

Company announcement no 2022-13

1 November 2022

Pre-announcement of Interim Management Statement for Q3 2022 and updated outlook

Group revenue growth of 11% (1% organic) in Q3 due to market share gains in Hearing Aids and Diagnostics
 Contrary to expectations, US private pay market is increasingly negatively impacted by macroeconomic conditions

Outlook for 2022 adjusted to reflect updated market views and lower-than-expected performance for the Group:
 Organic growth of 2-4% (prev. 4-6%) and EBIT of DKK 3,150-3,450 million (prev. DKK 3,500-3,800 million)
 Implementation of cost reduction initiatives to align the business to the current market development

"In the third quarter of the year, our Diagnostics business has performed well and it continued to gain market share. Following recent negative development in our markets, we have seen lower-than-expected performance in our Hearing Care, Hearing Aids and Communications businesses. Our revised outlook implies continued weak market developments as well as macroeconomic uncertainties, causing low consumer confidence, and we no longer see this development as a temporary event. Therefore, we implement cost adjustment initiatives in some areas of the Group, while keeping sharp focus on delivering life-changing innovative products and solutions to our users and customers," says Søren Nielsen, President & CEO of Demant.

Business area	Revenue (DKK million)		Growth				
	Q3 2022	Q3 2021	Organic	Acquisitive	LCY	FX	Reported
Hearing Aids	2,446	2,222	6%	-2%	4%	6%	10%
Hereof sales to Hearing Care	-470	-381	10%	7%	17%	7%	24%
Hearing Care	2,018	1,848	-5%	8%	3%	7%	9%
Diagnostics	613	469	12%	5%	18%	13%	31%
Hearing Healthcare	4,607	4,159	1%	3%	4%	7%	11%
Communications	256	243	0%	0%	0%	5%	5%
Group	4,863	4,402	1%	2%	4%	7%	11%

Business area	Revenue (DKK million)		Growth				
	YTD 2022	YTD 2021	Organic	Acquisitive	LCY	FX	Reported
Hearing Aids	7,288	6,639	8%	-2%	6%	4%	10%
Hereof sales to Hearing Care	-1,365	-1,252	0%	5%	5%	4%	9%
Hearing Care	5,950	5,585	-4%	5%	2%	5%	7%
Diagnostics	1,679	1,312	15%	3%	18%	10%	28%
Hearing Healthcare	13,552	12,284	4%	1%	5%	5%	10%
Communications	808	864	-10%	0%	-10%	3%	-7%
Group	14,360	13,148	3%	1%	4%	5%	9%

- In Q3, the **Group** generated organic growth of 1% with additional growth of 2% from acquisitions and of 7% from exchange rate effects. Total reported revenue growth for the Group was 11%.
- **Hearing Healthcare** saw organic growth of 1% due to solid performance in Diagnostics, whereas Hearing Aids and Hearing Care delivered below expectations in Q3.
 - In **Hearing Aids**, we continued to gain market share in Q3 despite the increasing impact of macroeconomic headwinds on the hearing aid market. Growth was driven by solid unit growth, whereas the ASP growth was slightly negative. The ASP was positively impacted by price increases from the beginning of Q3, but geography and channel mix changes impacted the ASP more negatively than expected in the period, especially due to negative growth in the US private pay market.

