Financial report

Financial review

In the 2019/20 financial year, Sonova achieved sales of CHF 2,916.9 million, an increase of 8.7% in local currencies and 5.6% in Swiss francs. The Group performed well above expectations until the global health and economic crisis resulting from the COVID-19 pandemic severely affected the Group's business activities in the final weeks of the financial year.

Strong organic growth, partly offset in March by COVID-19

In the 2019/20 financial year, Sonova Group reported sales reached CHF 2,916.9 million, an increase of 8.7% in local currencies or 5.6% in Swiss francs. Returns for credit related to the voluntary field corrective action in the Cochlear Implants segment reduced sales by CHF 11.1 million or 0.4%, resulting in adjusted sales of CHF 2,928.0 million, up 9.1% in local currencies or 6.0% in Swiss francs. Adjusted organic growth reached 8.1%, while the net impact of acquisitions and divestments contributed growth of 1.0%. Exchange rate fluctuations had a significant negative impact, reducing growth by 3.1% due to a strengthening of the Swiss franc against most major currencies. In March 2020, most key markets were impacted by significantly lower in-store consumer traffic as a result of restrictions on movement, as well as by reduced cochlear implant surgeries.

Sales by regions

in CHF m	2019/20			2018/19	
	Sales	Share	Growth in local currencies	Sales	Share
EMEA	1,544.4	53%	5.8%	1,521.0	55%
USA	877.6	30%	18.0%	746.7	27%
Americas (excl. USA)	220.9	8%	(0.3%)	228.5	8%
Asia/Pacific	274.0	9%	6.7%	267.0	10%
Total sales	**2,916.9**	**100%**	**8.7%**	**2,763.2**	**100%**

Sales driven by strong performance in North America and solid EMEA and APAC development

Europe, Middle East and Africa (EMEA), the Group's largest region, showed a solid increase in sales of 5.8% in local currencies. Sales were driven by improvements in commercial excellence and further supported by the continued success of Phonak Marvel and the introduction of Marvel 2.0 in August 2019. The performance of the Hearing Instruments business was driven by strong growth in France, the Nordics, and in developing markets. The Audiological Care business benefited from targeted growth initiatives across the region. Sales in the Cochlear Implants business were largely driven by upgrade sales. The EMEA share of Group sales decreased from 55% in 2018/19 to 53% in 2019/20.

Sales in the United States increased by 18.0% in local currency, resulting in solid market share gains. Supported by the continued success of the Phonak Marvel platform and investment in the sales team, the Hearing Instruments business achieved a double-digit increase. Other growth drivers included the introduction of Phonak Audéo™ Marvel to the US Department of Veterans Affairs (VA) in May 2019 and a new private label contract with a large US hearing aid retailer. The Cochlear Implants segment started the year strongly supported by the success of the HiRes™ Ultra 3D implant and strong upgrade sales, but slowed down in the second half. The region accounted for 30% of Group sales in 2019/20 versus 27% in the prior year. Sales in the rest of the Americas (excluding the US) were flat in local currencies. Strong growth of our Audiological Care and Cochlear Implants business in Brazil was offset by the discontinuation of distribution of certain non-Sonova products in the country.

Sales in the Asia/Pacific (APAC) region rose by 6.7% in local currencies, driven by double-digit growth in the Hearing Instruments business. Strong growth in Australia, Korea and India were partly offset by the COVID-19 impact on China starting in February and by weaker growth in New Zealand.

