

Company announcement no 2023-13

Interim Management Statement for Q3 2023

7 November 2023

Group organic growth of 13% in Q3 driven by sustained market share gains in Hearing Healthcare
Strong profitability and cash flow generation for the Group despite negative effect of Gaming wind-down
Outlook for 2023 narrowed: Organic growth of 12-13% (prev. 11-14%) and EBIT of DKK 4,050-4,350 million
(prev. DKK 4,000-4,400 million)

“Our Hearing Healthcare business segment continues to be in very good shape, delivering an impressive double-digit organic growth rate, particularly lifted by Hearing Aids that generated 25% organic growth in sales to external customers in Q3. I attribute our success to the innovative and broad product portfolio – Oticon Real is doing very well – and our strong focus on customer collaboration and personalised care. Demant has gained significant market share over the last quarters in a normalised hearing healthcare market, but we still see negative effects of the results in Communications on the Group’s performance due to the decision to wind down our Gaming activities as well as to a weak market for audio solutions. Nonetheless, we have delivered strong profitability and cash flow, allowing us to continue to invest in developing our life-changing hearing healthcare solutions,” says Søren Nielsen, President & CEO of Demant.

Business area	Revenue (DKK million)		Growth				
	Q3 2023	Q3 2022	Organic	Acquisitive	LCY	FX	Reported
Hearing Aids, total revenue	2,924	2,446	21%	0%	21%	-1%	20%
Hearing Aids, internal revenue	-494	-470	4%	5%	9%	-4%	5%
Hearing Aids, external revenue	2,430	1,976	25%	-1%	24%	-1%	23%
Hearing Care	2,152	2,018	6%	6%	12%	-5%	7%
Diagnostics	625	613	6%	2%	8%	-6%	2%
Hearing Healthcare	5,207	4,607	14%	2%	17%	-4%	13%
Communications	196	256	-20%	0%	-20%	-4%	-23%
Group	5,403	4,863	13%	2%	15%	-4%	11%

Business area	Revenue (DKK million)		Growth				
	YTD 2023	YTD 2022	Organic	Acquisitive	LCY	FX	Reported
Hearing Aids, total revenue	9,012	7,288	22%	0%	22%	1%	24%
Hearing Aids, internal revenue	-1,594	-1,365	13%	6%	19%	-2%	17%
Hearing Aids, external revenue	7,418	5,923	24%	-1%	23%	2%	25%
Hearing Care	6,660	5,950	7%	7%	15%	-3%	12%
Diagnostics	1,823	1,679	6%	5%	11%	-3%	9%
Hearing Healthcare	15,901	13,552	15%	3%	18%	-1%	17%
Communications	657	808	-17%	0%	-17%	-2%	-19%
Group	16,558	14,360	13%	3%	16%	-1%	15%

Unless otherwise indicated, the commentary below relates to Q3 2023.

- The **Group** generated organic growth of 13%, driven entirely by Hearing Healthcare. Acquisitive growth was 2% and exchange rate effects were -4%. Reported revenue growth was 11%.
- **Hearing Healthcare** saw organic growth of 14%, fuelled by strong growth in Hearing Aids, with additional growth of 2% related to acquisitions in Hearing Care and Diagnostics.
 - Performance in **Hearing Aids** continued at a very high level with sustained market share gains across markets and channels, driven by the success of new premium hearing aids launched in Q1, including our flagship product, Oticon Real. Growth was primarily driven by unit growth, while the ASP development was slightly positive.
 - **Hearing Care** delivered solid performance, driven by good momentum in most medium-sized markets. This offset slightly negative growth in France, which saw adverse market developments, and weaker-than-expected growth in China due to weak market dynamics. Acquisitions in several markets also contributed to growth in the period, primarily in Germany.
 - In **Diagnostics**, organic growth was solid, albeit with a slightly negative impact of weak market dynamics in China. Growth continued to be supported by minor acquisitions.
- **Communications** continued to see weak momentum and negative growth, as the markets for both enterprise solutions and for gaming headsets remained challenging. Our Enterprise Solutions business saw organic growth of -24%. The gradual wind-down of our Gaming activities announced on 29 August 2023 entails the clearing of Gaming-related inventories, which has been realised at lower prices than anticipated. Together with other minor one-off costs, this is expected to impact EBIT negatively by an additional DKK 50-100 million in H2. Along with other cost savings, the wind-down will shorten the path back to profitability in Communications.
- The Group's **gross margin** was in line with expectations and improved sequentially relative to H1. This was driven by positive developments in Hearing Healthcare, which offset a significant sequential gross margin decline in Communications due to the clearing of Gaming-related inventories.
- **OPEX** was in line with expectations with high single-digit growth in local currencies of which roughly half was organic, reflecting a combination of continued investments in Hearing Healthcare and cost savings in Communications with a view to improving profitability.
- The Group's **EBIT** was in line with expectations, as material operating leverage in Hearing Healthcare offset larger-than-anticipated negative one-off effects related to the wind-down of our Gaming activities and softening market dynamics in China.
- The Group's **CFFO** and **FCF** continued at a high level driven by improved profitability. Despite a high level of acquisitions in Q3, the Group slightly reduced its net interest-bearing debt. Combined with an increased EBITDA, the Group's gearing multiple was thus reduced slightly in Q3. No shares were bought back in Q3, but the Group may resume share buy-backs, however subject to cash generation and the level of acquisitions that will be closed in Q4.
- The divestment of our cochlear implants business to Cochlear Limited continues to progress, but the work is taking longer than expected. We now expect the transaction to close in H1 2024 (previously before the end of 2023). There are no changes to the outlook for profit after tax from discontinued operations, and in Q3, the operational performance of Hearing Implants was in line with expectations.