- **Hearing Care** delivered negative organic growth in Q3, which can be attributed to weaker-than-expected performance in the US, to negative developments in the US private pay market and to our decision to exit selected managed care plans. Adjusted for the development in the US, organic growth in Hearing Care was flat in Q3. High comparative figures in France due to the hearing healthcare reform implemented last year also had a negative impact on growth, which was in line with our expectations. Acquisitions in Hearing Care contributed considerably to growth in Q3, in part due to the financial consolidation of ShengWang from 1 July 2022.
- **Diagnostics** continued its very strong momentum in Q3, and growth was also positively impacted by the acquisition of Inventis Srl. in Q2.
- **Communications** saw organic growth of 0% in Q3, which is lower than expected. While Enterprise Solutions delivered growth, which was largely in line with our plans, growth in Q3 was negatively impacted by a continuously weak market for gaming headsets, where we have not seen the expected normal seasonality.
- The **Group's gross margin** improved compared to the gross margin of 74.6% realised in H1, partly supported by tailwind from previously announced price increases. The dynamic supply chain situation continues to impact the Group's gross margin negatively, and while the situation has improved slightly during Q3, our gross margin is negatively impacted by higher-than-normal wage inflation.
- In Q3, **OPEX** was in line with our plans, despite an impact on our cost base from increasing inflation, that, however, still remains manageable and broadly in line with expectations. The Group's OPEX saw low double-digit growth in local currencies, most of which is attributable to acquisitions.
- The Group's **EBIT** was below expectations in Q3 despite solid performance in Diagnostics and slightly positive exchange rate effects. This development is due to a soft hearing aid market and resulted in lower-than-expected revenue in Hearing Aids and Hearing Care, especially in the US, and continuously weaker-than-expected developments in the gaming market, which impacted Communications negatively.
- The Group's **operating cash flow** was solid in Q3 despite higher inventories, and we bought back shares worth DKK 493 million. In the light of the weaker-than-expected EBIT, a high M&A activity level throughout the year and the expected closing of the divestment of Hearing Implants in Q2 2023 instead of H2 2022 (please see below), we have decided to pause our share buy-backs for the remainder of the year. Total share buy-backs amount to DKK 1,840 million year-to-date 31 October.
- As announced on 27 April 2022, we have decided to discontinue our **Hearing Implants** business, which is therefore recognised separately as a discontinued operation. Subject to regulatory approvals and other customary closing conditions, the divestment of the business to Cochlear Limited is now expected to close in Q2 2023. Previously, closing was expected to take place at the end of 2022, but the Spanish competition authorities have handed over the case to the European Commission, which will prolong the approval process for the transaction.
- Following lower-than-expected market growth and to align the business to current market developments, we are implementing **cost reduction initiatives** in Hearing Care, Hearing Aids and Communications. In Hearing Care, we rationalise our US store footprint by approx. 50 stores and align the size of our organisation. In Hearing Aids, we will make adjustments to selected parts of our central organisation, and we have already initiated a closing and transfer of the Bernafon brand headquarter in Switzerland to the Group's headquarters in Denmark. In Communications, we also adjust the organisation to reflect the current market outlook. We expect these changes to be implemented over the coming months and to result in 150-200 redundancies globally across Hearing Aids, Hearing Care and Communications. We expect these initiatives to lead to improvements in our performance already in H1 2023.

Outlook for 2022

Our outlook for 2022, which is summarised in the table below, is adjusted to reflect weaker-than-expected performance in Q3 and lower expectations for the remainder of the year.

Metric	Outlook for 2022
Organic growth	2-4% (prev. 4-6%)
Acquisitive growth	2% based on revenue from acquisitions completed as of 31 October 2022
FX growth	5% based on exchange rates as of 31 October 2022 and including the impact of hedging
EBIT	DKK 3,150-3,450 million (prev. DKK 3,500-3,800 million)
Effective tax rate	22-23%
Gearing multiple	Gearing (NIBD relative to EBITDA) at the end of 2022 to end at or slightly below 3.0 (prev. to slightly exceed 2.0-2.5)
Share buy-backs	Currently paused. Year-to-date 31 October, share buy-backs amount to DKK 1,840 million
Profit after tax from discontinued operations	Negative by DKK 200-250 million (prev. negative by DKK 150-200 million)

The outlook continues to be based on a number of key assumptions as described below (changes in bold):

- **In Q3, value growth in the hearing aid market was below our updated expectations. We now expect total market unit growth in 2022 at the low end of the structural level of 4-6%. In addition, we now expect ASP growth in the market to be more negatively impacted by channel and geography mix changes than previously and to end below the normal 1-2% annual decline.**
- Growth in the French hearing aid market to be negative in 2022 following the extraordinary demand in 2021, which we estimate benefitted the Group's revenue by DKK 300 million and EBIT by DKK 150 million. We do not expect this benefit to recur. **Developments year-to-date were at least in line with our expectations.**
- **The market for enterprise and gaming headsets and video solutions to grow below the estimated structural growth level of around 12%. The weakening of the gaming market in Q3 was more pronounced than expected and we continue to see some supply chain challenges on certain product families in Enterprise Solutions.**
- **In H2, we expect to continue to see market share gains in Hearing Healthcare. For Communications, we now expect to see negative high single-digit organic growth in H2 compared to 2021.**
- Supply chain situation to remain dynamic throughout the year and to result in higher-than-normal component costs and freight charges with an impact that is roughly similar to the impact in 2021 but with no material disruption to sales activities.
- The Group's OPEX base to see no benefit from temporary cost savings in 2022, which we estimate amounted to DKK 150-200 million in H1 2021.
- **For Communications, we now expect EBIT of around DKK -225 million in 2022 due to continued negative market trends and supply chain challenges. In the medium- to long term, we still consider the fundamental growth drivers of the market to be fully intact.**
- **The planned divestment of Hearing Implants is now presumed to close in Q2 2023. Total profit after tax from discontinued operations in 2022 is now expected to be negative by around DKK 200-250 million, reflecting the delayed recognition of the positive one-off gain from the fair value adjustment of assets and liabilities in connection with the transaction. At closing, DKK 700 million of the total DKK 850 million consideration will be paid.**

Demant will host a conference call on 2 November 2022 at 13:00 CET. To attend this call, please use one of the following dial-ins: +45 7877 4197 (DK), +44 0 808 101 1183 (UK) or +1 (785) 424 1634 (US). The pin code is 70355#. A presentation for the call will be uploaded on www.demant.com shortly before the call.