Sonova Group key figures

in CHF m unless otherwise specified	**2019/20**	**2018/19**	**Change in Swiss francs**	**Change in local currencies**
Sales	2,916.9	2,763.2	5.6%	8.7%
Gross profit	2,083.6	1,966.2	6.0%	9.7%
EBITA[1]	554.3	582.5	(4.8%)	1.0%
EBIT[1]	510.0	536.2	(4.9%)	1.2%
Basic earnings per share (CHF)	7.61	6.98	9.0%	16.7%
Operating free cash flow[1]	638.5	411.8	55.1%	
ROCE[1]	18.2%	20.6%		
Sales (adjusted)[1]	2,928.0	2,763.2	6.0%	9.1%
Gross profit (adjusted)[1]	2,106.9	1,975.1	6.7%	10.4%
EBITA (adjusted)[1]	620.8	594.0	4.5%	10.4%
EBITA margin (adjusted)	21.2%	21.5%		
Basic earnings per share (CHF) (adjusted)[1]	7.39	7.11	4.0%	11.6%

[1] For detailed definitions, please refer to "5 year key figures".

Operating margin affected by significant FX headwinds

Reported gross profit reached CHF 2,083.6 million. In addition to the above mentioned returns for credit, this included restructuring costs of CHF 1.5 million related to further improving the operating structure and one-time costs of CHF 10.8 million related to Advanced Bionics' voluntary field corrective action (2018/19 restructuring costs: CHF 8.8 million). Adjusted for these costs, gross profit reached CHF 2,106.9 million, an increase of 10.4% in local currencies and 6.7% in Swiss francs. The adjusted gross profit margin was 72.0%, up from 71.5% in the prior year. The improvement was driven by higher unit volumes and a rise in average sales price (ASP) in the Hearing Instruments business, reflecting the continued positive market response to the Marvel platform as well as operating improvements. This was partly offset by a significant headwind from currency exchange rates and additional costs because of the higher proportion of rechargeable products.

Excluding acquisition-related amortization, reported operating expenses were CHF 1,529.3 million (2018/19: CHF 1,383.7 million). These included restructuring costs of CHF 17.2 million as well as one-time costs of CHF 26.0 million related to Advanced Bionics' voluntary field corrective action (2018/19 restructuring costs: CHF 2.6 million). In the following, we refer to operating expenses adjusted for these items. Adjusted operating expenses before acquisition-related amortization rose by 10.4% in local currencies or by 7.6% in Swiss francs to CHF 1,486.2 million.

Adjusted research and development (R&D) expenses before acquisition-related amortization were CHF 163.2 million, outpacing sales growth with an increase of 10.8% in local currencies, underpinning Sonova's ambition to lead innovation in audiological performance and consumer experience. Technology developments in apps, connectivity, reliability, and comfort represented an important share of R&D efforts. R&D spending as a percentage of sales increased to 5.6% (2018/19: 5.4%).

Adjusted sales and marketing costs before acquisition-related amortization were up 9.1% in local currencies to CHF 1,023.8 million. The increase reflects continued investment in strengthening Audiological Care's store network and lead generation capabilities, as well as expanding the customer-facing sales force of the Hearing Instruments and Cochlear Implants businesses to increase coverage and improve commercial execution.

Adjusted general and administrative costs increased by 13.5% in local currencies to CHF 299.3 million, representing 10.2% of sales, up from 9.7% in the prior year. This includes an increase in the allowance for doubtful receivables of CHF 20.3 million, largely reflecting a higher customer default risk related to the COVID-19 pandemic. The remaining increase of 5.6% in local currencies includes investment in a new integrated IT platform for the Audiological Care business and provisions for contract obligations to health insurance providers in the first half of the financial year.

Adjusted other income for the current period was CHF 0.1 million. This compares to CHF 4.4 million in the prior year, which was mainly related to a release of provisions for cochlear implant product liabilities.

Adjusted operating profit before acquisition-related amortization (EBITA) was CHF 620.8 million (2018/19: CHF 594.0 million), an increase of 10.4% in local currencies or 4.5% in Swiss francs. The adjusted EBITA margin was 21.2% (2018/19: 21.5%). A solid underlying margin development was more than offset by significant currency headwinds and the increase in the allowance for doubtful receivables related to the COVID-19 pandemic, which together reduced the adjusted EBITA margin by 1.2 percentage points. The reported EBITA increased by 1.0% in local currencies but declined by 4.8% in Swiss francs to CHF 554.3 million, corresponding to a margin of 19.0%. Acquisition-related amortization amounted to CHF 44.4 million (2018/19: CHF 46.3 million). Reported operating profit (EBIT) reached CHF 510.0 million (2018/19: CHF 536.2 million), down 4.9% in Swiss francs.

