Underlying* | H1 2018 | H2 2018 | FY 2018 |
|---|---:|---:|---:|
| Unit growth | 6% | 4% | 5% |
| ASP growth | 8% | 2% | 5% |
| Total growth | 15% | 7% | 10% |

** H1 and FY 2018 adjusted for three factors with material impact in H1 2018 (no adjustment made for H2 2018)*

Demant

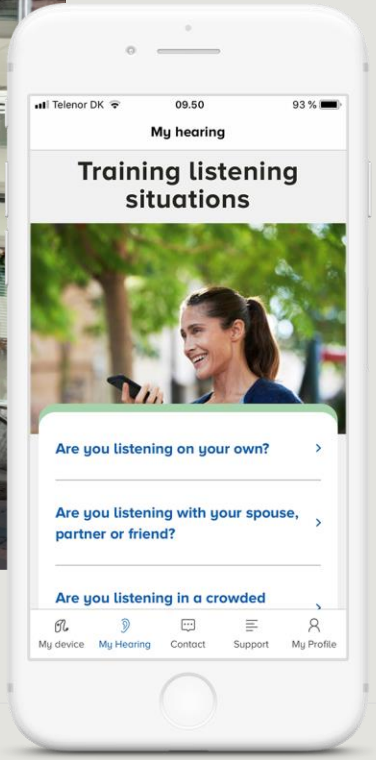
# Growth of 9% in local currencies in retail

- Growth driven by acquisitions, mainly related to a US-based retail network previously recognised as investments in associates
- Low organic growth with material differences between our markets
  - Strong organic growth in France where we have a strong operating model and unique brand (Audika)
  - US organic growth negative in H1 2018 – improvement in H2 less significant than expected
  - Australia impacted by lower efficiency in marketing and lead-generation, partly due to ACCC* ordering the discontinuation of main marketing campaign in H2



** Australian Competition and Consumer Commission*

# Investing in branding and digitalisation


- Audika established as leading brand in many European markets and gradually harmonising brands in other regions
- Digitalisation key to drive growth
  - Digital lead-generation
  - Call centres
  - End-user app
  - One global IT platform
- Significant investments in IT and store refurbishments

Demant

# 10% underlying growth in Hearing Implants

On a reported basis, organic growth was 5%

## Cochlear implants (CI)

- Successful launch of Neuro 2, the world’s smallest sound processor, with improved momentum in key European markets
- Almost concluded upgrade of existing Neuro One users to unique Neuro 2
- Growth exceeded estimated market growth of 10-12% when adjusting for decision to reduce activity level in select markets with lower prices

## Bone anchored hearing systems (BAHS)

- Modest growth driven by Ponto 3
  - Slightly above market growth, which we estimate was flat in 2018
- Towards end of H1 2019, our BAHS business will introduce a new Ponto sound processor based on a brand new platform, offering superior audiology and a range of improved functionalities.


# Continued market share gains in Diagnostic Instruments


- Exceptional performance with organic growth of 12%
    - Market growth estimated at approx. 5%
- Growth broadly based across brands and product categories with particularly strong growth in
    - Newborn hearing screening
    - Hearing fitting equipment
    - Balance equipment
    - Service business

Demant

# Growth of 46% in Personal Communication

- Our 50/50 joint venture, Sennheiser Communications, grew reported revenue by 46%
  - Enterprise Solutions, Gaming and Mobile Music segments all contributed to growth
  - Underlying revenue increased by 25% (i.e. sales from inventory to customers)
- Material improvement in contribution to Group EBIT from DKK 43 million to DKK 104 million
- Preparation for separation of joint venture from 1 January 2020 progressing according to plan

