Company announcement no 2014-04

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Interim information, first quarter

Significant unit growth in the Group's core business despite low market growth in North America

- Driven by acquisitions carried out in 2013 as well as organic growth, the Group realised fair revenue growth in local currencies in the first quarter. As expected, exchange rate fluctuations adversely affected both revenue and earnings.
- In the first quarter, the global market for hearing aids saw a unit growth rate somewhat above the expected interval of 2-4% unit growth for the full year. We estimate that the average selling price on the market went down in the first quarter, which is mainly due to the inter-country mix shifts we have seen between Germany and North America in particular. We thus estimate that in terms of value, the global market growth rate was slightly positive in the first quarter.
- Introduced with great success in all markets in February, Oticon Ria is the third complete product family based on Oticon's strong technological platform. Together with the sale of Oticon Nera and Oticon Alta, which continues to be satisfactory, this further strengthening of the product portfolios of our core business has contributed to securing significant unit growth. Our unit growth rate was high in Asia and Europe, and particularly in Germany, whereas sales in North America were hampered by very low market growth.
- Oticon's Made for iPhone (MFi) connectivity solution for hearing aids has significantly strengthened Oticon's total product offering since the end of the first quarter and was very well received by end-users and hearing care professionals alike.
- In the first quarter, our Group delivered strong cash flow and a modest level of acquisitions. This means that year-to-date we have bought back shares worth DKK 211 million and that for the 2014 full year, we maintain our expectation to buy back shares worth more than DKK 500 million.
- We maintain our previously announced outlook for 2014, including our expectation to generate growth in all our business activities and to deliver a rise in earnings per share of 5-10%. Acquisitions are expected to contribute by 3-4% to Group revenue in 2014, even though we expect more than half of this impact to be offset by the Group's weakened invoicing currencies. Foreign exchange rates are expected to negatively affect the Group's operating profit (EBIT) in 2014 by around DKK 100 million compared with 2013.

Market trends

In the first quarter, market growth in North America was very modest, and the overall unit growth rate of 1% in the USA was somewhat below the historical average market growth rate. The private sector of the US market saw flat unit growth, and growth was thus solely driven by VA that grew by just over 4%. The very low growth in North America can largely be attributed to the unusual winter weather in the first months of the year. However, a positive change in March in North America means that for the remaining part of the year, we expect a higher growth level for the region. Unit growth in Europe developed favourably on the comparative quarter, which was adversely impacted by changes in the reimbursement schemes in countries such as the Netherlands and Denmark. In Germany, unit growth was particularly high in the first quarter due to the changed reimbursement regulations that became effective on 1 November last year, and with a unit growth rate of just under 40%, Germany had a substantial positive impact on overall European unit growth. The rise in unit sales on the Japanese market was within our usual expectations of a 2-4% unit growth rate compared with the first quarter of 2013. We estimate that in the first quarter, global unit growth on the market was somewhat above the expected interval of 2-4% for the full year. This is, among other factors, due to weaker comparative figures as a result of the timing of Easter and thus fewer sales days.

The poor transparency in average selling price trends on the market and the absence of official price statistics mean that as usual, the average selling price on the market is largely based on our estimate. The first quarter of 2014 was characterised by country and channel mix shifts, which can particularly be attributed to the fact that global market growth is mainly to be found outside North America, e.g. in Germany, and also on the fact that we have seen zero growth in the private sector of the US market. To the best of our belief, the average selling price on the market thus decreased in the first quarter and based on that, we estimate that in the first quarter, global market growth in value was slightly positive.

Hearing Devices

The Group's core business, wholesale of hearing aids, generated significant unit growth in the first quarter. Our unit growth, which can partly be attributed to strengthened product portfolios in all our three hearing aid brands, was rather pronounced in Asia and Europe, and particularly in Germany, whereas corporate sales in North America were hampered by low market growth. The turning point in the market growth we saw in March in North America has increased our sales momentum – a trend that has continued into the second quarter.

The global launch in February of Oticon Ria in all styles was successful. Preliminary feedback from customers has been very positive, and the general sentiment is that performance is better in Oticon Ria than in its predecessor Oticon Ino. Positioned in the lower price categories, Ria is the third complete product family based on Oticon's strong technological platform. Oticon Nera and Oticon Alta, which belong to the mid-priced and high-end segments, respectively, also saw satisfactory unit growth in the first quarter. Oticon's first Made for iPhone (MFi) connectivity solution for hearing aids attracted positive attention at the recent AudiologyNOW! convention held at the end of March in Orlando, Florida, and has significantly strengthened Oticon's total product offering. Available to all present and future users of Oticon's ConnectLine hearing aids in the entire price spectrum, this solution was very well received by both end-users and hearing care professionals. In addition, the Group's two other hearing aid brands, Bernafon and Sonic, were off to a good start and have delivered satisfactory unit growth. At the end of 2013, Bernafon launched their mid-priced products Carista 3 and Carista 5 to complement Acriva, and Sonic continues the launch of their successful hearing aid Bliss and have most recently launched Bliss 40.