Earnings per share – Double digit increase in local currencies

Net financial expenses, including the result from associates, increased from CHF 6.6 million to CHF 7.6 million. As a result of the Swiss tax reform, income taxes were affected positively by CHF 64.1 million, reflecting a revaluation of the Swiss deferred tax positions and a resulting one-time deferred tax income. Excluding this one-time transition impact, the tax rate was 15.3% (2018/19: 13.1%). Income after taxes was CHF 489.5 million (2018/19: CHF 460.2 million). Basic earnings per share (EPS) reached CHF 7.61 (2018/19: CHF 6.98), an increase of 9.0% from the prior year. The adjusted EPS increased 11.6% in local currencies or 4.0% in Swiss francs to CHF 7.39.

Headcount

At the end of March 2020, the Group's total workforce was 15,184 full-time equivalents. This represents a rise of 444 or 3%, well below the local currency sales growth of 8.7%. This was largely driven by increases in R&D and in customer-facing staff in the Audiological Care and Hearing Instruments businesses. Despite a significant growth in volumes, employee numbers in manufacturing were largely unchanged, benefitting from efficiencies and the optimization initiatives announced in March and November 2019. Sonova continues to make progress in its drive to concentrate new hiring in lower-cost locations.

Hearing Instruments segment – Market share gains in both businesses

Sales in the Hearing Instruments segment grew by 9.6% in local currencies and 6.4% in Swiss francs to CHF 2,686.2 million. Organic growth was 8.5%, while the contribution from acquisitions in the reporting period (including the full-year effect of prior year acquisitions) was 1.2%. Prior year disposals reduced growth by 0.1%. Exchange rate fluctuations reduced growth by 3.2% in Swiss francs. As a result of restrictions on movement imposed in March in most major markets in response to the COVID-19 pandemic, audiology stores – both our own and third-party owned – were temporarily closed or operating with reduced hours, representing a significant headwind in the final weeks of 2019/20.

The Hearing Instruments business, which includes sales to independent audiologists, retail chains, multinational and government customers, but excludes our own Audiological Care business, maintained its strong momentum: Sales reached CHF 1,613.0 million, an increase of 11.8% in local currencies, driven by growth in both the number of units sold and ASPs. Strong double-digit growth in the US led to market share gains in all channels including a strong rebound in Sonova's share of business with the US Department of Veterans Affairs (VA). Further contributions came from a new private label contract with a large US hearing aid retailer and increased coverage by managed care. Strong growth in Australia was a further highlight, while growth in Germany was hampered by a temporary decline due to replacement of consignment inventory with loaner products.

The Audiological Care business increased sales by 6.5% in local currencies to CHF 1,073.2 million; the increase was driven by organic growth of 4.0%, supplemented by bolt-on acquisitions accounting for 2.9% of growth; prior-year disposals reduced growth by 0.3%. Most key markets – including the UK, the Netherlands, the Nordics, France, Italy, Brazil, Poland and Austria – achieved above-market growth rates. Improved in-store sales conversion and increasingly centralized lead generation management continued to drive sales. The positive market response to Phonak Marvel also supported growth and helped to increase Phonak's consumer brand awareness.

