

Company announcement no 2021-02

Annual Report 2020

9 February 2021

Growth of 14% in local currencies (2% organic) in H2 after strong recovery of hearing healthcare market
Strong EBIT of DKK 1,506 million in H2 driven by market recovery and tight cost control
Very strong cash flows in H2 with CFFO of DKK 1,892 million (+72%) and FCF of DKK 1,534 million (+141%)
Outlook for FY 2021 for the Group: Organic growth of 23-27% and EBIT of DKK 2,850-3,150 million
Still uncertainty about timing of normalisation and release of pent-up demand

In this Annual Report 2020, we have made several changes to our reporting structure to further enhance transparency in the value created by each of our different business areas. The changes include disclosing separate income statements for two business segments:

Hearing Healthcare: *Comprises the four business areas Hearing Aids (previously hearing aid wholesale), Hearing Care (previously hearing aid retail), Hearing Implants and Diagnostics.*

Communications: *Comprises only our headset business, which operates under the EPOS brand.*

Furthermore and in addition to reporting separate growth rates, we now also report separate revenues for our Hearing Aids and Hearing Care business areas. However, we no longer report separate growth rates for our cochlear implants (CI) and bone anchored hearing systems (BAHS) businesses but only one growth rate for Hearing Implants as a whole to simplify our reporting across business areas.

Growth	Group			Hearing Healthcare			Communications*		
	H1 2020	H2 2020	FY 2020	H1 2020	H2 2020	FY 2020	H1 2020	H2 2020	FY 2020
Organic	-27%	2%	-13%	-27%	2%	-13%			
Acquisitions	9%	12%	11%	2%	2%	2%			
Local currencies	-18%	14%	-2%	-25%	4%	-11%			
Exchange rates	0%	-3%	-1%	0%	-3%	-1%			
Total	-17%	11%	-3%	-25%	0%	-12%			

*Growth rates for Communications are not available, as there is no directly comparable base (EPOS was not consolidated in 2019).

- After the severe impact of coronavirus in H1, revenue for the **Group** improved significantly in H2 although it remained below the normal level. In line with the latest guidance of revenue growth of 12-14%, growth in H2 was 14% in local currencies with 2% organic growth and 12% growth from acquisitions. The latter included 10 percentage points attributable to the consolidation of EPOS. Exchange rates had an impact of -3%, including exchange rate hedging. For the full year 2020, revenue declined by 3% with organic growth of -13%, acquisitive growth of 11% and exchange rate effects of -1%.
- As previously announced, revenue in the comparative period (H2 2019) was negatively impacted by an estimated DKK 575 million due to the IT incident that occurred on 3 September 2019. Adjusted for this, underlying organic growth was -5% and -16% for H2 and the full year 2020, respectively.

Revenue and growth rates	Revenue (DKK million)			Organic growth			Underlying organic growth*		
	H1 2020	H2 2020	FY 2020	H1 2020	H2 2020	FY 2020	H1 2020	H2 2020	FY 2020
Hearing Aids	2,937	3,886	6,823	-25%	1%	-12%	-25%	-8%	-16%
<i>Hereof sales to Hearing Care</i>	-465	-657	-1,122	-27%	5%	-11%	-27%	-4%	-15%
Hearing Care	2,154	3,310	5,464	-35%	4%	-16%	-35%	-4%	-19%
Hearing Implants	246	277	523	-18%	-9%	-13%	-18%	-9%	-13%
Diagnostics	660	815	1,475	-3%	4%	1%	-3%	4%	1%
Hearing Healthcare	5,532	7,631	13,163	-27%	2%	-13%	-27%	-5%	-16%
Communications**	546	760	1,306						
Group	6,078	8,391	14,469						

*Organic growth adjusted for estimated impact of IT incident in H2 2019.

**Growth rates for Communications are not available, as there is no directly comparable base (EPOS was not consolidated in 2019).