In the first quarter, Oticon Medical saw satisfactory business trends with increased sales both in bone-anchored hearing systems (BAHS) and in cochlear implants (CI). The revenue increase in the BAHS business was driven by the launch of Ponto Plus at the end of 2013 and also by the fact that sales are beginning to pick up in several new markets. With the recently formed partnership with Professor Bo Håkansson on the development of an active, transcutaneous product concept, our BAHS business is well equipped for a future with a larger product offering to patients with conductive hearing loss and single-sided deafness. Also the CI business showed positive trends in the first quarter, which was characterised by extensive focus on the launch of the Saphyr NEO Collection processor whose improved signal processing features were well received by the market. As far as renewing and strengthening the product range is concerned, the integration of the CI business is in general progressing according to the plans made and is cause for optimism in terms of sales potential. In addition, we continuously strengthen our distribution, as agreements with new distributors fall into place.

In the first quarter, the growth rate in our retail business was in pace with the market growth rate in those countries where the Group operates retail businesses. The unusual weather conditions in North America in January and February had a considerably adverse effect on the retail business, but we saw a significant improvement in growth in March. In Europe and Australia, we have seen positive trends with growth rates exceeding market growth rates.

Other business activities

Diagnostic Instruments generated satisfactory growth in local currencies in the first quarter of which almost half was organic growth. All major markets contributed fairly to growth with the exception of North America where bad weather hampered growth. Especially Interacoustics generated strong sales in the first quarter and has just begun the building of a new domicile in Middelfart, Denmark. Interacoustics expects to move into the new premises at the beginning of the second quarter of 2015.

The Group’s implementation of new IFRS accounting standards, which took effect on 1 January 2014, has eliminated the possibility of proportionate consolidation of joint ventures, including Sennheiser Communications. Thus, the remaining revenue in the business activity Personal Communication only makes up an insignificant part of consolidated revenue, which means that in our interim report for 2014 and going forward, we will no longer show Personal Communication as a separate business activity, but instead include revenue from Phonic Ear and FrontRow in the business activity Hearing Devices. As far as comparative figures for 2013 are concerned, this means that revenue in Personal Communication will decrease by DKK 248 million, since Sennheiser Communications will no longer be proportionately consolidated, and that the remaining revenue of DKK 131 million from Phonic Ear and FrontRow will be transferred to Hearing Devices.

Other matters

As expected, the acquisition level in the first quarter was relatively low, and since we have in this period – as usual – generated significant cash flows, we have continued our share buy-back programme. Year-to-date, the Company has thus bought back a total of 426,315 shares worth DKK 211 million. The Group’s overall portfolio of treasury shares corresponds to 1.1% of the share capital. We will continue to use the share buy-back programme to channel our surplus cash flow back to the shareholders.

Outlook

Based on the market and business trends described in our annual report for 2013, the Group maintains its expectations of 2014.

In 2014, we expect to continue to deliver growth in all of our business activities. Acquisitions are expected to contribute by 3-4% to Group revenue in 2014, mainly driven by acquisitions made in 2013. Based on foreign exchange levels in late February, more than half of the positive impact from acquisitions will be offset by changes in exchange rates.

In consideration of a weakened set of invoicing currencies as well as gains from our hedging activities, exchange rates are expected to negatively affect the Group's operating profit (EBIT) in 2014 by around DKK 100 million compared with 2013. In 2013, the Group once again generated a strong cash flow, reflected in a cash conversion ratio (CFFO/EBIT) of 74%. Also in 2014, we expect to deliver a high cash conversion ratio. Keeping in mind that our near-term acquisition opportunities are rather limited and that our net interest-bearing debt target is DKK 2.0-2.5 billion, we expect to be able to buy back Company shares worth more than DKK 500 million in 2014. In order to maintain a high level of flexibility, this level of share buy-back is subject to change, should additional attractive acquisition opportunities present themselves.

All in all, the Group will continue to deliver growth in earnings in 2014. Following a 14% growth rate in the Group's net profit and earnings per share (EPS) in 2013, we expect to see growth in EPS of 5-10% in 2014.

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