# Strategic Group initiatives ended in 2018

- All strategic initiatives announced in 2016 completed at end of 2018 according to plan
  - Very satisfied with improvements in efficiency and scalability realised since 2016
  - Annual cost savings of DKK 200 million from 2019 – partly reinvested in R&D
- Continuous efficiency improvements going forward
  - Will no longer report financial figures adjusted for restructuring costs

| Major initiatives |
|---|
| • Transferring activities from production site in Thisted, Denmark, to Poland<br>• Closing down facility in Eagan, USA<br>• Ramping up custom instrument, service and repair activities in Mexico<br>• Transferring R&D activities in Switzerland to Denmark and Poland, including opening new software development site in Warsaw, Poland |

| Realised (DKK million) | 2016 | 2017 | 2018 | Total |
|---|---|---|---|---|
| Restructuring costs | 188 | 166 | 120 | 474 |
| Cash flow impact | 77 | 151 | 82 | 310 |

| Realised (DKK million) | 2016 | 2017 | 2018 | 2019 |
|---|---|---|---|---|
| Annual cost savings (2016 cost base) | - | ~100 | ~150 | ~200 |

# Financial update

Demant

# Adjusted income statement

| (DKK million) | Reported 2018 | Restruc. costs | Adjusted 2018 | Reported 2017 | Restruc. costs | Adjusted 2017 | Growth (reported) | Growth (adjusted) |
|---|---|---|---|---|---|---|---|---|
| Revenue | 13,937 | 0 | 13,937 | 13,189 | 0 | 13,189 | 6% | 6% |
| Production costs | -3,153 | -41 | -3,112 | -3,163 | -38 | -3,125 | 0% | 0% |
| **Gross profit** | **10,784** | **-41** | **10,825** | **10,026** | **-38** | **10,064** | **8%** | **8%** |
| *Gross profit margin* | *77.4%* | | *77.7%* | *76.0%* | | *76.3%* | | |
| R&D costs | -1,009 | -15 | -994 | -919 | -63 | -856 | 10% | 16% |
| Distribution costs | -6,616 | -37 | -6,579 | -6,095 | -38 | -6,057 | 9% | 9% |
| Administrative expenses | -761 | -27 | -734 | -727 | -27 | -700 | 5% | 5% |
| Share of profit after tax, associates and JVs | 134 | 0 | 134 | 53 | 0 | 53 | 153% | 153% |
| **Operating profit (EBIT)** | **2,532** | **-120** | **2,652** | **2,338** | **-166** | **2,504** | **8%** | **6%** |
| *Operating profit margin (EBIT margin)* | *18.2%* | | *19.0%* | *17.7%* | | *19.0%* | | |

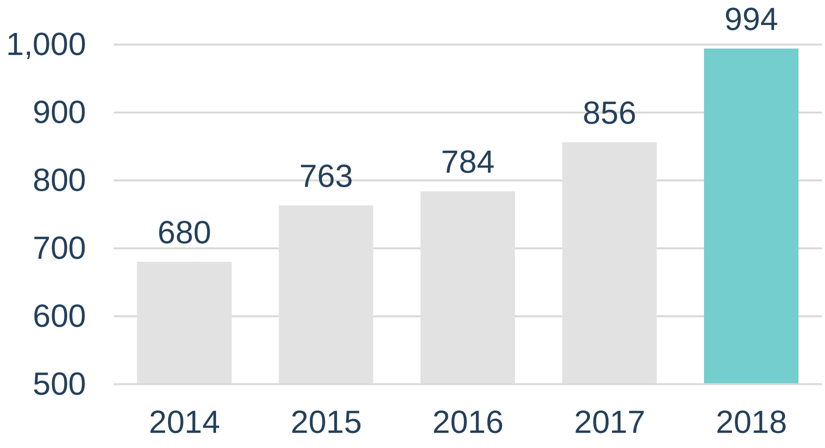
# Development in capacity costs

- Increase in R&D costs driven by ambitions within software and connectivity solutions and further digitalisation of our business
- Distribution costs primarily driven by retail and roughly evenly split between organic and acquisitive growth
- Administrative expenses reflects increased activity level as well as expansion of financial shared service centre

**Capacity costs – DKK million***

| (DKK million) | 2018 | 2017 | Change DKK | Change LCY |
|---|---|---|---|---|
| R&D costs | 994 | 856 | 16% | 17% |
| Distribution costs | 6,579 | 6,057 | 9% | 12% |
| Administrative expenses | 734 | 700 | 5% | 7% |
| **Total capacity costs** | **8,307** | **7,613** | **9%** | **12%** |

