Appendix 4D

Cochlear Limited
Half Yearly Report
As at 31 December 2018

Results for announcement to the market

		Movement from 31 December 2017		$m
Sales Revenue	up	11%	to	711.9
Total Revenue	up	8%	to	703.8
Earnings before interest and taxes (EBIT)	up	10%	to	177.0
Net profit for the period attributable to members	**up**	**16%**	**to**	**128.6**
Basic earnings per share (cents)	up	16%	to	223.1
Dividend (dollars)	up	11%	to	$1.55

Net tangible assets per share at 31 December 2018 (cents)	up	23%	to	493.3
Net tangible assets per share at 31 December 2017 (cents)				401.1

Dividends	Amount per security	Franked amount per security	Conduit foreign income per security
Interim dividend per share (dollars)	$1.55	$1.55	$0.00
Previous corresponding period (dollars)	$1.40	$1.40	$0.00

Record date for determining entitlements to the dividend	Tuesday 26 March 2019
Dividend payment date	Tuesday 16 April 2019

No dividend reinvestment plans were in operation during or since the half-year.

Additional Appendix 4D disclosure requirements can be found in the 31 December 2018 Interim financial report lodged with this document. This report is based on the 31 December 2018 Interim financial report which has been reviewed by KPMG with the Independent auditor’s review report included in the 31 December 2018 Interim financial report.

Cochlear Limited and its controlled entities

ACN 002 618 073
Interim financial report
31 December 2018

The directors present their report, together with the consolidated interim financial report of the Consolidated Entity (Cochlear), being Cochlear Limited (the Company) and its controlled entities, for the half year ended 31 December 2018 and the auditors' review report thereon.

Directors

The directors of the Company during or since the end of the interim period are:

Name	**Period of directorship**
Non-executive directors	
Mr Rick Holliday-Smith, *Chairman*	Director since March 2005
Mrs Yasmin Allen	Director since August 2010
Mr Glen Boreham, AM	Director since January 2015
Professor Edward Byrne, AC	Director from July 2002 to 16 October 2018
Ms Alison Deans	Director since January 2015
Mr Andrew Denver	Director since February 2007
Mr Donal O'Dwyer	Director since August 2005
Professor Bruce Robinson, AM	Director since December 2016
Mr Abbas Hussain	Director since December 2018
Executive directors	
Mr Dig Howitt, *CEO & President*	Director since November 2017 Managing Director since 3 January 2018

Principal activities and review of operations and results

Other than as discussed in this report, there were no significant changes in the nature of operating activities during the half year ended 31 December 2018 and the results of those operations are set out below.

Review of operations

The following provides a summary of Cochlear's performance for the half year ended 31 December 2018.

	31 Dec 2018 $m	31 Dec 2017 $m
Total Revenue	**703.8**	**649.6**
Sales revenue[1]	711.9	639.6
Earnings before interest and tax (EBIT)	177.0	160.4
Profit attributable to members	**128.6**	**110.8**
Basic earnings per share (cents)	223.1	192.7
Diluted earnings per share (cents)	223.0	192.5
Interim dividend per share (dollars)	$1.55	$1.40

[1] Sales revenue is the primary revenue reporting measure used by Cochlear for the purpose of assessing revenue performance of the Consolidated Entity. It represents total revenue excluding foreign exchange (FX) contract gains/(losses).

Product and service highlights

	31 Dec 2018 $m	31 Dec 2017 $m	Change % (Reported)	Change % (CC) [1]
Cochlear implants (units)	16,740	15,972	⬆ 5%	
Sales revenue				
Cochlear implants	413.9	393.3	⬆ 5%	⬆ 0%
Services (sound processor upgrades and other)	207.2	161.6	⬆28%	⬆21%
Acoustics (bone conduction and acoustic implants)	90.8	84.7	⬆ 7%	⬆ 1%
Total sales revenue	**711.9**	**639.6**	**⬆11%**	**⬆ 6%**

[1] Constant currency (CC) removes the impact of foreign exchange (FX) rate movements and FX contract gains/(losses) to facilitate comparability. See Notes on page 10 for further detail.

Cochlear implants – 58% of sales revenue

Cochlear implant revenue grew 5% (0% in CC) with unit growth of 5%. Cochlear's developed markets business, which represents around 80% of revenue, delivered units and CC revenue in line with last year.

The US experienced a lower rate of growth with a loss of share following a competitor product launch. Western European growth was affected by a combination of factors including health budget constraints in a few markets and increased competitor activity. Japan was the highlight, growing strongly following the expansion of indications and funding for cochlear implants in late 2017.

The seniors segment continues to be the fastest growing segment across the developed markets as awareness increases. Surgeries for seniors, in the US in particular, are increasingly being driven by the company's successful direct-to-consumer marketing campaigns, with a small but growing number being referred from the hearing aid channel.

Emerging markets units grew by over 15%. Emerging markets provide a long-term growth opportunity with growing awareness and affordability for cochlear implants. Cochlear continues to increase its direct presence across all regions.

Services (sound processor upgrades and other) – 29% of sales revenue

Reported Services sales revenue increased by 28% (21% in CC). Sound processor upgrade revenue increased by 26% in CC driven by strong uptake of the Nucleus 7 Sound Processor. The growing recipient base, initiatives to strengthen connectivity with recipients as well as the product's market leading functional and lifestyle features, have all contributed to the strong Services growth.

Cochlear continues to invest to provide its growing customer base with a world-class customer experience with increased connectivity and engagement. Cochlear Family, the recipient membership program, provides Cochlear with the opportunity to connect directly with recipients to provide service and support. Membership continues to grow rapidly, increasing by 20% since June 2018, to now exceed 120,000 members with an acceleration in recruitment in recent years driven by a combination of direct outreach programs and improvements in customer onboarding.

Cochlear Family members upgrade to new technology at a greater rate than non-members and adopt new products more rapidly. They are also more likely to volunteer to provide implant candidates with support on their hearing loss journey, an important factor for many in deciding to proceed to surgery.

Acoustics (bone conduction and acoustic implants) – 13% of sales revenue

Reported Acoustics revenue increased by 7% (1% in CC) with solid demand continuing for the Baha 5 sound processor range.

Regional review

Sales revenue	31 Dec 2018 $m	31 Dec 2017 $m	Change % (Reported)	Change % (CC)
Americas	350.5	317.2	⬆ 10%	⬆ 3%
EMEA (Europe, Middle East and Africa)	248.4	221.7	⬆ 12%	⬆ 8%
Asia Pacific	113.0	100.7	⬆ 12%	⬆ 8%
Total sales revenue	**711.9**	**639.6**	**⬆ 11%**	**⬆ 6%**

Americas (US, Canada & Latin America) – 49% of sales revenue

Reported sales revenue increased by 10% (3% in CC). The US experienced a lower rate of growth with a loss of share following a competitor product launch. Services performed strongly driven by upgrades to the Nucleus 7 Sound Processor.