Outlook for 2023

The Group's outlook for 2023, which is summarised in the table below, has been narrowed with respect to organic growth and EBIT to reflect reduced overall uncertainty. The narrowed outlook reflects material operating leverage in Hearing Healthcare, offsetting larger-than-anticipated negative effects of the wind-down of our Gaming activities as well as softening market dynamics in China.

Metric	Outlook for 2023
Organic growth	12-13% (previously 11-14%)
Acquisitive growth	3% based on revenue from acquisitions completed as of 6 November 2023
FX growth	-1% based on exchange rates as of 6 November 2023 and including the impact of hedging (previously -2%)
EBIT	DKK 4,050-4,350 million (previously DKK 4,000-4,400 million)
Net financials	Negative by around DKK 700 million
Effective tax rate	24-25%
Gearing multiple	Gearing multiple (NIBD/EBITDA) at the end of 2023 within our medium- to long-term target of 2.0-2.5
Share buy-backs	May be resumed, subject to cash generation and the level of acquisitions completed
Profit after tax from discontinued operations	Negative by DKK 700-850 million

The outlook is based on a number of key assumptions as described below (changes versus most recent outlook in bold):

- Following a stabilisation of the global hearing aid market in H1, we expect the market unit growth rate in 2023 to be slightly above the structural growth rate of 4-6%. We expect a negative contribution from ASP declines around the normal level of 1-2% due to mix effects.
- We expect the weak momentum in the markets for enterprise solutions and gaming headsets to continue throughout 2023. In 2023, we expect our Communications segment to see negative organic growth and to generate EBIT that is more negative than the level in 2022, as lower revenue and gross margin are only partly offset by cost savings already implemented. **The wind-down of our Gaming activities is expected to have an additional negative one-off impact on the Group's EBIT in H2 of DKK 50-100 million, which is included in the Group's outlook.**
- **We expect the level of bolt-on acquisitions in 2023 to be slightly higher than normal, but a number of acquisitions that we had planned for completion in 2023 are now expected to close in 2024.**
- Despite higher-than-normal cost inflation, we plan to grow OPEX less than revenue through focused cost control in order to support margin improvement.
- **The divestment of our cochlear implants business is expected to close in H1 2024. Our bone anchored hearing systems business will remain with the Group for now, pending a review of our strategic options.**

Demant will host a conference call on 7 November 2023 at 14:00 CET. To receive dial-in details for this call, please pre-register via this link: <https://dpregrister.com/sreg/10183674/facb9ae4f2>. 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 we address, which comprises the markets for hearing aids and diagnostic instruments and services, saw positive growth in Q3. Compared to Q2, growth accelerated primarily as a reflection of soft comparative figures, and if we compare to pre-pandemic levels, growth in the global hearing aid market developed in line with the structural growth rate.

Hearing aid market

Based on available market statistics, covering around 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 8% in Q3 compared to the same period in 2022. Growth was positive across regions, and we estimate that geography and channel mix changes resulted in a slightly negative ASP development. Consequently, value growth in the hearing aid market in Q3 was in line with our expectations.

Estimated hearing aid market unit growth by region

Region	2023			YTD
	Q1	Q2	Q3	
Europe	4%	-4%	7%	2%
North America	9%	5%	11%	8%
<i>Hereof US (commercial)</i>	9%	5%	12%	9%
<i>Hereof US (VA)</i>	9%	4%	4%	6%
Rest of world	9%	10%	7%	9%
Global	7%	3%	8%	6%
<i>CAGR vs 2019</i>	5%	5%	5%	5%

Compared to the same period in 2022, we estimate that in Q3, market unit growth in Europe was 7%. Growth was predominantly driven by very strong growth in the NHS, although in the UK, the commercial market also grew in the period. In Germany, growth was slightly positive, whereas France saw negative growth, as the hearing aid market continued to normalise following the hearing healthcare reform implemented in 2021. Several smaller markets saw strong growth, particularly Spain.

Growth in North America was 11% in Q3, driven by strong development in the US commercial market where growth was 12%. Relative to the same period last year, unit growth in the US commercial market continues to be driven by managed care and large chains growing faster than the independent market. Growth in VA was solid, and growth in Canada was also strong.

Looking beyond Europe and North America, we estimate that market unit growth in Rest of world was 7%. Growth in Japan was strong, whereas in China, growth decelerated, although we estimate that it remained slightly positive in the period. Growth in Australia was negative, but we estimate that several emerging markets delivered good growth in Q3.