**R&D costs – DKK million***




** The figures for 2015-2018 are shown on an adjusted basis.*

Demant

# Solid underlying development

| DKK million | Reported | | | Restructuring | | Adjusted | | | Transaction | | Translation | | Underlying / LCY | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **2017** | **2018** | **%** | **2017** | **2018** | **2017** | **2018** | **%** | **2017** | **2018** | **2017** | **2018** | **2017** | **2018** | **%** |
| Revenue | 13,189 | 13,937 | *6%* | *0* | *0* | 13,189 | 13,937 | *6%* | 49 | 21 | 368 | 0 | 12,772 | 13,917 | *9%* |
| EBIT | 2,338 | 2,532 | *8%* | -166 | -120 | 2,504 | 2,652 | *6%* | -43 | 7 | 78 | 0 | 2,469 | 2,644 | *7%* |
| *EBIT margin* | *17.7%* | *18.2%* | | | | *19.0%* | *19.0%* | | | | | | *19.3%* | *19.0%* | |

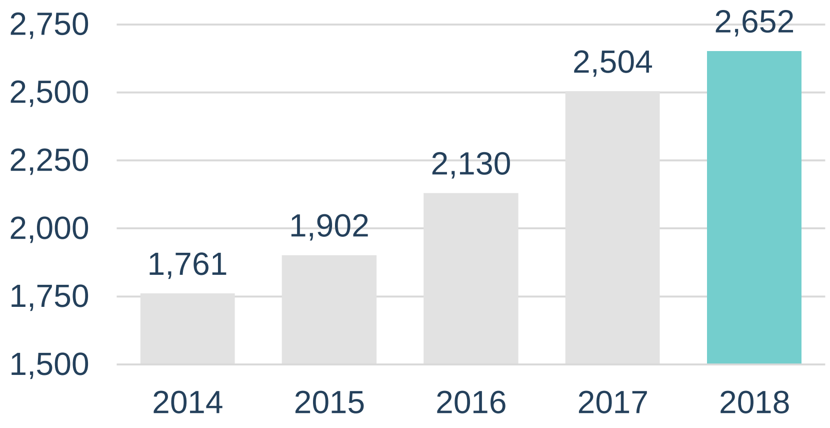
- Revenue and EBIT for 2017 restated to reflect exchange rates in 2018
  - Material translational impact on revenue and EBIT for 2017
  - 9% growth in underlying revenue and 7% growth in underlying EBIT
  - Underlying EBIT margin for 2018 0.3 percentage points lower than 2017

Demant

# Continued growth in EBIT and EPS

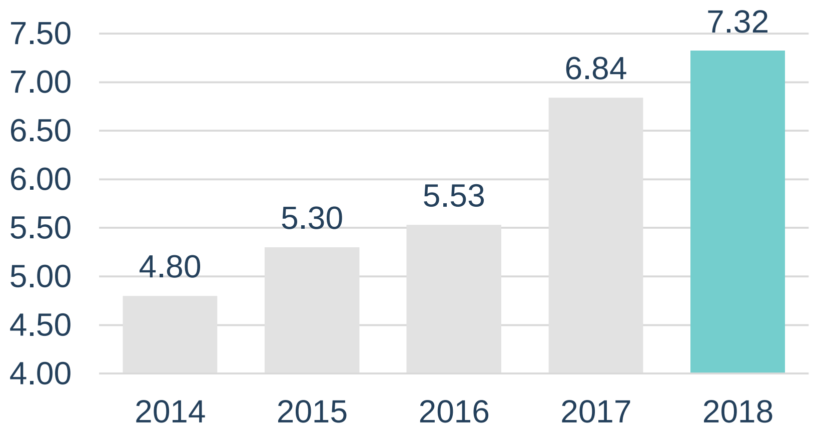
- Reported EBIT growth of 8% and adjusted EBIT growth of 6%
  - Driven by growth and operating leverage in hearing aid wholesale business and Diagnostic Instruments
  - Weighed down by low organic growth in hearing aid retail business
- EPS growth of 7% in 2018
- Reported EBIT and EPS CAGR of 11% since 2014