The business continues to invest in expanding field sales and direct-to-consumer marketing in the US with a growing emphasis on working with the hearing aid channel to grow referrals. The Cochlear Provider Network is expanding rapidly and is increasing education of the indications and benefits of cochlear implants to hearing aid audiologists and providing a referral pathway to cochlear implant surgeons.

EMEA (Europe, Middle East and Africa) – 35% of sales revenue

Reported sales revenue increased by 12% (8% in CC). Unit growth in Western Europe was affected by a combination of factors including health budget constraints in a few markets and increased competitor activity, particularly in Germany. Services however performed strongly driven by upgrade demand for the Nucleus 7 Sound Processor.

Western Europe continues to invest in expanding the field sales organisation, building its market access resources and direct-to-consumer marketing to build awareness of cochlear implants and drive demand at clinics.

Expansion of indications and funding for cochlear implantation in Western Europe is a key opportunity, with expectations of an expansion of indications and funding for the UK in the coming months.

Units and sales revenue across EMEA's emerging markets grew strongly as a result of the timing of a number of tenders and is underpinned by investments in the organisation in recent years.

Asia Pacific (Australasia & Asia) – 16% of sales revenue

Reported sales revenue increased by 12% (8% in CC). Japan experienced strong unit growth, with Australia delivering strong growth in sound processor upgrades. Solid unit growth was delivered across a number of smaller countries in the region driven by a combination of tender activity, expanded indications and Cochlear's growing presence.

There were only a small number of Chinese Central Government tender units delivered in both HY19 and HY18, with no impact on revenue growth for the region.

Financial review

Profit & loss

	31 Dec 2018 $m	31 Dec 2017 $m	Change % (Reported)	Change % (CC)
Sales revenue	**711.9**	**639.6**	**11%**	**6%**
Costs of goods sold	179.5	176.4	2%	(2%)
% gross margin	*75%*	*72%*	*3 pts*	*2 pts*
Selling, marketing and general expenses	216.1	189.1	14%	10%
Administration expenses	47.5	44.2	7%	7%
Research and development expenses	88.2	80.6	9%	8%
% of sales revenue	*12%*	*13%*		
Total expenses	**531.3**	**490.3**	**8%**	**5%**
Other net income	4.5	1.1		
FX contract (losses) / gains	(8.1)	10.0		
Earnings before interest and tax (EBIT)	**177.0**	**160.4**	**10%**	**11%**
% of sales revenue	*25%*	*25%*		
Net finance expense	2.7	3.8	(29%)	
Income tax expense	45.7	45.8	0%	
% effective tax rate	*26%*	*29%*		
Net profit	**128.6**	**110.8**	**16%**	**16%**
Net profit margin %	*18%*	*17%*		

Reported sales revenue increased by 11% (6% in CC) to $711.9 million while total expenses increased by 8% (5% in CC) to $531.3 million. As a result, the business generated an EBIT increase of 10% (11% in CC) to $177.0 million, with the EBIT margin remaining stable at 25%.

Key points of note:

- Reported cost of goods sold increased by 2% (down 2% in CC) to $179.5 million, reflecting manufacturing efficiencies, lower warranty costs and lower repair expenses resulting from the centralisation of repairs. As a result, gross margin improved by three percentage points to 75%;
- Selling, marketing and general expenses increased by 14% (10% in CC) to $216.1 million. The increase reflects the continued investment in the sales force and direct-to-consumer marketing, with a growing investment in longer-term market growth activities including standard of care and market access initiatives;
- Investment in research and development increased 9% (8% in CC) to $88.2 million, representing 12% of sales revenue;
- Other net income of $4.5 million includes $5.3 million relating to a release in the contingent consideration value of Sycle and a $3.5 million write down in the investment in Earlens; and
- The effective tax rate reduced from 29% to 26% primarily reflecting the impact of the $5.5 million revaluation of the deferred tax asset in HY18, a result of the changes to the US federal corporate tax rate.

Cash flow

	31 Dec 2018 $m	31 Dec 2017 $m	Change $m
EBIT	177.0	160.4	16.6
Depreciation and amortisation	17.5	15.4	2.1
Changes in working capital and other	19.0	(24.2)	43.2
Net interest paid	(2.7)	(3.7)	1.0
Income taxes paid	(46.7)	(55.2)	8.5
Operating cash flow	**164.1**	**92.7**	**71.4**
Capital expenditure	(36.0)	(15.1)	(20.9)
Acquisition of other intangible assets	(8.7)	(1.4)	(7.3)
Other investments	(20.9)	(3.4)	(17.5)
Free cash flow	**98.5**	**72.8**	**25.7**

Operating cash flow increased by $71.4 million to $164.1 million and free cash flow increased by $25.7 million to $98.5 million.

Key points of note:

- EBIT increased by $16.6 million driven by the 11% increase in sales revenue;
- Changes in working capital and other increased by $43.2 million, primarily reflecting a reduction in trade receivables;
- Capital expenditure (capex) increased by $20.9 million to $36.0 million, reflecting stay in business capex as well as the commencement of construction of the China manufacturing facility;
- Acquisition of intangible assets primarily relates to investments in IT software; and
- Other net investments of $20.9 million primarily relates to the investment in Nyxoah, a medical device company focused on the development and commercialisation of a best-in-class hypoglossal nerve stimulation therapy for the treatment of Obstructive Sleep Apnea.

Capital employed

	31 Dec 2018 $m	30 Jun 2018 $m	Change $m
Trade receivables	275.0	299.1	(24.1)
Inventories	176.5	167.4	9.1
Less: Trade and other payables	(144.1)	(140.5)	(3.6)
Working capital	307.4	326.0	(18.6)
Working capital / sales revenue[1]	*22%*	*24%*	*(2%)*
Debtor days	*69*	*69*	*-*
Inventory days	*178*	*171*	*7*
Property, plant and equipment	140.9	128.4	12.5
Intangible assets	368.8	345.3	23.5
Other net liabilities	(90.9)	(102.7)	11.8
Capital employed	**726.2**	**697.0**	**29.2**

[1] Based on doubling HY19 sales revenue.

Capital employed increased by $29.2 million to $726.2 million since June 2018.

Key points of note:

- Working capital decreased by $18.6 million driven by a reduction in trade receivables. The improvement is a combination of a strong focus on collections and business mix, with a lower mix of tenders with long payment terms; and
- Intangible assets increased by $23.5 million to $368.8 million primarily reflecting investments in IT.