Sales by business – Hearing Instruments segment

in CHF m	2019/20			2018/19	
	Sales	Share	Growth in local currencies	Sales	Share
Hearing Instruments business	1,613.0	60%	11.8%	1,474.7	58%
Audiological Care business	1,073.2	40%	6.5%	1,050.1	42%
Total Hearing Instruments segment	**2,686.2**	**100%**	**9.6%**	**2,524.8**	**100%**

Reported EBITA for the Hearing Instruments segment amounted to CHF 601.6 million, up 12.5% in local currencies. The structural cost initiatives announced in March and November 2019 progressed according to plan and yielded year-on-year cost improvements of over CHF 10 million with additional savings expected in financial year 2020/21. Restructuring costs related to these initiatives amounted to of CHF 18.6 million (2018/19: CHF 11.5 million). Excluding these restructuring costs, the adjusted EBITA increased by 13.5% in local currencies to CHF 620.3 million, corresponding to an EBITA margin of 23.1% (2018/19: 22.8%).

Cochlear Implants segment – Flat system sales from COVID-19 and voluntary field action, strong upgrade sales

The Cochlear Implants business achieved sales of CHF 230.7 million versus CHF 238.4 in the prior year. This includes returns for credit of CHF 11.1 million in conjunction with the voluntary field corrective action announced in February 2020, which involved the retrieval of un-implanted devices from the initial version of the HiRes Ultra and Ultra 3D cochlear implants. Excluding this, adjusted sales reached CHF 241.8 million, up 3.4% in local currencies and 1.4% in Swiss francs. A strong performance through most of 2019/20 was offset toward the year-end by lower demand related to the postponement of non-essential surgeries in countries affected by COVID-19, as well as by lower demand following the voluntary field corrective action. As a result, system sales were essentially flat for the year in local currencies. Double-digit growth in upgrade revenues was driven by strong momentum in the US and in Germany.

Sales by product groups – Cochlear Implants segment (adjusted)[1)]

in CHF m	2019/20			2018/19	
	Sales	Share	Growth in local currencies	Sales	Share
Cochlear implant systems	175.0	72%	(0.4%)	178.9	75%
Upgrades and accessories	66.8	28%	14.8%	59.5	25%
Total Cochlear Implants segment	**241.8**	**100%**	**3.4%**	**238.4**	**100%**

1) In 2019/20, excluding impacts from returns for credit related to the voluntary field corrective action of CHF 11.1 million.

The reported EBITA loss of CHF 46.2 million includes returns for credit of CHF 11.1 million as well as one-time costs of CHF 36.7 million, both related to the voluntary field corrective action. Excluding these items, the adjusted EBITA for the year was CHF 1.6 million versus CHF 19.7 million in the prior year, resulting in a margin of 0.7% (2018/19: 8.2%). A solid performance in the first half of the year, driven by higher volume, operational efficiency improvements and higher ASPs on upgrades and systems, was offset by a sharp decline in adjusted sales toward the year-end.

Strong growth in cash flow

Cash flow from operating activities was CHF 843.3 million, compared to CHF 533.2 million in the prior year. Growth was largely driven by improvements in working capital changes of CHF 194.7 million, in large part from better receivables collections. In addition, the adoption of IFRS 16 resulted in a positive one-time effect of CHF 68.3 million with a corresponding offset in the cash outflow from financing activities. Net investments in tangible and intangible assets increased to CHF 127.7 million from CHF 117.3 million in the prior year, mainly as a result of investments in IT systems and store improvements in the Audiological Care business.

Operating free cash flow, including payments for lease liabilities of CHF 68.3 million, reached CHF 638.5 million, up by 55.1% over the prior year and resulting in a strong cash conversion of 103%. Cash consideration for acquisitions net of disposals amounted to CHF 74.8 million, up from 64.9 million in the prior year. In summary, this resulted in a free cash flow of CHF 563.7 million, up by 62.5% over the prior year.

Cash outflow from financing activities was CHF 550.4 million, compared to CHF 522.1 million in the prior year. This largely reflects net share repurchases of CHF 470.1 million, mainly related to the share buyback program prior to its suspension in February. Cash outflow from financing also includes dividend payments of CHF 186.5 million and CHF 68.3 million for leases, based on IFRS 16, which was adopted for the first time this fiscal year.