**Operating profit (EBIT) – DKK million***




** The figures for 2015-2018 are shown on an adjusted basis.*

**Earnings per share (EPS) – DKK**



Demant

# Cash flow by main items

| (DKK million) | 2018 | 2017 | Growth |
|---|---|---|---|
| **Adjusted operating profit** | **2,652** | **2,504** | **6%** |
| **Adjusted cash flow from operating activities** | **1,765** | **2,023** | **-13%** |
| Cash flow from restructuring costs | -82 | -151 | -46% |
| **Reported cash flow from operating activities** | **1,683** | **1,872** | **-10%** |
| Cash flow from investing activities | -498 | -485 | 3% |
| **Reported free cash flow** | **1,185** | **1,387** | **-15%** |
| Acquisition and divestment of enterprises, participating interests and activities | -940 | -656 | 43% |
| Buy-back of shares | -1,751 | -1,031 | 70% |
| Other financing activities | 1,123 | 265 | 324% |
| **Cash flow for the period** | **-383** | **-35** | **994%** |

- Cash flow from operating activities negatively impacted by low inventory levels at beginning of the year, product launch preparations and timing of tax payments
- Material increase in cash flow from acquisitions due to increase in ownership of US-based retail network previously recognised as investments in associates
- Settlement of loans issued to acquired entities prior to acquisition has been reclassified compared to Interim Report 2018

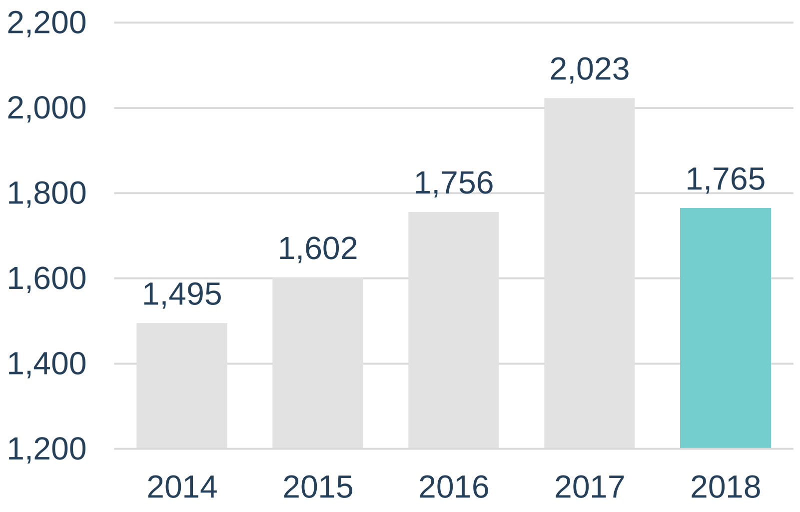
# Extraordinary operating cash flow impacts

- Adjusted cash flow from operating activities decreased by 13%

- Increase in net working capital
  - Low inventory levels at the beginning of the year (~DKK 70 million)
  - Preparation for upcoming product launches

- Tax payments made in 2018 relating to 2017 and 2019 (~DKK 80 million)