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Hearing Healthcare

Market trends

Overall, the hearing healthcare market that we address, which comprises the markets for hearing aids and diagnostic instruments and services, saw slight negative growth in Q3.

Hearing aid market

Based on available market statistics, covering slightly less than two-thirds of the hearing aid market, and on our own assumptions, we estimate that the global hearing aid market saw unit growth of around 1% in Q3 compared to the same period in 2021. Growth was more positive in the public channels, such as the NHS and Veterans Affairs (VA), none of which have, however, normalised compared to pre-pandemic growth rates. We estimate that emerging markets saw solid growth in the period. In Q3, we saw increasing impacts of general consumer uncertainty, not least in markets dominated by private pay, especially the US. We estimate that geography and channel mix changes in the market resulted in a more negative ASP development than expected. Consequently, value growth in the hearing aid market was below expectations and negative in Q3.

Estimated hearing aid market unit growth by region

Region	2022			
	Q1	Q2	Q3	YTD
Europe	20%	9%	0%	10%
North America	8%	1%	0%	3%
<i>Hereof US (commercial)</i>	6%	-1%	-3%	1%
<i>Hereof US (VA)</i>	19%	2%	9%	9%
Rest of world	4%	4%	4%	4%
Global	12%	5%	1%	6%
CAGR vs. 2019	4%	6%	4%	5%

Compared to the same period in 2021, we estimate that in Q3, market unit growth in Europe was flat. In the UK, market growth was driven by the NHS, whereas the commercial market declined slightly. Germany delivered growth in the period, and France saw slightly negative growth despite the extraordinary positive impact of the hearing healthcare reform implemented last year.

Unit growth in North America was also flat in Q3. Growth was predominantly driven by VA, which grew by 9%. The commercial part of the market declined in the period, in part driven by high comparative figures, as we saw the release of pent-up demand in Q3 2021, and in the US, managed care continues to grow more than the general market, while the private pay market is declining. Unit growth in Canada continued the solid trend in Q3, and the market growth rate was in line with the normal level.

Looking beyond Europe and North America, we estimate that market unit growth in China was slightly positive in Q3, which is an improvement following the impacts of lockdowns and coronavirus-related restrictions in Q2. Also, unit growth in Australia was solid compared to the same period last year, but in Japan, the market saw negative growth in the period, and it remains below the pre-pandemic level.

In August 2022, the long-awaited regulation of the over-the-counter (OTC) category of hearing aids was finalised by the US Food and Drug Administration (FDA), and the rule took effect on 17 October 2022. As previously communicated, the content of the final rule does not change our fundamental belief in the importance of providing a combination of personal counselling, individual fitting, life-long service and highly advanced technology, but the new category may supplement the existing hearing aid categories well.

Diagnostics market

The market for diagnostic instruments and services remains resilient. We estimate that, compared to the same period last year, the market growth rate in Q3 was above the estimated structural annual growth rate of 3-5%.

Hearing Aids

Despite adverse market conditions, especially in the latter part of Q3, our Hearing Aids business delivered good performance relative to the market in Q3 with organic growth of 6%. Acquisitive growth was -2% due to the divestment in October 2021 of FrontRow Calypso LLC, and exchange rate effects were 6%.

Revenue	Revenue (DKK million)		Growth				
	Q3 2022	Q3 2021	Organic	Acquisitive	LCY	FX	Reported
Total revenue	2,446	2,222	6%	-2%	4%	6%	10%
Internal sales to Hearing Care	470	381	10%	7%	17%	7%	24%
Sales to external customers	1,976	1,841	5%	-3%	2%	6%	7%

Revenue	Revenue (DKK million)		Growth				
	YTD 2022	YTD 2021	Organic	Acquisitive	LCY	FX	Reported
Total revenue	7,288	6,639	8%	-2%	6%	4%	10%
Internal sales to Hearing Care	1,365	1,252	0%	5%	5%	4%	9%
Sales to external customers	5,923	5,387	10%	-3%	6%	4%	10%

Organic growth was driven by solid sales to external customers, which grew organically by 5% due to strong sales in Europe and market share gain in the US. We also saw good momentum in Asia and in the Pacific region. Internal sales to Hearing Care accounted for 19% of total revenue in Hearing Aids. Growth in Hearing Aids was driven entirely by an increase in unit sales, whereas the ASP, despite being positively impacted by price increases from the beginning of Q3, declined slightly due to geography and channel mix changes.