Net debt

	31 Dec 2018 $m	30 Jun 2018 $m	Change $m
Loans and borrowings:			
Current	3.5	3.7	(0.2)
Non-current	161.5	144.0	17.5
Total debt	165.0	147.7	17.3
Less: Cash and cash equivalents	(92.3)	(61.5)	(30.8)
Net debt	**72.7**	**86.2**	**(13.5)**
Weighted average debt maturity[1]	3.3 years	3.8 years	(0.5) years
AUD debt	69%	98%	(29%)

[1] Based on facility limits.

Net debt decreased by $13.5 million to $72.7 million since June 2018, driven by improved earnings.

Dividends

	31 Dec 2018	31 Dec 2017	% Change
Interim ordinary dividends (per share)	$1.55	$1.40	11%
Payout ratio %	70%	73%	
Franking %	100%	100%	

Strong free cash flow and the continued strength of the balance sheet have supported the declaration of an interim dividend of $1.55 per share, an increase of 11%, franked at 100% and representing a payout of 70% of net profit.

The record date for determining dividend entitlements is 26 March 2019 and the interim dividend will be paid on 16 April 2019.

Patent dispute contingent liability

In November 2018, the US District Court awarded damages of USD 268 million against Cochlear Limited and its US subsidiary Cochlear Americas (the Defendants) in the long-running patent dispute with Alfred E. Mann Foundation for Scientific Research (AMF) and Advanced Bionics LLC (AB). The Defendants have appealed the Judgment, including the damages award and the finding of "willfulness" and has arranged an insurance bond of USD 335 million to stay the Judgment pending the appeal.

AMF and AB have subsequently asked the District Court to award USD 123 million in prejudgment interest. The Defendants have opposed both the application and the calculation methodology. The Judge has reserved his decision until further notice. The Defendants have arranged a facility to enable the procurement of an insurance bond to stay execution on any prejudgment interest award pending the outcome of the appeal against damages.

The Board of directors has obtained independent legal advice on the Defendants' appeal prospects. The Board is of the opinion it is probable that the Defendants' appeal will result in the lawsuit being remanded to the District Court for a retrial on damages.

There is significant uncertainty on the final damages award following a retrial. Given the inherent uncertainties in assessing the likely damages amount of this case following the appeal, the Board is unable to make a reliable estimate of the amount that will ultimately be paid to AMF and AB. As a result, the provision for damages held at 30 June 2018 of AUD 21.3 million has been released and a contingent liability is disclosed.

Subsequent to the District Court's November 2018 Judgment, a provision for estimated future costs including legal fees, bond costs and other costs associated with defending this matter was made. As at 31 December 2018, AUD 19.6 million of the provision remains.

Cochlear's current product portfolio is not affected by this litigation as the patent at issue has expired.

In the event the appeal is unsuccessful, the Board is confident that Cochlear will be able to access debt facilities to fund the existing Judgment and any award of interest and costs.

Notes

Forward looking statements

Cochlear advises that this document contains forward looking statements which may be subject to significant uncertainties outside of Cochlear's control. No representation is made as to the accuracy or reliability of forward looking statements or the assumptions on which they are based. Actual future events may vary from these forward looking statements and it is cautioned that undue reliance not be placed on any forward looking statement.

FY19 financial outlook

For FY19, Cochlear reaffirms its expectations of delivering reported net profit of $265-275 million, an 8-12% increase on FY18. Cochlear expects to continue to deliver growth in revenue and earnings in the coming years, underpinned by the significant investments made in product development and market growth initiatives.

Cochlear will continue to invest operating cash flows in activities aimed at building awareness and market access, with the objective of delivering consistent revenue and earnings growth over the long-term. Cochlear is targeting to maintain the net profit margin, reinvesting any efficiency gains, currency or tax benefits into market growth activities, adapting the pace of investment to revenue growth.

Over the next few years, Cochlear has a number of large long-term investment projects including the development of the China manufacturing facility, with the construction phase expected to be complete by the end of FY20, and investments in IT platforms to strengthen Cochlear's connected health, digital and cyber security capabilities. Cochlear has previously advised the market that these projects are expected to increase capital expenditure levels to $80-100 million per annum over the next few years.

The balance sheet and free cash flow generation remain strong and Cochlear continue to target a dividend payout ratio of around 70% of net profit.

Key guidance considerations for FY19:

- Revenue growth to be driven by the Services business, with strong uptake of the Nucleus 7 Sound Processor, particularly in the first half;
- Expect a lower rate of cochlear implant growth across the developed markets for FY19;
- Emerging market growth rates over time continue to be strong, however, annual growth rates can be variable driven by the timing of tender based activity and macro-economic conditions;
- Continued investment to retain market leadership and drive long-term market growth with the target of maintaining the net profit margin; and
- Forecasting a weighted average AUD/USD exchange rate of 72 cents for FY19 (77 cents in FY18) and AUD/EUR of 0.63 EUR (0.65 EUR in FY18).

Non-International Financial Reporting Standards (IFRS) financial measures

Given the significance of exchange rate movements, the directors believe the presentation of the non-IFRS financial measure, constant currency, is useful for the users of this document as it reflects the underlying financial performance of the business. This non-IFRS financial measure has not been subject to review or audit. However, KPMG has separately undertaken a set of procedures to agree the non-IFRS financial measures disclosed to the books and records of the group.

Constant currency

Constant currency removes the impact of foreign exchange rate movements to facilitate comparability of operational performance for Cochlear. This is done by converting the prior comparable period net profit of entities in the group that use currencies other than Australian dollars at the rates that were applicable to the current period (translation currency effect) and by adjusting for current year foreign currency gains and losses (foreign currency effect). The sum of the translation currency effect and foreign currency effect is the amount by which reported EBIT and net profit is adjusted to calculate the result at constant currency.

Reconciliation of constant currency net profit to reported net profit

	31 Dec 2018	31 Dec 2017	% Change
Net profit (reported)	128.6	110.8	16%
FX contract movement		(18.1)	
Spot exchange rate effect to sales and expenses[1]		18.9	
Balance sheet revaluation[1]		(1.1)	
Net profit (CC)	**128.6**	**110.5**	**16%**

[1] HY19 actual v HY18 at HY19 rates.

Dividends

Dividends paid or declared by the Company since the end of the previous financial year are:

	$m
In respect of the previous year:	
A final ordinary dividend of $1.60 per share, franked to 100% with Class C (100%) franking credits, in respect of the year ended 30 June 2018, paid on 10 October 2018.	92.3

The interim dividend in respect of the current financial year has not been provided for in this financial report as it was not declared until after 31 December 2018. Since the end of the financial half-year, the directors declared an interim dividend of $1.55 100% franked amounting to a total of $89.5m.