**Cash flow from operating activities (CFFO) – (DKK million)***

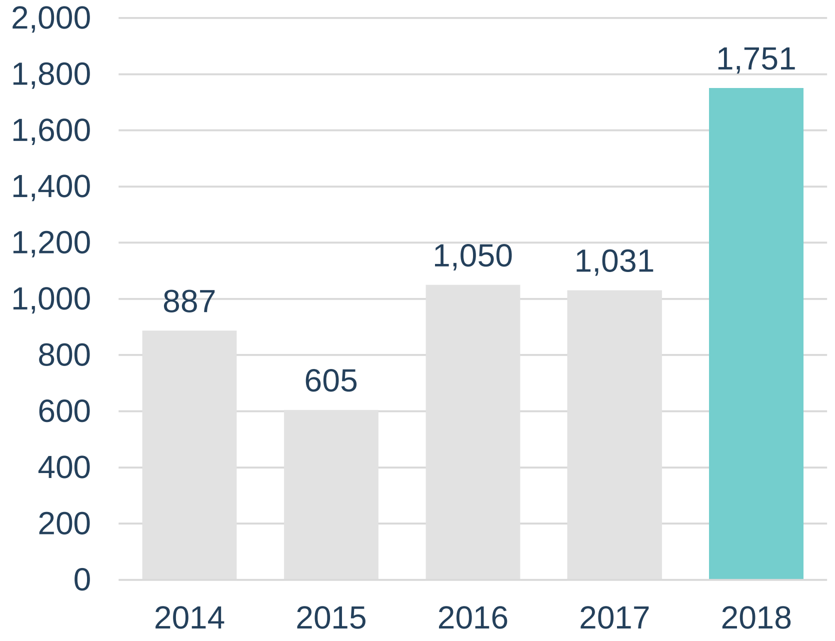



** The figures for 2015-2018 are shown on an adjusted basis.*

Demant

# Share buy-backs in line with guidance

**Share buy-backs – DKK million**




- Share buy-backs increased by 70% in 2018 to DKK 1,751 million
- 7.6 million shares bought at average price of DKK 230.30
- In line with guidance for DKK 1.5-2.0 billion

Demant

# Balance sheet by main items

| (DKK million) | 2018 | 2017 | Growth |
|---|---|---|---|
| Non-current assets | 11,930 | 10,882 | 10% |
| Inventories | 1,641 | 1,351 | 21% |
| Trade receivables | 2,763 | 2,573 | 7% |
| Cash | 630 | 697 | -10% |
| Other current assets | 971 | 719 | 35% |
| **Total assets** | **17,935** | **16,222** | **11%** |
| Equity | 7,059 | 7,433 | -5% |
| Non-current liabilities | 3,390 | 3,086 | 10% |
| Trade payables | 499 | 516 | -3% |
| Other current liabilities | 6,987 | 5,187 | 35% |
| **Total equity and liabilities** | **17,935** | **16,222** | **11%** |

- Growth in total assets of 11% driven by goodwill from acquisitions
- Total equity decreased by 5% driven by share buy-backs
- Increase in net working capital of 27% driven by increased inventory levels from a low level at the beginning of the year
- Net interest-bearing debt (NIBD) increased by 45% to DKK 5,835 million
- Gearing multiple (NIBD/EBITDA) of 2.0x

# Estimated impacts of IFRS 16

- Implemented with effect from 2019 (comparative figures not re-stated)
- Nearly all leases recognised on balance sheet, i.e. material impact on financial statement (see note 9.1 in Annual Report 2018)

| (DKK million) | 2018 reported | IFRS 16 impact* |
|---|---|---|
| **P&L (DKK million):** | | |
| EBITDA | 2,978 | ~500 |
| EBIT | 2,532 | Minor positive |
| Profit before tax | 2,368 | Minor negative |
| **Cash flow (DKK million):** | | |
| CFFO / FCF | 1,765 / 1,185 | ~500 *less* minor interest |
| CFFF | -628 | ~-500 *plus* minor interest |
| **Balance sheet (DKK million):** | | |
| Total assets/total liabilities | 17,935 | ~2,000 |
| Net interest-bearing debt (NIBD) | 5,835 | ~2,000 |
| **Financial ratios:** | | |
| Gearing (NIBD/EBITDA) | 2.0x | 0.3x |