- Following the very challenging market conditions in most of H1, our **Hearing Healthcare** business segment saw significant recovery in H2, particularly in the first months of the period where our Hearing Aids and Hearing Care business areas benefitted from the release of some pent-up demand in Europe. At the beginning of Q4, we saw rising infection rates and the implementation of new restrictions in most regions, resulting in a halt in the market recovery although clinics remained open and showed some resilience. Towards the very end of 2020, restrictions were once again tightened in most markets, and revenue remained below the normal level, particularly in the UK and to a lesser extent in the US. Starting in December, all our four hearing aid brands introduced new flagship products, and we have thus entered 2021 in an excellent commercial position.
- In **Communications**, our EPOS brand saw very strong demand for its virtual collaboration tools in 2020 following the surge in remote working. After a slow start to the year, revenue increased significantly from mid-March and accelerated further in H2, as demand remained strong and production capacity was increased. In 2021, we have so far continued to see high demand and high double-digit organic growth, and the number of backorders remains above the normal level.
- The **gross margin** in H2 was 72.5%, a decrease of 1.5 percentage points compared to H2 2019. The consolidation of EPOS diluted the Group's gross margin by 2.0 percentage points, but for our Hearing Healthcare segment, the gross margin increased slightly as a result of mix effects.
- The Group drove material savings in **OPEX** throughout 2020, and in H2, OPEX only saw flat growth in local currencies despite the increase related to the consolidation of EPOS. Savings were both temporary and structural, and as previously announced, the structural savings amount to around DKK 250 million on an annual basis with full effect from H2 2020. Temporary savings mostly related to lower sales and marketing costs as well as lower travelling expenses but also included global support from government compensation schemes of around DKK 100 million and a positive effect of DKK 50 million from the reversal of part of the provision for bad debt recognised in H1.
- Despite the challenging market conditions, profitability was very strong in H2, and **EBIT** for the Group amounted to DKK 1,506 million before EPOS one-offs, corresponding to an EBIT margin of 17.9%. Including the negative EBIT in H1, EBIT for the full year 2020 amounted to DKK 1,313 million, corresponding to an EBIT margin of 9.1%.
- EPOS one-offs** amounted to DKK -90 million in H2 of which DKK -52 million related to extraordinary branding costs and DKK -38 million to the negative adjustment of inventory purchased as part of the demerger of Sennheiser Communications. The latter had no effect on cash flows. Including the net positive one-offs in H1, EPOS one-offs were net positive by DKK 217 million for the full year 2020.
- Cash flow from operating activities** (CFFO) increased by 72% to DKK 1,892 million in H2, and the **free cash flow** (FCF) increased by 141% to DKK 1,534 million. The very strong cash flows were driven by tight working capital management, and the free cash flow was further supported by the temporary suspension of non-essential investments from mid-March and into H2.
- Having been suspended from 15 March until today, **share buy-backs** totalled DKK 197 million for the full year 2020.

Outlook for 2021

Our outlook (summarised below) is subject to greater uncertainty than usual due to the continued impact of coronavirus in most markets. In 2021, the hearing healthcare market has so far continued to be negatively impacted by coronavirus, and the Group's revenue remains below the normal level. In our outlook for 2021, we assume that the global hearing healthcare market will gradually normalise during H1 supported by the global roll-out of coronavirus vaccines, which will make it possible to lift coronavirus-related restrictions in developed markets. However, we expect a slower pace of normalisation in certain government channels and in emerging markets and for the latter, normalisation may even go beyond 2021. Furthermore, we assume that some pent-up demand for hearing healthcare solutions will be released, predominantly in H2, and despite strong comparative figures for 2020, we expect that the demand for headsets will continue to grow in line with structural growth trends of 8-10%.

Group organic growth	23-27%, with Hearing Healthcare realising a higher organic growth rate than Communications.
Group acquisitive growth	1% based on revenue from acquisitions completed as of 8 February 2021.
Group exchange rate growth	-2% based on exchange rates as of 8 February 2021 and including the impact of exchange rate hedging.
EBIT	DKK 2,850-3,150 million, with EBIT skewing towards H2.
Effective tax rate	Around 23%.
Gearing	Gearing multiple at the end of 2021 in line with our medium- to long-term target of 2.0-2.5 measured as NIBD relative to EBITDA.*
Share buy-backs	More than DKK 2 billion.

* Our gearing target no longer excludes the impact of leasing. The target remains unchanged if adjusted for the estimated impact of leasing on our gearing of 0.3.