Lead Auditor's Independence Declaration under Section 307C of the Corporations Act

The lead auditor's independence declaration is set out on page 12 and forms part of the Directors' Report for the half year ended 31 December 2018.

Rounding off

The Company is of a kind referred to in Australian Securities and Investments Commission (ASIC) (Rounding in Financial/Directors' Reports) Instrument 2016/191 (Rounding instrument) dated 24 March 2016 and in accordance with that Instrument, amounts in the Directors' Report and Financial Report have been rounded off to the nearest one hundred thousand dollars unless otherwise indicated.

Dated at Sydney this 19th day of February 2019.

Signed in accordance with a resolution of the directors:

Director

Director

Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To: the directors of Cochlear Limited

I declare that, to the best of my knowledge and belief, in relation to the review for the half-year ended 31 December 2018 there have been:

(i) no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the review; and

(ii) no contraventions of any applicable code of professional conduct in relation to the review.

KPMG

KPMG

Julian McPherson, *Partner*

Sydney, 19 February 2019

Cochlear Limited and its controlled entities
Consolidated Interim Financial Report
Interim Income Statement
For the half year ended 31 December 2018

	Note	31 Dec 2018 $m	31 Dec 2017 $m
Revenue	2.2	703.8	649.6
Cost of sales	2.3	(179.5)	(176.4)
Gross profit		**524.3**	**473.2**
Selling, marketing and general expenses		(216.1)	(189.1)
Administration expenses		(47.5)	(44.2)
Research and development expenses		(88.2)	(80.6)
Other income	2.4	9.2	1.2
Other expense	2.3	(4.7)	(0.1)
Results from operating activities		**177.0**	**160.4**
Finance income - interest		0.3	0.2
Finance expense - interest		(3.0)	(4.0)
Net finance expense		**(2.7)**	**(3.8)**
Profit before income tax		**174.3**	**156.6**
Income tax expense	3	(45.7)	(45.8)
Net profit		**128.6**	**110.8**
Basic earnings per share (cents)	2.5	223.1	192.7
Diluted earnings per share (cents)	2.5	223.0	192.5

The Consolidated Entity has initially applied AASB 9 and AASB 15 at 1 July 2018. Under the transition methods chosen, comparative information is not restated. See Note 1.5

The notes on pages 18 to 26 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities
Consolidated Interim Financial Report
Interim Statement of Comprehensive Income
For the half year ended 31 December 2018

	31 Dec 2018 $m	31 Dec 2017 $m
Net profit	**128.6**	**110.8**
***Other comprehensive income/*(loss)**		
Items that may be reclassified subsequently to the income statement:		
Foreign currency translation differences	15.0	3.3
Effective portion of changes in fair value of cash flow hedges, net of tax	(18.8)	1.6
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	5.7	(7.0)
Financial investments measured at fair value through other comprehensive income, net of tax	(1.8)	(0.1)
Total items that may be reclassified subsequently to the income statement	0.1	(2.2)
Other comprehensive income/(loss), net of tax	**0.1**	**(2.2)**
Total comprehensive income	**128.7**	**108.6**

The Consolidated Entity has initially applied AASB 9 and AASB 15 at 1 July 2018. Under the transition methods chosen, comparative information is not restated. See Note 1.5

The notes on pages 18 to 26 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities
Consolidated Interim Financial Report
Interim Balance Sheet
For the half year ended 31 December 2018

	Note	31 Dec 2018 $m	30 Jun 2018 $m
Assets			
Cash and cash equivalents		92.3	61.5
Trade and other receivables		293.8	316.7
Forward exchange contracts		3.0	3.7
Inventories		176.5	167.4
Current tax assets		12.1	9.6
Prepayments		28.9	25.3
Total current assets		**606.6**	**584.2**
Other receivables		2.2	2.1
Forward exchange contracts		0.3	0.4
Property, plant and equipment		140.9	128.4
Intangible assets		368.8	345.3
Investments		33.1	15.8
Deferred tax assets		97.0	80.7
Total non-current assets		**642.3**	**572.7**
Total assets		**1,248.9**	**1,156.9**
Liabilities			
Trade and other payables		144.1	140.5
Forward exchange contracts		26.6	13.1
Loans and borrowings	5.1	3.5	3.7
Current tax liabilities		32.8	22.1
Employee benefit liabilities		53.9	57.3
Provisions		27.5	24.5
Deferred revenue		39.2	26.5
Total current liabilities		**327.6**	**287.7**
Trade and other payables		18.4	28.1
Forward exchange contracts		12.6	9.2
Loans and borrowings	5.1	161.5	144.0
Employee benefit liabilities		12.2	12.0
Provisions		56.5	54.4
Deferred tax liabilities		5.1	8.1
Deferred revenue		1.5	2.6
Total non-current liabilities		**267.8**	**258.4**
Total liabilities		**595.4**	**546.1**
Net assets		**653.5**	**610.8**
Equity			
Share capital		182.2	173.0
Reserves		(29.2)	(33.8)
Retained earnings		500.5	471.6
Total equity		**653.5**	**610.8**

The Consolidated Entity has initially applied AASB 9 and AASB 15 at 1 July 2018. Under the transition methods chosen, comparative information is not restated. See Note 1.5

The notes on pages 18 to 26 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities
Consolidated Interim Financial Report
Interim Statement of Changes in Equity
For the half year ended 31 December 2018