** The impact from IFRS 16 is the estimated impact for 2019*

# Reclassification of cash acquisition cost in H1 2018

- Settlement of loans issued to acquired entities prior to acquisition has been reclassified compared to Interim Report 2018
  - Previously offset in the reported cash acquisition cost
  - Now part of investing activities (non-current assets)
- Decrease of DKK 291 million in cash flow from investing activities and corresponding increase in cash flow from acquisitions in H1 2018
- No effect for H2 2018

| (DKK million) | H1 2018 (old) | H1 2018 (new) | H2 2018 | FY 2018 |
|---|---|---|---|---|
| **Reported cash flow from operating activities** | **996** | **996** | **687** | **1,683** |
| Cash flow from investing activities | -341 | -50 | -448 | -498 |
| **Reported free cash flow** | **655** | **946** | **239** | **1,185** |
| Acquisition and divestment of enterprises, participating interests and activities | -494 | -785 | -155 | -940 |
| Buy-back of shares | -902 | -902 | -849 | -1,751 |
| Other financing activities | 549 | 549 | 574 | 1,123 |
| **Cash flow for the period** | **-192** | **-192** | **-191** | **-383** |

Demant

# Consolidation of Sennheiser Communication joint venture in 2020

- As previously communicated, the Gaming and Enterprise Solutions (CC&O) segments of our Sennheiser Communications JV will be fully consolidated with effect from 1 January 2020

- Previously communicated guidelines for modelling purposes:
  - Adding approx. 2/3 of the JV’s revenue (DKK 1,085 million in 2018) plus a distribution mark-up of approx. 1/3 to Group revenue
  - More or less neutral impact on absolute EBIT for the Group

- Net effect in 2020: Additional revenue, neutral EBIT and dilutive effect on EBIT margin

# 2019, a year of strong product introductions

Introducing the new Oticon Opn S™

# Breaking a law of physics

# Laws of physics

relating to hearing aids?