"I am pleased to see how well the entire global organisation has steered Demant through a year impacted by the worst ever market conditions for hearing healthcare. The first half-year was tough, but in the second half, we saw strong recovery for the Group, not least thanks to the success of our new brand in premium audio solutions, EPOS. At the same time, we successfully managed costs, and particularly in the second half-year, we saw strong cash flows. Having now entered 2021, our business is showing good resilience, despite abnormal hearing healthcare market conditions, and all our business areas are ready to capture market shares. So, with our proven business model in place and vaccines rolling out, I take an optimistic view on the coming year where many factors will contribute to good growth, such as the release of pent-up demand and our recently launched flagship products in all our hearing aid brands. So far, Oticon More, the world's first hearing aid using a deep neural network – AI technology – has been rolled out in most major markets where it has seen strong traction. Oticon More will no doubt be an important growth driver in 2021," says Søren Nielsen, President & CEO of Demant.

Demant will host a conference call on 9 February 2021 at 14:00 CEST. To attend this call, please use one of the following dial-ins: +45 3544 5577 (DK), +44 3333 000 804 (UK) or +1 6319 131 422 (US). The pin code is 38012667#. A presentation for the call will be uploaded to www.demant.com shortly before the call.

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Key figures and financial ratios

	H2 2020	H2 2019	Change	FY 2020	FY 2019	Change
Hearing Healthcare						
Revenue	7,631	7,596	0%	13,163	14,946	-12%
Organic growth	2%	3%		-13%	4%	
Gross margin	74.5%	74.0%		73.6%	75.8%	
Operating profit (EBIT)	1,425	1,000	43%	1,211	2,085	-42%
EBIT margin	18.7%	13.2%		9.2%	14.0%	
Communications						
Revenue	760	-	-	1,306	-	-
Organic growth	-	-		-	-	
Gross margin	52.9%	-		50.3%	-	
Operating profit (EBIT)*	81	38	113%	102	66	55%
EBIT margin	10.7%	-		7.8%	-	
Group						
Income statement						
Revenue	8,391	7,596	10%	14,469	14,946	-3%
Adjusted gross margin**	72.5%	74.0%		71.5%	75.8%	
Gross margin	72.1%	74.0%		70.4%	75.8%	
EBITDA	1,949	1,528	28%	2,578	3,110	-17%
EBITDA margin	23.2%	20.1%		17.8%	20.8%	
Adjusted EBIT**	1,506	1,038	45%	1,313	2,151	-39%
Adjusted EBIT margin**	17.9%	13.7%		9.1%	14.4%	
Operating profit (EBIT)	1,416	1,038	36%	1,530	2,151	-29%
EBIT margin	16.9%	13.7%		10.6%	14.4%	
Net financial items	-106	-121	-12%	-194	-240	-19%
Profit for the year	1,013	700	45%	1,134	1,467	-23%
Balance sheet						
Total assets	21,927	21,798	1%	21,927	21,798	1%
Net interest-bearing debt (NIBD)	7,135	8,185	-13%	7,135	8,185	-13%
Equity	8,279	7,645	8%	8,279	7,645	8%
Cash flow statement						
Adjusted cash flow from operating activities (CFFO)**	1,944	1,102	76%	2,710	2,149	26%
Cash flow from operating activities (CFFO)	1,892	1,102	72%	2,621	2,149	22%
Investment in property, plant and equipment, net	251	310	-19%	493	561	-12%
Free cash flow	1,534	636	141%	2,023	1,338	51%
Share buy-backs	-	682	-	197	946	-79%
Other key figures						
Return on equity	25.7%	18.0%		14.3%	19.5%	
Equity ratio	37.8%	35.1%		37.8%	35.1%	
Gearing multiple (NIBD/EBITDA)	2.8	2.6		2.8	2.6	
Earnings per share (EPS)***	4.18	2.87	46%	4.68	6.00	-22%
Free cash flow per share (FCFPS)***	6.40	2.62	144%	8.44	5.49	54%
Price/earnings (P/E) ratio	57.6	73.1	-21%	51.4	35.0	47%
Share price, end of period***	240.60	209.80	15%	240.60	209.80	15%
Average number of shares outstanding	239.78	243.55	-2%	239.78	243.55	-2%
Market capitalisation	57,718	50,470	14%	57,718	50,470	14%
Average number of employees	16,203	15,660	3%	16,155	15,352	5%

*EBIT for Communications in 2019 relates to the Group's share of profit after tax from our former joint venture Sennheiser Communications.

**Adjusted for EPOS one-offs in 2020.

***Per share of nominally DKK 0.20.