Amounts $m	Issued capital	Translation reserve	Hedging reserve	Fair value reserve	Share based payment reserve	Retained earnings	Total equity
Balance at 1 July 2017	169.4	(63.5)	15.2	(0.3)	35.7	387.1	543.6
Total comprehensive (loss)/income							
Net profit	-	-	-	-	-	110.8	110.8
Other comprehensive (loss)/income							
Foreign currency translation differences	-	3.3	-	-	-	-	3.3
Effective portion of changes in fair value of cash flow hedges, net of tax	-	-	1.6	-	-	-	1.6
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	-	-	(7.0)	-	-	-	(7.0)
Financial investments measured at fair value through other comprehensive income, net of tax	-	-	-	(0.1)	-	-	(0.1)
Total other comprehensive (loss)/income	**-**	**3.3**	**(5.4)**	**(0.1)**	**-**	**-**	**(2.2)**
Total comprehensive (loss)/income	**-**	**3.3**	**(5.4)**	**(0.1)**	**-**	**110.8**	**108.6**
Transactions with owners, recorded directly in equity							
Performance rights vested	-	-	-	-	(1.4)	-	(1.4)
Share options exercised	3.5	-	-	-	(1.8)	-	1.7
Share based payment transactions	-	-	-	-	5.6	-	5.6
Deferred tax recognised in equity	-	-	-	-	(2.8)	-	(2.8)
Dividends paid to shareholders	-	-	-	-	-	(80.5)	(80.5)
Balance at 31 December 2017	**172.9**	**(60.2)**	**9.8**	**(0.4)**	**35.3**	**417.4**	**574.8**
Balance at 1 July 2018 (as reported)	173.0	(59.8)	(12.8)	(0.2)	39.0	471.6	610.8
Change on initial application of AASB 9, net of tax	-	-	-	0.4	-	(2.3)	(1.9)
Change on initial application of AASB 15, net of tax	-	-	-	-	-	(5.1)	(5.1)
Balance at 1 July 2018 (restated)	**173.0**	**(59.8)**	**(12.8)**	**0.2**	**39.0**	**464.2**	**603.8**
Total comprehensive income/(loss)							
Net profit	-	-	-	-	-	128.6	128.6
Other comprehensive income/(loss)							
Foreign currency translation differences	-	15.0	-	-	-	-	15.0
Effective portion of changes in fair value of cash flow hedges, net of tax	-	-	(18.8)	-	-	-	(18.8)
Net change in fair value of cash flow hedges transferred to the income statement, net of tax	-	-	5.7	-	-	-	5.7
Financial investments measured at fair value through other comprehensive income, net of tax	-	-	-	(1.8)	-	-	(1.8)
Total other comprehensive income/(loss)	**-**	15.0	(13.1)	(1.8)	-	**-**	0.1
Total comprehensive income/(loss)	-	**15.0**	**(13.1)**	**(1.8)**	**-**	**128.6**	**128.7**
Transactions with owners, recorded directly in equity							
Performance rights vested	-	-	-	-	(0.1)	-	(0.1)
Share options exercised	9.2	-	-	-	(1.0)	-	8.2
Share based payment transactions	-	-	-	-	5.3	-	5.3
Deferred tax recognised in equity	-	-	-	-	(0.1)	-	(0.1)
Dividends paid to shareholders	-	-	-	-	-	(92.3)	(92.3)
Balance at 31 December 2018	**182.2**	**(44.8)**	**(25.9)**	**(1.6)**	**43.1**	**500.5**	**653.5**

The Consolidated Entity has initially applied AASB 9 and AASB 15 at 1 July 2018. Under the transition methods chosen, comparative information is not restated. See Note 1.5
The notes on pages 18 to 26 are an integral part of these consolidated interim financial statements.

Cochlear Limited and its controlled entities
Consolidated Interim Financial Report
Interim Statement of Cash Flows
For the half year ended 31 December 2018

	31 Dec 2018 $m	31 Dec 2017 $m
Cash flows from operating activities		
Cash receipts from customers	740.7	641.8
Cash paid to suppliers and employees	(529.4)	(491.4)
Grant and other income received	2.2	1.2
Interest received	0.3	0.2
Interest paid	(3.0)	(3.9)
Income taxes paid	(46.7)	(55.2)
Net cash from operating activities	**164.1**	**92.7**
Cash flows from investing activities		
Acquisition of leasehold improvements and plant and equipment	(22.7)	(10.0)
Acquisition of enterprise resource planning system	(13.3)	(5.1)
Acquired technology	(8.1)	-
Acquisition of other intangibles	(0.6)	(1.4)
Acquisition of investments	(22.2)	(3.7)
Disposal of investment	1.3	-
Proceeds of sale of non-current assets	-	0.3
Net cash used in investing activities	**(65.6)**	**(19.9)**
Cash flows from financing activities		
Repayment of borrowings	(285.0)	(65.0)
Proceeds from borrowings	301.1	90.0
Proceeds from exercise of share options, net	8.1	0.3
Dividends paid	(92.3)	(80.5)
Net cash used in financing activities	**(68.1)**	**(55.2)**
Net increase in cash and cash equivalents	**30.4**	**17.6**
Cash and cash equivalents at 1 July	61.5	89.5
Effect of exchange rate fluctuation on cash held	0.4	(0.2)
Cash and cash equivalents at 31 December	**92.3**	**106.9**

The Consolidated Entity has initially applied AASB 9 and AASB 15 at 1 July 2018. Under the transition methods chosen, comparative information is not restated. See Note 1.5

The notes on pages 18 to 26 are an integral part of these consolidated interim financial statements.

1 Basis of preparation

1.1 Reporting entity

Cochlear Limited (the Company) is a company domiciled in Australia. The Consolidated Interim financial report of the Company as at and for the half year ended 31 December 2018 comprises the Company and its controlled entities (together referred to as Cochlear or the Consolidated Entity). Cochlear is a for-profit entity and operates in the implantable hearing device industry. Cochlear's Consolidated Annual Financial Report as at and for the year ended 30 June 2018 is available upon request from the Company's registered office at 1 University Avenue, Macquarie University NSW 2109, Australia or at www.cochlear.com.

1.2. Statement of compliance

The Consolidated Interim financial report is a general purpose financial report which has been prepared in accordance with AASB134 *Interim financial reporting* and the *Corporations Act 2001*, and with IAS 34 *Interim financial reporting*.

The Consolidated Interim financial report does not include all of the information required for a full annual financial report, and should be read in conjunction with Cochlear's Consolidated Annual Financial Report as at and for the year ended 30 June 2018. This report should also be read in conjunction with any public announcements made by Cochlear Limited during the half year ended 31 December 2018 in accordance with continuous disclosure obligations arising under the Corporations Act 2001.

The Consolidated Interim financial report was approved by the Board of Directors on 19 February 2019.

The Consolidated Entity is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 (Rounding instrument) dated 24 March 2016 and in accordance with that Instrument, all financial information presented in Australian dollars (AUD) has been rounded to the nearest one hundred thousand dollars unless otherwise stated.

1.3 Significant accounting policies

The accounting policies applied by the Consolidated Entity in this Consolidated Interim financial report are the same as those applied by the Consolidated Entity in the Consolidated Annual Financial Report as at and for the year ended 30 June 2018.

1.4 Estimates and judgements

The preparation of the Consolidated Interim financial report requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

In preparing this Consolidated Interim financial report, the significant judgements made by management in applying Cochlear's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the Consolidated Annual Financial Report as at and for the year ended 30 June 2018, except for new significant judgements and key sources of estimation uncertainty related to the application of AASB 15 and AASB 9, which are described in Note 1.5.

1.5 Changes in accounting policies

AASB 9 *Financial Instruments* has replaced the previous financial instruments guidance including AASB 139 *Financial Instruments: Recognition and Measurement*.