Balance sheet remains strong

Reported net working capital was negative at CHF –18.9 million, compared to CHF 163.0 million at the end of the prior year. This is due to a CHF 138.5 million reduction in accounts receivables, stemming both from improved collection throughout the year, including during the slowdown in March, and from lower sales towards the end of the year. Despite significant sales growth, inventories were reduced by CHF 16.6 million year-on-year through better inventory management. Capital employed was CHF 2,692.5 million, a slight increase from CHF 2,630.0 million in the prior year. An increase from the adoption of IFRS 16 and a one-time capitalization of deferred tax assets as a result of the Swiss tax reform was largely offset by the impact of the strength of the Swiss franc on assets held in foreign currencies.

The Group's equity position amounted to CHF 2,029.4 million, down from CHF 2,376.1 million in the previous year, partly as a result of the share buyback program (which was paused on March 16, 2020 to avoid cash outflow during the COVID-19 crisis); the result was an equity ratio of 45.2%. The net debt position stood at CHF 663.0 million, compared to CHF 253.9 million at the end of the prior year. This increase was expected as a result of the share buyback and was in line with a previously announced debt leverage target. The return on capital employed (ROCE) decreased to 18.2% from 20.6% in the prior year, primarily driven by the adoption of IFRS 16 and further impacted by the strength of the Swiss Franc.

Dividend proposal

At the Annual General Shareholders' Meeting in June 2020, the Board of Directors will propose a stock dividend. The required number of Sonova shares would be sourced from shares bought back under the recent share buyback program, which have not yet been canceled. Each shareholder would be entitled to receive one Sonova share for 150 existing Sonova shares with fractions paid out in cash. This represents a further measure to ensure a good liquidity level for Sonova and an attractive alternative for our shareholders during these challenging times.

Outlook

Global uncertainty about the development of the COVID-19 pandemic prevents accurate guidance for the 2020/21 financial year. However, the attractive fundamentals of the hearing care market remain very much intact and the Group is confident that the market will rebound following these temporary challenges. Sonova is well prepared to master these difficult times and expects that the Group will continue to grow faster than the market and will further expand its strong competitive position.

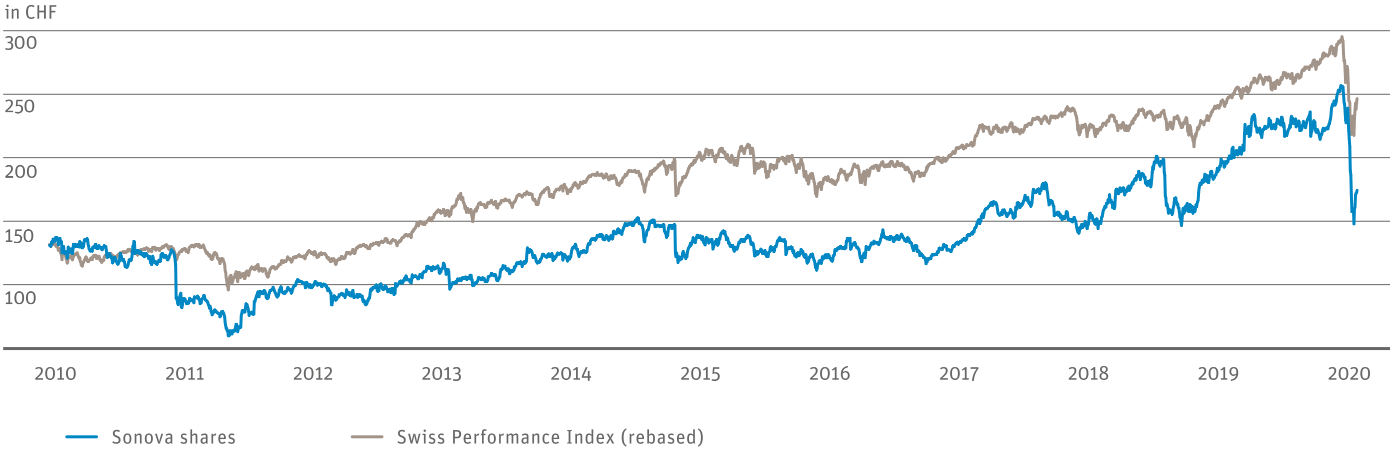
Reconciliation of non-GAAP financial measures