Hearing Aids continued to gain market share driven by good performance in many markets and supported by the expansion of our portfolio of industry-leading hearing aids with new custom form factors built on our ground-breaking Polaris technology.

In Europe, we saw growth in Q3. France saw solid growth in the period in spite of strong comparative figures, and other countries, such as Germany, Poland and Spain, also saw good growth in the period. After a strong H1, growth in the UK slowed down but remained positive driven by sales to the NHS. The impact of the halt of sales to Russia, Belarus and the provinces of Donetsk and Luhansk continued to have a slightly negative impact on growth in Q3.

North America delivered flat organic revenue growth. In the US, we continue to gain market share, but the market grew less than expected, especially due to negative growth in the private pay market. Sales to VA, where our unit market share increased from 14.7% in September 2021 to 15.9% in September 2022, contributed positively to growth and in Canada, we delivered solid growth in Q3. In a generally competitive environment, our Hearing Aids business in North America continues to see good traction thanks to Oticon More and Philips HearLink.

Growth in Asia and the Pacific region was strong, in part driven by low comparative figures. In China, we have seen good growth, partly driven by a partial market rebound following lockdowns in Q2, and in Japan and Australia, growth was solid in the period despite the fact that some coronavirus-related restrictions were still in force at the beginning of Q3. Sales to our *Other countries* region, which mostly comprises emerging markets, saw strong growth in Q3 driven by continuously good commercial momentum.

Hearing Care

Sales in Hearing Care saw organic growth of -5% in Q3, which is below expectations. Adjusted for the development in the US, organic growth in Hearing Care was roughly flat in Q3. Acquisitive growth was 8% and exchange rate effects added 7%. Despite strong comparative figures in France, the weak development in Hearing Care is mainly attributable to performance in the US and in Q3, we saw many smaller countries deliver growth.

In Europe, growth was negative in Q3. We saw positive developments in several markets, such as Poland and Switzerland, but in France, we continue to annualise tailwinds from the hearing healthcare reform in 2021, which, as expected, negatively impacted growth in Q3.

North America delivered organic growth below expectations in Q3 due to slow momentum in the private pay market in the US. Our strategic decision to reduce the share of sales related to managed care continues to have a more negative impact than expected on growth and profitability, and it has proven more difficult than expected to

generate new leads to replace the managed care activities that we have exited. In Canada, we saw growth in the period, and acquisitions continue to contribute to growth in both countries.

Impacted by coronavirus-related restrictions in the comparative period, Australia saw good growth in Q3 despite being impacted by some restrictions in the early part of Q3.

Diagnostics

Diagnostics delivered strong organic growth of 12% in Q3 and continued to gain market share. In addition, the business area realised growth of 5% from acquisitions and 13% from exchange rate effects. Growth was broadly based across most regions, and the order intake continues to be strong. All our geographical regions performed well, with Asia and the US as the biggest contributors to growth in the period.

Diagnostics generated growth in all product categories, with instruments for tympanometry, hearing aid fitting and balance testing contributing the most to growth.

Communications

Market trends

We estimate that the market growth rate for enterprise solutions and gaming was mixed in Q3. The market for enterprise solutions saw growth in Q3, but the market has seen some softening recently. The gaming market continues to see negative growth, and the impact of the weakening of consumer spending in Q3 has been more negative than previously expected.

The market for enterprise and gaming headsets and video solutions is expected to see growth in 2022 below the estimated structural level of around 12%, primarily due to the development in the market for gaming headsets. However, we still believe that the fundamental growth drivers of the market remain fully intact in the medium to long term, and we still expect the structural market growth rate to be around 12%.

Communications (EPOS)

The Communications business area, which operates under the EPOS brand, saw organic growth of 0% in Q3, which is below expectations. Exchange rate effects were 5%. Compared to last year, we saw growth in Asia and Europe, negative growth in the Pacific region and flat growth in the US.

Growth in our Gaming segment was negative and continued to be impacted by high inventories in the sales channels, which remains a drag on growth. In Q3, our Enterprise Solutions segment saw good growth, which was broadly based across geographies, but with Asia as the most prominent growth driver.

Cost reduction initiatives

Following lower-than-expected market growth and to align the business to current market developments, we are implementing cost reduction initiatives in Hearing Care, Hearing Aids and Communications. In Hearing Care, we rationalise our US store footprint by approx. 50 stores and align the size of our organisation. In Hearing Aids, we will make adjustments to selected parts of our central organisation, and we have already initiated a closing and transfer of the Bernafon brand headquarter in Switzerland to the group headquarter in Denmark. In Communications, we also adjust the organisation to reflect the current market outlook. We expect these changes to be implemented over the coming months and to result in 150-200 redundancies globally across Hearing Aids, Hearing Care and Communications. We expect these initiatives to lead to improvements in our performance already in H1 2023.