The Consolidated Entity performed a review of its classification and measurement of financial assets and liabilities, as well as hedge accounting, for compliance with AASB 9. The new standard has had the following impacts on Cochlear's consolidated financial statements:

- investments held in the form of ordinary shares previously classified as Available for Sale investments are now classified as Fair Value through Other Comprehensive Income under AASB 9, having elected to make this designation for investments held at 1 July 2018. Under AASB 139 fair value gains or losses are recognised in Other Comprehensive Income whilst impairment losses are recognised in the Income Statement. Under AASB 9 all gains or losses from these investments, including impairment losses, will be recognised in Other Comprehensive Income. In addition, any realised gains or losses on disposal will no longer be recycled through the Income Statement;

- other investments, which includes instruments convertible into ordinary shares were previously classified as Available for Sale investments are now classified as Fair Value through Profit or Loss under AASB 9. Under AASB 9 all gains or losses from these investments, including impairment losses, will be recognised in the Income Statement. Previously recognised fair value losses in the Fair Value Reserve of $0.4 million (net of tax) have been transferred to retained earnings as at 1 July 2018; and
- impairment losses on financial assets, including trade receivables, are now required to be measured using an expected credit loss model rather than the incurred credit loss model. Under the new model, Cochlear is required to recognise the expected credit loss from possible future default events rather than only the credit losses arising from counterparties with indicators of impairment. This resulted in a decrease in retained earnings of $1.9 million (net of tax) at 1 July 2018 with a corresponding impact on the carrying value of trade receivables and deferred tax asset. Other financial assets held by Cochlear are not expected to be impacted by the new standard.

AASB 15 *Revenue from Contracts with Customers* has replaced the previous revenue recognition guidance including AASB 118 *Revenue*.

The Consolidated Entity performed a review of its revenue recognition policies for compliance with AASB 15. The new standard has had the following impacts on Cochlear's consolidated financial statements:

- The core principle of AASB 15 is that an entity recognises revenue related to the transfer of goods or services when control of the goods or services passes to the customer. AASB 15 requires the identification of discrete performance obligations within a transaction and an allocation of a portion of the transaction price to each of these obligations. Under AASB 15, revenue is recognised to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur.

  As at 1 July 2018, an adjustment to opening retained earnings of $5.1 million (net of tax) has been made to defer revenue related to supplemental warranties and to reflect changes in the timing of revenue for certain customer pricing arrangements and expected product returns.

1.6 New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for financial years beginning on or after 1 July 2019, and have not been applied in preparing these consolidated financial statements. Of the new standards, only the below is expected to have an effect on the consolidated financial statements of Cochlear.

AASB 16 *Leases* becomes mandatory for Cochlear's 2020 consolidated financial statements. Cochlear is performing a detailed assessment on the potential impact on its consolidated financial statements resulting from the application of AASB 16. The following impacts are expected:

- the total assets and liabilities on the balance sheet will increase with a decrease in net assets, due to the depreciation of right of use assets being on a straight-line basis whilst the lease liability reduces by the principal amount of repayments;
- operating lease expense will be replaced by depreciation and interest except for short-term leases, low-value leases and certain leases with variable payments. Interest expense will be greater earlier in a lease's life, due to the higher principal value, causing profit variability over the term of lease. This effect may be partially mitigated due to the number of leases held by Cochlear at various stages of their terms; and
- operating cash flows will be higher and financing cash flows will be lower, as repayment of the principal portion of all lease liabilities will be classified as financing activities.

2. Performance for the half year

2.1 Operating segments

	Americas		EMEA[(i)]		Asia Pacific		**Total**	
	2018	2017	2018	2017	2018	2017	**2018**	**2017**
	$m	$m	$m	$m	$m	$m	**$m**	**$m**
Reportable segment revenue	350.5	317.2	248.4	221.7	113.0	100.7	**711.9**	**639.6**
Reportable segment EBIT	190.5	166.7	114.8	96.0	35.0	29.7	**340.3**	**292.4**

(i) Europe, Middle East and Africa

Reconciliations of reportable segment revenues and profit or loss

Revenues	Cochlear implants	Services (sound processor upgrades and other)	**Total Cochlear implants**	Acoustics (bone conduction and acoustic implants)	**Reportable segment revenue**	Foreign exchange (loss)/gain on hedged sales	**Consolidated revenue**
	$m	$m	**$m**	$m	**$m**	$m	**$m**
31 Dec 2018	413.9	207.2	**621.1**	90.8	**711.9**	(8.1)	**703.8**
31 Dec 2017	393.3	161.6	**554.9**	84.7	**639.6**	10.0	**649.6**

Profit or loss	Reportable segment EBIT	Corporate and other net expenses	Foreign exchange (loss)/gain on hedged sales	Net finance expense	**Consolidated profit before income tax**
	$m	$m	$m	$m	**$m**
31 Dec 2018	340.3	(155.2)	(8.1)	(2.7)	**174.3**
31 Dec 2017	292.4	(142.0)	10.0	(3.8)	**156.6**

2.2 Revenue

	31 Dec 2018	31 Dec 2017
	$m	$m
Sale of goods revenue before hedging	695.9	626.2
Foreign exchange gains on hedged sales	(8.1)	10.0
Revenue from the sale of goods	**687.8**	**636.2**
Rendering of services revenue	16.0	13.4
Total revenue	**703.8**	**649.6**

2.3 Expenses

	31 Dec 2018 $m	31 Dec 2017 $m
Cost of sales		
Carrying amount of inventories recognised as an expense	174.4	172.5
Write-down in value of inventories	1.7	1.0
Other	3.4	2.9
Total cost of sales	**179.5**	**176.4**
Other expense		
Net foreign exchange loss	1.2	0.1
Fair value loss on investments measured at fair value through profit and loss	3.5	-
Total other expense	**4.7**	**0.1**

2.4 Other income

	31 Dec 2018 $m	31 Dec 2017 $m
Grant received or due and receivable	0.9	0.5
Release of contingent consideration	5.3	-
Fair value gain on investments measured at fair value through profit and loss	1.3	-
Other	1.7	0.7
Total other income	**9.2**	**1.2**

2.5 Earnings per share

Basic earnings per share

The calculation of basic EPS has been based on the following net profit attributable to equity holders of the parent entity and weighted average number of ordinary shares of the Company:

	31 Dec 2018	31 Dec 2017
Net profit attributable to equity holders of the parent entity	$128,630,000	$110,805,000
Weighted average number of ordinary shares (basic):		
Issued ordinary shares at 1 July (number)	57,547,820	57,426,649
Effect of options and performance shares exercised (number)	109,908	76,896
Effect of shares issued under Employee Share Plan (number)	3,341	4,582
Weighted average number of ordinary shares (basic)	**57,661,069**	**57,508,127**
Basic earnings per share (cents)	**223.1**	**192.7**

Diluted earnings per share

The calculation of diluted EPS has been based on the following net profit attributable to equity holders of the parent entity and weighted average number of shares outstanding after adjustments for the effects of all dilutive potential ordinary shares:

	31 Dec 2018	31 Dec 2017
Net profit attributable to equity holders of the parent entity	$128,630,000	$110,805,00
Weighted average number of ordinary shares (diluted):		
Weighted average number of shares (basic) (number)	57,661,069	57,508,127
Effect of options, performance shares and rights unvested (number)	23,032	65,437
Weighted average number of ordinary shares (diluted)	**57,684,101**	**57,573,564**
Diluted earnings per share (cents)	**223.0**	**192.5**

2.6 Options and performance rights

The Company has granted options and performance rights to certain employees and key management personnel under the Cochlear Executive Incentive Plan (CEIP). The terms and conditions of the plan are disclosed in the Consolidated Annual Financial Report as at and for the year ended 30 June 2018.