April 1 to March 31, CHF million					2019/20
	Income statement as reported	Acquis. related amortization	**Income statement EBITA separation**	Adjustments[3]	**Income statement adjusted**
Sales	**2,916.9**		**2,916.9**	**11.1**	**2,928.0**
Cost of sales	(833.3)		(833.3)	12.2	(821.1)
Gross profit	**2,083.6**		**2,083.6**	**23.3**	**2,106.9**
Research and development	(167.0)	0.9	(166.1)	2.9	(163.2)
Sales and marketing	(1,074.3)	43.5	(1,030.8)	6.9	(1,023.8)
General and administration	(309.0)		(309.0)	9.7	(299.3)
Other income/(expenses), net	(23.4)		(23.4)	23.6	0.1
Operating profit before acquisition-related amortization (EBITA)[1]			**554.3**	**66.4**	**620.8**
Acquisition-related amortization		(44.4)	(44.4)		(44.4)
Operating profit (EBIT)[2]	**510.0**		**510.0**	**66.4**	**576.4**
Basic earnings per share (CHF)			**7.61**	**(0.22)**	**7.39**

April 1 to March 31, CHF million					2018/19
	Income statement as reported	Acquis. related amortization	**Income statement EBITA separation**	Adjustments[3]	**Income statement adjusted**
Sales	**2,763.2**		**2,763.2**		**2,763.2**
Cost of sales	(797.0)		(797.0)	8.8	(788.1)
Gross profit	**1,966.2**		**1,966.2**	**8.8**	**1,975.1**
Research and development	(149.4)	1.0	(148.4)	0.6	(147.8)
Sales and marketing	(1,015.7)	45.4	(970.3)	1.3	(969.1)
General and administration	(269.3)		(269.3)	0.8	(268.6)
Other income/(expenses), net	4.4		4.4		4.4
Operating profit before acquisition-related amortization (EBITA)[1]			**582.5**	**11.5**	**594.0**
Acquisition-related amortization		(46.3)	(46.3)		(46.3)
Operating profit (EBIT)[2]	**536.2**		**536.2**	**11.5**	**547.7**
Basic earnings per share (CHF)	**6.98**		**6.98**	**0.13**	**7.11**

1) Earnings before financial result, share of profit/(loss) in associates/joint ventures, taxes and acquisition-related amortization (EBITA).
2) Earnings before financial result, share of profit/(loss) in associates/joint ventures and taxes (EBIT).
3) In 2019/20, excluding one-time costs and returns for credit related to the voluntary field corrective action in the Cochlear Implants segment of CHF 47.8 million and restructuring costs in the Hearing Instruments segment of CHF 18.6 million (2018/19: CHF 11.5 million).

Share price development – Sonova versus Swiss Performance Index (rebased)



Share price performance history[1)]

	10 years	5 years	3 years	2 years	1 year
Sonova shares	33.1%	28.9%	25.6%	14.9%	-11.5%
Swiss Performance Index (SPI)[2)]	88.4%	23.9%	17.4%	11.1%	0.7%
Sonova shares relative to the SPI	-55.3%	+5.0%	+8.1%	+3.8%	-12.2%

1) Performance of the Sonova shares and SPI refers to the respective period prior to the last trading day of the 2019/20 financial year.
2) The Swiss Performance Index (SPI) is considered Switzerland's overall stock market index. It comprises practically all of the SIX Swiss Exchange-traded equity securities of companies that are domiciled in Switzerland or the Principality of Liechtenstein.