Diagnostics market

We estimate that, compared to the same period last year, the market growth rate in Q3 was in line with the estimated structural growth rate of 3-5% per year, albeit likely at the low end of the range due to weak market momentum in China.

Hearing Aids

Our total Hearing Aids business delivered strong organic growth of 21% in Q3 thanks to 25% organic growth in sales to external customers. This was the result of broad-based commercial momentum and was boosted by the successful launches of new premium hearing aids in Q1, which has led to market share gains across markets and channels. Growth was primarily driven by unit growth, and the ASP development was slightly positive.

In Europe, we saw double-digit organic growth, particularly in Germany and the UK, but many of our other markets also saw good performance in Q3. In France, growth was slightly positive in Q3 despite negative market developments in the period.

North America delivered strong double-digit growth in Q3 driven by both the US and Canada. In the US commercial market, we continued to see good sales momentum in chains and independents, and in VA, we saw strong growth helped by the launch of Oticon Real at the beginning of May. Following strong growth in H1, Canada continued its good performance in Q3.

In Asia, organic growth was strong. In Japan, incremental market share gains continued to drive strong growth, but in China, growth was negative in the period. In the Pacific region, we saw negative organic growth, partially due to low market growth in Australia, whereas in our Rest of World region, mostly comprising emerging markets, we saw strong double-digit growth, especially in South America.

Hearing Care

Hearing Care delivered solid performance in Q3 with organic growth of 6%. Acquisitive growth was also 6%, driven in particular by Germany but also by a number of minor acquisitions in other markets. Similar to H1, organic growth was driven by good momentum in our medium-sized markets. Our two biggest markets, the US and France, grew at a slower pace, with France in slightly negative growth territory, due to negative market developments. Organic growth was predominantly driven by units, but we continued to also experience a slight tailwind from an increasing ASP.

Regionally, Europe was the largest growth driver thanks to positive developments in several markets. Poland continued to see particularly strong growth, and also the UK delivered good growth. In France, we saw slightly negative organic growth, which was a drag on total Hearing Care growth in Q3, but the growth rate was still better than the market growth rate.

Organic growth in North America was positive thanks mostly to the US, which was helped by low comparative figures and strong market growth rates in Q3, although market growth was primarily driven by managed care. Following our strategic decision last year to reduce our share of sales related to managed care, we have increased our focus on the private pay part of the market, which has led to a stabler business model and supported the ASP development and profitability. Canada also saw slightly positive organic growth.

In our other geographies, Australia saw slightly positive organic growth in Q3. In China, Sheng Wang saw weaker-than-expected revenue due to weak market dynamics but still delivered positive organic growth helped by low comparative figures.

Diagnostics

Organic growth in Diagnostics was 6%, which is above the estimated market growth rate. In addition, the business area saw acquisitive growth of 2%, mainly related to minor acquisitions in previous quarters. Overall, growth in Q3 was solid despite a slightly negative impact of weak market dynamics in China, and we continued to see a good order intake.

In terms of geographies, organic growth was driven by Europe, where we saw good growth in several markets, and by the US. In Asia, we saw negative organic growth due to weak market dynamics in China. In terms of product categories, Diagnostics mainly generated growth in the service business, which performed strongly in Q3, but instruments for balance testing and audiometers also performed well.

Communications

Market trends

After a weak H1 2023, we estimate that the market growth rate for enterprise solutions and gaming headsets continued to be negative in Q3. Both market segments continued to see tough market conditions with lower spending by both corporates and consumers, and visibility remains limited.

Communications (EPOS)

Our Communications business saw organic growth of -20% in Q3 because of weak market development and significant pressure on our realised sales prices due to promotional activities and to sales of legacy, co-branded products at discounted prices. Compared to last year, we continued to see negative organic growth in all regions.

As announced on 29 August, Demant has decided to gradually wind down its Gaming business following a review of the future growth potential and competitiveness of the business. Following this decision, we have focused on reducing our inventory of gaming products, and while revenue in Gaming grew slightly in Q3, sales prices were lower than anticipated due to very significant promotional activities. This negatively impacted profitability in Communications in Q3 and is expected to have an additional negative one-off EBIT impact of DKK 50-100 million in H2.

In Q3, Enterprise Solutions accounted for approx. 85% of Communications revenue, and organic growth was -24%, as we continued to be impacted by material hesitation to buy among end-customers, a factor that we expect will continue throughout H2. Looking ahead, we will in Enterprise Solutions focus on solidifying our position in a number of target markets, on further strengthening our product portfolio of premium audio and video solutions for enterprises and on expanding our distribution partnerships.

As a step in this direction, EPOS is today announcing a strategic agreement with Lenovo to provide high-quality audio solutions for business professionals. Through the agreement, EPOS will be Lenovo's global audio partner for PC audio accessories, which entails the inclusion of the EPOS portfolio in Lenovo's third-party reseller programme and the co-development of future hardware, software and services to create professional audio solutions. The agreement will have limited impact in 2023, but we expect a positive contribution to growth in 2024.