Grants made in the current period to certain employee and key management personnel under the CEIP are set out below.

Grant date	Exercise price per option	Number of options	Number of performance rights	Contractual life
August 2018[1]	N/A	N/A	28,446	2 years
October 2018[2]	$202.84	80,231	9,280	3-4 years

1. Performance rights offered under deferred short-term incentives.
2. Options and performance rights offered under long-term incentives.

2.7 Dividends

Dividends recognised in the current and prior financial period by Cochlear Limited are:

	Dollars per share	Total amount $m	Franked/ unfranked	Date of payment
31 December 2018				
Final – ordinary	1.60	92.3	100% Franked	10 October 2018
31 December 2017				
Final – ordinary	1.40	80.5	100% Franked	11 October 2017

Subsequent event

Since the end of the reporting period, the directors declared the following dividend:				
Interim – ordinary	1.55	89.5	100% Franked	16 April 2019

The financial effect of these dividends has not been brought to account in the Consolidated Interim financial report for the half year ended 31 December 2018 and will be recognised in subsequent financial statements.

Franked dividends declared or paid during the financial year were franked at a tax rate of 30%.

3. Income taxes

Numerical reconciliation between income tax expense and profit before income tax

	31 Dec 2018 $m	31 Dec 2017 $m
Net profit	128.6	110.8
Income tax expense	45.7	45.8
Profit before income tax	**174.3**	**156.6**
Tax at the Australian tax rate of 30% (Dec 2017: 30%)	52.3	47.0
Increase in income tax expense due to:		
Effect of change in US tax rate on deferred tax balances[1]	-	5.5
Non-deductible expenses	2.4	-
Decrease in income tax expense due to:		
Research and development allowances	(4.9)	(4.9)
Non-assessable income	-	(0.6)
Effect of tax rate in foreign jurisdictions	(2.2)	(0.4)
	47.6	46.6
Adjustment for prior years	(1.9)	(0.8)
Income tax expense on profit before income tax	**45.7**	**45.8**

[1] Restatement of US deferred tax balances as at 31 December 2017 resulting from the enactment of H.R. 1 (US tax reform legislation) on 22 December 2017.

4. Operating assets and liabilities

4.1 Patent dispute

In a trial of the patent infringement lawsuit by Alfred E. Mann Foundation for Scientific Research (AMF) and Advanced Bionics LLC (AB) in January 2014, a jury found that Cochlear Limited and its US subsidiary Cochlear Americas (the Defendants) infringed four claims across two patents and awarded USD 131.2 million in damages. The jury also found the infringement was “willful”.

On 1 April 2015, a judge in the United States District Court in Los Angeles, California held that three of the four patent claims were invalid and the Defendants’ infringement of the remaining claim was not “willful.” The judge also vacated the damages awarded because three of the four claims were held to be invalid. On 21 April 2015, the Court entered Judgment on liability only and stayed a new trial on damages pending the outcome of the appeals by all parties from the Judgment.

On 18 November 2016, the Court of Appeals affirmed the Judgment as to infringement, affirmed the Judgment as to invalidity of one patent, and reversed the Judgment of invalidity as to one claim in the other patent. The Court of Appeals then remanded to the District Court the issue of damages and willfulness of infringement of two claims in the one remaining patent at issue.

On 9 November 2018, the District Court awarded damages based on the prior jury verdict of USD 131.2 million, upheld infringement of the second claim, added USD 2.8 million for post-verdict infringement, enhanced damages based upon the jury’s verdict of willful infringement, and entered Judgment for a total of USD 268.1 million against the Defendants.

The Defendants have appealed the Judgment including the verdict of willful infringement. To stay the execution of the Judgment pending the outcome of the appeal, the Defendants have arranged for a USD 335 million insurance bond by a third party surety which is held by the District Court. The amount of the bond secures the Judgment amount and any post judgment interest, AMF and AB attorney costs and appeal costs that may be awarded against the Defendants. The bond has no impact on net debt and an annual premium is paid for the bond.

AMF and AB have subsequently asked the District Court to award USD 123 million in prejudgment interest. The Defendants have opposed both the application and the calculation methodology. The Judge has reserved his decision until further notice. The Defendants have arranged a facility to enable the procurement of an insurance bond to stay execution on any prejudgment interest award pending the outcome of the appeal against damages.

The Board of directors has obtained independent legal advice on the Defendants' appeal prospects. The Board is of the opinion it is probable that the Defendants' appeal will result in the lawsuit being remanded to the District Court for a retrial on damages.

There is significant uncertainty on the final damages award following a retrial. Given the inherent uncertainties in assessing the likely damages amount of this case following the appeal, the Board is unable to make a reliable estimate of the amount that will ultimately be paid to AMF and AB. As a result, the provision for damages held at 30 June 2018 of AUD 21.3 million has been released and a contingent liability is disclosed.

Subsequent to the District Court's November 2018 Judgment, a provision for estimated future costs including legal fees, bond costs and other costs associated with defending this matter was made. As at 31 December 2018, AUD 19.6 million of the provision remains.

Cochlear's current product portfolio is not affected by this litigation as the patent at issue has expired.

In the event the appeal is unsuccessful, the Board is confident that Cochlear will be able to access debt facilities to fund the existing Judgment and any award of interest and costs.

4.2 Contingent liabilities

The only contingent liability, other than the patent dispute disclosed in Note 4.1 is the product liability claims described below. The directors are of the opinion that provisions are either adequate or are not required in respect of these matters, as it is either not probable that a future sacrifice of economic benefits will be required, or the amount is not capable of reliable measurement.

Product liability claims

Cochlear is currently and/or is likely from time to time to be involved in claims and lawsuits incidental to the ordinary course of business, including claims for damages relating to its products and services.
In addition, Cochlear has received legal claims and lawsuits in various countries including the United States by recipients who have had Cochlear implant CI500 series devices stop functioning for the reason that led to the September 2011 voluntary recall of unimplanted CI500 series devices.