OPTIMAL GAIN

OPEN FITTING

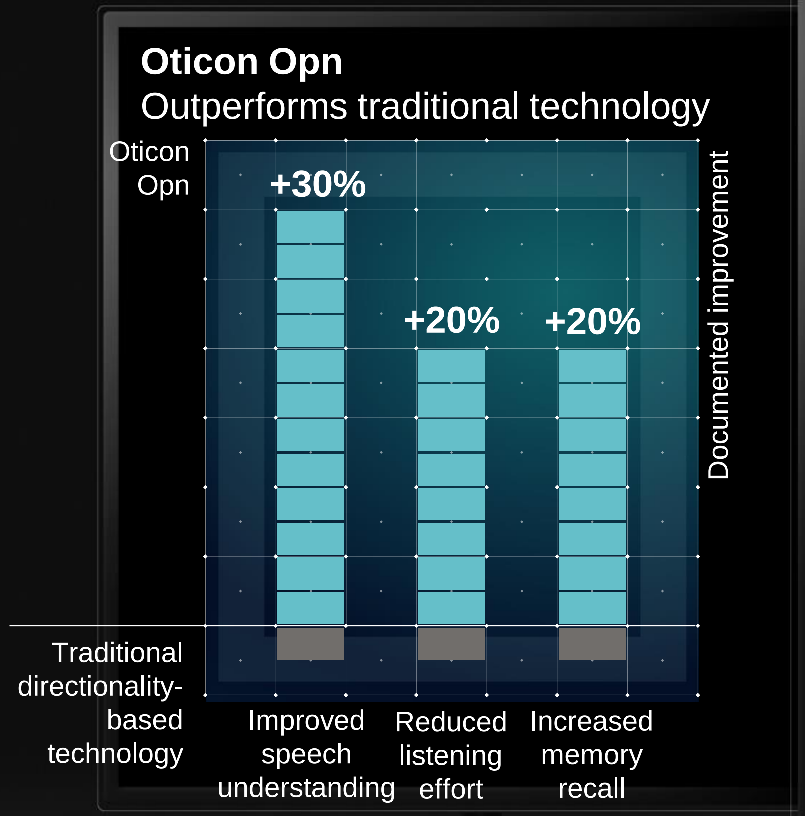
FEEDBACK

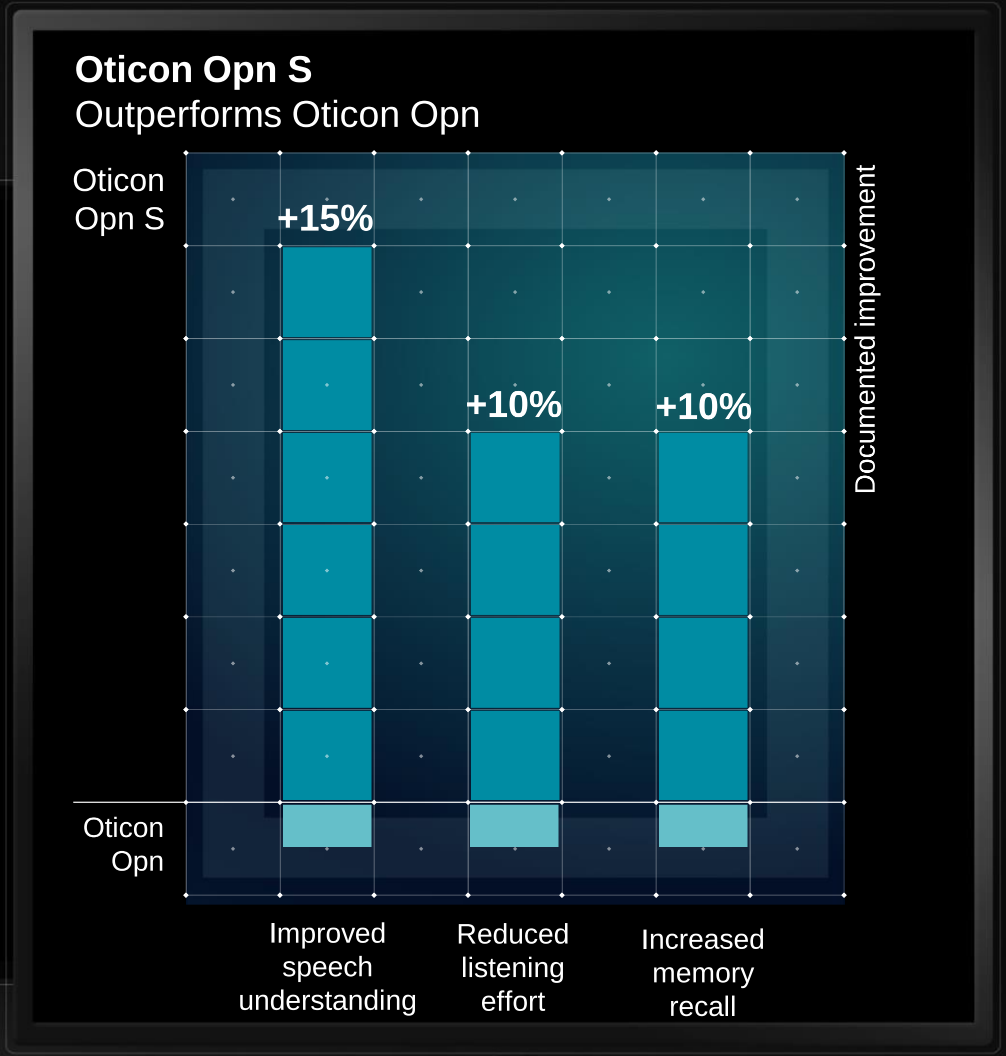
**Trapped**
in a world of
compromise

**until now...**


Freedom to deliver
**optimal gain**
Freedom to deliver
**open fitting**
**Oticon Opn S with**
**OpenSound Optimizer™**
**A new level**
**of fitting freedom**