Cochlear carries product liability insurance and has made claims under the policies. The insurers have agreed to indemnify Cochlear in accordance with the terms and conditions of the policies including deductibles and exclusions. In the opinion of the directors, the details of the product liability insurance policies are commercially sensitive and any disclosure of these details may be prejudicial to the interests of Cochlear.

5. Financial and capital structure

5.1 Loans and Borrowings

	31 Dec 2018 $m	30 Jun 2018 $m
Loans and borrowings:		
Current	3.5	3.7
Non-current	161.5	144.0
Total loans and borrowings	165.0	147.7
Less: Cash and cash equivalents	(92.3)	(61.5)
Net debt	**72.7**	**86.2**

Multi-option bank facilities - Unsecured bank loan

As at December 2018, Cochlear's bank loan facilities are as follows:

Debt Facility	2 year term $m	3 year term $m	4 year term $m	5 year term $m	Total facilities $m
Committed Debt including Guarantees	47.5	100.0	100.0	115.0	362.5

In December 2018, the AUD 50 million July 2020 facility established in June 2018, was converted to a SEK 300 million facility limit with the same expiry date.

All facilities are unsecured and have interlocking guarantees provided by certain controlled entities. Interest on the facilities is variable and changed at prevailing market rates.

Other credit facilities

Unsecured bank overdrafts

Certain unsecured bank overdrafts are payable on demand and are subject to annual review. Interest on unsecured bank overdrafts is variable and is charged at prevailing market rates.

Secured bank loan

Cochlear has no secured bank loans.

Bank guarantees

As at 31 December 2018, Cochlear had contingent liability facilities denominated in United States dollars, Euros, Sterling, Indian rupees and New Zealand dollars totaling AUD 5.9 million (June 2018: AUD 4.4 million).

5.2 Financial Instruments

Fair values

The carrying amounts and estimated fair value of Cochlear's financial assets and liabilities are materially the same.

The fair value of forward exchange contracts is based upon the listed market price, if available. If a listed market price is not available, the fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using benchmark bill futures and swap rates. These fair values are provided by independent third parties.

Valuation of financial assets and liabilities

For financial asset and liabilities measured and carried at fair value, Cochlear uses the following levels to categorise the valuation methods used:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

All of Cochlear's forward exchange contracts were valued using observable market inputs (Level 2) and there were no transfers between levels during the half year.

The equity securities classified as financial assets measured at fair value through other comprehensive income are valued where available using quoted prices (Level 1), or where not available using unobservable market inputs (Level 3).

The fair value losses and gains in Note 2.3 and Note 2.4 respectively were measured using Level 3 inputs. Investments includes $33.1 million (30 June 2018 $15.8 million) measured using Level 3 inputs. During the period, no transfers were made into or out of Level 3 of the fair value hierarchy.

Unobservable inputs are those not readily available in an active market. These inputs are generally derived from other observable inputs that match the risk profile of the financial instruments and validated against current market assumptions and historical transactions where available.

6 Other notes

6.1 Events subsequent to reporting date

Other than reported below, there has not arisen in the interval between the reporting date and the date of this financial report, any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of Cochlear, the results of those operations, or the state of affairs of Cochlear in future financial years.

Dividends

For dividends declared after 31 December 2018, see Note 2.7.

Cochlear Limited and its controlled entities
Directors' Declaration
For the half year ended 31 December 2018

In the opinion of the directors of Cochlear Limited:

1. The consolidated financial statements and notes set out on pages 13 to 26 are in accordance with the *Corporations Act 2001*, including:

    a. giving a true and fair view of the Consolidated Entity's financial position as at 31 December 2018, and of its performance, for the six month period ended on that date; and

    b. complying with Australian Accounting Standard AASB 134 *Interim financial reporting* and the *Corporations Regulations 2001*; and

2. There are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Signed in accordance with a resolution of the directors:

Dated at Sydney this 19th day of February 2019.

Director

Director

KPMG

Independent auditor's review report

To the Members of Cochlear Limited

Report on the consolidated interim financial report

Conclusion

We have reviewed the accompanying consolidated interim financial report of Cochlear Limited.

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the consolidated interim financial report of Cochlear Limited is not in accordance with the *Corporations Act 2001*, including:

- Giving a true and fair view of the Consolidated Entity's financial position as at 31 December 2018 and of its performance for the half-year ended on that date; and
- Complying with *Australian Accounting Standard AASB 134 Interim financial reporting* and the *Corporations Regulations 2001.*

The consolidated interim financial report comprises:

- the consolidated interim balance sheet as at 31 December 2018;
- the consolidated interim income statement, consolidated interim statement of comprehensive income, consolidated interim statement of changes in equity and consolidated interim statement of cash flows for the half-year ended on that date;
- Notes 1 to 6 comprising a summary of significant accounting policies and other explanatory information; and
- the Directors' Declaration.

The Consolidated Entity comprises Cochlear Limited (the Company) and the entities it controlled at the half-year's end or from time to time during the half-year.

The interim period is the 6 months ended on 31 December 2018.

Emphasis of matter – Patent dispute

We draw attention to Note 4.1 in the consolidated interim financial report, which describes the inherent uncertainty in the final future outcome related to the patent infringement lawsuit filed against Cochlear Limited and its US subsidiary Cochlear Americas (the lawsuit).

The uncertainty relates to the Consolidated Entity's appeal process in the Court system regarding the issue of damages and willfulness of infringement of two claims. The range of possible outcomes and associated estimation of financial outflows of the likely loss cannot be reliably estimated, the resolution of which may significantly impact the Consolidated Entity.

In our judgement, this issue is fundamental to users' understanding of the consolidated interim financial report, the financial position and performance of the Consolidated Entity. Our opinion is not modified in respect of this matter.

Responsibilities of the Directors for the consolidated interim financial report

The Directors of the Company are responsible for:

- the preparation of the consolidated interim financial report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*; and
- such internal control as the Directors determine is necessary to enable the preparation of the consolidated interim financial report that is free from material misstatement, whether due to fraud or error.

Independent auditor's review report

Auditor's responsibility for the review of the half-year financial report

Our responsibility is to express a conclusion on the consolidated interim financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 Review of a Financial Report Performed by the Independent Auditor of the Entity, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the consolidated interim financial report is not in accordance with the Corporations Act 2001 including: giving a true and fair view of the Consolidated Entity's financial position as at 31 December 2018 and its performance for the half-year ended on that date; and complying with Australian Accounting Standard AASB 134 Interim Financial Reporting and the Corporations Regulations 2001. As auditor of Cochlear Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of an Interim Period Financial Report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

In conducting our review, we have complied with the independence requirements of the Corporations Act 2001.

KPMG

KPMG
Sydney, 19 February 2019

Julian McPherson, *Partner*