# Oticon Opn S takes the BrainHearing™ benefits even further




Juul Jensen 2019, Oticon Whitepaper

Demant

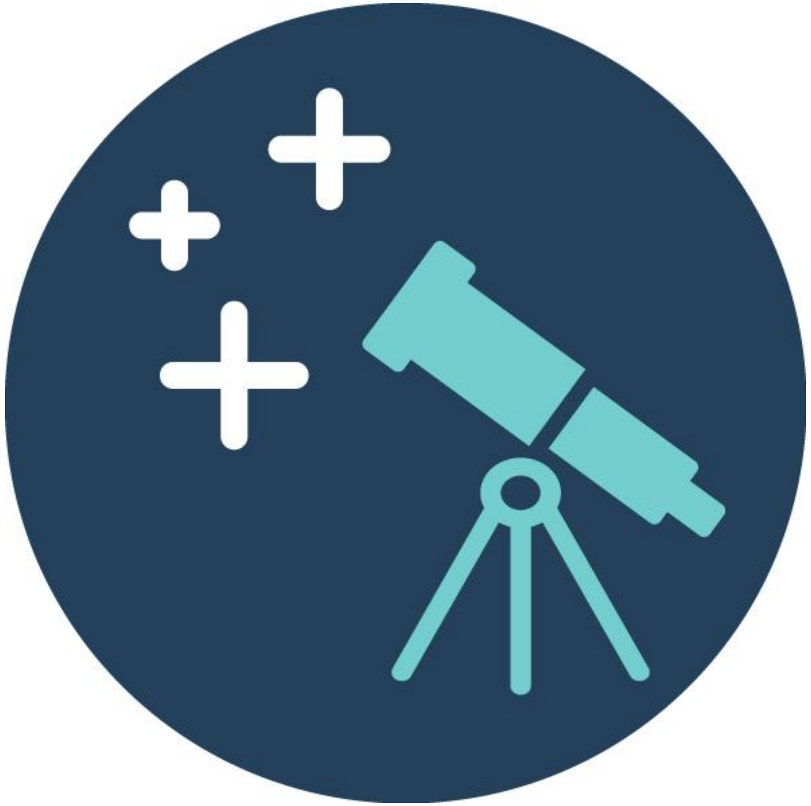
# Extensive range of new product launches


- Over the coming weeks, Oticon will introduce new premium products based on a new platform
  - Proven to deliver even better speech understanding than the ground-breaking Oticon Opn™ thanks to new breakthrough technologies
  - Available in top three price points and four styles, including our first rechargeable technology based on lithium-ion
- Bernafon and Sonic will also launch new, strong product portfolios in the second quarter of 2019
- Expect to introduce new Philips-branded hearing solutions to the market in the second quarter of 2019

# Outlook 2019

Demant

# The hearing healthcare market in 2019



- Total hearing healthcare market estimated to see value growth rate of 5%
- The hearing aid wholesale market estimated to see value growth of 2-4%
  - Unit growth of 4-6%
  - Low single-digit percentage fall in ASP
- The hearing implants market estimated to see value growth of 10-15%
- The diagnostic equipment market estimated to see value growth of 3-5%

Demant

# Outlook 2019

- We expect to generate organic sales growth above market level in 2019 accelerating through the year as we start seeing the effect of new product launches
- Based on exchange rates as of 18 February 2019 and including the impact of exchange rate hedging, we expect a positive exchange rate effect on revenue of 1% in 2019
- We are guiding for a reported operating profit (EBIT) of DKK 2.65-2.95 billion
- We 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

# IR contacts

**Søren B. Andersson**
Vice President, Investor Relations
Email: sba@demant.com
Tel: +45 3913 8967
Mob: +45 5117 6657

**Mathias Holten Møller**
Investor Relations Officer
Email: msmo@demant.com
Tel: +45 3913 8827
Mob: +45 2924 9407

Demant

## Roadshows and conferences:

| | |
|---|---|
| 20 February | **Copenhagen** (Nordea) |
| 21-22 February | **London** (Goldman Sachs) |
| 21-22 February | **The Netherlands & Belgium** (DNB) |
| 22 February | **Edinburgh** (Goldman Sachs) |
| 25 February | **Geneva** (Credit Suisse) |
| 26 February | **Zurich** (Kepler Cheuvreux) |
| 27 February | **Frankfurt** (Carnegie) |
| 27-28 February | **New York** (J.P. Morgan) |
| 06 March | **London** (Credit Suisse Conference) |
| 07 March | **Stockholm** (SEB) |
| 13 March | **Paris** (Deutsche Bank) |
| 25 March | **Toronto** (Mirabaud) |
| 25-26 March | **New York** (Kepler Cheuvreux) |
| 26 March | **Chicago** (DNB) |
| 27-29 March | **Columbus, Ohio** (AudiologyNOW!) |


# Thank You